Analysis of the Ponzi Scheme in P2P Platform: Taking Ezubo as an Example

Yilin Cao [1], Xiaohan Zhang [2], Xinwen Zhang [3, *]

[1] Department of Accounting, Zhuhai College of Beijing University of Technology, Zhuhai, China

[2] Department of Applied Economics, Beijing Normal University - Hong Kong Baptist University United International College, Zhuhai, China

[3] Department of Smart Accounting, Northeast Agricultural University, Harbin, China

* Corresponding Author Email: a08210241@neau.edu.cn

Abstract. Driven by economic development, P2P online lending platforms have become a new area for the development of the financial industry. The rise of P2P platforms reflected the improvement in people's quality of life and the increasing demand for investment. This is good for economic development, but it also increases the difficulty of market supervision, and investment fraud from the perspective of Ponzi schemes is becoming more and more serious. This paper took Ezubo as an example to study the causes of the Ponzi scheme. According to research, it was found that the formation of a Ponzi scheme was closely related to corporate financial fraud, corporate and P2P risk problems, and social factors. The paper analyzed Ezubo's financial fraud, conducted risk analysis, and made suggestions on risk management and strengthening education. This paper helps to complement the shortcomings of current research on Ponzi schemes, and the advice on such behavior also has some practical implications to help people stay away from investment fraud.

Keywords: Ponzi scheme; Ezubo; investment fraud; risk analysis.

1. Introduction

With the continuous development of the economy, people's living standards improve and the demand for investment has gradually increased. At the same time of rapid economic development, China's Internet finance has developed initially, supporting facilities are not perfect, and people's understanding is low, which increases the difficulty of supervision [1]. Ezubo, as a P2P platform, designed a Ponzi scheme to raise funds illegally, harming the interests of countless investors, and having negative impacts on the development of the economy. Compared with Western countries, Internet finance developed late in China, and there are few studies on Ponzi schemes. This paper analyzed Ezubo, clarified the reasons for the Ponzi scheme, and proposed some suggestions. An in-depth study of Ezubo's Ponzi schemes is beneficial for individuals to understand the Ponzi schemes in a specific situation or a company. It urges enterprises to understand legitimate investment and formulate reasonable investment strategies. This paper has also enriched the theory of the cause of the Ponzi scheme and the analysis of Ezubo, providing theoretical and practical significance for the subsequent researches.

2. Ezubo's Ponzi Scheme Introduction

2.1. Company Overview

2.1.1. Introduction of the Ezubo platform

Ezubo, known as "Jin Yi Rong (Beijing) Network Technology Co., Ltd.", is a wholly-owned subsidiary of Anhui Yucheng Group, established in July 2014, with a registered capital of 100 million RMB [2]. Ding Ning, Peng Li'an, and Zhang Min are in charge. In November 2015, the cumulative turnover of Ezubo exceeded 70 billion yuan, and the total number of investors exceeded 900,000 people [3]. However, it didn't last long. On December 16th, 2015. Ezubo was accused of potential illegal fund-raising. So far Ezubo has been the largest "illegal fundraising" P2P platform in China.

This was also the first time for China's legal department to judge the self-financing nature of P2P platform funds.

2.1.2. Ezubao's business model

Ezubo was committed to building financing bridges for lessors, lessees and investors and provided mid-market support. Ezubo operates in A2P mode, the online lending model of financial leasing and internet finance. Ezubo as an intermediary, by releasing the project, get funds from investors. The funds would be invested in its financial leasing company, the platform will obtain a debt transfer contract from a financing leasing company, which will purchase the leased property from the supplier according to the lessee's needs, and the water well will be provided to the lessee for use, and the lessee will regularly pay rent to the platform [2]. The platform will pay interest to investors and repay the principal before the due date. The platform would pay the interest to the investor and repay the principal at maturity. Among them, the factoring company did risk control and provided a bad debt guarantee for the platform, and the guarantee companies bore responsibility to protect the rights and interests of investors. In addition, Ezubo had strong external publicity, which aimed to attract more investors.

2.2. Basic Information of Ezubo Ponzi Scheme

2.2.1. Principle of the Ponzi scheme

The Ponzi scheme refers to a kind of financial fraud, which, according to the definition of the SEC, takes the investment of newly added investors as the return of investment to existing investors. Organizers of Ponzi schemes usually promise to invest investors' funds in so-called low-risk or no-risk projects and induce investment opportunities with high yields to continuously recruit new investors.

