

Financial Fraud, Audit Failure, and Regulatory Implications under the Registration-Based System: A Case Study of Zeda Yisheng

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Abstract

As the most emblematic case of financial fraud on the STAR Market following the implementation of the registration-based system, the Zeda Yisheng incident involved comprehensive accounting fraud throughout the IPO process by the prospective listed company, ultimately resulting in the mandatory revocation of its listing status by regulatory authorities. This case extends beyond the company itself to involve multiple types of securities intermediaries. More critically, it exposes numerous loopholes in the STAR Market's listing review process and the practice of certified public accountants, providing a valuable reference case for analyzing false accounting disclosures and inadequate auditing in China's A-share securities market. This paper takes the Zeda Yisheng violation case as its research subject, employing a case study methodology to systematically trace the chronological development of its financial fraud and its core operational techniques. It examines the specific mechanisms used to inflate main business revenue under fabricated business scenarios and, based on the securities regulatory authorities' penalty decision, delves into the underlying reasons why the audit firm failed to exercise due professional care. This detailed examination of the case not only enriches the theoretical framework and empirical evidence in detecting accounting fraud in securities markets but also offers valuable insights for improving the oversight of securities intermediaries' professional conduct, refining the exit mechanisms for listed companies, and strengthening investor protection systems. Analysis reveals that Zeda Yisheng deliberately constructed a fraudulent chain involving fabricated contracts, false documents, and circular fund flows to intentionally inflate revenue scale and profit metrics during the reporting period. The auditors' failure to properly execute key verification procedures—such as examining purchase and sales contracts and verifying original documents like waybills—was the fundamental factor leading to the misrepresentation in the audit opinion. The strict legal punishment in this case and the subsequent settlement of the investor class action lawsuit fully demonstrate the regulatory authorities' firm stance on cracking down on securities violations and ensuring the orderly operation of the capital market. It also sends a crucial warning to all market participants that they must adhere to compliance standards.

Keywords: Financial Fraud; Audit Failure; False Trade; Compulsory Delisting

1. Introduction

Under the overarching context of comprehensively advancing the reform of the registration-based system for stock issuance, China's capital market is undergoing a profound institutional transformation. Centered on information disclosure, the registration-based system aims to enhance market operational efficiency and strengthen the accountability of market entities. Its successful implementation relies on the truthful, accurate, and complete disclosures by issuers, as well as the diligent fulfillment of the "gatekeeper" role by intermediary institutions. However, the implementation and refinement of this new system inevitably bring challenges. Some companies seeking listing have exploited the transitional frictions during the shift in the review mechanism, meticulously planning and executing systematic financial fraud in an attempt to pass scrutiny with false information. This severely undermines the integrity foundation upon which the registration-based system depends, posing a direct threat to market order and investor confidence.

The outbreak of the Zeda Yisheng financial fraud case precisely epitomizes the complexities of this transition period. As the "first stock implicated in fraud" on the Science and Technology Innovation Board, its misconduct was not an isolated or sporadic accounting error but rather a meticulously planned and persistently executed full-chain fraud initiated from the initial public offering (IPO) application stage. Through fabricating trade backgrounds, forging a complete set of business documents, designing closed-loop fund circulations, and other means, the company systematically inflated revenue and profits, ultimately securing a listing on the Science and Technology Innovation Board. However, as truth cannot be concealed indefinitely, its illegal activities were ultimately investigated and penalized by regulatory authorities, triggering the clauses for compulsory delisting due to major violations. This has become a landmark punitive case in the A-share market. The distinctiveness of this case lies not only in the concealment and completeness of its fraudulent methods but also in its extensive involvement of multiple parties including the listed company, actual controllers, accounting firms, and sponsor institutions. It exposes vulnerabilities and failures across multiple links, such as internal corporate governance, intermediary practice, and regulatory coordination.

An in-depth study of the Zeda Yisheng case holds significant theoretical value and practical implications. From a theoretical perspective, this case provides a vivid and extreme research sample for analyzing the motivations, methods, and identifying characteristics of financial fraud in the early stages of the registration-based system. It contributes to enriching and advancing theories on securities market fraud. For instance, agency theory posits that conflicts of interest between principals (shareholders) and agents (managers) can lead managers to prioritize personal gain over firm value, a dynamic evident in Zeda Yisheng where management pursued listing-related personal benefits at the expense of long-term corporate health and shareholder interests. Furthermore, the fraud triangle theory provides a robust framework for dissecting the case: the pressure to meet stringent STAR Market financial thresholds, the opportunity presented by weak internal controls and a transitional regulatory environment, and the rationalization by

management that such fraud was a necessary "shortcut" to success. These theories collectively illuminate the multi-layered drivers of the fraud. From a practical standpoint, a detailed analysis of this case acts as a multifaceted prism, reflecting numerous pressing issues in the current capital market ecosystem: the moral hazards and short-sighted behavior of companies seeking listing amidst fierce competition and the allure of going public; the imbalance and lapses of intermediary institutions between commercial interests and professional ethics; and how regulators can effectively identify and combat increasingly concealed illegal activities while adhering to market-oriented and rule-of-law principles. Additionally, the subsequent securities class action settlement related to this case provides practical reference for exploring new pathways for investor rights remediation.

