Library of Selected Cases from the Chinese Court

China Institute of
Applied Jurisprudence *Editor*

Selected Cases from the Supreme People's Court of the People's Republic of China

Volume 1

法律出版社
LAW PRESS·CHINA

Springer

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This series focuses on telling Chinese legal stories in Chinese voices, vividly and intuitively demonstrating the concept, achievements and real-world experience of socialist rule of law with Chinese characteristics. In addition, it is intended to further comparative research on Chinese and foreign cases, promote international legal exchanges, and contribute Chinese judicial wisdom and judicial experiences to global governance.

The cases presented in the series are strictly selected by the trial departments of the Supreme People's Court from their concluded cases, which include guiding cases of the Supreme People's Court; cases deliberated on by the Judicial Committee of the Supreme People's Court; and cases discussed at the Joint Meetings of Presiding Judges from the various tribunals. These cases are of great significance in terms of revealing or clarifying the application of legal rules, establishing new methods of adjudication, and filling in legal loopholes or gaps. The writers are the presiding judges for the respective cases, and possess substantial experience in making judicial decisions. Their familiarity with the facts of the case, legal thinking and reasoning, the decisional methodology and the application of the law makes them ideally suited to conveying to readers the legal processes, legal methodology and ideology in an intuitive, clear, and accurate manner.

This series aims to: a) improve the guiding case system and promote consistency regarding the applicable standards of law; b) contribute to a harmonious society by employing judicial rationality; and c) share China's judicial wisdom with the rest of the world and foster international legal exchanges.

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ISSN 2662-5261 ISSN 2662-527X (electronic)
Library of Selected Cases from the Chinese Court
ISBN 978-981-15-0341-2 ISBN 978-981-15-0342-9 (eBook)
https://doi.org/10.1007/978-981-15-0342-9

Jointly published with Law Press China
The print edition is not for sale in China Mainland. Customers from China Mainland please order the print book from: Law Press China.

This Springer imprint is published by the registered company Springer Nature Singapore Pte Ltd.
The registered company address is: 152 Beach Road, #21-01/04 Gateway East, Singapore 189721, Singapore

Preface

Sitting at the top of the judicial hierarchy in this country, the Supreme People's Court of the People's Republic of China has adjudicated a great number of vital and hard cases each year, which has greatly exerted enormous influence on the rule of law in China and contributed Chinese judicial wisdom to the world. In order to give full play to the legal value and social functions of the Supreme People's Court cases, to achieve the goal of "serving the trial practices, serving economic and social development, serving legal education and legal scholarship, serving international legal exchanges among Chinese and foreign legal communities, and serving the rule of law in China", the China Institute of Applied Jurisprudence, on approval of the Supreme People's Court, has made a decision of editing "Selected Cases from the Supreme People's Court of the People's Republic of China" in both Chinese and English languages since 2018 for domestic and overseas distribution.

The selected cases in the series are strictly sifted by the trial departments of the Supreme People's Court from their adjudicated cases, which include the guiding cases of the Supreme People's Court, the cases deliberated by the Judicial Committee of the Supreme People's Court, and the cases discussed at the Joint Meetings of Presiding Judges from various tribunals. These cases are of typical significance in revealing or clarifying the application of the legal rules, establishing new methods of adjudication, filling in legal loopholes or gaps. The writers are the presiding judges of these selected cases, who are experts in the trials at the Supreme People's Court. They have possessed profound legal attainments and rich experience in making judicial decisions. Their familiarity with the facts of the cases, legal thinking and reasoning, the decisional methodology, and the application of laws has enabled them to convey to readers the legal processes, legal methodology and ideology in an intuitive, clear, and accurate manner.

The selected cases from the Supreme People's Court of the People's Republic of China are subdivided into four sections: (a) Cases by Justices (judges next to the Chief Justice in the court hierarchy), which are cases that have exerted profound influence throughout the country and the world; (b) Selected Judicial Opinion(s), which is (are) the excellent judgment documents that the Supreme People's Court has heard and which has (have) aroused widespread concern in the whole society

this year and affected the legal development of China; (c) "Hot Cases", which are the edge-cutting and hard cases that have aroused great concern of the public, to function a role of early warning or predicting the legal issues in the hot spots; and (d) "Representative Cases", cases involving criminal, civil, commercial, intellectual property, and administrative law, to reflect the latest endeavor and adjudication of the Supreme People's Court in various fields.

By modeling upon the layout and design of the case systems at home and abroad, the editors, for the convenience of the readers, take into account the reading habits of readers of different legal systems and use subtitles to identify accurately the core legal issues and highlights of the case. The case layout includes such elements as **Title**, **Subtitle**, **Rule**, **Case Information**, **Essential Facts**, **Issue(s)**, **Holding**, and **Comment on Rule** for reading or retrieval.

Through the publication of the series of Selected Cases from the Supreme People's Court of the People's Republic of China, we hope to achieve the following objectives: (a) to improve the guiding case system and promote the uniformity of the applicable standards of law. Through systematically editing and publishing the classic cases adjudicated by the Supreme People's Court every year, we hope to guide the trial practices of people's courts at all levels to unify judicial standards, to restrain the judicial discretions, to treat like cases alike, to promote justice, to maintain legal unity, to establish the authority and confidence among the public of the people's courts, and to prevent effectively various legal risks; (b) to promote a harmonious society by imparting the judicial rationality. By way of these cases, people can be informed of adjudicative methodology and ideology as well as authoritative positions held by the Supreme People's Court toward the newer, challenging, and complex issues in the current economic, cultural, scientific, and social life so as to promote the rule of law, display fairer concept of justice, and show due respect toward law; and (c) to contribute to the world China's judicial wisdom and help promote the international legal exchanges.

The series are to be published in Chinese and English languages, orienting at telling Chinese law stories in Chinese voice, vividly and intuitively demonstrating the concept, achievements and experience of socialist rule of law with Chinese characteristics, furthering comparative research on Chinese and foreign cases, promoting international legal exchanges, and contributing Chinese judicial wisdom and judicial experiences to the global governance.

Editorial Board
December 2018

Editorial Instructions

As a great many laws and regulations and other legal texts are covered in this volume, and most often they are used in their simpler form, three types, namely laws, regulations, and judicial interpretations or other normative documents, are classified for easy reading or retrieval.

Laws (Statutes Enacted by the National People's Congress)

Constitutional Enactments

The Organic Law of the Local People's Congress and Local People's Governments of the People's Republic of China (Rev. 2015)
Hereinafter referred to as "Organic Law of Local Congresses and Local Governments"; adopted at the Second Session of the Fifth National People's Congress on July 1, 1979, publicized by Order No.1 of the Chairman of the Standing Committee of the National People's Congress on July 4, 1979, implemented on January 1, 1980; amended for the first time in accordance with the Decision on Revising Certain Provisions of the Organic Law of the Local People's Congresses and Local People's Governments of the People's Republic of China, adopted at the Fifth Session of the Fifth National People's Congress on December 10, 1982; amended for the second time in accordance with the Decision on Revising the Organic Law of the Local People's Congresses and Local People's Governments of the People's Republic of China, adopted at the Eighteenth Session of the Standing Committee of the Sixth National People's Congress on December 2, 1986; amended for the third time in accordance with the Decision on Revising the Organic Law of the Local People's Congresses and Local People's Governments of the People's Republic of China, adopted at the Twelfth Meeting of the Standing

Committee of the Eighth National People's Congress on February 28,1995; amended for the fourth time in accordance with the Decision on Revising the Organic Law of the Local People's Congresses and Local People's Governments of the People's Republic of China adopted at the Twelfth Meeting of the Standing Committee of the Tenth National People's Congress on October 27, 2004; and amended for the fifth time in accordance with Decision on Revising the Organic Law of the Local People's Congresses and Local People's Governments of the People's Republic of China, on Revising the Election Law of the National People's Congress and Local People's Congresses of the People's Republic of China, and on Revising the Law of the People's Republic of China on Deputies to the National People's Congress and to the Local People's Congresses at Various Levels, adopted at the Sixteenth Meeting of the Standing Committee of the Twelfth National People's Congress on August 29, 2015.

The Law of the People's Republic of China on Legislation (Rev. 2015)
Hereinafter referred to as "Legislation Law"; adopted at the Third Session of the Ninth National People's Congress on March 15, 2000, revised at the Third Session of the Twelfth National People's Congress on March 15, 2015, in accordance with the Decision on Revising the Legislative Law of the People's Republic of China.

Anti-Terrorism Law of the People's Republic of China (Rev. 2018)
Hereinafter referred to as "Anti-Terrorism Law"; adopted at the Eighteenth Session of the Standing Committee of the Twelfth National People's Congress on December 27, 2015, and amended in accordance with the Decision on Revising the Border Health and Quarantine Law of the People's Republic of China and Five Other Laws adopted at the Second Session of the Standing Committee of the Thirteenth National People's Congress on April 27, 2018.

Administrative Enactments

Land Administration Law of the People's Republic of China (Rev. 2004)
Hereinafter referred to as "Land Administration Law"; adopted at the Sixthteenth Session of the Standing Committee of the Ninth National People's Congress of the People's Republic of China on June 25, 1986; revised in accordance with the Decision on Amending Land Administration Law of the People's Republic of China; revised and adopted at the Fourth Session of the Standing Committee of the Ninth National People's Congress of the People's Republic of China on August 29, 1998, implemented as of January 1, 1999; revised at the Eleventh Session of the Standing Committee of the Tenth National People's Congress on August 28, 2004.

The Environmental Protection Law of the People's Republic of China (Rev. 2014)
Hereinafter referred to as "Environmental Protection Law"; adopted at the Eleventh Session of the Standing Committee of the Seventh National People's Congress on December 26, 1989, revised at the Eighth Session of the Standing Committee of the Twelfth National People's Congress on April 24, 2014.

Law of the People's Republic of China on Administrative Reconsideration (Rev. 2017)
Hereinafter referred to as "Administrative Reconsideration Law"; adopted at the Ninth Meeting of the Standing Committee of the Ninth National People's Congress on April 29, 1999, publicized by the Presidential Order No. 16 of the People's Republic of China; implemented on October 1, 1999; the first revision made in accordance with the Decision on Amending Certain Laws at the Tenth Meeting of the Standing Committee of the Eleventh National People's Congress on August 27, 2009, the second revision made in accordance with the Decision on Amending Eight Laws of the People's Republic of China at the Twenty-Ninth Meeting of the Standing Committee of the Twelfth National People's Congress on September 1, 2017.

Criminal Enactments

The Criminal Law of the People's Republic of China (Rev. 2017)
Hereinafter referred to as "Criminal Law"; adopted at the Second Session of the Fifth National People's Congress on July 1, 1979, by No. 5 Chairman Decree of the Standing Committee of the National People's Congress on July 6, 1979, and implemented as of January 1, 1980; revised at the Fifth Session of the Eighth National People's Congress on March 14, 1997, announced by the Presidential Order No. 83 of the People's Republic of China on March 14, 1997; Amendment to the Criminal Law of the People's Republic of China on December 25, 1999; Amendment to the Criminal Law of the People's Republic of China (II) on August 31, 2001; Amendment to the Criminal Law of the People's Republic of China (III) on December 29, 2001; Amendment to the Criminal Law of the People's Republic of China (IV) on December 28, 2002; Amendment to the Criminal Law of the People's Republic of China (V) on February 28, 2005; Amendment to the Criminal Law of the People's Republic of China (VI) on June 29, 2006; Amendment to the Criminal Law of the People's Republic of China (VII) on February 28, 2009; Amendment to the Criminal Law of the People's Republic of China (VIII) on February 25, 2011; Amendment to the Criminal Law of the People's Republic of China (IX) on August 29, 2015; Amendment to the Criminal Law of the People's Republic of China (X) on November 4, 2017.

Civil and Commercial Enactments

The Trademark Law of the People's Republic of China (Rev. 2013)
Hereinafter referred to as "Trademark Law"; adopted by the Twenty-fourth Session of the Standing Committee of the Fifth National People's Congress on August 23, 1982; first revision in accordance with the Decision on Revising the Trademark Law of the People's Republic of China of the Thirtieth Session of the Standing Committee of the Seventh National People's Congress on February 22, 1993; second revision in accordance with the Decision on Revising the Trademark Law of the People's Republic of China of the Twenty-fourth Session of the Standing Committee of the Ninth National People's Congress on October 27, 2001; third revision in accordance with the Decision on Revising the Trademark Law of the People's Republic of China of the Fourth Session of the Standing Committee of the Twelfth National People's Congress on August 30, 2013.

The Patent Law of the People's Republic of China (Rev. 2008)
Hereinafter referred to as "Patent Law"; adopted by the Fourth Session of the Standing Committee of the Sixth National People's Congress on March 12, 1984, implemented as of April 1, 1985; first revision in accordance with the Decision on Revising the Patent Law of the People's Republic of China of the Twenty-seventh Session of the Standing Committee of the Seventh National People's Congress on September 4, 1992; second revision in accordance with the Decision on Revising the Patent Law of the People's Republic of China of the Seventeenth Session of the Standing Committee of the Ninth National People's Congress on August 25, 2000; third revision made in accordance with the Decision on Revising the Patent Law of the People's Republic of China of the Sixth Session of the Standing Committee of the Eleventh National People's Congress on December 27, 2008.

General Principles of Civil Law of the People's Republic of China (Rev. 2009)
Hereinafter referred to as "General Principles of Civil Law"; adopted on April 12, 1986, by the Fourth Session of the Sixth National People's Congress, implemented as of January 1, 1987; revised at the Tenth Session of the Meeting of the Eleventh National People's Congress on August 27, 2009.

The Company Law of the People's Republic of China (Rev. 2018)
Hereinafter referred to as "Company Law"; adopted by the Fifth Session of the Standing Committee of the Eighth National People's Congress on December 29, 1993; revised in accordance with the Decision on Revising the Company Law of the People's Republic of China by the Thirteenth Session of the Standing Committee of the Ninth National People's Congress on December 25, 1999; revised in accordance with the Decision on Revising the Company Law of the People's Republic of China by the Eleventh Session of the Standing Committee of the Tenth National People's Congress on August 28, 2004; revised by the Eighteenth Session of the Standing Committee of the Tenth National People's Congress on October 27, 2005; revised in accordance with the Decision on Revising Seven Laws Including

the Law of the People's Republic of China on Protection of Marine Environment by the Sixth Session of the Standing Committee of the Twelfth National People's Congress on December 28, 2013; revised in accordance with the Decision of the Standing Committee of the National People's Congress on Revising the Company Law of the People's Republic of China at the Sixth Session of the Standing Committee of the Thirteenth National People's Congress of the People's Republic of China on October 26, 2018.

The Commercial Banking Law of the People's Republic of China (Rev. 2015)
Hereinafter referred to as "Commercial Banking Law"; adopted on May 10, 1995, by the Thirteenth Session of the Eighth National People's Congress; revised on December 27, 2003, in accordance with the Decision on Revising the Commercial Banking Law adopted by the Sixth Session of the Standing Committee of the Tenth National People's Congress; revised at the Sixteenth Session of the Standing Committee of the Twelfth National People's Congress on August 29, 2015, in accordance with the Decision of the Standing Committee of the National People's Congress on Revising the Commercial Banking Law of the People's Republic of China.

The Security Law of the People's Republic of China
Hereinafter referred to as "Security Law"; adopted on June 30, 1995, by the Fourteenth Session of the Standing Committee of the Eighth National People's Congress.

The Contract Law of the People's Republic of China
Hereinafter referred to as "Contract Law"; adopted at the Second Session of the Ninth National People's Congress on March 15, 1999.

The Trust Law of the People's Republic of China
Hereinafter referred to as "Trust Law"; adopted on April 28, 2001, at the Twenty-first Meeting of the Standing Committee of the Ninth National People's Congress, issued by the Presidential Order No. 50 of the People's Republic of China on April 28, 2001.

Enterprise Bankruptcy Law of the People's Republic of China
Hereinafter referred to as "Enterprise Bankruptcy Law"; adopted at the Twenty-third Session of the Standing Committee of the Tenth National People's Congress on August 27, 2006, to be implemented on June 1, 2007.

The Real Right Law of the People's Republic of China
Hereinafter referred to as "Real Right Law"; adopted at the Fifth Session of the Tenth National People's Congress on March 16, 2007, publicized by the Presidential Order No. 62 of the People's Republic of China, implemented on October 1, 2007.

The Tort Law of the People's Republic of China
Hereinafter referred to as "Tort Law"; adopted at the Twelfth Session of the Standing Committee of the Eleventh National People's Congress on December 26, 2009, to be implemented on July 1, 2010.

General Rules of the Civil Law of the People's Republic of China
Hereinafter referred to as "General Rules of the Civil Law"; adopted at the Fifth Session of the Twelfth National People's Congress of the People's Republic of China on March 15, 2017, to be implemented on October 1, 2017.

Economic Enactments

Law of the People's Republic of China against Unfair Competition (Rev. 2017)
Hereinafter referred to as "Law against Unfair Competition"; adopted at the Third Session of the Standing Committee of the Eighth National People's Congress on September 2, 1993, publicized by the Presidential Order No. 10 of the People's Republic of China; revised at the Thirtieth Session of the Standing Committee of the Twelfth National People's Congress on November 4, 2017.

The Anti-monopoly Law of the People's Republic of China
Hereinafter referred to as "Anti-monopoly Law"; adopted on August 30, 2007, at the Twenty-ninth Session of the Standing Committee of the Tenth National People's Congress, publicized by the Presidential Order No. 68 of the People's Republic of China, implemented on August 1, 2008.

Procedural Enactments

Criminal Procedure Law of the People's Republic of China (Rev. 2018)
Hereinafter referred to as "Criminal Procedure Law"; adopted at the Second Session of the Fifth National People's Congress on July 1, 1979, amended for the first time in accordance with the Decision on Revising the Criminal Procedure Law of the People's Republic of China, adopted at the Fourth Session of the Eighth National People's Congress on March 17, 1996; amended for the second time in accordance with the Decision on Revising the Criminal Procedure Law of the People's Republic of China, adopted at the Fifth Session of the Eleventh National People's Congress on March 14, 2012; amended for the third time in accordance with the Decision on Revising the Criminal Procedure Law of the People's Republic of China, adopted at the Sixth Session of the Standing Committee of the Thirteenth National People's Congress on October 26, 2018.

Administrative Procedure Law of the People's Republic of China (Rev. 2017)
Hereinafter referred to as "Administrative Procedure Law"; adopted on April 4, 1989, by the Second Session of the Seventh National People's Congress; revised on November 11, 2014 in accordance with the Decision of the Standing Committee of the National People's Congress on Revising the Civil Procedure Law of the People's Republic of China and the Administrative Procedure Law of the People's Republic of China; revised at the Twenty-eighth Session of the Standing Committee of the Twelfth National People's Congress on June 27, 2017, in accordance with the Decision of the Standing Committee of the National People's Congress on Revising the Civil Procedure Law of the People's Republic of China and the Administrative Procedure Law of the People's Republic of China.

Civil Procedural Law of the People's Republic of China (Rev. 2017)
Hereinafter referred to as "Civil Procedural Law"; adopted at the Fouth Session of the Standing Committee of the Seventh National People's Congress on April 9, 1991, publicized by the Presidential Order No. 44 of the People's Republic of China; revised for the first time in accordance with the Decision on Revising the Civil Procedural Law of the People's Republic of China of the Thirtieth Session of the Standing Committee of the Tenth National People's Congress on October 28, 2007; revised for the second time in accordance with the Decision on Revising the Civil Procedural Law of the People's Republic of China of the Twenty-eighth Session of the Standing Committee of the Eleventh National People's Congress on August 31, 2012; revised for the third time in accordance with the Decision of the Standing Committee of the National People's Congress on Revising the Civil Procedural Law of the People's Republic of China and the Administrative Procedure Law of the People's Republic of China on June 27, 2017.

Regulations

Provisional Regulations of the People's Republic of China on Urban and Township Land Use Tax (Rev. 2013)
Hereinafter referred to as "Provisional Regulations on Urban and Township Land Use Tax"; adopted at the Twelfth Session of the Standing Committee of the People's Republic of China, publicized by No. 17 Decree of the State Council Order of the People's Republic of China on September 27, 1988, implemented on November 1, 1988; for the first time in accordance with the Decision of the State Council on Revising the Provisional Regulations of the People's Republic of China on Urban and Township Land Use Tax on December 31, 2006; revised for the second time in accordance with the Decision of the State Council on Repealing and Revising Certain Administrative Regulations on January 8, 2011; revised for the third time in accordance with the Decision of the State Council on Repealing and Revising Certain Administrative Regulations on December 7, 2013.

Administrative Measures of the People's Republic of China for Registration of the Mining of Mineral Resources (Rev. 2014)
Hereinafter referred to as "Administrative Measures for Registration of the Mining of Mineral Resources"; publicized by No. 241 Decree of the State Council Order of the People's Republic of China on February 12, 1998; revised in accordance with the Decision of the State Council on Repealing and Revising Certain Administrative Regulations on July 29, 2014.

Rules for Implementation of the Land Administration Law of the People's Republic of China (Rev. 2014)
Hereinafter referred to as "Rules for Implementing Land Administration Law"; publicized on December 24, 1998, by No. 256 Decree of the State Council Order of the People's Republic of China; revised for the first time in accordance with the Decision of the State Council on Repealing and Revising Certain Administrative Regulations on January 8, 2011; revised for the second time in accordance with the Decision of the State Council on Repealing and Revising Certain Administrative Regulations on July 29, 2014.

Implementation Regulations for the Copyright Law of the People's Republic of China (Rev. 2013)
Hereinafter referred to as "Regulations on Implementing the Copyright Law"; publicized by No. 359 Decree of the State Council Order of the People's Republic of China on August 2, 2002; revised for the first time in accordance with the Decision of State Council on Repealing and Revising Certain Administrative Regulations on January 8, 2011; revised for the second time in accordance with the Decision of State Council on Revising the Implementation Regulations for the Copyright Law of the People's Republic of China on January 30, 2013.

Regulations of the People's Republic of China on the Disclosure of Government Information (Rev. 2019)
Hereinafter referred to as "Regulations on the Disclosure of Government Information"; publicized by No. 492 Decree of the State Council Order of the People's Republic of China at the 165th Session of the Standing Committee on January 17, 2007, implemented on May 1, 2008.

Regulations of the People's Republic of China on the Expropriation of Houses on State-Owned Land and Compensation
Hereinafter referred to as "Regulations on the Expropriation of Houses on State-Owned Land and Compensation"; publicized by No. 590 Decree of the State Council Order of the People's Republic of China at the 141st Session of the Standing Committee on January 19, 2011, implemented on the same date of publication.

The Provisional Regulations of the People's Republic of China on Real Property Registration
Hereinafter referred to as "Provisional Regulations on Real Property Registration"; publicized by No. 656 Decree of the State Council Order of the People's Republic of China at the 656th Session of the Standing Committee on November 24, 2014, implemented on March 1, 2015.

Judicial Interpretations and Other Normative Documents

Interpretation of the Supreme People's Court on Certain Issues Concerning the Application of the Contract Law of the People's Republic of China (I) (SPC JI [1999] No. 19)
Hereinafter referred to as "Judicial Interpretation of Contract Law (I)"; adopted at the 1090th Session of the Judicial Committee of the Supreme People's Court on December 1, 1999, implemented on December 29, 1999.

Interpretation of the Supreme People's Court on the Application of Administrative Procedure Law of the People's Republic of China (SPC JI [2018] No. 1)
Hereinafter referred to as "Judicial Interpretation of the Application of Administrative Procedure Law"; adopted at the 1088th Session of the Judicial Committee of the Supreme People's Court on November 24, 1999; publicized as of March 8, 2000, and implemented as of March 10, 2000; invalidated as of February 28, 2018.

Interpretations of the Supreme People's Court on Several Issues Concerning the Application of the Security Law of the People's Republic of China (SPC JI [2000] No. 44)
Hereinafter referred to as "Judicial Interpretations of Application of the Security Law"; adopted at the 1133rd Meeting of the Judicial Committee of the Supreme People's Court on September 29, 2000, announced on December 8, 2000, and implemented on December 13, 2000.

Rules of the Supreme People's Court on Evidence in Civil Procedures (SPC JI [2001] No. 33)
Hereinafter referred to as "Rules on Evidence in Civil Procedures"; adopted at the 1201st Meeting of the Judicial Committee of the Supreme People's Court on December 6, 2001, announced on December 21, 2001, and implemented on April 1, 2002; adjusted in accordance with the Decision of the Supreme People's Court on Adjusting Judicial Interpretations and Other Documents Cited in the Civil Procedure Law of the People's Republic of China on December 16, 2008.

Rules of the Supreme People's Court on Several Issues Concerning Evidence in Administrative Litigation (SPC JI [2002] No. 21)
Hereinafter referred to as "Rules on Evidence in Administrative Litigation"; adopted by the 1224th Meeting of the Judicial Committee of the Supreme People's Court on June 4, 2002, announced on July 24, 2002, and implemented on October 1, 2002.

Interpretation of the Supreme People's Court on Issues Relating to Application of Law to the Copyright Dispute Cases (SPC JI [2002] No. 31)
Hereinafter referred to as "Judicial Interpretation of Applicable Law to Copyright Dispute Cases"; adopted on October 12, 2002, at the 1246th Meeting of the Judicial Committee of the Supreme People's Court; announced on October 12, 2002; implemented on October 15, 2002.

Interpretation of the Supreme People's Court on Certain Issues Concerning the Application of Law to Trademark Dispute Cases (SPC JI [2002] No. 32)
Hereinafter referred to as "Judicial Interpretation of Applicable Law to Trademark Dispute Cases"; adopted at the 1246th Meeting of the Judicial Committee of the Supreme People's Court on October 12, 2002, and implemented on October 16, 2002.

Interpretation of the Supreme People's Court on Issues Concerning Applicable Laws to Construction Contract Dispute Cases (SPC JI [2004] No. 14)
Hereinafter referred to as "Judicial Interpretation of Applicable Laws to Construction Contract Dispute Cases"; adopted at the 1327th Meeting of the Judicial Committee of the Supreme People's Court on September 29, 2004, announced on October 25, 2004, and implemented on January 1, 2005.

Interpretation of the Supreme People's Court on Issues Concerning the Application of Law to Contract Dispute Cases Regarding the State-Owned Land Use Rights (SPC JI [2005] No. 5)
Hereinafter referred to as "Judicial Interpretation of Issues Concerning State-Owned Land Use Rights Disputes"; adopted at the 1334th Meeting of the Judicial Committee of the Supreme People's Court on November 23, announced on June 18, 2005, and implemented on August 1, 2005.

Interpretation of the Supreme People's Court on Several Issues Concerning the Applicable Laws to Unfair Competition Cases (SPC JI [2007] No. 2)
Hereinafter referred to as "Judicial Interpretation of the Applicable Laws to Unfair Competition Cases"; adopted at the 1412th Meeting of the Judicial Committee of the Supreme People's Court, announced on January 12, 2007, and implemented on February 1, 2007.

Interpretation of the Supreme People's Court on Issues Concerning the Application of the Contract Law of the People's Republic of China (II) (SPC JI [2009] No. 5)
Hereinafter referred to as "Judicial Interpretation of Contract Law (II)"; adopted at the 1,462nd Meeting of the Judicial Committee of the Supreme People's Court on February 9, 2009, announced on April 24, and implemented on May 13, 2009.

Interpretation of the Supreme People's Court on Several Issues Concerning the Application of Law to Building Ownership Disputes (SPC JI [2009] No. 7)
Hereinafter referred to as "Judicial Interpretation of Building Ownership Disputes"; adopted at the 1464th Meeting of the Judicial Committee of the Supreme People's Court on March 23, 2009, announced on May 14, 2009, and implemented on October 1, 2009.

Interpretation of the Supreme People's Court on Certain Issues Regarding the Application of Law to Patent Infringement Cases (SPC JI [2009] No. 21)
Hereinafter referred to as "Judicial Interpretation of Applicable Law to Patent Infringement Cases"; adopted at 1,480th Meeting of the Judicial Committee of the Supreme People's Court on December 21, 2009, announced on December 28, 2009, and implemented on January 1, 2010.

Rule of the Supreme People's Court on Several Issues Concerning the Trial of Housing Registration Cases (SPC Rule [2010] No. 15)
Hereinafter referred to as "Regulations on the Trial of Housing Registration Cases"; adopted at the 1491st Meeting of the Judicial Committee of the Supreme People's Court on August 2, 2010; announced on November 5, 2010; implemented on November 18, 2010.

Interpretation of the Supreme People's Court on Certain Issues Relating to the Specific Application of Law to the Hearing of Illegal Fund Raising Cases (SPC JI [2010] No. 18)
Hereinafter referred to as "Judicial Interpretation of Applicable Law to Illegal Fundraising Cases"; adopted at the 1502nd Meeting of the Judicial Committee of the Supreme People's Court on November 22, 2010; announced on December 13, 2010; implemented on January 4, 2011.

Provisions of the Supreme People's Court on Several Issues Concerning the Trial of Administrative Cases of Government Information Disclosure (SPC JI [2011] No. 17)
Hereinafter referred to as the "Regulations on the Administrative Cases of Government Information Disclosure"; adopted at the 1505th Meeting of the Judicial Committee of the Supreme People's Court on December 13, 2010; announced on July 29, 2011; implemented on August 13, 2011.

Interpretation of the Supreme People's Court on the Application of the Criminal Procedure Law of the People's Republic of China (SPC JI [2012] No. 21)
Hereinafter referred to as "Judicial Interpretation of Criminal Procedure Law"; adopted at the 1559th Meeting of the Judicial Committee of the Supreme People's Court on November 5, 2012; announced on December 20, 2012; implemented on January 1, 2013.

Interpretation of the Supreme People's Court on Several Issues Regarding Application of Company Law of the People's Republic of China (III)(SPC JI [2014] No. 2)
Hereinafter referred to as "Judicial Interpretation of the Application of Company Law (III)"; adopted at the 1504th Meeting of the Judicial Committee of the Supreme People's Court on December 6, 2010; announced on January 27, 2011; implemented on February 16, 2011; amended at the 1607th Meeting of the Judicial Committee of the Supreme People's Court on February 17, 2014.

Interpretation of the Supreme People's Court on Issues Regarding Application of Law to Calculation of Debt Interests during Deferred Performance Period in Enforcement Process (SPC JI [2014] No. 8)
Hereinafter referred to as "Judicial Interpretation of Calculation of Debt Interests during Deferred Performance Period"; adopted at the 1619th Meeting of the Judicial Committee of the Supreme People's Court on June 9, 2014; announced on June 9, 2014; implemented on August 1, 2014.

Interpretation of the Supreme People's Court on Several Issues Concerning the Application of Law in the Trial of Public Interest Litigation Cases in Environmental Law (SPC JI [2015] No. 1)
Hereinafter referred to as the "Judicial Interpretation of Public Interest Cases"; adopted at the 1631st Meeting of the Judicial Committee of the Supreme People's Court on December 8, 2014; announced on January 6, 2015; implemented on January 7, 2015.

Interpretations of the Supreme People's Court on Application of the Civil Procedural Law of the People's Republic of China (SPC JI [2015] No. 5)
Hereinafter referred to as "Judicial Interpretation of the Application of Civil Procedural Law"; adopted at the 1636th Meeting of the Judicial Committee of the Supreme People's Court on December 18, 2014; announced on January 30, 2015; implemented on February 4, 2015.

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Hereinafter referred to as "Judicial Interpretation of Rules Concerning Objection to Performance and Reconsideration Cases"; adopted at the 1638th Meeting of the Judicial Committee of the Supreme People's Court on December 29, 2014; announced on May 5, 2015; implemented on May 5, 2015.

Rules of the Supreme People's Court on Application of Laws to the Private Lending Cases (SPC JI [2015] No. 18)
Hereinafter referred to as "Rules of Applicable Law to Private Lending Cases"; adopted at the 1655th Meeting of the Judicial Committee of the Supreme People's Court on June 23, 2015; announced on August 6, 2015; implemented on September 1, 2015.

Interpretation of the Supreme People's Court on Several Issues Concerning the Application of the Real Right Law of the People's Republic of China (I) (SPC JI [2016] No. 5)
Hereinafter referred to as "Judicial Interpretation of Real Right Law (I)"; adopted at the 1670th Meeting of the Judicial Committee of the Supreme People's Court on December 10, 2015; announced on February 22, 2016; implemented on March 1, 2016.

Rules of the Supreme People's Court on Issues Relating to the Administrative Cases Involving Granting or Affirming Trademark Rights (SPC JI [2017] No. 2)
Hereinafter referred to as "Rules on Administrative Cases involving Granting or Affirming Trademark Rights"; adopted at the 1703rd Meeting of the Judicial Committee of the Supreme People's Court on December 12, 2016; announced on January 10, 2017; implemented on March 1, 2017.

Interpretation of the Supreme People's Court on the Application of Administrative Procedure Law of the People's Republic of China (SPC JI [2018] No. 1)
Hereinafter referred to as "Judicial Interpretation of Administrative Procedural Law"; adopted at the 1,726th Meeting of the Judicial Committee of the Supreme People's Court on November 13, 2017; announced on February 6, 2018; implemented on February 8, 2018.

Opinions of the Supreme People's Court about Implementing the Criminal Policy of Tempering Justice with Mercy (SPC JI [2010] No. 9)
Hereinafter referred to as "Lenient and Harsh Punishment Opinions"; announced by the Supreme People's Court on February 8, 2010; implemented on February 8, 2010.

Several Opinions of the Supreme People's Court on Giving Full Play to the Role of Trial Functions and Effectively Maintaining Public Safety" (SPC JI [2015] No. 12)
Hereinafter referred to as "Opinions on the Role of the Trial Function to Safeguard the Public Safety"; announced on September 16, 2015; implemented on September 16, 2015.

Guidance of the Supreme People's Court for the Prevention and Sanction of Sham Litigation (SPC JI [2016] No. 13)
Hereinafter referred to as "Guidance for Prevention and Sanction of Sham Litigation"; announced on June 20, 2016; implemented on June 20, 2016.

Guiding Opinions of the Supreme People's Court on Several Issues Concerning the Transfer of Cases from Performance of Bankruptcy Review (SPC JI [2017] No. 2)
Hereinafter referred to as the "Guiding Opinions on the Transfer of Cases from Performance of Bankruptcy Review"; announced on January 20, 2017; implemented on January 20, 2017.

Notice of the Supreme People's Court on Issuing the Minutes of the Symposium on Issues Concerning Applicable Legal Rules in the Hearing of Administrative Cases (SPC JI [2004] No. 96)
Hereinafter referred to as "Symposium Minutes of Hearing Administrative Cases"; as announced by the Supreme People's Court on May 18, 2004; implemented on May 18, 2004.

Notice of the Supreme People's Court on the Announcement of the Revised Rules on Causes of Action for Civil Cases (SPC Rule [2011] No. 42)
Hereinafter referred to as "Rules on Causes of Action for Civil Cases"; adopted at the 1438th Meeting of the Judicial Committee of the Supreme People's Court on October 29, 2007; announced on February 4, 2008; implemented on April 1, 2008; revised on February 18, 2011.

Interim Rules of the Supreme People's Court on Several Issues Concerning the Participation of Technical Commissioner of Intellectual Property Courts in Litigation
Hereinafter referred to as "Interim Rules on Participation of Technical Investigation Officer in IP Court"; announced on December 31, 2014; implement on December 31, 2014.

The Opinions of the Supreme People's Court, the Supreme People's Procuratorate, the Ministry of Public Security, and the Ministry of Justice on Several Issues Concerning the Application of Laws in Handling Terrorist Activities and Extremist Crimes (SPC/SPP [2018] No. 1)
Hereinafter referred to as "Opinions about Handling Terrorist and Extremists Cases"; announced on March 16, 2018; implemented on March 16, 2018.

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Chenzhou Fanlongdui Mining Co., Ltd. v. the Ministry of Land and Resources of the People's Republic of China (Administrative Reconsideration Decision about the Land and Resources)—The Judicial Control over the Administrative Reconsideration Authority's Revocation of the Mining Rights

Bixin Jiang, Yongwei Huang and Baojian Gen

Rule

No prohibitions are contained in the current laws and regulations against the establishment of mining rights with overlapping vertical projections. With regard to some overlapping mining rights that have been established for historical reasons, the administrative agencies, under the premises of safe production, environmental protection and the conducive utility of full and effective use of different types of mineral resources, should evaluate comprehensively the formation and geological conditions of mineral resources, show due respect toward the mining intentions, mining capacity and mining technology of different mining rights holders as well as the development rules of mineral deposits, and treat them differently.

The administrative agency shall be bound by the initial administrative license for the discretion and judgment of the extension of the administrative license. Should the first license be flawed or illegal, the administrative agency shall prudently exercise its power of non-extension.

In the case that there are multiple treatments for the overlapping of mining rights and there may be multiple reconsideration conclusions, the reconsideration agency

The retrial collegiate bench: Jiang bixin, Huang Yongwei, Gen Baojian (Translated by: Zheng Daxuan; Proofread by: Zhang Hongsheng).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_1

shall, in making a revocation decision, fully evaluate the extent of loss of interest caused by the license revocation to the state, other people and the right holder(s), and balance the relationship between full and partial revocation, and supply full explanation or justifications for the decision.

Case Information

1. Parties

Retrial applicant (Plaintiff at trial, Appellant at the second instance trial): Chenzhou Fanlongdui Mining Co., Ltd (hereinafter referred to as "Fanlongdui Mining Co., Ltd.")
Respondent (Defendant at trial, Respondent at the second instance trial)): the Ministry of Land and Resources of the People's Republic of China
Respondent (Third party at trial, Respondent at the second instance trial): CITIC Group Xingguang Mining Co., Ltd. (hereinafter referred to as "CITIC Xingguang Mining Co. Ltd.") (CITIC refers to China International Trust & Investment Corporation)

2. Procedural History

First Instance: No. 839 [2015], Trial, Adm. Division, the First Intermediate People's Court of Beijing (dated Jul. 1 of 2015)
Second Instance: No. 3209 [2016], Final, Adm. Division, the Higher People's Court of Beijing (dated Mar. 2 of 2016)
Retrial: No. 6 [2018], Retrial, Adm. Division, the Supreme People's Court (dated Mar. 7 of 2018)

3. Cause of Action

Administrative reconsideration of land and resources

Essential Facts

On January 16, 2006, Hunan Provincial Land and Resources Bureau issued a mining license to Chenzhou Xingguang Mining Co., Ltd. The mine name is Hongqiling Mining Co., Ltd. of Chenzhou Xingguang Mining Co., Ltd. and the mining types are tin, tungsten and arsenic. Later, Hongqiling Mining Co., Ltd. cooperated with CITIC Group to establish CITIC Xingguang Mining Co., Ltd. In November 2010 and October 2011, CITIC Xingguang Mining Co., Ltd. handled the mining license renewal registration procedure in the Ministry of Land and Resources. The validity period of the mining license lasts from October 7, 2011 to October 7, 2012.

On March 24, 2006, Chenzhou Municipal Bureau of Land and Resources issued the mining license for the "Non-ferrous Metal Mines in the Northern Fanlongdui in Suxian District". The mining types are lead ore, zinc and silver, and the effective

period lasts from March of 2006 to March of 2011. Then through re-registration and extension of validity periods, Fanlongdui Mining Co. Ltd. is incorporated and registered as the new mining right holder, the mining license is valid from September 1, 2011 to September 9, 2014. Owing to inadequate solutions to the mining rights with overlapping vertical projections, CITIC Xingguang Mining Co. Ltd. applied in November 2012 to the Ministry of Land and Resources for an administrative reconsideration, requesting the Ministry of Land and Resources to cancel the mining license obtained by Fanlongdui Mining Co., Ltd. On July 14, 2014, the Ministry of Land and Resources made an administrative reconsideration decision numbered Administrative Reconsideration Decision on Land and Resources [2014] No. 455, in which the mining license issued by Hunan Provincial Land and Resources Bureau to Fanlongdui Mining Co., Ltd. was revoked Fanlongdui Mining Co., Ltd. refused the decision and filed an administrative lawsuit.

On July 1, 2015, the court of first instance (the First Intermediate People's Court of Beijing) made a judgment, No. 839 [2015], Trial, Adm. Division, the First Intermediate People's Court of Beijing, rejecting the claims of the said company. On March 2, 2016, the court of second instance (the Higher People's Court of Beijing) made a judgment, No. 3209 [2016], Final, Adm. Division, the Higher People's Court of Beijing, which dismissed the appeal and upheld the original judgment.

After the judgment came into effect, Fanlongdui Mining Co., Ltd. applied to the Supreme People's Court for retrial, requesting the Supreme People's Court to dismiss the judgments of the first and second instance courts, to revoke the administrative reconsideration decisions, and to order the Ministry of Land and Resources to made a new decision about the administrative reconsideration in accordance with law.

Issues

1. Is it legitimate for the Ministry of Land and Resources to handle the application by CITIC Xingguang Mining Co. Ltd. for administrative reconsideration?
2. Whether any illegality in the administrative licensing behavior in 2006 will inevitably affect the legality of the 2011 administrative licensing behavior?
3. Whether the vertical projection of the scope of the mining rights can overlap?
4. What are the terms and conditions for an administrative agency to process or cancel the overlapping projection mining licenses?
5. Is it necessary for the reconsideration decision-making agency to state the reasons?

Holding

The Supreme People's Court holds that, when applying for administrative reconsideration, CITIC Xingguang Mining Co. Ltd., although its mining license has expired,

still has legal rights other than mining resources and has the qualification for administrative reconsideration. The Ministry of Land and Resources accepts the application for administrative reconsideration of CITIC Xingguang Mining Co., Ltd., which is in compliance with the requirements of the *Administrative Reconsideration Law* regarding the acceptance of administrative reconsideration. Although the Ministry of Land and Resources of Hunan Province entrusted the Chenzhou Municipal Bureau of Land and Resources to issue the 2006 Mining License to Fanlongdui Mining Co., Ltd., although it was flawed, it was corrected because the Hunan Provincial Department of Land and Resources issued its certificate in its own name in 2011. The reason for the reconsideration by claiming that 2006 Mining License is illegal so that 2011 Mining License has to be revoked for this illegality cannot stand. The 2011 Mining License and the corresponding vertical projection overlap of the mining area specified by CITIC Xingguang Mining Co., Ltd. are true, but the disputed reconsideration decision did not fully investigate the facts and the overlaps. In the case of multiple treatments of overlapping issues and the availability of multiple reconsideration decisions, the failure to explain adequately the reasons and justifications, the failure to provide evidence for the necessity and urgency for making revocation decision, a rash revocation decision that 2011 mining license obtained by Fanlongdui Mining Co., Ltd. was revoked, and inadequate application of legal norms, have to be made right in accordance with law. The decisions made by the first and the second instance court to uphold the administrative reconsideration decision is not adequate and should be corrected altogether. Therefore, the Supreme People's Court holds: "The administrative judgments of the first and second instance courts were to be revoked; the administrative reconsideration decision of the administrative agencies was to be denied, and the Ministry of Land and Resources of the People's Republic of China was ordered to make a de novo administrative reconsideration decision."

Comment on Rule

The present case is concerned, in essence, with the re-cancellation of cancelling the administrative reconsideration in the legal relationship of the mining rights. The core issue in this case is whether the mining license obtained by CITIC Xingguang Mining Co. Ltd. and the mining license obtained by Fanlongdui Mining Co. Ltd. constitute "overlapping vertical projections" and whether the mining license later acquired (by Fanlongdui Mining Co. Ltd.) ought to be struck down by the administrative agency when overlapping vertical projections were recognized. "Mining rights are characterized with both the administrative license (franchising) and the property rights in civil law. In handling the legal relationships of mining rights, the law has to be properly applied to accommodate the state intervention and private autonomy."[1] We are

[1] Jiang [1].

to make further explanations of the reasons for coming to the conclusion from the perspectives of fact-finding and legal determinations of the overlapping vertical projection of the mining rights, the legality and validity of extending the administrative license, the substantive and the procedure control aspects of the benefits-granting administrative actions.

1. **Defining the "Overlapping Vertical Projection" of the Mining Rights**

The "overlapping vertical projection" of the mining rights is both technical and legal issue. The main reason for the decision to revoke or strike down the mining license of Fanlongdui Mining Co. Ltd. in this case is that there appears an overlapping vertical projection of mining rights acquired through the mining license granted to Fanlongdui Mining Co. Ltd. and CITIC Xingguang Mining Co. Ltd. It is generally believed that the overlapping vertical projection of the mining rights in the mining areas is referred to as the two mining rights in the upper and lower positions respectively. Although there is no physical intersection, the vertical projection forms an overlap on the plane. The overlapping vertical projection of the mining rights in the mining areas is invariable because the mineral resources available for mining are distributed on the surface of the earth or below the surface, and different types of mineral deposits may be layered in vertical spaces of different depths.

The current laws and regulations have not expressly provided for the overlapping of mining areas. However, from the perspective of safety production, vertical projections may overlap in whole or in part, which may pose certain safety hazards. Therefore, in order to facilitate administrative management, no vertical projection overlap is required in principle by the Ministry of Land and Resources.

As for the normative documents, Article 2 of the *Opinions of the Ministry of Land and Resources on Further Regulating the Management Order of Rectifying Mineral Resources* provides that in principle, there shall be only one mining entity to be approved by the state, and no illegal overlap or cross-prospection and cross-mining rights are allowed. In the meanwhile, Article 4 (3) (4) of the *Measures for the Administration of Registering the Mineral Resources* provides that the examination and approval authority shall "protect the existing prospecting rights and interests of the mining rights holders when demarcating the scope of the mining areas. In delineating the scope of the mining areas, if the ground projection or surface subsidence areas overlap with the scope of the established prospecting and mining rights, or has exerted other influences, the mining registration authority shall not affect the existing prospecting right holders when approving the scope of the mining areas. The applicant for the mining right shall reach an agreement with the existing prospecting right holder or mining right holder on aspects that may have an impact on prospecting or mining rights. If the prospecting right owner or the mining right owner agrees to the mining, the mining registration authority may delineate the scope of the mining areas; if the prospecting right holder or the mining right holder believes that there is influence and sufficient evidences are produced, the mining registration authority may set for a technical justification. If the result of the technical justification indicates the existence of certain impacts and no technical handling can result, the scope of the mining areas are not to be delineated."

However, none of the above provisions definitely prohibits the dipartite mining rights or overlapping mining rights, nor does it regulate that mining rights for "overlapping vertical projection" must be revoked, instead, the "vertical projection overlap" of mining rights can be regulated in terms of state intervention and private autonomy. If we are to examine the symbiosis and the concomitance processes of mineral resources, and different types of mineral resources in different vertical stratification, and if we simply emphasize that mining rights already existed in the same mining areas without considering the formation of mineral resources, and such other factors as geological conditions, differences in mining process, different mining intentions for different mining right holders, mining capacity and mining technology, and development rules of mineral deposits, etc., believing that other mining rights in the overlapping vertical projections shall not be set, or all the established overlapping mining rights shall be revoked, then all these will be unconducive to the promotion of comprehensive conservation and efficient recycling of limited mineral resources, and will be unconducive to the protection of property rights over the mineral resources. In practice, there are many ways to resolve the overlap, including the integration of different mining right entities into one same mining rights entity, adjusting and narrowing the scope of mining licenses to resolve the overlapping issues, establishing mining coordination mechanisms among different mining right entities, and developing timing and concluding cooperative agreement under the premises of safe production, canceling the mining license for one party and compensating losses, etc. Accordingly, in the case where the mining rights are different and the mining rights overlap, the ways to settle disputes are multiple and can be comprehensively applied. The revocation of overlapping mining licenses is only one of them, and the respondent's reconsideration decision is not comprehensively considered. In the case of specific factors, the mere revocation of overlapping mining licenses runs counter to the legislative intent.

2. Determining the Legitimacy and Effectiveness of Extending the Administrative License

The determination of the legitimacy and effectiveness of extending the administrative license involves whether the review over the legality of the prior administrative license must be extended to the judging of legality of the subsequent administrative license, and whether the illegality of the prior administrative license is necessarily extended to the subsequent administrative license, which revokes the effectiveness of the administrative actions.

The theory of presumptive rightfulness about the administrative action asserts that a specific subject has a legal obligation to comply with administrative actions, and if this compliance obligation is substantiated, that can be manifested in the definiteness or determinacy of the administrative action and the effectiveness or validity of the constituent elements.[2] According to the principles manifesting the theory of presumptive rightfulness about the administrative actions, the relative person cannot

[2]Zhang [2].

dispute the administrative action (formal rightfulness) after a certain period of time, and the administrative agency cannot revoke or abolish the administrative action after the administrative action took effect (substantive rightfulness); the effectiveness or validity of the constituent elements pinpoints this restriction to other agencies and courts. However, the theory of illegality succession of administrative actions believes that in the revocation proceedings of subsequent actions, although the subsequent behavior itself contains no inherent flaws, it can revoke the subsequent administrative actions by claiming that the prior administrative action is illegal.[3] "The subsequent administrative actions shall be the constituent elements of the prior administrative actions, and the judgment of the same or related issues cannot be contrary to the previous administrative actions. If the previous administrative action is illegal, the illegality will inevitably be succeeded by the subsequent administrative action."[4]

The essence of the conflict between the theory of presumptive rightfulness and the theory of illegality succession is the value conflict between substantive justice and stability (*Rechtssicherheit*). Some commentators have pointed out that the theory of presumptive rightfulness in the early stages denied the illegality succession of administrative behavior in principle, but only recognized the succession of administrative illegality from the perspective of the effect relationship between the behavior and the purpose of redress. The latest development focuses upon the procedural perspectives. The requirements of the protection of rights and the requirements of legal stability have broken through the existing theoretical model of "principle-exception".[5]

As regards the issue of determining the legitimacy and effectiveness of extending the administrative license, the judgment of this present case, on the one hand, acknowledges that when reviewing the 2011 mining license applied for administrative reconsideration, the 2006 mining license shall also be included in the scope of review, believing that as administrative license by Hunan Provincial Department of Land and Resources in 2011 was the succession and continuation of the administrative license of the Chenzhou Municipal Bureau of Land and Resources in 2006, the review on the legality of the 2011 administrative license will inevitably involve evaluating the legality of the administrative license issued in 2006, or even evaluating the validity and efficacy of establishment of mining rights, as such other actions as auction or transfer or assignment in 2006. On the other hand, it limits the scope of illegality succession. It is considered that the review of the legality of administrative licenses in 2006 and the review of the legality of administrative licenses in 2011 shall be different. Only when there are gross and apparent violations of law or the violations of law are impossible to correct, can the administrative licenses in 2006 affect the legality of the administrative license in 2011, rather than the illegality of the prior administrative action succeeded by the subsequent administrative actions. In case the license period of an administrative license expires, the license-issuing authority shall not only consider the legality of the original license, and also consider the impact of changes in the legal norms on whether to extend, and whether

[3] Zhu [3].

[4] Zhao [4].

[5] Wang [5].

the license can be extended out of the need for public interest. Thus it can be seen that even if there is illegality in the prior administrative license, the administrative agency shall consider such objective factors as the public interest and the change of circumstances when deciding not to extend, and cannot simply refuse to extend the administrative license because of the illegality.

It is generally believed that the theory of presumptive rightfulness for an administrative action is to occur during the duration of the administrative action, but in the case of the binding effect of the previous administrative license on the subsequent administrative license, it mainly involves whether the administrative agency will choose to continue or extend or whether evaluation of the legality of the subsequent administrative licenses contains the evaluation of the legality of the previous administrative license. Thus, when an administrative agency makes the initial license, the licensing authority may not issue the license even for the licensing which falls within the permitted scope of discretion recognized by the law, but the discretion and judgment of the extension of the license shall be subject to the first license. Even if defect(s) or infraction(s) may be detected in the first license, the licensing authority shall still prudently exercise its power of non-extension or non-continuation, for the reason that the reliance interests of the administrative counterparts can be protected. When the administrative reconsideration agency or the people's court examines the discretionary power of the licensing authority, it shall show due respect to the licensing authority who has set restriction or limit to its discretionary powers. In the case at hand, though the administrative action (licensing) made by Chenzhou Municipal Bureau of Land and Resources in 2006 on its own behalf or in its own name violated the state's regulations that require the provincial Land and Resources department(s) to approve the licensing or not to authorize the licensing, Fanlongdui Mining Co. Ltd. shall not be held liable for the Hunan Provincial Department of Land and Resources authorizing the issuance of the permit to the city-level land and resources departments. Fanlongdui Mining Co. Ltd. has acquired the mining rights by way of formalizing such required legal procedures as mining and public listing and auction, concluding assignment contracts of mining rights, paying mining right expenses, and handling relevant administrative licensing procedures. Thus the legal mineral rights and interests shall be protected by law. After the 2006 Mining License issued by the Chenzhou Municipal Bureau of Land and Resources expired in 2011, the approval authorizing authority for the extension permit has been changed from Chenzhou Municipal Bureau of Land and Resources to Hunan Provincial Bureau of Land and Resources, and Hunan Provincial Bureau of Land and Resources reissued the 2011 mining license in its own name. Therefore, although there was an ultra vires case in the licensing action in 2006, the defect has been remedied by the 2011 licensing action by Hunan Provincial Bureau of Land and Resources, which may not constitute an illegality succession issue. This also shows that the legal stability (*Rechtssicherheit*) can limit the application of the administrative illegality succession, and can be realized at the technical level through the curing defect theory.

3. Limiting the Power of Revocation by an Administrative Agency by the Principle of Reliance Protection

It is generally believed that the revocation of an administrative action is subject to the principle of the legal stability (*Rechtssicherheit*), which signifies that the continuity of the state's public power, norms and institution (stability) may not be necessarily directed towards the protection of the individual rights and interests of citizens, sometimes, this stability itself may even be unfavorable to citizens. But different from the principle of the legal stability (*Rechtssicherheit*), the principle of protecting the reliance means that an administrative agency may not revoke or alter an administrative decision that has already taken effect without providing justifiable legal reasons or without going through legal procedures; if any necessity out of state interest, public interests or other legal reasons entails making revocation or alteration of an administrative decision, it shall be carried out in accordance with the statutory authority and procedures, and the property damage suffered by the administrative counterpart shall be compensated.[6] The essential significance of the reliance protection is to substantiate the individual rights and interests by resort to the reliance on protecting the right of claims, which is also the subjectivized legal stability (*Rechtssicherheit*).[7]

The application of the principle of reliance protection in the field of administrative license is to protect the licensee's reliance interest on the administrative action by way of administrative license, and limits must be set upon the withdrawal, modification or revocation of such administrative action.[8] In principle, the administrative agency may not revoke or abolish a legitimate administrative licensing action, because it meets the requirements of the principle of law-based administration of government, unless the administrative license is no longer lawful due to changes in facts or law. Regarding the unlawful administrative license, we can subdivide it into continuity protection and property protection. In the former case, if the administrative license "is basically only an economic burden for the public authority, not a duty that should be performed within the scope of the responsibilities", and if the beneficiary has already relied upon the administrative license, and the said beneficiary has made certain dispositions on the basis of the administrative license, the reliance interest is worth protecting against the public interest, then the continuity protection can be applied to the existing administrative license. Upon this moment, the public interest and the private interest are weighed on an equal footing. As long as the private interest is worth protecting against the public interest, the administrative decision cannot be revoked even if it is unlawful. In the latter case, for other administrative license that may bring about property benefits to the administrative counterparts, but may not engender any economic burden for the administrative agency or agencies, the administrative license

[6] Hu [6].
[7] Liu [7].
[8] Zhou [8].

may be revoked by the administrative agency on the prerequisite that the loss suffered by the administrative counterpart shall be adequately compensated.[9]

In addition to the belief that the principle of reliance protection applies to the administrative agency that originally made the administrative action, the judgment of the present case is also explicitly extended to the administrative reconsideration agency. It is considered by this court that the administrative reconsideration agency is also subject to the limitation of the principle of reliance protection when making a revocation decision in the reconsideration procedure, should weight the promotion of public interest against the damage incurred to the private interests. The judgment specifically pointed out that "basic requirement of the rule of law entails law-based administration of government and correction of mistakes made by the administrative agencies, but the rule of law does not rigidly or unexceptionally require the revocation of an administrative action that have existed, contained some defects or contained some violations. Different cases have to be handled differently under different circumstances or situations. The issuance of mining licenses is a typical benefit-granting administrative action. The revocation of mining licenses must take into account the licensee's reliance interest, the loss of interest to the state, others and mining right holders. If there is a necessity to revoke the mining license, principle of proportionality shall be taken into account to weigh the relationship between the full revocation and the partial revocation. The administrative reconsideration agency may make such administrative reconsideration decision as revocation, alteration or confirmation of illegality of an administrative action, but the administrative reconsideration agency shall prudently make a determination of the decision types, should weigh such relevant factors as the degree of damage to the legal order, the loss or damage to the legitimate rights and interests of the right holder and the cost or the expenses incurred from taking other remedial measures; if the revocation does not conform to the public interest, it may decide not to revoke and choose to make a confirmation of illegality decision or other reconsideration opinions; if necessity entails making a revocation decision, an administrative agency shall specify the loss or damage caused to the licensee as well as the type of compensation or the extent of compensation. Only in this way, can an administrative revocation decision be valid."

