
ANGEL OR DEMON?

THE ETHICS OF ONLINE PEER-TO-PEER LENDING FIRMS

天使还是魔鬼？
P2P贷款公司道德规范

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ABSTRACT

Online Peer-to-Peer (P2P) lending schemes began to flourish in China in 2015. This lending model, where lender and borrower could do transactions without involving banking institutions, was welcomed by many start-ups and entrepreneurs because it provided an effective solution for reaching borrowers directly. One of these borrower classes was college students. Campus loans, facilitated through P2P platforms, quickly became popular. However, after a series of university scandals, questions emerged as to the morality of the industry and the responsibility of the P2P platforms within it to guard against abuses inflicted upon college students and the borrower market as a whole.

Alipay, a part of Ant Financial Service Group (Ant Financial, n.d.), is one of the leading third-party online payment platforms in China. It was launched in 2004 and has become widely known for its integration of a variety of consumer-oriented features, including “payment, lifestyle service, civil services, social networking, wealth management, insurance and public welfare.” It also boasted “over 450 million registered users and 200 financial institution partners” as of June, 2016. (Ant Family, n.d.)

Since its inception Alipay has produced a number of software updates for its smartphone application. At the launch of Alipay 9.0, a financing platform titled, “I Owe You (IOU),” was introduced. It was well received among younger generations, especially those at university and working far away from their hometowns. To use IOU, the only requirement is that the lender and borrower are mutual “friends” – for example, on WeChat, or a related Chinese social media application. Once friendship status is established, the steps for acquiring a loan are as follows:

1. Choose the friend you would like to ask for a loan.
2. Choose the IOU function.
3. Fill in a form, including information on the amount to be borrowed, period of repayment, suggested interest rate, and purpose of the funds.
4. Send the form to the friend specified in step 1 until the money you’ve required is transferred into your account. (Roy, 2015)

However, after nine months of operation, Alipay terminated its IOU function. Why? On March 9, 2016, a sophomore in Henan Province, going by the alias of “Zheng Xu,” committed suicide because he was unable to pay back the money he had borrowed (RMB 600,000 in total) from several online lending firms, Alipay’s IOU among them. Zheng, having come from a poor, agrarian background, was a model student in secondary school. It came as a shock to find out he had compiled such a massive debt, and even involved 28 of his classmates in his borrowing activity. Zheng’s borrowing came to an unfortunate conclusion when, feeling depressed and hopeless under the weight of the debt, he left a final message to his family before ending his life:

As a son of yours, I feel very sorry to you. But I’m not up to [living anymore], especially when I found [that all of my efforts in life were in vain]...I heard that jumping from the building may feel very painful, but I’m really tired! I do appreciate your help and the meticulous

care you showed me as always, and I’m so sorry to all of you. (Hu, 2016)

After Zheng’s suicide, Chen Zijun, a lawyer from Shanghai, mentioned that the rise of peer-to-peer (P2P) lending practices on college campuses posed real challenges, both ethical and legal, and currently lack substantial regulation:

According to the *Interim Measures for the Administration of Personal Loans*, the personal loans shall be in accordance with the legal compliance, principle of prudent operation, equality, voluntary, fairness and sincerity. In consideration of the particularity of college students, the legislation shall take into full account their repayment capacity, enhance a healthy consumption concept and protect their lawful rights and interests. It was in response to Zheng’s death that Alipay removed its IOU function from its list of services. (Hu, 2016)

But not for long. Several days after it was removed, the Ministry of Education and the Chinese Banking Regulatory Commission issued its *Notification on Strengthening the Risk Prevention and Educational Guidance of Bad Online Lending Practice on Campus*, which requires “colleges and universities to establish a monitoring and precautionary system to protect students from the schemes of irregular online lending firms” (Tang, 2016). Since August, 2016, Alipay’s IOU function has been back in operation.