Therefore, this paper selects the Zeda Yisheng financial fraud case as the research subject, aiming to conduct a systematic case analysis to deeply interpret the specific techniques and key stages of its fraudulent operations. It explores the root causes of the fraud from multiple dimensions, including internal corporate demands, ethical deficiencies in management, and pressures from the external environment. The analysis focuses particularly on the reasons for the audit institution's failure—such as perfunctory execution of procedures, compromised independence, ineffective risk assessment, and deficiencies in quality control—and further reflects on the underlying issues of commercial ethics anomie embedded within. Through a comprehensive examination of this typical case, the paper aims to provide valuable insights and references for regulatory authorities to improve verification mechanisms, for intermediaries to enhance professional practice quality, and for investors to strengthen risk identification capabilities. It seeks to contribute to reinforcing the information disclosure defense under the registration-based system and to promoting the long-term, healthy, and stable development of the capital market.

2. Introduction to the Financial Fraud Situation and Analysis of Fraud Methods

2.1. Overview of the Case Basics

2.1.1. Fraud Perpetrator and Timeline

Zeda Yisheng is the first company on the Science and Technology Innovation Board (STAR Market) to be compulsorily delisted due to financial fraud during the IPO stage, earning it the title of the STAR Market's "first stock implicated in fraud." Its financial fraud was not sporadic but characterized by clear planning and persistence. According to investigations and verification by the China Securities Regulatory Commission (CSRC), Zeda Yisheng's financial fraud began as early as the IPO application stage. To meet the financial thresholds required for listing on the STAR Market, the company started systematically fabricating financial data during the preparation of its application materials. After successfully listing on the STAR Market, the fraudulent activities did not cease but continued into the post-listing continuous supervision period. The company maintained the "impressive" appearance of its financial reports through ongoing false transactions to stabilize its stock price and mislead investors. It was only after regulatory authorities initiated a special investigation that this long-running, large-scale financial

fraud case was completely exposed. Ultimately, the company was deemed to have committed serious violations, triggering clauses for compulsory delisting from the capital market due to major illegal acts. This case became a landmark example of IPO financial fraud leading to delisting in the A-share market, serving as a warning bell for subsequent listing applicants and intermediary institutions.

2.1.2. Consequences of the Fraud and Market Impact

The disclosure of the Zeda Yisheng financial fraud incident dealt a fatal blow to the listed company, its shareholders, and the order of securities trading. From the corporate perspective, as the illegal facts became public, the company's market value plummeted to virtually zero, ultimately leading to its delisting by the exchange. This resulted in the loss of its qualification to raise funds through the securities market, the instantaneous collapse of its market reputation built over many years, and the subsequent paralysis of all its business operations. For the investor community, particularly minority shareholders, their invested capital suffered significant losses, severely damaging their property rights and interests.

Notably, this case set a precedent in China's securities field for resolving a class-action lawsuit through a settlement. Driven by the coordinated efforts of judicial and regulatory authorities, the relevant securities service institutions were required to bear joint and several liability for compensation, paying a substantial settlement sum to the affected investors. This institutional arrangement not only provided a referable model for investor rights remediation but also fully demonstrated the regulatory authorities' firm resolve to safeguard the legitimate interests of minority investors.

Considering the overall environment of the securities market, as a listed company on the STAR Market, Zeda Yisheng's fraudulent actions severely damaged the market credibility of the board's "hard tech" brand. It shook investors' fundamental trust in the truthfulness and accuracy of information disclosure, creating a negative impact on the integrity system construction and the healthy, orderly development of the capital market that will be difficult to repair in the short term.

2.2. Compilation of Core Fraud Information

2.2.1. Primary Perpetrator and Core Methods

The core perpetrator of this financial fraud was Zeda Yisheng Company itself, with the company's management playing a leading role throughout the entire fraudulent process. From designing the fraud scheme and colluding with upstream and downstream partners, to forging false documentation and manipulating financial data—all were advanced under the centralized arrangement of the management. The core fraudulent method employed by Zeda Yisheng was to construct fictitious trade transactions lacking genuine commercial substance to inflate revenue. The primary objective was unequivocal: to meet the financial threshold requirements for its IPO on the Science and Technology Innovation Board (STAR Market). The STAR Market imposes stringent requirements on core financial indicators such as revenue scale and revenue growth rate for prospective listing companies. As Zeda Yisheng's genuine operating performance failed to meet these standards, it chose to artificially inflate its revenue and profit data through fabricated trade activities, aiming to bypass scrutiny and achieve its goal of accessing the capital market.

2.2.2. Collaborating Parties in the Fraudulent Operations

The financial fraud at Zeda Yisheng was not carried out in isolation but involved a collusive chain of interests among multiple parties. The company actively conspired with its upstream and downstream partners, leveraging the capital and documentation support from related parties or cooperating enterprises involved in illicit benefit transfers to establish a complete closed loop of fictitious transactions. These collaborating enterprises, complying with Zeda Yisheng's directives, entered into fake purchase and sales contracts, facilitated fund transfers, and even assisted in forging logistics and acceptance documents, thereby serving as accomplices in the financial fraud. It was precisely due to the coordinated cooperation of these enterprises that Zeda Yisheng's fictitious trade operations maintained a formal semblance of completeness, allowing them to evade regulatory and audit scrutiny for an extended period.

2.2.3. Regulatory Investigation Outcome

The regulatory authority responsible for investigating this financial fraud case was the China Securities Regulatory Commission (CSRC). Through comprehensive and meticulous investigation, the CSRC clarified the fraudulent facts of Zeda Yisheng and imposed severe penalties in accordance with the law. Ultimately, besides Zeda Yisheng Company being compulsorily delisted, Tianjian Certified Public Accountants, which was responsible for the IPO audit and subsequent annual report audits, was also penalized. It received an administrative penalty involving confiscation and a fine totaling 9.24 million yuan. The relevant signing accountants were subjected to market entry bans, permanently prohibiting them from engaging in securities-related business. Simultaneously, intermediaries including the sponsor Dongxing Securities were also held accountable. Tianjian Certified Public Accountants and intermediaries such as Dongxing Securities were required to jointly pay 155 million yuan in settlement funds to investors. This series of penalties not only imposed heavy economic costs on the involved parties but also created a strong deterrent effect within the industry, conveying the regulators' firm stance of "zero tolerance" toward combating financial fraud.

