



Management of Supermarket Operations

CONTENTS

	<i>Page</i>
CHAPTER 1 INTRODUCTION AND THE LAW	
Introduction	1
Prevention of Bribery Ordinance (PBO)	
(Laws of Hong Kong Cap. 201)	1
<i>Principal</i>	1
<i>Agent</i>	1
<i>Advantage</i>	2
<i>Principal's Permission</i>	2
<i>Deception by Using Receipt, Account or Other Documents</i>	2
<i>Custom Constitutes No Defence</i>	2
<i>Verbal Agreement Counts</i>	2
<i>Penalty</i>	2
Related Laws	2
CHAPTER 2 CODE OF CONDUCT	
Introduction	3
Code of Conduct	3
Corporate Commitment	4
Acceptance of Advantages	4
Acceptance of Entertainment	4
Conflict of Interest	5
<i>Examples of Conflict of Interest</i>	5
Handling of Confidential Information	5
<i>Information Systems Security</i>	5
<i>Internet and Email Usage Policy</i>	6
<i>"Chinese Walls" Requirement</i>	6
Investment Restrictions	6
Effective Enforcement	6

	<i>Page</i>
CHAPTER 3 PROCUREMENT OF FOOD AND GOODS FOR SALE	
Introduction	7
Procurement in a Supermarket Operation	7
Basic Checks and Balances	7
Proactive Sourcing	8
<i>Establishing Genuine Need</i>	8
<i>Compiling Suppliers' Lists</i>	9
<i>Inviting Quotations</i>	9
<i>Evaluation of Quotations/Tenders</i>	10
<i>Third Party Assessment</i>	11
<i>Negotiation of Trading Terms</i>	12
<i>Appointment of Suppliers</i>	12
<i>Performance Appraisal</i>	13
<i>Contract Renewal</i>	13
Handling Approaches by Suppliers	13
Sourcing Suppliers at Food Fairs	14
Changing Retail Prices	14
Handling of Goods or Food Samples	14
CHAPTER 4 CHAIN STORE OPERATIONS	
Introduction	16
Inventory Control	16
Supervision of Concession Counters	16
"Planogram" Administration	17
Racks or Locations for Promotional Items	17
Product Recalls from Sale	18
Site Checks	18
CHAPTER 5 ACCOUNTING CONTROL IN CHAIN STORES	
Introduction	19
Operational Guidelines	19
Recording of Sales Transactions	19
Cash Handling	20
Refund to Customers	20
Shopping Vouchers and Gift Coupons	20
Management Monitoring	21
Handling of Credit Card Information	21
Internal Audit	21

	Page
CHAPTER 6 ORDERING, WAREHOUSING AND DISTRIBUTION	
Introduction	22
Company Policy and Guidelines	22
Segregation of Duties	22
Ordering and Delivering Stock	23
Receipt of Food or Goods Items	23
<i>General Merchandise Items</i>	23
<i>Fresh Food Items</i>	24
Issue of Food Items or Goods to Supermarkets in the Chain	24
Physical Security	25
Independent Stock Checks	25
Disposal of Stocks	25
CHAPTER 7 GOOD GOVERNANCE AND INTERNAL CONTROLS	
Introduction	26
Good Governance and Ethical Practices	26
Internal Control Systems	26
<i>Setting Sales and Staff Performance Benchmarks</i>	26
<i>Laying Down Clear Policy and Procedures</i>	26
<i>Defining Staff Responsibilities</i>	27
<i>Segregating Duties and Functions</i>	27
<i>Safeguarding Sensitive Information</i>	27
<i>Initiating Effective Supervision</i>	27
<i>Producing Management Information Reports</i>	27
<i>Enhancing Checks and Balances</i>	27
<i>Establishing Channels for Complaints and Feedback</i>	27
ADVISORY SERVICES GROUP	28

Introduction

Nowadays, supermarkets play an important role in serving the local community. They are places where the majority of the public shop for goods, food and grocery. In this competitive business, it is important for supermarket operators to maintain an edge, sustain business developments and foster consumers' trust. This can only be achieved through upholding an ethical business culture and adopting good practices in their operations.

This document aims to provide a checklist of good practices for adoption in supermarkets with chain stores. As supermarket operations are diverse and broad in scope, this document focuses on areas where abuse and corruption could arise. Individual operators may make adaptations to the recommended practices and procedures to suit their own operational needs. Other retailers who run chain stores selling food items or other goods may also find this document relevant to their operations.

Prevention of Bribery Ordinance (PBO) (Laws of Hong Kong Cap. 201)

Section 9 of the PBO sanctions corruption offences in the private sector. In essence, it is an offence for an agent to solicit or accept an advantage, without the permission of his principal (e.g. the employer), as an inducement to, or reward for, his doing or forbearing to do any act in relation to his principal's affairs. Any person who offers an advantage to an agent under such circumstances is also guilty of an offence.

The key components of Section 9 and other relevant Sections of the PBO are detailed below for easy reference. Any person who requires an interpretation of the PBO provisions should seek professional legal advice.

Principal

In the context of this document, a principal is the "employer". In a private organization, the "employer" means the proprietor or the board of directors, including authorized persons acting on their behalf.

Agent

An agent is a person acting for, or employed by, the principal. If a company appoints another person to act for it in business, that person becomes the agent, whether the appointment is full-time or part-time, and whether or not the agent receives a fixed salary or a fee from the company. Any director or employee acting for the supermarket is an agent of the company.

Advantage

Advantage refers to anything that is of value such as money, gift, commission, employment, service or favour, etc. Entertainment, which is defined as food or drink provided for immediate consumption on the occasion, is not an advantage.

