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ARTICLE

ANALYSIS OF ZEDA YISHENG'S FINANCIAL FRAUD CASE AND RESEARCH ON AUDIT COUNTERMEASURES

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ABSTRACT

With the gradual improvement of China's capital market supervision and management system, financial fraud cases represented by Zeda Yisheng, a company listed on the Science Technology Innovation Board, have received extensive attention in the capital market. This paper takes the financial fraud case of Zeda Yisheng as the research object, explores the causes of audit failure by deeply analyzing the specific means of its financial fraud, and puts forward targeted audit countermeasures and suggestions to prevent financial fraud. Zeda Yisheng mainly carried out financial fraud through means such as fabricating business transactions and falsifying financial data, resulting in serious distortion of its financial data. Regarding the causes of audit failure, it is mainly manifested in insufficient assessment of enterprise audit risks, ineffective internal control testing, as well as deficiencies in the professional capabilities and professional ethics of relevant auditors. As for how to better prevent financial fraud in the future, this paper puts forward suggestions and countermeasures, including improving relevant laws, regulations and supervision systems, optimizing the audit process, improving the internal audit and risk control systems of enterprises, and enhancing the professional quality and independent and objective awareness of auditors.

KEYWORDS

Financial Fraud, Audit Countermeasures, Case Study

1. INTRODUCTION

In recent years, with the rapid growth of China's capital market, financial fraud incidents represented by Zeda Yisheng have emerged. These incidents have seriously damaged the interests of investors, undermined the fair competition environment of the market, and reduced the resource allocation efficiency of the securities market. The existence of these events has led to deviations in market signals and errors in resource allocation, preventing resources from flowing to the enterprises and projects that truly need them and affecting the healthy and orderly development of the economy. Therefore, in depth study of the Zeda Yisheng financial fraud case, revealing the motivation and mechanism behind it, is of great practical significance for improving the regulatory system of the capital market, enhancing audit quality, and protecting the interests of investors. The main objective of this paper is to explore the specific means of financial fraud, the reasons for the failure of internal control of Zeda Yisheng through in depth analysis of its financial fraud case, and put forward corresponding audit countermeasures and suggestions. It is hoped that through the study of this case, it can provide useful reference for audit practice, promote the development of audit theory, and contribute to the healthy development of the capital market.

2. OVERVIEW OF THE FINANCIAL FRAUD CASE OF ZEDA YISHENG

2.1 Company Overview

Zeda Yisheng (Tianjin) Technology Co., Ltd., a high tech enterprise founded on January 15, 2013, focuses its core business on the field of pharmaceutical informatization services. The company's business scope mainly includes customized pharmaceutical software, system integration, and information technology services, and it creates comprehensive digital solutions for the pharmaceutical industry. Zeda Yisheng successfully listed on the Science and Technology Innovation Board in June 2020. Subsequently, by virtue of its advantages in technological innovation and continuous expansion of its business scope, it has become a competitive enterprise in the field of medical informatization. However, shortly after its listing, it attracted high attention from regulatory authorities and the capital market due to serious financial fraud.

2.2 The Process of Uncovering the Fraud Incident

The exposure process of the financial fraud incident of Zeda Yisheng Co., Ltd. is a dramatic and highly cautionary experience. In June 2020, Zeda Yisheng was listed on the Science and Technology Innovation Board. Relying on its unique business model in the field of pharmaceutical informatization and rapid development momentum, it was regarded as a leader in the industry by the outside world. However, shortly after the listing, the market began to have doubts about the authenticity of its financial data. The relevant financial data announced by Zeda Yisheng in 2021 showed significant abnormal fluctuations, attracting a lot of attention from the capital market. The China Securities Regulatory

Commission (CSRC) initiated an investigation into Zeda Yisheng on April 21, 2022, which marked the official intervention of the regulatory authorities. On April 22, 2023, the CSRC officially announced the "Administrative Penalty Decision" and the "Market Ban Decision" on Zeda Yisheng Co., Ltd., and severely punished the relevant personnel involved in the case. On June 8, 2023, the forced delisting procedure of Zeda Yisheng was initiated, and it was finally officially delisted on July 7, 2023. This series of events not only reflects the seriousness of Zeda Yisheng's financial fraud but also demonstrates the regulatory authorities' uncompromising attitude towards illegal and irregular behaviors in the capital market.