2.3. Analysis of Fraudulent Operation Methods

2.3.1. Signing False Purchase and Sales Contracts

Entering into fictitious procurement and sales agreements with upstream and downstream enterprises constituted the initial step in Zeda Yisheng's execution of financial fraud, providing the foundation for constructing an illegitimate trade chain. The sales and purchase contracts signed by the company with its suppliers and customers strictly adhered to the formal standards of commercial agreements in terms of textual format, detailing core business terms such as product names, measurement units, transaction prices, delivery timelines, and settlement conditions. On the surface, these contracts appeared fully complete and compliant.

However, in essence, these agreements were "sham contracts" lacking any genuine transfer of goods. The rights, obligations, and transaction pricing stipulated therein were unilaterally and meticulously orchestrated by Zeda Yisheng, with the fundamental intent of fabricating revenue streams from core business operations. By executing such false agreements, Zeda Yisheng successfully inflated its operating revenue data in its accounting records, thereby embellishing

key indicators such as operational scale and expansion speed during the issuance application phase. This created a false image of the company as highly profitable with significant growth potential, ultimately enabling it to superficially meet the issuance review criteria for the Science and Technology Innovation Board (STAR Market).

2.3.2. Fabricating a Complete Set of Transaction-Supporting Documents

In order to enhance the surface credibility of its fabricated trade background, Zeda Yisheng systematically produced a complete set of transaction-evidence materials alongside the fictitious purchase and sales contracts, establishing a formally complete evidence system. These materials included warehousing receipts, logistics waybills, delivery confirmation documents, and value-added tax invoices, among others. Their format and elements meticulously simulated real business scenarios, meeting the formal requirements for accounting treatment and audit verification in terms of textual standardization and content completeness. Specifically, the fabricated waybills detailed information such as carrier vehicle numbers, loading and unloading addresses, and specific time points, while the forged delivery confirmation documents imitated the approval process of handling personnel, appearing fully compliant with procedural requirements in their presentation. However, in substance, the transfer of ownership and physical movement of goods corresponding to the aforementioned documents never actually occurred. There was neither a genuine process of inventory dispatch and transportation nor an actual goods receipt stage. The entire set of materials was specifically designed to support the fabricated transactions, with the fundamental intent of misleading regulatory authorities and auditors, thereby concealing the lack of commercial substance in the transactions.

2.3.3. Designing a False Closed-Loop Fund Circulation

Cash flow is a critical basis for verifying the authenticity of trade transactions. To make its fabricated trade activities appear more credible, Zeda Yisheng specifically designed a false closed-loop fund circulation operation. Specifically, funds were transferred out of Zeda Yisheng's company account and paid to upstream partner enterprises under the guise of purchase payments. After receiving the funds, these upstream partners, in accordance with pre-arranged agreements, transferred the funds to downstream partner enterprises. Finally, the downstream enterprises returned the funds to Zeda Yisheng's account under the pretense of sales receipts. Through this fund flow path, a false cycle of "fund payment → fund transfer → sales receipt" was created. From a financial accounting perspective, Zeda Yisheng's sales revenue appeared to be supported by corresponding fund inflows, further enhancing the deceptive nature of the fabricated trade activities.

In reality, however, these fund transfers were not accompanied by any actual goods transactions. They merely represented empty transfers between different corporate accounts, essentially constituting a self-orchestrated financial game.

2.3.4. Irregular Financial Data Processing

Upon the completion of the aforementioned actions involving the signing of false agreements, fabrication of documents, and execution of fund circulation schemes, Zeda Yisheng proceeded to engage in irregular accounting practices, systematically manipulating the data in its financial

statements.

First, regarding the revenue recognition process, the company seriously violated relevant accounting standards by recognizing operating income prematurely or falsely, without meeting the established criteria for revenue recognition. According to accounting standards, revenue from sales can only be recognized when the principal risks and rewards associated with the ownership of goods have been substantially transferred to the buyer. However, Zeda Yisheng confirmed revenue based solely on fabricated contracts and fund flows, in the absence of any actual delivery of goods.

Second, at the cost accounting level, the company matched the cost data with the inflated revenue by overstating costs and artificially adjusting the allocation ratios of period expenses (Healy & Wahlen, 1999). Specifically, the company reverse-calculated cost amounts based on the inflated revenue volume while simultaneously adjusting the allocation methods for expenses in accounts such as administrative expenses and sales expenses. This manipulation resulted in key indicators in the financial statements—such as operating revenue, net profit, and gross profit margin—exhibiting seemingly reasonable fluctuation trends and remaining broadly consistent with the financial metrics of industry peers. Consequently, these actions helped the company evade regulatory scrutiny and audit verification, thereby concealing the true nature of the financial fraud.