Principal's Permission

It is lawful for an agent to accept an advantage in relation to his official duties with his principal's permission. The permission must be given by the recipient's principal, NOT the offeror's principal. In any case where an advantage has been accepted without prior permission, the agent must apply for his principal's approval as soon as reasonably possible afterwards.

Deception by Using Receipt, Account or Other Documents

Any agent who, with an intent to deceive his principal, uses any receipt, account or other document, shall be guilty of an offence.

Custom Constitutes No Defence

It is not a defence to claim that an advantage accepted or offered is customary in any profession, trade, vocation or calling.

Verbal Agreement Counts

The offeror and the recipient of a bribe are liable to prosecution if a verbal agreement of corruption is reached, notwithstanding the purpose of bribery has not been carried out.

Penalty

A person convicted of an offence under Section 9 of the PBO is subject to a maximum penalty of seven years' imprisonment and a fine of HK\$500,000.

Related Laws

Apart from the PBO, the supermarket operators should take note of other relevant ordinances and regulations; for instance, the Companies Ordinance, the Employment Ordinance, the Personal Data (Privacy) Ordinance, the Inland Revenue Ordinance, the Public Health and Municipal Services Ordinance, and the Trade Descriptions Ordinance, etc. (Please visit website <http://www.justice.gov.hk> for details of the above ordinances.)

Introduction

Commitment to lawful and ethical practices is the key to good governance in the running of a business. It is advisable for supermarket operators to issue a **Code of Conduct** to staff, stating the company's commitment to ethical and lawful practices and setting out the proper practices and standards required of them. A well established Code can help prevent corruption and fraud, build the company's reputation, as well as enhance the trust of customers, suppliers and business associates.

In appointing term suppliers (e.g. vendors running concession counters in supermarkets in the chain), supermarket operators could require them to issue a similar Code of Conduct to their employees (e.g. the on-site staff manning the counters).

Regarding fair trade practices, supermarket operators may also wish to make reference to the Good Corporate Citizen's Guide I and II issued by the Consumer Council (http://www.consumer.org.hk/website/ws_en/competition_issues/model_code/list.html).

Code of Conduct

The Code (a sample code obtainable from the Advisory Services Group (p.28) upon request) should include the following key elements:

- corporate ***commitment to ethical practices***;
- rules governing ***acceptance of advantages and acceptance of entertainment***;
- requirements to ***avoid and declare any conflict of interest*** when performing official duties (e.g. when making procurement) and the procedures for handling such declarations;
- requirements to ***protect confidential and commercially sensitive information*** obtained through work;
- requirements to ***maintain proper books and records***;
- requirements to comply with ***investment restrictions***;
- requirements to ***report breaches of the Code*** and other matters of concern to the company;
- obligations to ***comply with all relevant laws and regulations***; and
- ***rules governing relations with suppliers, customers and business associates***.

Further elaboration of some provisions in the Code is explained below.

Corporate Commitment

The Code should include a statement of commitment that the company:

- admits that integrity, accountability and fair competition are the company's business conduct;
- adopts "zero tolerance" against corruption, fraud and malpractice;
- demands the highest standards of business ethics from all staff members and expects all suppliers and business associates to conform to these standards;
- regards highly its moral and legal responsibilities in ensuring the health and safety of customers as a retailer of food products; and
- seeks to provide an efficient and courteous customer service.

Acceptance of Advantages

Staff, in particular those responsible for procurement of food items and goods for sale at the chain stores, may be offered samples of food or goods, some of which may be expensive like abalone. Some may even be offered commission by suppliers. As such offers may be bribes in disguise and acceptance may affect one's objectivity in conducting business, supermarket operators should have **a policy prohibiting employees from accepting advantages** which include any gift, loan, commission, employment, contract, services, etc., from persons with whom they have official dealings. Reference should be made to **Section 9 of the Prevention of Bribery Ordinance**. If employees are allowed to accept token gifts, the permissible value should be specified.

Acceptance of Entertainment

Entertainment is an acceptable social activity, but extravagant and frequent entertainment offered to the staff by suppliers or business associates may be a calculated act to "sweeten" them in order to build up a store of goodwill for future demands of favouritism (e.g. in the selection of suppliers). Supermarket operators should issue guidelines, **advising the staff in particular the procurement staff and their supervisors to avoid accepting meals or entertainment that are excessively lavish or frequent**.

Conflict of Interest

A conflict of interest situation arises when the private interest of staff competes or conflicts with the interest of the company. The staff should be advised to **avoid** any actual or perceived conflict of interest and to **report** to their supervisors when such a situation arises.

Examples of Conflict of Interest

It would be helpful to staff if examples of conflict of interest could be provided in the Code of Conduct. The following are some examples of conflict of interest situations that may arise from procurement activities, staff administration and supervision:

- A staff member involved in the procurement process has financial interest in a company which is being considered by the supermarket operator in the selection of a supplier.
- A supplier under consideration in a procurement process is a close friend or relative of the staff member responsible for the procurement.
- A staff member invests in the business of a supplier who supplies goods to the chain store under his supervision.
- A candidate under consideration in a recruitment exercise is a relative of the staff member responsible for the recruitment.
- A staff member responsible for appointing transport service providers engages the selected contractor to provide him with free transport services or services at a discounted price for personal use (e.g. home moving).

Handling of Confidential Information

Staff may have access to confidential information such as commercially sensitive information relating to the supermarket's business.

