SPP Guiding Case No. 222: Case of Zhao Moumou et al. for Manipulating the Securities Market

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Decided at the 36th meeting of the 14th Procuratorial Committee of the Supreme People's Procuratorate on September 13, 2024; issued on January 3, 2025.

Keywords

Securities market manipulation / private funds / over-the-counter options / illegal gains

Holding

When handling cases of manipulating the securities market using private funds, the People's Procuratorate shall conduct a whole-chain review of the flow process of the private funds, including their source, use, and destination, and especially whether the acts violate the relevant provisions on fund supervision and administration, so as to accurately determine the criminal facts of each link. The different criminal means of transaction-type manipulation and information-type manipulation shall be distinguished, and the judicial interpretation shall be correctly applied to determine "serious circumstances" and "especially serious circumstances." The act of buying and selling over-the-counter options in coordination with stock manipulation does not constitute the crime of manipulating the futures market, but the gains therefrom are cross-market illegal gains of the crime of manipulating the securities market and shall be recovered in accordance with the law.

Basic Facts

The defendant Zhao Moumou was the former deputy general manager of the asset management department of Company A Futures Co., Ltd. The defendant Zhao Moujia was an employee of the asset management department of Company A Futures Co., Ltd. The defendants Zhu Mou and Jin Moumou were both persons employed by Zhao Moumou.

From May 2016 to August 2018, Company A Futures Co., Ltd. ("Company A") issued five tranches of FOF series funds (i.e., funds that invest in private funds) with fund products as the investment target, raising a total of RMB 1.086 billion, which was invested in the subscription of nine private funds totaling RMB 936 million. During this period, Zhao Moumou took advantage of his position in managing and operating the FOF fund products to require the private fund companies to provide "channel services" in violation of regulations and to cede the management and risk-control authority of the fund products, thereby obtaining the authority to manage, invest, and use the funds.

From the end of 2017 to August 2018, Zhao Moumou directed Zhao Moujia and Zhu Mou to contact clients and cyclically divert the funds raised by the FOF funds to provide off-market capital allocation for others' stock trading, totaling more than RMB 1.8 billion, and used personal bank cards under his control to collect capital allocation margins and interest.

From August to December 2018, Zhao Moumou, Zhu Mou, and Jin Moumou conspired with Ruan Mou (handled in a separate case), a shareholder of Yi Group Co., Ltd. ("Company Yi"), to jointly manipulate the shares of Company Yi in the name of "market value management." Zhao Moumou directed the trading team managed by Zhu Mou and Jin Moumou to use the funds in the nine private fund accounts in which Company A's FOF funds had invested to buy shares of Company Yi and drive up the share price. At the same time, Zhao Moumou deposited the off-market capital allocation margins and interest he had personally collected into personal securities accounts under his control to buy shares of Company Yi simultaneously. After the

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share price was driven up, Zhao Moumou sold the shares in his personal accounts, while the private fund accounts bought shares at high prices to take over. By the time the case arose, Zhao Moumou's personal accounts under his control had bought more than RMB 480 million of Company Yi shares and sold more than RMB 600 million, with gains of more than RMB 125 million; the nine private fund accounts in which Company A's FOF funds had invested had bought more than RMB 1.27 billion of Company Yi shares and sold more than RMB 37 million. After the case arose, the above private funds were liquidated successively from December 19, 2018 to August 14, 2019, and Company A's FOF funds suffered total losses of more than RMB 500 million.

In addition, during the period of manipulating the share price of Company Yi, Zhao Moumou and others used RMB 132 million of capital allocation margins and interest collected by individuals to purchase over-the-counter call options on Company Yi shares from multiple companies such as Shanghai Bing Financial Services Co., Ltd. After the manipulation of the securities market drove up the share price, Zhao Moumou exercised the options and obtained gains totaling more than RMB 125 million.

As determined by the China Securities Regulatory Commission, from July 18 to December 3, 2018, the circulating shares of Company Yi held in aggregate by the private fund accounts and personal securities accounts controlled by Zhao Moumou and others reached more than 30% of the total actually circulating shares of the stock. Among them, from November 6 to December 3, 2018, the cumulative trading volume for 20 consecutive trading days reached more than 50% of the total trading volume of the securities during the same period.

Zhao Moumou and others also committed the crime of accepting bribes as non-state functionaries and the crime of offering bribes to non-state functionaries.

Procuratorate Performance of Duties

(1) Review for prosecution. On September 27, 2019, the Shandong Provincial Public Security Department transferred Zhao Moumou, Zhao Moujia, Zhu Mou, Jin Moumou, and others to the Shandong Provincial People's Procuratorate for prosecution on suspicion of the crimes of manipulating the securities market and diverting funds and other crimes, and the Shandong Provincial People's Procuratorate designated the Qingdao Municipal People's Procuratorate to exercise jurisdiction over the case.