2.4. Comparative Analysis of Financial Indicators Before and After Fraud

2.4.1. Actual Operating Indicators

Under genuine operating conditions, Zeda Yisheng's main business revenue was entirely based on actual trade volume, with its business layout and market competitiveness positioned in the middle to lower tier of the industry. Consequently, its corresponding revenue scale was relatively limited. In terms of revenue growth rate, the company's growth aligned with the industry average. Influenced by factors such as market demand and industry competition, its growth pace was relatively moderate, with no signs of explosive expansion. Regarding asset operation efficiency, the company's accounts receivable turnover ratio remained within a normal range, and the collection speed of receivables was generally consistent with the industry average, matching the company's own sales policies and customer structure. Overall, Zeda Yisheng's actual financial indicators were mediocre, showing a significant gap from the "hard-tech" growth attributes expected of a company seeking listing on the STAR Market, thus failing to meet the financial threshold requirements for listing.

2.4.2. Abnormalities in Post-Fraud Financial Statement Indicators

Under the manipulation of financial fraud, the financial data disclosed by Zeda Yisheng presented a "stellar" performance that was completely contradictory to its actual operational reality. In terms of revenue scale, the post-fraud operating revenue was significantly inflated, far exceeding the company's genuine operational capacity. Furthermore, it exhibited a sustained and rapid growth trend during the IPO application period, fully meeting the financial indicator requirements for listing on the Science and Technology Innovation Board (STAR Market). Regarding the revenue growth rate, the post-fraud figure was substantially higher than the

industry average, showing an "abnormally impressive" growth trajectory that sent a misleading signal to the market and investors about the company's strong development momentum.

However, behind the seemingly prosperous financial data lay difficult-to-conceal indicator anomalies (Wang, 2023), the most evident being the accounts receivable turnover ratio. As the accounts receivable corresponding to the fictitious revenue were largely suspended on the books for extended periods and could not be genuinely collected, the company's accounts receivable turnover ratio exhibited abnormal fluctuations—either artificially inflated or depressed. This severely mismatched the disclosed revenue growth rate and also showed a significant deviation from the accounts receivable turnover levels of industry peers. These indicator anomalies should have been a key focus for regulatory and audit scrutiny.

2.4.3. Exposure of Audit Negligence Issues

The numerous abnormal indicators presented in Zeda Yisheng's financial statements should have provided crucial leads for the audit work. However, Tianjian Certified Public Accountants, the firm undertaking the audit engagement, failed to effectively fulfill its verification responsibilities, ultimately missing the fraudulent activities. This constituted a classic case of audit failure. According to auditing standards, Certified Public Accountants are required to perform sufficient audit procedures on key areas such as the authenticity of the auditee's revenue and the recoverability of accounts receivable. Specific procedures include sending confirmation requests to debtors, reviewing sales agreements and shipping documents, and conducting on-site client visits.

However, during its engagement, Tianjian CPA did not effectively verify the purchase and sales agreements or shipping documents. Its review of critical areas such as revenue recognition and cost measurement was merely perfunctory. The firm neither conducted an in-depth analysis of the abnormal accounts receivable turnover situation nor verified the authenticity of significant sales transactions. Consequently, it failed to detect the financial fraud schemes and issued a misleading audit opinion. This action not only severely infringed upon the legitimate rights and interests of investors but also resulted in substantial consequences for the firm itself.

3. Analysis of Motivations for Financial Fraud

3.1 Corporate Level: Listing Aspirations and Profit-Driven Motives

3.1.1. Meeting the Financial Threshold for Listing on the STAR Market

As a specialized capital market segment focusing on "hard-tech" enterprises, the Science and Technology Innovation Board (STAR Market) sets clear and stringent financial thresholds for prospective listed companies, including core indicators such as revenue scale and growth stability. These thresholds are essential prerequisites for successfully listing on this board. Under actual operating conditions, Zeda Yisheng's business development was relatively stagnant, with its revenue scale consistently ranking in the middle to lower tier of the industry. Its growth lacked momentum, and its core financial data fell significantly short of the STAR Market's listing review standards. Had the company applied with its true performance, its listing application would

inevitably have been rejected.

For the company, listing on the STAR Market not only meant gaining access to stable capital market financing channels but also leveraging the board's endorsement to enhance brand visibility and expand business cooperation opportunities. These potential benefits made it difficult for the management to abandon the goal of going public. Faced with the reality that its genuine performance could not meet the requirements and was unlikely to improve through compliant operations in the short term, the management ultimately abandoned the path of long-term compliant development. Instead, they chose to artificially inflate revenue and profit data through financial fraud (Dechow et al., 1996), systematically embellishing the financial statements during the IPO application period. This approach was intended to precisely meet the various rigid indicator requirements for the listing application, attempting to fulfill the core objective of listing on the STAR Market through fraudulent means.

3.1.2. Chasing Excess Profits in the Capital Market

The multiple excess benefits that a company can leverage after a successful listing are the core driving force behind Zeda Yi Sheng's implementation of financial fraud. In terms of direct benefits, the rise in stock price after listing directly leads to substantial appreciation of shareholders' equity, which is highly tempting for company management and key shareholders (Jensen & Meckling, 1976). At the same time, maintaining an artificial high market valuation can create favorable conditions for subsequent refinancing activities such as private placements and convertible bond issuances, further broadening financing channels and reducing financing costs. In terms of indirect benefits, being a listed company inherently brings brand premium effects, which can enhance the company's influence and voice within the industry, increase trust among customers and partners, and facilitate market expansion and business cooperation. Additionally, listed companies have obvious advantages in bank lending and supply chain negotiations, enabling them to obtain resource support at lower costs. The combination of these direct and indirect benefits traps management in short-term gain thinking, causing them to completely overlook the importance of compliant operations for the company's long-term healthy development and regard financial fraud as a 'shortcut' to quickly obtain profits, thereby reinforcing the decision to commit fraud.