Information Systems Security

To protect the interest of the operator and to prevent abuse, the classification of information should be made known to all staff. Restriction on access to confidential information should be clearly defined. While individual staff members should be held responsible for the protection of the confidential information in their possession, the management should ensure that there are adequate safeguards to protect data integrity in the computer and sufficient physical security in the office. (More information is available in the **Best Practice Module on Information Systems Security** (p. 28).)

Internet and Email Usage Policy

To ensure the internet and email are used for official purposes and to protect proprietary and confidential information privy to the company, there should be a clear policy on the usage of office internet and email by staff to restrict usage mainly to company business. Examples of authorized usages (e.g. for company-based research and business dialogues) and unauthorized usages (e.g. for online personal shopping) should be provided to staff. The company should reserve the right to monitor all email messages and internet usage.

“Chinese Walls” Requirement

Staff should be required to avoid inter-departmental communication of confidential information (e.g. bidding prices and schedule of spot checks by the quality assurance team). Staff should consult the management if in doubt.

Investment Restrictions

There should be clear guidelines governing investments by staff, e.g. staff should be prohibited from dealing directly or indirectly in the company’s shares or other shares of any listed company at any time when he is in possession of information obtained as a result of his employment by or his connection with, the company or its Group, and the information is not generally available to the shareholders of the company or the public.

Effective Enforcement

To effectively enforce the Code of Conduct, the company should ensure that it is :

- issued with the ***full support of the management***;
- incorporated in the company’s staff handbook issued upon appointment and ***strictly enforced***;
- promoted through ***continuous capacity building workshops*** to foster good practices;
- ***communicated to suppliers, clients and business associates*** to ensure that they are aware of the company policy and the ethical standards expected of the staff; and
- ***updated*** as necessary.

PROCUREMENT OF FOOD AND GOODS FOR SALE

Introduction

Procurement of food and goods for sale is a core activity of a supermarket. To maximize business profit, it is important for supermarket operators to ensure that the food and goods purchased are value for money and are of the quality standard required. An effective and competitive procurement system helps achieve this purpose and makes good business sense.

Procurement in a Supermarket Operation

Procurement in a supermarket operation has its unique characteristics :

- Food and goods purchased are for immediate sale to customers whose preferences must be accorded top priority.
- As food safety is of great importance, the procurement and quality assurance personnel involved in the process, in particular those responsible for purchases of fresh food, must have the expertise and experience required.
- Purchases of the majority of food items and goods are frequent and repeated but sourcing is on-going as there is a need for the procurement staff to proactively enhance the variety of products.
- Procurement in supermarket operations is of high corruption risk as the chain supermarkets could provide guarantee for customers. Suppliers are therefore keen to approach the procurement staff and to maintain a long-term relationship with them, some may do this through improper means, as the latter could make decisions or make recommendations regarding the appointment of suppliers.

Basic Checks and Balances

A sound procurement system should have the following basic *checks and balances* :

- select suppliers through **competitive bidding** and **continuous review** of their performance, inviting fresh bidding where necessary;
- **segregate duties** as far as practicable (e.g. the front-line procurement staff should only take up an advisory role in sourcing suppliers for bidding instead of performing an executive function **in the selection and appointment of suppliers and in approving the trading terms**);

- designate **approval authorities** at the right level for purchases of specified financial limits and for approving different trading terms;
- specify **procurement methods** for different types and values of purchases (e.g. inviting quotations or tenders based on the value of purchase);
- specify the **authority for approval of exceptional purchases** (e.g. purchases from single source);
- require the procurement staff to **keep proper records** for random supervisory checks and for audit purpose;
- issue **clear instructions** and guidelines for staff's compliance; and
- remind the procurement staff **to make declaration of conflict of interest** to the company regarding their relationship with the suppliers periodically and at the beginning of major procurement exercises.

Proactive Sourcing

From time to time, the procurement staff may need to proactively source suppliers for :

- operating concession counters (e.g. counters for flowers, sushi or a bakery) in chain supermarkets;
- manufacturing and packaging the supermarket's brand name food items or goods;
- supplying food or goods in regular demand (e.g. vegetables, fruits and seafood); and
- supplying food or goods on an ad hoc basis (e.g. organic food).

Establishing Genuine Need

To ensure sourcing of suppliers and purchases are primarily based on actual need, the following safeguards are recommended :

- Procurement staff and their supervisors in charge of goods of the same category and of different categories should be required to meet periodically to **discuss and exchange information regarding the market trend**, new products and the popularity of existing products.
- Decisions on inclusion of new products and concession counters, as well as deletion of old products should be made by **a panel of staff at the appropriate level**.

Compiling Suppliers' Lists

In compiling the suppliers' list, the following safeguards are recommended :

- ***Considerations for inclusion of suppliers should be pre-determined*** for different categories of food items and goods (e.g. for the seafood concession counter, considerations may include availability of third party insurance, delivery trucks with an aeration system, a licensed private fish farm or a wholesale supplier with strong sourcing support, a client list, track record in the field, and years of experience).
- Particular attention should be paid to the ***legal requirements***, particularly in respect of sourcing fresh food outside Hong Kong (e.g. considering only vegetable suppliers authorized by the Mainland).
- ***Invitation to suppliers should be open and transparent*** as appropriate to avoid allegations of favouritism. If invitation is restricted, justifications should be documented.
- ***Nominations of suppliers by staff or business associates*** based on personal knowledge should not be exempted from assessment against the pre-determined criteria.
- Should there be a ***pre-qualification exercise*** (e.g. through the issue of questionnaires to suppliers), guidelines should be provided to the staff concerned, covering the criteria for assessment (e.g. track record and job reference) and the shortlisting method.
- The shortlist should be ***reviewed*** and ***approved*** by a senior staff member.
- ***Separate approved lists of suppliers*** should be kept for different food items or types of goods to facilitate selection of suppliers for invitation to bid.
- The approved suppliers' list should be ***properly managed and periodically updated*** with a view to admitting new suppliers and removing inactive or under-performed suppliers, taking into account the views of the procurement personnel. An independent third party should be assigned to undertake the overall management of the approved list.

