

# Optimization of the Judicial Regulation Path for the Crime of Trading in Undisclosed Information

Youchen Geng

*Criminal Justice College, East China University of Political Science and Law, Shanghai, 201600, China*

*\*Corresponding author. Email: gengyouchen@foxmail.com*

## ABSTRACT

In the era of preventing and resolving major financial risks, how to prevent illegal securities activities has become an important task of current financial work and political-legal work. From the analysis of the Huarong case, the Baoshang Bank case, the HNA case and the Evergrande case, it can be fully concluded that the accumulation of violations in the securities market and the lack of supervision have become an important incentive for China's systemic financial risks. At present, in the process of investigating and handling the crime of trading in undisclosed information, there are problems such as unclear determination of the constituent elements of "use", lack of supervision of the "administrative-judicial" transfer mechanism, and vague standards of crime and non-crime. The above problems directly cause the crime of trading in undisclosed information has grown significantly in recent years. Governing and preventing the crime of trading in undisclosed information is a systematic social governance activity. It should give full play to the advantages and efficiency of collaborative governance, optimize and improve it by scientifically defining the use behavior, improving the transfer judicial supervision mechanism, and clarifying the criminalization standards.

**Key words:** *The crime of trading in undisclosed information, Crime of insider trading, Judicial transfer, Undisclosed information, Constituent elements*

## 1. INTRODUCTION

The Party Central Committee has repeatedly emphasized that the focus should be on preventing and defusing major risks in the financial sector. At present, under the new historical orientation of social development entering a new era of socialism with Chinese characteristics, it is necessary to prudently resolve local government debt risks, continue to promote structural deleveraging, and resolutely curb the growth of local government implicit debt. Under the timely disposal of the Party Central Committee and various departments across the country, a number of major financial risks have been resolved, various high-risk financial institutions have been dealt with in an orderly manner, shadow banking risks have continued to converge, "precise bomb disposal" has been effective, and Internet financial risks have been effectively prevented and controlled, a diversified bond default disposal mechanism has been gradually established, an overall supervision framework for systemically important financial institutions, financial holding companies, financial infrastructure have been initially established to achieve important phased results in the battle to prevent and defuse major financial risks,

and the overall financial market is running smoothly. At present, when systemic financial risks are generally curbed, the moral hazard of securities market practitioners, especially those who use unpublished information, has become an important incentive for systemic financial risks.[1] Therefore, how to study the regulation of the crime of trading in undisclosed information from different levels of legislation, law enforcement, and justice has become an important work content to prevent and resolve major financial risks. For any legal issues, we should return to the research dimension of legal studies to deal with and respond to them. Therefore, it is an urgent requirement of the times to study how to properly establish rules and regulations, tighten the cage of the system, and realize the effective judicial regulation of illegal and criminal acts by using undisclosed information to trade.

## **2. THE MAIN DILEMMA OF JUDICIAL REGULATION OF THE CRIME OF TRADING IN UNDISCLOSED INFORMATION**

### ***2.1. The identification of the constituent elements of "use" is not clear***

The dilemma of judicial regulation of the crime of trading in undisclosed information is mainly caused by the vagueness of some of the elements of the crime and the lack of clear identification standards. Among them, the most typical difficult problem is "how to correctly understand and identify the so-called 'use'", which is currently very controversial in judicial practice. For the most typical type of behavior of the crime of trading in undisclosed information, that is, the so-called "rat warehouse" transaction, whether it is a transaction using undisclosed information often adopts the so-called "top five and last two" determination standard, that is if the actor has the same-direction trading behavior with the nature of undisclosed information within a specific time interval, it constitutes a rat trade.[2] However, in current practice, how to identify "use", the disputes in practice mainly include the following two opinions: one is that the so-called the first five and the bottom two can only be understood as being applicable in the case of the same-direction transaction. The reason is that, even in this situation, although the transaction of the actor's personal stock is included in the range of the top five and the bottom two, the overall transaction behavior of the actor is completely opposite to that of the broader market. Two independent operations, the reverse trading behavior did not take advantage of the advantages brought by the fund trading market, so it should not be regarded as "using" unpublished information for trading.[3] Another view holds that whether it is a co-directional transaction or a reverse transaction, it should be regarded as a transaction that "uses" undisclosed information. The main reason is that after the actor uses undisclosed information to operate the market during a certain period of time, he re-operates his personal account to buy and sell in the opposite direction, based on the delayed impact on stock price fluctuations after buying stocks in the fund market, and the subsequent purchases still use the information of funds that he knew before to buy, therefore, the reverse transaction still belongs to the use of undisclosed information.[4] The above disputes have resulted in different standards for understanding the legal application of "use" in judicial practice.