Zhao Moumou defended that Company A was aware of his management of the private funds' investment in Company Yi shares, that the use of funds conformed to the provisions on private fund investment, and that the acts did not constitute the crime of manipulating the securities market. The procuratorial organ returned the case to the public security organ for supplementary investigation and put forward specific opinions: first, to supplement the retrieval of the investment agreements signed between the managers of the nine private funds and Company A, the trading authority and trading records of the private funds actually controlled by Zhao Moumou, witness testimony, and other evidence, to prove whether Zhao Moumou, in violation of regulatory provisions and entrusted investment agreements, controlled the private fund funds and investment trading; second, to supplement the retrieval of Company A's business decision records, fund use arrangement plans, and relevant witness testimony, to prove whether Company A was aware that the private funds were actually controlled by Zhao Moumou; third, to ascertain the amounts of capital allocation margins and interest collected by Zhao Moumou, whether all of the above funds were used to purchase Company Yi shares and over-the-counter options, and whether the final gains flowed into Zhao Moumou's personal accounts, to prove whether Zhao Moumou used the FOF fund capital allocation to obtain start-up funds for manipulating the securities market, trading over-the-counter options, and illegally profiting; and fourth, to ascertain the corresponding relationship between the private funds' purchase of Company Yi shares and the sale of Company Yi shares by Zhao Moumou's personal accounts, to prove whether Zhao Moumou used the private funds to take over at high prices.

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The public security organ comprehensively collected and transferred the relevant evidence in accordance with the requirements of the supplementary investigation outline. After review, the Qingdao Municipal People's Procuratorate held that the evidence on file was sufficient to prove the criminal facts that Zhao Moumou and others, in violation of the provisions on FOF fund and private fund administration, diverted fund funds for capital allocation as personal start-up funds for manipulating the securities market, controlled the private funds in violation of regulations to drive up share prices, had the funds take over at high prices while individuals obtained huge illegal benefits, and purchased over-the-counter call options in advance to multiply the manipulation gains.

On May 11, 2020, the Qingdao Municipal People's Procuratorate initiated public prosecution before the Qingdao Intermediate People's Court against Zhao Moumou, Zhu Mou, Zhao Moujia, and Jin Moumou for the crimes of manipulating the securities market and diverting funds and other crimes.

(2) Charging and proving the crime. In November 2020, January 2021, and May 2021, the Qingdao Intermediate People's Court held public hearings in this case. During the trial, the defense counsel raised the opinions that the gains from over-the-counter options did not constitute illegal gains and should not be determined as "especially serious circumstances," and the public prosecutor conducted targeted responses.

First, regarding the over-the-counter options. The defense counsel argued that investing in over-the-counter options was a component of the FOF fund design, and that Zhao Moumou's option exercise gains were not illegal gains and should not be recovered. The public prosecutor pointed out that the funds used to purchase the over-the-counter options were the margins and interest obtained by Zhao Moumou from diverting FOF funds for off-market capital allocation; that he profited from the corresponding over-the-counter option transactions through manipulation of the securities market; that the option exercise gains were transferred into personal securities accounts controlled by Zhao Moumou and continued to be used to manipulate Company Yi shares; and that they never entered the FOF fund or private fund accounts, so they were Zhao Moumou's personal illegal gains and should be recovered in accordance with the law.

Second, regarding whether "especially serious circumstances" should be determined. The defense counsel argued that the securities market manipulation in this case occurred in 2018, so under the principle of applying the old law if it is more lenient, the 2010 Provisions of the Supreme People's Procuratorate and the Ministry of Public Security on the Standards for Filing and Prosecution of Criminal Cases under the Jurisdiction of Public Security Organs (II) ("2010 Filing and Prosecution Standards") should apply and the act should be determined as "serious circumstances"; and that the 2019 Interpretation of the Supreme People's Court and the Supreme People's Procuratorate on Several Issues Concerning the Application of Law in Handling Criminal Cases of Manipulating the Securities and Futures Markets ("2019 Judicial Interpretation") could not apply, so the act should not be determined as "especially serious circumstances."

The public prosecutor responded: first, the 2019 Judicial Interpretation lowered the filing standards for trading indicators for this crime compared with the 2010 Filing and Prosecution Standards, so under the principle of applying the old law if it is more lenient, this case still applied the 2010 Filing and Prosecution Standards to determine that the acts constituted a crime. Second, when the criminal acts were committed in 2018, there was no judicial interpretation prescribing the standard for "especially serious circumstances"; in accordance with the Provisions of the Supreme People's Court and the Supreme People's Procuratorate on Issues Concerning the Temporal Effect of the Application of Criminal Judicial Interpretations, where there was no relevant judicial interpretation at the time of the acts but a judicial interpretation prescribing "especially serious circumstances" already exists at the time of handling, the case shall be handled in accordance with the 2019 Judicial Interpretation. Therefore, Zhao Moumou and others' acts of manipulating the securities market should be determined as "especially serious circumstances."