Inviting Quotations

The following arrangements help enhance control and minimize the risk of manipulation in inviting bids from suppliers :

- The listed suppliers should always be ***invited to bid on a fair share principle***, i.e. all listed suppliers should be given a fair chance to bid. Any deviation from this practice should be justified and approved by a designated authority.

- The **minimum number of suppliers** to be invited for different values of purchases and the authority to approve the selection should be specified if not all listed suppliers are invited to bid. Responsible managerial staff should conduct random checks to see if the same few suppliers are repeatedly selected for bidding which is unfair to other listed suppliers.
- **Specifications** of the required food items or goods, such as the price and description and the evaluation criteria in broad terms etc. should be included in the invitation for bids to enhance transparency.
- **All quotations**, whether obtained verbally or by fax, should be **protected from tampering or leakage** before the deadline. Verbal quotations should be recorded or confirmed in writing as far as practical. A designated fax machine installed in a secure area or a computer terminal with password control should be used for receiving quotations by fax. All written quotations should be kept securely, preferably by a staff member not involved in the procurement process, to enhance checks and balances.
- To prevent false quotations, a supervisor may **randomly call the bidders** to confirm the genuineness of the quotations received or contact the invited suppliers who have failed to return any quotation to see whether they have actually been invited to bid.
- **Records of quotations** should be kept for random supervisory checks and audits.
- Quotations should be **opened** after the deadline and recorded jointly by two staff members.

Evaluation of Quotations/ Tenders

To ensure fair and objective evaluation of comparable bids, the following measures are recommended :

- Quotations/tenders should be **assessed by a senior staff member or a panel as far as practicable**, taking into account the value of purchase.
- Quotations/tenders should be assessed in accordance with **pre-determined criteria** (e.g. price, profit margin, profit sharing percentage in the case of concession contracts, suppliers' track record, goods or food quality, and delivery efficiency) if price is not the only consideration. Justifications for departure from the assessment criteria should be documented.
- For high value purchases where price is not the only consideration, a **marking scheme** with weightings for the respective predetermined criteria could be used for evaluation.

- To facilitate evaluation, suppliers could be required to make a ***presentation*** before the evaluation panel where appropriate. The requirements for the presentation should be pre-determined and made known to the suppliers (e.g. samples of the product required, the outer packaging to demonstrate packing configuration, the market potential, and promotional activities for new products).
- ***Expert advice*** (e.g. through scientific research conducted by reputable institutions or personnel) should be sought where appropriate, particularly in the evaluation of new products or food items that may have health and safety implications (e.g. imported frozen seafood carrying a name which is not widely acknowledged in the local community or market) or that are not regulated under existing laws and regulations.

Third Party Assessment

Supermarket operators usually engage a quality assurance team to conduct quality control checks before and after the appointment of suppliers. As this is an important part of the appointment exercise, the following measures to enhance control are recommended :

- For food items or goods purchased from local or mainland companies, staff should be ***given clear guidance on the scope of checks, particularly in respect of food items*** (e.g. the acceptable pesticide standard adopted by a farm and the requirement for proof of the checks conducted) to ensure that checks have been effectively and properly conducted.
- For the sake of checks and balances, the quality assurance staff who conduct the ***pre-appointment checks*** on the suppliers should not perform the ***after appointment checks*** as far as practicable.
- All ***spot-check schedules*** should be ***kept confidential*** and confined to the “need-to-know” to prevent leakage to suppliers.
- Staff at ***outposts*** (e.g. in the Mainland) conducting checks on suppliers should be issued with specific guidelines on acceptance of offers of advantages and entertainment (e.g. standard of hotel accommodation to be accepted if this is provided free of charge by the supplier, and the entertainment acceptable from the company’s perspective).

Negotiation of Trading Terms

Negotiations with potential suppliers on the trading terms are common practice, covering among others payment terms, credit period, mode of deliveries, arrangements for promotional activities, incentive rebate, damaged goods allowance and display location, etc. To enhance control, the management may adopt the measures recommended below :

- set the ***minimum goal*** to be achieved for each negotiation appointment (e.g. the profit margin for each item);
- lay down the ***policy and procedures*** for offering trading terms to suppliers (e.g. the essential terms and approval authority);
- have the ***negotiation conducted by a team*** comprising at least two persons as far as practical;
- closely monitor the staff involved in negotiations with suppliers, in particular the new suppliers, e.g. through setting ***negotiation baselines*** and designating the authority for making decisions; and
- ***review*** the terms periodically to ensure the offer is compliant with the laid down policies.

Appointment of Suppliers

The following measures to enhance monitoring are recommended prior to the formal appointment of a supplier :

- ***Quality control check*** should be a prerequisite for final contract approval.
- The accounts or finance department should ***counter check the approval authority*** and the contract terms, and obtain the required documentary proofs (e.g. copies of the supplier's company registration certificates, company articles of incorporation and credit details such as bank account numbers).
- The contract signed with the appointed supplier should contain ***clauses*** on protection of confidential information obtained during the course of business with the company and on prohibition of offers of advantage to staff of the company. The supplier should be required to guarantee that the products supplied are in absolute conformity with all local laws and the laws of the exporting country and country of origin as appropriate.
- ***Contract terms*** should be subject to ***review*** by an independent third party such as the accounts or finance department ***prior to contract renewal***.