3.2. Management Level: Lack of Ethics and Accountability Deficiencies

3.2.1. Weak Awareness of Business Ethics

The management of Zeda Yisheng generally lacked fundamental integrity in business operations and a sense of social responsibility, relying on short-term speculative behavior rather than long-term value creation for corporate development. When formulating corporate strategies, the management's focus was consistently centered on personal interests and the company's short-term performance. They one-sidedly pursued the personal fame and gains brought by a successful IPO and the short-term valuation boost for the company, entirely overlooking the potential harm that financial fraud could inflict on investors, capital market order, and even the broader socio-economic environment. The principles of "truthfulness, accuracy, and completeness" in information disclosure are fundamental norms of the capital market and the baseline that

companies must adhere to. However, to achieve the goal of listing, the management of this company blatantly violated this core requirement, deceiving regulatory authorities and investors through fabricated transactions and falsified data. This fully reflects a severe lapse in business ethics and a lack of the professional integrity and accountability expected of corporate managers.

3.2.2. Failure of Internal Control Mechanisms and Abuse of Power

The company's internal governance structure exhibited significant defects, with internal control mechanisms becoming mere formalities that failed to effectively constrain or supervise management decision-making (Beasley, 1996). In daily operations, the management held absolute decision-making authority, while the oversight functions of the board of directors and the supervisory board were severely weakened. This led to an ineffective system of checks and balances, ultimately resulting in a management landscape dominated by a "one-person rule."

This imbalanced management model enabled the management to seamlessly orchestrate the entire process of financial fraud without any hindrance. From designing fictitious trade chains and coordinating collusion among upstream and downstream partners to forging purchase and sales contracts, logistics documents, and other supporting evidence, and finally manipulating financial data and compiling false financial reports—each step proceeded without undergoing rigorous internal approval or supervision, nor was there any concern about detection by internal oversight bodies. The absence of a robust internal monitoring mechanism created a conducive environment for financial fraud, allowing the management's fraudulent intentions to be effortlessly translated into actual actions.

3.3. External Environmental Level: Dual Impact of Regulation and Market Environment

3.3.1. Window Period in Initial Review and Supervision

As an innovative sector of China's capital market, the Science and Technology Innovation Board (STAR Market) was in a phase of rapid expansion and mechanism refinement during its initial establishment. In this special period, the workload of listing reviews was substantial, and the pace was fast. The details of the review mechanism were continuously being adjusted and optimized based on market conditions, resulting in certain limitations in the depth and breadth of verifying the business authenticity of some listing applicants. This created a temporary regulatory window period (Ye, 2018).

The management of Zeda Yisheng keenly identified this regulatory characteristic and meticulously designed a complete fraud chain of "fake contracts - forged documents - closed-loop funds." By masking the lack of genuine trade substance behind seemingly compliant surface processes, they successfully circumvented some of the verification steps in the initial review. During the early-stage checks, regulatory authorities, lacking mature experience in detecting such systematic fraud, failed to promptly uncover their fraudulent methods. This allowed the company to narrowly pass the listing review, providing a critical external opportunity for the implementation of the fraud.

3.3.2. Survival Anxiety Under Industry Competition Pressure

The niche sector in which Zeda Yisheng operates is characterized by intense competition, with

cyclical fluctuations in market demand heavily influenced by both macroeconomic trends and technological industrial transformations. Industry players generally face multiple pressures from battling for market share and breaking through with technological innovations. In comparison, Zeda Yisheng exhibited significant shortcomings in key areas such as technological R&D breakthroughs, marketing network development, and cultivating core product advantages, showing a notable gap compared to industry leaders. This placed its actual operational quality at risk of continuous deterioration.

Amidst the dual pressures of cutthroat industry competition and a sense of survival crisis, the decision-makers failed to focus on building core competitive barriers through standardized paths such as independent R&D, product structure upgrades, and operational efficiency improvements. Instead, they fell into the cognitive bias of short-sightedness, opting for the desperate measure of financial data fraud. Their intent was to fabricate inflated operating performance to maintain the company's artificially high image in the capital market, thereby misleading investors and business partners and alleviating the imminent operational difficulties. However, following the exposure of the fraudulent activities and the subsequent compulsory termination of its listing qualification, the company ultimately plunged completely into an operational quagmire.

4. Analysis of Business Ethics Issues

4.1 Lack of Corporate Integrity: Violation of Basic Business Ethics Principles

4.1.1. False Information Disclosure Infringes on the Right to Know

Integrity is the cornerstone upon which the capital market survives and develops. Truthful and transparent information disclosure is a core prerequisite for ensuring the effective functioning of the capital market. Market participants, including investors, regulatory authorities, and partners, all rely on the truthful information disclosed by companies to make investment decisions, enforce regulations, and assess collaborations. To achieve its listing goal, Zeda Yisheng blatantly violated the fundamental business ethics of "honesty, trustworthiness, fairness, and justice." By fabricating trade activities, falsifying financial data, and compiling fraudulent financial reports, the company disseminated false information to the market. Based on this inaccurate information, the majority of investors misjudged the company's operational condition and investment value, leading to misguided investment decisions (Li, 2025). Not only was their statutory right to know severely infringed upon, but the funds they invested also suffered significant losses due to the company's delisting. Furthermore, such behavior severely undermined the principle of truthfulness in capital market information disclosure, shook the trust foundation that market participants place in the information disclosed by listed companies (Fan & Wong, 2002), eroded market confidence, and disrupted the normal operational order of the capital market.