(3) Outcome. On May 25, 2021, the Qingdao Intermediate People's Court rendered a first-instance judgment, determining that Zhao Moumou had committed the crime of manipulating the securities market and sentencing him to six years of fixed-term imprisonment, which, combined with the crime of diverting

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funds and other crimes under combined punishment for multiple crimes, resulted in a decided term of seventeen years of fixed-term imprisonment and a fine of RMB 60.4 million, and ordering the recovery of more than RMB 250 million in gains from market manipulation and over-the-counter option trading. The court determined that Zhu Mou had committed the crime of diverting funds and the crime of manipulating the securities market, that Zhao Moujia had committed the crime of diverting funds, and that Jin Moumou had committed the crime of manipulating the securities market, sentencing them respectively to fixed-term imprisonment ranging from eight years to three years, with fines imposed. Zhao Moumou, Zhu Mou, Zhao Moujia, and Jin Moumou appealed. On December 20, 2021, the Shandong Higher People's Court rendered a second-instance ruling, dismissing the appeals and affirming the original judgment.

Guiding Significance

(1) Ascertain through a whole chain the flow of private fund funds used in crimes, and severely punish in accordance with the law the criminal acts in each link of manipulating the securities market using private funds. Manipulating the securities market using private funds infringes both the interests of securities market investors and the interests of private fund investors, causing serious cross-field harmful consequences. In handling such cases, the flow process of the private fund funds shall be reviewed, the source, use, and destination of funds shall be tracked through a whole chain, and the focus shall be on reviewing whether there exist violations of the Securities Investment Fund Law and the Regulations on the Supervision and Administration of Private Investment Funds, such as "private fund managers shall not entrust investment management duties to others" and "shall not use private fund property or position convenience to seek benefits for persons other than investors," so as to accurately determine the criminal facts and criminal means of the actor's controlling private funds in violation of regulations, illegally using fund funds, and using the advantage of funds to manipulate securities trading prices and trading volumes at each link. Where fund funds are diverted to commit the crime of manipulating the securities market, and the acts separately constitute the crime of diverting funds and the crime of manipulating the securities market, combined punishment for multiple crimes shall be applied in accordance with the law.

(2) Accurately determine the "serious circumstances" and "especially serious circumstances" of the crime of manipulating the securities market. The crime of manipulating the securities market can be divided into transaction-type manipulation and information-type manipulation. Transaction-type manipulation mainly uses trading indicators such as shareholding ratio and trading volume ratio to determine whether the standards for criminalization and escalated statutory punishment are met. Compared with the 2010 Filing and Prosecution Standards, the 2019 Judicial Interpretation lowered the criminalization standards for trading indicators. For transaction-type manipulation committed before July 1, 2019, the 2010 Filing and Prosecution Standards shall apply to determine whether a crime is constituted; for the determination of "especially serious circumstances," because there was no judicial interpretation prescribing the standard at the time of the acts, the 2019 Judicial Interpretation shall apply. In cases of transaction-type manipulation before the implementation of the 2019 Judicial Interpretation where the trading indicators did not meet the 2010 Filing and Prosecution Standards, the 2019 Judicial Interpretation shall not be directly applied to criminalize or even escalate the statutory punishment.

(3) The act of buying and selling over-the-counter options in coordination with stock manipulation cannot be determined as the crime of manipulating the futures market, but the gains therefrom are cross-market illegal gains of the crime of manipulating the securities market and shall be recovered in accordance with the law. Buying over-the-counter call options before manipulating the securities market and continuously driving up the share price, and then profiting from the increase, is a typical cross-market manipulation act. Under Article 3 of the Futures and Derivatives Law of the People's Republic of China, exchange-traded options are futures, while over-the-counter options are derivatives, not futures. Therefore, the act of buying and selling over-the-counter options does not constitute the crime of manipulating the futures market, and the transaction amount of buying and selling over-the-counter options shall not be included in the crime amount.

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However, the gains from such option trading are cross-market gains from manipulating the securities market and driving up the share price, and shall be determined as illegal gains of the crime of manipulating the securities market and recovered in accordance with the law.

Relevant Legal Provisions

Article 182(1) of the Criminal Law of the People's Republic of China (2006 Amendment) (currently Article 182(1) of the Criminal Law of the People's Republic of China applies).

Article 272(1) of the Criminal Law of the People's Republic of China (1997 Revision) (currently Article 272(1) of the Criminal Law of the People's Republic of China applies).

Item (1) of Article 4 of the Interpretation of the Supreme People's Court and the Supreme People's Procuratorate on Several Issues Concerning the Application of Law in Handling Criminal Cases of Manipulating the Securities and Futures Markets (Fa Shi [2019] No. 9).

Item (1) of Article 39 of the Provisions of the Supreme People's Procuratorate and the Ministry of Public Security on the Standards for Filing and Prosecution of Criminal Cases under the Jurisdiction of Public Security Organs (II) (Gong Tong Zi [2010] No. 23) (currently item (1) of Article 34 of the Provisions of the Supreme People's Procuratorate and the Ministry of Public Security on the Standards for Filing and Prosecution of Criminal Cases under the Jurisdiction of Public Security Organs (II) (Gong Tong Zi [2022] No. 12) applies).

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