Another P2P lending platform, Jiedaibao, was established by Kunwu Jiuding Capital Holdings Co., Ltd. Like Alipay, Jiedaibao has a relatively basic loan approval process, but claims to go further in terms of privacy, especially for the lender. Lenders on Jiedaibao enjoy what the firm calls “unidirectional anonymity,” which prohibits the borrowers from knowing from whom their loans are originating. This operational model was praised by the industry and garnered a number of awards, including the Annual Most Influential Brand by the 2015 Global Mobile Internet CEO Summit, the New Financial Service Award by

the *National Business Daily*, and The Most Innovative APP in Financial Field by the CNR News (Jiedaibao, n.d.).

However, Jiedaibao found itself at the centre of controversy at the end of November, 2016, when a substantial number of nude pictures and videos were leaked online (CnBeta, 2016). The pictures and videos were collected as a substitute for instalments on loans borrowed by (mostly) female college students. The *China Daily* reported:

Many Chinese university students were found to have used their nude pictures as IOUs on some online lending platforms, putting themselves at risk of having everybody - including their parents - see them naked. (Jiang, 2016)

It was also reported that some lenders were charging inordinately high interest rates, 1,564 percent being one of the highest, which may have contributed to the fact that these women could not pay their instalments. These revelations created a public outcry. A collection of sentiments from Chinese social media are set out below:

I will never ever understand such behaviours taken by female students who took nude picture in order to borrow one or two thousand yuan, while some of them lent out one thousand yuan at an excessive rate of interest. [...] Most of college students are adults, who had to learn to take responsibility for their own mistakes. Meanwhile, they must stand out for rights violation. – Dianfeng Juanke (He, 2017)

Taking nude pictures for loan revealed a crucial point of social reality that for young ladies of those pictures, the indignity of being poor has now far exceeded the indignity of being naked - this feeling forced them to put their entire privacy and networking at risk for [a few] thousand yuan. – Caiwang (He, 2017)

Their 'buy first, pay later' idea was easy to sell. Credit service users could choose between delayed payments and repayments in instalments. Students need to spend just five minutes to fill in the consumer credit application online. – *China Daily* (Jiang, 2016)

In response to the resulting outrage, Jiedaibao posted an official statement clarifying their position:

Jiedaibao is an online P2P lending platform adhering to the principle of lawfulness and compliance. The company [claims] no responsible [or ownership] for the nude pictures. These inappropriate photos came from private deals between users and third parties through irregular operations...Concerning the spreading of nude pictures online, the Department of Legal Affairs has collected the relevant evidence and already reported this to the responsible public security organ. We intend to take legal actions to crack down on the persons responsible for the illegal lending practices and for [disseminating the nude photographs]. (CnBeta, 2016)

P2P lending, which is an offshoot of a more general borrowing trend on college campuses¹, is becoming more popular among students. Quick access to cash without the barriers that traditional banks impose, on the one hand, gives students more freedom of choice at university. On the other, however, it can be a temptation that smothers one in debt. Such a situation can result in tragedies like those aforementioned. According to a survey distributed by Beijing Zhicheng Credit Service Co., Ltd. in April, 2015, 78 percent of college students responded that they experienced a shortage of funds either frequently or occasionally. 2.6 percent of respondents reportedly applied for microcredits and 8.6

1 Other types of credit acquired by university students include shopping loans offered by shopping platforms, credit lines offered by companies such as Taobao and JD, and microloans offered by traditional banks.

percent indicated that they investigated online P2P firms. 15.5 percent stated they addressed their financial shortcoming through traditional bank loans (Zou, 2016). Another survey, within the *Consumption Report of Online P2P Lending in College Students*, revealed that 29 percent of respondents applied for loans, of which over 60 percent obtained financing through a P2P platform (Jin, 2017).

As P2P lending grows in prevalence, questions are emerging as to the responsibilities of platforms such as Alipay and Jiedaibao to their users, both lenders and borrowers. Given their role as intermediaries who simply provide the means for lenders and borrowers to facilitate financing transactions, are they absolved from responsibility if, for example, lenders engage in predatory practices? Are they responsible if lenders, for example, begin demanding nude

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photos from female borrowers? Or if lenders are charging over 1,000 percent interest? The basic requirement for entering into a financing transaction using Alipay's IOU is that lender and borrower be "friends." This assumes that, by virtue of their status as "friends," the parties will carry out their exchanges within reason, and without exposing one or the other party to undue risk.