4. The Procedural Control of the Administrative Agency to Revoke the Benefit-granting Administrative Action

Three modes for controlling executive power are generally recognized, namely command control, guidance control and competition control. Command control through rules can be important to suppress or cancel the unnecessary discretion; guidance control through principles not only defines the operational standards for the administrative agency, but also retains some space to make choices; competition control through processes or procedures is intended to establish a "public-private" competitive structure, under which a counterpart of an administrative act guided by procedural rules, challenges the administrative discretion and breaks away from the

[9] Liu [7].

monopoly of knowledge, information and discourse by the administrative agency.[10] In the face of diversified social realities, especially for decision-making in some technical or professional fields, the executive authorities often enjoy full discretion, and this discretion is to be generally respected in a judicial review. Only when the judgment discretion is obviously inappropriate, will the judiciary exercise its power to revoke the administrative decision. The competition control mode through processes or procedures may be considered an effective "weapon" for judicial intervention in administrative discretion and a challenge against the administrative decision-making.

Different from the procedural control through the rules of administrative procedures, the justifications provided by the administrative agency for making obligatory or benefit-granting actions have become increasingly refined and more technical. Justifications supplied by the administrative agency for making an administrative action that may have adverse effect upon the legitimate rights and duties of the counterpart, require the agency to explain to the him such factors as facts, legal basis as well as policy or the public interest which have been considered in exercising discretionary powers.[11] "The blueprint for administrative action is the judgment of the court."[12] As any judgment must pronounce who is the losing party, it is necessary to fully explain or justify the factual and legal bases of the judgment. Similarly, the revocation of a benefit-granting administrative action, which means loss or damage to the rights and interests of the counterpart, shall also be fully justified.

The judgment in the present case clearly indicates that justifications for making administrative action may be used as the procedural control for the administrative reconsideration authority to exercise the power of revocation, any failure to provide the justifications for an administrative action is to be regarded as one of the rash decisions, which further lays foundation for judicial review in exercising the power of revocation. The judgment pointed out that "in exercising the discretionary power, the administrative agency shall specify the reasons for making an administrative decision. The people's court shall give due and full respect to the judgment, discretion, decision and reasons made by the administrative reconsideration agency, for a reconsideration decision resembles a ruling in the manner of an interim quasi-judicial power, which has also inherited the exercise of professional judgment power by the higher-level administrative agency. Likewise, reasons or justifications for an administrative reconsideration decision should be supplied to indicate that the reconsideration agency has thoroughly and objectively ascertained the facts and comprehensively measured all the factors related to the case rather than making decisions rashly or arbitrarily. Only by means of written decisions and the reasons or justifications stated in the dossier, can the people's court know of the relevant or irrelevant factors considered by the administrative agency in order to effectively review and evaluate the legitimacy of the administrative decision. If a decision contains no reasons or justifications for the discretionary process and the final decision, it can neither convince the counterpart of the administrative action nor effectively control the administrative discretion, it

[10] Wang [9]

[11] Zhang [10].

[12] Meyer [11].

can also bring obstacles for subsequent judicial review." The case at hand involves multiple solutions to the handling of the overlapping mining rights and various conclusions which may be rendered by the reconsideration agency, but Ministry of Land and Resources chose to revoke the administrative decision simply by the occurrence of the overlapping, without taking into account various factors involved in the decision-making from all the evidences and the complete set of the case dossiers, and this can be hardly supported by the people's court. The people's court held that, unless the evidences provided by the reconsideration agency can meet the requirements for judicial review, and have fully justified its decision to make a revocation, the administrative reconsideration agency is ordered to make de novo investigation and provide relevant, basis for judicial review and adequately justify the reasons for making an administrative decision.

5. Conclusion

An irreconcilable contradiction between regulation and autonomy persists in modern society, and the same case can be found in handling the mining rights, "which are a complex bundle of rights".[13] In the exercise of the power of revoking a mining license, in addition to considering the public interest, such other factors have to be taken into account, i.e. mining right acquired by the counterpart of an administrative act through the extension of the mining license, the proportional relationship between the enhancement of public interest and the diminution of rights of the private mining entity, so as to prevent the private entity from fully bearing the cost of public interest enhancement, whereby any contradiction(s) between regulation and autonomy may be eliminated, and justice may be achieved to the greatest extent possible in the particular case.

Bernard Schwartz once stated, administrative discretion is the core of administrative power. If administrative law is not a law that controls administrative discretion, then it is nothing.[14] So, the administrative discretion manifests not only a color of the rule by the people, but also appears indispensable. Without the involvement of the administrative discretion, the rules (of laws and regulations) themselves cannot cope with the complexity of modern administration. However, if the discretion is arbitrary, it is undoubtedly the contempt and arrogance of the rule of law.

The resolution of the case at hand can be said to respond to some theoretical issues as to how the administrative discretionary powers can be exercised in re-cancelling the revocation of a administrative reconsideration decision. With regard to the theory of presumptive rightfulness about an administrative action, the judgment of the case at hand affirms that an administrative agency possesses the first judgment and discretionary power to decide on a specific administrative matter, and there exist some restraints this prior judgement or discretionary power has over the subsequent administrative actions made by the said or other administrative agencies, also asserts that this survivability can be extended to the administrative reconsideration and judicial review processes. As for the theory of illegality succession of an administrative

[13] Jiang [1].

[14] Schwartz [12].

action, the present judgment recognizes the necessity of the adjudicating agency's power to review the legality of the previous administrative action under appropriate circumstances, and the coupling of trial practice with the illegality succession theory within the "minimum" of the invalidity of an administrative action. In terms of the principle of reliance interests, the present judgment clearly delineates that proportionality of administrative actions can be a technical tool to determine the violation of the principles of reliance interests. Furthermore, the present judgment has also elaborated on a diversified administrative reconsideration system to differ from the traditional mono-dimensional review of the administrative reconsideration system. The present judgment holds that the administrative reconsideration itself is an administrative action,[15] which entails that the reconsideration agency shall moderately reflect the principle of "correcting every wrong" when making an administrative reconsideration decision to reinforce the internal hierarchical supervision; an administrative reconsideration resembles an interim judgement by a judicial organ, that is, when exercising the power to revoke an administrative decision, this agency shall, like a judicial organ, supply sufficient reasons or grounds for making its decision to revoke an administrative action, so that relevant rights can be fully remedied and disputes successfully resolved. This can also be seen as a response of the trial departments in the Supreme People's Court to the amendment of the *Administrative Reconsideration Law*.

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Michael Jeffrey Jordan v. Trademark Review and Adjudication Board of the State Administration for Industry and Commerce of the People's Republic of China & Jordan Sports Co., Ltd. (Administrative Disputes over Trademark)—Right to One's Name May Constitute "Prior Right" Protected by Trademark Law

Kaiyuan Tao, Chuang Wang, Junli Xia, Yanfang Wang and Weike Du

Rule[1]

The right to one's name is an important personal right of a natural person to his or her name, and the right to one's name may constitute the "prior right" provided for in Article 31 of the *Trademark Law* amended in 2001.

[1]On December 8, 2016, the Supreme People's Court pronounced its judgements on 10 administrative dispute cases on trademark among the retrial applicant (Michael Jeffrey Jordan), respondant (Trademark Review and Adjudication Board of the State Administration for Industry and Commerce of the People's Republic of China), and the third party (Jordan Sports Co., Ltd.). Regarding the Supreme People's Court judgments numbered No. 15 [2016], No. 26 [2016], No. 27 [2016], Retrial, Adm. Division, SPC, involving "Jordan" trademark, the registration of the disputed trademark prejudiced the retrial applicant's prior right (right to name). This is not in conformity with Article 31 of the *Trademark Law* (Rev. 2001), which provides that, "application for trademark registration shall not prejudice the existing prior rights of others". The registration shall therefore be revoked. Hence, the Supreme People's Court held that, the respondant's ruling made by the Trademark Review and Adjudication Board shall be revoked, and ordered the Trademark Review and Adjudication Board to make a newer ruling on the disputed trademark. The Comment on Rule of this case is illustrated by the example of the Supreme People's Court's judgment numbered No. 27 [2016], Retrial, Adm. Division, SPC.

The retrial collegial panel: Tao Kaiyuan, Wang Chuang, Xia Junli, Wang Yanfang, Du Weike (Translated by: Zheng Daxuan; Proofread by: Zhang Hongsheng).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_2

"Use" is one of the rights of the right holder, and it is neither the obligation undertaken by the holder nor a statutory prerequisite for the name holder to claim the right to protect his name. Subject to the conditions for the protection of the right to name, the natural person has the right to obtain the protection of the name in accordance with the provisions of Article 31 of the *Trademark Law* amended in 2001.

If a natural person claims for the protection of a name on a specific name, the following three conditions shall be met: first, the specific name enjoys a certain popularity in China and is known to the general public; second, the relevant public uses the specific name to refer to the natural person; third, a stable correspondence has been established between the specific name and the natural person. If the Chinese translation of the foreigner's name meets the above three conditions, his right to the name may be protected according to law.

The market order or commercial success claimed by the trademark owner is not entirely a result of good faith, but is based on a certain degree of misunderstanding of the general public. Maintaining such market order or commercial success is not only unconducive to protecting the legitimate rights and interests of the name right holder, but detrimental to protecting the interests of consumers, and nor is it conducive to the sound environment or atmosphere for the trademark registration and use.

Case Information

1. **Parties**

Retrial applicant (Plaintiff in the first instance, Appellant in the second instance): Michael Jeffrey Jordan (hereinafter referred to as "Jordan")
Retrial respondent (Defendant in the first instance, Appellee in the second instance): Trademark Review and Adjudication Board of the State Administration for Industry and Commerce of the People's Republic of China (hereinafter referred to as "Trademark Review and Adjudication Board")
The third party: Jordan Sports Co., Ltd. (hereinafter referred to as "Jordan Sports Company")

2. **Procedural History**

First Instance: No. 9163 [2014], Trial, IP/Adm. Division, the Intermediate People's Court of Beijing City (dated Apr. 1 of 2015)
Second Instance: No. 1915 [2015], Final, IP/Adm. Division, the Higher People's Court of Beijing City (dated Aug. 17 of 2015)
Retrial: No. 27 [2016], Retrial, Adm. Division, the Supreme People's Court (dated Dec. 8 of 2016)

3. **Cause of Action**

Administrative dispute over trademark

Essential Facts

In the serial trademark dispute cases involving the applicant (Jordan), the respondent (Trademark Review and Adjudication Board), and the third party of the first instance Jordan Sports Company (hereinafter referred to as "Jordan" trademark dispute case), No. 6020569 "Jordan" trademark (hereinafter referred to as the disputed trademark) was a trademark applied for by Jordan Sports Company on April 26, 2007, to be approved for use on the commodities in "Sports Equipment, Swimming Pool (Entertainment only), Roller Skates, Christmas Tree Decorations (except Lighting and Candy)" according to the Directory of International Classification. The exclusive right period lasts from March 28, 2012 to March 27, 2022. On October 31, 2012, Jordan applied for cancellation of the disputed trademark on the grounds that its registration damaged his prior rights. On April 14, 2014, the Trademark Review and Adjudication Board (TRAB) issued a decision titled "No. 6020569 'Jordan' Trademark Dispute Determination" (hereinafter referred to as Business Review [2014] No. 052058 Decision), affirmed the registration of the disputed trademark. Jordan refused to accept and filed an administrative lawsuit.

After the trial of first instance, the First Intermediate People's Court of Beijing held that there is no sufficient evidence in this case to prove that the separate "Jordan" trademark clearly pointed to Jordan. In addition, the goods or commodities with the disputed trademarks are different from the basketball profession where Jordan enjoys greater influence. It is not easy for the general public to link the disputed trademarks with Jordan. The evidences in this case are insufficient to prove that the registration and use of the disputed trademarks had made improper use of Jordan's popularity or have exerted other effects on Jordan's right to his name. The registration of the disputed trademark did not prejudice Jordan's right of name. The court of first instance affirmed the No. 052058 Decision. Jordan refused to accept the judgment of the first instance and filed an appeal. After the trial of second instance, Beijing Higher People's Court dismissed the appeal and upheld the original judgment. Jordan still refused to accept the judgment of first and second instances and filed an application for retrial with the Supreme People's Court, and the Supreme People's Court brought the cases by way of certiorari.

Issues

The core issue whether the registration of the disputed trademark infringes upon the right of name "Jordan" claimed by the retrial petitioner, and is against the provisions of Article 31 of the *Trademark Law* regarding "no application for trademark registration may infringe upon the existing prior rights of others". It is subdivided into the following eight specific issues:

1. What is the legal basis for the retrial applicant to claim protection of the right to name;
2. What is the specific content protected by the right to name claimed by the applicant;
3. To what extent and in what scope does the applicant have the popularity in China;
4. Whether the applicant and its authorized Nike company voluntarily use the trademark "Jordan", and to what extent has voluntarily use has affected the right to name claimed by the applicant in the case;
5. Whether the specific circumstances of the disputed trademark will cause the relevant public to misunderstand that it is related to the applicant;
6. Whether Jordan Sports Company has actual subjective malice for the registration of the disputed trademarks;
7. What effect does the business operation status of Jordan Sports Company, its enterprise name, the promotion of business, the use, prize-winning and the protection of the trademark have in this case;
8. Whether the applicant is slack to protect the claimed right to his name and what effect this negligence will have in the case.

Holding

After bring the case by way of certiorari, the Supreme People's Court made a judgment, numbered No. 27 [2016], Retrial, Adm. Division, the Supreme People's Court, on December 8, 2016, "the ruling made by the Trademark Review and Adjudication Board and the original judgments of the courts of the first and second instances shall be revoked, and the Trademark Review and Adjudication Board is ordered to make a ruling anew over the disputed trademark."

The Supreme People's Court holds that:

1. **The legal basis for retrial applicants to claim the right to his name.**

Article 31 of the *Trademark Law* provides that "application for trademark registration shall not prejudice the existing prior rights of others." Prior rights that have been specifically provided for in the Trademark Law shall be protected in accordance with the special provisions of the Trademark Law. For the civil rights and interests for which there is no special provision in the *Trademark Law*, but it shall be protected in accordance with the provisions of the *General Principles of Civil Law*, the *Tort Liability Law* and other laws, and such civil rights or interests that have been enjoyed by civil subjects before the date of filing of the disputed trademark, shall be protected in accordance with this general rule. Article 99(1) of the *General Principles of the Civil Law* and Article 2(2) of the *Tort Liability Law* explicitly provide that natural persons have the right to name according to law. Therefore, the right to one's name may constitute the "prior right" as regulated in Article 31 of the *Trademark Law*. Where the registration of a disputed trademark prejudices the prior right to of others, it shall be deemed that the registration of the disputed trademark violates the provisions of Article 31 of the Trademark Law.

Names are used to refer to, designate, and distinguish between specific natural persons. Right to name is important personal right of natural persons to his name. With the continuous development of China's socialist market economy, it is increasingly common for natural persons with certain popularity in China to commercialize their names and endorse specific goods and services through contracts and other means for economic benefits. When the provisions of Article 31 of the *Trademark Law* are applied to protect the right to name of another person, it not only protects the personal dignity of the natural person, but also protects the economic interests embodied in the name of that natural person, especially the name of a famous person. If the name of the person who has the prior right is registered as a trademark without permission, it is easy for the general public to mistakenly believe that the goods or services marked with the trademark have specific relations with the natural person, such as endorsement, permission, etc., and thus the registration of trademark containing the name shall be deemed to a violation of one's prior right (right to name), specifically, a violation of the provisions of Article 31 of the *Trademark Law*.

2. **The specific content protected by the right to name claimed by the applicant.**

Natural persons shall satisfy the necessary conditions when claiming the protection of the right to a particular name in accordance with the provisions of Article 31 of the *Trademark Law*.

In the first place, the specific name should enjoy a certain degree of popularity, be known to the general public, and be used to designate the said natural person. Article 6 (2) of the *Judicial Interpretation of Applicable Law to the Unfair Competition Cases* is a judicial interpretation of the determination of an unfair competition act, that is, "the use of the name of others without authorization, misleading the public to regard a commodity as one of another person", is also an infringement, in essence, upon the right to name of others. The expression "misleading the public to regard a commodity as one of another person" is closely related to whether the registration of the said disputed trademark in the present case is likely to cause the public to mistakenly believe that there is a specific connection such as endorsement or permission. Therefore, in this case, the conditions for the protection of the name of a natural person can be determined by applying mutatis mutandis the provisions of the above-mentioned judicial interpretation.

Secondly, the specific name should have established a stable or continual correspondence with the natural person. In resolving the conflict of rights between the prior right to name and the registered trademark right in this case, the protection standard of the prior right to name should be reasonably determined to balance the interests of the prior name holder and the trademark owner. We cannot simply determine that the registration of the disputed trademark may prejudice the right to name of a natural person only because the name that is just famous among certain part of the public is or temporarily used by the natural person is contained or used in the disputed trademark . Nor can we raise harsh standard for the protection of one right to his name, as it is claimed by the Trademark Review and Adjudication Board that a "name" advocated by the natural person forms a "unique" correspondence with the natural person. When a specific name advocated by a natural person has established a

stable and continual correspondence with the natural person, even if the corresponding relationship does not reach the "uniqueness" standard, the right to his name can be protected according to law. In sum, in applying the provisions of Article 31 of the *Trademark Law* regarding the "shall not prejudice to the existing prior rights of others", if the natural person claims the protection of the right to a specific name, the following three conditions shall be met: first, the specific name enjoys a certain popularity in China and is known to the general public; second, the relevant public uses the specific name to refer to the natural person; third, a stable correspondence has been established between the specific name and the natural person.

When judging whether a foreigner can claim the right to part of translated Chinese translation of his or her foreign language name, it is necessary to take into account how we Chinese customarily address a foreigner. If the Chinese translation meets the above three conditions, the protection of the right to name may be claimed in accordance with the law. The existing evidence in this case is sufficient to prove that "Jordan" has a high reputation in China and is known to the relevant public. The relevant public in China usually refers to "乔丹" as the applicant, and "Jordan" has formed a stable and continual relationship with the applicant. So the retrial applicant has the right to the name "Jordan".

3. **Regarding the extent and the scope of the applicant's popularity in China.**

A correct determination of the extent and scope of the applicant's popularity in China matters a great deal to determine whether the applicant can have the right to the name "Jordan", whether there is actual subjective malice on the behalf of Jordan Sports Company in registering the disputed trademarks, and whether the relevant public will mistakenly believe that the goods marked with the disputed trademark have certain relations with the applicant.

The evidences in this case can ascertain, before the filing date of the disputed trademark, even until 2015, the applicant has always had a high degree of reputation in China, and the scope of his fame or reputation is not only limited to the basketball field, but has become a public figure enjoying a high reputation.

4. **Whether the applicant and its authorized Nike company voluntarily use "Jordan", and to what extent has the use has affected the right to name claimed by the applicant in the case.**

First of all, according to the provisions of Article 99(1) of the *General Principles of the Civil Law*, "Use" is one of the rights of the right holders, and it is neither the obligation undertaken by the holder nor a statutory prerequisite for the holder of a name to "prohibit others from interfering, embezzling or counterfeiting" the name in claiming the protection of their rights to names.

Secondly, when the provisions of Article 31 of the *Trademark Law* are applied to protect the prior rights of another person, such important factor as whether it is easy for the public to mistakenly believe that the goods or services marked with the disputed trademark have specific links with the natural person, such as endorsement, permission, etc., have to be taken into account in determining whether the trademark

registration prejudices a natural person's right to name. Therefore, in the case of satisfying the above-mentioned three conditions concerning the protection of the right to name, the natural person has the right to obtain the protection of the right to his name in accordance with the provisions of Article 31 of the *Trademark Law* even if a specific name has not been voluntarily used.

Finally, for foreigners who have a certain popularity in China, they themselves or the interested parties may have not voluntarily used their names in China; or because of the convenience of expressing the names, language habits, or cultural differences, the names with which the general public and news media in China are familiar, are different from the names they themselves would voluntarily use. For example, in this case, the public and news media in China will generally refer to the applicants as "Jordan", while the applicant himself or Nike Company will chiefly use "Michael Jordan". However, whether it is "Michael Jordan" or "Jordan", it has a high reputation among the public, and is generally used by the public to refer to that name as the applicant in the retrial, and the applicant himself has not raised any motions or objections. Therefore, the opinion raised by Trademark Review and Adjudication Board and Jordan Sports Company that the applicant is not entitled to the protection of his right to name because the Applicant or Jordan Sports Company has not voluntarily used "Jordan" shall not be supported by this court.

5. **Whether the specific circumstances of the disputed trademark will cause the relevant public to misunderstand that it is related to the applicant.**

The disputed trademark in this case is the "Jordan" trademark No. 6020569, and the designated commodity category is category 28 including "sports equipment, swimming pool (entertainment only), roller skates, and Christmas tree decorations (except lighting and candy)". Among them, "sports equipment, swimming pool (entertainment), roller skates" are common commodities in sports, and "Christmas tree decorations (except lighting and candy)" are common commodities in daily life. The relevant public of the above-mentioned goods is likely to mistakenly believe that the goods marked with the disputed trademark have specific contacts such as endorsement and permission. The specific reasons are listed as follows: Firstly, the evidences in this case are sufficient to prove that the applicant for retrial and its name "Jordan" have long-term and extensive popularity in China, and the relevant public is familiar with "Jordan" and they generally use "Jordan" to designate the applicant in this retrial. A stable and steady relation has been established between "Jordan" and the applicant. Since the disputed trademark mark is only the word "Jordan", it is easy for the relevant public to associate the disputed trademark with the Applicant, then believe that the product or commodity marked with the disputed trademark is specifically endorsed, or licensed by the applicant. Secondly, Jordan Sports Company specifically stated in the "Brand Risk" of the "Prospectus", "Specially reminding investors that there may be some consumers who associate the issuer and its products with Michael Jordan to bring about misunderstanding or confusion. Investors are advised to pay special attention." This indicates that the Company has recognized that the public is likely to associate "Jordan" with the Applicant, which may lead to misunderstanding. Jordan Sports Company also recognized in the transcript of

the trial in the first instance that "there will be a possibility that the public who has not purchased our goods will have developed this association". Finally, two survey reports can be combined with other evidences to prove further that the public is likely to mistakenly believe that "乔丹" has a specific relationship with the Applicant. In addition, two survey reports can further corroborate with other evidences that the public will designate the name "乔丹" as the applicants and "乔丹" has established a stable and steady relation with the applicant. On the one hand, the facts and laws of the case at hand are closely related to the cognitive status of the public. Therefore, objective, fair, standardized and transparent market investigations can help the people's courts to further ascertain the public knowledge about "Jordan". According to the facts ascertained, two survey reports submitted by the Applicants were completed by the Horizon Research Consultancy Group. The investigation activities were carried out in Beijing, Shanghai, Guangzhou, Chengdu and Changshu respectively to obtain the general knowledge of the relationship between the Applicant and Jordan Sports Company. The survey process was notarized by the notary public in Beijing Chang'an Notary Office and Shanghai Oriental Notary Office. Detailed descriptions have been made about the composition of the respondents, the way of access, the sampling method, and the formation of the survey conclusions. Attached with two survey reports are detailed "Technical Description", "Questionnaires" and Question Cards. Therefore, the authenticity and weight of the survey conclusions are relatively high, and can be used concurrently with other evidences at hand to prove the existence of relevant facts. Although the Trademark Review and Adjudication Board and Jordan Sports Company questioned the two survey reports, they have neither provided sufficient counter-evidences, nor have they raised reasonable objections, the court refused their clams. On the other hand, the survey data displayed by the two survey reports corroborates with other relevant facts in the case. It can be proved that the general public in China usually refer to "乔丹" as the applicant, and "乔丹" has established a stable correspondence with the applicant in this retrial.

6. **Whether Jordan Sports Company has actual subjective malice for the registration of disputed trademarks.**

In this case, whether Jordan Sports Company applied for registration of the disputed trademark out of actual subjective malice is an important factor for determining whether the registration of the disputed trademark impairs the right to name. The evidences in this case are clear and sufficient to prove that Jordan Sports Company has not negotiated with the applicant to obtain his permission or authorization, but arbitrarily registered a large number of trademarks (including the disputed trademark "Jordan") closely related to the applicant, let the public believe that the products marked with the disputed trademarks have specific links with the applicant, so that Jordan Sports Company can achieve the goal of "Jordan Speaks for the Company" without incurring any excessive cost. Such conduct by Jordan Sports Company violates the good faith principle provided in Article 4 of the *General Principles of Civil Law*, and the obvious subjective malice for the registration of disputed trademarks can be determined without any doubt.

Firstly, from 1984 to 2015, the applicant has a considerable long-term and extensive visibility or popularity in China. The general public in China mainly designates "乔丹" as the applicant. Jordan Sports Company was previously known as the "Second Chenjianxibian Daily Necessities Factory in Jinjiang City of Fujian Province", which has nothing at all to be associated with "Jordan", but it was renamed "Jinjiang Jordan Sports Goods Co., Ltd." in June 2000, and in September 2000 it was renamed "Fujian Jordan Sports Goods Co., Ltd.", and renamed to the current name in December 2009. Jordan Sports Company is mainly engaged in the design, production and sales of sports shoes, sportswear and sports accessories. Its business is highly correlated with the career of the applicant, they must have developed a considerable understanding of the applicant and his popularity. As a matter of fact, Jordan Sports Company also explicitly admitted that it has registered the disputed trademark in the case of "knowing the visibility or popularity of him (the applicant)".

Secondly, as for the grounds for using "乔丹" to apply for the registration of disputed trademarks, Jordan Sports Company has made three different interpretations of "乔丹" in the court pre-trial hearings, the court sessions during the first-instance, and the court sessions in *M. Jordan v. Jordan Sports Company* by the Second Intermediate People's Court of Shanghai. But among these three *Interpretations*, whether "the grass and wood in the South", or "good meaning", "common meaning, good will", or "in the mid-1990s, when it was a village-owned enterprise, when they sought the assistance of the local trademark office to provide a name in Jinjiang, "乔丹" was included", it is obviously contrary to common sense or there is lack of factual basis, it is difficult to be convinced. Therefore, Jordan Sports Company cannot make a reasonable explanation for the use of "乔丹" to be registered as a trademark.

Finally, in addition to applying for the registration of disputed trademark, Jordan Sports Company and its affiliates have also applied for the registration of a series of other trademarks closely related to the Applicant, further highlighting their subjective malice. These trademarks include: (a) Jordan Sports Company has applied for the registration of several trademarks by using the names of the two children of the applicant, "Jeffrey Jordan, "Marcus Jordan, and the Chinese Pinyin. One of the its shareholding companies, Fujian Baiqun Company, a controlling shareholder outside the case, have applied for the registration of 16 trademarks attached with such names as "Jeffrey", "Marcus", "Jiefuli" and "Makusi" on the products. (b) By analogizing with the photos of the Applicant published in the 1998 US Basketball Catalogue (Chinese International Edition), Jordan Sports Company has applied for the registration of multiple trademarks by using the same graphics as the applicant's body contour as components alone or together, with "Jordan", "qiaodan", or the applicant's jersey number "23"; (c) Its affiliate company, Mike Corporation, by using the graphics in Nike's trademarks No. 643806 and No. 4932232, has separately applied for the registration of the combined trademark No. 1407911; (d) Targeting at NFL team "Lakers", Lakers Sports Company, Jordan Sports Company's affiliated company, has applied for the registration of "lakersteam" trademarks numbered 1905046, 1967177, 2009309, and, and the registration of the trademark "Lakeren hurendui" numbered 1905050, 1967878, 1961198, has the "湖人队" (Laker Team) used as the font size in its business name. In sum, the use of "Jordan" by Jordan Sports Company

to apply for the registration of trademarks is not an isolated or accidental event, but rather it has applied for the registration of the trademarks with "Jordan" attached to the products because they knowingly understand that the applicant has a higher visibility or popularity in China. So Jordan Sports Company is not entitled to the legal protection of the prior right to the name of "Jordan", or the jersey number "23", especially the names of the two children of M. Jordan. The opinions raised by Jordan Sports Company and the Trademark Review and Adjudication Board that the conduct of Jordan Sports Company falls within the continuous registration and defensive registration of the registered trademark shall not be upheld for lack of factual and legal basis.

7. **What effect does the business operation status of Jordan Sports Company, its business name, the promotion of business, the use, prize-winning and the protection of the trademark have on the adjudication of the present case?**

The business operations of Jordan Sports Company, its business name, the promotion of business, the use, prize-winning and the protection of the trademark are not sufficient to make the registration of disputed trademarks legal and legitimate.

Firstly, from the nature of the right and the elements of the damage to the prior right to a name, a name is used to designate, address, and distinguish a particular natural person. The right to name is the personal right of the natural person to their name. The role of a trademark is to distinguish the source of goods or services, belonging to property rights. When determining whether the registration of a disputed trademark prejudices the prior rights of another person, the key lies in whether it is easy for the relevant public to mistakenly believe that there is a specific connection between the goods or services marked with the disputed trademark and the name holder, such as endorsement, permission, etc.. So it is different from the confirmation of infringement upon trademarks for the elements. Therefore, even after years of operation, publicity and use, Jordan Sports Company has made Jordan Sports and its "Jordan" trademarks highly recognized in specific commodity categories, and the relevant public can recognize that the products marked with the "Jordan" trademark originate from Jordan Sports Company, it is insufficient to determine that the general public is not easy to mistakenly believe that there is a specific connection between Jordan and the goods marked with "Jordan" trademark.

Secondly, the malicious application by Jordan Sports Company for the registration of a disputed trademark, which has infringed upon the Jordan's prior right to the name, is obviously contrary to the good faith principle. The market order or commercial success claimed by the Trademark Review and Adjudication Board and Jordan Sports Company is not entirely a legitimate outcome of the good faith management of Jordan Sports Company, but is based on a considerable degree of the public misunderstandings. Maintaining such market order or commercial success is not only unconducive to protecting the legitimate rights and interests of the name holder, but is also detrimental to protecting the interests of consumers, and nor is it conducive to the sound environment or atmosphere for the trademark registration and use.

8. **Whether the applicant has failed to protect the claimed right to his name and what effect this negligence will have on the case.**

Article 41(2) of the *Trademark Law* provides, "a registered trademark, if in violation of Article 31 of this Law … within five years from the date of trademark registration, … may be revoked or withdrawn after the assessment of the Trademark Review and Adjudication Board." The provision of "within five years from the date of trademark registration" in the above is the prescribed time limit for applying to the Trademark Review and Adjudication Board for the cancellation of a disputed trademark. The legislator has fully considered the balance of interests between prior rights holder and trademark owner when prescribing the time limit. The time limit set in the law can urge the right holder or the interested party to claim rights in a timely manner, and avoid the controversy of the registered trademark over a long period of time, thereby affecting the publicity and the use of the disputed trademark by the trademark owner, undermining the legitimate rights and interests of the right holder. In the present case, the applicant filed an application for cancellation of the decision made by Trademark Review and Adjudication Board within five years from the date of registration of the disputed trademark, which is in compliance with the above-mentioned legal provisions. Therefore, the claims raised by the Trademark Review and Adjudication Board and Jordan Sports Company that the applicant is slack to protect the claimed right to name shall not be upheld for lack of factual and legal basis.

In sum, the "prior right" provided in Article 31 of the *Trademark Law* include the right of name that others have enjoyed before the date of filing the disputed trademark. The applicant has the prior right to name in the disputed trademark mark "Jordan". The fact that Jordan Sports Company knowingly understands that the Applicant has long-term and wide-ranging popularity in China, but it still uses "Jordan" to apply for the registration of the disputed trademark, which may easily mislead the public into believing that the goods marked with the disputed trademark have specific connections, such as endorsements or permissions, with the Applicant, has infringed upon the prior rights to the name of the applicant, and Jordan Sports Company has a clear subjective malice for the registration of disputed trademarks. The business operations of Jordan Sports Company, its business name, the promotion of business, the use, prize-winning and the protection of the trademark are not sufficient to make the registration of disputed trademarks legal and legitimate. Therefore, the registration of a disputed trademark violates the provisions of Article 31 of the Trademark Law and shall be revoked in accordance with the provisions of Article 41(2) of the *Trademark Law*. The Trademark Review and Adjudication Board is requested to make a newer ruling on the disputed trademark.

Comment on Rule

"Strict protection" and "balance of interests", two issues concerning the policies and values in the judiciary have always been important issues in the theory and practice of the intellectual property rights law in terms of balance of interest and value selection. The conflict of interest and balance between the prior right to a name of a name holder and the trademark right holder in the *Trademark Law* can be described as a typical representative of this value tradeoff.

As an important system in the Trademark Law of China amended in 2001, the protection of prior rights provided for in Article 31[2] reflects the respect and protection of prior rights in China's Trademark Law, but in the administrative practice of trademark authorization and the practice of judicial trial, there is a certain controversy as to how to identify the protected content and identification standard for the prior right to a name, whether the fact of active use has any influence on the protection of right to name, whether the clash between subjective malice of a trademark infringer and the negligence on the behalf of the rights holders can be set off, whether a foreigner can claim the right to his name being translated into Chinese language etc., which have to some extent affected the unity of the adjudication standards and scales.

The legal principles and legal standards established by the Supreme People's Court in the "Jordan" trademark disputes have important theoretical significance and trial guidance on how the people's courts weigh the strict protection and balance of interests, and how to determine the essentials for the protection of right to a name. It is of epoch-making significance to promote the good faith principle, maintain a fair market order, and purify the trademark registration and trademark use environment.

1. **The adjudication of the "Jordan" case has important significance for the application of relevant laws.**

The right to name is the basic personal right enjoyed by natural persons. There are no clear provisions in China's laws on the standards and conditions for the protection of prior rights to a name in the administrative cases concerning the grant or authorization and confirmation of trademarks, and no less controversy is to have been detected in judicial practice. The applicable standards of law set forth by the Supreme People's Court in the judgment of this case will have an important impact on the trial of such cases. By applying the provisions of Article 31 of the *Trademark Law*, the adjudication of the disputes in the case has granted the prior rights to a name of the applicant "Jordan", which has protected the personal dignity of the right holder, as well as the economic interests for the right holder, especially the name of the celebrity so that great significance has been manifested in maintaining a fair market order, and in purifying the environment and atmosphere of the trademark registration and use.

[2] Article 31 of the *Trademark Law* amended in 2001 provides that, "Trademark registration applications shall not harm existing prior rights of others, use of improper means to forestall registration of a trademark which is in use and has certain impact shall not be allowed". The said law was revised in 2013 for the third time, and it has made identical provisions in Article 32.

In the *Rules on Administrative Cases involving Granting or Affirming Trademark Rights* announced by the Supreme People's Court on January 11, 2017, the relevant rules in the judgment were fully absorbed. Four articles in *Rules on Administrative Cases involving Granting or Affirming Trademark Rights* have been used for the judicial interpretation of "trademark registration applications shall not harm existing prior rights of others", which have respectively covered the scope of prior rights,[3] prior rights to a name, prior copyrights, and prior rights to fonts.

Among them, Article 20 of *Rules on Administrative Cases involving Granting or Affirming Trademark Rights* provides for right to a name as follows, "in determining whether the disputed trademark impairs the right to one's name, if the relevant public believes that the mark is designated as the natural person, and if the public is easy to think that the commodity attached with the trademark is approved by the natural person or has a specific connection with the natural person, the people's court shall deem that the trademark is prejudiced against the natural person's name; if the party claims the right to his or her name with a specific name such as the pseudonym, stage name (or showbiz name or screen name), and translated name, the people's court will sustain the said right to name if the said specific name has won considerable popularity, has established a stable or steady relations with that natural person, or the public designates that name as the natural person." The above-mentioned provisions have, on the one hand, clarified the criteria for judging the damage to the prior rights to name, that is, "the public is easy to believe that the name has established a stable or steady relations with that natural person," On the other hand, the protected scope of the right to name is not limited to the original name, but has also ascertained the terms and conditions that the natural person should meet when claiming the right to a specific name, that is, "a specific name is considerably popular, it has established a stable and steady relations with the natural person or the public designates that name as the natural person."

2. **The judgment of the said disputed case can further promote fair justice and judicial openness.**

Justice is the lifeline of rule of law. It plays an importantly leading role in social justice. Compared with abstract legal provisions and judicial policies, the fair judgment of the case enables the public to be more aware of the judiciary, to understand the judiciary and respect the justice. The retrial judgments of the series of cases have fully reflected China's firm determination to protect the legitimate rights and interests of Chinese and foreign parties, strengthened the protection of intellectual property rights, and expressed firm attitude toward the intellectual property system. It has also reflected the firm conviction that laws and regulations must be enforced,

[3] Article 18 of *Rules on Administrative Cases involving Granting or Affirming Trademark Rights* provides, "the prior rights provided in Article 32 of the Trademark Law include the civil rights enjoyed by the parties before the filing date of the trademark application or other legal rights that should be protected. When the trademark is approved for registration, nonexistence of the prior right does not affect the registration of the disputed trademark".

orders obeyed and prohibitions checked in the context of comprehensively governing the country according to law or law-based governance.[4]

To promote fair justice, we must persist in promoting justice and public trust. In the course of hearing the series of cases, the Supreme People's Court conducted a public trial and a public judgment on the basis of the principle of "full media live broadcast and comprehensive interpretation", and the judgment was placed online on the China Judicial Documents Network shortly after the judgement was pronounced. During the public hearing of the case on the World Intellectual Property Day on April 26, 2016, China Court Network managed by the Supreme People's Court, the Supreme People's Court Official Weibo, and the Court Channel of Sina Network have conducted a live broadcast of the trial processes. The total number of viewers on the Sina Court Channel has exceeded 1.5 million.

In pronouncing the judgment on December 8, 2016, the Supreme People's Court conducted a full-media live broadcast of the pronouncement of the judgment through such new media network platforms as the China Open Court Network and the Sina Court Channel. According to some statistics, from December 8:00 to 14:00 o'clock of December the 14th, nearly 7001 online news reports, 380 newspaper articles, and 6514 microblogs are related to the Jordan case. The trial of the Jordan case fully reflects the open, self-confident attitude as well as constantly innovative conception of trial of the people's court, which has further demonstrated a good image of open and transparent justice in the Chinese people's courts. The public trial and public pronouncement of the judgment of the said case have exerted positive and far-reaching effect on disseminating legal knowledge, enhancing the concept of rule of law for the whole people, and promoting the construction of a society based on rule of law.

3. **The adjudication of the case has vigorously promoted the socialist core values and given full play to the basic guarantee of the intellectual property system for innovation.**

Innovation is the first driving force for development. As China's economic development enters a new normal, China's economic structure is deeply adjusted, and new and old kinetic energy are continuously transformed. It has reached a new stage of sustainable development only by relying on innovation. In view of the prevalence of the phenomenon of "counterfeiting" in the society for a period of time, of maliciously damaging the legitimate prior rights of others or squatting on trademarks that have been used and have certain influence on others, intellectual property trials must be duty-bound to play a leading role in protecting innovation and maintaining fair competition and in strengthening the basic role of the intellectual property system for innovation, and in promoting the construction of quality power and Chinese brands.

Judicature is the last line of defense to maintain social fairness and justice. Justice in plays an importantly leading role in social justice. The adjudication in the Jordan case highlighted the importance of the principle of good faith in the registration and use of trademarks, and the court has taken a clear-cut and firm attitude towards the

[4]He [1].

malicious violation of the prior rights enjoyed by others in the application for trademark registration. The judgment of the case has played the leading role in guiding the market entity to operate the business in good faith, respecting the legitimate prior rights of others, and fostering the development of independent marks or brands. The standards for the application of laws in the case are of great significance for China to create a fair market order, improve the trademark registration system, and implement brand strategy.

Reference

1. He Xiaorong, "Making Individual Cases Fairly Promote the Rule of Law", *People's Daily*, December 12, 2016.

The People v. Nie Shubin (Intentional Homicide and Rape)—Fact-Finding and Application of Law in Criminal Retrial Procedure

Yunteng Hu, Daohu Xia, Zhengping Yu, Yingshi Guan and Zhiyong Luo

Rule

In a criminal retrial case, if there in no sufficient evidence found in the original trial court to determine such elements as the time of the victim's death and the cause of death, the source of the instruments for committing the homicide, and the time of committing crime, there are doubts as to the authenticity, legality of the guilty confessions, and it is also dubious whether the corpus delicti are committed by others, and the standard of proof of certainty and sufficiency has not yet met due to the incomplete chain of evidence proving the accused's guilt. If so, the accused shall be found innocent of intentional homicide and rape of woman in accordance with law on the ground that the facts are unclear and the evidence is not reliable and sufficient.

Case Information

1. Parties

Prosecution agency in the first instance: The People's Procuratorate of Shijiazhuang City, Hebei Province
Petitioner: Zhang X, Female; Han Nationality; born on December 13, 1944; a peasant; residing in XXX Village, Luquan District, Shijiazhuang City, Hebei Province; (Nie Shubin's Mother)

The retrial collegial bench: Hu Yunteng, Xia Daohu, Yu Zhengping, Guan Yingshi, Luo Zhiyong (Translated by: Zheng Daxuan; Proofread by: Zhang Hongsheng).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_3

Petitioner: Nie X (A), Male; Han Nationality; born on August 1, 1945; a retired worker; residing in XXX Village, Luquan District, Shijiazhuang City, Hebei Province; (Nie Shubin's Father)
Petitioner: Nie X (B), Female; Han Nationality; born on January 31, 1972; a teacher; residing in No. X, XX Street, Qiaoxi District, Shijiazhuang City, Hebei Province; (Nie Shubin's Elder Sister)
Agent ad litem: Li XX, a lawyer from Beijing Tianyuheng Law Firm
The Accused in the first instance trial: Nie Shubin, Male; Han Nationality; born on November 6, 1974; educated at Junior Middle School; a Mechanic of Luquan Metallurgical Factory in Hebei Province; settled in XXX Village, Huolu County (renamed Luquan County), Shijiazhuang City, Hebei Province; arraigned on September 23, 1994, placed under residential surveillance on September 24, detained on October 1, and arrested on October 9; and executed for death penalty on April 27 of 1995.

2. **Procedural History**

First Instance: No. 53 [1995], Trial, Crim. Division, the Intermediate People's Court of Shijiazhuang City, Heibei Province (dated Mar. 15 of 1995)
Second Instance: No. 3 [2016], Retrial, Crim. Division, the Higher People's Court of Heibei Province (dated Apr. 25 of 1995)
Retrial: No. 3 [2016], Retrial, Crim. Division, the Supreme People's Court (dated Dec. 2 of 2016)

3. **Cause of Action**

Intentional homicide; rape

Essential Facts

On the morning of August 10, 1994, Kang X (B) of the lower Niezhuang Village in the suburb of Shijiazhuang City, Hebei Province reported to the suburban branch of the Public Security Bureau of Shijiazhuang City, claiming that his daughter Kang X (A) was missing. On the afternoon of the same day, Kang X (B) and Yu X and others (Kang X (A)'s colleague) found a skirt and a panty of Kang X (A) buried in the weeds in the west cornfield of Kongzhai Village. On the morning of August 11, Kang's body was found in the western cornfield of Kongzhai Village. On the afternoon of the same day, the public security agency inspected the body of Kang X (A). During the investigation of the case, the public security agency were informed by the masses that a young man who was riding a blue X mountain bike was often idling about the public toilet situated in the bungalow dormitory of the Shijiazhuang Electrochemical Factory, around 3 km away from the crime scene. As long as a woman was found in the restroom, that man was found engaged in hooliganism for peeping the woman. Some team members handling the case were sent around the public toilet, watching and guarding the passersby. At 18 o'clock on September 23, 1994, when the accused

Nie Shubin biked though the toilet with a blue X mountain bike, the investigators believed that he was the young man reported by the masses and got the young man caught. Nie Shubin was then taken in that evening to the Liuying Local Police Station, the suburban branch of Shijiazhuang City Public Security Bureau. He was kept in the Liuying Local Police Station and continued to be held on the second day on account of residential surveillance. On October 1 of the same year, Nie Shubin was criminally detained on the charge of intentional homicide and the rape of a woman. He was arrested on October 9. On March 3, 1995, the People's Procuratorate of Shijiazhuang City filed a public prosecution with the Intermediate People's Court of Shijiazhuang City for the crime of intentional homicide and rape of a woman by Nie Shubin.

On March 15, 1995, the Intermediate People's Court of Shijiazhuang City issued a criminal judgment numbered No. 53 [1995] Trial, Crim. Division, with incidental civil judgment. In the judgment, the court held, at 17 o'clock on August 5, 1994, the accused Nie Shubin rode a bicycle and stalked stealthily after a female worker, named Kang X (A),who went off work from Shijiazhuang City Hydraulic Parts Factory; while close to the middle section of Shifen Road, Kongzhai Village, the suburb of Shijiazhuang City, Nie Shubin deliberately hit Kang X (A) with the bicycle and she fell down, then Nie Shubin dragged her into the cornfield in the east part of the said road, and struck Kang X (A) on the head and in the face with his fist, and raped Kang X (A) when she fell into a coma. After that, Nie Shubin used a piece of flowery shirt which was carried with him, and strangled the victim around the neck and caused the victim to suffocate and the victim died thereafter. On March 15, 1995, the Intermediate People's Court of Shijiazhuang City of Hebei Province issued a criminal judgment with incidental civil judgment, numbered No. 53 [1995] Trial, Crim. Division and held in the sentencing part, "Firstly, the accused Nie Shubin has committed the crime of intentional homicide, and shall be sentenced to death and deprived of political rights for life; the accused Nie Shubin has also committed the crime of raping a woman, and shall be sentenced to death deprived of political rights for life (but in the original judgment, Chinese character 'Shen' (身), which means 'body', is missing). Concurrently, the accused Nie Shubin was sentenced to death penalty, with deprivation of political rights for life. Secondly, the accused Nie Shubin was held to be liable for civil compensation, he shall compensate the plaintiff in the incidental civil action for funeral expenses and other expenses incurred at RMB 2000 yuan, which is to be paid in full within one month after the judgment takes effect."

After the first-instance judgment was made, the accused appealed to the Higher People's Court of Hebei Province by claiming that he was small in age, he was but a first-time offender without any prior criminal record; and as his admission of his guilt is sound and good, the sentencing of the fist instance court was too heavy, and thus he requested the court that he should be given a lesser punishment.

The Higher People's Court of Hebei Province held that the court of the first instance has ascertained that Nie Shubin had intentionally murdered and raped a woman, the fact-finding was sound and the evidence was sufficient to incriminate Nie Shubin. Nie Shubin intercepted and raped a woman, and killed her in case any divulgence of secrets was to be revealed. The circumstance and the consequences of

the crime were particularly serious and severe. Though Nie Shubin's attitude toward admission of his guilt is true, the crimes are so severe that the society at large was endangered, so he cannot be exonerated from death. The sentencing for the intentional homicide and the amount of incidental civil compensation were adequate, but the sentencing for the crime of rape of women is harsh. In accordance with Articles 136(1) and (2) of the Criminal Procedure Law of 1979, the judgment affirmed the conviction and sentencing of Nie Shubin's crime of intentional homicide, and revoked the sentencing of Nie Shubin's crime of rape of a woman, and sentenced him to 15 years' imprisonment. Combining the rape with the intentional homicide, the court sentenced him to death penalty and deprivation of his political rights for life. At the same time, according to the delegation of the Supreme People's Court on authorizing the Higher People's Court to verify and approve part of the death penalty case, the said judgment verified and approved Nie Shubin's death sentence.

On April 27, 1995, the accused Nie Shubin was executed.

In January 2005, when Wang X, who was pursued online because he was suspected of murder in other cases by the public security agencies of Hebei Province, was arrested by the public security organs of Fuyang City, Henan Province, he admitted that Kang X (A) was killed by him.

In May 2007, the close relatives of the accused Nie Shubin, Zhang X, Nie X (A), and Nie X (B), filed complaints with the Hebei Higher People's Court and various other departments, requesting that Nie Shubin be pronounced innocent.

On December 4, 2014, the Supreme People's Court appointed the Shandong Higher People's Court to review the case. The Higher People's Court of Shandong Province composed a collegial panel in accordance with the law. After a comprehensive review of the case, it was recommended by the said People's Court that the Supreme People's Court initiate trial supervision process to retry the case.

On June 6, 2016, the Supreme People's Court made a decision numbered No. 188 [2016], Retrial, Crim. Division, the Supreme People's Court, and decided to bring the case up for trial itself.

Issues

1. Whether the facts in the first instance trial are clear-cut and whether the evidences sufficient to determine that Nie Shubin has committed the crime of intentional homicide and rape of a woman, whether the chain of evidences in the case could be found, and how is the evidence with major procedural flaws handled?
2. How to define the scope of the re-trial to solve the problem of "one case, two murderers"? In this case, from the originally archived documents, Nie Shubin always pleaded guilty and never denied the commission of the crime. When Wang X was caught in 2005, he made more than 30 confessions to the public security agencies in Henan Province and Hebei Province, claiming that he was the real murderer of the case, which has attracted widespread concern in the whole society. How to deal with the problem of "one case, two murderers" in the retrial procedure has become one of the focal issues to be resolved in this re-trial.

3. How to apply the previous law and the prevailing criminal procedure law. More than 20 years has been spent from the occurrence of the crime to the retrial. During this period, China's criminal procedure law has undergone two major revisions in 1996 and 2012. Its the legal provisions, content and spirit have witnessed great changes. Whether the previous Criminal Procedure Law (Criminal Procedure Law of 1979) or the present law (Criminal Procedure Law of 2012) is applicable has direct relevance to the protection of the rights of the parties and the evaluation of judicial proceedings.

Holding

On December 2, 2016, the Supreme People's Court made the final judgment numbered No. 3 [2016], Retrial, Crim. Division, the Supreme People's Court.

As the facts incriminating the original accused, Nie Shubin for committing the crime of intentional homicide and the crime of raping a woman trial were unclear and uncertain, and the evidences were insufficient, the judgments numbered No. 129 [1995], Final, Crim. Division, the Higer People's Court of Heibei Province (dated April 25 of 1995) by the Higer People's Court of Heibei Province and the crimibal judgment numbered No. 53 [1995], Trial, Crim. Division, the Intermediate People's Court of Shijiazhuang City (dated March 15 of 1995) together with incidental civil judgment by the Intermediate People's Court of Shjizhuang City are to be reversed and Nie Shubin is to be found not guilty of any crimes.

Comment on Rule

The Nie Shubin case, which was directly brought up for trial by the Supreme People's Court, was one of the most socially important rule of law events in China's judiciary in 2016. On December 2, 2016, the Second Circuit Court of the Supreme People's Court made a public announcement of the Nie Shubin's case outcome involving intentional homicide and rape of a woman to answer the call of the great concerns home and abroad, reversing the judgments concerning the guilty verdict of the accused Nie Shubin by Shijiazhuang Intermediate People's Court of Hebei Province and the Hebei Higher People's Court in 1995 by declaring that Nie Shubin was not guilty of any crimes. Till this time, this hard, complex major case, causing all kinds of speculations and controversies, which occurred, tried and executed more than 20 years ago, and has been retried because in 2005 another accused, Wang X, was caught and confessed of being the murderer in that case, was finally brought to a perfect close. The principle of adjudicating the cases in accordance with evidences in the retrial process, the concept of human rights protection and the applicable judgment methods, can be offered as an "open course for rule of law for the people at large", which has reflected the progress and further development of the criminal justice concept and criminal legal system in contemporary China.

1. **Adhering to the principle of adjudicating the cases in accordance with evidences and the principle of "in dubio pro reo" (innocent until proven guilty)**

The principle of adjudicating the cases in accordance with evidence is a basic principle in criminal proceedings, requiring that the facts of the case be based on the evidences, the determination of the facts of the crime meet the evidence and sufficient standards. As the basis for determining the facts of the case, the evidence must be authentic, legitimate and must go through court investigation procedures. In the case of Nie Shubin, the original basis for the investigation of the facts involving Nie Shubin's charge of intentional homicide and rape of women was Nie Shubin's guilty confessions, and whether Nie Shubin's guilty confession was consistent with other evidence in the case. However, viewing the whole case, the retrial collegial panel believes, no objective evidence or evidences can be directed toward Nie Shubin's committing the prosecuted crimes. Nie Shubin's time for committing the crimes cannot be confirmed; the source of the criminal tool(s) or equipment cannot be ascertained; the time of the victim's death and the cause of death cannot be ascertained; furthermore, the veracity and legitimacy of Nie Shubin's confessions are dubious; the guilty confessions are inconsistent with the authenticity and reliability of the other evidences in the archived documents; the evidence based on the original judgment did not form a complete chain, and did not meet the evidence, the full and sufficient statutory standards, the original trial found that Nie Shubin committed the crime of intentional homicide. The facts of rape of women are unclear and insufficient evidence. The specific analysis is made as follows:

(1) The evidence found in the first instance indicating the time of victims' death and the cause of death are indefinite and inconclusive. The original judgment found that Kang X (A) was strangled to death after being raped by Nie Shubin on the way off work at 17:00 o'clock on August 5, 1994. After close review, the retrial collegial panel held that the evidence of the time and cause of Kang's death was not reliable and insufficient. The main reasons are generalized as follows:

   (A) The autopsy report did not make an inference about the time of Kang X (A)'s death. In the case, the body was highly corrupted and rotten at the time, not any stomach contents of Kang X (A) could be extracted by the forensic scientist to determine the time of death. At the time of the site investigation, the corpses and the surroundings were covered with mites and maggots, and the forensic scientist has not made any inference about the time of death on the basis of the based on mites and maggots on the corpse.
   (B) The testimonies in the case cannot be used to indicate the time of Kang X (A)'s death. The testimonies of witnesses Yu X, Wang X and others can only confirm that Kang X (A) was still working normally in the factory on the afternoon of August 5, 1994. After she left the factory after work, she was never met again afterwards, but all this cannot be said that the victim

was killed to death upon her off-work on August 5th, and neither can the policemen regard the time of the missing time of the victim as the time of her death.

(C) The opinion of the autopsy report on the cause of Kang X (A)'s death is not certain. The autopsy report records that "the death of Kang X (A) is in compliance with death due to suffocation", in addition, the report says it is an advisory "analytical opinion" and is not a definitive conclusion. In this regard, the forensic scientist who examined the body in that year explained during the retrial that the body was highly corrupted and rotten during the test, loss of test conditions could only enable him to make a unclear and inconclusive conclusion, thus he could only make a tendency analysis. The Shandong Higher People's Court have consulted forensic experts twice. The forensic experts did not make a definitive conclusion on the cause of Kang's death. They only guessed about the greater possibility of death resulted from mechanical asphyxia or that mechanical asphyxiation could not be ruled out.