4.1.2. Erosion of the Spirit of Contractual Integrity Undermines Commercial Order

Zeda Yisheng's actions also severely eroded the spirit of contractual integrity that underpins commercial order. By signing false contracts with upstream and downstream partners, the company not only engaged in deception itself but also implicated other enterprises in unethical

practices. This behavior corrodes the foundational trust required for stable commercial relationships. When contracts are rendered meaningless as tools of fraud, the entire system of commercial exchange is threatened, increasing transaction costs and fostering an environment of suspicion. Such erosion of contractual integrity has lasting negative repercussions on the broader commercial ecosystem, far beyond the immediate parties involved.

4.2. Neglect of Stakeholder Responsibilities: Triggering Multiple Ethical Crises

4.2.1. Deficiency in Responsibility Towards Investors

Small and medium investors constitute a vital component of the capital market and represent one of the core sources of funding for corporate financing. Companies bear a fundamental fiduciary duty to investors, including the obligation to disclose information truthfully and ensure investment security along with reasonable returns. As a company seeking listing and subsequently listed, Zeda Yisheng should have fully respected the rights and interests of its investors and created value for them through genuine operational performance. However, the company deceived investors through financial fraud, causing a large number of small and medium investors to suffer severe financial losses due to false information, with some investors even losing their entire capital. This behavior completely deviated from the company's fiduciary duty to its investors, triggering a serious investment ethics crisis (Li, 2025). Although subsequent compensation was paid to investors by the involved intermediaries through the securities class action settlement mechanism, the investors' total losses could not be fully compensated. More importantly, such a breach of trust is difficult to repair in the short term, causing long-term negative impacts on investor confidence in the market. This has led some investors to develop fear and distrust toward the capital market.

4.2.2. Deviation from Responsibilities Towards Regulation and Society

As a crucial component of the socio-economic system, enterprises are not only market operators but also bearers of social responsibility. Complying with laws and regulations, maintaining market order, and promoting the healthy development of the socio-economy are fundamental social responsibilities that enterprises must fulfill. Laws and regulations such as the Securities Law explicitly prohibit practices like financial fraud and false information disclosure, which represent the baseline requirements for corporate operations. However, Zeda Yisheng, fully aware that its actions were illegal, chose to take risks by deliberately evading regulation and deceiving the market. This not only challenged the enforcement authority of regulatory bodies but also severely harmed public interests.

As a company listed on the STAR Market, its label as the "first stock implicated in fraud" severely undermined the credibility of the STAR Market's "hard-tech" positioning. This has led to market skepticism regarding the authenticity of information disclosed by STAR Market companies, affecting the board's core function of serving the real economy and supporting technological innovation. Simultaneously, its actions disrupted the efficiency of resource allocation in the capital market, diverting social funds to companies with falsified performance and wasting precious market resources. Such conduct contradicts the social responsibility and accountability that enterprises ought to uphold.

4.3. Anomie in Industry Ethics: Undermining the Professional Ethics of Intermediary Institutions

4.3.1. Intermediary Institutions' Collusion in Fraud Violates Professional Standards

Securities service institutions (including audit firms and sponsors), serving as the "gatekeepers" of the capital market, have the fundamental responsibility to ensure the truthfulness, accuracy, and completeness of information disclosed by issuers through diligent verification and supervision. This is essential for establishing a fundamental barrier for risk prevention and control in the securities market. According to professional standards, auditors are required to conduct prudent examinations of the substance of transactions and the compliance of financial data, while sponsors must comprehensively verify the qualifications and the authenticity of the performance of listing applicants.

However, in the case of Zeda Yisheng, Tianjian CPA, which was responsible for the IPO audit, failed to effectively carry out key procedures such as reviewing sales agreements, verifying logistics documents, and confirming intercompany balances through external confirmations. It also did not conduct in-depth investigations into significantly abnormal financial indicators. At the same time, sponsors such as Dongxing Securities failed to strictly fulfill their sponsorship duties and did not identify the company's fraudulent activities. Such negligence by these intermediary institutions essentially turned them into "accomplices" in Zeda Yisheng's financial fraud, seriously deviating from professional ethics and norms. This breached the risk prevention baseline of the capital market and significantly amplified the harm caused by the fraudulent activities.

4.3.2. Industry Trust Crisis Impacts the Ethical Ecosystem

The failure of securities service institutions to exercise due diligence, as revealed by the Zeda Yisheng incident, has led to widespread skepticism and a crisis of confidence among investors regarding the credibility of the entire securities service industry's professional integrity. As critical intermediaries connecting issuers with securities trading venues, the compliance and professional standards of these institutions directly determine the sound operation of the securities market.

In this case, the involved service providers failed to uphold professional ethical boundaries, prioritizing economic benefits such as audit fees and underwriting revenues over risk management. Such behavior not only resulted in severe regulatory penalties for themselves—for instance, Tianjian Certified Public Accountants was fined and penalized 9.24 million yuan, and relevant responsible individuals were subjected to market entry bans—but also caused significant damage to the ethical environment of the entire industry.

Investors' trust in securities service institutions has noticeably diminished, making them less likely to readily accept assurance reports, sponsorship documents, and other certifications issued by professional service organizations. The cost for companies seeking listing to issue securities in compliance with regulations has also increased, requiring them to expend more resources to substantiate the authenticity of their operating results. Meanwhile, improper competition within the industry has intensified, as some institutions may lower their verification standards for fear of losing clients, further exacerbating the disorder in industry ethical norms. Ultimately, this has

profound negative implications for the stable development of the securities market and the reconstruction of its ethical order.