3. ANALYSIS OF FINANCIAL FRAUD MEANS

3.1 Means of Fabricating Business Transactions

In the financial fraud case of Zeda Yisheng Co., Ltd., fabricating business transactions was one of its main methods. The specific ways of fabricating

transactions mainly included fabricating sales contracts and customers, etc., to inflate operating revenue and profits, thus exaggerating its business results. During the period from 2016 to 2019, Zeda Yisheng Co., Ltd. signed false contracts with its wholly owned subsidiaries to inflate its sales business. The cumulative inflated operating revenue reached 342 million yuan. These illegal acts of fabricating business transactions not only seriously violated the integrity principles of the capital market but also severely damaged the legitimate rights and interests of investors and other stakeholders. During the process of fabricating business transactions, Zeda Yisheng, through careful planning and organization, constructed a complete but false business flow and capital flow information, making it difficult for the regular audit process to detect its financial fraud. For example, Zeda Yisheng Co., Ltd. inflated its operating revenue by fabricating customers and transactions. At the same time, relying on the fabricated business flow and capital flow information, it concealed its true financial situation, making the company's financial statements seriously inconsistent with the facts (see Table 1).

Table 1: Statement of Inflated Revenue and Profit of Zeda Yisheng from 2016 - 2021

Year	2016	2017	2018	2019	2020	2021
Inflated operating revenue (in thousands of yuan)	35573.7	73888.8	118039	114794.8	152168.6	71043.5
Inflated profit (in thousands of yuan)	22438.2	37407.6	61608.5	65281	82469.2	26657.8

3.2 Means of Manipulating Financial Data

As one of the main fraud means of Zeda Yisheng, manipulating financial data is achieved mainly through methods such as profit rigging, inflating assets, and concealing liabilities to reach its illegal goals. In order to cover up its true financial situation, Zeda Yisheng manipulated profits by inflating revenues and profits. From 2016 to 2019, the cumulative inflated operating profit reached 187 million yuan. In 2016 alone, the inflated profit accounted for as high as 104.72% of the profit of that year. At the same time, Zeda Yisheng inflated assets by fabricating construction in progress projects. For example, in 2021, Zeda Yisheng prepaid a total of 42.6906 million yuan for equipment to Zhejiang Guantao Intelligent Technology Company. However, 36.3206 million yuan of the equipment payment had no actual cost incurred in the corresponding construction in progress project. In addition, Zeda Yisheng falsified financial data by concealing liabilities and expenses [1]. For instance, in order to cover up its true intention of off balance sheet fund circulation, the company concealed a large number of external guarantees. This not only seriously underestimated the company's liability situation but also increased the risks for investors.

3.3 Means of Fraud in Related Party Transactions

Fraud in related party transactions is another key means of fraud employed by Zeda Yisheng. Its methods are both covert and complex, seriously misleading investors and the market. It is mainly manifested in the non-disclosure or false disclosure of related party relationships, followed by the transfer of funds and the fabrication of profits through related party transactions, thus creating an off balance sheet fund circulation. Zeda Yisheng conducted seriously unfair transactions through undisclosed related parties. For example, the company sold goods to undisclosed related parties at prices much higher than those for other customers, thereby inflating revenues and profits [2]. Zeda Yisheng also enabled its own funds or funds of related parties to circulate off balance sheet through disclosed or undisclosed related parties and specific third parties, so as to fabricate transactions, inflate revenues and profits. In addition, the fraud in Zeda Yisheng's related party transactions is also reflected in commercial terms such as transaction prices, delivery methods, payment terms, and settlement methods. These terms are significantly different from those of other customers or suppliers. For instance, while Zeda Yisheng uses bill settlement methods for other suppliers, it uses cash transactions for a newly added supplier, or uses the method of offsetting multi-party creditor's rights and debts for settlement, further concealing the true nature of related party transactions.

4. EXPLORATION OF THE CAUSES OF AUDIT FAILURE

4.1 Inadequate Audit Risk Assessment

Audit risk assessment holds a crucial position in the audit process. Its purpose is to identify and evaluate the potential risks of material misstatements in the financial statements. When auditing Zeda Yisheng Co., Ltd., accountants lacked an assessment of the financial fraud risk points. For instance, Zeda Yisheng Co., Ltd. had long standing issues such as signing asset management contracts exceeding the authorization limit of the general meeting of shareholders. This reflected a relatively serious financial fraud risk in the company's internal fund management and use [3]. However, during the audit process, auditors did not assess these financial fraud risk points or take further review measures, causing a large number of financial fraud behaviors of Zeda Yisheng Co., Ltd. to be overlooked. In addition, auditors also failed to assess the particularity of the industry to which the enterprise belongs. As a company listed on the Science and Technology Innovation Board, Zeda Yisheng Co., Ltd. operates in a highly competitive industry. To meet the listing requirements and the expectations of capital market investors, it has a strong motivation for financial fraud. Nevertheless, during the audit of Zeda Yisheng Co., Ltd., accountants did not fully consider the situation of the enterprise and its industry, ultimately resulting in audit failure.