### ***2.2. The "administrative-judicial" transfer mechanism lacks supervision***

At present, although the regulatory agencies centered on the China Securities Regulatory Commission have gradually strengthened the supervision and enforcement

of the crime of using undisclosed information, there is still a serious problem of "substitute administrative penalty for criminal punishment" for the above-mentioned crimes. This is manifested in the fact that the CSRC's administrative penalty decision clearly states that the cases that have met the conditions for criminal prosecution are extremely rare to be investigated for criminal responsibility by the judicial authorities. In other words, the number of administrative law enforcement cases and the number of criminal cases are "inverted" in an unbalanced proportion. The reasons mainly include the following two factors: First, the "sporting" securities supervision has a bright color.[5] The so-called "sporting" securities supervision usually means that decision makers break through existing procedural frameworks and systems, coordinate and allocate amount of social resources to conduct centralized and high-intensity governance in a short period of time, while ignoring the importance of establishing rules and regulations for governance work. Some scholars have found through research that after the "sporting" governance or rectification is over, the problems being governed tend to rebound to varying degrees.[6] Second, due to the lack of an institutionalized cooperation mechanism between the CSRC and the judicial department, and the lack of a system for the judicial organs to effectively transfer the illegal punishment cases investigated by the CSRC to supervision, whether the cases investigated and handled by the securities regulatory department violated the criminal law and satisfied the conditions for criminal filing is often impossible to supervise. Judicial authorities are usually unable to actively discover, review or supervise cases handled by securities regulatory authorities using undisclosed information to trade. Therefore, based on the above two reasons, in practice, the relevant acts of illegal trading using undisclosed information that are investigated and dealt with by the CSRC are often not effectively criminally regulated and managed, but are decriminalized within the securities supervision and management system.

### ***2.3. The criminalization criteria are relatively vague and difficult to grasp***

As a new type of economic crime, the crime of trading in undisclosed information is generally unfamiliar to the judicial organs, which makes its criminalization standard ambiguous and difficult to grasp. The reasons specifically include the following aspects: First, the amount issue. The reason why the criminalization criteria for the crime of trading in undisclosed information is ambiguous is that it is difficult to grasp the criteria for determining the amount of crime. Due to the basic characteristics of securities market crimes, the crime of trading in undisclosed information is often very hidden, and the perpetrator's trading behavior is difficult to be discovered by the public security organs and securities regulatory

agencies. Especially for most of the occasional criminal activities that use undisclosed information to trade, if the perpetrator only conducts a one-time co-directional or reverse transaction for a specific stock, his behavior trajectory can hardly be confirmed in the vast securities market; That is, it is impossible to confirm the illegal and criminal behavior and related amounts of the perpetrator through the usual transaction trajectory of the perpetrator. Second, the causality issue. It is difficult to confirm the causal relationship between the benefits obtained by the actor through the use of undisclosed information transactions and his behavior. In judicial practice, it is often difficult to distinguish between the legitimate gains obtained by the actor through normal investment behavior and the illegal gains, and the source and causal relationship of the gains cannot be verified either, which also increases to some extent. As a result, the public security organs and the people's procuratorate have different criteria for judging criminal convictions. In addition, there is the issue of the boundary between this sin and that sin. Since the crime of trading in undisclosed information and the crime of insider trading are "twin brothers", the two are very similar in terms of the elements of the crime, and the only difference is that the types of information media are different.[7] Therefore, in practice, some judicial organs often confuse the distinction. As a result, the basic principle of statutory crime and punishment cannot be implemented. Since the public security organs are familiar with the standards for the crime of insider trading, according to the situation of judicial cases in various places, there is a crime of using undisclosed information as an insider to varying degrees. The case of dealing with the crime of trading confuses the boundaries between one crime and another, which leads to confusion in judicial application.

### **3. THE PERFECT PATH OF JUDICIAL REGULATION FOR THE CRIME OF TRADING IN UNDISCLOSED INFORMATION**

#### ***3.1. Clarifying the criteria for identifying "use"***

According to the authoritative interpretation of the Legislative Affairs Commission of the Standing Committee of the National People's Congress, the so-called "use" should be understood as the conduct of the perpetrator in the issuance of securities, securities, futures transactions or other transactions that have a significant impact on securities and futures prices, except for insider information. other unpublished information, before it has been disclosed, buy or sell the securities, or engage in futures trading related to the inside information, or disclose the information, or express or imply that others are engaged in the above-mentioned trading activities. Therefore, it should be understood that the actors use undisclosed information to conduct the same

or reverse operations as belonging to the category of "use". In addition, it should be noted that the subjects of "use" include not only securities and futures exchanges and their staff, but also financial institutions such as state-owned and mixed-ownership commercial banks, investment bank brokerages, futures brokerage companies, fund sales companies, trust companies, and insurance companies. The staff of securities regulatory agencies and trading venues, industry associations, and registration and settlement departments should also be included.[8] Since the above-mentioned persons may be dismissed or learn of other undisclosed information except insider information in the course of performing their duties, in judicial practice, the issue of the above-mentioned use subject must also be clarified before the determination of "use" can be fully grasped.[9]