The examples above show how lenders can abuse borrowers. But given the rather sketchy requirements for borrowers to obtain financing, there is also the possibility of lenders being taken advantage of, especially because companies like Alipay and Jiedaibao do not guarantee the loans transacted on their platforms. There is good

reason for this. In August 2015, the Supreme People's Court of China ruled that "online P2P lending platforms who offer guarantee for the loan shall bear the responsibility for bond" (Article 22) (Supreme People's Court, 2015). In other words, Alipay and Jiedaibao do not have much incentive to guarantee loans, given the risk of having to assume liability for loan defaults.

Another area of concern is whether Alipay and Jiedaibao are enabling predatory lenders to exploit needy borrowers, due to their all-too-easy requirements for borrowers obtaining credit. The four steps for obtaining a loan through Alipay's IOU couldn't be more basic and reveal nothing of the borrower's credit history or current financial standing. This can put borrowers – and potentially their families – in desperate situations if they borrow more than they can repay. Perhaps that is why, in April, 2017, the China Banking Regulatory Commissions declared that "offering online lending service to college students under 18 years old is prohibited" (Jin, 2017). This is likely because young, uninformed borrowers are at a higher risk of entering into financing agreements they are unable to uphold, and thereby at a higher risk of being sued, or worse exploited, by unsympathetic lenders.

A parallel example of how a platform might allow predatory behaviour is Baidu. Their Tieba forums were the cause of scandal, when in 2016 the company began bidding out the administration of its disease-related forums –that is, the ability to monitor and manage the content of exchanges– to unlicensed private hospitals, unqualified doctors and pharmaceutical companies. This decision allowed predatory, for-profit organizations to begin pushing their own products and services to the users of the forums. The result? Many users who decided to buy the products or procure the services soon found out that either the offers were fabricated or not at all what they expected. In other words, Baidu was the platform through which exploitative exchanges were being facilitated. Public outrage eventually forced Baidu's hand, and they altered their policies to curb the abuse; but the damage was done. Similar responses are becoming increasingly common in the P2P industry. Critics suggest that companies

like Alipay and Jiedaibao ought to engage in proactive self-governance instead of waiting for either government regulations to catch up or a public scandal to force a reactionary adjustment.

A related area of concern surrounds the idea of disclosure. In the *Consumption Report of Online P2P Lending for College Students*, 68 percent of college students reported that they received less than RMB 1,500 per month for living expenses, mostly from their parents. This has caused students to look for additional sources of income, one of those sources being P2P companies. However, P2P companies seem to have done a poor job ensuring that new borrowers are well informed of their debt obligations. For example, in the study cited above, only 22 percent of those who borrowed money “understood the terms of loans well” (Jin, 2017). This is a major problem, because had they understood the terms of their loans thoroughly, they may not have gone through with it in the first place.

Perhaps at this point Confucius’ teaching should be recalled:

Wealth and high rank are what people desire; if they are attained by not following the *dao*, do not dwell in them. Poverty and mean rank are what people hate; if they cannot be overcome by following the *dao*, do not depart from them. (Confucius, 2015, p. 14)

Building on this wisdom, a commentary from *Netease* on the P2P phenomenon on college campuses in China stated that:

A normal financial ecology on campus means that: college students take their own responsibility for the debt default; financial institutions who issue irregular loans bear the loss by itself; the financial supervisory departments offer financial education and punish the abusive mortgage lenders in a timely fashion. (Nie, 2016)

As P2P lending grows and becomes more prevalent, what can pioneer platforms like Alipay and Jiedaibao do to help prevent the kind of

tragedies and abuses described above?