2.2.2. Ezubo's behavior of using the Ponzi scheme

Most of the financial products on the "Ezubo" platform had an expected annual yield of 13% to 15% in 2016. During the same period, the expected annual rate of return of financial products under other financial enterprises was only around 8% [3]. It was much higher than the market average yield, attracting many investors. E-Cheng Group concocts a large number of companies with financing needs by buying enterprises or registering shell companies, signing agreements with them, and then fictitious projects on the "Ezubo" platform, releasing relevant financing news, Ezubo Group because there was no actual investment channel to obtain income or the return on investment was far less than the promised return on investment, so for the return on investment of old customers, can only rely on the addition of new customers or other financing arrangements to achieve [4]. The higher investment return lasted only by relying on the joining in of new customers. The business scope of E-Cheng Group was mainly to promote financing projects, including eight major business segments, including "Ezubo" online sales and "Ezubo" offline sales, most of which were set up around the operation of "Ezubo". This allows the range of its customer distribution to expand. At the same time, the company used 1.5% to 2% of the financing amount to buy information from enterprises and released false projects on the platform to attract more funds.

2.3. The Consequences of the Ezubo's Ponzi Scheme

In September 2017, the Beijing First Intermediate People's Court publicly pronounced the verdict on this case in accordance with the law. Yucheng International Holding Group Limited Company fined RMB 180.3 million Anhui Yucheng Holding Group was fined RMB 100 million for fundraising fraud. Ding Ning commits the crimes of fundraising fraud, smuggling precious metals, illegal possession of firearms, and cross-border smuggling, and is sentenced to life imprisonment, deprivation of political rights for life, and a fine. Other people were also punished. On January 16, 2020, the "Ezubo" and "Sesame Finance" networks participated in fundraising and participated in information verification and registration of damaged fundraising participants for fund withdrawal [2].

With the decline of Ezubo Company, the country has also introduced a series of policies to increase the management of P2P platforms.

3. Analysis of the Causes of Ezubo's Ponzi Scheme

3.1. Financial Factors

According to relevant information, the financing enterprise of "Financial Leasing Debt Transfer Project No. 156B " was "Anqing Shengyang Chemical Co., Ltd.", according to the information of the national enterprise credit information publicity system, the enterprise "lost 2.17 million yuan and liabilities of 41.66 million yuan in 2013; In 2014, it lost 2.42 million yuan and lied 41.66 million yuan", and through the Internet, you can search for contract disputes in the financing company. However, according to the introduction page of the e-lease platform, as shown in Table 1 the company "had an annual sales revenue of 91.6465 million yuan in 2014, a net profit of more than 7.4 million yuan, and a net profit margin of 8.08%, which can fully cover the principal and interest of this loan". This financial fraud also confirms that the Ezubo treasure was a complete Ponzi scheme, and this financial fraud was also one of the causes of the Ponzi scheme. Ezubo's treasure was to create the illusion of making money as the traction, tear down the east wall to make up the western wall, use the money of new investors to pay interest and short-term returns to old investors and cheat more investment.

Table 1. Ezubo Financial Information.

Enterprise asset status information			
Total assets	52 million yuan	Total owner’s equity	2.34 million yuan
Total operating income	6.19 million yuan	Total profit	-2.42 million yuan
The main business income of the total operating	6.19 million yuan	Net profit	-2.42 million yuan
Total tax	120,000 yuan	Total liabilities	41.66 million yuan

3.2. Platform Risk Factors

The three risks of the Ezubo platform were also the causes of Ponzi schemes. First, there was a pool of funds. Internet platforms only provide information intermediary services, cannot set up their own capital pools, and do not provide credit guarantees. However, according to the investigation, the funds absorbed by "Ezubo treasure" enter the self-set capital pool in the form of a "borrowing" third-party payment platform. Another point was that users were not aware of the management of the funds and their actual use after obtaining the investment funds. "Ezubo" took advantage of this vulnerability to carry out huge fraudulent activities, created fake non-existent wealth management products, frantically absorbed funds, and then closed the loophole for the recovery of funds from previous lenders. Second, the quality of information disclosure was low [5]. A careful observation of the Ezubo platform will show that the packaging of the operation team was too beautiful. The incomplete disclosure of the borrower's information does not rule out that the borrowing company was a shell company, fabricating borrowing facts and illegal fraud. By falsifying information, the company was whitewashed and the public was "making money", thereby completing the entire Ponzi scheme [6]. Third, there were related party transactions and there was suspicion of self-financing. The business taken over by Ezubo was mainly in the form of financial leasing, and the entire transaction process should be to transfer the claims obtained by the financial leasing company to the investors. However the guarantee company and factoring company of Ezubo also had a close relationship with E-Cheng Group, so it was difficult to clear the suspicion of self-financing of related party transactions. Ezubo was "self-financing and self-investment", so as to boost the popularity of the platform and induce new investors to enter so that the nominal deposit absorption amount was higher than the actual deposit absorption amount. Therefore, Ezubo was more convinced that it was a Ponzi scheme.

3.3. Social Factors

3.3.1. Incomplete policies

From 2014 to 2016, the number of P2P lending platforms grew exponentially, reaching 2,238 in 2014, an average increase of 335.4% per year. Ezubo was founded at the beginning of July 2014. Due to the rapid expansion of P2P platforms, risks accumulated seriously, but the policy had not yet landed, leading many enterprises to seize the loopholes of the system. Ezubo secretly carried out a Ponzi scheme. At that time, there were few management policies on Ponzi schemes and P2P platforms, which led to the continuation of such behaviors of Ezubo and there was little public attention.