Performance Appraisal

To ensure the suppliers' performance is objectively appraised and sub-standard suppliers would not be corruptly tolerated, the following preventive measures are recommended :

- subject the suppliers' performance to ***periodic appraisals*** to ensure under-performed suppliers will not have their contracts renewed or will not be invited to bid in the future;
- draw up a set of ***evaluation criteria*** (e.g. sales performance, service standard of concession counters, food safety standard, and delivery performance);
- adopt ***multi-tier performance appraisals*** to be conducted independently by the procurement staff, regional and area managers, store supervisory staff and the quality assurance team as appropriate;
- put in place a ***disciplinary system*** to sanction suppliers who have been non-compliant with the contract conditions (e.g. issue of warnings or suspension from invitation to bid for future contracts); and
- ***collect consumers' feedback*** as an independent third party appraisal as appropriate.

Contract Renewal

To minimize abuse in contract renewal, the following measures are recommended :

- lay down the ***criteria*** for renewing a contract (e.g. sales performance, market trends and issue of a staff code of conduct) and the approval authority; and
- periodically review the need to conduct a ***fresh appointment exercise*** to enhance competition and to minimize the perceived over-reliance on a particular supplier.

Handling Approaches by Suppliers

Suppliers usually approach the procurement staff to promote their products for sale in the supermarkets. To ensure such approaches are properly handled, the following measures are recommended :

- A ***procedure*** should be established for suppliers to introduce their products and the procedure, including the information required (e.g. company and product profile) and the criteria for evaluation, should be made known to all interested suppliers, via the corporate website or information leaflets.
- The ***assessment of products*** by the procurement staff, rejections or recommendations for further assessment with justifications, and approval of appointment of the supplier ***should be recorded*** in the computer to facilitate future review.

- **Unsuccessful suppliers** should be notified of the outcome.
- The management should monitor any **outstanding submissions** (e.g. pending documents required) to detect any unnecessary or deliberate holding up.

Sourcing Suppliers at Food Fairs

To keep abreast of consumers' need and market trends, the procurement staff may attend local or overseas food fairs to source potential suppliers of new food products. To enhance control, the measures to control handling of approaches by suppliers are applicable except that submissions are made by the procurement staff to supervisors.

Changing Retail Prices

Due to market re-positioning of individual products, suppliers may initiate retail price changes after the price has been agreed in the contract. To minimize abuse, the following measures are recommended :

- All applications for price changes should be made in a **standard form for approval** at the senior level with a prescribed minimum of reasonable days of advance notice.
- The approving staff should be **prohibited from entering into any unethical retail price fixing arrangements** with the supplier.
- The management should be **constantly wary of the market positioning of individual products**, taking into account the changing market conditions.
- A central unit of the supermarket operation should **conduct price comparisons** periodically, say weekly, to ensure the proposed price changes are reasonable.

Handling of Goods or Food Samples

Suppliers may offer samples of goods or food items to the procurement staff as a sales tactic. The offer of expensive samples like abalone or wine which have resale value may be a bribe in disguise to the staff in return for business. Supermarket operators should establish a system for handling of food or goods samples, incorporating the following safeguards :

- There should be a policy **prohibiting acceptance of food or goods samples by individual staff**, unless otherwise authorized.

- ***Receipt and disposal of samples*** with commercial value ***should be properly recorded*** in a register and subject to the supervisor's random checks.
- ***Evaluation of the quality of samples*** should be conducted ***by a team*** including managerial staff. To enhance objectivity, tasting of food or drink samples could be conducted without revealing the supplier's identity to the evaluators.

Introduction

This chapter focuses on the internal operations of supermarkets in the chain and should be read jointly with the Chapter on Accounting Control in Chain Stores.

Inventory Control

Supermarket operators usually maintain a central warehouse for distribution of goods and food items to supermarkets in the chain and a store in each supermarket. While most stock items are distributed from the central warehouse to individual supermarkets in the chain, for some commodities (in particular those of a perishable nature, e.g. milk), individual supermarkets place order direct with the suppliers selected by the operator.

Acceptance of goods by supermarket stores, in particular those delivered direct from suppliers, is an area prone to abuse. Compromised staff could cover up short delivery or accept goods or food items of poor quality. To deter malpractice, the following inventory control measures are recommended :

- To enhance accountability, the staff responsible should be required to **inspect and count goods/food items upon delivery** against the quantity specified in the delivery note, cross-referencing the relevant purchase orders if any, and to certify acceptance.
- There should be a procedure for staff to **record defective or short delivered goods or food items** and to follow up promptly with the supply department or the supplier direct.
- The types and quality of food or goods to be replenished directly by the concession counter staff should be subject to **checks before sale**.
- **Random supervisory checks** should be conducted on the quality and quantity of accepted food or goods, especially those of high value.

Supervision of Concession Counters

Supermarket operators may enter into joint ventures with vendors assigned concession counters (e.g. a bakery) in the chain stores. These counters are usually manned by staff from the vendors. To ensure they follow the supermarkets' laid down service standards and business conduct, there is a need for supermarket operators to enhance supervision over these staff. The following control measures are recommended :

- apply the **Code of Conduct** issued to the supermarket staff to these employees, prohibiting them from acceptance or offer of advantages;

- require the store supervisor and the manager to **monitor the concession counter staff** to ensure they provide satisfactory customer service; and
- **prevent** these counter staff from **pocketing the sales income** by putting up a sign asking customers to pay at the cashier counter only and compare customer patronage and sales income of the same concession counters in different chain stores with a view to detecting irregularities.