- Proactively work with the Chinese government to develop consumer-centric industry regulations: Firms like Alipay and Jiedaibao bring valuable industry experience that can help regulatory agencies develop appropriate guidelines for the marketplace. This is advantageous because the firms who contribute to this process will not, except in cases of wilful disregard, find themselves in trouble with the law. It also sends a message to their consumers that their best interests are being taken to heart and that they want to be compliant, transparent, and fair. This kind of behaviour creates win-win outcomes for all stakeholders involved.
- Offer values education to college students: As P2P lending becomes popular on university campuses in China, there is an opportunity for leading companies like Alipay and Jiedaibao to educate prospective borrowers about the risks involved in obtaining financing. Informing borrowers about predatory lending, illegal loan outlets, interest rates and amortization tables, and living within one’s means, will not only create better and more responsible borrowers, but also position certain brands as trustworthy authorities within an industry. The more trust a firm demands from the market, the more likely they will be top of mind when prospective borrowers begin searching for credit. Firms could conduct values education by setting up on-campus lectures or workshops, or offering a live hotline for borrowers to learn about financing and the specific risks facing them as students.
- Partner with universities to provide scholarships or related aid: If Alipay, for example, wanted to offer services to a university, then they could provide incentives, such as scholarships, to students in need as a means of promotion and brand building. This would encourage the university to do its due diligence, to ensure they are not promoting exploitative platforms to their students, while incentivising the platforms to hold themselves accountable to strict standards of excellence,

so as not to tarnish their image amongst target markets.

- Setting standards of excellence in the industry: P2P lending firms would be wise to target those borrowers who can demonstrate an ability to repay their debts. Establishing a more robust qualification process will weed out unlikely borrowers and assure lenders that their borrowers will make good on their loans. This is win-win. It allows borrowers to acquire needed cash and lenders to make money from interest payments. It protects borrowers from entering into lending situations they don't fully understand and prevents lenders from exploiting gullible borrowers. It hedges against scandal and promotes sustainability.

The regulatory environment for the P2P industry in China is still developing. Significant ambiguity exists concerning how P2P companies should operate their platforms. Given this, in May, 2017 the China Banking Regulatory Commission (CBRC), Central Committee of the Communist Youth League and Ministry of Education jointly released a regulatory notice stipulating a series of restrictions on P2P companies and requiring local authority and banking institutions to adopt measures to put an end to financial exploitation on university campuses (China Banking Regulatory Commission, 2017). At the same time, the central government has begun monitoring the source of campus loans and prohibiting P2P lending firms from offering credit services to college students without the approval of the CBRC.

One counter to the abuses within the P2P industry, particularly as practiced in university settings, is financial education. The first Chinese platform dedicated to such education, "Practical Money Skills", was co-developed by Visa Greater China and the China Financial Literacy Education Synergy Innovation Center at Beijing Normal University in 2017. Then CEO of Visa, Shirley Yu-Tsui, considered it "a meaningful attempt in the field of digital financial education" (Sina, 2017). The platform was designed to "equip people worldwide with money management tools and resources." Given the company's expertise in financial services, Visa Greater China was

able to help "individuals and communities to build healthy futures by receiving interactive tools and educational resources." They did this through online learning and through commercial banks who would reach out to local colleges and universities to provide a range of financial literacy services, including teach-ins, forums, and training seminars. One example of the latter was the launch of, "Introducing Financial Literacy to Campus", an initiative developed by 62 universities and 35 Chinese-funded commercial banks in Shanghai in response to the lack of such resources on university campuses in China (Lin, 2017). Many well renowned financial institutions participated, including the China Construction Bank Shanghai Branch, Shanghai Pudong Development Bank, and Industrial Bank Co., Ltd. Similar initiatives have been launched in Beijing as well. For example, the Bank of Communications Beijing Branch developed a series of financial literacy lectures, which were integrated into curriculums at Beijing Forestry University (The Beijing News, 2017). Likewise, the Banking Association of Guangdong carried out promotional campaigns focusing on the dangers of bad loans and irresponsible borrowing (Li, 2016).

It is promising to see China's financial institutions responding to the central government's call to reduce abuse and increase knowledge about financial literacy on China's university campuses. For P2P companies, this knowledge will result in more prudent borrowers and more honest lenders. Paired with the commendable and ongoing efforts of China's authorities in developing responsible regulations for the P2P industry, there is hope for reform, the rebuilding of trust and the shaping of P2P practices toward the common good.

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