(2) There was a major doubt in the original judgment that the accused committed the crime. In the original judgment, Nie Shubin was found to have raped and killed Kang X (A) on August 5, 1994. After reviewing the original trial, the collegial panel held that evidence about Nie Shubin's crime on August 5, 1994 was not definite and adequate, the facts concerning the commission of crimes could not be ascertained. The main reasons can be summarized as follows:

(A) Nie Shubin's confessions cannot verify the fact that the crime was committed on August 5, 1994. In the archived 13 guilty confessions made by Nie Shubin, the time of commission of crimes was mentioned nine times. In the investigation stage, Nie Shubin's six confessions were capricious and changeable about the date of the crime, and no specific date for the crime was confessed. In the first interrogation transcript on September 28, 1994, he confessed that the crime was committed the next day after the work when Nie Shubin was criticized by Ge X in early August; in the Written Self-Criticism by Nie Shubin on September 29, it was said that the crime was committed on the day when he was criticized and scolded by Ge X. In the confessions made on October 1st, it was said to be the next day of Nie Shubin's being criticized. Since October 17, the date for the commission of crimes has been changed back to be the same day when Nie Shubin was criticized by Ge X. Ever since the prosecution stage, Nie Shubin's three confessions have clearly stated that the crimes were committed on August 5. At the beginning of the case, Nie Shubin was unable to provide a specific date for committing the crime, but a few months later, he was able to clarify and stabilize the confessions. There is not any explanation in the archived documents for why Nie Shubin had a vague memory some times, and why he has possessed a clear memory later on. Therefore, Nie Shubin's confessions about the date of crime on August 5 are inadmissible.

(B) The date when Nie Shubin was criticized by Ge X cannot be ascertained to be August 5, 1994. It is of vital importance to determine the specific date when Nie Shubin was criticized. Whether it is the same day when he was criticized or the next day when he was criticized by Ge X matters a great deal in this case. Nie Shubin repeatedly said in the investigation stage in his confessions that although he could not remember the specific date of going to work in early August, he was sure that in early August, he has got two days off work, and the third day when he resumed work, he was scolded and criticized by Ge X. Ge X confirmed that Nie Shubin was on duty on August 3, 1994. Nie did not go to work on the 4th of August, and Ge X has got a vague memory of whether Nie Shubin's going to work on the 5th or the 6th day, he scolded and criticized Nie, after that Nie Shubin left the unit in an angry manner; the attendance records from the employer obtained by the police has confirmed that Nie Shubin did not go to work at the factory from August 4th to August 11th, which confirmed that Nie Shubin was working on August 3. Therefore, Nie Shubin's mention of two-day absence from work might be August 4th or August 5th, and the third day, i.e. on the 6th August, when Nie went to work, Nie was criticized by Ge X. If the crimes were to be committed the same day when Nie Shubin was being criticized, it might be falling on the 6th of August; if the crimes were to be committed on the next day when Nie was being criticized by Ge X, then the date for the commission of crimes might fall on the 7th of August, which contradicted inevitably with the date of the commission of crimes on August 5 found by the first instance court.

(C) The subsequent testimonies by eyewitness Hou X made a major change to the time of the final meeting with the victim. The two testimonies of Hou X in the archived documents revealed that his wife, Kang X (A) went off to work at 12:55 on August 5, 1994, and they have not met since. During the review and retrial of the present case, Hou X repeatedly said in his testimony that the time when he last saw his wife Kang X (A) was definitely not correct, for he met his wife at about 11 o'clock on the evening of August the 5th. During the review, we found that Hou X's two testimonies in the first instance trial were made separately on October 1 and on October 27 of 1994. The interrogator for the first testimony was unknown, and the second testimony was made at the pre-trial stage, and other previous testimonies were altogether missing, seriously affecting the probative force of these two testimonies. Now, great changes has been detected in the testimony, so that the time of the commission of crimes found in the original trial becomes dubious.

(3) The source of the crime instruments identified in the original trial is doubtful and cannot be confirmed. In the record of the crime scene investigation (Site survey transcript), a short-sleeved flowery blouse was found wrapped around the neck of Kang X (A)'s neck. In the original judgment, it was identified as a crime tool for Nie Shubin's intentional murder. During the reviewing process,

the collegial panel believe, the available evidences at present could not prove whether the said short-sleeved flowery blouse (shirt) was stolen by Nie Shubin, and it was impossible to ascertain that the said was the instrument for Nie Shubin to have killed the victim. Therefore, short-sleeved flowery blouse as the crime instrument held in the original trial are to be excluded. We will specify this point as follows:

(A) It is contrary to the common sense for the first instance court to find that Nie Shubin have stolen a short-sleeved flowery blouse for self-wearing. According to Nie Shubin's confessions and the testimonies made by some witnesses, the economic conditions of Nie Shubin's family were pretty good at the time. Nie Shubin could ride a mountain bike worth more than 400 yuan; the monthly salary was several hundred yuan, and there was no shortage of food and clothing, and there were many shirts, so, apart from being a bit languid at work, there is no evidence to prove that Nie Shubin had previously committed theft and other misdeeds, and there is also no evidence to demonstrate that he was interested in women's clothing. The blouse (shirt) in the case is a woman's flowery blouse with a length of only 61.5 cm and some stitches of mending in the torn blouse, which is definitely unsuitable to be worn by Nie Shubin. Thus the confessions by Nie Shubin that he himself is to put on the blouse sounds odd and queer, and not self-contained and it was contrary to common sense.

(B) The source of the flowery blouse is unclear. According to Nie Shubin's confessions, he stole the flowery blouse from a waste collection in Zhangying Village, a suburb of Shijiazhuang. After investigation, the testimony of the person who collected the waste product, Liang X, was obviously inconsistent with the confessions made by Nie Shubin. Therefore, there is no evidence to indicate the specific location of Nie Shubin's stolen flowery blouse.

(C) The identification record of the flowery blouse lacks probative force. The photo of the flowery blouse taken for identification purposes in the original archived documents differs greatly from the clothing wrapped around the victim's neck. The person who handled the case explained in later occasions that the blouse was cleansed because the blouse wrapped around the neck of the body was eroded by rain and rot. However, there is no record or explanation in the archived documents whether the flowery blouse for identification is identical to the clothing wrapped around the neck of the corpse. Moreover, in the identification records when Nie Shubin was to identify the flowery blouse among three pieces of blouses used as foils, two pieces were long-sleeved, which were significantly different from the identified objects. Another one was short-sleeved but it is unknown whether it is old or new, for there are no photo attachments. Thus, the record has not probative for lack of a standard identification.

(4) The veracity of the accused's guilty confessions is doubtful, and the possibility of directions or inducements can not be excluded, thus these confessions cannot be used as the basis for determining the facts of the case. The archived original documents in the original court indicate that 13 confessions have been made by the accused, Nie Shubin, from the first confession made on September 28, 1994 till the time when he was executed on April 27, 1995, including 11 interrogation transcripts (8 in the investigation stage, one during the prosecution, one in the first instance, and one in the second instance, one self-written Self-Criticism, and one confession made during the court session). The retrial collegial panel concludes, taking into account all the evidences in the case, that in the first five days after Nie Shubin was caught by the police, other confessions made by Nie Shubin cannot be excluded and among these guilty confessions, confessions made under directions or inducements are not to be exclude. Therefore, the veracity or authenticity and legitimacy of Nie Shubin's guilty confessions are doubtful, which cannot be used as the basis for determining the facts of the case. The following specific analysis can be made therefrom.

(A) There is inconsistency and capriciousness in Nie Shubin's confessions of key facts. Regarding the time for committing crimes, different versions can be found, such as the second day after Nie was criticized by the director Ge X or the same day when Nie was criticized by the director Ge X, or unclear or exactly on the August 5th. As for the specific location of the stolen flower blouse, we also find multiple versions, sometime on the tricycles, sometimes on the broken piles. With regard to the time when the victim's underwear was removed, we find such versions as stripping the underwear-rape-taken away, stripping the underwear under the knee-rape-taken away. Regarding the bicycle models, sometimes, the bicycle is Type 26, the other times, the bicycle is Type 24. In addition, there is also inconsistency among Nie Shubin's confessions with regard to the motive, the facts and the circumstances of the crime, the age of the victim and the characteristics of the skirt, etc. In all the archived documents, we find that Nie Shubin always pleaded guilty on the one hand, and on the other hand the basic facts about the commission of crimes were unclear, especially fundamental facts. The confessions of key facts are inconsistent, capricious and even contrary to common sense.

(B) The consistency between confessions and evidence as well as the authenticity and reliability of the evidence dubious. The confessions by Nie Shubin about the location of the crimes, the place where the clothes were buried, the white vest on the corpse, the flowery blouse wrapped around the neck, the sandals worn by the victim, and the position of the bicycle, etc., are basically consistent with the record of crime scene investigation, site survey transcripts and autopsy reports, but all are obtained first by evidence, then come the confessions. Furthermore, no witnesses have been

invited, thus the identification and pointing by others are not standardized, which makes the consistency between confessions and evidence as well as the authenticity and reliability of the evidence dubious.

(C) The possibility of extorting confessions under directions or inducements may not be excluded. With regard to any illegality in collecting the evidence, such as extorting confessions by torture, or inducement, even though we find no traces of extortion or inducements by examining the archived documents, the testimonies, court transcripts, and the explanations by the policemen who handled the case, evidence of extorting confessions by directions or inducements may not be excluded. For example, Nie Shubin once confessed that he did not want to say anything, but the policeman "persuaded him and helped to explain the whole process"; Nie Shubin's changeable confessions about the location of the stolen flowery blouse; some transcripts showed that the content of the interrogation is clearly oriented; the investigators were arranged to cross-check the location of the crime scene, etc. Therefore, the possibility of extorting confessions or inducements may not be excluded.

2. **Focusing on the functions performed by retrial, and determining the scope of retrial**

There are two kinds of opposite views for the determination of the scope of the retrial of Nie Shubin case. Some believe that the scope of retrial can only be limited to the original judgment against Nie Shubin and other people or other cases are excluded. Others think, as Wang X has made a confession of murdering the victim, whose confessions constitute the new evidences beneficial to the accused Nie Shubin. In accordance with relevant laws and regulations, new evidence that is beneficial to the defendant during the retrial process shall be tried, therefore, it is necessary to review the relevant files or archived documents of Wang X's case in the retrial process.

The retrial collegial panel believes that the above-mentioned opinions can be partly justified, but considering that the purpose of the retrial in this case is to find out whether Nie Shubin is the murderer, rather than finding out who is the actual murderer in this "one case, two murderer" controversy, therefore, in the retrial process, that no review of the confessions made by Wang X might be more in line with the nature of the law and the retrial procedure. Meanwhile, according to the original evidences submitted in the Nie Shubin case, no review of the confessions made by Wang X does not affect the fair judgment of the Nie Shubin case. Therefore, in retrial process, confessions made by Wang X are not considered in judging Nie Shubin's behavior, that is, "Wang X's case falls without the scope of the present case".

3. **Ascertaining the applicable rules of criminal procedures on the basis of the protection of human rights**

There are controversies over whether the 1979 Criminal Procedure Law or the 2012 Criminal Procedure Law is to be applicable to the Nie Shubin case. The retrial collegial panel believes that the new Criminal Procedure Law should be applied. The

reasons are generalized as follows. Firstly, it is imperative that the application of the current or the previous law be beneficial to the parties, especially favorable to the accused. Viewing from two revisions of the current Criminal Procedure Law, the protection of the defendant's rights has been reinforced strengthened more than once, so the application of the current law is obviously more conducive to the accused. Thus in handling the present case, a principle of selecting the applicable newer criminal procedural law is to be adhered to. Only if the relevant provisions of the prevailing law are not conducive to the accused, the previous law is applied as an exception. This is also a general rule for choosing the applicable laws in some other countries. Secondly, the applicable principles of criminal law are different from the applicable principles of criminal procedure law. Because the revision of the criminal law may be beneficial to the accused, such as the abolition of the death penalty for certain crimes or increasing the standard for conviction of a certain crime; it may also be detrimental to the accused, such as criminalizing an offence that was originally not a crime or raising certain standards to punish the crimes statutorily. Therefore, there might be a doctrine that the choice of a criminal law has to follow "the old with the lighter" criminal law. In the context of the continuous development and advancement of rule of law, the revision of the procedural law is generally beneficial to the accused, so there should be no so-called principle of "following the older or the lighter" criminal law in handling the criminal cases. Thirdly, although no exclusionary rule of the illegally obtained evidences has been recognized in the Criminal Procedure Law of 1979.

Article 32 explicitly states, "Judges, procurators, and investigators must collect all the evidence according to law to prove that the defendant is guilty or not guilty, and or decide whether the circumstances of the crime are Light or heavy. It is strictly forbidden to extort confessions by torture and collect evidence by threats, inducements, deceptions and other illegal methods". Accordingly, even if the previous law is applicable, if the evidence of the case had been obtained by torture, or other illegally obtained methods, the evidence should be excluded in accordance with the prevailing law or judicial interpretations.

In addition, the reasons for applying the current Criminal Procedure Law in this case can also be summarized as follows. In the first place, the law of procedures is chiefly legislated to regulate the conduct and activities of the judiciary to be engaged in the litigation. The principle of "following newer provisions" in the procedural laws and "following the old with the lighter provisions" in the substantive laws, which are two basic principles in the criminal justice system, shall be adhered to strictly. In the second place, different standards should be adopted to protect the rights of the parties and other litigants and to evaluate the behaviors of the personnel handling the cases. Specifically, the current law is applied to protect the rights of the parties and other litigants, which is beneficial to the protection of the rights of the accused from the procedural perspectives; and the application of the previous law, not today's legal standards to evaluate the conduct and behaviors of personnel handling the case, on the one hand, does not violate the legislative spirit, and on the other hand, conforms to the laws and rules handling cases. And thirdly, the announcement of the Supreme People's Court issued on June 8, 2016 on the retrial of the Nie Shubin case has clearly stated "in accordance with Article 242 (2) and Article 243 (2) of the Criminal

Procedure Law of the People's Republic of China, the case is to be further brought up for trial." From this, we can point out that basis for making the retrial of the present case is the current governing criminal procedure law.

Finally, it is worth mentioning that in Nie Shubin's case, some new measures have been adopted by the Supreme People's Court to ensure procedural fairness or due process, to remedy the rights of the parties, and to rectify every wronged in accordance with law, which has achieved pretty good results. Firstly, the Supreme People's Court has appointed a different court to re-examine the case to avoid delays in the case due to excessive reliance on the local court for self-correction. As the first-instance and second-instance trials of the Nie Shubin case were handled in Hebei Province, the defendant's family had filed complaints for many years, but to no avail. In order to ensure that the case can be handled fairly, the Supreme People's Court appointed the Shandong Higher People's Court to re-examine the case, which is a rarity in the history of criminal proceedings in China. The handling of the Nie Shubin case in different places other than the place where the major interest matters, has guaranteed the neutrality of the re-examination to the maximal extent, has promoted the fairness and credibility of the re-examination, and has ushered in a new epoch for the investigation of further dubious and suspected cases. Secondly, the Supreme People's Court directly initiated the relief procedure for the wrongful cases and decided to review the case by the lower courts. As a way of trial supervision by the Supreme People's Courts, clear provisions are set in the laws and regulations, but it is relatively rare for the Supreme People's Court to make similar review practices. After the Higher People's Court of Shandong Province re-examined the case and recommended that the Supreme People's Court re-examine the case, the Supreme People's Court has not adopted the usual practice of rectifying the case, that is to say, remanding the case to the original courts or other courts, but decided to bring up the case for retrial itself. The Second Circuit Court of the Supreme People's Court heard the case, which has created a precedent procedurally for the Supreme People's Court to retry the wrongful cases discovered by itself in its own right, and this, by itself, has directly promoted the fairness and justice, and has revealed the courage possessed by the Supreme People's Court to correct the wrongful criminal case and the willingness to shoulder the responsibilities in the New Era.

Selected Judicial Opinion(s)

The Criminal Judgment of the Supreme People's Court of the People's Republic of China
The People v. Zhang Wenzhong (The Crimes Regarding Fraud, Institutional Bribery and Misappropriation of Funds)

Huapu Sun, Yingshi Guan, Su Qi, Zhaoyang Dong and Qing Zhou

No. 3 [2018], Retrial, Crim. Division, SPC

The Public Prosecution Agency in the First Instance: The People's Procuratorate of Hengshui City, Hebei Province

The accused, Zhang Wenzhong, male, Han nationality, was born on July 1, 1962, Jimo County, Shandong Province (now Jimo District, Qingdao City, Shandong Province), Ph.D. education, Ex-President of Wu Mart Group. He was detained on December 7, 2006 and was arrested on December 20 of the same year. On March 30, 2009, Zhang Wenzhong was sentenced to 12 years in prison for fraud, institutional bribery and misappropriation of funds with a fine of RMB 500,000 Yuan (paid in full). On April 19, 2010, he was declared to have a three-year reduction of imprisonment from sentenced 12 years of imprisonment. On March 19, 2012, he was curtailed another two years and ten-month imprisonment. He was released from prison on February 6, 2013.

Defender: Zhao Bingzhi, a lawyer from Beijing Zhongwen Law Firm
Defender: Zuo Jianwei, a lawyer form Beijing Trensun Partners

The accused, Zhang Weichun, male, Han nationality, was born on April 27, 1958. Beijing, undergraduate education, Chief Executive of Wu Mart Group. He was detained on December 29, 2006 and was placed under residential surveillance on January 1 of 2007 and was arrested on February 14, 2007. On March 30, 2009, Zhang Weichuan was sentenced to 5 years in prison for fraud with a fine of RMB 200,000 Yuan (paid in full). On July 28, 2010, he was determined to be on probation. On February 11, 2012, the probation expires.

Translated by: Zheng Daxuan.

H. Sun (✉) · Y. Guan · S. Qi · Z. Dong · Q. Zhou
The Supreme People's Court of the People's Republic of China, Beijing, China

Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_4

Defender: Wu Jianping, a lawyer from Beijing Zewen Law Firm
Defender: Zhao Lei, a lawyer from Beijing Zewen Law Firm

The institution where the accused was employed, Wu Mart Group (formerly Beijing Wu Mart Commercial Group Co., Ltd., hereinafter referred to as Wu Mart Group), was located on the 8th floor of Building 3, No. 30 Complex, Shixing Street, Shijingshan District, Beijing. On March 30, 2009, the said institution was fined RMB 5.3 million Yuan (paid in full) for the crime of institutional bribery.

Litigation representative: Xu Ying, President of Wu Mart Group

The Intermediate People's Court of Hengshui City of Hebei Province heard the case prosecuted by the People's Procuratorate of Hengshui City who asserted that the accused, Wu Mart Group, committed bribery; the accused, Zhang Wenzhong, committed the crime of fraud, institutional bribery, misappropriation of funds, and the accused, Zhang Weichun, committed fraud, and issued the judgment on October 9th, 2008, numbered (No. 22 [2008], Trial, Crim. Division, Hengshui), in which the Wu Mart Group was found guilty of bribery and sentenced to a fine of RMB 5.3 million Yuan; Zhang Wenzhong was found guilty of fraud (sentenced to 15 years in prison, and fined RMB 500,000), the institutional bribery (sentenced to three years in prison), and misappropriation of funds (sentenced to one year in prison), the prison term totaling 18 years with a fine of RMB 500,000 yuan; the court also held that the accused, Zhang Weichun, was convicted of fraud and sentenced to five years in prison with a fine of RMB 200,000 yuan; the proceeds that Zhang Wenzhong and Zhang Weichun had illegally obtained should be turned over to the state treasury.

Upon receiving the court's pronouncement of the judgment, Wu Mart Group, Zhang Wenzhong and Zhang Weichun filed an appeal. On March 30, 2009, the Higher People's Court of Hebei Province in the Criminal Judgment number (No. 89 [2008], Final, Crim. Division, Hebei) affirmed the conviction part against Wu Mart Group and Zhang Weichun, and affirmed that the proceeds that Zhang Wenzhong and Zhang Weichun had illegally obtained should be confiscated, and further affirmed that the accused Zhang Wenzhong had committed crime of fraud, institutional bribery, and misappropriation of funds. The court struck down the first-instance judgment on Zhang Wenzhong's fraud and the execution of the penalty, and found that Zhang Wenzhong had committed fraud, should be sentenced to 10 years in prison with a fine of RMB 500,000 yuan (five hundred thousand yuan). Together with the crime of institutional bribery and misappropriation of funds, the court held that Zhang Wenzhong was to serve a 12-year imprisonment with a fine of RMB 500,000 yuan.

After the judgment took effect, Zhang Wenzhong filed a complaint with the Hebei Higher People's Court, and the Hebei Higher People's Court rejected the complaint on December 21, 2015. In October 2016, Zhang Wenzhong petitioned to the Supreme People's Court. After review, this court made a retrial decision numbered No. 683 [2017], Crim. peti., the Supreme People's Court, on December 27, 2017 to retry the case. The said court has composed a collegiate bench in accordance with the law,

and held a pre-trial conference meeting on February 7, 2018. The case was publicly heard on February 12th, 2018. The Supreme People's Procuratorate appointed prosecutors Yin Yijun and Du Yaqi, assistant prosecutors Han Dashu and Liu Wenfeng to perform their duties. Zhang Wenzhong and his defenders Zhao Bingzhi and Zuo Jianwei, Zhang Weichun and his defenders, Wu Jianping and Zhao Lei, the litigation representative Xu Ying of Wu Mart Group, and the witness Huang X attended the meeting. The case has now been tried and concluded.

The Intermediate People's Court of Hengshui City of Hebei Province held:

(A) With Regard to the Crime of Fraud

In the early 2002, the accused Zhang Wenzhong learned that the state was to implement interest discount subsidy policy for the technological renovation projects via national debt interest discounts by key enterprises and key projects. He discussed the matter with the accused Zhang Weichun and Zhang X (A), vice president of Wu Mart Group, and sent Zhang Weichun to the former State Economic and Trade Commission to inquire into the matter. After learning that the government treasure bonds interest discount funds are mainly used to support the technological renovation projects by the state-owned enterprises. As a privately-owned enterprise, Wu Mart Group invariably does not fall within the scope of support, Zhang Wenzhong and Zhang Weichun decided to apply for the subsidy in the name of China Chengtong Holdings (state-owned enterprise, hereinafter referred to as Chengtong Company), by assuming that Wu Mart Group is the subsidiary company of China Chengtong Holdings. To this end, Zhang Wenzhong communicated several times with the President of China Chengtong Company, Tian X (A), and had Tian X (A) agreed to Zhang Wenzhong's request. Under Zhang Wenzhong's instructions, Zhang Weichun and others have drafted a "Feasibility Study Report" of Wu Mart Group's Technological Renovation Project with false and fabricated data and information, and applied to the former State Economic and Trade Commission for the subsidy under the name of a subsidiary company of China Hengtong Group. After the logistics project was approved, Wu Mart Group neither implemented nor applied for a loan from the bank. Later, Wu Mart Group, in the name of an information project, concluded a factitious equipment purchase contract with its affiliated company, Beijing Hekangyoulian Technology Co., Ltd. (hereinafter referred to as Hekangyoulian Company), and with some false invoices, obtained a loan of RMB 130 million yuan for the daily operation of the company, but with no information project implemented. On October 29, 2003, the Ministry of Finance appropriated RMB 31.9 million yuan of government debt interest discount funds to Chengtong Company, and Chengtong Company remitted the funds to the Wu Mart Group's account, with which Wu Mart Group misappropriated the funds to repay the company loans. In the process of the present case being prosecuted, RMB 31.9 million yuan has been recovered.

The evidences substantiated the above facts include "The Administrative Measures for the National Key Technological Renovation Projects via National Debts Interest Discount", "The Administrative Measures for Special Funds for National

Key Technological Renovation Projects via National Debts Interest Discount", "Notice for Applying for 2002 National Key Technological Renovation Projects via National Debts Interest Discount", "Notice on the National Key Technological Renovation Projects via National Debt Interest Discount in 2002 (the eighth batch of treasury bonds special fund project)", project plan, purchase contracts, bank-in slips (collection notices) and other documentary evidences, the testimonies made by witnesses Zhang X (A), Tian X (A), Li X (A), Li X (B), Yu X (A), Yang X (A), Yang X (B), Zhang X (B), Yu X (B) et al., Zhang Wenzhong's and Zhang Weichun's confessions.

(B) With Regard to the Institutional Bribery

In 2002, in the process of acquiring 50 million shares of Taikang Life Insurance Co., Ltd. (hereinafter referred to as Taikang Company) held by China International Travel Service Co., Ltd. (hereinafter referred to as China Travel Service), the accused Zhang Wenzhong asked for the help of Zhao X (A), the director of the general manager's office, and promised a benefit fee. Under the active coordination and assistance of Zhao X (A), at the end of 2002, Wu Mart Group successfully acquired the shares of 50 million shares of Taikang Company held by China International Travel Service Co., Ltd. in the name of an affiliate named Hekangyoulian Company. Subsequently, Zhang Wenzhong directed Zhang X (A) to pay Zhao X RMB 300,000 yuan. From January 2003 to February 2004, Zhang X (A) paid RMB 300,000 yuan to Zhao X through the cost of reimbursement by another Wu Mart Group's affiliate named Custer Investment Consultancy.

In 2002, in the process of acquiring 50 million shares of Taikang Company held by Guangdong Utrust Trust and Investment Co., Ltd. (hereinafter referred to as Guangdong Utrust Company), the accused Zhang Wenzhong promised RMB 5 million yuan as personal benefit to the general manager Liang X (A) of Guangdong Utrust Company. By the end of 2003, Wu Mart Group had acquired 50 million shares of Taikang Company held by Guangdong Utrust Company in the name of its affiliated company Huamei Modern Distribution Development Co., Ltd. (hereinafter referred to as Huamei Distribution Company). Then Zhang Wenzhong directed Zhang X (A) to pay Liang X RMB 5 million yuan through Beijing Jingyehekang Investment Consultancy Center (hereinafter referred to as Jingyehekang Consultancy).

The evidences substantiated the above facts include the Statement of Facts issued by Wu Mart Group; the equity transfer agreement(s); transfer check(s); bank-in slip(s) (collection notice) and other documentary evidences; the testimonies made by witnesses Zhao X, Liang X, Chen X (A), Li X (C), Zhang X (A), together with Zhang Wenzhong's confessions.

(C) With Regard to the Misappropriation of Funds

In March 1997, the accused Zhang Wenzhong and the President Chen X (A) of Taikang Life Insurance Company Co. Ltd agreed through consultation to misappropriate RMB 40 million yuan of Taikang's funds to purchase newly issued shares for profit making. Later, Zhang Wenzhong instructed Zhang X (A), specifically in

charge of purchasing newly issued shares, to transfer RMB 40 million yuan from Taikang Company. Zhang Wenzhong and Chen X (A) also agreed with Tian X (A), the President of China International Futures Co., Ltd. (hereinafter referred to as CIFCO), to make a transfer of the said money through Henan International Trust and Investment Corporation (hereinafter referred to as HITIC) in order to cover up the misappropriation of funds and the three agreed to share the profits earned from the stock transactions, with a ratio of 3:3:4 distribution of the profits among Zhang Wenzhong, Tian X (A) and Chen X (A). In the process of going through the inspection by the People's Bank of China, the three had transferred RMB 50 million yuan from Taikang Company to repay the misappropriated money through HITIC in July 1997. On August 19, 1997, Zhang X (A) returned RMB 40 million yuan to Taikang Company. On September 3 and September 9 of the same year, Zhang X (A) returned RMB 50 million yuan. During the whole process, they have profited RMB 10 million yuan from the stock transactions.

The evidences substantiated the above facts are Taikang Company's check request forms; the commission contract for investment in government treasury bonds, bank-in slip(s) (collection notice); cash flow invoices and other documentary evidences; the testimonies made by witnesses Chen X (A), Tian X (A), Zhang X (A), Li X (D) and Zhang Wenzhong's confessions.

The Intermediate People's Court of Hengshui City of Hebei Province held that the accused Zhang Wenzhong and Zhang Weichun, for the purpose of illegal possession, have fabricated facts, concealed the truth, and defrauded the state loan interest discounts and the amount was extraordinarily enormous, which constituted the crime of fraud; the accused institution, Wu Mart Group, which has granted material benefits to the state functionary during the process of acquiring the equity shares of Taikang Company, committed a crime of institutional bribery; as the one who was put in charge of the accused institution, Zhang Wenzhong should be criminally liable; Zhang Wenzhong and others, by making improper use of their official powers, has misappropriated the funds of the Taikang Company for private profit-making activities, and the sum was sufficiently large, which constitutes a principal offender in the crime of misappropriation of funds, and Zhang Wenzhong also committed separate crimes within the time limit for prosecution and should be investigated further for his criminal liability. The facts and criminal charges accused by the public prosecution agency should be supported. Thus concludes the first-instance judgment.

After the judgment was pronounced in the first instance trial, the accused institution, Wu Mart Group, the accused Zhang Wenzhong and the accused Zhang Weichun respectively appealed, and they all believed that their actions did not amount to crime.

The facts and evidences found in the second instance judgment at the Higher People's Court of Hebei Province are consistent with those in the first instance judgment. The court of second instance held that Zhang Wenzhong and Zhang Weichun, for the purpose of illegal possession, claimed that Wu Mart Group was a subsidiary company of a state-owned enterprise. By applying for the national technological renovation projects via government debt interest discount with false and fabricated projects, and by defrauding funds from the national technology renovation projects via national debt interest discounts, Wu Mart Group obtained extraordinarily huge

amount of money, which constituted fraud. In the process of acquiring the equity of Taikang Company, Wu Mart Group, by granting material benefits to the state functionary in violation of the state regulations, has committed a crime of institutional bribery; Zhang Wenzhong, as an executive officer directly responsible for the operation of Wu Mart Group, shall bear the corresponding criminal responsibility. Zhang Wenzhong joined hands with others, by making use of the official position, has misappropriated the company funds for private profit-making activities, and the amount is large, his conduct constituted the crime of misappropriation of funds. Though the above activities occurred in 1997, Zhang Wenzhong committed new crimes within the time limit for the prosecution of the crime, which should be further investigated for criminal liability. Zhang Weichun plays a supporting role in fraud and is an accomplice, whose criminal punishment can be alleviated. Although the amount of money defrauded in the present case is extraordinarily enormous, the defrauded money has been recovered, which has not caused actual economic losses to the state; meanwhile, considering the defrauded money is not to be used for personal gains, Zhang Wenzhong and Zhang Weichun can be awarded a lightly discretionary punishment. Fifteen (15) years in imprisonment for Zhang Wenzhong in the first-instance judgment because of the fraud is slightly harsh for him and should be vacated and reversed. Thus concludes the aforementioned second instance judgment.

In the retrial by this court, the accused Zhang Wenzhong and his defenders argued that the original sentences were wrong in determining that Zhang Wenzhong was guilty of crimes of fraud, institutional bribery and misappropriation of funds and should be dismissed by this court. The main issues and the defense opinions are summarized as follows:

(a) Wu Mart Group, as a privately owned enterprise, is eligible to apply for the 2002 national technological renovation projects via national debt interest discounts by way of an affiliated company of a state owned enterprise, Chentong Company, for that was a channel to submit the project applications; Zhang Wenzhong did not participate in the preparation of the application and has not instructed Zhang Weichun and others to draft the Feasibility Study Report by way of fabricated facts and materials. The logistics project and information project applied by Wu Mart Group are real, and the information project has been implemented and has reached the predicted objectives in the Feasibility Study Report. The main objectives of the logistics project in the application phase, though encountered many objective obstacles, such as the adjustment of the land use right by the state and by the logistics industrial park in Tongzhou District of Beijing, have been achieved through implementation in a different place. Lack of intention and conduct on the part of Zhang Wenzhong in adjudging the defrauding of state interest discount funds in the national technological renovation projects via national debts interest discounts does not constitute fraud.
(b) The RMB 300,000 yuan involved in the case is the remuneration offered to Zhao X, and RMB 5 million yuan is the intermediary fee for the middleman Li X and other two persons, which is not paid by Wu Mart Group; it is the Hekangyoulian Company who has made the acquisition of the equity of China Travel Service;

and it is Huamei Distribution Company who has made the acquisition of 50 million shares of Taikang Company held by Guangdong Utrust Company. Wu Mart Group cannot satisfy the subject requirements in determining the institutional bribery in this case, thus does not constitute an institutional bribery. Zhang Wenzhong, as the person directly responsible for the Wu Mart Group, therefore, does not constitute an institutional bribery; and

(c) The RMB 40 million yuan is borrowed from Taikang Company by the Custer Investment Consultancy. The nature of this transaction can be analogous to the borrowing and lending of money among the institutions or companies, which cannot be said to misappropriate funds for personal benefits and Zhang Wenzhong's conduct may not amount to the crime of misappropriating funds.

The accused Zhang Weichun and his defenders believed that Zhang Weichun's conduct did not constitute a crime of fraud and should be acquitted according to law.

In addition to the similar arguments and defense opinions raised by Zhang Wenzhong and his defenders, Zhang Weichun also raised the point that he was appointed by the board of directors of Wu Mart Group to be responsible for the application of the logistics project and information project, and he was performing the officially designated duties and he does not possess the subjective intent of committing the crime of fraud.

The litigation representative of Wu Mart Group agreed with the accused Zhang Wenzhong's defense and his defender's defense opinions and claimed that Wu Mart Group did not commit an institutional bribery and should be acquitted according to law.

The opinions of the above-mentioned parties were heard at the pre-trial meeting. With regard to the crime of fraud, the accused Zhang Wenzhong and the accused Zhang Weichun, together with their defenders, motioned to the court for the appearance at the court hearing of a witness named Huang X (A) and submitted three new evidences to the court to support the defense opinions: (a) a fact sheet for 2002 National Key Technological Renovation Projects via National Debts Interest Discount issued by witness Gan X on January 25, 2018; (b) a fact sheet raised the witness Li X (A) on January 25, 2018; and (c) the testimony of the witness Yu X (A) on December 16, 2008. For the crime of the institutional bribery Zhang Wenzhong's defender submitted four sets of new evidences to the court to support his defense opinions: (a) the testimony of witness Liu X (A) on March 8, 2009; (b) an "Additional Statement of Zhao X's Official Position in Taikang Company" issued by the Taikang Company on March 18, 2009; (c) Registration and Sign-in Books for the Taikang Company's 2003–2008 Shareholders' General Meetings and Extraordinary Meetings, Powers of Attorney issued by the Shareholder(s), and Shareholders' Voting Record, Director Nomination Letter, Shareholders' meeting votes; and (d) Taikang Company's Resolution for 2008 General Meeting of Shareholders, dividend payment instructions issued by Huamei Company and Hekangyoulian Company, Taikang Company payment receipt, bank payment system special certificates, accounting vouchers of Huamei Company and Hekangyoulian Company.

Prosecutors from the Supreme People's Procuratorate believe that the original judgment has mistakenly applied the law, resulting in errors in conviction and sentencing, and suggested to this court that the accused Zhang Wenzhong, Zhang Weichun, and the institution where they were employed, Wu Mart Group, be acquitted. The reasons can be summarized as follows: (A) there are no grounds for the original judgment to determine that Wu Mart Group lacks sufficient qualifications for applying for the National Key Technological Renovation Projects via National Debt Interest Discount. There might be some inaccurate information about the Fact Sheet of Enterprises and the Feasibility Study Report about the logistics project in the application documents submitted by Wu Mart Group, but these information may not amount to business fraudulent practices, thus committing the crime of fraud, and state functionaries have not fallen into a misconception of the business practices because of the inaccurate information submitted in the application documents. Furthermore, RMB 31.9 million yuan obtained from the National Key Technological Renovation Projects via National Debts Interest Discount to repay other debts, though in violation of specific use for special government funds, was still placed under the control of the government, for in the financial accounting items, this sum of the money was listed as "payable to the People's government", which will not be said to be misappropriated by Wu Mart Group. Thus the act committed by Zhang Wenzhong and Zhang Weichun will not constitute the crime of fraud; (B) In the acquisition of the Taikang Company's shares, Wu Mart Group, the parent company, has not sought any illegitimate interests in the process of acquiring shares even if RMB 300,000 yuan and RMB 5 million yuan involved in the case were respectively given to Zhao X and Liang X for their help in the acquisition of the shares, despite the fact Zhao X and Liang X have not offered any undue assistance for the acquisition, thus the conduct of Wu Mart Group and of Zhang Wenzhong would not constitute the crime of the institutional bribery and (C) Zhang Wenzhong, Chen X (A), and Tian X (A) have conspired to misappropriate RMB 40 million yuan from Taikang Company for profit-making from the stock transactions, which will not count as an activity by the institution; Zhang Wenzhong' s conduct constitutes the crime of misappropriation of funds, but has exceeded the time limit for prosecution.

After reviewing the submitted facts in the re-trial process, this court has ascertained that,

1. **With Regard to the Crime of Fraud**

In the early 2002, Zhang Wenzhong learned of the policy of interest discount subsidy and that the former State Economic and Trade Commission were organizing the application for 2002 National Key Technological Renovation Projects via National Debts Interest Discount, then after deliberation with others, Zhang Wenzhong instructed Wu Mart Group to appoint Zhang Weichun to be specifically responsible for the application. Then, Zhang Weichun went to the former State Economic and Trade Commission and other departments for consultation. As a matter of and for the sake of convenience, Zhang Wenzhong and Zhang Weichun decided to apply for interest discount subsidy in the name of Chengtong Company, and they have obtained the approval of Tian X (A), the President of Chengtong Company.

Wu Mart Group applied to the former State Economic and Trade Commission with its two National Key Technological Renovation Projects via National Debts Interest Discount (hereinafter referred to as logistics project and information project), and has got all the required application materials, such as the "Feasibility Study Report", among these materials, the land use planning opinions and drawings attached to the "Feasibility Study Report" of the logistics project are not standardized and have no statutory effect. After the approval of the two projects by the former State Economic and Trade Commission and other departments, Wu Mart Group and Heyoukangian Company signed a false equipment purchase contract, issued false invoices, and obtained a loan of RMB 130 million yuan for the information project, which was later used for the company's daily operations. The logistics project was not implemented as originally planned due to objective reasons, and not any loan has been obtained. Till November 2003, Wu Mart Group obtained a total of RMB 31.9 million yuan from the National Key Technological Renovation Projects via National Debt Interest Discount with its logistics project and information projects through Chengtong Company, which was then used to repay the other loans of the company. After the case was prosecuted, RMB 31.9 million yuan was recovered.

The above-mentioned facts were evidenced by the facts that have been produced and confirmed by the trial court as "The Administrative Measures for National Key Technological Renovation Projects" and the "Measures for the Administration of Special National Funds for National Key Technological Renovation Projects via National Debts" and the "Circular Notice for Organizing the Application for the National Key Technological Renovation Projects via National Debt Interest Discount in 2002", "The Announcement of the Project Plan for 2002 National Key Technological Renovation Projects via National Debt Interest Discount (the 8th Batch of National Debt Special Fund Project), "Announcement of the 2nd Batch of Investment Plan for the National Key Technological Renovation Projects via National Debt Interest Discount in 2003", "The Announcement of the 2nd Batch of National Debts Special Funds for National Key Technological Renovation Projects in 2003), and other related government documents ; the Fact Sheet of Businesses/Enterprises, Fact Sheet of the Applied-for Project(s), "Feasibility Study Report" for the Logistics Project, "Feasibility Study Report" for Information Project, Planning Opinions, Purchase Contracts, Loan Contracts, Bank-in Slip(s) (Collection Notices); Transfer Check Stubs, Loan Vouchers, Special Vouchers/Certificates of the Bank Payment system, Invoices, Lists of Seized Items, etc.; the testimonies made by witnesses Zhang X (A), Wang X (A), Wu X (A), Tian X (A), Li X (A), Li X (B), Hao X (A), Men X, Gan X, Huang X(A), Yu X(A), Xu X, Li X(E), Hao X (B), Chen X (B), Luo X, Qi X, Yang X, Yuan X, Zhang X (B), Zhang X (C), Liu X (B), Zhang X (D), Yu X (B), Meng X, Li X (F), and Wang X (B), and the confessions made by the accused Zhang Wenzhong and Zhang Weichun.

Taking into account the defense of the accused Zhang Wenzhong and the defense opinions their defenders made about the crime of fraud, and the opinions issued by the Supreme People's Procuratorate prosecutors, together with the ascertained facts and evidences during the retrial process, we make the following observations.

(1) Wu Mart Group, a privately-owned enterprise, possesses the required qualifications to apply for the National Key Technological Renovation Projects via National Debt Interest Discount. The application for the projects under the name of the affiliated Company of Chengtong Company does not bring about any misunderstanding of the competent departments in charge of project examination and approval.

A. Relevant policy documents contain no prohibitions against private enterprises from applying for the National Key Technological Renovation Projects via National Debt Interest Discount. The applications submitted by Wu Mart Group, which is a private enterprise, conform to the policy concerns and are in line with requirements in the 2002 National Key Technological Renovation Projects via National Debt Interest Discounts. The original judgment that Wu Mart Group, as a private enterprise, does not fall within the scope of application for the National Key Technological Renovation Projects via National Debt Interest Discounts, is based on the policy consideration of the National Key Technological Renovation Projects via National Debt Interest Discounts issued by the former State Economic and Trade Commission, the former National Development Planning Commission, the Ministry of Finance, and "the Administrative Measures for National Key Technological Renovation Projects" and the "Measures for the Administration of Special National Funds for National Key Technological Renovation Projects via National Debt Interest Discounts" issued by the People's Bank of China in 1999. In all these policy documents, no explicit prohibitions against the private enterprises from applying for key national technological renovation projects to obtain financial support or subsidies have been discovered. Since China's official accession to the World Trade Organization in December 2001, and the completion of the goals of three-year reform and getting rid of operational difficulties or challenges for the state-owned enterprises, the state has adjusted the dimensions and the focus of the key national technological renovation projects, and has further clarified the fact the each and every business, whether state-owned or privately-owned, enjoys equal treatment, has thus contained the logistics project and the information project in the scope of the key national technological renovation projects via national debt interest discount. Similar explicit provisions in favor of the private businesses can be also found in the attachment named "Investment Highlights according to Types of Businesses of the Technological Renovation Projects Via National Debt Interest Discount in 2002" to "The Circular Notice for Organizing the Application for the National Key Technological Renovation Projects via National Debt Interest Discount in 2002" issued by the former State Economic and Trade Commission on February 27, 2002, "Suggestions for Promoting the Development and the Operations of the Chain Businesses in China" issued jointly by the State Institutional Reform Office and the former State Economic and Trade Commission and forwarded by the General Office of the

State Council in 2002, and "The Outlines of the Structural Adjustment Plan for the Commodity Circulation Industry during the Tenth Five-year Plan" issued by the former State Economic and Trade Commission on October 16, 2002. Upon Wu Mart Group's applying for the key national technological renovation projects in 2002, the state's policy toward private enterprises and the policy of subsidies for the key national technological renovation projects via national debt interest discount have been adjusted. Thus the logistics project and information project by Wu Mart Group fall within the scope of state subsidies. As a large-scale domestic circulation enterprise, Wu Mart Group positively applied for the key national technological renovation projects via national debt interest discount, which is in line with the requirements of the national economic development and industrial policies at the time.

B. Evidences have also substantiated the fact that the privately-owned enterprises were eligible to apply for the national key technological renovation projects via national debt interest discounts.
   (a) During the first instance trial, the news coverage on November 16, 2001 that "Equal Treatment of All Businesses for the China's National Key Technological Renovation Projects via National Debts Interest Discount" submitted by the defender indicates, persons in charge of the former State Economic and Trade Commission have made explicit expression of the equal treatment of all businesses for the "National Key Technological Renovation Projects via National Debt Interest Discount" since 2002.
   (b) Witness Men X confirmed that in 2002, the state did not ban the regulation on subsidies for the national key technological renovation projects via national debt interest discount to be supportive of privately-owned circulation enterprises. At the time, in the seventh, eighth and ninth batches of national key technological renovation via national debt interest discounts, there were indeed private enterprises that were supported and have obtained interest discounts.
   (c) The "Investment Plan for the National Key Technical Renovation Project of the Second Batch of National Debt Special Funds for 2003" submitted by the defender and the industrial and commercial registration materials of relevant enterprises have confirmed that among the same enterprises as Wu Mart Group approved at the same time, several private enterprises have also obtained interest discounts.
   (d) During the retrial period, the "Notes on the Relevant Situations of the 2002 National Key Technological Renovation Projects via National Debt Interest Discount" given by the witness Gan X confirmed that since 2001, some private enterprises have been included in the plan for interest discounts for the national key technological renovation projects via national debt interest discounts; witness Huang X (A), appearing in the court room, also testified that the eight batches of

national key technological renovation projects via national debt interest discounts contained no restrictions on the ownership of enterprises. The above evidences are sufficient to confirm that private enterprises in 2002 have possessed the qualification to apply for the national key technological renovation projects via national debt interest discounts.

C. Wu Mart Group's application for the national key technological renovation projects via national debt interest discounts in the name of Chengtong Company has not concealed the fact that it was a privately owned enterprise, nor did it cause the competent government departments who are responsible for examination and approval to misunderstand.
   (a) After investigation, according to the "Notice on Agreeing to the Financial Relations of China Chengtong Holding Company" and the "List of Member Institutions of China Chengtong Holding Company", Wu Mart Group is indeed not the member of Chengtong Company in the Ministry of Finance. But Wu Mart Group applied for the subsidy of the national debt technical reform in the name of the company affiliated to Chengtong Company, and obtained the consent of Chengtong Company, and Wu Mart Group reported in the basic information of the enterprise in the application documents that "Beijing Mart Supermarket Co., Ltd." after the approval of the Investment and Planning Department of the former State Economic and Trade Commission, was adjusted to Wu Mart Group, and it was declared under the real name of the enterprise and had not concealed.
   (b) The testimony of the witness Huang X (A) and the letter from the former Ministry of Domestic Trade for determining the first batch of chain enterprises in China have confirmed that Wu Mart Group is the designated contact enterprise of the former Ministry of Domestic Trade and the former Trade and Economic Cooperation Bureau of the State Economic and Trade Commission. The witness Li X (B) confirmed that during the application process of the Wu Mart Group, he had heard reports from Zhang Wenzhong, Zhang Weichun and others, and inspected the supermarkets and logistics bases of Wumart, and participated in the examination and approval, which was considered to be in line with the principle of national debt project arrangement. It can be seen that the former State Economic and Trade Commission, as the examination and approval department, is clear about the nature of the Wu Mart Group. Zhang Wenzhong and Zhang Weichun reported that the Wu Mart Group applied for the technical reform of the national debt in the name of the company affiliated to Chengtong Company, and did not make the relevant personnel of the former State Economic and Trade Commission responsible for the examination and approval work misunderstand the nature of the enterprise.

(2) The logistics project and information project applied for by Wu Mart Group are not fictitious or fabricated.

A. The logistics project is not fabricated. The failure to have the said project implemented as planned and no loan obtained were due to objective reasons, but the said project has been implemented in a different place.

(a) The logistics project itself is not fictitious. On April 18, 2002, after the application, The Cooperation MOU signed by Wu Mart Group with the People's Government of Tongzhou District, Beijing, has confirmed that, if Wu Mart Group actively participated in the construction of the logistics industrial park in Tongzhou District, the People's Government of Tongzhou District would provide certain support in policy and resources to assist Wu Mart Group to establish a large-scale modern logistics center in Tongzhou District; in September 2002, the Environmental Impact Assessment Report for the Construction Projects by Beijing Environmental Protection Bureau issued by the Environmental Impact Assessment Office of Tsinghua University has confirmed that, upon the commission of Wu Mart Group, the Environmental Impact Assessment Office has appraised the environmental impact for the logistics project in Tongzhou District Logistics Industrial Park. Thus it can be seen that the logistics project of Wu Mart Group is not fabricated.

(b) The failure to have the logistics project implemented as planned and no loan obtained were due to objective reasons, but the said project has been implemented in a different place. The testimonies of witnesses Wang X (A), Wu X (A), Yu X (A), Li X (E), Xu X, Zhang X (B), Yuan X, Wang X (B), and others have confirmed that the logistics project of Wu Mart Group in Tongzhou District was initially delayed owing to SARS at that year. Later, as for the method of land use right assignment, the Administration Office of Tongzhou District Logistics Industrial Park required businesses to make a purchase of the land use right, which conflicted with Wu Mart Group's original plan to lease the land, for the investment cost is too high, thus Wu Mart Group failed to reach an agreement with the Tongzhou District Logistics Industrial Park. So Wu Mart Group built its logistics centers in Beijing Baiziwan and other places. The witness Yu X (A) has, in the investigation stage, also confirmed that due to the inability to provide land use and commencement procedures, the logistics project in Tongzhou District of Beijing could not obtain bank loans. Though required to go through the procedures for changing the site of implementing the logistics project in other places, the logistics project was not implemented at all. Therefore, it can be seen that failure to have the logistics project implemented in the planned site and no loan obtained were due to such objective reasons as the SARS epidemics and the change of land use

right assignment policy from lease to purchase by Tongzhou District Logistics Industrial Park.

(c) Although the "feasibility study report" of the logistics project submitted by Wu Mart Group contains some misrepresentations, it is not enough to negate the feasibility and authenticity of the project. The Feasibility Study Report of the Logistics Project, planning opinions and certificates issued by Beijing Tongzhou District Planning Bureau, the testimonies made by witnesses Zhang X (A), Yu X (B), Meng X, Li X (F), Zhang X (B), Liu X (B), Zhang X (D) together with the confessions of the accused Zhang Weichun in the original trial, have confirmed that Wu Mart Group, in the process of preparing the "Feasibility Study Report" for the logistics project, Vice President Zhang X (A) and others went to Tongzhou District, Beijing for the on-site inspection of the logistics project and requested the production of the land use right certificates. The Planning Bureau of Tongzhou District issued a planning opinion with attached Special Seals for Bureau Planning and Administration, and reached consensus of admitting Wu Mart Group to construct a commercial project in the logistics industrial park of Tongzhou District. In the meanwhile, Wu Mart Group attached the geographical location map and floor plan of the proposed project rather than the standardized land topographic map in the concluding part of the said planning opinion. Although the above mentioned planning opinions and drawings are not standardized and have no legal effect, they cannot be resorted to deny the feasibility and authenticity of the entire logistics project.

B. There is insufficient justification for the original judgment to find that Wu Mart Group has applied for a factitious/fabricated information project.

(a) The main contents of the information project by Wu Mart Group include, but not limited to: transformation or renovation of various stores; updating of the headquarters computer hardware and software systems; business organization, modes of management and operation that quickly adapt to market changes; improvement in the network support system; establishment of modern logistics system; management system for supply chain; e-commerce application system and business decision-making support systems. Upon the investigation, it is found that Wu Mart Group has invested heavily in these aspects in its daily operations. The original judgment which held that Wu Mart Group has misappropriated the loan from the applied information project for the purpose of its daily operation of the company, thus failed to implement the information project, was not justified.

(b) Although Wu Mart Group applied for the information project by concluding a false contract, we have no grounds to determine that the information project was false. The purpose of the National Key Technological Renovation Projects via National Debt Interest Discounts

is to encourage the enterprises or businesses to renew or renovate the technology, and the project applied for by Wu Mart Group falls within policy support. According to the application process, when Wu Mart Group applied for a bank loan, the application for the National Key Technological Renovation Projects via National Debt Interest Discounts has been approved. After that, Wu Mart Group applied for bank loans for the information project loan by concluding a false contract, though in violation of certain rules or regulations, that cannot be said to be a fraudulent act to defraud the interest discount funds, and we cannot come to the conclusion that the information project was fabricated, or fictions.

C. The use by Wu Mart Group of RMB 31.9 million yuan in violation of rules or regulations granted the National Key Technological Renovation Projects via National Debt Interest Discounts does not constitute a crime of fraud.

Upon a grant of RMB 31.9 million yuan from the National Key Technological Renovation Projects via National Debt Interest Discounts, Wu Mart Group used the fund to have repaid other loans of the company. However, it has been listed as "payable to the People's government" in the financial accounts, and has not concealed or embezzled. In addition, Wu Mart Group has the ability to return the funds at any time. Therefore, the conduct of Wu Mart Group, though in violation of the provisions for the special funds (treasury bond) for special purposes in the "Measures for the Administration of Special Funds for National Key Technological Renovation Projects via National Debt Interest Discounts", cannot be said to constitute a fraudulent act for illegal possession of the interest discount project funds. In sum, the defense by the accused Zhang Wenzhong, Zhang Weichun and the defense opinions by their defenders that Wu Mart Group, as a private enterprise, is eligible to apply for the National Key Technological Renovation Projects via National Debt Interest Discounts; and Zhang Wenzhong and Zhang Weichun has not defrauded in applying for the National Key Technological Renovation Projects via National Debt Interest Discounts have not manifested any deliberate intention of defrauding, thus the defense and defense opinions regarding the crime of fraud were tenable and are to be adopted by this court; and the opinions offered by the inspectors from the Supreme People's Procuratorate that the conduct of Zhang Wenzhong and Zhang Weichun did not constitute a crime of fraud was tenable and is also to be sustained by this court.

2. **With Regard to the Crime of the Institutional Bribery**

In 2002, the accused Zhang Wenzhong, in the first instance trial, was informed that the China International Travel Service wished to transfer 50 million shares of Taikang Company, then he expressed to the Director General of the General Office of the China Travel Service, Zhao X (handled in a separate case), his intention to acquire the said 50 million shares of Taikang Company by Wu Mart Group. In the meanwhile, Zhang Wenzhong wished to have the help of Zhao X and promised to offer some fair benefit to Zhao X. Then, Wu Mart Group and China Travel Service reached initial consensus about the acquisition of shares after repeated negotiations. On June

26, 2002, Wu Mart Group, in the name of its affiliated company, Hekangyoulian Company, concluded an equity transfer agreement with China Travel Service. By the arrangement of Zhang Wenzhong, Zhang X (A) has made a payment of RMB 300,000 yuan to Zhao, between January 2003 and February 2004, by means of reimbursement expenses through the Custer Economic Evaluation Center, an affiliated company of Wu Mart Group.

In 2002, Guangdong Utrust Company decided to transfer the 50 million shares of Taikang Company to help alleviate the company operational difficulties. Chen X (A), the President of Taikang Company, informed the accused Zhang Wenzhong of this decision and suggested Zhang Wenzhong to make this acquisition, to which Zhang Wenzhong agreed. In order to promote the transfer of equity, Chen X (A) offered RMB 5 million yuan benefit fee to Liang X, the General Manager of Guangdong Utrust Company, and requested Zhang Wenzhong to propose the similar offer to Liang X, to which Zhang Wenzhong agreed. Under the request of Chen X (A) and Zhang Wenzhong, Li X (C) (the President of Guangzhou Huayi Advertising Co. Ltd. and Guangzhou Huayi Culture Co. Ltd.), Liang X's alumni, was also urged to persuade Liang X to provide adequate help for Wu Mart Group to acquire the Taikang Company shares. Then, Wu Mart Group proposed to transfer the shares of Taikang Company held by Guangdong Utrust Company at a price of RMB 1.35 yuan per share, but refused by Liang X. According to Liang's proposal, Guangdong Utrust Company entrusted Guangzhou Enterprises Mergers and Acquisitions Services (GEMAS) to log into the bidding system of GEMAS for transferring the shares, with the bidding price set at RMB 1.45 yuan per share, to no avail, the bidding failed. Then, Guangdong Utrust Company and Wu Mart Group have engaged several rounds of negotiations, and finally reached an agreement at a price of RMB 1.4 yuan per share to acquire the Taikang Company shares held by Guangdong Utrust Company. On March 20, 2003, Wu Mart Group signed an equity transfer agreement with Guangdong Finance Company in the name of its affiliated company, Huamei Company. A few months later, Li X (C) demanded through Chen X (A) RMB 5 million yuan from Zhang Wenzhong, but to no knowledge of Liang X. At the request of Chen X (A), Zhang Wenzhong arranged for Zhang X (A) to transfer RMB 5 million yuan to the corporate account of Li X (C). Later when Liang X learned of the matter, he expressly stated that he had nothing to do with the matter and refused to accept the payment. So the money has been occupied by the Li X (C)'s company.