“Planogram” Administration

“Planogram” is a master plan of the physical display locations of various categories of food or goods in a chain store, showing among others the racks and number of shelves in a rack. As some positions may be deemed more “advantageous” for display purposes, there is room for manipulation by compromised supermarket staff who may allocate more “advantageous” display locations to the food or goods of a particular supplier.

Supermarket operators may adopt the following safeguards to prevent malpractice :

- **have the “planogram” set by a department independent of the store operation** according to predetermined criteria and prohibit store staff from being involved in the process; and
- require the store supervisor or manager to conduct **on-site spot checks** to ensure that the items are placed correctly in accordance with the “planogram”.

Racks or Locations for Promotional Items

Some racks and locations in the supermarket are designated for promotional items. As some staff (e.g. the procurement staff) are authorized to supervise the usage of these racks or locations, there may be room for manipulation such as allowing non-promotional goods to be displayed on these racks. To prevent abuse, the following control measures are recommended :

- require **justification and documentation** for recommending goods as promotional items;
- seek **independent views** to enhance checks and balances (e.g. requiring the supply department to check the sales performance of the recommended goods for display in the previous promotion exercises);
- **set the promotional period** (e.g. seven days) for a promotional item and require the store supervisor or manager to ensure the promotion deadline is strictly adhered to; and

- lay down ***the criteria for extension of the promotion period*** (e.g. based on sales performance or availability of other promotional items).

Product Recalls from Sale

Sometimes, products which are potentially unsafe or not in full conformity with the laws and regulations are withdrawn from sale. To ensure the recalls are properly handled, the following safeguards are recommended :

- establish a clear policy and procedures for withdrawing products from sale;
- set the deadline for withdrawal of products; and
- announce the recalls as appropriate.

Site Checks

Supermarkets in the chain are subject to different levels of site checks (e.g. by the regional and area managers, store supervisors and managers, the quality assurance team and the internal audit team). One of the purposes of these checks is to ensure the food items or goods on sale meet the required quality and safety standards (e.g. to ensure correct labeling and withdrawal of expired products). To enhance the effectiveness of these checks, the following measures are recommended :

- keep the ***schedule of checks confidential*** and make it known only to the “need-to-know”;
- supervisors should define the ***scope of checks and set the sample size*** for the respective persons or teams conducting such checks, and require them to record their findings for management information; and
- periodically engage ***“mysterious customers”***, e.g. a professional survey company, to conduct checks and require the findings to be reported to the management and systematically analyzed and followed up.

ACCOUNTING CONTROL IN CHAIN STORES

Introduction

Supermarket operators are not in short of professionals who oversee and handle their accounting matters. This chapter aims to highlight the malpractice and the preventive measures in the handling of sales transactions in supermarkets store, which are usually settled in cash, or by EPS (an electronic payment system) or credit card.

Common malpractice in handling sales transactions includes non-recording or cancellation of bill items to pocket the sales income, credit card fraud, and pilfering of cash collection, etc. In supermarket operations, such risks may be mitigated by the use of advance billing systems and customers' personal monitoring over the cashier counter. However, administration of refund to customers, shopping vouchers, gift redeem coupons and cancelled bills are areas vulnerable to abuse and malpractice.

Operational Guidelines

To ensure consistency in practice, staff should be issued ***procedural guidelines*** covering receipt of payments, recording of transactions, handling of cash registers, refund, shopping vouchers, gift coupons and receipt vouchers, and conduct of supervisory checks, etc. The level of staff and their responsibilities should be set out in the guidelines and the authority for approving certain sales transactions (e.g. refund to customers) should also be specified.

Apart from the guidelines, it is advisable to generate ***daily and periodical sales and receipt reports*** to be prepared and signed by the staff responsible as this could provide an audit trail and enhance staff accountability.

Recording of Sales Transactions

While all sales transactions are recorded electronically using an automated bar-coding system, staff should be required to report any reversion to manual recording in case of system breakdown. Such records should be subject to supervisory checks.

Cash Handling

To prevent manipulation, the following control measures are recommended :

- The **guidelines** on handling of cash should set the maximum amount of cash flow per day for each store, the banking frequency, and the requirement for daily cash position reports.
- **Notes handling procedures** should specify, among others, the bank notes, e.g. HK\$500 notes and Renminbi (RMB) \$100 notes, to be tested using a money tester by a sales assistant and HK\$1000 notes by a store supervisor; and the designated staff authorized to handle currency exchange and conversion in respect of RMB and HK dollars.
- **CCTV with tape recording facilities** could be installed to monitor cash handling at the cashier counters if necessary.
- A responsible staff member at the appropriate level should be designated to conduct **day-end reconciliation** of electronic sales records against the cash in hand and to make spot checks on other operational activities daily at random.
- **Compliance with cash collection security requirements** by the staff responsible (e.g. keeping and handover of cash) should be subject to supervisory and audit checks.

Refund to Customers

Supermarket operators should lay down **guidelines** for making refunds to customers. Refunds made should be justified (e.g. damaged goods), authorized by designated staff, recorded for audit review, and the returned goods properly disposed of under supervision.

Shopping Vouchers and Gift Coupons

As vouchers and coupons have cash value, they should be subject to normal accounting control. The **receipt, custody and disposal of these vouchers/coupons** should be properly recorded electronically and be subject to random supervisory checks.