4.2 Malfunction of Internal Control Testing

The failure of internal control testing is one of the main reasons for the audit failure of Zeda Yisheng Co., Ltd. During the internal control testing of Zeda Yisheng Co., Ltd., auditors had the problem of lacking tests on key control nodes. When conducting internal control tests on key areas such as the company's operating income and monetary funds, they failed to effectively test key control links [4]. For example, Zeda Yisheng had long term fraud in the signing and approval of sales contracts, as well as the issuance and confirmation of relevant invoices. However, due to the lack of a complete internal testing system, relevant auditors failed to detect situations such as false transactions. At the same time, during the internal control testing of Zeda Yisheng Co., Ltd., relevant auditors found abnormal financial data in the enterprise. For example, the tested sample materials were inconsistent and contradictory to the content of financial accounting vouchers. However, auditors did not conduct in depth analysis, comparison, or adopt audit procedures for these abnormal situations, resulting in the inability of the internal control testing to evaluate the effectiveness of the system.

4.3 Deficiencies in the Collection and Analysis of Audit Evidence

The collection and analysis of audit evidence, as the core part of audit work, directly influence the accuracy and reliability of audit conclusions. During the collection of audit evidence, auditors lack the initiative to

expand the collection of external relevant evidence and overly rely on the materials provided by the enterprise [5]. When examining the related party transactions of Zeda Yisheng Co., Ltd., relevant auditors did not fully collect evidence and materials such as bank statements and third party contracts, resulting in limitations in the scope of evidence collection regarding the company's related party transaction fraud. In addition, when reviewing the financial data of Zeda Yisheng Co., Ltd., relevant auditors did not conduct in depth analysis of abnormal data. They failed to study the cross checking relationships and trend changes among the data, thus failing to detect the existence of false businesses and related party transactions. Moreover, during the audit work, accountants did not fully utilize data analysis tools for in depth exploration to identify data abnormalities and fraud risks within the company.

4.4 Lack of Professional Competence and Professional Ethics among Auditors

The professional competence and professional ethics of auditors are key elements in ensuring audit quality. During the audit of Zeda Yisheng Co., Ltd., relevant auditors had the problem of insufficient professional competence [6]. They lacked the ability to identify complex audit tasks and fraud methods. Faced with the continuous false business operations and financial data fraud of Zeda Yisheng Co., Ltd., accountants failed to use effective audit methods and technical means for identification and response, which reflects the insufficient professional competence of relevant auditors [7]. In addition, some auditors may have engaged in unethical behavior such as colluding with the audited entity. This led to a failure to maintain the necessary independence and objectivity during the audit process, ultimately resulting in the audit failure of Zeda Yisheng Co., Ltd. In this case, the accounting firm involved was punished by the regulatory authorities for alleged failure to exercise due diligence during the practice. This reflects that the relevant auditors involved had professional ethics issues and failed to fulfill their due professional responsibilities.

5. AUDIT COUNTERMEASURES AND SUGGESTIONS FOR PREVENTING FINANCIAL FRAUD

5.1 Improve Laws, Regulations and the Regulatory System

The case of Zeda Yisheng reflects the deficiencies in the current laws, regulations and regulatory systems for preventing financial fraud. The government can gradually increase the penalties for financial fraud. At present, the penalties for financial fraud in China's laws and regulations are relatively lenient and it is difficult to form an effective deterrence. The amount of fines for financial fraud can be increased, and the pursuit of criminal liability of relevant responsible persons can be strengthened, making them pay a heavy price and thus enhancing the deterrence of the law. For example, relevant provisions of the US Sarbanes-Oxley Act can be referred to, implementing severe criminal and civil penalties for financial fraud. The government can also continuously optimize the regulatory approach and strengthen the collaborative cooperation among regulatory departments. At present, there are problems such as multiple-head regulation and non-sharing of information in China's capital market regulatory system. In response, a unified regulatory platform can be prepared and established to strengthen the information sharing and collaborative cooperation between departments such as the China Securities Regulatory Commission and the Tax Bureau, forming a regulatory synergy and improving regulatory efficiency. At the same time, relevant government departments can make full use of big data and artificial intelligence technologies to strengthen the real time monitoring of listed companies' financial data, promptly detect abnormal situations, and continuously improve the accuracy and effectiveness of supervision.