The above-mentioned facts have been substantiated by Fact Sheet issued by Wu Mart Group, the chart of Wu Mart Group's affiliation relationship, the minutes of meeting of China Travel Service, the business license of the China Travel Service, and the notice of the China Travel Service about the appointment and removal of officials, the minutes of the meeting of the Guangdong Utrust Company, the letter on the transfer of Taikang Company shares, the letter on the acceptance of the transfer of Taikang Company shares, the equity transfer agreement, the approval granted by China Insurance Regulatory Commission, the Articles of Incorporation and MOU of Taikang Company, the business license of Guangdong Utrust Company and its shareholders, transfer cheques, bank-in slips (collection notices), accounting vouchers, invoices, etc., the testimonies made by witnesses Zhao X, Liang X, Chen X (A),

Li X (C), Zhang X (A), Wang X (A), Zhang X (E), Xu X, Li X (G), Wang X (C), Sun X, Huang X (B), Tian X (B), Pan X, Liu X (C), Liu X (D), Han X, Cai X, Li X (H), Zhang X (G) and others, forensic accounting appraisal opinions and the confessions made by the accused Zhang Wenzhong, all of which are confronted and corroborated during the first-instance and re-trial processes.

Taking into account the defense of the accused Zhang Wenzhong, the defense opinions his defender(s) made about the crime of the institutional bribery, the defense opinion the litigation representative of WU Mart Group submitted as well as the opinions issued by the Supreme People's Procuratorate inspectors, together with the ascertained facts and evidences during the retrial process, we make the following observations.

(1) Wu Mart Group has implemented the act of giving Zhao RMB 300,000 yuan and paying RMB 5 million yuan to Li X (C)'s company.
The accused and his defender in the first and second instances, and the litigation representative of Wu Mart Group, claimed that RMB 300,000 yuan to Zhao X and RMB 5 million yuan WTO Li X (C)'s company were not paid by Wu Mart Group, which are found to be contrary to the facts and evidences.

A. Hekangyoulian Company, Huamei Company, Custer Economic Evaluation Center, Jingyehekang Center and others are directly controlled by Wu Mart Group. Forensic accounting appraisal opinions, the chart of Wu Mart Group's affiliation relationship, Fact Sheets issued by Wu Mart Group, the testimonies made witnesses Zhang X (A), Wang X (A), Xu X, Zhang X (E), and others, and the confessions made by the accused Zhang Wenzhong have confirmed, Zhang Wenzhong's registered capital in Wu Mart Group amounts to 61.78% of company capital, and he is also the controlling shareholder of such companies as Hekangyoulian Company, Huamei Company, Custer Economic Evaluation Center and Jingyehekang Center; the capital of Wu Mart Group and the capital of the above-mentioned affiliated companies are handled uniformly by the Accounting and Finance Department of Wu Mart Group; the financial and accounting work of these affiliated companies is managed by the Wu Mart Group financial staff on a part-time basis, and is directly under the guidance of Zhang X (A), the vice president of Wu Mart Group.

B. The decision to acquire the equity in the name of the affiliated company is made by the board of directors of Wu Mart Group. The fund-raising was also managed by Wu Mart Group. The payment of such expenses as the equity purchase fee is made by Zhang X (A) himself or a designated accountant under the request of the accused Zhang Wenzhong. The Fact Sheet issued by Wu Mart Group, the Articles of Incorporation and MOU of Taikang Company, transfer checks, accounting vouchers, etc., the testimonies made by witnesses Chen X (A), Zhang X (A), Zhao X, Li X (G), Liang X, Han X, as well as the confessions made by Zhang Wenzhong have confirmed that the acquisition by Wu Mart Group of the Taikang Company shares

held by China Travel Service or Guangdong Utrust Company was completed through negotiating with China Travel Service or Guangdong Utrust Company. As Wu Mart Group has held a certain proportion of Taikang Company's shares, in order not to violate Taikang Company's provisions in the Articles of Association that a single shareholder's shareholding is not allowed to exceed 10%,the board of directors of Wu Mart Group decided to use its affiliates, i.e. Hekangyoulian Company and Huamei Company respectively to make the acquisition, with each affiliated company concluding equity transfer agreements with China Travel Service and Guangdong Utrust Company respectively; the amount of payment was made by Hekangyoulian Company or Huamei Company respectively through internal dispatch of money to the respective bank account by Wu Mart Group. RMB 300,000 yuan to Zhao X and RMB 5 million yuan to Li X (C)'s companies, were completed by the affiliated companies, namely, Custer Economic Evaluation Center and Jingyehekang Center, all the money were forwarded to each company by Mart Group, including RMB 5 million yuan paid by Jingyehekang Company.

(2) The conduct of Wu Mart Group's payment of RMB 300,000 yuan benefit fee to Zao X (A) does not constitute an institutional bribery.
Transfer checks, such documentary evidences of payment to reimburse Zhao X as conference fee invoices or invoices indicating expenses of interior decoration materials, the testimonies made by witnesses Zhao X, Zhang X (A), Chen X (A), Sun X, Huang X (B), Tian X (B), Pan X, Liu X (C) and Liu X (D), together with the confessions by the accused Zhang Wenzhong at the criminal investigation stages have corroborated with each other and it is sufficient to confirm that RMB 300,000 yuan to Zhao X by Wu Mart Group is a benefit fee rather than a remuneration. Zhang Wenzhong's defender submitted new evidences to the court during the retrial to prove that Zhao X, a supervisor as well as a shareholder of Taikang Company from April 2003 to 2008, has provided some labor services for Wu Mart Group's affiliated companies, namely, Hekangyoulian Company and Huamei Company. Upon close investigation, this court has made sure that the time when Wu Mart Group made a payment of RMB 300,000 yuan to Zhao X was not consistent with the time when Zhao X served as the supervisor and shareholder of Taikang Company and provide labor service. There was no correlation between the two.
In accordance with Article 393 of the Criminal Law of the People's Republic of China, where an institution offers bribes for the purpose of securing illegitimate benefits or, in violation of State regulations, gives rebates or service charges, if the circumstances are serious, that constitutes the crime of institutional bribery. RMB 300,000 yuan benefit fee to Zhao X by Wu Mart Group is a violation of state regulations by giving benefit fees, service charges or rebates to whoever handles the state affairs in the economic activities. However, according to the transferred equity of Taikang Company, the minutes of the meetings, the analysis report of equity transfer, the equity transfer agreement, the testimonies by

witnesses Zhao X and Li X (G), and the confessions made by Zhang Wenzhong, the following factors shall be taken into account in deciding whether there is a crime of institutional bribery.

(a) When National Travel Service has transferred the shares of Taikang Company to ease the financial strain, and communicated with the President of Taikang Company, Chen X, and Wu Mart Group decided to acquire and negotiate with the China Travel Service. Consistently, no third party participated in the equity acquisition, there was no exclusion of other buyers and a competitive advantage. The transactions between the two parties did not violate the principle of fairness. (b) In the absence of third party participation and the parties' willingness to reach the acquisition intention, Wu Mart Group promised to grant the benefit fee not for illegitimate interests. (c) The China Travel Service Headquarters transferred the shares of Taikang Company to Wu Mart Group and the specific transfer price, etc., all of which were discussed and decided by the joint meeting of the Party and Government leaders of the China Travel Service Headquarters. The final transaction price of both parties was also advanced in the China Travel Service. Within the determined price range, Wu Mart Group did not receive illegitimate interests, and the interests of China Travel Service were not damaged. (d) Zhao X, as the director of the general manager's office of the China Travel Service, only played a communication role in the equity transaction process, and did not seek illegitimate interests for the Wu Mart Group. Considering the above situation comprehensively, it can be concluded that the behavior of Wu Mart Group is not serious in the circumstances, and the conduct of the company does not constitute a crime of institutional bribery.

(3) The payment of RMB 5 million yuan to Li X (C)'s company by Wu Mart Group does not constitute an institutional bribery.

A. When Guangdong Utrust Company intends to transfer shares, it is Chen X (A) who has proposed to Liang X to enable Wu Mart Group to acquire the shares, and Zhang Wenzhong was requested to give Liang X a benefit fee of RMB 5 million yuan. Therefore, before the equity transfer, the benefit fee to Liang X was proposed by Chen X (A), and Zhang Wenzhong only passively accepted Chen X (A) request.

B. The evidences at hand have ascertained that Liang X did not agree to the transfer price proposed by Wu Mart Group, and Liang X also proposed to transfer the shares at a price higher than the bidding price; the final equity transaction price paid by Wu Mart Group to Guangdong Utrust Company has gone through repeated negotiations. Therefore, Liang X is said to have provided no assistance to Wu Mart Group in the process of equity transfer, and Wu Mart Group has not obtained any illegitimate benefits.

C. The evidences at hand have also been ascertained that after concluding the equity transfer agreement, Wu Mart Group has not paid a benefit fee of RMB 5 million yuan, to Liang X, and Liang X has made no mention of the matter. Until a few months later, to no knowledge of Liang X, Li X (C) demanded RMB 5 million yuan through Chen X (A) from Zhang Wenzhong, and Zhang

Wenzhong arranged for Zhang X (A) to have transferred the money to Li X (C)'s company account. When Liang X finally learned of the payment, he explicitly stated that he had nothing to do with the matter and refused to accept any money. The payment of RMB 5 million yuan by Wu Mart Group has been occupied by the Li X (C)'s company since then. Therefore, after the equity transfer, RMB 5 million yuan paid by Wu Mart Group is said to be demanded by Li X (C), no subjective intent to pay bribes for illegitimate interests has ever been recognized on the behalf of Wu Mart Group.

To sum up, the defense by the accused Zhang Wenzhong and defense opinions by his defender, the opinion from the institution, Wu Mart Group, that RMB 300,000 yuan was to reimburse Zhao X for the labor remuneration runs contrary to the ascertained facts and evidences, and it is not to be accepted by this court; the opinion by the Supreme People's Procuratorate inspectors that RMB 300,000 yuan awarded to Zhao X as a benefit and that Wu Mart Group was the subject to acquire the Taikang Company's shares are well justified and is to adopted by this court.

3. **With Regard to the Crime of Misappropriation of Funds**

In March 1997, the accused Zhang Wenzhong and the President, Chen X, of Taikang Company Chen and the President, Tian X (A), of the Zhongqi Company agreed to use RMB 40 million yuan of Taikang Company to purchase new shares for profit. On March 27 of the same year, RMB 40 million yuan from Taikang Company was transferred to the stock account in Beijing Fangzhuang Business Department of Cathay Securities Corporation opened by the Custer Investment Consultancy (renamed from Custer Economic Evaluation Center), an affiliated company of Wu Mart Group. Zhang X (A) was put in charge of the stock purchases according to the arrangement of Zhang Wenzhong. In order to avoid risks, the Finance and Accounting Department of Taikang Company executed a commission contract for investment in government bonds and a mortgage contract with Custer Investment Consultancy. In July of the same year, owing to the inspection by the People's Bank of China, Zhang Wenzhong, Chen X (A) and Tian X (A) agreed to transfer RMB 50 million yuan from Taikang Company to HITIC Company, which is also administered by Zhongqi Company. HITIC Company transferred RMB 40 million yuan to the account of the Custer Investment Consultancy to repay the previously borrowed RMB 40 million yuan to Taikang Compnay. On August 19 of the same year, the Custer Investment Consultancy returned RMB 40 million yuan to Taikang Company. On September 3 and September 9 of the same year, the Custer Investment Consultancy and Henan CITIC Company returned a total of RMB 50 million yuan to Taikang Company.

The above facts have been substantiated by the a commission contract for investment in government bonds (treasury bonds), a mortgage contract, transfer cheque, money order, bank-in slip (Collection Notice), accounting vouchers, cash flow invoices and other documentary evidence, the testimonies made by the witnesses Chen X (A), Tian X (A), Zhang X (A), Li X (D), Wu X, Ren X, Shi X and et al., as well as the confessions made by Zhang Wenzhong, all of which have been confronted and confirmed in the first instance.

On the basis of the accused Zhang Wenzhong's defense and defense opinions of his defender on the crime of misappropriation of funds, as well as the opinions issued by the Supreme People's Procuratorate prosecutors, together with the reexamined facts and evidences, this court makes the following overarching evaluations.

The original judgment found that the fact that Zhang Wenzhong and other people have misappropriated RMB 40 million yuan from Taikang to purchase new shares for profit, and then used RMB 50 million yuan to make the repayment to cover up the facts is justified, but it is unclear and there is insufficient evidence that Zhang Wenzhong and Chen X (A) and Tian X (A) have misappropriated the funds of Taikang Company for personal use and for personal gain.

(1) All the documentary evidences in the case at hand have indicated that the funds involved are transferred between the institutions, reflecting the cash flow between the institutions, and there is insufficient evidence to prove that the funds are used by individuals.

A. All the transfer checks, bank-in slips (collection notice), accounting vouchers, cash flow invoices and other documentary evidence have confirmed: On March 27 of 1997, RMB 40 million yuan from Taikang Company was transferred to the stock account in Beijing Fangzhuang Business Department of Cathay Securities Corporation opened by the Custer Investment Consultancy, an affiliated company of Wu Mart Group, and was later transferred to the stock trading account of the Custer Investment Consultancy in Beijing Fangzhuang Business Department of Cathay Securities Corporation. On August 19 of the same year, RMB 40 million yuan was transferred back to the Taikang Company from the stock trading account of the Custer Investment Consultancy in Beijing Fangzhuang Business Department of Cathay Securities Corporation through Beijing Securities Registration Co. Ltd. and the Custer Investment Consultancy. The cash flow involved is always made between the accounts of the institutions.

B. The commission contract for investment in government treasury bonds, and mortgage contract signed between Taikang Company and the Custer Investment Consultancy, have objectively turned into the evidence of Taikang Company to lend RMB 40 million yuan to the Custer Investment Consultancy. When the People's Bank of China has determined after its inspection of Taikang Company that there is violation of regulations for the said RMB 40 million yuan, and urged Taikang Company to terminate the contract as soon as possible, Taikang Company, on the request by the decisions made by the President's Office, issued a letter to the Custer Investment Consultancy to terminate the commission contract for investment in government treasury bonds. The conduct is an act made between the institutions.

C. In order to cover up the violation of RMB 40 million yuan of funds, Taikang Company transferred RMB 50 million yuan to Henan CITIC Company, through which, to repay the previously appropriated RMB 40 million yuan. The said money or funds are still flowing between the institutions.

(2) There is no sufficient evidence to prove that the misappropriated money or funds is for personal benefit or gain.

A. The accused Zhang Wenzhong and the witnesses Chen X (A) and Tian X (A) admitted during the investigation stages that any profit from the stock transactions by the purchase of new shares with the appropriated money was to be distributed proportionately among the three, but Zhang Wenzhong and Chen X (A) have refused the admissions they have made during the review period for prosecution and the first instance trial, claiming that the purchase of new shares is for the benefit of their respective companies, not for personal gain. Thus results the discrepancies between the earlier and later confessions or admissions.

B. The fact recognized in the original judgment that Zhang Wenzhong and others had earned a total profit of more than RMB 10 million yuan by misappropriated RMB 40 million yuan of Taikang Company to purchase new shares was inconsistent with the evidences at hand. The customer accounting vouchers (Deposit and Withdrawal) of Beijing Fangzhuang Business Department of Cathay Securities Corporation indicated that when the first payment of RMB 40 million yuan was withdrawn on August 19, 1997, the balance in the account of the Custer Investment Consultancy is RMB 9335 yuan, and when the second payment of RMB 40 million yuan was withdrawn on September 3 of the same year, the balance in the account is RMB 4.23 million yuan. As there is lack of such evidence as the transaction record of the stock account of the Custer Investment Consultancy, it remains dubious whether the above balances can be thought of the profit from the purchase of new shares; even if the stock transactions are profitable, there is a big difference between the amount of profit determined by the original judgment.

C. As there is lack of such evidence as the transaction record of the stock account of the Custer Investment Consultancy, it remains unclear and uncertain how cash flows and how the specific stock transactions are handled. In addition, there is no evidence to prove that Zhang Wenzhong has acquired the possession of the profit/gain from the stock transactions of new shares.

To sum up, the defense of Zhang Wenzhong and the defense opinions made his counsel that the conduct of Zhang Wenzhong may not constitute the crime of misappropriation of funds for personal use have been established and will be sustained by this court. The opinions submitted by the Supreme People's Procuratorate that Zhang Wenzhong's conduct of misappropriated RMB 40 million yuan of Taikang Company for personal gain constituted crime but has gone beyond the prescriptive period cannot be sustained and is to be rejected by this court.

The Court holds, when the Wu Mart Group applied for the National Key Technological Renovation Projects via National Debt Interest Discount, the policy of subsidized interest discount for the these projects has been adjusted. The private enterprises are eligible for application, and the logistics projects and information projects by the Wu Mart Group fall within the State's key project fund support, which

is also in line with the country's economic development and industrial policies at the time. In the process of applying for the projects, the accused Zhang Wenzhong and Zhang Weichun have not implemented the fraudulent acts of inventing facts and concealing the truth to defraud the money from the government's subsidized interest discount projects, though there are certain breaches of government regulations. In the process of application, the subjective intent of illegal possession of RMB 31.9 million yuan of the National Key Technological Renovation Projects via National Debt Interest Discount has been found nonexistent, which does not meet the constituent elements of the crime of fraud. Therefore, the original judgment that Zhang Wenzhong and Zhang Weichun's conduct constituted a crime of fraud were adjudged by this court to be a mistake in the fact-finding and application of laws, which is to be corrected according to law. RMB 300,000 yuan that was given by Wu Mart Group to Zhao X as a benefit fee after the acquisition of the shares of Taikang Company owned by China Travel Service cannot be said to be for the purpose of seeking illegitimate benefits, nor for serious circumstances, which cannot meet the constituent elements of the institutional bribery crime; The requested payment of RMB 5 million yuan to Li X (C)'s Company after Wu Mart Group has acquired the shares of Taikang Company held by Guangdong Utrust Company, was no subjective intent for the bribery for the purpose of seeking improper benefits, and it did not meet the constituent elements of the unit/institutional/institutional bribery. Thus, the conduct by Wu Mart Group does not constitute a crime of unit/institutional/institutional bribery, and Zhang Wenzhong, as the person in direct charge of Wu Mart Group, should not be held criminally liable for the crime of unit/institutional/institutional bribery. The original judgment that the conduct of Wu Mart Group and Zhang Wenzhong constitute a unit/institutional/institutional bribery is adjudged by this court to be a mistake in the fact-finding and application of laws, which is to be corrected in accordance with law. The submitted evidences have substantiated that Zhang Wenzhong has colluded with Chen X (A) and Tian X (A) and made use of the convenience of Chen X (A)'s position in Taikang Company to have transferred RMB 40 million yuan to the stock trading account of the Custer Investment Consultancy for profit-making activities, but the facts and the evidences will not justify the original judgment that Zhang Wenzhong has misappropriated funds for personal use and for personal gain. Thus the original judgment that Zhang Wenzhong's conduct constitutes a crime of misappropriation of funds is held to be a mistake in fact-finding and the application of laws, which is to be corrected in accordance with law.

In all, the defense by the accused Zhang Wenzhong and Zhang Weichun, the defense opinions by their defenders, the opinion by the litigation representative of Wu Mart Group, and the opinion submitted by the prosecutors from the Supreme People's Procuratorate on the acquittal of Zhang Wenzhong, Zhang Weichun and Wu Mart Group are established and adopted by the court. In accordance with Article 245 paragraph 1, Article 225, paragraph 1 (b), (c) of the *Criminal Procedural Law of the People's Republic of China*, and Article 389, paragraphs 1 (c), (d), paragraph 2 and Article 445 of the *Judicial Interpretation by the Supreme Court's Court of Applying the Criminal Procedural Law of the People's Republic of China*, and after

deliberation of the Judicial Committee of the Supreme People's Court, we make the following judgement:

1. The Criminal Judgment of the Higher People's Court of Hebei Province (2008), Hebei Crim. Final No. 89, and the Criminal Judgment of the Intermediate People's Court of Hengshui City of Hebei Province (2008), Hengshui, Crim. Trial, No. 22 shall be vacated and reversed;
2. The accused Zhang Wenzhong was found not guilty;
3. The accused Zhang Weichun was found not guilty;
4. The accused institution Wu Mart Holding Group Co. Ltd. was found not guilty; and
5. The fines and property recovered after the original judgment has been executed shall be returned in accordance with the law.

This decision is final.

Presiding Judge: Sun Huapu
Judge: Guan Yingshi
Judge: Qi Su
Judge: Dong Zhaoyang
Judge: Zhou Qing

May 30, 2008
Assistant Judge: Deng Liang
Assistant judge: Sun Zizhong

Court Clerks
Clerk: Xiu Junyan
Clerk: Liu Muhua

Relevant legal provisions

The Criminal Procedure Law of the People's Republic of China

Article 245 Where a People's court retries a case under the trial supervision procedure, a new collegial panel shall be formed if the retrial is conducted by the original trial court. If the case is originally tried by a court of first instance, it shall be retried under procedures at first instance and the sentence or ruling rendered may be appealed or pretested. If the case is originally tried by a court of second instance or is a case directly retried by a people's court at a higher level, it shall be retried under procedures at second instance and the sentence or ruling rendered shall be final.

When a people's court retries a case in a court session, the people's procuratorate at the same level shall appoint procurators/prosecutors to attend the court.

Article 225 After hearing a case of appeal or protest against a judgment of first instance, a people's court of second instance shall handle it in one of the following manners in light of the different situations:

(1) If the original judgment was correct in the determination of facts and the application of law and appropriate in the meting out of punishment, the people's court shall order rejection of the appeal or protest and affirm the original judgment.
(2) If the original judgment contained no error in the determination of facts but the application of law was incorrect or the punishment was inappropriately meted out, the people's court shall revise or renew the judgment.
(3) If the facts in the original judgment were unclear or the evidences insufficient, the people's court may revise or renew the judgment after ascertaining the facts, or it may rescind the original judgment and remand the case to the people's court which originally tried it for retrial.

Where a defendant appeals or the people's procuratorate presents a protest after the original trial court renders a sentence for a case remanded for retrial under item (3) of the preceding paragraph, the people's court of second instance shall render a sentence or order in accordance with law and may not remand the case again to the original trial court for retrial.

The Judicial Interpretation of the Supreme People's Court on the Application of the Criminal Procedure Law of the People's Republic of China

Article 389 after retrial, retrial cases shall be dealt with separately according to the following circumstances:

(1) If the original judgment, the ruling and the applicable law are correct, and the sentencing is appropriate, the grievance or protest shall be dismissed and the original judgment or ruling shall be upheld;
(2) The original judgment or ruling is accurate and the sentencing is appropriate, but if there is any defect in the determination of the facts or the applicable law, it shall be decided to correct and maintain the original judgment and ruling;
(3) If the original judgment or ruling determines that the facts are correct, but the applicable law is wrong, or the sentencing is improper, the original judgment or ruling shall be revoked and the judgment shall be changed according to law;
(4) In the case tried in accordance with the second-instance procedure, if the original judgment or the ruling is unclear or the evidence is insufficient, the judgement may be revised or renewed after further facts are ascertained, or the original judgment may be revoked and remanded to the people's court of the original trial for retrial. If the original judgment or ruling is unclear or the evidence is insufficient, if the facts have been found out, the facts shall be judged according to the facts newly ascertained; if the facts cannot be ascertained and the evidence is insufficient, the defendant cannot be found guilty, the original judgment or ruling shall be reversed, the accused shall be declared not guilty.

Article 345 If all or part of the property penalty is revoked, the property that has already been executed shall be returned to the person subject to execution in whole or in part; if it cannot be returned, it shall be duly compensated in accordance with law.

Hot Cases

Chongqing Haoyun Real Estate Development Co., Ltd. v. Owners' Committee of Dijing Hoayuan, Xipeng, Jiulongpo District, Chongqing (Dispute over Parking Spaces)—Parking Spaces Occupying Roads or Other Places Jointly Owned by the Owners are Subject to Common Ownership by the Owners

Yongfeng Pan

Rule

The Developer, when developing the community, paid the fees for the grant of land use rights within the construction area, thus becoming the holder of construction land use rights. Upon completion of the community, the land use rights within the construction area of the community, along with the sale of the housing within the community, are also transferred to the owners of the community. The land use rights to the common areas of the community shall be jointly owned by the owners of the community, so those ground parking spaces which cannot be registered as owned by specific owner to become an exclusively-owned area with separate ownership are parking spaces occupying roads or other places jointly owned by the owners for parking cars, and, subject to Article 74 of the *Property Law*, shall be jointly owned by the owners.

Collegial panel judges of the Supreme People's Court for re-trial: Pan Yongfeng, Wang Jijun, Wang Dan (Written by: Pan Yongfeng, Supreme People's Court; Translated by: Niu Benlin).

Y. Pan (✉)
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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_5

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellant in the second instance): Chongqing Haoyun Real Estate Development Co., Ltd. (hereinafter referred to as "Haoyun Real Estate")
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): Owners' Committee of Dijing Hoayuan, Xipeng, Jiulongpo District, Chongqing (hereinafter referred to as "Dijing Haoyuan Owners' Committee")

2. Procedural History

First Instance: No. 00862 [2015], Trial, Civ. Division, Chongqing No. 5 Intermediate People's Court (dated Dec. 10 of 2015)
Second Instance: No. 7 [2016], Final, Civ. Division, Chongqing Higher People's Court (dated Dec. 28 of 2016)
Application for Retrial: No. 2817 [2017], App. Ruling, Civ. Division, the Supreme People's Court (dated Aug. 24 of 2017)

3. Cause of Action

Dispute over parking spaces

Essential Facts

In March 2007, Haoyun Real Estate obtained state-owned land use rights of the community at issue, covering a total area of 76,337 square meters. Thereafter, Chongqing Planning Bureau issued a Construction Project Planning Permit to Haoyun Real Estate, allowing it to construct the ground parking spaces at issue, but the Permit does not calculate the ground parking spaces in the construction area. Haoyun Real Estate acknowledged that all the approximately 270 ground parking spaces cannot be handled by going through formalities for title registration. On March 27, 2015, when Haoyun Real Estate intended to lease some of the parking spaces, the Owners' Committee of Dijing Haoyuan posted notice for objection in the community, and failed to reach an agreement with Haoyun Real Estate through consultation.

Haoyun Real Estate then filed a lawsuit with the court of first instance pleading it to: lawfully confirm that the title to the 393 ground parking spaces (which totals RMB 1.179 million, with each parking space valued at RMB 30,000) planned to park cars within the construction area of Dihao Jingyuan shall be owned by Haoyun Real Estate. Dijing Haoyuan Owners' Committee claims that: the ground parking spaces of the community, instead of belonging to Haoyun Real Estate, shall be jointly owned by the owners of the community. With regard to the land within the building area of the community, the owners, pursuant to law, jointly enjoy the construction land use rights, therefore the ground parking spaces on the land jointly owned by the owners

shall be subject to common ownership by all the owners. The parking spaces are not calculated in the plot ratio, so the title thereto shall be jointly owned by all the owners. The court of first instance rendered a judgment on December 10, 2015, dismissing all the claims of Haoyun Real Estate. Unsatisfied with the judgment of the court of first instance, Haoyun Real Estate lodged an appeal and court of second instance rendered a judgment on December 28, 2016, dismissing the appeal and sustaining the original judgment. Haoyun Real Estate filed a petition to the Supreme People's Court of the People's Republic of China for retrial, pleading the Court to revoke the judgment of the court of second instance, issue a certiorari, and support its claims.

Issue(s)

Are the ground parking spaces jointly owned by the owners if they cannot become exclusively-owned areas through title registration?

Holding

Upon review, the Supreme People's Court finds that: Article 142 of the *Property Law*, instead of Paragraph 2 of Article 63 of the *Regulations of Chongqing Municipality on Realty Management*, shall be applicable to Haoyun Real Estate's claim for wrongful application of law by the original judgment in its application for retrial. Article 142 of the *Property Law* provides that: "the holder of construction land use rights is entitled to the ownership of the buildings, constructions and auxiliary facilities thereof constructed by the holder, unless any contrary evidence proves otherwise." Paragraph 2 of Article 63 of the *Regulations of Chongqing Municipality on Realty Management* provides that: "(t)he construction entity may, after lawfully obtaining title registration of parking spaces or garages, sell the parking spaces or garages to the owners. If the number of parking spaces or garages to be sold is the same or less than the number of apartments within the area of realty management, each household owner can only purchase one parking lot or garage." The two provisions are not contradictory. As Haoyun Real Estate sells housing to the owners of the community, the land use rights within the community are also transferred to the owners of the community, so the land use rights of the jointed owned land of the community shall be jointly owned by the owners of the community. Therefore, Haoyun Real Estate's claim that the ground parking spaces at issue shall belong to it pursuant to Article 142 of the Property Law cannot be established. The original judgment's application of Paragraph 2 of Article 63 of the *Regulations of Chongqing Municipality on Realty Management* intends to clarify that only when the construction entity obtains title registration of parking spaces or garages can it sell, but it is not capable of obtaining title registration of the parking spaces or garages at issue, so it cannot sell. Therefore, it is not inappropriate for the original judgment to apply Paragraph 2 of Article 63 of

the *Regulations of Chongqing Municipality on Realty Management*, and Haoyun Real Estate's application for retrial due to the original judgment's wrongful application of law cannot be established and cannot be supported.

Pursuant to Article 2(1) of the *Interpretation of Several Issues Concerning the Specific Application of the Law in Disputes over the Partitioned Ownership of Buildings*, which provides that "premises within a developed area that satisfy the following conditions, as well as parking spaces, booths and other such specific spaces shall be deemed exclusively-owned parts as mentioned in Chapter VI of the *Property Law*: (1) they are independent in structure and can be clearly distinguished; (2) they are independent in use and can be used to the exclusion of others; and (3) they are capable of being registered as the object of the ownership of a specific owner", the parking spaces at issue are not capable of obtaining title registration, therefore, cannot become exclusively-owned areas. Although Haoyun Real Estate has, in developing the Dijing Haoyuan community, paid the fees for the grant of land use rights within the construction area, thus becoming the holder of construction land use rights, the land use rights within the construction area after the construction of the community have been transferred with the sale of the housing of the community, then the land use rights of the jointly-owned areas of the community shall be jointly owned by the owners of the community. Because the parking spaces at issue are not capable of obtaining title registration and becoming exclusively-owned areas, it is not inappropriate for the original judgment to ascertain that those parking spaces are parking spaces occupying roads or other places jointly owned by the owners for parking cars. It is a fundamental obligation of the developer to pass the acceptance check with regard to the constructed community, and whether the greening has exceeded the planning area is not necessarily linked with the finding that the parking spaces have occupied the place jointly owned by the owners. Therefore, Haoyun Real Estate's cause for retrial that the finding of the original judgment, i.e., the parking spaces at issue are parking spaces occupying roads or other places jointly owned by the owners, lacks factual basis cannot be established. The conclusion reached by the court of first instance and court of second instance are correct and shall be supported. The Supreme People's Court rules to dismiss Haoyun Real Estate's application for retrial.

Comment on Rule

Dispute over ownership of parking spaces, mostly between developers and owners of the community, concerns developer's huge economic interests and the owners' basic daily needs. Developers tend to hold that parking spaces shall be owned by the developers because they are financed and constructed by them after obtaining land use rights by paying corresponding fees for the grant of land use rights, and passing the construction planning. On the other hand, the owners of the community argue that parking spaces shall be jointly owned by all the owners because the parking spaces, as ancillary facilities for the purchase of commercial housing, are constructed on the

jointly-owned roads of the community. From courts' trial practices across the country, different views exist on the determination of the ownership of parking spaces, which has currently become one of the hot and difficult issues in civil and commercial trials. This case is typical in that the dispute at issue is over the ownership of ground parking spaces. To correctly determine the ownership of ground parking spaces, the following issues shall be taken into full consideration:

1. **The key factor in determining the ownership of ground parking spaces is whether the parking spaces can be recognized as the exclusively-owned areas of the buildings referred to in the *Property Law*.**

In economic life, a developer's obtaining land use rights of the land for the construction of the community by paying the fees for the grant of land use rights does not necessarily mean that they enjoy the ownership of ground parking spaces as of right, because, in the sale of the apartments to the owners after completion of the commercial housing, the developer also transfers to the owners the land use rights within the area occupied by the housing, together with other rights to use the jointly owned land. And the developer's obtaining of construction planning permit alone cannot be used to determine that it enjoys the ownership of ground parking spaces as of right. It is one duty of the developer to construct corresponding ancillary facilities in its development of commercial housing, such as roads, green space, parking spaces, etc. within the community. Article 73 of the *Property Law* provides "roads within the building area, except for municipal public roads, are jointly owned by the owners. Green space within the building area, except for municipal public green space or green space explicitly provided to be privately owned by individuals, shall be jointly owned by all the owners. Other public spaces, common facilities and premises used for realty management services within the building area shall be jointly owned by all the owners." Accordingly, roads and green space of the community obtaining construction planning are jointly owned by the owners, so whether it falls within "construction planning" alone cannot be used to determine the ownership of ground parking spaces.

The key to whether the developer can separately retain the ownership of the parking spaces when transferring the commercial housing to the owners is whether the parking spaces can be regarded as the exclusively-owned areas of the buildings as referred to in the *Property Law*, thus possible to become the object of partitioned ownership of specific owners. Pursuant to Article 74 of the *Property Law*, the parking spaces or garages within the building area planned for parking cars shall first meet the needs of the owners. The ownership of the parking spaces or garages within the building area planned as vehicle parking spaces shall be agreed upon by the relevant parties in regard to their sale, complimentary use or leasing, etc. Parking spaces occupying roads or other areas jointly owned by all owners shall be under the joint ownership of all the owners. Only when the parking spaces can become the object of ownership of specific owners, can the relevant parties agree on their ownership.

Although partitioned ownership may be labeled differently in various countries and scholarly writings, its essence remains the same, i.e., abstract generalization of the form of real estate ownership established by taking specific part of a building

as its object. Partitioned ownership of buildings is a composite right, comprised of the rights of the owners of exclusive ownership, common ownership and partitioned ownership to manage the buildings and residents living in the buildings. By virtue of Article 70 of the *Property Law*, which provides "(a)n owner is entitled to the ownership of the exclusively-owned areas including residential premises or premises used for business purposes within a building, and to the common ownership and management over the common areas of the building other than the exclusively-owned areas," partitioned ownership of buildings in China adopts a triarchic theory of partitioned exclusive ownership, partitioned common ownership and membership right. Partitioned exclusive ownership, which is to distinguish the owner's ownership of the exclusively-owned areas, is known as "independent soul" of the partitioned ownership because it is a premise for the obtaining of all other rights.

The object of partitioned exclusive ownership is to distinguish the exclusively-owned areas of the building owned, and, pursuant to Article 2(1) of the *Interpretation of Several Issues Concerning the Specific Application of the Law in Disputes over the Division of Ownership of Buildings*, the parking space that is capable of being registered as the object of the ownership of a specific owner is possible to be determined as the exclusively-owned areas. Then the premise to whether it can be registered as the object of the ownership of a specific owner, i.e., whether an independent certificate of ownership can be obtained, lies in that the gross floor area of the parking space must have corresponding share in land use rights. This is the roots for courts' repeated emphasis in the first instance and second instance on the issue of floor area ratio.

2. **Importance of the standard of floor area ratio in determining the ownership of ground parking spaces**.

The floor area ratio, as a term in construction, means the ratio of a building's gross floor area to the size of the piece of land upon which it is built. In principle, only the building that calculates the floor area ratio can obtain area share to the land use rights of corresponding land number. When the developer, upon completion of the construction project, applies to the registration agencies for initial registration of the real estate, the gross floor area of the building not calculating the floor area ratio is not apportioned with any area share to the land use rights, so it is impossible for it to have separate housing ownership and land use rights, which can only be attached to the gross floor area of the building calculating the floor area ratio. In its sale of the commercial housing, the developer undoubtedly transfers to the owner the land use rights corresponding to the gross floor area of the commercial housing, together with the rights of the building not calculating floor area ratio that can only be attached to the building calculating the floor area ratio, which will be under the common ownership of all the owners, and their developing costs is correspondingly apportioned to the sales price of each commercial housing. So the prerequisite for the ground parking space to obtain certificate of title is that its gross floor area must have corresponding share to the land use rights, commonly known as calculating the floor area ratio. Then the developer can in its sale of the commercial housing retain separate ownership to corresponding parking space.

On a last note, the issue in this case is the dispute between the developer and the owners of the community over the ownership of ground parking spaces, one important factor in which is the floor area ratio. However, the floor area ratio shall not as a matter of cause by analogy be applied to determine the ownership of underground parking spaces. As mentioned before, with regard to ground parking spaces, calculating the floor area ratio means that its gross floor area is apportioned with a share in land use rights, so whether calculating the floor area ratio is vital for the determination of the ownership of ground parking spaces. On the other hand, underground garage is special in its use of certain space under the ground. In practical terms, most departmental rules and local regulatory documents currently in force stipulate that underground garage, non-operational stilt floor, etc. are not calculated in the floor area ratio, but some local legislation also acknowledge that underground space that can be lawfully and independently used can be determined to have independent right to land. Therefore, determining the ownership of underground garage cannot take as its standard the calculation of floor area ratio, because it is possible for lawful right to land to exist even though it is not calculated in the floor area ratio, and only with lawful land use rights can underground garage become the object of partitioned exclusive ownership.

Given the social sensitivity of the dispute between the developers and the owners over the ownership of parking spaces, it is of great social impact and profound social significance to correctly determine the ownership of parking spaces and adequately reflect guarantee by law of legal titles.

Representative Cases

The People v. Zhang X (A) (Illegal Pooling of Public Deposits)—Determination of the Actor's Identity in Illegal Pooling of Public Deposits and Its Amount

Baojun Dong

Rule

Article 1(2) of the *Interpretation of the Supreme People's Court of Several Issues on the Specific Application of Law in the Handling of Criminal Cases about Illegal Fund-raising* stipulates the circumstances for not incriminating "whoever does not make public advertisement to the society, only pooling funds from specific targets such as relatives and friends", but his relatives and friends will be included in the social public if the actor also makes public advertisement to the social public, then the corresponding part of the pooled funds shall be included in the amount of illegal pooling of public deposits. If at the outset the actor only pools funds from specific targets such as relatives and friends, and then gradually from the social public, or at the outset pools funds from the social public, and then gradually from specific targets such as relatives and friends, a distinction shall be made as to specific circumstances, and it is not appropriate to include funds pooled from specific targets such as relatives and friends in the total amount of illegally pooled funds.

Article 3 of the *Interpretation* clarifies the conviction and sentencing standards for the crime of illegal pooling of public deposits, which shall be taken full consideration in finally determining the appropriate sentencing when the actor concurrently meets several circumstances as listed in this Article.

Article 4(2) of the *Interpretation* stipulates that different actors in the joint commission of illegal pooling of funds shall be convicted by their subjective intents and those without the purpose of illegal possession shall not be convicted of the crime of illegal fund raising by fraudulent means.

Collegial panel judges of the Supreme People's Court for re-trial: Liu Heting, Yin Ze, Guo Xuejun (Written by: Dong Baojun, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_6

Case Information

1. Parties

Public prosecuting agency: People's Procuratorate of Fanshi County, Shanxi Province
The accused (Appellant in the second instance, Applicant in the retrial): Zhang X (A)

2. Procedural History

First Instance: No. 014 [2012], Trial, Crim. Division, Fanshi People's Court of Shanxi Province (dated Dec. 10 of 2012)
Second Instance: No. 55 [2013], Final, Crim. Division, Yizhou Intermediate People's Court of Shanxi Province (dated Mar. 5 of 2013)
Application for Retrial: No. 231 [2016], Crim. Sup. Notice, the Higher People's Court of Shanxi Province (dated Sep. 22 of 2016)

3. Cause of Action

Crime of illegal pooling of public deposits

Essential Facts

In May 2006, Zhang X (A) joined Beijing Beautiful Mountains Forestry Development Service Center founded by Zhang X (B) (treated at a separate case). On December 3, 2007, Zhang X (A) registered and established Standing Trees Trading Service Station under Fanzhi County Jianjun Agriculture and Forestry Professional Cooperative in Fanshi County, Shanxi Province, serving as the station master and also as a trader. Thereafter, Yue X and Zhang X (C) became the traders of the station, publicizing and promoting standing trees' trading. In the name of the service station, Zhang X (A) has signed forest-based elderly care contracts with 28 people including Jin X, Li X and Ma X. As of August 2011, Zhang X (A) had illegally pooled deposits of RMB 1,217,500, of which RMB 67,500 were from relatives, and RMB 546,000 from the public, all of which has been refunded after case-filing. Trader Yue X (sentenced) of the service station has signed forest trading contracts with 13 people, illegally pooling deposits of RMB 574,000, all of which has been refunded after case-filing; Zhang C (prosecuted at a separate case) signed trading contracts with guaranteed profits with 28 people, illegally pooling deposits of RMB 451,700, of which RMB 415,700 has not been refunded. Yue X and Zhang X (C), as traders of the station, are responsible only for signing trading contracts with others, with deposit cards transacted by the bank under their names kept by Zhang X (A), deposits illegally pooled handed over to Zhang X (A), and their salary paid by Zhang X (A) pursuant to their respective transaction amounts.

The court of first instance rendered a judgment on December 10, 2012 that the accused Zhang X (A), convicted of illegally pooling of public deposits, is sentenced

to pay a fine of RMB 50,000, in addition to sentence of imprisonment for a term of 3 years. Unsatisfied with the judgment of the court of first instance, Zhang X (A) lodged an appeal and the court of second instance rendered a judgment on March 5, 2013, dismissing the appeal and sustaining the original judgment.

Issues

1. Whether the investment funds pooled by Zhang X (A) from his relatives and friends are included in the amount of illegally pooled public deposits;
2. Whether Zhang X (A)'s act meets the elements of the crime of illegal pooling of public deposits;
3. If the crime is constituted, how to apply sentencing standards to Zhang X (A).

Holding

Upon review in the retrial, the Supreme People's Court finds that: when promoting the so-called "Trading of Standing Trees", Zhang X (A) and the service station traders did recommend extensively relatives and friends to make investment, but the target of promotion was not limited to relatives and friends, but also to the unspecified objects in the society at large, falling under the act of "pooling funds from the public, that is, unspecified objects" as stipulated in Article 1(1)(i) of the *Interpretation of the Supreme People's Court of Several Issues on the Specific Application of Law in the Handling of Criminal Cases about Illegal Fund-raising*. As of August 2011, Zhang X (A) illegally pooled funds totaling RMB 1,217,500, of which RMB 671,500 from relatives and friends should not be deducted; in addition, traders Yue X and Zhang X (C) from Zhang X (A)'s service station, in the name of the service station, illegal pooled funds of RMB 574,000 and RMB 451,700 respectively, for which Zhang X (A) shall also assume corresponding liability because Zhang X (A), as the station master of the service station, is responsible for the management and coordination of the service station by handing over the illegally pooled funds to the headquarters on time and giving rewards to fund providers as agreed. Zhang X (A) does not have subjective intention to illegally possess the raised funds when participating in the illegal fund raising, so the original judgment does not find that his act constitutes the crime of illegal fund raising by fraudulent means. However, Zhang X (A)'s act of illegal absorption of public deposits through the so-called "Trading of Standing Trees", which has seriously undermined the state's financial management order, constitutes the crime of illegally absorption of public deposits. Although Zhang X (A) has returned all the funds illegally absorbed by him after the case-filing, not returned was RMB 415,700 illegally absorbed by other traders at the service station, for which Zhang X (A) shall also be criminally liable as the stationmaster of the

service station. Despite of the huge amount involved in Zhang X (A)'s participation in the illegal absorption of public deposits, it is not inappropriate for the trial court to impose a lighter punishment, taking into consideration such circumstances as his returning of absorbed funds to his friends and relatives. In summary, the Supreme People's Court dismisses the appeal.

Comment on Rule

1. **The nature of joint offenders shall be determined by the existence of illegal possession as its purpose, so the act of accused in this case constitutes the crime of illegally absorption of public deposits**.

Article 4(2) of the *Interpretation of the Supreme People's Court of Several Issues on the Specific Application of Law in the Handling of Criminal Cases about Illegal Fund-raising* clarifies that different actors in the joint crime of illegal fund-raising shall be convicted and punished subject to the existence of illegal possession as its purpose. Any actor who has illegally raised funds for the purpose of illegal possession shall be convicted and punished for the crime of illegal fund raising by fraudulent means; and any actor who has illegally raised funds not for the purpose of illegal possession shall be convicted and punished for the crime of illegal absorption of public deposits.

In this case, there are four levels in the series of cases of "Trading of Standing Trees" dominated by Zhang X (B), namely, "headquarters—district center station—service station—traders", in which Zhang X (A) serves as the stationmaster and trader of the Fanshi County Service Station. Zhang X (B) has raised a total of about RMB 270 million, of which RMB 44 million is paid for the cost of fund raising, RMB 59 million for real estate, commercial operations, stock trading, and personal squandering, only RMB 28 million for forest land investment, and still more than RMB 140 million remaining unaccounted for. Relevant facts and evidence prove that Zhang B, having obvious purpose of illegal possession, shall be convicted of and punished for the crime of illegal fund raising by fraudulent means. On the other hand, in the joint offense of illegal fund-raising, Zhang X (A), as the stationmaster of one service station under the headquarters, has paid return on investment on time pursuant to the investment contract signed with the investors, and all the funds absorbed were turned over after deducting the relevant management fees. Evidence in the case shows that Zhang X (A), unknown of Zhang X (B)'s criminal purpose and project operation and, unlike Zhang X (B), without subjective joint intent and act of illegal possession of raised funds, shall not be convicted of and punished for the crime of illegal fund raising by fraudulent means.

In the "Trading of Standing Trees", Zhang X (A) set up the service station and developed 8 other traders. In order to maintain the operation of the service station and get more commissions, he has his absorbed investment funds allocated under the name of other traders who do not perform well, and also provides convenience to

other two service stations in Fanshi County in using the official seal of the cooperative. By promoting the "Trading of Standing Trees" to friends, relatives, and villagers, Zhang X (A)'s service station illegally absorbed investment funds of more than RMB 1.7 million, of which Zhang X (A) has absorbed up to more than RMB 1.2 million, and, up until Zhang X (B)'s headquarters was seized in March 2011, he nevertheless instructed his fellow traders to continue to conduct business, causing most of the investment funds absorbed during this period unrecoverable. It is sufficient for evidence in the case to show that Zhang X (A) has the intention to illegally absorb public deposits.

Pursuant to Article 176 of the *Criminal Law*, whoever illegally or in disguised form absorbs public deposits and disrupts financial order commits the crime of illegal absorption of public deposits. Article 1(1) of the *Interpretation of the Supreme People's Court of Several Issues on the Specific Application of Law in the Handling of Criminal Cases about Illegal Fund-raising* provides a more detailed standard for this, specifying four conditions for illegal absorption of public deposits, namely, (1) "absorbing funds without lawful approval by relevant agencies or in the form of legitimate operations"; (2) "promoting to the public through media, promotion conferences, flyers, mobile phone text messages, etc."; (3) "undertaking to repay the principal with interest in the form of money, kind, equity, etc. within the prescribed time limit"; and (4) "absorbing funds from the public, i.e., unspecified objects from the public". Only when an act meets all of the above four conditions can it be considered as "illegal absorption of public deposits or absorption of public deposits in disguised form" as stipulated in Article 176 of the *Criminal Law*, except as otherwise provided by the *Criminal Law*.

In this case, although "Trading of Standing Trees" is a legitimate means of doing business, Zhang X (B) did not spend all the raised funds to forest management, and Zhang X (A) also did not actually transfer the forest rights to the investors. The contracts signed are deceiving, which in essence was illegally absorbing funds by legitimate means of operation. By such means as organizing other traders and investors to participate in the promotion meetings at the headquarters, and mouth-to-mouth communication by himself and other traders, Zhang X (A) publicly promotes the legitimacy and benefits of the "Trading of Standing Tree" to attract villagers, friends and relatives to make investment. The three modes of investment, namely becoming-rich forest, elderly-care forest and profit-guaranteed forest as declared by the headquarters all promise to repay principal with interest in the form of money within the prescribed time limit, but the cost of fund raising, including profits of the investor, commission of the traders and the service station, etc. in fact has far exceeded the monthly interest rate of two points. Zhang X (A) and his traders in the service station are actually absorbing funds from unspecified objects in the society. Therefore, Zhang X (A)'s act of "illegal absorption of funds by such means as entrusted management of transferred forest rights" fits squarely into the four conditions stipulated in the *Interpretation of the Supreme People's Court of Several Issues on the Specific Application of Law in the Handling of Criminal Cases about Illegal Fund-raising*, thus constituting the crime of illegal absorption of public deposits.

2. **Whether the investment funds absorbed from friends and relatives is included in the amount of illegally absorbed public deposits**.

Article 1(2) of the *Interpretation of the Supreme People's Court of Several Issues on the Specific Application of Law in the Handling of Criminal Cases about Illegal Fund-raising* provides: "(w)hoever absorbs funds from friends, relatives, or specified objects within the entity, instead of promoting to the public, does not commit the act of illegally or in disguised form absorbing public deposits." This provision, concerning the special case of "instead of promoting to the public, only absorbing funds from such specified objects as friends and relatives", is intended to conform to public sentiment, giving the perpetrators the opportunity to reconcile with their friends and relatives in case of limited scope of the act involved. It should be noted that any act of absorbing funds from "friends and relatives" does not necessarily fall outside the act of illegally or in disguised form absorbing public deposits.

In this case, because Zhang X (A) and the traders of the service stations illegally absorb funds mainly from other unspecified objects from nearby villages, Zhang X (A)'s friends and relatives, accounting for part of the funds raised, shall be included in the "unspecified objects from the society". "Trading of Standing Trees" in this case is intended to be open to unspecified person from the society and whoever agrees to the contract of the "Trading of Standing Trees" can make investment. At the same time, the legislative intent for the crime of illegal absorption of public deposits is to maintain normal order in financial management, but Zhang X (A)'s act has seriously disrupted such order, and Zhang X (A)'s friends and relatives invested in "Trading of Standing Trees" have with no exception been affected by the consequences of the disruption. Therefore, under such circumstance, the investors, being acquaintance of Zhang X (A) or Zhang X (A)'s relatives and friends or not, shall be regarded as "unspecified objects from the society", and the funds illegally absorbed by Zhang X (A) from his friends and relatives shall be counted as part of the amount involved in the crime of illegal absorption of public deposits.

It shall be noted that, if at the outset the actor only absorbs funds from specific objects such as relatives and friends, and then gradually from the social public, or at the outset absorbs funds from the social public, and then gradually from specific objects such as relatives and friends, a distinction shall be made as to specific circumstances, and it is not appropriate to include funds absorbed from specific objects such as relatives and friends in the total amount of illegally absorbed funds.

3. **How to sentence the perpetrator with dual identities in the crime of illegal absorption of public deposits**.

Article 3 of the *Interpretation of the Supreme People's Court of Several Issues on the Specific Application of Law in the Handling of Criminal Cases about Illegal Fund-raising* identifies the standard for the amount in sentencing the crime of illegal absorption of public deposits, and makes a distinction between individuals and entities. In sentencing Zhang X (A), the accused in this case, the consequences caused by him separately as the station master and a trader of the service station shall be fully taken into account. The following aspects are fully attended to in sentencing:

Firstly, Zhang X (A)'s illegally absorbed public deposits in the amount of RMB 1,217,500 as of August 2011 meets the threshold as provided in Paragraph 2 of Article 3 of the *Interpretation*, i.e., "any individual who illegally or in disguised form absorbed public deposits in the amount of more than RMB 1 million, or any entity who illegally or in disguised form absorbed public deposits in the amount of more than RMB 5 million", falls under "the amount involved is huge or other serious circumstances", and, pursuant to Article 176 of the *Criminal Law*, shall be sentenced to pay a fine of not less than RMB 50,000 nor more than RMB 500,000, in addition to a sentence of imprisonment for a term of not less than 3 years nor more than 10 years. Secondly, Zhang X (A), as the stationmaster of the service station shall also be liable for RMB 1,751,500 absorbed by the service station, as indicated in the service station's statement of investment. Pursuant to Paragraph 1 of Article 3 of the *Interpretation*, which provides "any individual who illegally or in disguised form absorbed public deposits in the amount of more than RMB 1 million, or any entity who illegally or in disguised form absorbed public deposits in the amount of more than RMB 5 million", Zhang X (A)'s service station has reached the incriminating standard for the crime of illegal absorption of public deposits. Paragraph 2 of Article 176 of the *Criminal Law* stipulates that "where an organization commits the crime of the preceding paragraph, the organization shall be sentenced to pay a fine, and person who are directly in charge and other persons who are directly responsible for the crime shall be punished pursuant to the provisions of the preceding paragraph." Accordingly, Zhang X (A) shall be sentenced to pay a fine of not less than RMB 20,000 nor more than RMB 200,000, only or in addition to imprisonment for a term of not more than 3 years or criminal detention.

Thirdly, Zhang X (A)'s refund of all the illegally absorbed sums after case filing to reduce the economic losses of the victims falls under of Paragraph 3 of Article 3 of the *Interpretation*, i.e., "the amount returned before and after the case filing can be taken into account as mitigating circumstances at court's discretion", so Zhang X (A) may be sentenced to a lighter punishment at court's discretion. However, by the time the case was heard by the court of first instance, there was still RMB 415,700 left to be refunded by Zhang X (C), a trader from Zhang X (A)'s service station, for which Zhang X (A), as the stationmaster of the service station, shall be liable. Based on the above factors, it is not inappropriate for the trial court to sentence Zhang X (A) to pay a fine of RMB 50,000, in addition to a sentence of 3 years' imprisonment. The Supreme People's Court is right in refusing to support Zhang X (A)'s claim that "he can be exempted from criminal punishment or his act shall not be treated as a crime" and dismissing the appeal of the case.

The People v. Yi X (Organizing, Leading and Participating in Terrorist Organization, Intentional Homicide)—Culpability of the Members of Terrorist Organizations and the Application of the Death Penalty

Xinjun Chen

Rule

A terrorist organization means a criminal organization composed of 3 or more persons for the purpose of carrying out terrorist activities. The criminal liability assumed by each member in a terrorist organization shall be determined on the basis of accurate distinction of the organizers, leaders, active participants, and other participants.

Crimes of terrorist activities are so harmful to the society that they shall be severely punished pursuant to law. The organizers, leaders, and key members of a terrorist organization shall be the key targets for severe punishment, and those who have committed extremely severe crimes and shall be sentenced to death pursuant to law shall be resolutely sentenced to death pursuant to law. However, those violent terrorists who have committed severe crimes that are not lawfully punishable by death penalty shall not be sentenced to death for mere emphasis on strictly cracking down on such crimes.