Management Monitoring

An effective management monitoring system could help deter and detect malpractice. Supermarket operators may require the stores to generate ***periodic computer reports for management information***, such as reports showing the sales income, cash balance, sale of shopping vouchers and issue of the gift coupons, and refunds to customers.

Handling of Credit Card Information

Handling of customers' credit cards is an area where malpractice is known to exist. Unscrupulous staff may accept bribes from criminal syndicates in return for capturing customers' credit card information for the production of counterfeit cards. They may also corruptly condone the use of counterfeit cards. Such illicit activities are not easy to detect but if there is any suspicion of malpractice, supermarket operators should report the case to the ICAC or Police as appropriate.

The following preventive measures could help mitigate the risk of such malpractice :

- ***Briefing sessions*** may be arranged ***for staff to raise their awareness*** of the criminality of such activities and the company's disciplinary action if such activities are discovered.
- ***Clear instructions*** should be given ***to staff*** on the handling of credit card transactions, e.g. requiring the handling staff to sign on the credit card payment slips to hold them accountable for the transactions.
- Effective ***security measures*** should be adopted to minimize the risk of information leakage, e.g. to keep the credit card payment slips in a secure place with restricted access.
- The staff should be informed of the ***channels for reporting*** approaches by criminal syndicates and incidents of suspected corrupt practices.

Internal Audit

Sales and accounting operations should be subject to internal audit.

ORDERING, WAREHOUSING AND DISTRIBUTION

Introduction

In supermarket operations, stock control is important because the aggregate value of food items (e.g. wine and abalone) and goods in store is significant and, more importantly, they have a re-sale value. Moreover, control of fresh food items could be difficult because of their perishable nature.

Malpractice, such as favouritism to suppliers by placing excessive orders for certain food items/goods, pilfering, and improper disposal of expired but usable items, will result in financial loss to the supermarket. Corruption arises if such malpractice is covered up by compromised or colluding supervisors. This chapter aims to help supermarket operators in setting up an effective store control system from making purchase requisitions and warehousing to distribution of food/goods to stores in the chain.

Company Policy and Guidelines

Supermarket operators should make known to all staff the **company policy** that any misuse or misappropriation of company assets and resources will not be tolerated.

The staff and suppliers should be issued with **clear guidelines** on the handling of stocks, covering the procedures for ordering stock, acceptance of food/goods, distribution to chain stores, and disposal of surplus or expired stock. The levels of authority for various store control functions should be specified.

Segregation of Duties

To enhance **checks and balances**, the duties for making purchases, ordering stocks, receiving and issuing food items/goods, and stocktaking should be segregated as far as practicable.

Ordering and Delivering Stock

There should be established procedures with adequate safeguards for purchase requisitions and delivery of items, covering the following areas :

- A **standard requisition form**, preferably in an electronic format to facilitate electronic data interchange between the operator and the supplier or sending of electronic fax, should be used to provide an audit trail. The form should show details such as the description, quantity and place of origin of the goods/food items required, the agreed price, the delivery address, the expected date of delivery, the name of the requesting person, and the approval authority as appropriate. Phone orders should be confirmed in writing afterwards. Any deviations should be approved by the appropriate authorities.
- Supermarket operators usually set the target lead time for delivery by suppliers (e.g. local orders must be confirmed not later than 24 hours prior to the expected delivery date and overseas orders confirmed within seven days upon receipt of requisition). Any request from suppliers for **extension of the lead time should be justified and approved by senior staff**.
- There should be clear instruction to the staff that **over-deliveries or short-deliveries** should normally not be accepted unless justified and authorized.
- **Suppliers' performance in stock delivery should be appraised** (e.g. whether there are incidents of short deliveries or delay in delivery, and the quality of delivered stock, in particular fresh food). The appraisal should be recorded as this provides useful reference in future selection of suppliers.

Receipt of Food or Goods Items

The following **safeguards** are recommended to ensure that only food items or goods of the quantity and quality specified in the purchase orders are accepted. For the receipt of general merchandise items, the following measures are recommended:

General Merchandise Items

- Before authorization of payment, **random counter-checks** on the stocks received against the purchase orders should be conducted by a supervisor or a staff member not involved in the placing of orders.
- Procedures should be clearly laid down for **reporting and handling of food items of poor quality and damaged goods**, as well as any short-delivery and over-delivery.
- **Serially numbered receipts** recording the receipt of goods (e.g. description of the food items/goods, quantity or weight) should be issued to the supplier and copied to the accounts or finance department.

Fresh Food Items

Receipt of fresh food items (e.g. meat, seafood, vegetable and fruit) is a vulnerable area because there are frequent deliveries (some on a daily basis), weight measurement could be disputed and easy to manipulate, and they are perishable in nature. Some fresh food items are processed before distribution to supermarkets in the chain for sale (e.g. cutting and packing).

Apart from the safeguards for the receipt of general merchandise items, the following measures are recommended:

- Supervisors of the food receiving and processing teams should have the relevant expertise and experience. They should be required to ***closely monitor the receipt, processing and issue*** of food items to ensure that the process is proper and complies with the laid down instructions (e.g. the industry approved frozen or chiller requirements such as temperature requirement) as this is important to assure the quality and hygiene of food.
- The transaction records should be properly kept, preferably in a computer and updated daily. A designated staff member should ***reconcile daily the quantity received and delivered to the supermarkets in the chain***, taking into account the percentage of wastage due to food processing.
- Quality assurance staff not involved in the process should be assigned to conduct ***spot checks on the acceptance and processing of food items***, recording any poor quality or short-delivered items or improper processing for follow up action.