5. Analysis of Audit Failure Causes

As the first company exposed for fraud on the STAR Market, Zeda Yisheng engaged in systematic financial fraud spanning from its IPO application period to the post-listing continuous supervision phase. This fraud ultimately went undetected by the audit firm. The core issue lies in Tianjian Certified Public Accountants violating audit standards and professional ethics throughout the entire audit process. The firm failed to effectively verify the complete fraud chain involving "false contracts - forged documents - closed-loop funds," ultimately allowing false financial information to enter the capital market and creating a classic audit failure case.

5.1. Audit Procedures Were Carried Out Perfunctorily, with Critical Evidence Verification Omitted

5.1.1. Contract and Voucher Verification Was Superficial

Auditors failed to conduct thorough verification of the fraudulent purchase and sales contracts signed by Zeda Yisheng. They neither verified the alignment of transaction subjects with the core businesses of both parties nor the market fairness of transaction prices. They also neglected to investigate obvious anomalies in some contracts, such as "signing dates later than logistics acceptance dates" and "discrepancies between customer registration addresses and actual business locations." They remained oblivious to the deliberately designed "shadow contracts." Additionally, for supporting documents like fabricated warehouse receipts, logistics transport records, and acceptance certificates, auditors relied solely on scanned copies and stamped photocopies provided by the company. They failed to conduct substantive verification methods such as on-site visits to logistics firms, cross-checking transport vehicle routes, or telephone follow-ups with clients. Consequently, they completely missed that the goods flows corresponding to these documents were entirely fictitious.

5.1.2. Omissions in Fund and Metric Verification

During fund flow verification, auditors failed to trace the complete path of capital movements. They merely cross-checked superficial financial transactions between Zeda Yisheng and its upstream/downstream enterprises, failing to recognize the closed-loop circular nature of funds flowing out of Zeda Yisheng, transiting through related parties, and then returning under the guise of sales receipts. This allowed the fraudulent chain of "fictitious transactions + fund recycling" to remain unbroken. Furthermore, regarding abnormal signals revealed in the financial statements—such as the accounts receivable turnover rate fluctuating wildly for consecutive years, revenue growth rates exceeding the industry average by more than threefold, and cost allocation ratios showing significant discrepancies compared to peers—auditors failed to execute additional audit procedures (Albrecht et al., 2008). Instead, they hastily dismissed these anomalies as "normal phenomena during business expansion," completely squandering a critical opportunity to identify fraud through financial indicator irregularities.

5.2. Seriously Compromised Audit Independence and Professional Judgment Influenced by Interests

5.2.1. Client Interests Hijack Audit Stance

As a key client of Tianjin Certified Public Accountants, Zeda Yisheng's IPO audit and subsequent annual report audit services provided the firm with stable and substantial revenue, with the project's annual fees accounting for 9.1% of the firm's revenue that year. To maintain this long-term relationship, the audit firm repeatedly compromised on unreasonable demands made by the company during the audit process. For instance, it failed to reject non-compliant requests such as "simplifying the on-site verification process for logistics documents," "omitting confirmation letters for certain large related-party clients," and "reducing the scope of verification for R&D expenditures" in accordance with auditing standards. Instead, it proactively narrowed the verification scope and lowered verification standards.

5.2.2. Audit Opinions Deliberately Catering to the Company

Auditors identified multiple non-compliance issues during the audit, including revenue recognition timings inconsistent with contract terms, cost allocation ratios lacking reasonable basis, and inadequate disclosure of related-party transactions. However, they failed to insist on corrective adjustments. Instead, swayed by the company's lobbying and financial inducements, they chose to "turn a blind eye." Ultimately, the audit firm issued an unqualified audit opinion aligned with the company's wishes, causing the audit work to completely lose its core principles of objectivity and impartiality. It became a "tool" for the company to embellish financial data and achieve its listing goals.

5.3. Risk Assessment System Failure and Insufficient Professional Competence

5.3.1. Risk Identification Disconnected from Industry Characteristics

Zeda Yisheng operates in the pharmaceutical IT sector—a capital-light, R&D-intensive field—and was undergoing IPO filing, a stage prone to fraud. Compounded by the financial threshold pressures under STAR Market's "hard technology" positioning, this should have been classified as an extremely high-risk audit project. However, the audit firm continued to apply risk assessment models designed for traditional manufacturing. Failing to incorporate industry-specific characteristics and IPO-stage risk features, it inadequately prioritized critical risk points such as "fictitious revenue," "related-party fund occupation," and "manipulation of R&D expenditure capitalization." This resulted in audit resources not being allocated to high-risk areas, causing a significant deviation in verification priorities.

5.3.2. Insufficient Professional Capabilities to Address High-Risk Projects

Auditors lacked deep understanding of STAR Market companies' business models and lacked experience identifying fraud techniques employed by Zeda Yisheng, such as inflating revenue through fake project contracts, fictitious client collaborations, and fabricated technical service deliverables. When verifying R&D expenditures and intangible assets, auditors failed to validate their authenticity and reasonableness against industry-specific technical characteristics. For instance, they confirmed the value of the company's inflated RMB 82 million in software

intangible assets solely through invoice copies, without conducting on-site functional testing or third-party assessments. Additionally, the audit team demonstrated significant deficiencies in professional judgment. They failed to promptly detect violations of accounting standards, such as the company's improper revenue recognition without actual goods delivery and retroactive cost adjustments based on inflated revenues, exposing gaps in their professional capabilities.