Collegial panel judges of Kunming Intermediate People' Court of Yunnan Province for the first instance: Wang Yong, Zhang Jun, Gu Yi. Collegial panel judges of the Higher People's Court of Yunnan Province for the second instance: Mei Yu, Ding Wanhu, Fan Liying. Collegial panel judges of the Supreme People's Court of Yunnan Province for review of death sentence: Zhang Jie, Duan Huang, Chen Xinjun (Written by: Chen Xinjun, Supreme People's Court; Translated by: Niu benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_7

Case Information

1. **Parties**

The accused: Yi X (A)
The accused: Tu X
The accused: Yu X (A)
The accused: Pa X

2. **Procedural History**

First Instance: No. 88 [2014], Trial, Crim. Division, Kunming Intermediate People's Court of Yunnan Province (dated Sep. 12 of 2014)
Second Instance: No. 1377 [2014], Final, Crim. Division, the Higher People's Court of Yunnan Province (dated Oct. 31 of 2014)
Review of Death Sentence: No. 12803065 [2015], Rev., Crim. 2nd Division, the Supreme People's Court (dated Mar. 10 of 2015)

3. **Cause of Action**

Crime of organizing, leading and participating in terrorism organization, intentional homicide

Essential Facts

Affected by religious extreme thoughts, since December 2013, Yi X (A), Tu X, Yu X (A), Pa X, A X (A), Mang X, A X (B), Yu X (B), Ba X, Ai X (B), Sa X and others, for the purposes of illegal emigration and committing violent terrorist activities, have gathered together to engage in such activities as leader voting, physical training, preparation of dangerous weapon in such places as Guangzhou and Zhuhai of Guangdong Province, Nanyang of Henan Province, and Gejiu of Yunnan Province, gradually forming a terrorist organization. Yi X (A), elected as deputy leader in Nanyang, has repeatedly played audio and video clips of religious extremism and violent terrorism to members of the organization, proclaiming religious extremism and violent terrorism thoughts; Tu A has provided financial support for the organization for several times; and Yu X (A) has invited Tu X and Yu B to join the organization and provide funding for the activities.

After unsuccessful attempt for illegal emigration, Yi X (A), Tu X, Yu X (A), Pa X, A X (A), Ai X (A), A X (B), Mang X and others were gathering several times in late February 2014 in Shadian District, Gejiu, Yunnan Province to collude and plan to carry out violent terrorist activities in the crowded Kunming Railway Station or Gejiu Railway Station by means of homicide with knives, with Tu X providing funds for purchasing long knives and short knives as tools for the crime, and Pa X and others making two terrorism banners.

On the 27th of the same month, Yi X (A), Tu X, and Yu X (A) were arrested in Shadian District, Gejiu on suspicion of illegally crossing the state border. After being arrested, Yi X (A), Tu X, and Yu X (A) concealed the violent terrorist activities to be carried out by the members of the organization. On March 1st of the same year, unable to get in touch with Yi X (A) and the others, A X (A), Ai X (A), A X (B), P X, and Mang X decided to carry out violent terrorist activities in Kunming Railway Station that day as planned. At about 17:30, the 5 person started out from Shadian in a rented car, carrying the tools for the crime, and arrived at Kunming Railway Station at about 20:30. At about 21:12, starting from the temporary waiting area of Kunming Railway Station, through the Front Square, Second Booking Area, Booking Office, Small Luggage Depository, and other places, the 5 person flagged the banners and indiscriminately killed innocent people with the knives, which has resulted in 31 deaths and 141 injured, 40 of whom were seriously injured. Resisting the arrest, Pa X was injured by police's shooting and arrested, A X (A), Ai X (A), A X (B) and Mang X were shot to death by the police on the spot.

In the first instance, Yi X (A), Tu X, and Yu X (A) should be sentenced to death for intentional homicide, deprived of political rights for life; and sentenced to life imprisonment for organizing and leading terrorist organization, deprived of political rights for life, and it is decided to execute the death penalty, with deprivation of political rights for life. Pa X should be sentenced to life imprisonment for deliberate homicide, deprived of political rights for life; sentenced to imprisonment for a term of 10 years for participating in the terrorist organization, and it is decided to execute life imprisonment, with deprivation of political rights for life.

In the second instance, it is ruled to dismiss the appeal and sustain the original judgment, and report the death sentence of Yi X (A), Tu X, and Yu X (A) to the Supreme People's Court for approval.

Issues

1. How to identify a terrorist organization;
2. How to determine the culpability of the members in a terrorist organization;
3. How to apply death penalty to perpetrators of terrorist activities.

Holding

Upon review, the Supreme People's Court finds that: affected by religious extreme thoughts, Yi X (A), Tu X, and Yu X (A), for the purpose of carrying out violent terrorist activities, organized, gathered, or cooperated with others to elect leaders, take physical training, listen and watch religious extremist and violent terrorist video and

audio clips, and engage in other activities, jointly planned to carry out violent terrorist activities by means of homicide with knives, all of which constitute the crimes of organizing and leading terrorist organization and intentional homicide. They shall be subject to concurrent punishments pursuant to law. Yi X (A) has repeatedly invited and called on others for his promotion of religious extremist and violent terrorist thoughts, was elected as deputy chief in Nanyang, and participated in the planning of violent terrorist activities at Kunming Railway Station; Tu X has repeatedly provided financial support for the organization, participated in the planning of the violent terrorist activities at Kunming Railway Station and provided the funds for purchasing the knives used for the commission of the crimes; Yu X (A) invited Tu X and Yu B to join the organization, provided funds for the activities, and participated in the planning of violent terrorist activities at Kunming Railway Station. Yi X (A), Tu X and Yu X (A), by organizing and leading the terrorist organization, serve as the organizers and leaders of the terrorist organization, and are the planners of violent terrorist activities at Kunming Railway Station. After being arrested, they concealed the forthcoming violent terrorist activities by the members of the organization, resulting in extremely serious criminal consequences, and shall be punished for all the crimes committed by the organization. Yi X (A), Tu X and Yu X (A) shall be punished pursuant to law for their severe subjective malice, great social harmfulness, and extremely serious crimes. The courts of first instance and second instance have rendered judgments based on clear facts, true and sufficient evidences, convict and sentence the accused accurately and appropriately by following due process of law. Accordingly, the death penalty of Yi X (A), Tu X and Yu X (A) is approved pursuant to law.

Comment on Rule

1. **Identification of a terrorist organization**

Article 120 of the *Criminal Law* only gives a simple account of the crime of organizing, leading, and participating in a terrorist organization by briefly describing the elements of the crime, without specifying the concept and characteristics of terrorist organizations. Paragraph 2 of Article 2 of the *Decision of the Standing Committee of the National People's Congress on Issues concerning Strengthening Anti-Terrorism Work* ("*Decision on Anti-Terrorism*") adopted on October 29, 2011 stipulates that "(t)errorist organization means a criminal group organized to carry out terrorist activities". Before the promulgation of the *Anti-Terrorism Law*, the above-mentioned provision of the *Decision on Anti-Terrorism* is an important basis for the people's courts to identify terrorist organizations. In this case, during the implementation of the *Decision on Anti-Terrorism*, Yi X (A), Tu X, Yu X (A), Pa X have mustered to gradually form a relatively stable criminal group with relatively large number of members organized and led by Yi X (A), Tu X and Yu X (A) for the purpose of carrying out terrorist activities, which shall be identified as a terrorist organization because

it meets the characteristics of a terrorist organization specified in the *Decision on Anti-Terrorism*.

On December 27, 2015, the 18th Session of the Standing Committee of the 12th National People's Congress passed the *Anti-Terrorism Law*, which takes effect as of January 1, 2016, and the *Decision on Anti-Terrorism* is abolished at the same time. Pursuant to the *Opinions on Certain Issues concerning the Application of Law in Handling Criminal Cases Involving Terrorism and Extremism*, after the implementation of the *Anti-Terrorism Law*, terrorist organizations shall be identified pursuant to the provisions of the *Anti-Terrorism Law*. Paragraph 3 of Article 3 of the *Anti-Terrorism Law* stipulates that a terrorist organization means a criminal organization composed of 3 or more persons for the purpose of carrying out terrorist activities. Under this provision, a terrorist organization has 3 characteristics: (1) for the purpose of carrying out terrorist activities; (2) composed of 3 or more persons; and (3) has formed a criminal organization. In judicial practice, when specifically identifying a terrorist organization, the court shall comprehensively examine such factors as the purpose, number of members, and the organizational structure, among which the name, duration, and disciplinary rules of the organization are only reference factors, not the determining or necessary factors, for identifying a terrorist organization.

2. **Determination of the culpability of the members in a terrorist organization**

Article 120 of the *Criminal Law* divides members of a terrorist organization into three categories, i.e., organizers, leaders, and active participants and other participants, and prescribes different statutory penalties for each. Therefore, correctly identifying and distinguishing the 3 types of members in a terrorist organization becomes the key to accurate conviction and sentencing. it is generally agreed that organizers and leaders means those who initiate and create a terrorist organization and those who play a role in the planning, directing, and decision-making of the operation and activities of the organization; active participants means those who actively act and play an important role in the terrorist organization, such as voluntarily participating in the terrorist activities carried out by the terrorist organization, or occasionally participating in the terrorist activities carried out by the terrorist organization but playing a major role[1] in the terrorist activities they participated in other participants means members of a terrorist organization other than the organizers, leaders, and active participants.[2] In this case, Yi X (A) has repeatedly invited and called on others for his promotion of religious extremist and violent terrorist thoughts, and participated in the planning of violent terrorist activities at Kunming Railway Station; Tu X has repeatedly provided financial support for the organization, participated in the planning of the violent terrorist activities at Kunming Railway Station and provided the funds for purchasing the knives used for the commission of the crimes; Yu X (A) invited others to join the organization, provided funds for the activities, and participated in the planning

[1] Daoluan and Jun [1].

[2] See No. 1, 2, 3, 4, 5 Criminal Divisions of the Supreme People's Court editors-in-chief, the Reasoning part of "No. 1220 Guiding Case", *Reference to Criminal Trial*, 112 , Beijing, Law Press, 2018.

of violent terrorist activities at Kunming Railway Station. All three of them, taking the organizing and leading role in the terrorist organization, shall be identified as organizers and leaders. Pa X, as a member of the organization, shall be identified as an active participant because he actively participated in carrying out the terrorist homicide at Kunming Railway Station and played a prominent role.

After correctly identifying and distinguishing the 3 types of members in the terrorist organization, it is also necessary to determine the criminal liability each person shall assume pursuant to law. Paragraphs 3 and 4 of Article 26 of the *Criminal Law* stipulates that "(a)ny ringleader who organizes or leads a criminal group shall be punished on the basis of all the crimes that the criminal group has committed. Any principal offender other than the one stipulated in Paragraph 3 shall be punished on the basis of all the crimes that he participated in or that he organized or directed." Pursuant to the above provisions, the organizers and leaders of a terrorist organization as a criminal group shall be criminally liable for all the crimes committed by the organization; and active participants and other participants of the terrorist organization shall be criminally liable for the participated crimes. Specifically in this case, although Yi X (A), Tu X and Yu X (A) did not participate in the terrorist homicide at Kunming Railway Station, the 3 persons are both the organizers and leaders of the terrorist organization, and the planners of terrorist activities at Kunming Railway Station. After being arrested as suspect for other crimes, they concealed the forthcoming terrorist activities by the members of the organization, resulting in extremely serious criminal consequences. Therefore, they shall be punished for all the crimes committed by the organization, and be criminally liable for the serious consequences caused by terrorist attack at Kunming Railway Station. Pa X, as an active participant in the terrorist organization, shall be criminally liable for the crimes he participated in, i.e., making a terrorist flag for the implementation of violent terrorist activities at Kunming Railway Station, and directly participating in the implementation of terrorist homicide. He played a major role in the criminal activity of terrorist homicide at Kunming Railway Station, and, therefore, shall be criminally liable for the serious consequences of the terrorist attack at Kunming Railway Station.

3. **Application of death penalty to perpetrators of terrorist activities**

A basic criminal policy in China is tempering justice with mercy and an important policy for death penalty is "retaining the death penalty under strict control and prudent application". In the trial of any criminal case concerning terrorist activities, the death penalty shall be accurately applied pursuant to the law, based on the in-depth understanding of the criminal policy of tempering justice with mercy, and the policy of "retaining the death penalty under strict control and prudent application", to ensure an organic unification of the legal and social effects of the case's judgment. The *Several Opinions of the Supreme People's Court on Implementing the Criminal Policy of Tempering Justice with Mercy* issued by the Supreme People's Court in February 2010 clearly stating that, the following crimes shall be listed as the main target of severe punishment, for which a heavier punishment shall be imposed: crimes which seriously jeopardize the stability of state power, such as crimes endangering national security, crimes committed by terrorist organizations, by evil cult organizations,

by organizations bearing the nature of criminal gangs and by vicious forces, and crimes intentionally endangering public security. In particular, for criminals who are extremely hostile to the nation or society, aim to injure unspecified persons and are under any extraordinarily serious circumstances, heavier punishments shall be given when the law so provides, and death penalty shall be executed on those who deserve it. The *Several Opinions of the Supreme People's Court on Giving Full Play to the Functions of Trials and Effectively Maintaining Public Security* issued in September 2015 reiterates "(f)or terrorist crimes, the guideline of severe crackdown on such crimes shall be firmly adhered to, and the ringleaders, core members, and persons guilty of grave criminal offence, who shall be subject to heavy punishment or even death penalty shall be so punished pursuant to law." Therefore, the imposition of the death penalty on violent terrorist criminals guilty of most heinous crime is an important aspect in implementing not only the criminal policy of tempering justice with mercy, but also the policy of "retaining the death penalty under strict control and prudent application". In terms of specific application, sentence shall be lawfully imposed by strictly pursuant to Paragraph 1 of Article 48 of the *Criminal Law*, which stipulates that "(t)he death penalty shall be only applied to criminals guilty of guilty of most heinous crime", under such basic principles of criminal law as "no penalty without a law", and "punishment fits the crime", and taking comprehensive consideration of such factors as the circumstances of the crime, consequences of the crime and the subjective malice and personal danger of the accused. Meanwhile, prominence shall be given to crackdown on key targets. The organizers, leaders, and key members of a terrorist organization shall be the key targets for severe punishment, and those who shall be sentenced to death pursuant to law for having committed extremely severe crimes shall be resolutely sentenced to death pursuant to law, but those with statutory circumstances for lenient punishments shall be punished leniently pursuant to law.[3] In view of this case in which members of the terrorist organization carried out a terrorist attack at Kunming Railway Station by means of homicide with knives, resulting in 31 deaths and 141 injuries, as both the organizers and leaders of the terrorist organization, and the planner of the terrorist attack at Kunming Railway Station, Yi X (A), Tu X, and Yu X (A)'s concealment, after arrest, of the forthcoming terrorist attack by the members of the organization has caused extremely serious criminal consequences, which fully demonstrates the severe subjective viciousness, great social harmfulness, and extremely serious crimes of the 3 accused, so the Supreme People's Court's approval of their death penalty pursuant to law reflects the requirement of strictly punishing serious criminal offences in the criminal policy of tempering justice with mercy.

The *Several Opinions on Implementing the Criminal Policy of Tempering Justice with Mercy* stipulates: "(t)o implement the criminal policy of tempering justice with mercy, we must strictly abide by the law and maintain the unification and authority of law so as to guarantee good legal effects." However, in severely punishing violent

[3]See No. 1, 2, 3, 4, 5 Criminal Divisions of the Supreme People's Court editors-in-chief, the Reasoning part of "No. 1220 Guiding Case", *Reference to Criminal Trial*, 112, Beijing, Law Press, 2018.

terrorist criminals, those who have committed severe crimes not to warrant death penalty shall not be sentenced to death for mere emphasis on strictly cracking down on such crimes. Paragraph 1 of Article 49 of the *Criminal Law* stipulates "(t)he death penalty shall not be applied to persons who have not reached the age of 18 at the time the crime is committed or to women who are pregnant at the time of adjudication". The "death penalty shall not be applied" as stipulated in this paragraph includes both death penalty with immediate execution and death penalty with a two-year suspension of execution, because death penalty with a two-year suspension of execution is not an independent type of punishment, but a means of execution for the death penalty. At the same time, the inapplication of death penalty in that paragraph is absolute inapplication of death penalty, that is, with no exceptions, the death penalty shall not apply to persons who have not reached the age of 18 at the time the crime is committed or to women who are pregnant at the time of adjudication. During the implementation of the *Criminal Law* of 1979, the Research Office of the Supreme People's Court in March 1991 indicates in the *Telephone Reply on the Issue concerning How to Understand "Death Penalty Does not Apply to Women Who are Pregnant at the Time of Adjudication"* that death penalty does not pursuant to law apply to an accused who is a pregnant woman during the detention, whether or not pregnancy has violated the national family planning policy, whether or not she has undergone spontaneous abortion or induced abortion, and despite the length of time the case is transferred for prosecution or trial after abortion. After the implementation of the *Criminal Law* of 1997, the Supreme People's Court indicates in August 1998 in the *Reply on Whether Death Penalty Shall Apply to Pregnant Women in Adjudication Who Suffered from Spontaneous Abortion During Custody* (Interpretation No.18 [1998] of the Supreme People's Court) that "a pregnant woman who suffered from spontaneous abortion during custody for a suspected crime and is prosecuted and committed for trial for the same facts shall be regarded as 'a woman who is pregnant at the time of trial' and pursuant to law death penalty shall not apply." Subject to the above provisions, "women who are pregnant at the time of trial" as defined in Paragraph 1 of Article 49 of the *Criminal Law* shall be understood as the accused is a pregnant woman at the time of the trial, including a woman who was pregnant at the time of custody before the trial, and a woman who was pregnant during custody but suffered from spontaneous abortion or induced abortion. Specifically in this case, Pa X has committed extremely severe crimes by being an active participant in the terrorist organization and a direct perpetrator of the terrorist homicide, but, in view of the fact that she was a pregnant woman at the time of the crime, the death penalty shall pursuant to law not apply (including death penalty with a two-year suspension of execution). Therefore, she is sentenced to life imprisonment by the people's court.

It should be noted that the crime of organizing, leading, and participating in terrorist organizations is amended in *Amendment (IX) to the Criminal Law* by improving allocation of penalties, and adding property-oriented penalties, so as to more effectively deprive criminals of the ability and conditions to commit crimes again, but, because this case occurred before the implementation of the *Amendment (IX) to the Criminal Law*, no property-oriented penalties may be additionally imposed on the 4 accused pursuant to the *Criminal Law* then in force.

Reference

1. Zhou Daoluan and Zhang Jun editors-in-chief, *Accurate Explanation for Accusations of Criminal Law* (I), Beijing, People's Court Press, 2013, p. 102.

Civil and Commercial Cases and Execution Sichuan Panhua Technology Co., Ltd. v. Pangang Group Co., Ltd. (Dispute over Contract)—Determination of Whether Government Acts Constitute Force Majeure and the Application of Change of Circumstances

Yongfeng Pan

Rule

To determine whether government acts constitute force majeure, we should look at two aspects: first, whether government acts fall under objective circumstances that are unforeseeable, unavoidable, and insurmountable; and second, whether government acts do have a substantial impact on the performance of a contract. Only if the above two conditions are met can the government act be considered to be force majeure.

Change of circumstances in essence grants the parties the right to request amendment or rescission of the contract. Change of circumstances is not a statutory cause for exemption, over which the people's courts have discretion. A party to a contract who believes that there exists a change of circumstances but cannot cancel the contract with the opposite party through negotiation shall request the people's court to change or cancel the contract at its discretion, but may not, after unilateral cancellation of the contract, request to be exempted from its liability for breach of contract on the ground of change of circumstances.

Collegial panel judges of the Supreme People's Court for re-trial: Pan Yongfeng, Zhang Chun, Li Xiaoyun (Written by: Pan Yongfeng, Supreme People's Court; Translated by: Niu benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_8

Case Information

1. Parties

Applicant in the re-trial (Defendant in the first instance, Plaintiff in the counterclaim, Appellant in the second instance): Pangang Group Co., Ltd. (hereinafter referred to as "Pangang")
Respondent in the retrial (Plaintiff in the first instance, Defendant in the counterclaim, Appellant in the second instance): Sichuan Panhua Technology Co., Ltd. (hereinafter referred to as "Panhua Technology")

2. Procedural History

First Instance: No. 107 [2015], Trial, Civ. Division, Panzhihua Intermediate People's Court of Sichuan Province (dated Nov. 24 of 2015)
Second Instance: No. 438 [2016], Final, Civ. Division, the Higher People's Court of Sichuan Province (dated Aug. 31 of 2016)
Application for Retrial: No. 27 [2017], App. Ruling, Civ. Division, the Supreme People's Court (dated Mar. 17 of 2017)

3. Cause of Action

Contract dispute

Essential Facts

On June 29, 2006, Panhua Technology and Panzhihua Iron & Steel Co., Ltd. (which was later merged by entirety with Pangang, with the latter assuming all the claims and debts of Panzhihua Iron & Steel Co., Ltd.) signed and entered into a Master Cooperation Agreement on Sulfuric Acid and Waste Acid Disposal Project (hereinafter referred to as "Master Cooperation Agreement"). After the signing of the Master Cooperation Agreement, Panhua Technology began construction of Phase 1 production line with an annual output of 100,000 tons of sulfuric acid and 150,000 tons of waste acid concentration, which was completed in February 2007 and passed the acceptance inspection by the environmental protection authorities. In January 2011, Panhua Technology completed Phase 2 production line of production technology transformation project for concentration and recovery of titanium white waste acid, and subsequently passed the acceptance inspection for environmental protection purpose. Both parties continued to implement the Master Cooperation Agreement. On June 18, 2013, Titanium Co. (the entity under Panhua Technology and Panzhihua Iron & Steel Co., Ltd. that specifically implements the Master Cooperation Agreement) issued to Panhua Technology the Letter on the Termination of the Master Cooperation Agreement on Sulfuric Acid and Waste Acid Disposal Project, indicating that "(s)ubject to the requirements of the Letter of Responsibility for 2013 Panzhihua Environmental Protection Objectives signed by Pangang and Panzhihua Municipal

People's Government, our company's titanium dioxide factory will 'start the program in June 2013 and shut down before February 2015'. Our company … decides to stop the production in the titanium dioxide factory from July 1, 2013 and starts the corresponding relocation work. …" To this end, we hereby inform your company that the Master Cooperation Agreement signed by us on September 19, 2006 and its subsequent agreements and contracts will be terminated on July 1, 2013, and, the performance for the remaining part after the cancellation of the aforementioned agreements and contracts will be terminated. On July 12, 2013, Panhua Technology sent a reply letter to Titanium Co., stating that "because long-term deactivation of production equipment for sulfuric acid and waste acid disposal will cause irreversible damage, it cannot be deactivated for a long time. It is recommended that both parties sum up the cooperation over the past 6 years or so, and the relevant provisions of the Master Cooperation Agreement can be revised, supplemented and improved. However, our company does not consent to your company's unilateral cancellation of the Master Cooperation Agreement." On January 20, 2014, Titanium Co. and Panhua Technology signed the Settlement Agreement with Panhua Technology on Relevant Operations Prior to the Shutdown of Titanium Dioxide Factory. On March 10, 2014, Panhua Technology sent a letter to Panzhihua Iron & Steel Co., Ltd., requesting compensation for losses and assumption of liability for breach of contract. However, dispute arose between the parties for failure to reach an agreement on the compensation.

The court of first instance issued a judgment on November 24, 2015: "(1) The Master Cooperation Agreement signed by Panzhihua Iron & Steel Co., Ltd. and Panhua Technology is cancelled; (2) Pangang shall compensate Panhua Technology for the losses in the total amount of RMB 5,510,575.96 within 15 days after the effective date of this judgment; (3) Pangang shall pay Panhua Technology damages for breach of contract in the amount of RMB 1,653,172.79 within 15 days after the effective date of this judgment; (4) Pangang shall pay Panhua Technology the salary and welfare loss of the remaining staff in the amount of RMB 61,085.57 each month for the period commencing on March 2014 and ending on June 2014; (5) Panhua Technology shall return 6.84 tons of diesel and the occupied premises and assets to Pangang within 15 days after the effective date of this judgment; (6) Panhua Technology shall pay Pangang other expenses in the amount of RMB 70,000 within 15 days after the effective date of this judgment; (7) Other claims of Panhua Technology in this case are hereby dismissed; (8) Other counterclaims of Pangang are hereby dismissed."

Unsatisfied with the judgement of the court of first instance Panhua Technology and Pangang lodged an appeal.

The court of second instance rendered a judgment on August 31, 2016: "(1) Affirm Items 1, 5, 6 and 8 of the civil judgement (No.107[2014], Trial, Civ. Division); (2) Amend Item 2 of the civil judgement (No.107[2014], Trial, Civ. Division) to read as 'Pangang shall compensate Panhua Technology for the losses in the total amount of RMB 29,441,471.23 within 15 days after the effective date of this judgment'; (3) Amend Item 3 of the civil judgement (No.107[2014], Trial, Civ. Division) to read as 'Pangang shall pay Panhua Technology damages for breach of contract in the amount

of RMB 1,000,000 within 15 days after the effective date of this judgment'; (4) Reverse Items 4 and 7 of the civil judgement (No.107[2014], Trial, Civ. Division); (5) Pangang shall pay Panhua Technology the salary and welfare losses of the remaining staff in the amount of RMB 20,000 each month for the period commencing on July 2014 and ending on effective date of the judgment; 6. Dismiss other claims of Panhua Technology." Unsatisfied with the judgment of the second instance, Pangang applies to the Supreme People's Court for retrial.

Issues

Whether government act involved in this case falls within the scope of force majeure or change of circumstances, and whether Pangang's unilateral cancellation of the agreement can be exempted from liability based on such reason.

Holding

Upon review in the retrial, the Supreme People's Court finds that: there are 2 main issues in the application for retrial: (1) whether Pangang can be exempted from liability for its cancellation of the Master Cooperation Agreement due to alleged force majeure or change of circumstances; (2) whether Panhua Technology has breached the contract, and shall compensate Pangang for the losses and pay the liquidated damages.

1. **Whether Pangang can be exempted from liability for its cancellation of the Master Cooperation Agreement due to alleged force majeure or change of circumstances**

First of all, let's consider whether its liability can be exempted due to the alleged force majeure. Article 117 of the *Contract Law* stipulates that "(a) party who is unable to perform a contract due to force majeure is exempted from liability in part or in whole in light of the impact of the event of force majeure, except otherwise provided by law. Where an event of force majeure occurs after the party's delay in performance, it is not exempted from such liability. For purposes of this *Law*, force majeure means any objective circumstances which are unforeseeable, unavoidable and insurmountable." In this case, the Implementation Plan for Comprehensive Environmental Regulation issued by the General Office of Panzhihua Municipal People's Government, among other things, requires Pangang to "develop and improve in June 2013 the implementation plan for the relocation of Pangang Titanium Dioxide Plant and the closing of Pangang tailing pond". According to the *Technical Reform and Reconstruction Project of Pangang Titanium Dioxide Plant* indicated in the Appendix 6 to the *Letter of Responsibility for 2013 Environmental Protection Objectives* signed by Pangang and Panzhihua Municipal People's Government, "the plan shall be formulated and initiated in June 2013, and the current old factory shall be closed in February 2015".

From the above documents, in order to achieve the overall objectives of comprehensive urban environmental regulation, Panzhihua Municipal People's Government requires Pangang to formulate its own technological transformation and relocation plan based on the overall objectives of comprehensive urban environmental regulation. From the Letter of Responsibility for the Objectives, the technical reform and relocation of Pangang's Pangang Titanium Dioxide Plant shall be implemented in 3 steps: (1) formulate the plan; (2) initiate the implementation of the plan; and (3) shut down the old factory. The formulation of the plan shall include such specific issues as site selection for the relocation, relocation compensation, personnel resettlement, and government compensation, and requires consultation with the government and cooperative enterprises including Panhua Technology. Pangang failed to present evidence that it had formulated and improved the corresponding relocation implementation plan in June 2013 subject to the requirements of the Letter of Responsibility for Objectives. Instead, it directly shut down the Titanium Dioxide Factory on July 1, 2013, leading to factual termination of the Master Cooperation Agreement signed by the parties. This is inconsistent with the requirements of government documents and the Letter of Responsibility for Objectives, and does not fall under objective circumstances that are unforeseeable, unavoidable, and insurmountable, thus it shall be found that Pangang unilaterally terminated the contract. Therefore, Pangang's claim that its rescission of the Master Cooperation Agreement due to government act falls under force majeure, and shall be exempted from liability is not supported for lack of factual and legal basis.

Second, whether its liability can be exempted due to the alleged change of circumstances. Article 26 of the *Judicial Interpretation of the Contract Law (II)* stipulates that "(w)here, after the conclusion of the contract, the objective circumstances undergo significant changes that were unforeseeable by the parties at the time of the conclusion of the contract, not caused by the force majeure, and do not fall within commercial risks, and continued performance of the contract will be obviously unfair to one party or will not fulfill the purpose of the contract, the people's court shall, upon the request of one party for modifying or terminating the contract, determine whether to modify or terminate the contract under the principle of fairness and in light of the actual circumstances of the case". In this case, Pangang failed to present evidence that continued performance of the contract would be unfair to it or could not fulfill the purpose of the contract. After knowing the Implementation Plan for Comprehensive Environmental Regulation and signing the Letter of Responsibility for Objectives, Pangang did not invoke the clause of change of circumstances to request the people's court to change or cancel the contract, and did not claim change of circumstances during the first and second instances. Moreover, even if Pangang believes that there exists change of circumstances, but could not cancel the contract with the opposite party through negotiation, it shall request the people's court to change or cancel the contract at its discretion in light of the actual circumstances, instead of claiming exemption from liability for its breach of contract after unilateral cancellation of the contract. Therefore, Pangang's claim that government act falls under change of circumstances in the performance of the contract, and shall be exempted from liability is not supported for lack of factual and legal basis.

2. **Whether Panzhihua Technology shall compensate Pangang for losses and pay the damages for its breach of contract**

According to the facts found, Panhua Technology has already built two production lines for waste acid concentration and passed the acceptance check from environmental protection authorities. Panzhihua Environmental Protection Bureau, after testing by a commissioned testing agency, takes the view that the waste acid concentration production line built by Panhua Technology can meet the ability to dispose waste acid produced by the Titanium Dioxide Factory. At the same time, the Settlement Agreement with Panhua Technology on Relevant Operations Prior to the Shutdown of Titanium Dioxide Factory signed by the parties on January 20, 2014 does not mention that Panhua Technology due to its own reason failed to fully dispose the waste acid provided by Titanium Dioxide Factory of Pangang, but proves on the contrary that both parties are responsible for the continuous and stable operation of the waste acid concentration. The parties have agreed on the assumption of this responsibility by reducing the compensation for waste acid concentration, and have completed and so performed the settlement on the compensation for waste acid concentration. Pangang does not present sufficient evidence that Panhua Technology is in breach of contract by failing to fully dispose the waste acid provided by Titanium Dioxide Factory of Pangang, so its claim that Panhua Technology shall assume the liability for breach of contract, compensate for losses and pay damages is not supported for lack of factual and legal basis.

In summary, Pangang's claim that it shall be exempted from liability for its cancellation of the Master Cooperation Agreement due to force majeure cannot be established. The Supreme People's Court rules to dismiss Pangang's application for retrial.

Comment on Rule

In practice, government act is often invoked by the parties as a situation of force majeure, but it shall be handled and determined though detailed analysis in light of the merits of the case.

1. **Does government act constitutes force majeure?**

Contract cancellation is divided into statutory cancellation and cancellation by agreement. The legally prescribed reasons for the parties to the contract to exercise the right of rescission are mainly force majeure or breach of contract by one party that renders the performance of the contract unnecessary or impossible. In this case, Pangang claims that the Master Cooperation Agreement is cancelled due to force majeure, one of the legally prescribed reasons for cancellation stipulated in Article 94 of the *Contract Law*. No specific provision is stipulated in current Chinese law as to what constitutes force majeure affecting contract performance. From judicial practice, force majeure refers to objective circumstances that are unforeseeable, unavoidable, and insurmountable, usually including natural disaster, war, social abnormality, and

government act. Since the influence of force majeure on contract performance can be large or small, temporary or irreversible, Article 117 of the *Contract Law* stipulates: "(a) party who is unable to perform a contract due to force majeure is exempted from liability in part or in whole in light of the impact of the event of force majeure, except otherwise provided by law. Where an event of force majeure occurs after the party's delay in performance, it is not exempted from such liability."

As to whether government act constitutes force majeure, analysis shall be made on a case-by-case basis, without making any sweeping generalization. Two aspects shall be attended to: first, whether government acts fall under objective circumstances that are unforeseeable, unavoidable, and insurmountable; and second, whether government acts do have a substantial impact on the performance of a contract. In this case, Panzhihua Municipal People's Government, for the purpose of achieving the overall objectives of comprehensive urban environmental regulation, requires Pangang to formulate its own technological transformation and relocation plan based on the overall objectives of comprehensive urban environmental regulation. It is a process from the formulation of the plan to its final implementation and relocation, which Pangang should foresee. When formulating the relocation plan, Pangang can negotiate with Panhua Technology as to the continued performance of the contract, and, in case of any actual difficulty in implementation, shall further negotiate issues concerning compensation. Instead of actively taking corresponding measures when it was still likely to continue to implement the contract, Pangang's forthwith shutdown of the Titanium Dioxide Plant, leading to the actual termination of the Master Cooperation Agreement between the two parties, is obviously not force majeure, and it shall be found that Pangang unilaterally terminated the contract. Therefore, Pangang's claim that its rescission of the Master Cooperation Agreement due to government act falls under force majeure and shall be exempted from liability for breach of contract is not supported for lack of factual and legal basis.

2. **Does the government act constitutes change of circumstances?**

Pursuant to Article 26 of the *Judicial Interpretation of the Contract Law (II)*, change of circumstances is different from impossibility of performance due to force majeure in that it still allows continued performance of the contract unless continued performance is extremely difficult and will result in obvious unfairness or failure to achieve the purpose of the contract. In essence, change of circumstances, being not a legally prescribed reason for exemption, grants the parties and the court the right to request amendment or rescission of the contract and the power of fair adjudication. After change of circumstances occurs, it shall be settled by both parties through negotiation. If the negotiation fails, the parties must apply to the people's court or the arbitration institution to decide whether to change or terminate the contract. A party or both parties may not change or terminate the contract without the ruling of the people's court or the arbitral institution.

In this case, Pangang failed to present evidence that continued performance of the contract would be unfair to it or could not fulfill the purpose of the contract. Moreover, after knowing the Implementation Plan for Comprehensive Environmental Regulation and signing the Letter of Responsibility for Objectives, Pangang did

not invoke the clause of change of circumstances to request the people's court to change or cancel the contract. Even if Pangang believes that there exists change of circumstances, but could not cancel the contract with the opposite party through negotiation, it shall request the people's court to change or cancel the contract at its discretion in light of the actual circumstances, instead of claiming exemption from liability for its breach of contract after unilateral cancellation of the contract.

3. **Determination of who shall pay land use tax**.

Article 2 of the *Interim Regulations on Urban Land Use Tax* stipulates that "(t)he units and individuals using land within the scope of cities, county seats, administrative towns, industrial and mining areas shall be payers of urban and town land use tax (hereinafter referred to as land use tax) and shall pay land use tax in accordance with the provisions of these regulations". The units and individuals using land as stipulated in the above provision refers to the right holders registered on the land ownership certificates, unless otherwise stipulated by laws and regulations. In this case, Pangang, as the right holder registered on the land ownership certificate, is the taxpayer of urban land use tax, who shall pay the land use tax pursuant to law. As for Pangang's handing over of the land involved in the case to the actual use of Panhua Technology, whether the land use tax should be actually borne by Panhua Technology or whether Panhua Technology should give Pangang corresponding compensation for land use tax depends on the agreement between the two parties. The Master Cooperation Agreement signed by the two parties is silent on Panhua Technology's payment of land use tax for the land occupied. During the performance of the contract over the past several years, the two parties did not make any agreement on the payment of land use tax for the site occupied by Panhua Technology, and Pangang did not claim payment against Panhua Technology after actual payment of the land use tax. Therefore, Pangang's claim that Panhua Technology shall pay the land use tax of RMB 9.6 million is not supported for lack of factual and legal basis.

Aluminum Corporation of China Limited Chongqing Branch and Aluminum Corporation of China Limited v. Chongqing Fuli Mining Co., Ltd. (Dispute over Contract)—Determination of Cause of Action and Time of Rescission under Statutory Right of Rescission

Zhumei Liu

Rule

In commercial disputes, we shall accurately ascertain the nature of the dispute between the parties, so as to accurately determine the cause of action, and, based on the legal relationship reflected in the case, further apply relevant legal rules. The court of second instance, in light of the nature of a series of contracts signed by and disputes arising between both parties, accurately determines the case to be a dispute in a sales contract by tender, rather than a contract dispute identified by the court of first instance, and then resolve several disputes raised by the parties in a "package".

Upon request of one party to have the contract terminated by the exercise of the statutory right of rescission, the court's final determination that the contract shall be terminated is the court's exercise of the public power to determine the private commercial transaction between the parties, and then the time of rescission shall be deemed to be the date on which the judgment takes effect, rather than the date on which the complaint is delivered as determined by the court of first instance, and the judgement shall be drafted as ordering the contract to be rescinded rather than confirming the contract to be rescinded.

Collegial panel judges of the Supreme People's Court for the second instance: Liu Zhumei, Yang Xingye, Li Yanchen (Written by: Liu Zhumei, Supreme People's Court; Translated by: Niu benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_9

Case Information

1. **Parties**

Appellant (Defendant in the trial): Aluminum Corporation of China Limited Chongqing Branch (hereinafter referred to as "Chalco Chongqing Branch")
Appellant (Defendant in the trial): Aluminum Corporation of China Limited (hereinafter referred to as "Chalco")
Appellee (Plaintiff in the trial): Chongqing Fuli Mining Co., Ltd. (hereinafter referred to as "Fuli Mining")

2. **Procedural History**

First Instance: No. 00070 [2017], Trial, Civ. Division, Chongqing Higher People's Court (dated Jun. 29 of 2017)
Second Instance: No. 722 [2017], Final, Civ. Division, the Supreme People's Court (dated Dec. 29 of 2017)

3. **Cause of Action**

Dispute over sales contract by tender

Essential Facts

In 2007, Chinalco Chongqing Branch issued a tender notice for the supply of lime and limestone for its annual production of 800,000 tons of aluminium oxide. After successful bidding by Fuli Mining, the two parties signed the Lime Investment Construction Agreement and Limestone Investment Construction Agreement for a term of 25 years. Fuli Mining made special investment in the construction of mine, and lime and limestone production line. In 2014, Chinalco Chongqing Branch suspended the acquisition of relevant raw materials due to overcapacity, accelerated competition in the industry, and continued losses in the project. The purpose of the contract cannot be achieved due to discontinued production of the project, in addition to Chinalco's provision for assets impairment of RMB 3.3 billion for the project.

Thus, Fuli Mining filed a civil lawsuit with the court of first instance, requesting the contract be terminated and Chinalco Chongqing Branch and Chinalco liable for the breach of contract. On July 20, 2015, the court of first instance served a complaint with Chinalco Chongqing Branch.

On February 21, 2017, during the trial by the court of first instance, Chinalco orally raised a counterclaim for the loss caused by Fuli Mining's failure to provide raw materials for 18 months before the end of the court trial debate, but did not submit specific facts and claims. The court of first instance informed Chinalco in court that it should file a cross-compliant before February 28, 2017. After the trial, Chinalco Chongqing Branch mailed a cross-compliant to the court of first instance. On June 29, 2017, the court of first instance entered a civil ruling (No. 00070[2017], Trial,

Civ. Division), refusing to combine the counterclaim raised by Chinalco Chongqing Branch and Chinalco.

The court of first instance made a judgment on June 29, 2017: "(1) Confirm the Investment and Construction Agreement of Lime for the Production of Aluminum Corporation of China Limited Chongqing 800,000 Tons of Aluminium Oxide signed by Fuli Mining and Chinalco Chongqing Branch [Chinalco CQ (2007) No. 031] and Investment and Construction Agreement of Limestone for the Production of Aluminum Corporation of China Limited Chongqing 800,000 Tons of Aluminium Oxide [Chinalco CQ (2007) No. 033] was rescinded on July 20, 2015; (2) Chinalco Chongqing Branch shall compensate Yuli Mining RMB 109,698,501.94 and capital occupation losses within 10 days from the effective date of the judgment (capital occupation loss from March 31, 2009 to June 13, 2014 calculated on the benchmark interest rate of loans for the same period as stipulated by the People's Bank of China with the base number being RMB 102,311,833.56; and capital occupation loss from June 14, 2014 to the date of full payment calculated on the benchmark interest rate of loans for the same period as stipulated by the People's Bank of China with the base number being RMB 109,698,501.94); (3) Chinalco shall be liable for the part Chinalco Chongqing Branch fails to pay as determined in Item 2 of the judgment; 4. Dismiss other claims of Fuli Mining." Chinalco Chongqing Branch refused to accept the judgment, and filed an appeal to the Supreme People's Court.

Issues

Whether the counterclaim raised by Chinalco Chongqing Branch and Chinalco in the first instance should be accepted; the nature of the two agreements and a series of sales contracts; whether the relevant contracts should be cancelled.

Holding

Upon review, the Supreme People's Court holds that:

1. **Regarding whether the counterclaim raised by Chinalco Chongqing Branch and Chinalco in the first instance should be accepted**

Civil subjects may file a civil lawsuit to the people's court for their property relations and personal relations, and the premise for the acceptance by the people's court is that the case must meet the statutory requirements. The parties shall file a counterclaim pursuant to the requirements for filing a lawsuit as stipulated in Article 119 of the *Civil Procedure Law*, i.e., "(1) the plaintiff must be a citizen, legal person or other organization with a direct interest in the case; (2) there must be a specific defendant; (3) there must be a specific claim and a specific factual basis and grounds; and (4) the action must fall within the range of civil actions accepted by the people's courts and

within the jurisdiction of the people's court with which it is filed.", which shall also be in compliance with Article 232 of the *Judicial Interpretation on the Civil Procedure Law*, i.e., "the people's court, if possible, shall combine for trial any claim added by the plaintiff, counterclaim filed by the defendant or claim filed by a third party concerning the case after the acceptance of the case but before the conclusion of court arguments." In this case, the two companies do not meet the statutory requirements for filing a lawsuit and counterclaim due to failure of Chinalco Chongqing Branch to file a counterclaim before the conclusion of court arguments at the court of first instance, and failure of Chinalco to raise specific claim and facts despite raising counterclaim before the conclusion of court arguments at the court of first instance and to file cross-compliant within the time limit prescribed by law after clarification by the court of first instance.

Chinalco alleges that the cross-compliant filed by Chinalco Chongqing Branch within the time limit set by the court of first instance may be regarded as that filed by Chinalco. Although Chinalco Chongqing Branch is a branch of Chinalco, the two being different and independent civil entities in civil activities and litigation, they cannot substitute each other in acts of litigation. Chinalco also maintained that Chalco Chongqing Branch's expression of consent to the counterclaim raised by Chinalco before the conclusion of court arguments at the court of first instance could be regarded as a counterclaim raised by Chinalco Chongqing Branch. It is found after examination that Chinalco Chongqing Branch only approved the behavior of Chinalco, which could not be inferred as manifestation of intent to independently raising a counterclaim.

Accordingly, in view of the fact that the counterclaim raised by Chinalco and Chinalco Chongqing Branch at the court of first instance does not meet the requirements stipulated by law, the counterclaim shall be lawfully dismissed, but the court of first instance ruled that it is not combined for trial. This does not fall within the scope of appealable issues under Article 153 of the *Civil Procedure Law*, which has in fact deprived Chinalco Chongqing Branch and Chinalco of the right of appeal concerning whether its counterclaim should be accepted. When Chinalco Chongqing Branch and Chinalco Company appealed, they filed a petition for appeal, including appeal for such ruling. Considering the inappropriateness of the court of first instance to rule not to combine the counterclaim for trial rather than to dismiss the counterclaim, this court nevertheless examines the issue so as to protect its right of appeal in the substantive sense. It is held after examination that, although the ruling of the court of first instance affected Chinalco Chongqing Branch and Chinalco to exercise their right of appeal, the objective consequences are the same for the court of the first instance to dismiss the counterclaim and refuse to combine it for trial, because the counterclaim filed by Chinalco Chongqing Branch and Chinalco indeed did not meet the statutory requirements for filing a lawsuit and counterclaim. In addition, the two companies may file a separate lawsuit to claim relevant rights and interests, with their rights not substantively impaired. Therefore, this issue is not serious enough to affect the court of second instance to adjudicate on the merits of the case.

2. **With regard to the nature of the underlying contracts (the Lime Investment and Construction Agreement, and Limestone Investment and Construction Agreement) and a series of sales contracts involved in the case**

The court of first instance identified the nature of the contract as an appointment and sales contract and its cause of action as a secondary cause of action "contract dispute". The Court holds that the nature of the contract should be determined in light of the background of signing, content, main terms and purpose of the contract, and the legal relationship involved (the relationship of rights and obligations established by the parties to the contract). Specifically in this case, the nature of the two agreements and the subsequent series of supply and sales contracts involved in the case should be determined in light of the background of the disputes involved, bidding and bid, content of the agreement and content of subsequent series of supply and sales contracts. It is found after examination that the background of the transaction involved is that Chinalco Chongqing Branch made open bidding for lime and limestone required for its project of 800,000 tons of aluminum oxide that meets the specific production process and technical requirements, stipulating in its bidding documents requirements for production process, product standards, possession of mineral resources, market condition, production capacity, and other factors of the bidders. Under such circumstances, Fuli Mining won the bid. The two parties signed two agreements involved in the case, which is named Investment and Construction Agreement, stipulating, among other things, a 25-year cooperation period, signing of supply and sales contract every two years by the Parties, directed acquisition in addition to the general sales contract, supervision and inspection of the construction of the mining area, payment of the deposit, seeking compensation for infrastructure and production loss caused by one party. After the signing of the agreement, both parties began to invest funds in the construction of their respective production lines, and signed a series of supply and sales contracts thereafter.

According to the *Provisions on Causes of Action in Civil Cases*, a sales contract by tender is a sales contract signed by a biddee and a bidder where by the biddee sends an invitation to offer to specified or unspecified persons through bidding notice or invitation to bid, each bidder sends offer through bid, and the biddee accepts by selecting the successful bidder or after re-negotiation. The sales contract by tender, as a special kind of sales contract, has both general features of sales contracts and unique features due to its introduction of bidding and bid in the contracting process. The two agreements and a series of supply and sales contracts involved in the case as a whole possess the legal features of bidding sales contract, among which the two agreements involved in the case constitutes the basic framework agreement for the sales contract by tender, and the subsequent series of supply and sales contracts are sales contracts signed by the biddee and the winning bidder after re-negotiation. Therefore, the nature of the two agreements and a series of supply and sales contracts shall be the sales contract by tender, and the cause of action shall also be identified as dispute over sales contract by tender. It is not proper for the court of first instance to identify the nature of the contract as an appointment and sales contract and its cause of action as contract dispute, so this court will correct. The sales contract by tender

in this case shall be lawfully valid, for it is a genuine manifestation of the parties' intent, and not in violation of mandatory provisions of the law and administrative regulations.

3. **With regard to the time of contract cancellation in this case**

In this case, the request of Fuli Mining to exercise the statutory right of rescission was not directly filed with Chinalco Chongqing Branch and Chinalco, but with the people's court through litigation, demanding the contract be terminated by court decree. Whether the contract involved in the case can be rescinded shall be finally determined by the people's court and the time of rescission shall be the time when the judgment of the people's court takes effect. Chinalco Chongqing Branch and Fuli Mining did not specify the conditions for the termination of the contract in the two agreements involved in the case, nor did they reach an agreement on the termination of the contract. Under such circumstances, Fuli Mining's filing of lawsuit, requesting the people's court to order the contract be terminated, can be regarded as a manifestation of intent to rescind the contract, but whether the statutory right of rescission exercised is established or not shall be determined by the people's court pursuant to the performance of the contract and legal provisions. After case filing, service of the complaint of Fuli Mining by the court of first instance on Chinalco Chongqing Branch and Chinalco, in which the claim of rescinding the contract is included, is an act of public power to carry out the statutory civil procedure, and such act does not constitute Fuli Mining's manifestation to Chinalco Chongqing Branch and Chinalco of its intent to rescind the contract, which is of a private law nature. As previously mentioned, because Fuli Mining's request for rescission of the contract satisfies the statutory conditions for rescission, this court's judgment ordering rescission of the two contracts is the exercise by the people's court of its public power to adjudicate private commercial transactions between the parties, then the time of its rescission shall be the date on which the judgment takes effect. Although the determination of the time of contract rescission in this case has no effect on the substantive rights of the parties, the inappropriate application of law shall be corrected that the court of first instance ascertains the time of rescission of the two agreements involved in the case to be the date when the complaint is served on Chinalco Chongqing Branch.

The Supreme People's Court renders a civil judgment (No. 722 [2017], Final, Civ. Division): "(1) To reverse the civil judgment of Chongqing Higher People's Court (No. 00070 [2015], Trial, Civ. Division); (2) To rescind the Investment and Construction Agreement of Lime for the Production of Aluminum Corporation of China Limited Chongqing 800,000 Tons of Aluminium Oxide signed by Fuli Mining and Chinalco Chongqing Branch [Chinalco CQ (2007) No. 031] and Investment and Construction Agreement of Limestone for the Production of Aluminum Corporation of China Limited Chongqing 800,000 Tons of Aluminium Oxide [Chinalco CQ (2007) No. 033]; (3) To order Chinalco Chongqing Branch to compensate within 10 days from the effective date of the judgment Fuli Mining RMB 109,698,701.98 and the interest for the period of capital occupation calculated on the benchmark interest rate of loans for the same period as stipulated by the People's Bank of China

(with the base number being RMB 102,312,033.56 from March 31, 2009 to June 13, 2014 and RMB 109,698,701.98 from June 14, 2014 to the date of full payment); (4) To order Chinalco to be liable for the part Chinalco Chongqing Branch fails to pay as determined in Item 3 of this judgment; (5) To dismiss other claims of Fuli Mining; (6) To dismiss other claims in the appeal by Chalco Chongqing Branch and Aluminum Corporation of China Limited."

Comment on Rule

This is a major and complicated commercial case, with RMB 160 million in controversy, 27 volumes of files, 4,000 pages of evidence, and 5 petitions for appeal filed by the parties with regard to procedural rulings and substantive judgment made by the court of first instance concerning interwoven substantive and procedural issues, covering almost all difficult legal issues encountered in commercial litigation, such as determination of the nature of contract, termination of contract, liability for breach, calculation of loss, cause of action, action in chief and counterclaim. After investigation by the collegiate bench, this court made comprehensive correction of such issues as determination of the time of contract rescission, ascertainment of the nature of contract, improper ruling, incorrect cause of action and wrong calculation of the amount in controversy by the court of first instance.

1. **With regard to accurate determination of the cause of action and nature of dispute**

One premise of adjudicating cases is to determine the nature of the contract. Article 125, paragraph 1, of the *Contract Law* establishes the principle that "the contract shall be interpreted as a whole" so as to determine the true intent of the parties. Interpretation of contract as a whole, as an important means of contract interpretation, requires that the true intent of the parties shall not be limited to the literal meaning of the contract or certain clauses of the contract, let alone isolated phrases or sentences of the contract, but shall be determined by taking overall consideration of such issues as the background, process and purpose of entering into the contract, its performance and legal relationships involved. It is of great significance to use such method to accurately determine the nature of the contract, and then accurately apply the law and fairly adjudicate the case. Specifically in this case, determination by the court of first instance of the cause of action as a contract dispute, and the nature of the contract as dispute over an appointment and sales contract, has made the entire judgment more difficult for the handling of subsequent claims raised by the parties, and deviated the process of adjudication. Based on the specific background of the case and the process of bidding and bid, the case by its nature obviously falls with disputes over sales contract by tender. On this basis, the cause of action of the case should also be a dispute over the sales contract by tender, and in light of the nature of the legal relationship reflected by the cause of action, the legal rules for sales

contract by tender shall apply, thus the relationship between the two agreements and the subsequent series of supply and sales contracts will be easily resolved.

2. **Where one party requests the people's court to order rescission of the contract, if the people's court considers that its statutory right of rescission is established and orders the contract to be rescinded, the time for the contract to be rescinded shall be the date on which the judgment takes effect**

Article 96 of the *Contract Law* stipulates that "a party demanding termination of a contract in accordance with the provisions of Paragraph 2 of Article 93 and Article 94 of this *Law* shall notify the other party. The contract shall be terminated upon the receipt of the notice by the other party. If the other party objects to such termination, it may petition the people's court or an arbitration institution to confirm the validity of the termination of the contract, unless the laws and administrative regulations requires approval and registration for the termination of the contract." Accordingly, both parties to the contract have the right to request the people's court or arbitration institution to confirm the validity of the termination of the contract. If a party sues for an order to terminate the contract, and the court considers that it meets the requirements for termination by agreement or statutory termination, the contract shall be terminated from the date on which court judgment takes effect. In this case where the parties did not specify the requirements for termination by agreement nor did they agree on the termination of the contract, filing a lawsuit by one party shall be deemed as a way to manifest its intent to terminate the contract, and it is the court to lawfully determine whether its statutory right of termination is established or not. The fact the court of first instance takes the date on which the complaint is served on the other party as the date of termination is obviously wrong because it misjudge the act of public power in court's litigation proceedings as the manifestation of intent to terminate the contract, which is of a private law nature. Order of the people's court to terminate the contract is the court's exercise of public power to ascertain the private commercial transactions between the parties, so its time of termination shall be the date on which the judgment takes effect. Of course, if one party fulfills its obligation to notify the other party of the termination of the contract pursuant to Article 96 of the *Contract Law*, and the other party appeals to the court to confirm the validity of the notice of termination, the contract shall be terminated when the notice is delivered to the other party, if the court after examination considers the other party's objection not established.

3. **How should the court of second instance respond when the court of first instance determines that the counterclaim raised by the party fails to meet the statutory requirements, and rules not to merge it for trial rather than dismiss it, which has deprived the party of its right to appeal, but the party nevertheless "appeals" on this**

In civil and commercial litigation when the people's court needs to determine whether to accept the counterclaim raised by the defendant in the original trial, it should examine first whether it meets the requirements for general lawsuits set forth in Article 119 of the *Civil Procedure Law*, and then whether it meets the requirements

for counterclaim set forth in the *Judicial Interpretation on the Civil Procedure Law*. In this case where the court of first instance correctly determines through examination of facts that the counterclaim raised by the litigant does not meet the elements of a claim, the court shall rule to dismiss the counterclaim rather than rule not to merge it for trial. It is obviously not appropriate for the court of first instance to rule not to merge the counterclaim for combined trial, which means that the counterclaim is deemed to have satisfied the requirements for litigation but cannot be merged for combined trial at present case. However, the ruling made by the court of first instance does not fall under any one of the three types of appealable rulings under the *Civil Procedure Law*, thus directly depriving the parties of their right of appeal. If the parties insist on filing a petition for appeal, how should the court of second instance respond? In particular, when substantive judgment is the basis for the acceptance of case by the court of second instance, can the procedural rights raised by the litigant be completely ignored? The approach in this case is to first review whether the court of first instance is correct in making the ruling. If correct, the appeal filed by the litigant may be dismissed orally; or if it is indeed inappropriate, the court of second instance shall review the appeal filed by the litigant to guarantee its rights in litigation in the substantive sense. However, the court of second instance, upon review, holds that the objective consequences are the same for dismissing the counterclaim and refusing a combined trial, and the right of the litigant to file a separate case for the counterclaim is retained. Therefore, the wrong ruling of refusing a combined trial does not constitute a substantial impact on the litigant's rights, and the court of second instance finds that the issue is not serious enough to affect the trial on merits by the court of second instance.