5.2 Continuously Optimize the Audit Process and Strengthen Implementation

The Zeda Yisheng case has revealed the deficiencies in the existing audit process. Therefore, the continuous improvement and effective implementation of the audit process are important means to ensure audit quality and prevent financial fraud. Before conducting work on the audited entity, accountants should clarify the audit scope to ensure the rational allocation of audit resources. At the same time, they should optimize audit methods and procedures according to the main business content of the audited entity and the potential financial fraud risks [8].

For high tech enterprises like Zeda Yisheng, when formulating the audit plan, auditors should focus on areas with a high risk of financial fraud, such as research and development expenses, intangible assets, and related party transactions. Auditors can also make full use of technical tools to assist in the work. For example, they can use technologies such as big data and artificial intelligence to analyze and compare financial data, promptly identify abnormal data, and provide a high quality data foundation for subsequent audit analysis. In addition, during the audit process, auditors should improve the audit log, completely record the financial problems and data information discovered during the audit, provide sufficient evidence support for the audit work, and also facilitate subsequent review and traceability.

5.3 Improve the Enterprise's Internal Audit System and Risk Management Mechanism

The financial fraud case of Zeda Yisheng fully reflects the serious negative impact of the lack of an enterprise's internal audit system and risk management mechanism on its healthy development. On the one hand, enterprises can establish and improve relevant internal audit institutions and systems. As an important part of internal supervision, the internal audit department should regularly inspect and evaluate the enterprise's financial situation, internal control, and risk management to promptly identify potential financial fraud problems and risks. For example, the internal audit management system of Newmorning Technology Co., Ltd. clearly and in detail stipulates the powers and responsibilities of the internal audit department, including functions such as guiding and supervising the establishment and implementation of the internal audit system, reviewing the company's annual internal audit work plan, and urging the implementation of the internal audit plan. On the other hand, enterprises can also strengthen risk management by improving the risk management mechanism. For instance, enterprises can establish a risk assessment model to conduct quantitative analysis of various risks, formulate corresponding risk response strategies, and regularly re-evaluate and optimize the risk management mechanism to ensure its effectiveness and adaptability.

5.4 Continuously Enhance Auditors' Professional Competence and Awareness of Independence and Objectivity

Accounting firms can establish a comprehensive internal training plan. When international and domestic accounting standards are revised, they should promptly organize relevant audit personnel, especially frontline auditors, for training. By combining practical cases, the understanding of relevant standards and regulations among auditors can be deepened, thus improving their professional competence. In addition, the firm can establish a mentoring mechanism. For newly recruited accountants, an experienced mentor, who can be a partner or a senior manager, is assigned. When the newly recruited accountants encounter problems during the audit tasks, the mentors can provide guidance on audit related issues and share their experiences, ensuring that the new comers develop a professional and rigorous work attitude in their career development. At the same time, the firm should establish a sound supervision and review mechanism. Before the start of an audit project, conduct an interest review of the accountants involved in the audit work to ensure that there are no economic and interest related relationships between the accountants and the audited entity [9]. Moreover, accountants who adhere to the principles of independence and objectivity should be commended to encourage more accountants to develop an awareness of independence and objectivity.

6. CONCLUSION

The financial fraud case of Zeda Yisheng, a typical case among the first batch of compulsory delistings on the Science Technology Innovation Board, holds high research value. This case profoundly reveals the serious financial fraud problems existing in listed companies at the levels of financial management and internal control, serving as an important warning to all participants in the capital market. In terms of financial fraud means, Zeda Yisheng mainly resorted to illegal means such as fabricating business transactions, manipulating financial data, and committing fraud in related party transactions, which greatly distorted the company's financial situation and operating results. These fraud means not only misled market investors but also undermined the fairness and transparency of the capital market. Regarding the reasons for audit failure, the main issues include the auditors' failure to effectively

identify and assess fraud risks, the ineffectiveness of internal control testing, the incomplete collection and analysis of audit evidence, and the lack of professional competence and professional ethics among auditors. The existence of these problems has undermined the authenticity and reliability of the company's financial statements. In response to these problems, this paper proposes that, at the macro level, relevant laws, regulations, and the regulatory system should be improved, regulatory methods should be optimized, and penalties for financial fraud should be increased. For enterprises themselves, they need to continuously improve the audit process, strengthen and improve the internal audit system and risk management mechanism, and constantly enhance the professional quality and awareness of independence and objectivity of auditors. Through the study of the Zeda Yisheng financial fraud case, not only are the means and causes of financial fraud clearly revealed, but also practical countermeasures and suggestions are provided to prevent the recurrence of similar incidents. It is hoped that these research results can offer promotional suggestions for enhancing the financial transparency of listed companies, effectively protecting the interests of investors, and strongly safeguarding the healthy development of the capital market.

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