5.4. Quality Control Mechanisms Prove Ineffective, Review Procedures Fail to Function

At the risk prevention level, Tianjian Certified Public Accountants' internal quality control mechanisms failed to fulfill their intended purpose, resulting in superficial reviews throughout the entire process. First, during the internal review within the project team, reviewers focused solely on the formal compliance of audit files. They failed to question significant omissions such as "failure to perform confirmation for large accounts receivable" and "lack of substantive verification for freight documents," nor did they validate the sufficiency and appropriateness of audit evidence. Second, regarding independence quality reviews, the firm failed to adhere to the principle of separating reviewers from the project execution team. Review duties were assigned to personnel who had participated in the project's preliminary investigations, compromising the independence and objectivity of quality control and hindering the identification of systemic deficiencies in the audit process. Furthermore, the firm failed to establish dedicated quality management procedures for initial public offering audits and lacked effective oversight mechanisms for monitoring audit procedure execution. Consequently, it failed to promptly detect auditors' negligence and non-compliant practices during verification work. This nominal quality control model prevented internal correction of various deficiencies arising during the audit process, ultimately leading to an inaccurate audit opinion.

5.5. Insufficient Coordination Among Regulatory Authorities Leaves Weak Response to Multi-Party Collusive Fraud

Audit institutions have failed to establish effective regulatory synergy with other market intermediaries, lacking the necessary capabilities to identify and address financial fraud orchestrated through collusion among multiple parties. The accounting fraud at Zeda Yisheng was not an isolated incident but rather a coordinated network of deception involving suppliers, clients, and related parties, encompassing collaborative elements such as forged agreements, circular fund flows, and altered vouchers. However, during their engagement, the audit firm failed to establish information-sharing and joint verification mechanisms with sponsors like Dongxing Securities. They relied solely on their own audit evidence, neglecting to fully integrate external information resources such as the sponsor's due diligence materials and regulatory pre-approval opinions. Furthermore, regarding unusual transactions between the issuer and counterparties, the audit firm failed to conduct substantive verification of related-party relationships between the transacting parties. Instead, it accepted unilateral "no related-party relationship" statements issued by the enterprises at face value, thereby failing to uncover the true nature of the multi-party collusive fraud. This audit model, lacking collaborative coordination (Rezaee, 2005; Ye et al., 2022), made it difficult for auditors to penetrate the meticulously constructed fraudulent defenses of the enterprise, ultimately failing to detect the systemic financial fraud.

6. Conclusion

As a landmark case during the early stages of the STAR Market and the comprehensive registration-based IPO system, the Zeda Yisheng financial fraud case carries far-reaching implications and profound warnings. This case not only fully exposes the systematic chain of fraud meticulously orchestrated by the company to meet listing financial thresholds and pursue short-term capital gains—encompassing the signing of fake contracts, forgery of complete sets of vouchers, closed-loop fund designs, and non-compliant financial treatments—but also lays bare the intertwined risks during the market's rapid expansion and institutional adjustment period, including corporate governance failures, ethical lapses among management, breaches of gatekeeper responsibilities by intermediaries, and inadequate regulatory coordination. The case concluded with forced delisting and substantial civil damages, demonstrating regulators' zero-tolerance stance toward financial fraud. It also pioneered a practical pathway for investor protection through the class action settlement mechanism, effectively addressing market expectations for rule-of-law-based, market-oriented punishment and redress mechanisms.

Analysis of this case demonstrates that financial fraud is never an isolated incident perpetrated by a single entity, but rather the result of the combined effects of specific institutional environments, market pressures, corporate governance, and the quality of intermediary practices. Several key insights can be drawn from the Zeda Yisheng incident: First, while the registration system centers on information disclosure, the quality of such disclosure depends not only on issuers' self-discipline but also on the professional diligence and effective oversight of intermediaries. The lack of independence among audit firms, the formalization of procedures, and inadequate risk response capabilities directly led to fraudulent information not being filtered out, highlighting the urgency of strengthening intermediaries' ethical responsibilities and practice quality control. Second, preventing systemic, collusive fraud requires building a comprehensive governance system spanning corporate internal controls, intermediary verification, regulatory review, and daily monitoring. Particular attention should be paid to identifying complex methods such as collusion between upstream and downstream entities and closed-loop capital fraud, leveraging technological regulatory tools to enhance the ability to penetrate business substance and capital flows. Third, while the STAR Market is positioned to serve "hard technology" enterprises, the "hard technology" attribute cannot be simplistically equated with high growth in financial metrics. Review and oversight must balance innovation encouragement with substantive assessments of business authenticity, technological advancement, and growth logic, preventing companies from manipulating data to meet standards. Fourth, investor protection must shift from post-event punishment to equal emphasis on real-time alerts and post-event remedies. Refining diversified dispute resolution mechanisms and enforcing joint liability for intermediaries will foster a market ecosystem where fraudsters face consequences and victims have recourse.

Although the Zeda Yisheng case has concluded, the issues it exposed demand ongoing reflection and improvement from all capital market participants. Only when issuers uphold integrity, intermediaries fulfill their duties, regulators enforce with precision and strength, and investors act rationally and maturely can we collectively fortify the foundation for healthy capital market development under the registration-based system, truly achieving dual enhancements in

resource allocation efficiency and investor rights protection. Looking ahead, as regulatory frameworks continue to mature, enforcement capabilities steadily strengthen, and a culture of market integrity gradually takes root, malicious fraud cases like Zeda Yisheng's are expected to be more effectively curbed. Through ongoing case reflection and institutional refinement, China's capital markets will advance toward a new phase of development characterized by greater standardization, transparency, and resilience.

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