Panjin Urban Construction and Real Estate Development Co., Ltd. v. Xu X (Dispute over Real Estate Sales Contract)—When One Litigant Applies for Retrial, Whether Its Provision of Criminal Investigation Material of the Other Suspected of Committing a Crime is Sufficient to Overturn Facts Found in the Original Judgment

Xiaoguang Feng

Rule

Based on the principle of high probability of evidence, the trial court finds that the contract-issuing party's use of its commercial housing to offset project payment in arrears and the following conclusion of the sales contract of commercial housing with the actual constructor is valid. "High probability" stems from the basic legal relationship, i.e., the contract-issuing party defaults in making project payment under the construction contract, which has been confirmed by previous effective judgment. In the case of default in payment, it is reasonable and customary and not harmful to the interests of the contract-issuing party for it to offset its debt by the commercial housing constructed by the actual constructor at its market value. Now, the contract-issuing party as seller of the commercial housing alleges that the actual constructor as the buyer of the commercial housing fabricates the sales contract of commercial housing, who is suspected of bad faith lawsuit, and submits criminal investigation materials as new evidence for applying for civil retrial. Because nothing has changed to the basic fact of defaulting in project payment, and the criminal investigation materials proves the guilt or innocence, and the severity of the punishment, rather

Collegial panel judges of the Supreme People's Court for re-trial: Feng Xiaoguang, Luo Dian, Wan Ting (Written by: Feng Xiaoguang, Supreme People's Court; Translated by: Niu benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_10

than a civil claim, the probative value of the criminal investigation materials, which are not included in the civil proceedings and not subject to cross-examination by the other litigant, is insufficient to reverse the principle of high probability of evidence adopted by the trial court.

Case Information

1. **Parties**

Applicant in the retrial (Defendant in the first instance, Appellant in the second instance): Panjin Urban Construction & Real Estate Development Co., Ltd. (hereinafter referred to as "Urban Construction & Development Co.")
Respondent in the retrial (Plaintiff in the first instance, Appellee in the second instance): Xu X

2. **Procedural History**

First Instance: No. 00049 [2015], Trial, Civ. Division, Panjin Intermediate People's Court of Liaojiang Province (dated Oct. 15 of 2015)
Second Instance: No. 000569 [2016], Final, Civ. Division, the Higher People's Court of Liaoning Province (dated Mar. 11 of 2016)
Application for Retrial: No. 390 [2018], App. Ruling, Civ. Division, the Supreme People's Court (dated May 23 of 2018)

3. **Cause of Action**

Dispute over real estate sales contract

Essential Facts

On November 8, 2009, Panjin Urban Construction Co., Ltd. (hereinafter referred to as "Urban Construction Co.") entered into a Construction Contract for Construction Engineering with the Defendant Urban Construction & Development Co., whereby Urban Construction Co. will undertake Urban Construction & Development Co.'s International Apartment Project located to the east of Taishang Road and to the north of Huibin Street of Xinglongtai District. The Project was completed in May 2011 and delivered for use. The actual constructor of the Project is Xu X, the Plaintiff in this case. Because, during the construction of the Project, Urban Construction & Development Co. failed to make project payment in full pursuant to the Contract, the two parties entered into a Sales Contract of Commercial Housing on February 19, 2011, with Urban Construction & Development Co. being the Seller, and Xu X being the Buyer. The real estate for sale, located at No. 2, Unit 1, Building 1,

International Apartment, to the east of Taishang Road and north of Huibin Street, Xinglongtai District, is for commercial use, with a building area of 1244.75 m^2 (the address and area registered in Panjin Real Estate Transaction Administration Office are No. 102, International Apartment, located to the east of Taishang Road and north of Huibin Street, Xinglongtai District, and a building area of 1426.90 m^2), and a total amount of RMB 8,090,875 calculated by the building area at RMB 6,500 per square meter. The contract also contains such provisions as confirmation of area, handling of area difference, means and time of payment, time for the delivery of the real estate, and each party's liability for the breach of contract. On the day of signing the Contract, the accountant from Urban Construction & Development Co. issued a special collection voucher to Xu X for the amount of RMB 8,090,875.

In a separate case, Xu X sues Urban Construction & Development Co. for recovery of project payment in arrears. The Higher People's Court of Liaoning Province rendered a civil judgment (No. 00358 [2014], Final, Civ. Division) on May 13, 2015, finding that Urban Construction & Development Co. still owes Xu X the project payment in the amount of RMB 5,575,555.72.

Xu X files a lawsuit to the court, requesting the court to confirm the validity of the Sales Contract of Commercial Housing (No. 0029970) entered into by the Parties on February 19, 2011, and order Urban Construction & Development Co. to assist Xu X to go through formalities for real estate registration.

The court of first instance rules that: "(1) The Sales Contract of Commercial Housing entered into by the Plaintiff Xu X and the Defendant Urban Construction & Development Co. is valid and shall continue to be performed; (2) The Plaintiff Xu X shall pay the Defendant Urban Construction & Development Co. the outstanding real estate purchase price within 10 days after the effective date of this Judgment [total real estate purchase price of RMB 8,104,850 less the principal and interest of the outstanding project payment owed by Urban Construction & Development Co. to the Plaintiff, among which the principal is RMB 5,575,555.72, and the interest is calculated from the civil judgment of the Higher People's Court of Liaoning Province (No. 00358 [2014], Final, Civ. Division) to the date of execution of the judgment of this case]. On day when the Plaintiff fully settles the real estate payment, the Defendant shall deliver the real estate to the Plaintiff and assume the obligation to assist the Plaintiff in going through procedures for real estate registration."

Unsatisfied with the judgment of the court of first instance, Urban Construction & Development Co. lodged an appeal and the court of second instance ruled on December 28, 2016 to dismiss the appeal and sustain the original judgment. Unsatisfied with the judgment of the second instance, Urban Construction & Development Co. applied to the Supreme People's Court for retrial.

The main ground for Urban Construction & Development Co. to apply to the Supreme People's Court for retrial is that the discovery of new evidence that Xu X submitted to the trial court false evidentiary materials is sufficient to reverse the original judgment, alleging that evidence from the criminal case of bad faith lawsuit of which Xu X is suspected can be used as evidence for this civil retrial case. It obviously lacks sufficient basis for the courts of first instance and second instance to find in their judgments that the Sales Contract of Commercial Housing is truthful,

lawful and valid solely by the genuine official seal affixed to the original of the Sales Contract of Commercial Housing, causing erroneous finding of facts, logical errors and contradicted content in the judgment. It is pleaded to reverse the judgments of the courts of first instance and second instance and retrial the case.

Issues

1. Whether the Sales Contract of Commercial Housing involved in the case is a truthful contract;
2. Whether it is valid for Urban Construction & Development Co. to offset project payment in arrears by the contracted commercial housing.

Holding

Upon review, the Supreme People's Court holds that the application by Urban Construction & Development Co. for retrial does not fall under circumstances set forth in Article 200 (1) and (3) of the *Civil Procedure Law*. It is ruled to dismiss the application by Urban Construction & Development Co. for retrial.

Comment on Rule

The focus in this case is whether the Respondent Xu X's suspected crime of bad faith lawsuit is a legal cause for retrial.

1. **With regard to the nature of civil legal relationship in this case**

The civil legal relationship in this case is a sales contract of commercial housing in nature, with Urban Construction & Development Co. being the Seller, and Xu X being the Buyer. The underlying civil legal relationship is the construction contract, with Urban Construction & Development Co. being the Contract-issuing Party, and Xu X being the Contractor. In a separate case where Xu X sues Urban Construction & Development Co. for recovery of project payment in arrears, the Higher People's Court of Liaoning Province finds in its civil judgment of last resort (No. 00385 [2014], Final, Civ. Division) that Urban Construction & Development Co. still owes project payment in the amount of RMB 5,579,009.87. In the Statement of Fact and Commitment Letter issued by Urban Construction Co. on September 6, 2013, it agreed to use the claim in project payment to offset the purchase price of the real estate purchased by Xu X from Urban Construction & Development Co. The judgment of the second instance holds that it is another legal relationship that whether

the Sales Contract of Commercial Housing between Xu X and Urban Construction & Development Co. is formed and, if formed, whether it is valid, for which the Parties have filed a separate lawsuit, so it will not be handled in this case. Therefore, judgment of the second instance rules that: Urban Construction & Development Co. shall within 10 days from the effective date of this judgment make project payment of RMB 5,575,555.72 to Xu X and the interest thereon for the period from June 4, 2013 to the date of payment as determined in this judgment on the loan interest rate of the same kind for the same period as stipulated by the People's Bank of China. Unsatisfied with the judgment of the second instance, Urban Construction & Development Co. applies to the Supreme People's Court for retrial. The Supreme People's Court dismisses the application of Urban Construction & Development Co. for retrial in its civil ruling (No. 3367 [2015], App. Ruling, Civ. Division). Accordingly, the project payment of RMB 5,575,555.72 owed by Urban Construction & Development Co. to Xu X is confirmed by effective legal instrument. Urban Construction & Development Co. fails to perform its obligation of making project payment in arrears and the interest thereon on the date specified in the effective judgment. Pursuant to Article 93 of the *Judicial Interpretation on the Civil Procedure Law* and Article 9 of the *Rules of Evidence in Civil Procedure Evidence*, a party needs not produce evidence for facts confirmed by effective rulings issued by people's courts, unless sufficient evidence shows otherwise. Accordingly, the underlying civil legal relationship in this case is sufficient to confirm that Urban Construction & Development Co. owes Xu X project payment of RMB 5,575,555.72 and the interest thereon.

2. **With regard to whether there is any logical error or contradicted content in the original judgment**

There is no logical error or contradicted content in the original judgment. The Higher People's Court of Liaoning Province renders a civil judgment (No. 000569 [2015], Final, Civ. Division) affirms Item 2 of the civil judgment of the Intermediate People's Court of Panjin, Liaoning Province (No. 00049 [2013], Civ. Division): "The Plaintiff Xu X shall pay the Defendant Urban Construction & Development Co. the outstanding real estate purchase price within 10 days after the effective date of this Judgment (total real estate purchase price of RMB 8,104,850 less the principal and interest of the outstanding project payment owed by the Defendant to the Plaintiff…)." In a separate case, the Higher People's Court of Liaoning Province, in its civil judgment of last resort, rules that: Urban Construction & Development Co. shall within 10 days from the effective date of this judgment make project payment of RMB 5,575,555.72 to Xu X and the interest thereon for the period from June 4, 2013 to the date of payment as determined in this judgment on the loan interest rate of the same kind for the same period as stipulated by the People's Bank of China. Urban Construction & Development Co. claims that because real estate purchaser Xu X did not pay real estate seller Urban Construction & Development Co. the purchase price, it is logical for Xu X to pay the purchase price and overdue payment interest, instead of ordering Xu X to pay Urban Construction & Development Co. "project payment and interest", i.e., Urban Construction & Development Co. shall pay Xu X not only the principal of project payment in arrears, but the interest thereon, which

is obviously not in line with the judgment that "the Plaintiff Xu X shall pay the Defendant Urban Construction & Development Co. the outstanding real estate purchase price within 10 days after the effective date of this Judgment", contradictory in content and logic. The Supreme People's Court holds that: by comparing the wording of the judgments' texts of the preceding case and the current case adjudicated by the Higher People's Court of Liaoning Province, it is clear the textual content of the two documents is based on project payment of RMB 5,575,555.72 and the interest thereon owed by Urban Construction & Development Co. to Xu X, while the Sales Contract of Commercial Housing is signed based on the project payment owed by Urban Construction & Development Co. as contract-issuing party to Xu X as actual constructor, with the principal and interest of project payment in arrears used as real estate purchase price, for the purpose of offsetting creditor's claim in project payment against the debt of project payment in arrears as housing purchase price. Meanwhile, the judgment of the second instance holds that: "it is another legal relationship that whether the Sales Contract of Commercial Housing between Xu X and Urban Construction & Development Co. is formed and, if formed, whether it is valid, for which the Parties have filed a separate lawsuit, so it will not be handled in this case." The judgments of the preceding case and the current are clear in meaning and free from any contradiction or ambiguity by stating that the principal and interest of project payment owed by Urban Construction & Development Co. to Xu X will be used as real estate purchase price, with any balance paid by cash. Judging from trial practice, when the contract-issuing party owes project payment to the constructor, the constructor would choose payment in the first place, but would consider such alternatives as offsetting project payment in arrears by the contracted commercial housing if the contract-issuing party does not have sufficient means of payment. Judging by common sense, under the circumstances that Urban Construction & Development Co. owes project payment to Xu X, we cannot exclude the possibility that the developer would enter into a sales contract of commercial housing with the constructor at the normal market price at the time of signing to repay the project payment in arrears. Accordingly, there is no logical error or contradicted content in the original judgment.

3. **With regard to the probative value of the new evidence submitted by Urban Construction & Development Co. when applying for retrial**

The new evidence submitted by Urban Construction & Development Co. for retrial has probative value, not sufficient enough to overturn the original judgment. The new evidence is mainly documentary evidence from the public security sub-bureau on criminal investigations of Xu X suspected bad faith lawsuit, such as examination and filing of the case, investigation and evidence collection, letter reply to the reporter, and initial investigation report. The public security sub-bureau has filed the case concerning Xu X's suspected bad faith lawsuit and has not completed its investigation. The Supreme People's Court holds that: pursuant to Article 93 of the *Judicial Interpretation on the Civil Procedure Law* and Article 9 of the *Rules of Evidence in Civil Procedure*, the probative value of the above-mentioned documentary evidence

is not sufficient to overturn the relevant evidence supporting the original judgment with high probability.

For some of the new evidence submitted by Urban Construction & Development Co., its probative value would be affected for lack of procedural safeguards in civil proceedings. A civil action is an action filed by one party against the other party based on property or personal relations, with the parties having the same rights and obligations in litigation. The core is their equal status in litigation. Pursuant to Article 68 of the *Civil Procedure Law*, Articles 103, 104 and 105 of the *Judicial Interpretation on the Civil Procedure Law*, and other laws and judicial interpretations, evidence shall be analyzed and judged based on statutory rules for the use of evidence. Evidence not being cross-examined by the other party cannot be used as the basis for determining the merits of the case. In criminal proceedings, investigative measures taken, and documentary examination and authentication made, by investigating organs when detecting criminal cases for the purpose of proving the guilt or severity of the crime may but not necessarily have probative value for the facts to be proven in civil dispute. The conclusions submitted by Urban Construction & Development Co., which is made by the investigative organ after documentary examination and authentication when detecting criminal cases, has some probative value, but its probative value is affected for not being included in civil proceedings and not being subject to confrontation by the other party, so it cannot be treated equally as judicial expertise for civil disputes in civil proceedings.

4. **With regard to whether the case constitutes a civil bad faith lawsuit**

From the perspective of civil litigation, this case does not constitute a civil bad faith lawsuit. Pursuant to the *Guiding Opinions on Preventing and Punishing Bad Faith Lawsuits* and the *Opinions of the Supreme People's Court on Surveying "Offsetting Debts with Housing Properties" and Other Bad Faith Lawsuits*, typical bad faith lawsuits in civil litigation mainly refers to fabrication of facts at issue in civil disputes by the parties in civil litigation through collusion, malicious collaboration and coordination to acquire by fraud effective legal instruments through lawful civil proceedings with an aim to infringe upon national interests, social public interests or the legitimate rights and interests of person not involved in the case. The Supreme People's Court holds that there exists true dispute over civil rights and interests between Urban Construction & Development Co. and Xu X, and existing evidence is insufficient for the court to find malicious collusion between Urban Construction & Development Co. and Xu X and damage to the legitimate civil rights and interests of others, which is typical in a bad faith lawsuit.

The first instance, based on the evidence provided by both parties, finds that "the relative strong probative value of the evidence submitted by Xu X for its claim can prove the fact that there is sale of commercial residential building between the parties and Urban Construction & Development Co.'s offsetting project payment in arrears with housing properties; and the testimony and other evidence submitted by Urban Construction & Development Co. is obviously insufficient to overturn the documentary evidence submitted by Xu X. Therefore, it should be found that the Sales Contract of Commercial Housing signed by both parties is valid and the

contract should continue to be performed." In the second instance, with regard to the appeal filed by Urban Construction & Development Co., it cannot be concluded that the Sales Contract of Commercial Housing is a sham contract because the court holds that such issues as defective formal requirements regarding the contract involved in the case and failure to make online record that are alleged by Urban Construction & Development Co. are not elements for the formation of contract, and the testimony of witnesses called by Urban Construction & Development Co. does not indicate any direct and negative manifestation of intent to the Sales Contract of Commercial Housing, nor deny the finding that the seal affixed to the Sales Contract of Commercial Housing is identical to the official seal of Urban Construction & Development Co..

The Supreme People's Court holds that, from opinions of the first-instance and second-instance judgments, the findings are made through comprehensive analysis based on the basic legal relationship of a construction contract between the parties by comparing the probative value of the evidence provided by the parties pursuant to the rule of high probability of evidence. Despite of its compliance with the law and basis from legal theory, there is a possibility that this method of adjudicating does not match the actual situation. Paragraph 1, Article 108 of the *Judicial Interpretation on the Civil Procedure Law* stipulates that "for evidence provided by a party who bears the burden of proof, the people's court shall find the facts existing if it is convinced through examination and together with relevant facts that there is a high probability for the existence of the facts to be proven." Paragraph 1, Article 75 of the *Rules of Evidence in Civil Procedure* stipulates that "if two parties respectively produce contradictory evidence on the same fact, but fails to rebut the other party's evidence by sufficient ground, the people's court shall, in light of the circumstances of the case, determine whether the probative value of the evidence provided by one party is significantly greater than that by the other party, and confirm the evidence with greater probative value." In the case of Xu X's suspected bad faith lawsuit alleged by Urban Construction & Development Co., where a valid criminal judgment has yet been entered to confirm that the civil contract involved is a sham contract, the new evidence provided by Urban Construction & Development Co. is not sufficient to overturn the reasonableness of the original judgment in its determination that the Sales Contract of Commercial Housing is genuine.

Zheshang Jinhui Trust Co., Ltd. v. Zhejiang Sunion Group Co., Ltd., Sunion Holdings Group Co., Ltd., et al. (Dispute over Financial Loan Contract)—Creation of Mortgage of Project under Construction and the Scope of the Collateral

Lunjun Zhou

Rule

Mortgage of construction in progress, as a civil right set forth in the *Property Law*, falls under matters governed only by law as set forth in Article 8(8) of the *Legislative Law*. The content of such civil right cannot be derogated by undue restrictions or misunderstanding by any other person. The parties have expressly agreed in the mortgage contract that the scope of mortgage of the construction in progress includes the construction land use right and the construction in progress on it, and have submitted the mortgage contract, construction planning permit and other materials to the registration authority for filing. Under the circumstances that the registration authority due to any reason attributable to itself only issues certificate of title to the completed housing, the scope of the mortgage of the construction in progress shall be determined based on full account of the materials submitted by the parties for filing.

Collegial panel judges of the Supreme People's Court for re-trial: Zhou Lunjun, Zhang Aizhen, Wang Jun (Written by: Zhou Lunjun, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_11

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellant in the second instance): Zheshang Jinhui Trust Co., Ltd. (hereinafter referred to as "Jinhui Trust Co.")
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): Zhejiang Sunion Group Co., Ltd. (hereinafter referred to as "Zhejiang Sunion Co.")
Defendant in the first instance: Sunion Holdings Group Co., Ltd. (hereinafter referred to as "Sunion Holdings Co.")
Defendant in the first instance: Ma X
Defendant in the first instance: Lou X
Defendant in the first instance: Jinhua Huayuan Real Estate Co. Ltd. (hereinafter referred to as "Huayuan Real Estate Co.")

2. Procedural History

First Instance: No. 11 [2016], Trial, Civ. Division, Hangzhou Intermediate People's Court of Zhejiang Province (dated Jul. 29 of 2016)
Second Instance: No. 718 [2017], Final, Civ. Division, the Higher People's Court of Zhejiang Province (dated Apr. 24 of 2017)
Application for Retrial: No. 4047 [2017], App. Ruling, Civ. Division, the Supreme People's Court (dated Dec. 6 of 2017)
Second Instance: No. 722 [2017], Final, Civ. Division, the Supreme People's Court (dated Dec. 29 of 2017)

3. Cause of Action

Dispute over financial loan contract

Essential Facts

On March 10, 2014, Jinhui Trust Co. and Zhejiang Sunion Co. signed the Trust Loan Contract, stipulating that Jinhui Trust Co. will provide Zhejiang Sunion Co. with a loan of RMB 195 million, which will be used exclusively for follow-up construction of Sunion Guiyu Shanju Project (Phase II). On the same day, Zhejiang Sunion Co. and Jinhui Trust Co. signed the Mortgage Contract (Zhe Jin Trust Mort. HY-2014-016-1), stipulating that the land use right of the plot under the target project located at Andi Village Andi Town, Jinhua City and the construction in progress on the plot will be used as collateral for the above loan contract, and that, except as otherwise stipulated by law, any newly added buildings on the collateral during the mortgage period shall be included within the scope of collateral under this contract. The list of collaterals attached to the contract specifies that the collateral is the construction in

progress of the Guiyu Shanju (Phase II) developed by the Mortgagor and the land use right corresponding to the part of the construction in progress, including 48 townhouses of Buildings No. 14, 15 and 16, and 51 apartments of G5 and G6 High-rise Buildings. On March 12, 2014, Jinhui Trust Co. and Zhejiang Sunion Co. jointly applied for mortgage of construction in progress with Zhejiang Jinhua Real Estate Transaction Certificate Issuing Center. On March 13, 2014, Zhejiang Jinhua Housing and Urban-Rural Development Bureau issued a Certificate of Mortgage Registration of Construction in Progress for each of the 99 housing properties specified in the above-mentioned list of collaterals, in which the "Location of Construction in Progress" column was filled out with specific housing number. Zhejiang Sunion Co. subsequently submitted a Mortgage Release Application to Jinhui Trust Co., applying the latter to issue Mortgage Release Certificate for 179 housing properties in Guiyu Shanju Project (Phase II) on the ground that the sales contracts need to be filed with Housing Administration Bureau, among which 66 housing properties are on the list of collaterals attached to the above-mentioned Mortgage Contract, and the remaining 113 housing properties are not on the list of collaterals. Jinhui Trust Co. issued the Certificate to Zhejiang Jinhua Housing Administration Bureau, which then allowed the sale of the above-mentioned 179 housing properties.

On December 11, 2014, Zhejiang Sunion Co. and Jinhui Trust Co. signed the Mortgage Contract (Zhe Jin Trust Mort. HY-2014-016-3) to provide mortgage for the above-mentioned RMB 195 million trust loan, with the collateral being the construction in progress on the plot located at Andi Village, Andi Town, Jinhua, and the land use right of the area of its occupation. The list of collaterals indicates the number of Land Use Certificate, Planning Permit for Construction Land, Planning Permit for Construction Engineering, Construction Permit, and location, including 17 apartments of G5, G6, G7, and G8 High-rise Buildings. On December 11, 2014, both parties jointly applied to Zhejiang Jinhua Real Estate Transaction Certificate Issuing Center for mortgage of the construction in progress. On March 13, 2014, Zhejiang Jinhua Housing and Urban-Rural Development Bureau issued a Certificate of Mortgage Registration of Construction in Progress for each of the 17 housing properties specified in the above-mentioned list of collaterals, in which the "Location of Construction in Progress" column was filled out with specific housing number.

Due to the breach of contract by Zhejiang Sunion Co., Jinhui Trust Co. announced acceleration of the loan and filed a lawsuit with the court, requesting confirmation of the amount of the creditor's rights and priority in satisfaction of the above-mentioned debt against proceeds from auction, realization or otherwise of the mortgaged property, i.e., the above-mentioned land use rights and the construction in progress.

The Intermediate People's Court of Hangzhou, Zhejiang Province rendered a civil judgement (No. 11 [2015], Final, Civ. Division) "to confirm the creditor's rights of Jinhui Trust Co. against Zhejiang Sunion Co., Sunion Holdings Co. and Huayuan Real Estate Co. in the amount of the principal of RMB 195 million, interest of RMB 59,767,898.2, and attorney's fee of RMB 100,000, totaling RMB 254,867,898.2; to confirm Jinhui Trust Co.'s priority in satisfaction of the above-mentioned debt against the discounted price, or proceeds from auction or realization, of the 50 housing properties provided by Zhejiang Sunion Co.."

Unsatisfied with the above-mentioned judgment, Jinhui Trust Co. appealed to Zhejiang Higher People's Court. The court of second instance rendered a judgment on April 24, 2017, dismissing the appeal and sustaining the original judgment. Unsatisfied with the judgment of the second instance Jinhui Trust Co. applied to the Supreme People's Court for retrial.

The main ground for Jinhui Trust Co. to apply to the Supreme People's Court for retrial is that the land use right in its entirety and the corresponding entire construction in progress involved should be the subject matter of the mortgage, so it is wrong for the trial court in its fact finding and application of law to determine relevant rights solely on the basis of the certificate of encumbrance issued by the registration authority. Request to revoke judgment of the second instance and Item 2 of the judgment of the first instance judgment, and support its claims.

Issues

Whether the mortgage of the construction in progress is lawfully created and how to determine the scope of the collateral, i.e., whether the mortgage of the construction in progress enjoyed by Jinhui Trust Co. is limited to only the housing for which the registration authority has issued the Certificate of Mortgage Registration of Construction in Progress, or to the land use right in its entirety occupied by the construction in progress involved in the case together with the completed buildings on the plot and the buildings to be built in the future according to the planning.

Holding

Upon review, the Supreme People's Court holds that the ground for the application of Jinhui Trust Co. is established and decides to issue a writ of certiorari.

In the retrial, the Supreme People's Court finds that, pursuant to Articles 16 and 17 of the *Property Law*, the real property register is the basis for determining the ownership and contents of a real property, while the certificate of ownership of real property proves the right holder's real right in real property. In case of any inconsistency, the real property register shall prevail, unless evidence proves to the contrary. Thus, it is real estate registration that completes notice of real right in real property, and the legal effect of registration authority's respective issuance of the Certificate of Mortgage Registration of Construction in Progress for 116 housing properties involved in the case is to enable Jinhui Trust Co. to obtain the certificate of ownership to prove its rights. So the scope of the construction in progress of Jinhui Trust Co. as collateral shall be determined on the basis of real estate registration by the registration authority. In the case where the registration authority neither has a real property register, nor specify in the mortgage contract the method of mortgage registration for construction in progress, because the above-mentioned mortgage contract

and relevant registration application materials as well as the receipts issued by the registration authority all specify that the type of registration is the mortgage registration of the construction in progress, and these materials are registration materials filed by the registration authority for inspection, through which interested parties can know of any encumbrance on the collateral, it should be found that the registration authority's act of handling such business as mortgage registration of the construction in progress upon its receipt and review has completed the work of "recording" mortgage registration of the construction in progress, and the mortgage of the construction in progress is thus lawfully created. Therefore, in this case, mortgage of the construction in progress of Jinhui Trust Co. is lawfully created, and the scope of the collateral under the mortgage should be determined on the basis of the mortgage contract. The ground asserted by the Applicant Jinhui Trust Co. is established and shall be lawfully supported that, in addition to the housing properties already sold before mortgage registration and the 179 housing properties sold after mortgage registration with its consent and the corresponding land use right, the mortgage of the construction in progress shall include other state-owned land use right and the construction in progress thereon under the Certificate of State-owned Land Use Rights [Jin No. 103-02695 (2014)], including the uncompleted part. Finally, the Supreme People's Court rules to confirm Jinhui Trust Co.'s priority in satisfaction of the debt against the discounted price, or proceeds from auction or realization, of the buildings already built or to be built under the Planning Permit for Construction Engineering, and the corresponding State-owned land use right under the Certificate of State-owned Land Use Right, provided by Zhejiang Sunion Co., less the 201 housing properties and the corresponding land use right (the housing properties already sold before mortgage registration and the housing properties released with the consent of Jinhui Trust Co.).

Comment on Rule

The most important feature of mortgage of the construction in progress lies in the particularity of the collateral, i.e., it is not for buildings constructed, but for buildings under construction. This particularity has let to so different views in theory and practice on the scope of the subject matter of the mortgage of the construction in progress and how the mortgage of the construction in progress shall be created through registration that is affects the realization of the rights of the mortgagee.

1. **Whether mortgage registration of the construction in progress is registration per se or preliminary registration**

Registration of mortgage of construction in progress is in nature registration per se, and the right holder then enjoys mortgage, which is not conditioned on changing registration of mortgage of the construction in progress to registration of mortgage of the housing properties. The construction in progress is legally recognized real estate, and mortgage of the construction in progress is in nature real right in real property prescribed by law. Article 5 of the *Property Law* stipulates that the varieties

and contents of real rights shall be stipulated by law. Pursuant to the basic principles of the *Property Law*, an independent thing with the nature of specificity can be a subject matter of real rights, but independence here is not a physical concept, but should be determined according to general socio-economic ideas or legal provisions, because whether there is benefits under direct control and the possibility of notice will change with social and economic needs and technological progress. Although the construction in progress is in terms of physical form a future thing not yet independent or even unconstructed, the law specifically includes it within the scope of real right in real property because it can be disposed of in the market, the constructor can obtain proceeds by selling or mortgage the construction in progress, and such disposal can fully display the utility of the thing, enhance financing ability, and promote economic development. The *Property Law* stipulates that construction in progress can be mortgaged as collateral. Article 180 thereof listing construction in progress together with buildings and other real fixtures, construction land use rights, land contractual management rights, means of communication and transportation, etc. as property that can be mortgaged, confers the properties of a thing on the construction in progress on the one hand, and differentiate the construction in progress from the constructed buildings that have undergone formalities for first registration on the other hand, thus establishing mortgage of construction in progress as a separate civil real right. The *Property Law* specifies the creation of mortgage of the construction in progress. Article 187 thereof provides that, as for mortgage of a building under construction, mortgage registration shall be made, and the mortgage shall be created as of the date of registration. As such, the registration of the mortgage of the construction in progress directly produces the legal effect of creating the mortgage, and the mortgagee can claim priority in satisfaction against the exchange value of the mortgage. Therefore, such registration is not preliminary registration to preserve its claim for the future creation of mortgage of buildings, but registration per se for direct creation of mortgage. In this case, since Jinhui Trust Co. and Zhejiang Sunion Co. have jointly applied to Zhejiang Jinhua Real Estate Transaction Certificate Issuing Center for mortgage registration of the construction in progress, it should be found that the mortgage of the construction in progress has been created, and Jinhui Trust Co. has right to claim priority in satisfaction against the proceeds from the construction in progress.

2. **Scope of the subject matter of mortgage of construction in progress**

Article 187 of the *Property Law* stipulates that, as for the mortgage of a building under construction, mortgage registration shall be made and the mortgage shall be created as of the date of registration. Therefore, it has become a key issue that must be resolved in determining the scope of collaterals that the mortgage registration formalities conducted by the registration authority for the construction in progress is limited only to those parts recorded in the list of collaterals as indicated in the Certificate of Mortgage Registration of Construction in Progress already issued, or includes the land use rights as agreed in the mortgage contract and the parts constructed or to be constructed on the land.

As for methods of mortgage registration of the construction in progress, Paragraph 2 of Article 34 of the *Measures on the Administration of Mortgage of Urban Real Estate* (Order No. 98 of the Ministry of Construction of the People's Republic of China) stipulates that "in the case of the mortgage of a pre-sale commercial housing or construction in progress, the registration authority shall so indicate on the mortgage contract. Where the mortgaged real estate is constructed within the mortgage term, the parties shall go through formalities anew for mortgage registration of the real estate after the mortgagor obtains the certificate of the real estate ownership". Article 60 of the *Measures for Housing Registration* (Order No. 168 of the Ministry of Construction) stipulates that "to apply for registration of the creation of mortgage on the construction in progress, an applicant shall submit a registration application, applicant's identity certificate, mortgage contract, contract on principal creditor's rights, Certificate of Construction Land Use Rights or Real Estate Ownership Certificate recording the status of land use rights, Planning Permit for Construction Engineering, and other necessary materials". Paragraph 3 of Article 25 stipulates that "the housing registration authority shall issue a registration certificate after recording on the housing register the preliminary registration, registration of mortgage of construction in progress or any other matter as required by law or regulation". Pursuant to the above-mentioned normative documents, registration of mortgage of construction in progress includes recording on either the mortgage contract or the housing register. As for the relationship between ownership certificate and register, Articles 16 and 17 of the *Property Law* stipulate that the real property register is the basis for determining the ownership and contents of a real property, while the certificate of ownership of real property proves the right holder's real right in real property. In case of any inconsistency, the real property register shall prevail, unless evidence proves to the contrary. Thus, it is real estate registration that completes notice of real right in real property, and the legal effect of registration authority's respective issuance of the Certificate of Mortgage Registration of Construction in Progress for 116 housing properties involved in the case is to enable Jinhui Trust Co. to obtain the certificate of ownership to prove its rights. So the scope of the construction in progress of Jinhui Trust Co. as collateral shall be determined on the basis of real estate registration by the registration authority.

3. Influence of the Registration Authority's Registration Method on Mortgage of Construction in Progress in Practice

At the time when the mortgage of the construction in progress was registered, Zhejiang Jinhua Real Estate Transaction Certificate Issuing Center as the registration authority did not implement the housing register system, and the method for mortgage of construction in progress was not explicitly recorded on the mortgage contract. In this case, after Zhejiang Jinhua Real Estate Transaction Certificate Issuing Center accepted the application for mortgage registration of construction in progress by Jinhui Trust Co. and Zhejiang Sunion Co., subject to the requirements set forth in the *Several Opinions on Further Ensuring the Registration of Mortgage of Construction in Progress* issued by Zhejiang Provincial Department of Housing and Urban Development, Hangzhou Central Branch of the People's Bank of China, and Zhejiang

Office of the China Banking Regulatory Commission (Zhe Jian Fang [2012] No. 28), it adopted the "list of collateral" method to limit the scope of collateral of construction in progress to the constructed and saleable portion and issued a Certificate of Mortgage Registration of Construction in Progress to each housing property within the constructed and saleable portion. However, adopting such registration method does not necessarily lead to the conclusion that the registration authority deems the scope of collateral of construction in progress be limited to the constructed or saleable portion. As for the registration authority's handling of the mortgage release registration for the 179 housing properties involved in the case, the registration authority required Zhejiang Sunion Co. to obtain consent from Jinhui Trust Co., whether the housing properties to be sold by Zhejiang Sunion Co. are listed in the List of Collaterals or not. It follows that the registration authority had a logically inconsistent understanding with regard to the scope of mortgage of construction in progress, because its limitation of the scope of collateral to the constructed or saleable portion of the construction in progress is more out of consideration of the means of registration or technology, and with the progress of the construction, the scope of collateral for the mortgage of construction in progress will be expanded with the increase of the constructed or saleable portion. Article 5 of the *Property Law* stipulates that "the varieties and contents of real rights shall be stipulated by law". Mortgage of construction in progress, as a civil right set forth in the *Property Law*, falls under matters governed only by law as set forth in Article 8(8) of the *Legislative Law*. The content of such civil right cannot be derogated by undue restrictions or misunderstanding by any other person. From the perspective of legislative development, to the extent that "the buildings under construction" is not defined to the contrary in Article 180(5) and Article 187 of the *Property Law*, "mortgage of construction in progress" shall be understood by prior normative documents. Before the promulgation of the *Property Law*, Article 47 of the *Judicial Interpretation on the Guaranty Law* stipulates that "as for mortgage of the housing or other building for which a lawful permit is obtained but no construction has commenced or it is still under construction, the people's court may find the mortgage valid when the parties have registered the collateral". Paragraph 5, Article 3 of the *Measures on the Administration of Mortgage of Urban Real Estate* also stipulates that "'mortgage of construction in progress' as used in these *Measures* means the acts of the mortgagor, for the purpose of getting the loan for financing the construction in progress, to mortgage the land use rights lawfully obtained together with the assets invested in the construction in progress to the loan bank without transferring the possession thereof as the guarantee for the repayment of the loan". Accordingly, mortgage of construction in progress, as an independent type of mortgage, includes not only the state-owned construction land use rights, but also the buildings constructed and yet to be constructed within the scope of the planning permit, except as otherwise agreed by the parties in the mortgage contract. In this case, the parties specify in the mortgage contract that the collateral includes land use rights and construction in progress, and that newly-added buildings are included in the scope of collateral. In the case where the registration authority neither has a real property register, nor specify in the mortgage contract

the method of mortgage registration for construction in progress, because the above-mentioned mortgage contract and relevant registration application materials as well as the receipts issued by the registration authority all specify that the type of registration is the mortgage registration of the construction in progress, and these materials are registration materials filed by the registration authority for inspection, through which interested parties can know of any encumbrance on the collateral, it should be found that the registration authority's act of handling such business as mortgage registration of the construction in progress upon its receipt and review has completed the work of "recording" mortgage registration of the construction in progress, and the mortgage of the construction in progress is thus lawfully created. Whether the registration authority thereafter actually issues a certificate of rights to the mortgagee and the time and manner of issuing such certificate cannot be the basis for determining whether the rights of the mortgagee are legally established.

Founder BEA Trust Co., Ltd. v. Ganzhou Julong High-Tech Industry Co., Ltd. and AVIC Trust Co., Ltd. (Dispute over Financial Loan Contract)—Difference Between Equity Repurchase and Withdrawal of Capital Contribution under Equity Trust Financing

Jingchuan Liu

Rule

When a trust company makes capital investment to a target company and withdraws after obtaining fixed income within the agreed period, and the funds used for the acquisition of equity come from the target company, whether such act constitutes withdrawal of capital contribution shall be determined by taking full consideration of the real transaction background of the trust company's repurchase of equity through the target company and the merits of the case. To the extent that relevant provisions of the *Company Law* and *Trust Law* are not violated, and such agreements as Trust Contract, Capital Increase and Share Expansion Agreement and Equity Acquisition Agreement are all valid, it is not appropriate to regard the above situation as withdrawal of capital contribution.

Collegial panel judges of the Supreme People's Court for the second instance: Liu Jingchuan, Liu Xuemei, Fang Jingang (Written by: Liu Jingchuang, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_12

Case Information

1. **Parties**

Appellant (Plaintiff in the trial): Founder BEA Trust Co., Ltd. (hereinafter referred to as "Founder BEA Trust")
Appellee (Defendant in the trial): Ganzhou Julong High-Tech Industrial Co., Ltd. (hereinafter referred to as "Julong High Tech")
Appellee (Defendant in the trial): AVIC Trust Co., Ltd. (hereinafter referred to as "AVIC Trust")

2. **Procedural History**

First Instance: No. 25 [2016], Trial, Civ. Division, the Higher People's Court of Hubei Province (dated Sep. 21 of 2016)
Second Instance: No. 309 [2017], Final, Civ. Division, the Supreme People's Court (dated Jul. 27 of 2017)

3. **Cause of Action**

Dispute over financial loan contract

Essential Facts

On June 29, 2010, China Construction Bank Co., Ltd. (hereinafter referred to as "China Construction Bank") as the Trustor entered into a Trust Contract with South China Trust Co. as the Trustee, which stipulates that China Construction Bank will entrust part of the funds raised by its monthly-opened asset portfolio RMB financial product "China Construction Bank Qian Yuan 1 Day Xin Yue Yi" to South China Trust Co. for management, utilization and disposal. The direction of investment includes investing part of the funds in Julong High Tech for equity investment. The trust fund in the amount of RMB 120 million should be delivered on June 30, 2010 to the trust property account opened by South China Trust Co. for the trust. The trust period is from 30 June 2010 to 30 June 2012. This trust is a designated fund trust, by which the Trustee in its own name invests trust funds to Julong High Tech for equity investment in the form of capital investment for share increase pursuant to the instructions of the Trustor, and the Trustee will enjoy the relevant rights and interests pursuant to relevant provisions of the Capital Investment for Share Allocation Agreement involved in the investment project and the Articles of Incorporation of Julong High Tech. Upon the expiration of the trust, the Trustee shall sign a separate Equity Acquisition Agreement with the acquiring party to transfer all the equity to realize the trust interests. On the same day, Party A South China Trust, Party B Xie X and Sun X and Party C Julong High Tech signed a Capital Investment for Share Allocation Agreement, which stipulates that Party A shall make capital investment of RMB 120 million to Party C with the trust funds involved in the Capital Trust

Contract of China Construction Bank, after which the registered capital of Julong High Tech will increase from RMB 100 million to RMB 220 million, and, upon corresponding adjustment of share percentage, Party A will hold 54.55% of Party C's shares. The shareholding period after capital investment is from 30 June 2010 to 30 June 2012. On June 30, 2010, Party A Xie X and Sun X, Party B South China Trust Co. and Party C Ganxian District Shirui New Materials Co., Ltd. signed an Equity Acquisition Agreement, which stipulates that, upon the expiration of the trust involved in the above-mentioned two agreements, Party A undertakes to unconditionally acquire at a premium the shares of Julong High Tech held by South China Trust Co. due to its capital investment in Julong High Tech, failing which Party C shall perform all the acquisition obligations of Party A. On the same day, Jiangxi Ganzhou Junyi Accounting Firm Co., Ltd. issued a capital verification report (No. 104 [2010]), which indicates that Julong High Tech has received the newly increased registered capital of RMB 120 million paid by South China Trust Co. Corresponding changes were made to the Articles of Incorporation and business registration of Julong High Tech Co. on the same day. On December 30, 2010, South China Trust Co. changed its name to AVIC Trust Co. On June 29, 2012, Julong High Tech made two transfers of RMB 80 million and RMB 40 million (totaling RMB 120 million) to AVIC Trust through Jinyuan Branch of Ganzhou Bank to the bank account of AVIC Trust at Ganxian District Branch of China Construction Bank. Before and after the transfer, there was no record in the financial statements of Julong High Tech for the transfer in such items as creditor's rights receivable, debt payable, long-term liabilities or reduction of capital reserve.

On November 22, 2012, Founder BEA Trust and Julong High Tech signed a Trust Loan Contract (No. FBTC-2012-05-212-02), which stipulates that Founder BEA Trust shall grant a loan of RMB 80 million at an annual interest rate of 10.6% to Julong High Tech for a period of 24 months starting from the day when the loan was actually granted as indicated on the loan transfer certificate. If Julong High Tech fails to repay its principal as agreed, Founder BEA Trust has the right to collect corresponding penalties and compound interest on overdue loans at the borrowing rate. On November 26 of the same year, Founder BEA Trust granted the principal of the loan in the amount of RMB 80 million to Julong High Tech. Julong High Tech did not pay interest on schedule and did not repay the principal after the loan expired. As of March 15, 2016, Julong High Tech still owed Founder BEA Trust the principal of the loan in the amount of RMB 80 million and interest of RMB 37,999,320.7 (including penalty and compound interest). Jiangxi South China Trust Co., Ltd. (hereinafter referred to as "South China Trust Co.") as the controlling shareholder of Julong High Tech formerly holding 54.55% of the shares of Julong High Tech transferred RMB 120 million from the bank account of Julong High Tech on June 29, 2012. Founder BEA Trust claims that such act constitutes withdrawal of capital contribution by taking advantage of the status as the company's actual controller to damage the interests of the company's creditors, which will seriously damage Founder BEA Trust Co. in its realization of the creditor's rights in the borrowing. South China Trust Co. now changes its name to AVIC Trust Co. Pursuant to relevant law, AVIC Trust shall be supplementarily liable for failure of Julong High Tech to

pay off its debts to the extent of its withdrawal of capital contribution. Founder BEA Trust filed a lawsuit with the court, which caused the dispute in this case.

At the trial of the second instance, both Julong High Tech and AVIC Trust recognized that, in the implementation of the Capital Investment for Share Allocation Agreement, the director accredited by AVIC Trust did not participate in the daily operation and management of Julong High Tech. Julong High Tech paid the agreed dividend to AVIC Trust on a quarterly basis and, on June 29, 2012 when AVIC Trust received in full from Julong High Tech the payment for share acquisition, AVIC Trust withdrew from Julong High Tech and thereafter collected no dividend from Julong High Tech. On September 14, 2012, AVIC Trust issued a Repayment Informational Note to Ganxian District Industry and Commerce Administrative Bureau, agreeing to discharge the shares of Julong High Tech pledged by Xie X and Sun X with AVIC Trust.

The creditors of Julong High Tech in its equity restructuring entrusted Jiangxi Ganzhou Huasheng Accountants' Firm Co., Ltd. to conduct an inventory of Julong High Tech's assets and liabilities on February 28, 2013, which issued a Special Audit Report (No. 52 [2014]).

On August 12, 2013, the shareholders of Julong High Tech were changed from 2 shareholder of Xie X and Sun X to 38 shareholders. Among them, the paid-in capital contribution of Xie X is RMB 72.762 million, accounting for 33.07%; that of Sun X is RMB 9.02 million, accounting for 4.01%; and another 36 people became shareholders of Julong High Tech by debt-to-equity swap. The Articles of Incorporation of Julong High Tech as revised on August 16, 2015 indicates that its registered capital is RMB 220 million, with 38 shareholders.

The court of first instance ruled on September 21, 2016 "(1) To order Julong High Tech to repay RMB 80 million as the principal of the loan and RMB 37,999,320.7 as the interest in arrears, overdue penalty and compound interest up to March 15, 2016, totaling RMB 117,999,320.7, to Founder BEA Trust within 10 days from the effective date of this judgment; (2) To dismiss other claims of Founder BEA Trust." Unsatisfied with the judgment, Founder BEA appealed to the Supreme People's Court, requesting to set aside Item 2 of the judgment of first instance pursuant to law, and order AVIC Trust to be supplementarily liable to Founder BEA Trust for the principal and interest of the loan of Julong High Tech Company in the amount of RMB 117,999,320.70 (interest calculated until March 15, 2016) to the extent of the funds withdrew in the amount of RMB 120 million.

Issues

Whether the act of collecting share transfer payment of RMB 120 million by AVIC Trust constitutes an act of withdrawing funds, and whether it should be supplementarily liable for the debt owed by Julong High Tech to Founder BEA Trust.

Holding

In the second instance, the Supreme People's Court holds that:

First, from the content and method of implementing the Trust Contract, Capital Investment for Share Allocation Agreement, and Equity Acquisition Agreement, the essence of AVIC Trust's equity investment is to obtain fixed investment returns through capital investment for share increase, instead of participating in or controlling the operation and management of the target company, and there is no evidence that AVIC Trust abused its status as a majority shareholder to obtain investment repurchase payment and dividends.

Second, AVIC Trust withdrew from Julong High Tech after receiving the equity payment upon the expiration of investment as agreed in the Capital Investment for Share Allocation Agreement, and issued on September 14, 2012 a Repayment Informational Note to Ganxian District Industry and Commerce Administrative Bureau, agreeing to discharge the shares of Julong High Tech pledged by Xie X and Sun X with AVIC Trust. Thereafter, AVIC Trust collected no dividends from Julong High Tech. When Julong High Tech and Founder BEA Trust signed the Trust Loan Contract on November 12, 2012, AVIC Trust did not participate in the resolution of the Board of Directors. It shows that although at this time AVIC Trust has not changed its industrial and commercial registration, it is in fact no longer a shareholder of Julong High Tech.

Third, it is a defect for AVIC Trust not to promptly register the change in equity after receiving the equity payment. However, failure to promptly register change in equity was due to Xie X's refusal to cooperate for the needs of Julong High Tech's asset restructuring, so AVIC Trust is not subjectively at fault. As a professional institution engaged in trust business, Founder BEA Trust should also be aware of the nature of equity investment trust. Therefore, there is insufficient legal basis to order AVIC Trust to be liable for the loan involved in the case solely on the inappropriateness of AVIC Trust's not promptly going through formalities for industry and commerce registration for the change.

Fourth, collection by AVIC Trust of equity payment of RMB 120 million is not obtaining funds without any consideration, which does not fall under any circumstances of shareholder's withdrawal of capital contribution as regulated by the Company Law and relevant judicial interpretations. In this case, there existed no insufficient capital contribution in Julong High Tech when AVIC Trust withdrew. The equity payment of RMB 120 million collected by AVIC Trust is in compliance with the Capital Investment for Share Allocation Agreement, i.e., from the acquiring party or Julong High Tech. After the transfer of equity by AVIC Trust, the registered capital of Julong High Tech was not reduced, and the rights and obligations of Founder BEA Trust were not actually damaged. The claim of Founder BEA Trust lacks factual basis that AVIC Trust withdrew its capital investment through fictitious debt or non-payment of consideration. Finally, the Supreme People's Court dismisses the appeal and sustains the original judgment.

Comment on Rule

1. **Whether collection of AVIC Trust of equity transfer payment of RMB 120 million from Julong High Tech constitutes an act of withdrawing capital contribution**

Pursuant to Article 12 of *Judicial Interpretation on Company Law (III)*, which stipulates that "withdrawal of capital contribution by shareholders of a company mainly includes: (1) making false financial and accounting statements to falsely increase profits for distribution; (2) transferring out its capital contribution through fictitious creditor-debtor relationship; (3) transferring out capital contribution through affiliated transactions; or (4) other acts of withdrawing capital contribution without following legal procedures." Although collection by AVIC Trust of equity payment of RMB 120 million is apparently obtained from the bank account of Julong High Tech, but it was not obtained without any consideration, which does not fall under any circumstances of shareholder's withdrawal of capital contribution as regulated by the Company Law and relevant judicial interpretations.

First, the Special Audit Report (No. 52 [2014]) involved in the case indicates that, as of February 28, 2013, the audit-confirmed number of paid-in capital collected by Julong High Tech is RMB 220,000,000.00, of which Xie X contributed RMB 59,000,000.00, Sun X contributed RMB 41,000,000.00, and Jiangxi South China Trust Co. Ltd. contributed RMB 120,000,000.00, but AVIC Trust fully collected the equity payment on June 29, 2012, showing that there existed no insufficient capital contribution in Julong High Tech when AVIC Trust withdrew.

Second, the equity payment of RMB 120 million collected by AVIC Trust was not paid directly by Xie Ruihong and Sun X pursuant to Equity Acquisition Agreement, but by the account of Julong High Tech. In this regard, Julong High Tech maintained that it was paid on behalf of Xie X. The Special Audit Report (No. 52 [2014]) confirms that Xie X has lent more than RMB 654 million for external financing, and as of February 28, 2013, Julong High Tech still owed Xie X RMB 237.168 million, thus there is indeed a creditor-debtor relationship between Xie X and Julong High Tech. Meanwhile, because Julong High Tech is a family enterprise controlled by Xie X, it is reasonable for Julong High Tech to make equity payment on behalf of Xie X. And the equity payment from either the acquiring party or Julong High Tech is in line with the above-mentioned Capital Investment for Share Allocation Agreement. As for the problem raised by Founder BEA Trust that Julong High Tech did not record the transfer in its financial accounts, there are some irregularities in the financial management of Julong High Tech, but AVIC Trust has no fault in this regard.

Third, the registered capital of Julong Hi-tech Company did not decrease after the transfer of equity by AVIC Trust. After changing investors to Xie X and Sun X in the industrial and commercial registration on August 4, 2013, Julong High Tech further changed investors by adding 36 shareholders on August 12, 2012, with the registered capital still being RMB 220 million in cash contribution. Up to March 2016 when Founder BEA Trust filed this lawsuit, there was no evidence of insufficient contribution to the registered capital of Julong High Tech and possible infringement

on the interests of third parties. Therefore, collection of equity payment by AVIC Trust as agreed did not result in the decrease of the registered capital of Julong High Tech and actual damage to the rights and interests of Founder BEA Trust. The claim of Founder BEA Trust lacks factual basis that AVIC Trust withdrew its capital investment through fictitious debt or non-payment of consideration.

2. **Whether AVIC Trust should be supplementarily liable for compensation**

Although the agreement that AVIC Trust will obtain a fixed dividend during the two-year capital investment and shareholding period is not in line with relevant administrative provisions of the Company Law on profit distribution, it does not affect the validity of the Capital Investment for Share Allocation Agreement and Equity Acquisition Agreement involved in the case. After AVIC Trust received in full the equity payment of RMB 120 million from the bank account of Julong High Tech on June 29, 2012, its transfer of equity held in Julong High Tech to Xie X and Sun X was an act of fulfilling the provisions of the agreement involved in the case. AVIC Trust withdrew from Julong High Tech after receiving the equity payment upon the expiration of investment as agreed in the Capital Investment for Share Allocation Agreement, and issued on September 14, 2012 a Repayment Informational Note to Ganxian District Industry and Commerce Administrative Bureau, agreeing to discharge the shares of Julong High Tech pledged by Xie X and Sun X with AVIC Trust. Thereafter, AVIC Trust collected no dividends from Julong High Tech. When Julong High Tech and Founder BEA Trust signed the Trust Loan Contract on November 12, 2012, AVIC Trust did not participate in the resolution of the Board of Directors. It shows that although at this time AVIC Trust has not changed its industrial and commercial registration, it is in fact no longer a shareholder of Julong High Tech. Although industrial and commercial registration of shareholders is a way of external notice of shareholders, it is not the only basis to confirm shareholders, who shall be confirmed by taking consideration of the agreement of the parties and the merits of the case. Claim by Founder BEA Trust that AVIC Trust was still a shareholder of Julong High Tech at the time of borrowing involved in the case is not consistent with the facts ascertained. Paragraph 2 of Article 32 of the *Company Law* stipulates that "a company shall register each shareholder's name in the company registration authority. Where any of the registered items is changed, the company shall modify the registration. If the company fails to do so, it shall not, on the basis of the unregistered or un-modified registration item, stand up to any third party." In this case, it is a defect for AVIC Trust not to go through formalities for equity transfer until August 4, 2013, which should be handled promptly together with Julong High Tech Trust after receiving the equity payment in full. However, whether AVIC Trust shall assume corresponding liability under the Trust Loan Contract involved in the case that is signed by Founder BEA Trust and Julong High Tech should be determined by taking full consideration of such factors as whether AVIC Trust was at fault and whether Founder BEA Trust has exercised its duty of care. First, from the facts ascertained, failure of AVIC Trust to promptly register change in equity was due to Xie X's refusal to cooperate for the needs of Julong High Tech's asset restructuring. Because industrial and commercial registration actually needs cooperation between

the parties, AVIC Trust is not subjectively at fault for failure to register change in shareholders. Second, as a professional institution engaged in trust business, Founder BEA Trust also has the duty of due diligence to investigate Julong High Tech when signing the Trust Loan Contract with Julong High Tech, should know about the trust information of equity investment by AVIC Trust in Julong High Tech, and should understand the nature of equity investment trust. Therefore, there is insufficient legal basis to order AVIC Trust to be liable for the loan involved in the case solely on the inappropriateness of AVIC Trust's not promptly going through formalities for industry and commerce registration for the change.

Shanghai Pudong Development Bank Co., Ltd. Guiyang Branch v. Guiyang Jinchang Precision Casting Co., Ltd., Feng X, et al. (Dispute over Guarantee and Financial Loan Contract)—Whether upon the Expiration of the Mining Right the Mortgage Created Thereon Will Continue to be Valid

Yongfeng Pan

Rule

Mining right is a usufructuary right, by which the mining right holder lawfully enjoys the right of possession, use and benefit over the mineral resources. Because the mining right exists within a certain period of time, after the expiration of mining right licensing and before the completion of the examination and approval registration for extension, the original mining right holder does not have the right to use and benefit over the mineral resources. However, the original mining right holder has property rights and interests over the mineral resources, which have property value, but does not fall under mining right. If the mortgage contract specifies that mortgage is created on the mining right within a specified period of time, whether the mining right or property rights and interests beyond that period can be mortgaged shall be agreed by both parties.

The security on property and personal security provided by the debtor can co-exist, whereby the creditor and the guarantor agree that, to realize the creditor's rights, the creditor has the right to first request the guarantor to assume the guarantor liability; and meanwhile the creditor and the debtor agree that, to realize the creditor's rights, the creditor has the right to first request the mortgagor to assume the mortgagor liability. The above provisions are not contradictory, nor will it lead to ambiguity

Collegial panel judges of the Supreme People's Court for the second instance: Pan Yongfeng, Zhang Chun, Li xiaoyun (Written by: Pan Yongfeng, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_13

in the agreement for the realization of security on property and personal guaranty. To realize creditor's rights, the creditor has the right to first request the guarantor to assume the guarantor liability pursuant to the contract.