3.3.2. Herd effect

Ponzi schemes have been around for hundreds of years, and although they are constantly being debunked and cracked down, they still exist. Its roots lie in seizing on human weaknesses and then using new technologies to wrap themselves up and present themselves to society with a credible appearance. One of the most typical is the herd effect. The herd effect refers to the mentality that people tend to follow blindly and follow the crowd. In the case of inadequate information, people are easily influenced by other investors and imitate the decisions of other investors without considering their own actual situation [7]. Many investors in Ezubo were those who saw the short-term gains made by their friends and relatives and were recommended and tempted by them to enter the scheme without analyzing the essence of Ezubo. Ezubo made use of people's lack of knowledge about investment and their greed to make a profit. The Ponzi scheme it utilized was well hidden.

4. Suggestions

4.1. Emphasize the Effectiveness of Supervision

As an important means of financial supervision, finance was conducive to improving the risk management system, strengthening information disclosure, and promoting legal operations. Therefore, the introduction of Internet finance was crucial to improving the internal and external regulatory system and promoting the healthy development of Internet finance [6]. When building an internal control system for Internet financial enterprises, the management should attach great importance to the special role of internal financial auditing, reasonably set up an internal audit organization, and avoid all financial fraud. The department should make use of its unique information advantages, fully and timely obtain all kinds of information in the process of enterprise operation, and continuously track and supervise the audited economic activities, so as to facilitate the management to obtain daily work reports and ensure the effectiveness of supervision. In the "Ezubo" incident, the platform conspired with the guarantee company to defraud, causing investors to suffer huge losses.

4.2. Enhance the Risk Management of Platforms

In terms of preventing Ponzi schemes, we must first strengthen the internal risk management of Internet financial enterprises. For the P2P platform represented by Ezubo, it was necessary to find the correct market positioning, strengthen the intermediary nature of the platform, base it on long-term development, and better provide financing services for small and medium-sized enterprises and individuals [8]. In addition, the platform should also improve the information disclosure mechanism, enhance the transparency of the platform, and provide necessary relevant risk warnings to platform investors. In the process of platform operation, the professional quality of practitioners has a great impact on the development of the platform itself [6]. To improve the professional quality of platform personnel and help the risk management of the platform, the Internet financial platform can regularly organize relevant business knowledge lectures, classic case analysis research and other training work, so as to improve the risk identification ability, risk prevention and risk response ability of all employees.

4.3. Strengthen Investors' Interests

4.3.1. Improve investors' protection policies

The relevant departments should establish and improve relevant policies to protect investors. It is possible to set up an appropriate proportion of risk reserves and deposit the reserves in bank financial institutions to ensure the real existence and integrity of the reserves so that in the event of an accident, this part of the funds can be used to maximize the loss of investors [5]. We can also learn from the existing preferential compensation system in the securities market. Based on the public nature of the investor protection fund and its status as an investor protection fund, the investor protection fund company should provide financial compensation to investors, which helps to activate the function and utility of the investor protection fund [9]. At the same time, the establishment of compensation measures to achieve the sustainability of the first wage system, boost investor confidence, reduce the impact on other enterprises, and promote the development of the financial industry.

4.3.2. Strengthen investor education

Ezubo took advantage of investors' lack of investment knowledge and expectation of high returns and used higher investment returns than the market as a trap to entice the public to invest, resulting in many investors being deceived. It is important for investors to learn investment knowledge. It is not limited to methods. Learn investment-related information by self-learning financial knowledge, participating in related work to accumulate financial knowledge, learning financial knowledge from relatives and friends, receiving investor education, etc. The research showed that the mediating effects of investor education on improving the probability of investment return, total investment return probability, and average annual return probability are 19.41%, 17.09%, and 12.75% [10]. It also demonstrated the importance of strengthening investor education.

5. Conclusion

This paper took Ezubo Company as the case, analyzed the causes of its Ponzi scheme, and put forward countermeasures and suggestions. Ezubo constructed a Ponzi scheme and conducted investment fraud by using policy gaps and human greed. This paper made the public once again realize the harm of the Ponzi scheme and gave relevant suggestions. This paper not only has theoretical significance for modern society but also has practical significance for protecting people from investment fraud and risk management of P2P platforms. With the development of the economy and the improvement of people's living standards, more and more people choose to get more money through investment. Meanwhile, the situation becomes more serious when there are many greedy people and frauds. This paper began a new focus on the study of a specific case, but it is not enough. Because the company information disclosure is less and the information source is relatively single, the content analysis is not comprehensive enough. In future studies, we hope to obtain more comprehensive data, interview real victims, and make more targeted recommendations.

Authors Contribution

All the authors contributed equally and their names were listed in alphabetical order.

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