#### ***3.2. Building an effective "administrative-judicial" transfer supervision mechanism***

From the perspective of the Criminal Procedure Law, the basic idea is that the administrative organs should promptly transfer the clues of illegal and criminal crimes discovered in the process of handling cases to the judicial organs for investigation of criminal responsibility. The securities regulatory authority, as an important part of the administrative authority, shall conscientiously implement the basic principles of the Criminal Procedure Law in securities inspection and punishment, and promptly transfer criminal cases concerning the use of undisclosed information for trading. Specifically, the coordination mechanism of criminal prosecution and administrative supervision and inspection should be strengthened in the top-level design. The People's Procuratorate, as the legal supervision organ stipulated in the Constitution and the Organization Law of the People's Procuratorate, shall shoulder the responsibility of supervising the administrative act of the securities supervision and management department to transfer it to the judicial organ in accordance with the law. The Supreme People's Procuratorate has established the Supreme People's Procuratorate's procuratorial office in the China Securities Regulatory Commission in September 2021. This is the first time the Supreme People's Procuratorate has stationed a procuratorial office in an administrative organ. Therefore, the establishment of the above-mentioned institutions should be used as an opportunity to strengthen the implementation of the requirements of Opinions of the General Office of the CPC Central Committee and the General Office of the State Council on Strictly Cracking Down On Illegal Securities Activities in accordance with the Law, promote the construction of the rule of law in the capital market, and enable the Supreme People's Procuratorate, the China Securities Regulatory Commission and the Supreme People's Court, the Ministry of Law, the Ministry of Public Security, etc. maintain close coordination, accelerate the improvement of the judicial system and

mechanism for securities law enforcement, increase the investigation and punishment of major illegal cases, promote the improvement of securities market supervision in accordance with the law, and build an effective "administrative-judicial" transfer supervision mechanism on this basis.

### **3.3. Clarifying the criminalization standards for the crime**

As mentioned above, with regard to the criminalization standard of the crime of trading in undisclosed information, the core of which is how to correctly grasp the difference and connection between this crime and the crime of insider trading. Only by correctly defining the difference between the crime of trading with undisclosed information and the crime of insider trading, can the criteria for determining the crime of trading with undisclosed information be clarified from this perspective. The author believes that the essential difference between the two lies in the difference of information. From the perspective of the principle of adapting guilt to punishment and the principle of statutory law, the above-mentioned standard scope of so-called undisclosed information should be strictly limited to prevent judicial organs from arbitrarily classifying administrative violations in the general sense as criminal violations which cause improper interference and violation of citizens' personal rights and property rights. In addition, in response to the aforementioned standard issues, attention should also be paid to the addition and improvement of the Eleventh Criminal Law Amendment to the aforementioned issues, and the issue should be viewed from the perspective of development. The original legislative intent of the 11th Amendment to the Criminal Law is to severely punish illegal and criminal acts in the securities market, but at the same time, from another perspective, the pursuit of statutory crime and punishment is also the basis for the concept of justice in criminal law. Whether it is criminal law or civil law, governance by law is emphasized; only by consistently adhering to governance by law in the field of criminal law can we gradually promote the grand blueprint for the integration of criminal justice, and finally weave the legal network of the secret system and punish crimes in accordance with the law. At the same time, it maintains the trading order of the securities market, prevents and resolves major systemic financial risks, and realizes effective identification and regulation of criminal behaviors using undisclosed information to trade.

## **4. CONCLUSION**

At present, preventing and resolving major financial risks has become an inevitable requirement and an important topic of the times. By analyzing the cases of Huarong, Baoshang Bank, HNA and Evergrande, we can fully draw the conclusion that one of the important

incentives for my country's systemic financial risks is the accumulation of violations in the securities market and the lack of supervision. In the process of investigation and handling, there are problems such as unclear determination of the constituent elements of "use", lack of supervision of the "administrative-judicial" transfer mechanism, and vague standards of crime and non-crime, which directly lead to the use of undisclosed information to conduct transactions. The activity has grown significantly in recent years. The prevention of securities violations and the governance and prevention of the crime of trading in undisclosed information are a systematic social governance activity. The judiciary shall coordinate and cooperate to jointly optimize and improve the scientific definition of exploiting behavior, improve the transfer judicial supervision mechanism, and clarify the criminalization standards, so as to realize the grand blueprint for the modernization of the governance capacity and governance system in combating securities and financial crimes. However, this paper makes an academic discussion on the optimization of the judicial regulation path for the crime of trading in undisclosed information, and demonstrates from the theoretical point of view in the aspect of empirical analysis and research materials, and accordingly fills the research gaps at home and abroad, in order to give some guidance and inspiration to the corresponding judicial practice circles in practice.

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