Issue of Food Items or Goods to Supermarkets in the Chain

Issue of stores with the aid of computer systems could help record and monitor individual supermarkets' consumption rate. The issue of food items on a "first-in-first-out" basis, in particular those items with a specified consumption date or shelf life, should also be electronically monitored.

The number or weight of the food items should be ***confirmed in writing*** by the receiving stores.

Physical Security

To prevent theft or pilfering, stock items are usually kept in **a secure warehouse** with restricted access to authorized staff only. Items of high value should be kept under lock to enhance security and the key holders be held accountable for the stock. CCTVs may be installed to monitor access to the stores for keeping expensive items.

Independent Stock Checks

Stock checks could help detect and deter malpractice in stores management. **An independent checker or team** could be assigned to conduct periodic stocktaking exercises whilst the warehouse supervisor should make regular **surprise stock checks**. An effective stocktaking mechanism should include the following safeguards :

- The **frequency, scope and sample size** of the checks should be predetermined.
- A **master inventory record** of all stock items should be compiled to facilitate stock checks.
- **Procedures** should be established **to handle discrepancies** identified in stock checks, including investigation and reporting to the appropriate authority.
- Staff at the appropriate level should be designated to approve any **amendment of stores records** as a result of the stock checks.

Disposal of Stocks

Senior staff of supermarkets should tightly control the disposal of stock items to ensure that substandard food items or goods and those that have reached the expiry date will not be sold to members of the public.

The following safeguards are recommended to minimize malpractice :

- Supermarkets should have a clear policy **prohibiting** staff from putting up such **stocks for sale**.
- The disposal of stock items should follow established policies and procedures, including **inspection, approval and supervision of disposal**.
- If a “total dumping policy” is adopted, a designated staff member at the appropriate level acting as a witness should be assigned **to make sure that all written-off items are destroyed and disposed of as waste**.
- Disposal **records** should be kept and certified by the staff responsible.



GOOD GOVERNANCE AND INTERNAL CONTROLS

Introduction

In the foregoing chapters, measures to prevent malpractice and abuse in specific operations of a supermarket are recommended for adoption. To ensure that the measures adopted are understood and accepted by staff for implementation, an effective internal control system is important. Of equal importance is good governance and ethical practices to help sustain the effectiveness of internal control.

This chapter provides a checklist of measures which could help supermarket operators enhance internal control and effectiveness in management.

Good Governance and Ethical Practices

Supermarket operators should publicly commit to good governance and ethical practices. Good governance requires commitment from the management to put ethics into practice in the company. The values and attitudes held by the management exert great influence on staff. Senior managers and managers of supermarket operations should lead by example and commit themselves to ethical practices and personal integrity. If an ethical culture forms the basis upon which every staff member makes business dealings, the supermarket operator's image can be enhanced, overall efficiency improved and customers' trust fostered. This in turn will enhance the operator's competitive edge and profitability.

Internal Control Systems

The following are key considerations in the setting up of internal control systems:

Setting Sales and Staff Performance Benchmarks

- Avoid setting unrealistic sales quotas for staff so that they have to look for shortcuts or resort to unethical or illegal practices to meet quotas.
- Monitor and assess the performance of individual staff, e.g. by comparing food items or goods for sale in supermarkets in the chain and the overall sales performance of individual chain stores.
- Make performance benchmarks known to all staff and use a standard performance appraisal form.

Laying Down Clear Policy and Procedures

- Lay down in guidelines and instructions the policies and procedures for dealing with suppliers, customers and business associates, etc., highlighting the ethical and legal aspects.
- Organize capacity building workshops for staff as frequent as necessary.

- Ensure suppliers, customers and business associates are well aware of the company policies and business culture.

Defining Staff Responsibilities

- Define clearly the roles and responsibilities of each level of staff to enhance accountability.
- Lay down clearly the approval authorities for business or operational decisions.
- Allow discretion to be exercised only by staff at the appropriate level and with the required experience or expertise.

Segregating Duties and Functions

- Segregate the key duties and functions to enhance checks and balances.

Safeguarding Sensitive Information

- Properly classify and physically secure sensitive or confidential information.
- Adopt measures to prevent unauthorized access to sensitive or confidential information stored in computer systems.

Initiating Effective Supervision

- Require supervisors at different levels to conduct supervisory checks.
- Require supervisors to report observations and actions taken if any.

Producing Management Information Reports

- Require staff to keep accurate and proper records of major activities (e.g. documentation of tender exercises).
- Establish an effective information management system to ensure that useful data are produced regularly for management information.

Enhancing Checks and Balances

- Initiate independent internal or external audit on the activities of supermarkets in the chain, apart from revenue audits.
- Engage independent third parties (i.e. “mysterious customers”) to patronize the chain stores as customers and obtain feedback from them.

Establishing Channels for Complaints and Feedback

- Establish and publicize the channels for complaints or feedback from staff, customers and suppliers.
- Handle complaints promptly to show the management’s determination to address the problems identified.

ADVISORY SERVICES GROUP

Apart from this Best Practice booklet, a series of Best Practice Modules on systems such as procurement, staff administration, administration of maintenance and repair works, etc. are also available for your reference. They can be obtained from the **Advisory Services Group** of the Corruption Prevention Department of ICAC which provides free, confidential, and tailor-made corruption prevention advice to private organizations on request. For further information, please contact the Group at telephone no. **2526 6363** or fax no. **2522 0505** or email address: **asg@cpd.icac.org.hk**.



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