Case Information

1. **Parties**

Appellant (Plaintiff in the first instance): Shanghai Pudong Development Bank Co., Ltd. Guiyang Branch (hereinafter referred to as "SPD Bank Guiyang Branch")
Appellant (Defendant in the first instance): Guiyang Jinchang Precision Casting Co., Ltd. (hereinafter referred to as "Jinchang Precision Casting")
Appellant (Defendant in the first instance): Feng X
Appellant (Defendant in the first instance): Ying X
Appellant (Defendant in the first instance): Guizhou Wanchang Dingsheng Trading Co., Ltd. (hereinafter referred to as "Wanchang Trading")

2. **Procedural History**

First Instance: No. 261 [2017], Trial, Civ. Division, the Higher People's Court of Guizhou Province (dated Aug. 28 of 2017)
Second Instance: No. 971 [2017], Final, Civ. Division, the Supreme People's Court (dated Dec. 25 of 2017)

3. **Cause of Action**

Dispute over guarantee and financial loan contract

Essential Facts

On October 17, 2014, SPD Bank Guiyang Branch and Jinchang Precision Casting signed a Current Funds Loan Contract in the amount of RMB 4 million. Feng X, as the guarantor, signed the Maximum Guarantee Contract, which sets forth the joint and several liability guarantee, i.e., when Jinchang Precision Casting fails to fulfill its obligations as stipulated in the Master Contract, the creditor has the right to request the guarantor to assume the guarantor liability within the scope of the guaranty agreed in this Contract, without first requesting other guarantors to assume the guaranty liability, regardless of whether the creditor has other security rights for the creditor's rights under the Master Contract. On the same day, Ying X, as Feng X's spouse, by signing the Letter of Commitment on Consent to the Execution of Community Property, consented to the signing and performance of the Guarantee Contract for the performance of the Maximum Guarantee Contract, and that the creditor has the right to dispose of the community property when Feng X is required to assume the guarantor liability. Jinchang Precision Casting, as the mortgagor, signed

the Mining Right Maximum Mortgage Contract, which stipulates that mortgage is created on the iron mining right of Ren Mine located at Fengting Township, Luodian County under the name of Jinchang Precision Casting, and that when the debtor fails to fulfill his obligations under the Master Contract, the mortgagee has the right to first request the mortgagor to assume the mortgagor liability within the scope of the guaranty agreed in this Contract, without first requesting other guarantors to assume the guarantor liability, regardless of whether the mortgagee has other security rights for the creditor's rights under the Master Contract.

On November 13, 2014, SPD Bank Guiyang Branch and Jinchang Precision Casting signed a Current Funds Loan Contract in the amount of RMB 11 million, with Feng X as the guarantor and Jinchang Precision Casting as the mortgager. The provisions of the Guarantee Contract and Mining Right Mortgage Contract are consistent with the aforementioned facts.

On March 20, 2015, SPD Bank Guiyang Branch and Jinchang Precision Casting signed a Current Funds Loan Contract in the amount of RMB 7 million for loan for short-term current funds, with Feng X as the guarantor and Jinchang Precision Casting as the mortgager. The provisions of the Guarantee Contract and Mining Right Mortgage Contract are consistent with the aforementioned facts. Jinchang Precision Casting, as the mortgagor, also signed the Maximum Mortgage Contract, which stipulates that mortgage is created on the land use right of Wangguan Village, Longchang Township, Xiuwen County, Guiyang City under the name of Jinchang Precision Casting, and that when the debtor fails to fulfill his obligations under the Master Contract, the mortgagee has the right to first request the mortgagor to assume the mortgagor liability within the scope of the guaranty agreed in this Contract, without first requesting other guarantors to assume the mortgagor liability, regardless of whether the mortgagee has other security rights for the creditor's rights under the Master Contract.

On December 18, 2015, SPD Bank Guiyang Branch and Jinchang Precision Casting signed a Current Funds Loan Contract in the amount of RMB 300,000. Feng X and Wanchang Trading as the guarantor and the provisions of the Guarantee Contract are consistent with the aforementioned facts.

The loans involved in the above-mentioned loan contracts have expired on October 14, 2016, November 10, 2017, January 24, 2017 and December 17, 2016, respectively. As of February 15, 2017, Jinchang Precision Casting still owed SPD Bank Guiyang Branch loan principal of RMB 22,157,000 (the principals owned in 4 loans are RMB 6,921,000, RMB 11 million, RMB 3,936,000, and RMB 300,000 respectively) and interest of RMB 1,452,019.97, to which no objection was raised by Jinchang Precision Casting, Feng X, Ying X and Wanchang Trading.

In the second instance, the Supreme People's Court finds that the validity period specified in the mining right license involved in the case has expired and Jinchang Precision Casting is applying for the extension of the mining right. Annex I List of Mortgaged Property (Category of Mining Right Mortgage) to the Mining Right Maximum Mortgage Contract signed by SPD Bank Guiyang Branch and Jinchang Precision Casting on January 18, 2013 provides that "the period of validity of mining right license is from March 2005 to March 2015." Article 6.1 of the Mining Right

Maximum Mortgage Contract specifies that "the mortgagor undertakes to maintain the validity of the mortgaged mining right throughout the term of this Contract, to notify the mortgagee in writing half a year before the expiration of the mining license, and to complete the formalities for the extension of the mining right before the expiration of the mining license as required."

SPD Bank Guiyang Branch filed a lawsuit with the court of first instance, which on August 28, 2016, rendered a civil judgment (No. 261 [2016], Trial, Civ. Division): (1) To rescind the Current Funds Loan Contract (No. 37012014280973), Current Funds Loan Contract (No. 37012014281076), Current Funds Loan Contract (No. 37012015280253) and Current Funds Loan Contract (No. 37012015281291) signed by SPD Bank Guiyang Branch and Jinchang Precision Casting; (2) To order Jinchang Precision Casting to repay SPD Bank Guiyang Branch within 10 days from the day when the judgment takes effect the loan principal of RMB 22,157,000 and the interest of RMB 1,452,019.97 as of February 15, 2017 (for interest after February 16, 2017, at annual interest rate of 9.63% for the principal of RMB 6,921,000, at annual interest rate of 11.7% for the principal of RMB 11 million, at annual interest rate of 11.8% for the principal of RMB 3,936,000, at annual interest rate of 6.53% for the principal of RMB 300,000, respectively calculated to the day when the period for performance as determined in the judgment expires); (3) To order Jinchang Precision Casting to pay the attorney fee of RMB 232,393.8 paid by SPD Bank Guiyang Branch within 10 days from the effective date of the judgment; (4) To grant SPD Bank Guiyang Branch the priority over the proceeds from auction or realization of the land use right of an area of 27,857.95 square meters located at Wangguan Village, Long X Township, X County, Guiyang City under the name of Jinchang Precision Casting (Certificate of Mortgaged Property No. 07 [2010], and Certificate of Encumbrance No. 3 [2013]) to the extent of the creditor's right of RMB 3.65 million; (5) To order Feng X and Ying X to be jointly and severally liable for any shortfall after satisfaction of the mortgaged property as listed in Item 4 of the judgment to the extent of the creditor's rights as listed in Items 2 and 3 of the judgment, and Wanchang Trading to be jointly and severally liable for any shortfall after satisfaction of the mortgaged property as listed in Item 4 of the judgment against the principal of the 4th loan (RMB 300,000) and interest, with Feng x, Ying x and Wanchang Trading having the right to recover from Jinchang Precision Casting after assuming the joint and several liability for satisfaction; and (6) To dismiss other claims of SPD Bank Guiyang Branch. For the case acceptance fee of RMB 157,855.75, RMB 150,000 shall be borne by Jinchang Precision Casting, Feng Yongfei and Ying Lijiao, and RMB 7855.75 shall be borne by Wanchang Trading. Unsatisfied with the judgment of the first instance, all parties appealed to the Supreme People's Court.

It is also found that on January 28, 2011, the mining right mortgage was registered for filing which will expire in May 2015. The validity period of the mining license on file is from August 2011 to March 2015.

Issues

1. The security on property and personal security provided by Jinchang Precision Casting can co-exist, whereby SPD Bank Guiyang Branch and the guarantor agree that, to realize the creditor's rights, SPD Bank Guiyang Branch has the right to first request the guarantor to assume the guarantor liability; and meanwhile SPD Bank Guiyang Branch and Jinchang Precision Casting agree that, to realize the creditor's rights, SPD Bank Guiyang Branch has the right to first request the mortgagor Jinchang Precision Casting to assume the mortgagor liability. Whether the agreement is unclear as to the sequence of realizing the personal security and security on property by each party, and how could SPD Guiyang branch realize its own creditor's right?
2. The mining right license involved in the mortgage in this case has expired, and application extension has not yet been approved. During this period, what rights and interests does the original mining right holder enjoy, and whether SPD Bank Guiyang Branch still enjoys the priority in satisfaction of the original mining right?

Holding

In the second instance, the Supreme People's Court holds that:

1. **Whether agreement on the realization of security on property and personal guaranty involved in the case is unequivocal.**

The security on property provided by the debtor Jinchang Precision Casting and personal security provided by the guarantor co-exist in this case. It is specified in both the two Maximum Guarantee Contracts signed by SPD Bank Guiyang Branch and Feng X and the Maximum Guarantee Contract signed by SPD Bank Guiyang Branch and Wanchang Trading that when the debtor fails to fulfill its obligations as stipulated in the Master Contract, the creditor has the right to request the guarantor to assume the guarantor liability within the scope of the guaranty agreed in the Contract, without first requesting other guarantors to assume the guaranty liability, regardless of whether the creditor has other security rights for the creditor's rights under the Master Contract. The above provisions are unequivocal in the agreement for the realization of security on property and personal guaranty. The court of the second instance corrects the clerical errors made in the judgment of the first instance in reference to the above contract clauses. In this case, the Mining Right Maximum Mortgage Contract and Maximum Mortgage Contract signed by SPD Bank Guiyang Branch and Jinchang Precision Casting also provide that when the debtor fails to fulfill his obligations under the Master Contract, the mortgagee has the right to first request the mortgagor to assume the mortgagor liability within the scope of the guaranty agreed in this Contract, without first requesting other guarantors to assume the mortgagor liability.

This provision and the provisions in the above-mentioned Guarantee Contract are not contradictory, nor will it lead to ambiguity in the agreement for the realization of security on property and personal guaranty. Therefore, pursuant to Article 176 of the *Property Law* that "where a secured creditor's right involves both security on property and personal security, if the debtor fails to pay its debts due or any circumstance for realizing the security interest as agreed by the parties occurs, the creditor shall realize the creditor's right as agreed", SPD Bank Guiyang Branch has the right to first require the guarantor to assume the guarantor liability pursuant to the provisions of the contract when realizing the creditor's right. The court of second instance corrects the improper determination in the judgment of the first instance that the agreement by the other party on the order of realizing the personal security and security on property is equivocal. Such claim raised by SPD Bank Guiyang Branch in appeal with factual and legal basis is supported by the Supreme People's Court.

2. **Whether the mortgage created on the mining right involved in the case is extinguished.**

First, pursuant to Article 117 of the *Property Law*, a usufructuary right holder lawfully enjoys the right of possession, use and benefit of the real property or movable property owned by someone else. Mining right is a usufructuary right, by which the mining right holder lawfully enjoys the right of possession, use and benefit over the mineral resources. The mining right exists within a certain period of time, and specially in this case will expire in March 2015. Although Jinchang Precision Casting has applied for the extension of the mining right, the competent department of land and resources has not yet approved it. Jinchang Precision Casting shall not engage in any mining activities until the registration of the extension has been completed. Therefore, during such period, Jinchang Precision Casting did not enjoy the right to use and benefit of the mineral resources of Ren Mine in Fengting Township, Luodian County. If the competent land and resources authorities finally approves the above-mentioned application for the extension of mining right, Jinchang Precision Casting can continue to enjoy the right to use and benefit from the mineral resources of Ren Iron Mine in Fengting Township, Luodian County. Therefore, Jinchang Precision Casting currently has property rights and interests over the mineral resources of Ren Iron Mine in Fengting Township, Luodian County, which have property value, but does not fall under mining right; second, in this case, "the period of validity of mining right licensing from March 2005 to March 2015" is specifically agreed by SPD Bank Guiyang Branch and Jinchang Precision Casting to be the period during which mortgage is created on the mining right. Whether the mining right or property rights and interests beyond that period can be mortgaged shall be agreed by both parties. Moreover, the period for the performance of the Mining Right Maximum Mortgage Contract is longer than the existence of the mining right, and the two parties also specifies in the Contract that "the mortgagor undertakes to maintain the validity of the mortgaged mining right throughout the term of this Contract, to notify the mortgagee in writing half a year before the expiration of the mining license, and to complete the formalities for the extension of the mining right before the expiration of the mining license as required." As a result, SPD Bank Guiyang

Branch has foreseen the expiration of the relevant mining right license during the period for the performance of the Contract and its inability to exercise the mortgage on the mining right involved in the case. In summary, it is not inappropriate for the judgment of the first instance to hold that the mortgage created on the mining right involved in this case is extinguished, and the court of second instance will not support the claim of SPD Bank Guiyang Branch that it has the right to mortgage on the mining right of Ren Iron Mine in Fengting Township, Luodian County, and has priority in satisfaction by the above rights due to its lack of factual and legal basis.

In addition, judgment of the court of first instance in its reasoning part specifically supports the claim of SPD Bank Guiyang Branch for payment of the principal and interest involved in the case, with the interest calculated to the day when the principal and interest are paid off, but the conclusion part wrongfully states the deadline for the payment of interest by Jinchang Precision Casting to be the expiration date as determined by the judgment for performance, which might lead to the consequence that the debtor who has actually paid the principal within the performance period as determined by the judgment still has to pay the interest, or the debtor who fails to perform the effective judgment upon the expiration date for performance does not need to continue to pay corresponding interest. Such consequence is rectified by the court of second instance.

In summary, such erroneous fact finding by the court of first instance shall be corrected. The Supreme People's Court at the second instance modifies the original judgment and rules: "(1) To affirm Items 1, 3 and 4 of the Civil Judgment of the Higher People's Court of Guizhou Province (No. 261 [2016], Trial, Civ. Division); (2) To reverse Item 6 of the Civil Judgment of the Higher People's Court of Guizhou Province (No. 261 [2016], Trial, Civ. Division); (3) To modify Item 2 of the Civil Judgment of the Higher People's Court of Guizhou Province (No. 261 [2016], Trial, Civ. Division) to read as follows 'to order Jinchang Precision Casting to repay SPD Bank Guiyang Branch within 10 days from the day when the judgment takes effect the loan principal of RMB 22,157,000 and the interest of RMB 1,452,019.97 as of February 15, 2017 (for interest after February 16, 2017, at annual interest rate of 9.63% for the principal of RMB 6,921,000, at annual interest rate of 11.7% for the principal of RMB 11 million, at annual interest rate of 11.8% for the principal of RMB 3,936,000, at annual interest rate of 6.53% for the principal of RMB 300,000, respectively calculated to the day of actual paying off)'; (4) To modify Item 5 of the Civil Judgment of the Higher People's Court of Guizhou Province (No. 261 [2016], Trial, Civ. Division) to read as follows 'to order Feng X and Yin X to be jointly and severally liable for all principal of RMB 22,157,000 and interest as well as the attorney fee of RMB 232,393.8 payable by Jinchang Precision Casting to SPD Bank Guiyang Branch, and Wanchang Trading to be jointly and severally liable for the fourth batch of loan principal of RMB 300,000 and interest payable by Jinchang Precision Casting to SPD Bank Guiyang Branch, with Feng X, Ying X and Wanchang Trading having the right to recover from Jinchang Precision Casting after assuming the joint and several liability for satisfaction'; and (5) To dismiss other claims of SPD Bank Guiyang Branch."

Comment on Rule

1. Whether the mortgage created on the mining right will extinguish upon the expiration of the mining right

This issue is not specified in the current law, which is a legal vacuum. To determine whether the mortgage created on the mining right is extinguished or not, we need first determine whether the mining right itself extinguishes upon the expiration of the mining right. Article 117 of the *Property Law* stipulates that "a usufructuary right holder lawfully enjoys the right of possession, use and benefit of the real property or movable property owned by someone else." Article 123 stipulates that "the mineral prospecting right, mining right, water intake right and right to use water areas or tidal flats for breeding or fishery shall be protected by law." The mining right is usufructuary right in nature. The biggest difference between usufructuary right and ownership is that usufructuary right contains no right of disposal for the possessory things, because it is the right to possess, use and benefit from the property owned by others. Whether or not the right can be enjoyed and the period of enjoyment must be licensed by the state or other people as the owner. Based on this characteristic, the usufructuary right of mining right will no longer exist upon expiration of the mining right. In this case, the validity period specified in the mining right license of the mining right has expired, and the original mining right holder is applying for extension, which has not yet been approved by the competent authorities. Mining right is usufructuary right, which only lasts for a certain period of time. Even if the mining right has been applied for extension, Jinchang Precision Casting shall not engage in any mining activities until the registration of extension has been completed. Therefore, during such period, Jinchang Precision Casting did not enjoy the right to use and benefit from the mineral resources of Ren Mine in Fengting Township, Luodian County. Mining right, as usufructuary right, no longer exists when it cannot use and benefit from mineral resources. Pursuant to Article 58 of the *Guarantee Law*, which stipulates that "the mortgage will extinguish due to the loss of the mortgaged property", the mortgage created by the mining right involved in the case also extinguishes.

Second, it is specified in the *Notice of the Ministry of Land and Resources on Issues concerning Further Improving the Administration of Mining Right Registration* that "upon approval of the application for the extension of mining right, its validity shall commence on the expiry date of the original validity of the extended mining license." That is, upon the expiration of the mining right license, if the competent land and resources authorities finally approve the application for the extension of mining right, the mining right can continue to be enjoyed. During the period when the application for extended registration is examined, the original mining right holder still enjoys property rights and interests over mineral resources, the nature of which can be further discussed, but obviously it has certain property value. The Supreme People's Court in one case (No. 781 [2016], Final, Civ. Division) among cases of consenting to the transfer of such rights and interests in practice approved the transfer of mining right that fails to go through formalities for extension, on which mortgage can be created. However, in this case, the Mining Right Maximum Mortgage Contract creating the

mortgage over the mining right involved in the case stipulates that the period of validity of the mining right license is from March 2005 to March 2015, from which we can infer that both parties agree to create mortgage over the mining right within this period, and the mining right or property rights and interests upon the expiration of such period are not the mortgaged property agreed by both parties. Therefore, upon expiration of the term, if the mining right or property rights and interests are to be mortgaged, the parties concerned should make special agreements.

2. **Order of realizing personal security and security on property**

Article 176 of the *Property Law* stipulates that "where a secured creditor's right involves both security on property and personal security, if the debtor fails to pay its debts due or any circumstance for realizing the security interest as agreed by the parties occurs, the creditor shall realize the creditor's right as agreed; or the creditor shall first realize the creditor's right by the security on property, if there is no agreement or the agreement is ambiguous, and the security on property is provided by the debtor; or the creditor can either realize the creditor's right by the security on property or request the guarantor to assume the guarantor liability, if the security on property is provided by a third party. The third party providing the guarantee, after assuming the mortgagor liability, has the right to recover from the debtor." The above provision indicates that when security interest and third party guarantee co-exist in a creditor's right, the creditor and each guarantor are allowed to freely agree on the order of realizing the guarantee to fully reflect respect for the parties' autonomy. Agreement in the contract that both personal security and security on property are the first in order for the realization of the creditor's right cannot be regarded as ambiguous, rather it should be deemed that both the guarantor and the debtor or the third party providing security interest agree that the creditor can at its own discretion first require any of them to assume the mortgagor liability.

It should be noted that if the agreement made was intended by the parties to exclude the ambiguity, the security on property provided by the debtor must first be used to realize restraint on creditor's right. Therefore, the parties' agreement that the creditor can realize the creditor's right through either security on property first or guarantor liability by guarantor first does not violate the provisions of laws and regulations, but represents parties' autonomy. We should recognize the creditor's right of choice, and not deem it as ambiguous.

3. **On the deadline for payment of interest**

This issue actually hinges on the understanding of the relationship between general interest on debt and interest on delayed performance. Article 253 of the *Civil Procedure Law* specifies that if the execution debtor defers in performance, he shall pay twice the amount of interest on the debt for the period of delayed performance. This is a mandatory statutory provision, by which the court shall calculate the double interest ex officio regardless of execution applicant's application. The interest on the debt for the period of delayed performance is an overall concept, including the general interest on the debt for the period of delayed performance and doubt interest

on debt. General interest on debt refers to interest determined in the effective legal instrument pursuant to substantive law, while double interest on debt, also known as interest for delayed performance, refers to the interest that should be paid in addition pursuant to Article 253 of the *Civil Procedure Law* due to the delayed performance by the execution debtor in the enforcement procedure. Before the issuance of the *Judicial Interpretation on Calculation of Interest on Debt for the Period of Deferred Performance in the Enforcement Procedure*, there was a great controversy about the relationship between general interest on debt and interest for delayed performance. There are four main opinions: directly doubled general interest on debt, single calculation, selective calculation and parallel calculation. Among them, single calculation refers to the calculation of general interest on debt only by the day before the expiration of the performance period as determined by the effective legal instrument, and the calculation of interest on debt during the delayed performance period from the date of expiration at double interest rate. One of the main reasons is that Article 253 of the *Civil Procedure Law* is clear about the legal liability for delayed performance, which will be in conflict with calculation of general interest on debt by the paying-off day as indicated in the effective legal instrument. Extending the calculation of general interest on debt to the actual paying-off day is essentially excluding Article 253 of the *Civil Procedure Law* or will result in repeated calculation of interest for the debtor of delayed performance. However, the *Judicial Interpretation on Calculation of Interest on Debt for the Period of Delayed Performance in the Enforcement Procedure* adopts the method of parallel calculation by specifying in Article 1 that "the interest on debt for the period of delayed performance, when doubled pursuant to Article 253 of the *Civil Procedure Law*, includes the general interest on debt for the period of delayed performance and the double interest on debt. The general interest on debts during the period of delayed performance should be calculated by the method as determined by effective legal instrument; for interest that is not determined by the effective legal instrument, it will not be calculated. The formula of calculating the double interest on debt is as follows: the double interest on debt = the outstanding pecuniary debts determined by the effective legal instrument other than the general interest on debt × 0.175‰/day × the period of delayed performance." Explicit provision in the above Judicial Interpretation of the method and standard by which the interest on debt should be doubled for the period of delayed performance pursuant to Article 253 of the *Civil Procedure Law* if the execution debtor fails to fulfill its obligation of payment during the period as indicated in the legal instrument does not conflict or overlap with the calculation of the general interest on debt as determined in the effective legal document, and both should be applied in parallel.

Since the implementation of the *Judicial Interpretation on Calculation of Interest on Debt for the Period of Deferred Performance* as of August 1, 2014, there should no longer be any dispute over the above-mentioned issue. However, confusion in practice is caused by some courts' following the previous customary practice in the trial. For example, in this case, judgment of the court of first instance in its reasoning part specifically supports the claim of SPD Bank Guiyang Branch for payment of the principal and interest involved in the case, with the interest calculated to the day when the principal and interest are paid off, but the conclusion part wrongfully states the

deadline for the payment of interest by Jinchang Precision Casting to be the expiration date as determined by the judgment for performance. Since the implementation of the *Judicial Interpretation on Debt Interest during Delayed Performance*, the expression that "the interest shall be paid until the expiration date as determined by the judgment for performance" is already in contradiction with the explicit language of the Judicial Interpretation, which may lead to the obvious wrongful consequence that the debtor who has actually made payment prior to expiration of the performance period still has to pay the interest, or the debtor who fails to perform the effective judgment upon the expiration date for performance does not need to continue to pay general interest on debt. We should attach great importance to and timely correct such mistake of inconsistency between the expression and the original intent of the judgment, which is to require the general interest on debt to be paid until the actual date of paying off.

Yi X v. Industrial and Commercial Bank of China Limited Panjin Branch (Dispute over Bank Card)—Banks Should Exercise Their Duty of Utmost Care and Risk Warning When Receiving Deposits from Depositors

Dian Luo and Chengpeng Xing

Rule

Banks have strict security obligation for depositors' deposits. When conducting business, depositors shall exercise reasonable and diligent care corresponding to their expected income business. However, as professional institutions conducting financial business, banks are in an obviously dominant and advantageous position when conducting savings and other business for natural persons, who on the other hand are in a relatively controlled and disadvantageous position. Bank staff, therefore, should strictly abide by the workflow and business operation norms, strengthen internal management, and exercise their duty of utmost care and risk warning when conducting business for customers.

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellant in the second instance): Yi X

Collegial panel judges of the Supreme People's Court for re-trial: Luo Dian, Wu Jianhua, Pan Jie (Written by: Luo Dian and Xing Chengpeng, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_14

Respondent in the retrial (Defendant in the first instance, Appellant in the second instance): Industrial and Commercial Bank of China Limited Panjin Branch (hereinafter referred to as "ICBC Panjin Branch")

2. **Procedural History**

First Instance: No. 00035 [2016], Trial, Civ. Division, Panjin Intermediate People's Court of Liaojiang Province (dated Jan. 29 of 2016)
Second Instance: No. 502 [2016], Final, Civ. Division, the Higher People's Court of Liaoning Province (dated Jul. 25 of 2016)
Retrial: No. 174 [2017], Retrial, Civ. Division, the Supreme People's Court (dated Jun. 12 of 2017)

3. **Cause of Action**

Dispute over bank card

Essential Facts

In April 2011, Yi X was introduced to ICBC Panjin Branch staff Li X. Li X, in collusion with the defendants Zhou X and others in the criminal case, used high interest as bait for obtaining Yi X's trust by fabricating the false facts that ICBC pays high interest to absorb depositors' deposits and ICBC has investment projects that need to absorb funds, and instructed Yi X to open accounts at Liaohe Road Savings Office of Panshan Sub-branch of ICBC Panjin Branch. Yi X opened his first account at Liaohe Road Savings Office at 15:44 on April 26, 2011, the online banking business of which was opened at 15:50 on the same day (the depositor' signature was not that of Yi X himself, and ICBC Panjin Branch said that he did not obtain U Shield formalities). Yi X opened another account at Liaohe Road Savings Office at 10:55 on June 28, 2011, the online banking business of which was opened at 11:07 on the same day, but Yi X only signed ICBC Application for Individual Customer's Business that opened the online banking business, without signing for obtaining U Shield. Yi X opened two accounts in the same savings office, depositing RMB 14.5 million in total. The accounts opened by Yi X on April 26, 2011 and June 28, 2011 were current savings accounts. Li X withdraws a total of RMB 14,498,470 from Yi X's account by means of online bank transfer or payment, and paid RMB 3.1 million to Yi X as "interest". Li X was a staff of ICBC Panjin Branch when Yi X opened the accounts in ICBC Panjin Branch, whose labor relationship was later terminated by ICBC Panjin Branch. Yi X claimed after identification that the signatures on formalities for online banking business as provided by ICBC Panjin Branch were not signatures by himself, and therefore requested handwriting verification. The expert opinion confirms that the handwriting signature of "Yi X" at the place of "Signature of Applicant" on ICBC Application for Individual Customer's Business (Opening Online Banking)

on April 26, 2011, the handwriting signature of "Yi X" at the place of "Signature" on ICBC Application for Modification (Cancellation) of Items in Electronic Banking by Individual Customer on June 28, 2011, and the handwriting signature of "Yi X" at the place of "Receiver 1's Signature" on ICBC Handover Confirmation (U Shield Handover) on June 28, 2011, are not Yi X's handwriting signatures. The handwriting signature of "Yi X" at the place of "Signature of Applicant" on ICBC Application for Individual Customer's Business (Opening Online Banking) on April 26, 2011 is Yi X's handwriting signature.

On December 19, 2014, the People's Court of Panshan County, Liaoning Province convicted Li X of fraud, who was sentenced to confiscation of all his personal property, in addition to sentence of imprisonment for a term of 14 years. Unsatisfied with the judgment, Li X lodged an appeal to Panjin Intermediate People's Court of Liaojiang Province, which sustained the judgment of the first instance. The criminal judgments of the two instances found that: "in April 2011, the Defendant Li X won the victim Yi X's trust by cheating and instructed Yi X to open accounts in Liaohe Road Savings Office and deposited a total of RMB 14.5 million between April 26 and November 11, 2011. Li X withdrew RMB 14,498,470 from Yi X's account by means of online bank transfer or payment."

Yi X filed a lawsuit with the Intermediate People's Court of Panjin, Liaoning Province, requesting the court to order ICBC Panjin Branch to pay the principal of the deposit in the amount of RMB 14.5 million and interest to Yi X.

On January 29, 2016, the court of first instance rendered a judgment, ordering ICBC Panjin Branch to pay Yi X 60% of RMB 11,398,470 (RMB 14,498,470—RMB 3.1 million), i.e. RMB 6,839,080 and interest, and dismissing other claims of Yi X.

Unsatisfied with the judgment of first instance, ICBC Panjin Branch and Yi X lodged an appeal to the court of second instance, which on July 25, 2016 rendered a judgment, ordering ICBC Panjin Branch to pay Yi X the principal of the deposit in the amount of RMB 9,238,686 and interest, and dismissing other claims of Yi X. Yi X applied to the Supreme People's Court for retrial.

Issues

1. Is there a savings deposit contract between ICBC Panjin Branch and Yi X?
2. How to divide the liability for transferring the deposits involved in the case?
3. Whether the high interest rate of RMB 3.1 million obtained by Yi X should be deducted and how to calculate the deposit interest involved in the case?

Holding

After the retrial, the Supreme People's Court holds that:

1. **There is a savings deposit contract between ICBC Panjin Branch and Yi X.**

In this case, we can find pursuant to the criminal judgment involved in the case that the fact that Yi X deposited the money involved in the case into the bank due to Li X's deception that the deposits would yield high interest returns does not affect the legal validity of the deposit contract between Yi X and ICBC Panjin Branch.

2. **The bank shall assume the largest share of liability for the deposit's being transferred.**

First, there were illegal operations on the part of ICBC Panjin Branch when handling online banking business for Yi X. When handling online banking business for Yi X, ICBC Panjin Branch did not seriously examine his identity and the content of the application form. When opening online banking for him, the U Shield was not handed to Yi X himself. Therefore, there are serious violations on the part of ICBC Panjin Branch in both opening and cancellation of online banking business for Yi X on April 26, 2011 and June 28, 2011. Second, there is certain negligence on the part of Yi X for failure to fully exercise his duty of care in opening online banking. When opening a bank account on June 28, 2011, he also confirmed the opening of online banking services by signing the application for opening online banking. The application uses enlarged font to draw attention of Yi X to get U Shield, but, instead of noticing the contents of the application and voluntarily asking the staff of ICBC Panjin Branch for U Shield, Yi X transferred a huge amount of money to the account after opening an account and online banking, which caused loss of deposits involved in the case by allowing the criminals to use the U Shield to transfer his deposits in the card. In handling the account opening and depositing business, Yi X failed to exercise reasonable and diligent care corresponding to his expected income business. Therefore, Yi X is somewhat negligent for the deposit's being transferred after opening an account on June 28, 2011. Finally, ICBC Panjin Branch failed to fulfill its legal obligation of security guarantee for Yi X's deposits. In this case, the bank's numerous serious irregularities directly led to the loss of the deposits involved in the case, so ICBC Panjin Branch should assume primary and the largest share of liability for the loss of deposits involved in the case. In summary, the Supreme People's Court held that in this case Yi X shall be 1% liable for the large share of deposits being transferred by the criminals through online banking because he did not exercise reasonable and diligent care corresponding to his expected income business, while ICBC Panjin Branch shall be 99% liable because, under the obligation of strict security guarantee, it failed to fulfill the obligation of strict internal management, which resulted in loopholes in internal management, and the staff engaged in serious violations and failed to exercise their duty of utmost care and risk warning, and corrected the inappropriate apportion of liability for the loss of deposits as determined by the court of second instance.

3. **The high interest rate of RMB 3.1 million obtained by Yi X should be deducted when ICBC Panjin Branch returns the principal of deposit.**

In this case, Yi X's obtaining of RMB 3.1 million from Li X has no legal basis and should be deducted because there is no loan relationship between Yi X and Li X. As for Yi X's claim that deposit interest should be paid at the bank loan interest rate of the same period, the Supreme People's Court did not support Yi X's claim for lack of factual and legal basis because Yi X conducted the current deposit business. To sum up, Yi X's claims for retrial are partly established. Pursuant to paragraph 1 of Article 207 and Article 170(2) of the *Civil Procedure Law*, the Supreme People's Court rules "To reverse the judgments of first and second instances, order ICBC Panjin Branch to pay RMB 11,344,75 and interest to Yi X, and dismiss other claims of Yi X."

Comment on Rule

1. **On whether there is a savings deposit contract between ICBC Panjin Branch and Yi X**

Article 55 of the *General Principles of Civil Law* stipulates that "a civil juristic act shall meet the following requirements: (1) the actor has relevant capacity for civil conduct; (2) the intention expressed is genuine; and (3) the act does not violate the law or the public interest." In this case, we can find pursuant to the criminal judgment involved in the case that Yi X's manifestation of true intention is to deposit money into the bank to obtain high interest, and the deposit contract relationship between Yi X and the bank was established from the time when the bank accepted Yi X's deposit and delivered the deposit certificate. The fact that Yi X deposited the money involved in the case into the bank due to Li X's deception that the deposits would yield high interest returns does not affect the legal validity of the deposit contract between Yi X and ICBC Panjin Branch. The deposit contract relationship between ICBC Panjin Branch and Yi X is held to be established based on the fact that Yi X applied for opening a current deposit account with ICBC Panjin Branch, ICBC Panjin Branch opened an account and issued a bank debit card, and Yi X deposited money to the bank card.

2. **On the division of liability for transferring the deposits involved in the case**

In this case, Yi's deposit involved in the case was illegally withdrawn by Li X through online bank transfer or payment, so the key to the deposit being withdrawn by false pretense is the opening of online banking, control of U Shield and the obtaining of password of online banking. The premise for dividing liability for the loss involved in the case is to clarify whether ICBC Panjin Branch has committed irregularities in handling online banking business for Yi X and whether Yi X has fulfilled his duty of care in opening online banking.

(1) On whether there were irregularities on the part of ICBC Panjin Branch when handling online banking business for Yi X

According to Article 1 of Section 2 of Chapter 7 of the *Measures of Industrial and Commercial Bank of China for the Administration of Online Banking Business*, when conducting online banking business, the teller must carefully examine the identity of the customer to be the person applying for online banking and the content of the application form, deliver the U Shield or electronic bank password card to the customer himself, and ask the client himself to sign relevant documents for online banking business. The Appraisal Opinion confirms that ICBC Panjin Branch neither seriously examined his identity and the content of the application form when conducting online banking business for Yi X, nor delivered the U Shield to Yi X himself when opening online banking for him. Therefore, there are serious irregularities on the part of ICBC Panjin Branch in both opening and cancellation of online banking business for Yi X on April 26, 2011 and June 28, 2011.

(2) On whether Yi X has exercised his duty of care in opening online banking

In this case, because on April 26, 2011 Yi X did not open online banking after opening the account, there is no such issue as he handed over the U Shield to others and leaked the password of online banking. Although he has obtained the corresponding high interest rate, there is no direct causal relationship between his depositing tempted by high interest rate and the loss of money. Therefore, it is difficult to find X's fault for the loss of funds in the bank card opened on April 26, 2011. However, when opening the bank account on June 28, 2011, he also confirmed the opening of online banking services by signing the application for opening online banking. The application uses enlarged font to draw attention of Yi X to get U Shield, but, instead of noticing the contents of the application and voluntarily asking the staff of ICBC Panjin Branch for U Shield, Yi X transferred a huge amount of money to the account after opening an account and online banking, which caused loss of deposits involved in the case by allowing the criminals to use the U Shield to transfer his deposits in the card. In handling the account opening and depositing business, Yi X failed to exercise reasonable and diligent care corresponding to his expected income business. Therefore, Yi X is somewhat negligent for the deposit's being transferred after opening an account on June 28, 2011.

(3) On the assumption of liability for transferring the deposits involved in the case

First, Article 6 of the *Law on Commercial Banks* stipulates that "commercial banks shall protect the lawful rights and interests of the depositors against encroachment by any entity or individual." The bank has the legal obligation of security guarantee of depositors' deposits. With the rapid development of society, the more sophisticated the division of social labor becomes, the more dependent on specialization the public becomes. As corporate entities and specialized financial institutions that absorb public deposits, grant loans, handle settlement and other businesses, modern commercial banks enjoy a high degree of trust and integrity among the public. When conducting deposit business in banks, depositors' corresponding duty of care will be

reduced based on their great trust in banks. Faced with tedious processes, numerous specialized terminology and complex scientific and technological services, ordinary customers more often than not can only passively obey the arrangement of bank staff and conduct business according to the procedures as directed by the bank staff. Therefore, banks should fulfill more duty of care and strict security guarantee obligation for depositors' deposits by formulating sound business norms and strengthening internal management. When handling business for depositors, bank staff on behalf of banks should more strictly abide by the workflow and business operation norms. In this case, ICBC Panjin Branch should assume primary and the largest share of liability for the loss of deposits involved in the case because the bank's serious irregularities directly led to the loss of the deposits involved in the case, i.e., opening online banking business for Yi X on April 26, 2011 without his application, and handling U Shield business and handing it to others without Yi X's consent by the staff of ICBC Panjin Branch on June 28, 2011. Second, during Li X's employment with ICBC Panjin Branch, Li X, by taking use of his working status, fabricated high interest to induce Yi X to deposit the money involved in the case into ICBC Panjin Branch, and took U Shield from his colleague Zhao X through convenience of his work, resulting in the loss of the money involved in the case. The above facts can establish that there are loopholes in the internal management and serious irregularities by the staff of ICBC Panjin Branch, so ICBC Panjin Branch should be liable for the loss caused due to its poor management. Under the circumstances of frequent occurrence of financial fraud cases participated by bank staff, banks should put more emphasis on preventing such cases from happening by strengthening internal management so as to provide customers with higher quality and safer services. Third, despite of being a natural person with full civil capacity, Yi X, by believing in the lies about high interest returns told by the criminal Li X, a staff member of Panjin Branch of ICBC, went to the counter of ICBC Panjin Branch to open account, card and online banking business, and deposited a total of RMB 14.5 million into the account. As a natural person with full civil capacity, instead of exercising his utmost care for deposit with high returns and involving huge amount, Yi X decreased his awareness of risk prevention and relaxed his duty of care to the security of funds in his account. As a result, when opening an account and conducting online banking business on June 28, 2011, he failed to read carefully the tips on the application form for opening online banking, ask the bank for U Shield and exercise reasonable and diligent care corresponding to his expected income business. Therefore, he should assume the secondary and minor liability for a total of RMB 8.5 million deposited in 9 times which is being transferred from June 28, 2011 (account opening date) to November 11, 2011.

In summary, the Supreme People's Court holds that, banks as professional institutions conducting financial business are in an obviously dominant and advantageous position when conducting savings and other business for natural persons, who on the other hand are in a relatively controlled and disadvantageous position. Bank staff, therefore, should strictly abide by the workflow and business operation norms, and exercise their duty of utmost care and risk warning when conducting business for customers. In this case, Yi X shall be 1% liable for the large share of deposits

being transferred by the criminals through online banking because he did not exercise reasonable and diligent care corresponding to his expected income business, while ICBC Panjin Branch shall be 99% liable because, under the obligation of strict security guarantee, it failed to fulfill the obligation of strict internal management, which resulted in loopholes in internal management, and the staff engaged in serious violations and failed to exercise their duty of utmost care and risk warning.

3. **On whether the high interest rate of RMB 3.1 million obtained by Yi X should be deducted and the method of calculating the deposit interest involved in the case**

In this case, because there is no loan relationship between Yi X and Li X, Yi X's obtaining of RMB 3.1 million from Li X has no legal basis. It is merely high interest paid by Li X to Yi X to win Yi X's trust through fraud and further obtain online banking U Shield, so it shall be deducted when ICBC Panjin Branch returns the principal of deposit. As for Yi X's claim that deposit interest should be paid at the bank loan interest rate of the same period, the Supreme People's Court did not support Yi X's claim for lack of factual and legal basis because Yi X conducted the current deposit business.

Liaoning Shunda Traffic Engineering Maintenance Co., Ltd. v. Panjin Kaiyue Economic and Trade Co., Ltd. (Dispute over Contract for Work)—Applicable Rules for Transforming Claim in Real Right into Claim for Real Right Damages

Jianhua Wu and Hening Ma

Rule

In a contract for work, the proprietor provides the raw materials to be processed to the contractor, with the ownership of the raw materials being owned by the proprietor. After the performance of the contract, the proprietor's request for the contractor to return the remaining raw materials is the claim in real right of raw materials. When the raw materials cannot be returned due to loss, in order to fully protect the interests of the real right holder, the protection method for creditor's rights can be adopted by changing the proprietor's claim in real right to claim for real right damages. Then by the proprietor should claim for damages against the contractor within 2 years after the proprietor knew or should have known the loss of the raw materials.

Case Information

1. Parties

Applicant in the re-trial (Plaintiff in the first instance, Appellant in the second instance): Liaoning Shunda Traffic Engineering Maintenance Co., Ltd. (hereinafter referred to as "Shunda Co.")

Collegial panel judges of the Supreme People's Court for re-trial: Wu Jianhua, Dong Hua, Pan Jie (Written by: Wu Jianhua and Ma Hening, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_15

Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): Panjin Kaiyue Economic and Trade Co., Ltd. (hereinafter referred to as "Kaiyue Co.")

2. **Procedural History**

First Instance: No. 1 [2016], Trial, Civ. Division, the Intermediate People's Court of Panjin (dated May 10 of 2016)
Second Instance: No. 896 [2016], Final, Civ. Division, the Higher People's Court of Liaoning Province (dated Nov. 24 of 2016)
Retrial: No. 332 [2017], Retrial, Civ. Division, the Supreme People's Court (dated Nov. 29 of 2017)

3. **Cause of Action**

Dispute over contract for work

Essential Facts

In May 2011, Shunda Co. and Kaiyue Co. signed the Modified Asphalt Processing Contract, which stipulates that Shunda Co. will provisionally provide 2000 tons of base asphalt to Kaiyue Co. for its processing into modified asphalt at a unit price of RMB 1,250. Place of Delivery: Liaohe Petrochemical Co.; Means of Transportation: motor carrier (self-pickup). From June 19 to July 17 of the same year, Kaiyue Co. received 1930.2 tons of base asphalt from Shunda Co., and processed 1489.84 tons of modified asphalt for Shunda Co. On December 6, 2011, Kaiyue Co. confirmed that it still had 440.36 tons of base asphalt belonging to Shunda Co. In 2011, the unit price of base asphalt was RMB 4,756.

Shunda Co. filed a lawsuit with Panjin Intermediate People's Court of Liaoning Province, requesting Kaiyue Co. to return the 440.36 tons of base asphalt and price difference of RMB 773,272.16 or pay RMB 2,094,352.16 for asphalt and the interest calculated at the same period loan interest rate of the People's Bank of China from the date of default to the date of the determination of payment in this judgment.

Panjin Intermediate People's Court held that: an obligation is created when the Modified Asphalt Processing Contract signed by Shunda Co. and Kaiyue Co., by which after Shunda Co. handed over the base asphalt to Kaiyue Co., Kaiyue Co. should process the base asphalt into modified asphalt and then handed it back to Shunda Co., and in which the two parties agreed on the time of delivery, means of acceptance and calculation. Shunda Co.'s request cannot be supported for exceeding the limitations prescribed by law that the limitation for a party to claim creditor's rights is 2 years because the period between Kaiyue Co.'s issuance on December 6, 2011 of a confirmation letter to Shunda Co. that Kaiyue Co. still owed Shunda Co. 440.36 tons of base asphalt and Shunda Co.'s sending of a lawyer's demand letter on November 20, 2014 to Kaiyue Co. has exceeded the limitation of action prescribed by law and Shunda Co. failed to provide relevant evidence for its claim of rights during

the period. Panjin Intermediate People's Court rendered a civil judgment (No. 1 [2016], Trial, Civ. Division) on May 10, 2016, dismissing the claims of Shunda Co.

Unsatisfied with the judgement of the court of first instance, Shunda Co. lodged an appeal.

The Higher People's Court of Liaoning Province held that: after Shunda Co. and Kaiyue Co. signed the Modified Asphalt Processing Contract, the Contract shall govern the relevant rights and obligations. Because Kaiyue Co. fails to fulfill relevant obligations as stipulated in the Contract, Shunda Co. has the right to claim rights to Kaiyue Co. pursuant to the Contract. According to the law, the limitation of action for a party to claim creditor's rights is 2 years. The court of second instance cannot support Shunda Co.'s claim for there is no evidence to prove that Shunda Co. has exercised its rights within 2 years of the limitation of action. The judgment of first instance was clear in fact-finding and correct in application of law. It is ruled to dismiss the appeal and sustain the original judgment.

Unsatisfied with the judgment of the second instance, Shunda Co. applies to the Supreme People's Court for retrial.

Issues

Whether Kaiyue Co. should return 440.36 tons of base asphalt to Shunda Co. or compensate for its loss mainly depends on determining when Shunda Co.'s claim in real right is transformed to claim for real right damages, and whether Shunda Co.'s claim has exceeded the limitation of action.

Holding

In its retrial, the Supreme People's Court finds that both parties agree that the price of base asphalt in 2017 is RMB 2,700.

The Supreme People's Court holds upon trial that: the Modified Asphalt Processing Contract signed by Shunda Co. and Kaiyue Co. is a contract for work, whereby Shunda Co. as the proprietor provides asphalt raw materials and pays processing costs to Kaiyue Co. as the contractor, and Kaiyue Co. delivers its work products pursuant to the Contract. It is a claim in rem for Shunda Co. as the owner of the raw materials of base asphalt involved in the case to request Kaiyue Co. to return the 440.36 tons of base asphalt. Upon investigation, it is found that base asphalt can be stored for 2 to 3 years in the warehouse to avoid sunshine and rain. From December 6, 2011 to November 20, 2014, Shunda Co. had not claimed the return of 440.36 tons of base asphalt against Kaiyue Co., nor had Kaiyue Co. informed Shunda Co. that the base asphalt had been lost. The 2-year limitation is not exceeded from Shunda's knowledge that the remaining base asphalt is lost upon its lawyer's demand letter on November 20, 2014 to the lawsuit filed against Kaiyue Co. for compensation.

Both parties agree that the price of base asphalt is RMB 2,700. In the case of loss of base asphalt, there is factual and legal basis for Shunda Co. to request Kaiyue Co. to compensate for its loss. Pursuant to Articles 251 and 265 of the *Contract Law*, Articles 241 and 244 of the *Property Law*, Article 207(1) and Article 170(1)(2) of the *Civil Procedure Law*, it is ruled as follows: "(1) To reverse the Civil Judgment (No. 896 [2016], Final, Civ. Division) of the Higher People's Court of Liaoning Province and the Civil Judgment (No. 1 [2016], Trial, Civ. Division) of Panjin Intermediate People's Court of Liaoning Province; (2) To order Panjin Kaiyue Economic and Trade Co., Ltd. to pay Liaoning Shunda Traffic Engineering Maintenance Co., Ltd. RMB 1,188,972 for the asphalt within 10 days from the date when this Judgment takes effect; and (3) To dismiss other claims of Liaoning Shunda Traffic Engineering Maintenance Co., Ltd."

Comment on Rule

In judicial theory, there is a clear distinction between the claim in real right and the claim for real right damages, either of which the parties can claim. But in judicial practice, the legal relationship between the two parties will change with the occurrence of certain legal events, that is, there is a dynamic and changing process in the legal relationship. Faced with such a complex situation, courts may have difference understanding of the legal relationship in dynamic change. Therefore, it is necessary to determine the applicable rules for the conversion of claim in real right to claim for real right damages, so that the courts at all levels can accurately grasp the direction for handling the case.

1. Determination of claim in real right

To accurately grasp the standard for adjudication, we should first precisely position the underlying legal relationship between the two parties, i.e., to determine whether the underlying legal relationship between the two parties is claim in real right or claim in creditor's rights. Article 251 of the *Contract Law* stipulates that "a contract for work is a contract whereby the contractor shall, in light of the requirements of the proprietor, complete the work and deliver its work products, and the proprietor pays the remuneration therefor. Work includes processing, ordering, repairing, duplicating, testing, inspecting, etc." Article 251 of the *Contract Law* stipulates that "where the proprietor fails to pay the remuneration or cost for the materials, etc. to the contractor, the contractor is entitled to have a lien on the work products, except as otherwise agreed upon by the parties". Although the law does not directly provide for the ownership of the raw materials provided by the proprietor, Article 264 of the *Contract Law* clearly gives the contractor a lien, thus it can be reversely deduced that generally the work products, which certainly include raw materials, are owned by the proprietor. Therefore, when the proprietor requests the return of the raw materials provided by it, the underlying legal relationship is the claim in real right, not the claim in creditor's right. Therefore, the owner of the raw materials, i.e., the real right

holder may request the contractor to return the original object pursuant to Article 34 of the *Property Law*, which stipulated that "as for the untitled possession of a real property or movable property, the right holder may request for the returning of the original object."

2. **Transforming claim in real right into claim for real right damages**

Based on the special property that base asphalt can only be preserved for 2–3 years, the original base asphalt was lost when the owner brought the lawsuit. When the real right is seriously damaged and the original object cannot be returned, in order to fully protect the interests of the real right holder, we can adopt the method of protecting the creditor's rights, i.e., compensating the real right holder for the loss so than he can get compensation in value. Article 265 of the *Contract Law stipulates* that "the contractor shall keep the materials supplied by the proprietor and the completed work products with due care, and shall be liable for damages in case of any damage or losses due to improper care". Article 244 of the *Property Law* stipulates that "in case a real property or movable property under possession is damaged or lost, and the holder of this real property or movable property requests for compensations, the possessor shall return the insurance money, damages or indemnities obtained from the said destruction or loss to the holder; and in case the impairment to the holder has not been sufficiently made up, a malicious possessor shall be liable for compensations". Although it is lawful for the contractor to possess the base asphalt, it has not acquired the ownership of the base asphalt. When the things in possession is damaged or lost, the possessor shall still be liable for compensation to proprietor as the real owner of the things. Now, the owner's claim in real right is converted to the claim for real right compensation. Relevant attributes of rights are converted from rights in rem to creditor's rights. The remedy of claim for real right damages is in principle based on filling the loss to the property. Basic asphalt is homogeneous goods, which can be purchased in the market. Therefore, the amount of compensation can be calculated according to the price of the thing approved by both parties when the contractor cannot return the original object.

3. **Use of the rules of limitations during the conversion of claim in real right to claim for real right damages**

The application of the rules of limitations will change when the claim in real right is converted to the claim for real right damages. Limitations of action means the legal system in which the obligee loses the right to request the people's court to lawfully protect his rights due to his failure to exercise his rights within the period prescribed by law. The limitation of action has the following three characteristics: (1) The right to win a lawsuit losses when the limitation of action expires. The people's court will dismiss the plaintiff's claim, which has passed the limitation of action; (2) Substantive rights are not lost when the limitation of action expires. After the limitation of action expires, the plaintiff still enjoys substantive rights, and has the right to accept if the defendant performs its obligations on a voluntary basis; and (3) The limitation of action is mandatory. It is invalid for the parties to agree on the

period, method of calculation, suspension and interruption of limitation of action. The core value of the limitation of action system is to maintain the established social stability. When the obligee does not claim his rights for a long time and the obligor does not actively fulfill his obligations, the legal relationship between the two parties is in a indeterminable state, and the longer the duration, the heavier the burden the obligor has to bear, and the more unfavorable it is to maintain the stability of social transaction order. The purpose of the limitation of action system is to urge the obligee to promptly exercise his rights so as to maintain the order and security of transactions. The limitation period is generally divided into 3 categories: ordinary limitation period, special limitation period and longest limitation period. Among them, the ordinary limitation period means the period of limitation applicable to various kinds of civil legal relationships, except as otherwise provided by law. Article 135 of the *General Principles of the Civil Law* formulated in 1986 stipulates that "the limitation of filing a lawsuit to the people's court for protection of civil rights are 2 years, unless otherwise provided by law". Thus, the ordinary limitation period is determined to be 2 years. With the continuous innovation of social transaction mode and transaction type, the relationship between rights and obligations becomes more diversified and complicated. The 2-year limitation period can no longer fit the reality. Therefore, Article 188 of the *General Provisions of Civil Law*, which takes effect as of October 1, 2017, extends the ordinary limitation period to 3 years.

The rules of limitation do not apply to claims in real right. The subject matter of limitations is claims in the sense of substantive law, not in the sense of procedural law. The claim in substantive law is reflected in litigation as claim, but it cannot be considered that any claim asserted during litigation is subject to the limitation, such as the claim in real right. The claim in real right means the right to request the restoration to its perfect state or prevention of impairment when the right in things is infringed or threatened to be infringed. Article 196 of the *General Provisions of the Civil Law* stipulates that "the provisions for limitations do not apply to the following claims: (1) request to stop the infringement, remove the obstacles, or eliminate the danger; (2) the right holder requests returning of property for real estate and registered chattels; (3) request payment of alimony, support money or maintenance; or (4) other claims for which limitations are not applicable". Among them, requesting to stop the infringement, remove the obstacles, or eliminate the danger is for claim in real right. The claim in real right is the concrete embodiment of the validity of real right and is included in the functions of real right. As long as real right exists, the claim in real right should exist. Real right is a power over the things, to which limitations of action do not apply, so claim in real right such as restitution, ceasing the infringement, removing the obstacles, or eliminating the danger, as part of real right, should not be lost due to the expiration of limitation.

The rules of limitation apply to claim for real right damages. Upon the occurrence of the key legal event of the loss of the original object, the claim in real right is converted to the claim for real right damages. The limitation period shall begin from the time when the obligee can request the people's court to protect his claim. Pursuant to Article 188 of the *General Principles of the Civil Law*, limitations are calculated from the date on which the right holder knows or should have known the damage to

the rights and the obligor, unless otherwise provided by law. In this case, the statutory limitation period is not exceeded from the time when the owner of base asphalt either subjectively has "known" the fact that his rights had been infringed, or has known that his rights had be infringed based on objective law of development of things through reasonable duty of care to the time when this case was filed. Therefore, the application of the rules of limitations will change when the underlying legal relationship in this case is converted from the claim in real right to the claim for real right damages. For such cases, we need to consider the overall situation of the case, emphasize on the important circumstances embodying changes in underlying legal relationship, deepen the detailed consideration of the limitation of action system, and avoid the break in the chain of logical reasoning on such issues, so as to better implement the concept of fairness and justice in each case.

Qingdao Sanley Group Co., Ltd. v. China Haisum Engineering Co., Ltd. (Dispute over Construction Contract for Construction Engineering)—Difference Between Interest of Payment for the Engineering and Liquidated Damages

Shaojun Fu and Yongming Wang

Rule

If the construction engineering contracted by the constructor has serious quality problems which the constructor fails to repair or refuses to repair, the constructor's claim for liquidated damages for the progress payment for the engineering shall not be supported. In the case that one party does not claim for the interest on arrears of payment for the engineering, the people's court cannot regard the party's claim for liquidated damages for the progress payment for the engineering as the claim for interest on arrears of payment for the engineering, for default in paying liquidated damages for the progress payment for the engineering is a liability for breach of contract, while the interest on arrears of payment for the engineering is civil fruit. They are different in legal nature and function and should be distinguished.

Collegial panel judges of the Supreme People's Court for the second instance: Song Chunyu, Fu Shaojun, Ding Guangyu (Written by: Fu Shaojun and Wang Yongming, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_16

Case Information

1. Parties

Appellant (Defendant in the first instance): Qingdao Sanley Group Co., Ltd. (hereinafter referred to as "Sanley Group")
Appellant (Plaintiff in the first instance): China Haisum Engineering Co., Ltd. (hereinafter referred to as "Haisum Engineering")

2. Procedural History

First Instance: No. 6 [2016], Trial, Civ. Division, the Higher People's Court of Shandong Province (dated Dec. 15, 2016)
Second Instance: No. 476 [2017], Final, Civ. Division, the Supreme People's Court (dated Dec. 15 of 2017)

3. Cause of Action

Dispute over construction contract for construction engineering

Essential Facts

In March 2012, Haisum Engineering contracted Sanley Group's Stadium Engineering with a tentative total price of RMB 50 million, whereby the two parties agreed to pay 80% of the output value on a monthly basis. After the commencement of the engineering, Sanley Group had paid RMB 21,707,400 by August 2012. Thereafter, due to such problems as construction period and engineering quality, Sanley Group did not pay the progress payment of RMB 7.31 million for September 2012, nor confirm the progress payment for October, leading to intensified contradictions between the two parties and withdrawal of Haisum Engineering from the site.

On January 9, 2013, Sanley Group issued a Letter of Rescission to rescind the contract and Haisum Engineering subsequently filed a lawsuit against Sanley Group with Shandong Higher People's Court. After filing the lawsuit by Haisum Engineering, Sanley Group filed a separate lawsuit against Haisum Engineering with the People's Court of Chengyang District, Qingdao for payment of engineering quality maintenance and repair fee of RMB 800,000 (adjusted to more than RMB 35 million after appraisal) and the liquidated damages of RMB 4 million, and rescission of the Contract. It was ruled by the People's Court of Chengyang District, Qingdao in the first instance to rescind the Contract between the two parties, and Haisum Engineering pay more than RMB 32.69 million for engineering repair and RMB 1.26 million for appraisal. Qingdao Intermediate People's Court in the second instance sustained the original judgment.

Shandong Higher People's Court in the first instance held that some of the claims of Haisum Engineering had factual and legal basis and should be partially supported.

It was ruled that Sanley Group pay Haisum Engineering RMB 37,171,708.11 and interest on arrears of payment for the engineering within 10 days from the effective date of the Judgment, and to dismiss other claims of Haisum Engineering.

Unsatisfied with the judgment of the first instance, Haisum appealed to the Supreme People's Court.

In the second instance, the Supreme People's Court found that on December 15, 2016 Haisum Engineering paid the engineering repair fee as determined by Qingdao Intermediate People's Court (Judgment No. 261) to the bank account of Sanley Group, of which Haisum Engineering applied for freezing in property preservation proceeding of the case. On December 26, 2016, Sanley Group paid RMB 37,171,708.11 to the bank account of Haisum Engineering as the principal of the payment for the engineering as determined in the judgment of the first instance.

Issues

1. Is it correct for the judgment of the first instance to adopt the judicial appraisal report as the basis of the construction cost involved in the case?
2. Is it correct for the judgment of the first instance to refuse to support the economic losses of Haisum Engineering?
3. Is it correct for the judgment of the first instance to allocate the appraisal fee?
4. Is it correct for the judgment of the first instance to handle the interest in arrears on payment for the engineering?

Holding

At the second instance, the Supreme People's Court also finds that, with regard to the question that is it correct for the judgment of the first instance to adopt the judicial appraisal report as the basis of the disputed construction cost, Haisum Engineering believes that the appraisal of the construction cost by Good Faith Co., does not conform to relevant norms in its procedures, including composition of appraisers, signature on the appraisal report, etc., have serious errors and omissions in its content, so a new appraisal shall be conducted pursuant to relevant regulations and standards.

1. **On the correctness for the judgment of the first instance to adopt the appraisal report as the basis of the disputed construction cost**

The Supreme People's Court holds that the cost appraisal of the construction involved was lawfully entrusted by the court of first instance, and the parties did not object to

the certification and qualification of Good Faith Co.. Moreover, Good Faith Co., has Engineering Cost Consulting Enterprise Qualification Certificate. Although Haisum Engineering objected to the appraisal qualification of Good Faith Co., and its appraisers, it did not submit sufficient evidence to prove its claim. The appraisal procedure was legal because, after the insurance of the appraisal report, Good Faith Co., appeared in court for interrogation, responding to the objections raised by the two parties, and finally issued a supplementary appraisal report. This court does not support Haisum Engineering's claim that Good Faith Co., refused to submit appraisal basis to the court and the affixation of signature and seal on the appraisal report did not meet the requirements because the appraisal report and supplementary appraisal report set out the detailed appraisal basis, and are affixed with the seal of the appraisal agency and signature of the appraisers. With regard to the issue raised by Haisum Engineering that Good Faith Co., must comply with national regulations and national standards in its construction cost appraisal, Haisum Engineering did not submit evidence to prove that Good Faith Co., must comply with such regulations and standards in its construction cost appraisal. This court also does not support Haisum Engineering's claim for re-appraisal because it does not fall under any circumstances as listed in Article 27 of the *Provisions on Evidence in Civil Procedures*.

2. **On the issue that RMB 58,879,108.11 claimed by Haisum Engineering as its appraised construction cost is lower than RMB 59,161,110.14 claimed by Sanley Co.**

The Supreme People's Court holds that Sanley Co.,'s reference to the construction cost approved by Shandong Chengpin Cost Engineers Firm is to challenge the construction cost claimed by Haisum Engineering, rather than self-recognition, and Haisum Engineering's claim that the appraisal opinion of Good Faith Co., is not objective shall not be supported for lack of factual and legal basis. It is not improper for the court of first instance to adopt the appraisal opinion as the construction cost involved in the case and based on this to determine the payment for the engineering payable by Sanley Co., so it is maintained.

3. **On the correctness for the judgment of the first instance to refuse to support the economic loss of Haisum Engineering**

The evidence submitted by Haisum Engineering to prove its economic loss mainly includes claim report, specific cost of claim, schedule and statement, etc. Because the materials submitted by Haisum Engineering are all unilaterally produced by Haisum Engineering and have not been approved by Sanley Co., and there are many disputes between the two parties on such problems as engineering delay and engineering quality, the evidence submitted by Haisum Engineering cannot prove such facts as the reason, amount and liability of the claimed economic loss. In the case that the appraisal agency is unable to appraise relevant facts, it is not improper for the court of first instance to hold that Haisum Engineering should bear the legal liability for failing to provide the evidence, and not to support its claim for economic loss.

4. **On the correctness of the disposal of the liquidated damages for the progress payment for the engineering and interest on payment for the engineering by judgment of the first instance**

The Supreme People's Court holds that, according to the facts ascertained in the first instance, the progress payment for the engineering in September 2012 payable to Haisum Engineering was RMB 7.31 million, but Sanley Co., refused to pay on the ground of misrepresentation of payment for the engineering and serious problems in engineering quality on the part of Haisum Engineering. Therefore, the key to whether Sanley Co., should pay the liquidated damages for payment for the engineering is whether it has a legitimate cause for refusing to make payment for the engineering. As provided in Article 5.2 of the *General Contract for Design and Construction* that "progress payment for the engineering shall be paid up to 80% based on monthly output value, the output value of a previous month shall be reported on the 5th of each month, and Party A shall approve and make the progress payment for the engineering before the 25th of each month", Haisum Engineering must complete the corresponding workload every month before demanding Sanley Co., to make progress payment for the engineering. The fulfillment of the contractual obligations of both parties has a clear sequence, i.e., up-to-standard works completed by Haisum Engineering before progress payment for the engineering paid by Sanley Co., Article 67 of the *Contract Law* stipulates that "where both parties have obligations toward each other and there is an order of priority in respect of the performance, if the party who is to perform first fails to perform, the party who is to perform later has the right to reject the other party's demand for performance. If the performance of the obligations by the party who is to perform first is not in conformity with the agreement, the party who is to perform later has the right to reject the other party's demand for corresponding performance." Therefore, in the case that the engineering constructed by Haisum Engineering had quality problems which were not remedied, Sanley Co., shall not be liable for breach of contract because its refusal to make progress payment for the engineering has contractual and legal basis. Haisum Engineering's claim against Sanley Co., for liquidated damages for progress payment for the engineering also cannot be established.

5. **Interest in arrears on the payment for the engineering**

Although Haisum Engineering in its first claim requested Sanley Co., to make payment for the engineering, instead of claiming interest on payment for the engineering, the judgment of the first instance which held that the liquidated damages for the progress payment claimed by Haisum Engineering should be the interest in arrears on payment for the engineering and which ordered Sanley Co., pay Haisum Engineering interest on payment for the engineering was beyond the claim asserted by Haisum Engineering and should be corrected.

The Supreme People's Court finally rules as follows: "(1) To sustain Item 1 of the Civil Judgment of the Higher People's Court of Shandong Province (No.6 [2013], Trial, Civ. Division), i.e., ordering Sanley Co., to pay Haisum Engineering the payment for the engineering of more than RMB 37.17 million; (2) To set aside Items

2 and 3 of the Higher People's Court of Shandong Province (No. 6 [2013], Trial, Civ. Division), i.e., supporting the claim of Sanley Co., for not paying the interest in arrears on payment for the engineering; and (3) To dismiss other claims of Haisum Engineering."

Comment on Rule

1. **Does Sanley Co., has a legitimate cause for refusing to pay the progress payment for the engineering?**

Article 269 of the *Contract Law* stipulates that "a construction engineering contract is a contract whereby the contractor engages in engineering construction and the contract-issuing party pays the price. Construction engineering contracts include engineering survey, design, and construction contracts." Accordingly, in the legal relationship of a construction contract for construction engineering, the main contractual obligation of the contractor is to engage in construction as agreed in the contract and provide construction works that meet the quality requirements, and the main contractual obligation of the contract-issuing party is to make corresponding payment for the engineering as agreed in the contract. Article 5.2 of the *General Contract for Design and Construction* made by the parties stipulates the order in which the parties perform the main contractual obligations, i.e., up-to-standard works completed by Haisum Engineering before progress payment for the engineering paid by Sanley Co., In the case that the contract-issuing party has continuously raised problems concerning engineering quality, Sanley Co., has legitimate cause to refuse to make progress payment for the engineering to Haisum Engineering for it is an act of exercising the defense of improper performance by the other party as provided in Article 67 of the *Contract Law*, which does not constitute a breach of contract. In the absence of a breach of contract on the part of Sanley Co., it is without doubt that no liquidated damages for the progress payment shall be paid.

2. **Is it correct for the court of first instance to hold that the liquidated damages for the payment for the engineering is actually interest in arrears on payment for the engineering?**

In the case that the court of first instance did not support the constructor's claim for liquidated damages, its determination and support that the liquidated damages for progress payment for the engineering was actually the interest in arrears on payment for the engineering actually equals to support for liquidated damages for progress payment for the engineering, which was logically inconsistent, and because the constructor in filing the lawsuit did not claim interest in arrears on payment for the engineering, judgment of the first instance that the contract-issuing party shall pay the interest is obviously beyond the party's claim pursuant to the principle of adversary system in civil litigation.

Default in liquidated damages for the progress payment for the engineering and default in interest on payment for the engineering fall under two different legal

systems. Although both of them are represented by one party's monetary payment obligation to the other party and delay in performance, resulting in certain monetary compensation by the defaulting party to the other party, obvious differences also exist between them.

First is the difference in basis for claims. The basis for liquidated damages in arrears for the progress payment for engineering is the contractual provision as agreed by the parties, in the absence of which one party cannot claim, while the interest in arrears on payment for the engineering may either be agreed by the parties, or in the absence of which, be directly claimed pursuant to Article 17 of the *Judicial Interpretation on Construction Contracts for Construction Engineering* which stipulates that "the standard of calculation and payment of interest in arrears on payment for the engineering shall be governed by the agreement of the parties or, in the absence of which, the interest rate for loans of the same type for the same period issued by the People's Bank of China."

Second is the difference in periods of occurrence. Default in liquidated damages for the progress payment for the engineering occurs during the construction of the engineering, while default in interest on payment for the engineering usually occurs after settlement by the parties upon completion of construction of the engineering. The interest shall be calculated from the date when the payment for the engineering is payable, for which Article 18 of the *Judicial Interpretation on Construction Contract for Construction Engineering* specifies that "the interest shall be paid from the date when the payment for the engineering is payable. If there is no agreement between the parties as to the time of payment or such agreement is unclear, the following time shall be regarded as the time of payment: (1) the date of delivery, if the construction engineering is actually delivered; (2) the date when the completion settlement documents are submitted, if the construction engineering is not delivered; (3) the date when one party files the lawsuit, if neither the construction engineering is delivered nor the payment for the engineering is settled."

Third is the difference in nature and function. Default in liquidated damages for the progress payment for the engineering is a liability for breach of contract, the functions of which are guarantee for performance and compensation for damages;[1] Interest in arrears on payment for the engineering is civil fruit, which is monetary compensation paid by the contract-issuing party to the other party for occupying the constructor's funds due to delayed payment.

Fourth is the difference in amount. The amount of liquidated damages in arrears for the progress payment for the engineering shall be agreed by the parties, and one party can apply to the court or arbitration institution for adjustment only if it considers the agreed amount is abnormally high or abnormally low, while the interest in arrears on payment for the engineering, despite of the agreement by the parties, usually will be subject to statutory maximum interest.

It is precisely because of the above differences that the people's court cannot treat the liquidated damages in arrears for the progress payment for the engineering as the interest in arrears on payment for the engineering. Specifically in this case, to

[1] Wang [1].

the extent that the contract-issuing party shall not pay the liquidated damages in arrears for the progress payment for the engineering, and the constructor did not claim for the interest in arrears on payment for the engineering, ruling of the court of first instance that the contractor pay the interest in arrears on payment for the engineering both obscures the difference between the liquidated damages in arrears for the progress payment for the engineering and the interest in arrears on payment for the engineering, and exceeds the party's claim.

3. **Is it correct for the court of first instance to rule on the payment of interest in arrears on payment for the engineering?**

Because the main contractual obligation of Haisum Engineering is to provide engineering that meets the quality requirements, Haisum Engineering has the obligation to repair engineering quality problems by itself or pay Sanley Co., for the repair. In either case, the condition for making payment for the engineering will be satisfied only after the repair of the engineering is completed, thus it is necessary to pay the interest in arrears on payment for the engineering. Haisum Engineering chose to pay and paid the repair fee, but applied to freeze the account by which Sanley Co., received the repair fee, which caused Sanley Co., not able to use the repair fee to repair the engineering involved in the case. Under such circumstances, the condition for Sanley Co., to make payment for the engineering is not satisfied, so the interest on payment for the engineering shall not be paid.

Reference

1. Wang Hongliang, "Reflections on Functional Positioning of Liquidated Damages", *Law Science*, 2, 2014.

Tongzhou Construction General Contracting Group Co., Ltd. v. Inner Mongolia Xinghua Real Estate Co., Ltd. (Dispute over Construction Contract for Construction Engineering)—The Nature and Performance of the Offsetting Debt with Property Agreement upon Expiration of Debt Satisfaction Period

Wei Si

Rule

In determining the nature of the offsetting debt with property agreement upon the expiration of the debt satisfaction period, if it is not clearly specified, the offsetting debt with property agreement shall generally be regarded as a consensual new debt satisfaction agreement. When performing the agreement, the creditor should first exercise the right to claim for the fulfillment of new debt, and, if non-performance of the new debt when it becomes due renders the purpose of the offsetting debt with property agreement not fulfilled, the creditor has the right to request the debtor to continue to perform the old debt.

Collegial panel judges of the Supreme People's Court for the second instance: Han Mei, Si Wei, Shen Dandan (Written by: Si Wei, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_17

Case Information

1. Parties

Appellant (Plaintiff in the first instance, Defendant in the counterclaim): Tongzhou Construction General Contracting Group Co., Ltd. (hereinafter referred to as "Tongzhou General Contracting")
Appellee (Defendant in the first instance, Plaintiff in the counterclaim): Inner Mongolia Xinghua Real Estate Co., Ltd. (hereinafter referred to as "Xinghua Real Estate")

2. Procedural History

First Trial: No. 38 [2015], Trial, Civ. Division, the Higher People's Court of Inner Mongolia Autonomous Region (dated Dec. 18 of 2015)
Second Instance: No. 484 [2016], Final, Civ. Division, the Supreme People's Court (dated Dec. 27 of 2016)

3. Cause of Action

Dispute over construction contract for construction engineering

Essential Facts

On June 28, 2005, Xinghua Real Estate and Tongzhou General Contracting signed a Construction Contract for Construction Engineering, whereby Xinghua Real Estate contracted out the construction of Hohhot Water Supply Building Project (hereinafter referred to as "Water Supply Building Project") to Tongzhou General Contracting. On July 1, 2005, Xinghua Real Estate produced the Bidding Document, inviting bidding through limited competitive bidding for the civil works of the Water Supply Building. On July 14, 2005, Xinghua Real Estate and the bidding agency issued a Bid Winning Notice to Tongzhou General Contracting, confirming that Tongzhou General Contacting was the winning bidder. On the same day, Xinghua Real Estate issued a Bid Winning Confirmation Letter and Notice of Bidding Results to Hohhot Administrative Office of Construction Engineering Bidding and Bid and other bidders. On July 28, 2005, the two parties signed the Construction Contract for Construction Engineering, which was filed with Hohhot Administrative Office of Construction Engineering Bidding and Bid for record. After the contract was signed, Tongzhou General Contracting completed construction on site, which did not go through completion acceptance check before putting into use by Xinhua Real Estate at the end of 2010.

The court of first instance commissioned the appraisal for the cost of civil engineering and installation engineering involved in the case (excluding CCTV monitoring system, vehicle management system and newly-added items of engineering).

On September 21, 2009, the two parties confirmed that the CCTV monitoring system and vehicle management system was settled at RMB 820,000 and RMB 200,000 respectively, totaling RMB 1.02 million.

From May 2011 to January 2012, the two parties settled the added items at the total engineering cost of RMB 830,722, composed of RMB 95,000 for air-conditioning unit power supply installation engineering, RMB 150,000 for machine room modification engineering, RMB 525,722 for labor cost of weak electricity installation, and RMB 60,000 for newly-added steel structure engineering on the first floor of Area A.

On September 17, 2011, Tongzhou General Contracting submitted a Budget (Final Account) for Weak Electricity Installation Labor Fee to Xinghua Estate, with quoted price at RMB 584,135. As the legal representative of Xinghua Real Estate, Chen X gave instructions on October 12, 2011 "agree to settle 10% below the quoted price." In addition, for the settlement of payment for the works of other items in the added items, Chen X as the legal representative of Xinghua Real Estate signed on January 12, 2012 on the Budget (Final Account) for Machine Room Modification Engineering, consenting to the payment of RMB 150,000; on June 13, 2011 on the Budget (Final Account) for Newly-added Steel Structure Engineering on the First Floor of Area A submitted by Tongzhou General Contracting, consenting to the payment of RMB 60,000; and on May 13, 2011 on the Budget (Final Account) for Air-conditioning Unit Power Supply Installation Engineering, consenting to the payment of RMB 95,000. On December 16, 2011, Tongzhou General Contracting compiled the Summary Statement for the Settlement of Supplementary Items. Xinghua Real Estate has made payment for the works in the amount of RMB 59,211,582 and has provided materials at a value of RMB 24,568,708.65.

On January 13, 2012, Xinghua Real Estate and the Engineering Office (No. 2) of Tongzhou General Contracting Hohhot Branch signed an Agreement on Setting Off Payment for the Works with Housing, whereby both parties agree to set off payment for the works, i.e., Party A's Water Supply Fortune Building contracted by Party B, with housings on the 9th Floor in Block A of the Building.

Tongzhou General Contracting at the first instance claimed that: (1) Xinghua Real Estate pay Tongzhou General Contracting for project payment in arrears in the amount of RMB 59,423,053; (2) Xinghua Real Estate pay Tongzhou General Contracting for interest on project payment in arrears (calculated from February 20, 2011 to the date of actual payment at the bank's loan interest rate for the same period); (3) Xinghua Real Estate pay Tongzhou General Contracting liquidated damages of RMB 11,594,336; (4) Xinghua Real Estate bear all litigation costs in this case. Xinghua Real Estate counterclaimed that: (1) Tongzhou General Contracting provide the completion acceptance report and complete engineering completion data of the engineering involved; (2) Tongzhou General Contracting return the 350 m^2 shop on the first floor of Block A of Hohhot Water Supply Fortune Building and the 30 m^2 office on the first floor of the property management building, and pay for shop rent loss of RMB 997,500 of the shop on the first floor from February 20, 2011 to September 20, 2012 (RMB 5 $\times$ 350 m^2 $\times$ 570 days = RMB 997,500). If the shop

and office cannot be returned immediately, order it to pay the rent loss until the actual return.

The court of first instance rendered a judgment on December 18, 2015 "(1) To order Xinghua Real Estate to make payment for the works to Tongzhou General Contracting within 30 days from the effective date of the judgment in the amount of RMB 59,423,053 and interest (calculated from February 20, 2011 to the date of full payment at the bank's loan interest rate for the same period); (2) To order Xinghua Real Estate to deliver to Tongzhou General Contracting within 30 days from the effective date of the judgment the completion acceptance report and engineering completion data of the engineering involved; (3) To dismiss other claims of Tongzhou General Contracting; and (4) To dismiss other counterclaims of Xinghua Real Estate."

Unsatisfied with the judgement of the court of first instance, Xinghua Real Estate lodged an appeal. In the second instance, Xinghua Real Estate acknowledged that, with regard to the 9th floor of Block A of the Fortune Building, no first registration of ownership and any transfer registration had been made.

Issue(s)

Whether the 9th floor of Block A of the Water Supply Fortune Building used for setting off payment for the works should be included in the payment for the works already made.

Holding

In the second instance, the Supreme People's Court holds that:

1. **On whether the 9th floor of Block A of the Water Supply Fortune Building used for setting off payment for the works should be included in the payment for the works already made**

First, unless otherwise specified by the parties, the offsetting debt with property agreement signed by the parties upon expiration of debt satisfaction period does not take as the requirement for its establishment or taking effect the creditor's actual receipt of the debt-offsetting property or obtain the ownership, right to use or other property rights of the debt-offsetting property. In this case, the Agreement on Setting Off Payment for the Works with Housing signed by Xinghua Real Estate and the Engineering Office (No. 2) of Tongzhou General Contracting Hohhot Branch on January 13, 2012 is valid and effective because it is the true manifestation of intent of the parties, and is not in violation of any law and administrative regulation.

Second, the offsetting debt with property agreement signed by the parties upon expiration of debt satisfaction period may constitute either a change of debt, or a new

debt to be satisfied. Based on the concept of protecting creditor's rights, change of debt generally requires the explicit consent of the parties to eliminate the old debt. Otherwise, the offsetting debt with property agreement signed by the parties upon expiration of debt satisfaction period is in nature generally new debt to be satisfied. In this case, the Agreement on Setting Off Payment for the Works with Housing signed by the parties is silent on the so discharged corresponding payment for the works, so the Agreement should in nature be an agreement for the satisfaction of a new debt.

Second, the so-called "satisfaction" refers to the payment of the debt pursuant to the purpose of the debt, the real intention of which is performance pursuant to the agreement. If the debtor fails to actually perform the offsetting debt with property agreement, the old debt between the creditor and the debtor has not been eliminated. In this case, the mere fact that the parties signed the Agreement on Setting Off Payment for the Works with Housing is yet sufficient to find that the 9th floor of Block A of the Water Supply Fortune Building used for setting off payment for the works should be included in the payment for the works already made. It should also be determined in light of the actual performance of the agreement.

On the one hand, the ownership of the housing on the 9th floor of Block A of the Water Supply Fortune Building is not registered under the name of Tongzhou General Contracting, so Tongzhou General Contracting dose not obtain the ownership of the housing on the 9th floor of Block A of the Water Supply Fortune Building. On the other hand, Xinghua Real Estate has already put into use the housing involved in the case at the end of 2010, so Tongzhou General Contracting has in fact delivered the housing including the 9th floor of Block A of the Water Supply Fortune Building. Xinghua Real Estate does not have sufficient evidence to overturn this fact, and there is no evidence that the 9th floor of Block A of Water Supply Fortune Building is currently under actual control or use by Tongzhou General Contracting. Therefore, it cannot be found that the 9th floor of Building A of Water Supply Fortune Building is actually delivered to Tongzhou General Contracting. It is thus clear that Xinghua Real Estate has not fulfilled the obligations under the Agreement on Setting Off Payment for the Works with Housing by either delivering the 9th floor of Block A of Water Supply Fortune Building to the actual possession of Tongzhou General Contracting, or register it under the name of Tongzhou General Contracting by ownership transfer, so for Tongzhou General Contracting, the proposed setting off corresponding payment for the works by the housing as agreed in the Agreement is not eliminated.

Finally, the parties should follow the principle of good faith and fully fulfill their obligations pursuant to the agreement. Thus, under the circumstance that the creditor and the debtor have reached an offsetting debt with property agreement and the new debt and the old debt coexist, the creditor should realize the creditor's right by claiming the new debt or the old debt. If non-performance of the new debt as due renders the purpose of the offsetting debt with property agreement unrealized, the creditor has the right to require the debtor to perform the old debt, and the exercise of such right of claim is not premised on the offsetting debt with property agreement being invalid, cancelled or dissolved.

In this case, the engineering involved was delivered at the end of 2010, when Xinghua Real Estate should but failed to settle and make payment for the works. On the contrary, Xinghua Real Estate attempted to setting off payment for the works in arrears with housing, and thus entered into the Agreement on Setting Off Payment for the Works with Housing with Tongzhou General Contracting. In this regard, Xinghua Real Estate should also actively perform the corresponding obligations in accordance with this Agreement. However, after the signing of the Agreement on Setting Off Payment for the Works with Housing, Xinghua Real Estate attempted to change the location of the setting-off-debt housing as agreed in the Agreement, and under the circumstance of not obtaining consent from Tongzhou General Contracting, Xinghua Real Estate neither took the initiative to timely deliver the setting-off-debt housing to Tongzhou General Contracting, nor resumed the performance of the old debt, i.e., making corresponding project payment in arrears to Tongzhou General Contracting. Xinghua Real Estate's non-performance of its obligations under the Agreement on Setting-off Payment for the Works with Housing violates the principle of good faith, leading to the un-realization of the purpose for signing the Agreement on Setting-off Payment for the Works with Housing by Tongzhou General Contracting. Under such circumstance, filing a lawsuit against Xinghua Real Estate requesting the latter to directly make project payment in arrears is in line with the spirit of the law and the actual situation of the case.

In summary, the amount of payment for the works to be set off by the housing located at the 9th floor of Block A of the Water Supply Fortune Building as agreed in the Agreement on Setting Off Payment for the Works with Housing shall not be included in the amount of paid payment for the works, so it is proper for the court of first instance to find and order Xinghua Real Estate to make corresponding project payment in arrears to Tongzhou General Contracting.

2. **On whether the judgment of first instance double counts the labor cost of the weak electricity installation engineering in the amount of RMB 525,722 as payment for the works payable**

The Final Account of the Water Supply Building Yubo Fortune Building Central Engineering (Newly-added Part), Cost Verification for Professional Engineering of Huhhot Water Supply Building, and other evidences submitted by Xinghua Real Estate are insufficient to establish its claimed facts, for which Xinghua Real Estate shall bear adverse consequences. Moreover, with regard to the two projects of CCTV monitoring system engineering and weak electricity installation engineering, the former is the professional installation engineering in the normal performance of the contract, which was settled by the parties in September 2009; and the latter is one of the added items established after the construction has actually been put into use, which was settled by the parties in October 2011. Unless there is evidence that the parties agree that the latter will not be subject to separate payment for the works, there is no factual and legal basis to claim that the CCTV monitoring system engineering in the amount of RMB 820,000 includes the latter's payment for the works. In addition, on the Budget (Final Account) for Weak Electricity Installation Labor Fee submitted by Tongzhou General Contracting, Chen X, as the legal representative of Xinghua

Real Estate, instructed in writing on October 12, 2011 "agree to settle at 10% below the quoted price." It shows that Xinghua Real Estate agrees to pay the labor cost of the weak electricity installation engineering at 10% below the price quoted by Tongzhou General Contracting, which is calculated to be RMB 525,722.

3. **On whether the value of the materials provided as determined in the judgment of first instance is correct**

Xinghua Real Estate claimed by submitting evidence of purchase and sales contract, payment vouchers, etc. in the first instance that the materials it supplied was worth about RMB 25 million, but Tongzhou General Contracting acknowledged the value to be RMB 24,568,708.65. Xinghua Real Estate submitted evidence of purchase and sales contract and payment vouchers for the part of its claim exceeding RMB 24,568,708.65, but explicitly stated that they would not be used as new evidence for the second instance, and the evidence was not sufficient to prove that the corresponding materials had been provided to Tongzhou General Contracting for the construction of the engineering involved, or there was no repetitive inclusion relationship with the materials approved by Tongzhou General Contracting in the first instance, which were not recognized by Tongzhou General Contracting in the second instance. Therefore, Xinghua Real Estate shall bear corresponding adverse consequences.

4. **On when shall the interest on payment for the works in arrears start to be calculated**

Although the two parties agreed in the Construction Contract for Construction Engineering involved in the case that 95% of the payment for the works shall be made within 30 working days after the completion of the audit within 30 working days after it was submitted to the audit department approved by the parties, the parties did not agree on the selection of the audit department, and further virtually cannot fix the date for payment as agreed. Therefore, it is not improper for the judgment of first instance to find that there is no explicit provision for the date of payment.

Pursuant to Article 18 of the *Judicial Interpretation on Construction Contracts for Construction Engineering*, it shall be determined that the payment for the works in arrears involved in the case shall be calculated from the date of actual delivery of the engineering. The engineering involved in the case, in the absence of completion acceptance check, was actually transferred to Xinghua Real Estate at the end of 2010 for its possession and use, so calculation of interest on the payment for the works in arrears from the end of 2010 is in line with the actual situation of the case. Of course, since Tongzhou General Contracting claimed in the first instance that the interest should be calculated from February 20, 2011, which is later than the end of 2010, the interest on payment for the works in arrears shall be calculated from February 20, 2011, since parties have the right to dispose of their civil rights.

However, after the engineering involved in the case was actually delivered for use, Tongzhou General Contracting also engaged in some supplementary engineering pursuant to the agreement by the parties, and made corresponding settlement

from May 2011 to January 2012, involving RMB 830,722 for the payment for the works of newly added engineering. If the interest on this part of payment is also calculated from February 20, 2011, it is obviously contrary to the principle established in Article 18 of the *Judicial Interpretation on Construction Contracts for Construction Engineering*. Although the reason claimed in the petition for appeal by Xinghua Real Estate concerning the wrong calculation of interest on the payment for the works in arrears cannot be established, the appeal was made against the judgment of first instance concerning the calculation of interest on payment for the works in arrears, so the time for starting calculation of interest on payment for the works of newly added engineering in the amount of RMB 830,722 should also be dealt with. Considering that the payment for the works of each supplementary engineering is relatively small, and in the Summary Statement for the Settlement of Supplementary Items compiled by Tongzhou General Contracting on December 16, 2011, Chen X, as the legal representative of Xinghua Real Estate, signed on four supplementary engineering on different days, the latest of which being January 12, 2012, it is ruled within the court's discretion to calculate the interest on the payment for the works of supplementary engineering in the amount of RMB 830,722 from January 13, 2012. For the remaining payment for the works in arrears in an amount of RMB 25,173,837.35 (RMB 26,004,559.35–RMB 830,722), interest should nonetheless be calculated from February 20, 2011.

In summary, the Supreme People's Court rules "(1) To sustain Items 2, 3 and 4 of the judgment of first instance; (2) To amend Item 1 of the judgment of first instance to read as "to order Inner Mongolia xinghua Real Estate Co., Ltd." to make payment for the works to Tongzhou Construction General Contracting Group Co., Ltd. in an amount of RMB 26,004,559.35 and interest within 30 days from the effective date of this judgment (among which RMB 25,173,837.35 shall be calculated from February 20, 2011 to the date of full payment, and RMB 830,722 shall be calculated from January 13, 2012 to the date of full payment, at the interest rate of the People's Bank of China for the same period and same type of loan)."

Comment on Rule

1. Consensual offsetting debt with property agreement or real offsetting debt with property agreement

In judicial practice, it is highly controversial about the establishment of a offsetting debt with property agreement with only consent of the parties but no creditor actually receiving payment. The first view upholds that offsetting debt with property is "datio in solutum" (giving in payment) in nature, which means that the offsetting debt with property agreement is not established when the debtor has not actually received the payment. The second view is that the offsetting debt with property agreement should not be considered as a real contract.

The author believes that no generalization can be made as to the offsetting debt with property agreement is a consensual contract or a real contract, which shall be determined in judicial decisions by following the basic principles as follows:

(1) Do not equate offsetting debt with property with giving in payment

The giving in payment is only a situation of or an alternative to offsetting debt with property, but not all. Although from the perspective of traditional civil law theory, the giving in payment agreement should be a real contract, but it should not be considered that all offsetting debt with property agreements are real contracts. Otherwise, it will inevitably be caught in a mistake of taking part for all and not being exhaustive.

(2) The distinction between consensual contract and real contract can be traced back to the Roman law

From a strict perspective, the scope of consensual contracts is gradually expanding.[1] In modern civil law, the principle of freedom of contract is adopted, with no mandatory provisions for the type of contract. Since most of the contracts are established when the parties reach a consensus, they are consensual contracts, while real contract as a special contract must be specified by the law.[2] China's current law is silent on offsetting debt with property agreement being real contract, so from the perspective of basic jurisprudence, such an agreement in principle should be recognized as a consensual contract, i.e., the contract is formed when the parties reach a consensus.

(3) Offsetting debt with property takes party autonomy as its basic principle

Offsetting debt with property agreement, as one way to satisfy a debt, is the arrangement between the parties on how to pay off the debt, and, for the elements of such an agreement, the basic principle is respecting the parties' autonomy. Although China's law does not specify whether the offsetting debt with property agreement is a real contract, it does not preclude the parties from reaching an agreement based on the autonomy of the parities that the elements for the formation of the offsetting debt with property agreement is the creditor's actual receipt of the debt-offsetting property or obtaining such property rights as ownership and right to use. When the parties expressly make the above-mentioned agreement based on their true intention, it is generally deemed to constitute giving in payment, which is a real contract. However, if the parties do not explicitly make the above-mentioned agreement, in the interpretation of the contract, it is generally concluded that the offsetting debt with property agreement is established when the parties reached a consensus.

In addition, those who insist on the real nature of offsetting debt with property also hold that the purpose of offsetting debt with property is to use another property to offset the original debt, with the act of offsetting debt not changing the identity of the original debt, so only when the property right is transferred to the creditor, can the

[1] [Japan] Matsusaka [1], quoted from Han Shiyuan, *General Theory of Contract Law*, 3rd ed., Beijing, Law Press, 2011, p. 59.

[2] Han [2].

debt be eliminated. Therefore, consensus alone without actual transfer of property rights will not eliminate the debt, and the purpose of offsetting debt is not realized, hence from the perspective of offsetting debt, we should hold its real nature. The author believes that this reason also cannot be established.

Although giving in payment has fundamentally solved the problem of debt satisfaction, it is obviously too arbitrary and absolute to exclude the arrangement between the parties for debt satisfaction. In fact, after the formation of the offsetting debt with property agreement, the ultimate goal of offsetting debt is not reached before actual receipt of the debt-offsetting property, but it still has a positive impact for the purpose of debt satisfaction, because the creditor and debtor attempts to make arrangement on debt satisfaction and take a step further toward the positive development. Moreover, this arrangement is also subject to regulation on new debt satisfaction or change of debt in contract law, through which the ultimate effect of debt satisfaction can also be achieved.

In this case, in the Agreement on Setting Off Payment for the Works with Housing signed by Xinghua Real Estate and the Engineering Office (No. 2) of Tongzhou General Contracting Hohhot Branch upon expiration of debt satisfaction period, from the agreement of the parties, there is no consensus that the creditor's actual receipt of the debt-offsetting property or obtaining such property rights as ownership and right to use constitutes one element for the formation or taking effect of the Agreement, which is explicitly manifested by the parties and not in violation of any laws or administrative regulations, so the Agreement is lawfully formed and takes effect.

2. **Determination of the relationship between new debt and old debt**

An inevitable question in dealing with such disputes in practice is what is the nature of the legal relationship established between the parties when the parties reached an offsetting debt with property agreement upon expiration of debt satisfaction period, i.e., the old debt is replaced by or co-exists with new debt.

In judicial practice, how to distinguish change of debt and satisfaction of new debt when the parties sign the offsetting debt with property agreement upon expiration of debt satisfaction period? German scholar Dieter Medicus believes that change of debt is "change by contract the content and nature of the creditor's rights", whereby the creditor only has the new creditor's rights but not the old creditor's rights. However, "payment for satisfaction" is to juxtapose the new creditor's rights with the old creditor's rights, and the old creditor's rights are eliminated after the new creditor's rights are fulfilled. The debtor's assumption of new debt in favor of the creditor for the purpose of satisfying the creditor's rights without specifying in the contract the change of content and nature of the creditor's rights, i.e., the taking effect of new creditor's rights will eliminate the old creditor's rights for the latter has been changed, will be presumed to be "payment for satisfaction".[3] It can be seen that the

[3] See [Germany] Medicus [3].

new debt satisfaction agreement is only a consensus reached between the creditor and the debtor to add an alternative method of satisfaction. In the satisfaction of the new debt, the new debt assumed by the debtor is a method of fulfilling the old debt, rather than using the new debt to replace the old debt, so after the satisfaction of new debt is established, the new debt and the old debt are in a state of coexistence, with the old debt not directly eliminated due to the establishment of the new debt, and the completion of the new debt resulting in the elimination of the old debt. However, the change of debt is different in that the establishment of the new debt will simultaneously eliminate the old debt, with no correlation between the fulfillment of the new debt and the elimination of the old debt.

The author believes that, based on the difference between the two, in determining the legal nature of the offsetting debt with property agreement entered into by the parties upon expiration of debt satisfaction period, i.e., the relationship between the new debt and the old debt, the basic principles to be followed are as follows:

(1) Respect the party's autonomy

A contract in essence is an agreement whereby the parties ascertain their mutual rights and obligations through free negotiation and adjust their mutual relationship pursuant to their free will. As long as there is no malicious collusion in the contract to damage the interests of the state, collective or third party, cover illegal purpose by legitimate means, violate the mandatory provisions of laws and administrative regulations, the nature of the corresponding legal relationship shall be determined based on the agreement of the parties. The offsetting debt with property agreement is a change of debt if the parties specify that the debtor shall offset the debt with the ownership of certain property, and the old claim and debt relationship extinguishes when the agreement takes effect, or is satisfaction of new debt if the parties specify that the debtor shall offset the debt with the ownership of certain property, but the old debt will not extinguish before the debtor completes the performance of the new debt. Therefore, when determining the nature of the offsetting debt with property agreement, we should avoid a "single" and "one size fits all" approach, but make distinction pursuant to the consensus reached by the parties.

(2) Probe into the genuine intention of the parties in case of no agreement or ambiguous agreement as to whether the old debt extinguishes upon the formation of the new debt

When the contract needs to be interpreted for ambiguity, the judge shall interpret it in a manner that best suits the party's intention. Therefore, the debtor's negotiation with the creditor for the change of performance due to difficulties in the fulfillment of the old debt is a process of gaming between the creditor and the debtor for the purpose of fulfilling the creditor's rights, so we can infer the genuine intentions of the parties in light of the parties' manifestation of intention in their negotiation for offsetting debt with property.

(3) Interpret in favor of the creditor when the evidence is insufficient to infer that the parties have reached a consensus on the elimination of the old debt upon the establishment of the new debt

In the creditor-debtor relationship formed on the contract, the basic standpoint is to protect the creditor's rights, which is based not only on the basic principle that the contract should be fully and timely fulfilled, but also on the basic requirement of the principle of good faith. Therefore, in the interpretation of the contract, unless there is sufficient evidence to prove that the parties have reached a consensus, no explanation should be made in prejudice to the creditor's rights. There is a clear distinction between the change of debt and the satisfaction of new debt as to the extent of protecting the creditor's rights. In the change of debt, since the old debt is extinguished when the new debt is established, in case of impossibility of performance due to any legal or factual reason, the creditor's right cannot be returned to the old debt and would generally resides on the debtor's property of general liability, which is obviously less favorable for the creditor. Based on the concept of protecting the creditor's rights, the change of debt generally requires the explicit consent of the parties to eliminate the old debt, which it seems not appropriate in principle to conclude through the interpretation of semantically vague words such as "setting off" and "expiating". therefore, the offsetting debt with property agreement signed by the parties upon expiration of debt satisfaction period is usually satisfaction of new debt in nature.

In this case, the Agreement on Setting Off Payment for the Works with Housing signed by the parties is silent on the so discharged corresponding payment for the works, so the Agreement should in nature be an agreement for the satisfaction of a new debt.

3. **Selection from and restrictions on the performance of old debt or new debt**

The important role of new debt would be hard to reflect by merely recognizing the simple coexistence of new debt and old debt. Therefore, the question that needs to be further answered is how the parties should perform between the new debt and the old debt, how to coordinate the two in the performance, or whether the creditor or the debtor has the right to select (require) the performance of new debt or old debt.

In the new debt satisfaction contract, it is admittedly not wrong that the debtor unilaterally assumes the obligation to satisfy the debt pursuant to the new method, but based on the purpose of offsetting debt with property in the new debt satisfaction contract, i.e., the new debt satisfaction contract is signed to offset debt with property because it is difficult for the debtor fulfill the old monetary debt pursuant to the contract, there should be some limitations on the right of the creditor and debtor to select (require) performance of new debt or old debt.

As for the creditor, although, in the new debt satisfaction contract, the creditor does not assume the obligation of paying consideration, the contract is, after all, an arrangement for debt satisfaction with the debtor, which shall be performed pursuant to the principle of good faith. As some scholars have pointed out, it is not appropriate to allow a creditor to select from the two rights of claim, which will lead to the adverse consequences for the debtor - the debtor will prepare for the performance of

the new and old debts at the same time, waiting for the creditor's choice. This would undoubtedly aggravate its burden, unfair and insufficient to balance the interests of both parties. Even in case of new debt satisfaction between a third party and the creditor, allowing the creditor to select from the rights of claim would necessitate preparation for the performance of new and old debts by the third party and the debtor, which is not conducive to balancing the relationship between the three parties, and not in compliance with the principle of efficiency.[4] Therefore, in the case of a substituted performance agreement between the creditor and debtor and co-existence of the new debt and old debt, in determining whether the creditor should fulfill the creditor's right by claiming the new debt or the old debt, the principle of good faith and efficiency shall be followed to prioritize the new debt and the old debt. The creditor can only exercise the right to claim new debt first, and, if the new debt is not fulfilled within the prescribed time period, or if, in the absence of explicit agreement on the period of performance, the debtor expressly states or indicates through his act that it will not fulfill the new debt, thus rendering the purpose of the agreement on offsetting debt with property not able to be realized, the creditor has the right to request the debtor to fulfill the old debt, the exercise of which is not conditioned on the dissolution of agreement on offsetting debt with property.

As for the debtor, there is a view that the new debt satisfaction contract is a unilateral contract. The creditor, by entering into a new debt satisfaction contract, has in fact made certain concessions on the debtor's satisfaction of debt by agreeing to add means of satisfaction, and under such circumstances, allowing the debtor to back out at any time and choose to perform the old debt would place the creditor in an unpredictable state of instability. This viewpoint is not unreasonable, but from the aim of entering into the new debt satisfaction contract, even for the purpose of realizing the creditor's ultimate purpose, i.e., realizing its creditor's rights, it is obviously more advantageous for the debtor to perform the new debt satisfaction contract, and its reneging on the new debt satisfaction contract and fulfillment of the old debt instead is essentially abandoning the more beneficial means of debt satisfaction; on the other hand, the debtor's fulfillment of the old monetary debt is generally more favorable to the creditor, or at least in line with the expectation of the creditor's old debt with the debtor. Therefore, based on the particularity of offsetting debt with property and comprehensive balance of the interests of the creditor and the debtor, there should be some limitations on the new debt satisfaction contract binding on the debtor, i.e., the debtor can back out and choose to fulfill the old debt even after the new debt satisfaction contact is formed and takes effect. At this point, the arrangement on offsetting debt with property fails, and the creditor should exercise the creditor's right of claim based on the old creditor and debtor relationship.

[4] Fang [4].

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Xiamen Yuanchang Real Estate Development Co., Ltd. v. Hainan Yuexin Group Co., Ltd. (Contract Dispute)—Disposal as to When the Active Claims Claimed by the Creditor to be Used for Offsetting Exceed the Statute of Limitations

Hongyu Chen

Rule

That both parties' debts are due, as one of the positive conditions for the formation of statutory right of set-off, should be understood that both parties' debts have entered the period for fulfillment, i.e., entering the state of performance, and there should be overlapping parts between the parties' debts during the period from the time when the debts are due to the expiration of the statute of limitations. When the active claims claimed by the Creditor to be used for offsetting exceed the statute of limitations, because the statutory right of set-off has formed before the expiration of statute of limitations period, and no preemption is prescribed for statutory right of set-off in Chinese law, such claims can still be found to be lawfully set off, by taking full consideration of such factors as the guaranty function of the right of set-off, reasonable period for exercise, and substantive fairness.

Collegial panel judges of the Supreme People's Court for re-trial: Chen Hongyu, Wang Yuying, Cao Gang (Written by: Chen Hongyu, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_18

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellant in the second instance): Xiamen Yuanchang Real Estate Development Co., Ltd. (hereinafter referred to as "Yuanchang Real Estate")
Respondent in the retrial (Defendant in the first instance, Appellant in the second instance): Hainan Yuexin Group Co., Ltd. (hereinafter referred to as "Yuexin")

2. Procedural History

First Instance: No. 152 [2016], Trial, Civ. Division, Haikou Intermediate People's Court of Hainan Province (dated Sep. 28 of 2016)
Second Instance: No. 2 [2017], Final, Civ. Division, the Higher People's Court of Hainan Province (dated Mar. 29 of 2017)
Retrial: No. 51 [2018], Retrial, Civ. Division, the Supreme People's Court (dated May 29 of 2018)

3. Cause of Action

Dispute over entrustment contract

Essential Facts

On November 18, 2005, Yuexin, in the name of a promisor, issued a Commitment Letter to Yuanchang Real Estate and Hou X, which, among other things, provides: Yuexin is entrusted by Yuanchang Real Estate and Hou X on April 1, 2005 to be responsible for going through procedures with the army required for the development of Xiamen Yuanchang Real Estate Development Project (Xiamen Plot No. 2726A), for which the principal shall pay a total of RMB 30 million and deliver two Mercedes-Benz cars; Yuexin confirms that as of April 13, 2005 it has received entrustment fees of RMB 20 million; Yuexin undertakes to complete the entrusted matters before January 28, 2006, otherwise it will return before February 18, 2006 the full entrustment fees of RMB 20 million to Yuanchang Real Estate and Hou X, who can take other remedial measures if the payment is overdue.

In 2005, Yuanchang Real Estate and Yuexin engaged in negotiations for investment cooperation. On August 15, 2005, Yuexin remitted investment funds of RMB 28 million to the bank account of Yuanchang Real Estate, who latter on October 26, 2005 returned the investment funds of RMB 8 million to Yuexin. On November 29, 2011, Yuexin filed a lawsuit with the Higher People's Court of Fujian Province for the payment of the undistributed investment benefits of RMB 151,402,484 by Yuanchang Real Estate to Yuexin on the ground that RMB 20 million remitted to the bank account of Yuanchang Real Estate is investment funds to the equity interests

of Yuanchang Real Estate. The court in its judgment rejects the request of Yuexin, which has legally taken effect.

On June 26, 2014, Yuexin filed a lawsuit with the Intermediate People's Court of Haikou, Hainan Province (Dispute over corporate lending, No. 64 [2014], Civ. Division), requesting Yuanchang Real Estate to return RMB 20 million and interest, and Yuanchang Real Estate filed a counterclaim in the case, requesting confirmation that the claims and debts between Yuanchang Real Estate and Yuexin have been set off. The court held that the counterclaim filed by Yuanchang Real Estate was dispute over the entrustment contract, which was of a different legal relationship and based on different legal facts with that of the action in chief filed by Yuexin, and decided not to accept the counterclaim filed by Yuanchang Real Estate. The court ruled that Yuanchang Real Estate pay RMB 20 million and interest to Yuexin. Unsatisfied with the judgment of the court, Yuanchang Real Estate lodged an appeal with the Higher People's Court of Hainan Province, which ruled on July 26, 2016 to sustain the original judgment.

Thereafter, Yuanchang Real Estate also filed this lawsuit on the ground that Yuexin failed to pay the entrustment fees as set forth in the Commitment Letter, requesting to release the Commitment Letter; and confirm that Yuanchang Real Estate enjoys creditor's right against Yuexin and has right to offset it against the claims and debts with Yuexin in equal amount. On September 28, 2016, the Intermediate People's Court of Haikou, Hainan Province rendered a civil judgement (No. 152 [2016], Trial, Civ. Division) "(1) To release the Commitment Letter between Yuanchang Real Estate and Yuexin; (2) To confirm that Yuanchang Real Estate enjoys creditor's right of RMB 20 million and damages thereof against Yuexin; and (3) To dismiss other claims of Yuanchang Real Estate". After the judgment of the first instance, Yuanchang Real Estate and Yuexin lodged an appeal respectively, and on March 29, 2017 the Higher People's Court of Hainan Province rendered a civil judgment (No. 2 [2017], Final, Civ. Division) "To revoke the judgment of the first instance and dismiss the claims of Yuanchang Real Estate". Unsatisfied with the judgment, Yuanchang Real Estate applied to the Supreme People's Court for retrial.

Issues

1. How to determine the creditor's claim of Yuanchang Real Estate against Yuexin;
2. Whether the request of Yuanchang Real Estate to confirm the creditor's right has exceeded the statute of limitations;
3. Whether Yuanchang Real Estate can claim to offset the debt against Yuexin.

Holding

On December 27, 2017, the Supreme People's Court entered a civil ruling (No. 3368 [2017], App. Ruling, Civ. Division) to issue a writ of certiorari.

Upon review in the retrial, the Supreme People's Court finds that, pursuant to Paragraph 1, Article 99 of the *Contract Law*, which stipulates that "where the parties are liable to each other for obligations that are due, if the type and nature of the subject matter of such obligations are the same, then each party may offset its own obligation against the obligation of the other party, unless it is prohibited by law or the nature of the contract", before the expiration of the statute of limitations for the creditor's claim for the entrustment fees in the amount of RMB 20 million enjoyed by Yuanchang against Yuexin, Yuanchang and Yuexin are already liable to each other for monetary obligations, which satisfies the elements for offsetting, so Yuanchang's right of set-off is established. On May 29, 2018, the Supreme People's Court rendered a civil judgment (No. 51 [2018], Retrial, Civ. Division) "(1) To reverse the civil judgment of the Higher People's Court of Hainan Province (No. 2 [2017], Final, Civ. Division) and the civil judgment of the Intermediate People's Court of Haikou, Hainan Province (No. 152 [2016] Trial, Civ. Division); (2) To confirm that the mutual debt of RMB 20 million between Yuanchang Real Estate and Yuexin has been setoff; and (3) To dismiss other claims of Yuanchang Real Estate".

Comment on Rule

Paragraph 1, Article 99 of the *Contract Law* set forth the requirements for the formation of the statutory right of set-off, i.e., where the parties are liable to each other for obligations that are due, if the type and nature of the subject matter of such obligations are the same, then each party may offset its own obligation against the obligation of the other party, unless it is prohibited by law or the nature of the contract.

As for the positive conditions for its formation, the statutory right of set-off requires that the parties are mutually obligated, the obligations are due, and the type and quality of the subject matter are the same, among which the obligations are due shall be understood as follows: first, both parties' obligations have entered the period for fulfillment, i.e., entering into the state of performance; second, there should be overlapping parts between the parties' obligations during the period from the time when the debts are due to the expiration of the statute of limitations. That is to say, as for the obligation whose statute of limitations expire earlier, before the expiration of the statute of limitations, the creditor's claim of the other party has entered the period for performance; and as for the obligation whose statute of limitations expire later, at the time when the period for performance starts, the statute of limitations for the creditor's claim of the other party has not expired. In the overlapping part of the above time periods, the creditor's rights of both parties are in the state of being able to be performed, free from any defense for statute of limitations,

so the condition that "the obligations are due" is satisfied, and the satisfaction of such condition cannot be affected even if the active creditor's claim has exceeded the statute of limitations when the right of set-off is later exercised. On the other hand, if there is no overlapping part in the above time periods, i.e., the creditor's right of one party has not entered the period for performance when the statute of limitations for the creditor's right of the other party has expired, then when the former creditor's right can be performed, the other party can raise the defense that its own creditor's right has not entered to the period for performance; and when the later creditor's right can be performed, the other party can raise the defense that its own creditor's right has exceeded the statute of limitations. In this way, the creditor's rights of both parties are not at the same time in the state of being able to be performed and free from any defense mentioned above. Such condition cannot be said to be satisfied even if the later obligation has entered the period for performance when the right of set-off is later exercised. Because the defense of the statute of limitations for passive claims can be waived by the parties, it can be determined that when examining the positive conditions for the formation of the right of set-off, the emphasis should be put on the examination of the statute of limitations for active claims, i.e., where, before the expiration of the statute of limitations for the active claims, the passive claims enter the period for performance, it shall be considered that the condition that the obligations of both parties are due is satisfied, otherwise such condition shall not be found to be satisfied.

In terms of the passive conditions for the formation of the right, Paragraph 1, Article 99 of the *Contract Law* specifies that "unless it is prohibited by law or the nature of the contract". In this case, both parties have mutual monetary obligations arising from the entrustment contract and the loan contract, which are not obligations that cannot be offset pursuant to the law or by the nature of the contract. As for the issue of offsetting the obligations exceeding the statute of limitations, it falls within the content for the examination in the positive conditions for the formation of the right, which will not be repeated here. Paragraph 2, Article 99 of the *Contract Law* stipulates the exercise the statutory right of set-off, i.e., the party who claims such offset shall notify the other party. The notice shall become effective when it reaches the other party. The offset shall not be subject to any condition or time limit. Therefore, it can be concluded that the notice is only the means of exercising the statutory right of set-off, and whether the party has timely exercised the right of set-off by notifying the other party after the establishment of the right of set-off does not affect the establishment of the right of set-off. In addition, since both parties to the offsetting relationship assume obligation to each other, which to a certain extent functions as a guaranty for its own creditor's right, no preemption is prescribed for the right of set-off in Chinese law, rather it stipulates that the party claiming the right to set-off exercises its right of set-off, the other party can raise an objection within a certain period of time. But even so, the exercise of the right of set-off should not be unreasonably delayed.

China Resources Bank of Zhuhai Co., Ltd. v. Jiangxi Electric Power Fuel Co., Ltd. and Third Party Guangzhou Dayou Coal Sales Co., Ltd. (Dispute over Factoring Contract)—Debtor's Assumption of Liability in Dispute over Factoring Contract

Lunjun Zhou

Rule

In a factoring contract with recourse, the contract for the assignment of creditor's rights is an indirect payment contract for the settlement of debts under the loan contract, rather than a pure assignment of creditor's rights. Before the settlement of the factored debt, subject to the principle of good faith, the factor has the right and obligation to claim from the secondary debtor first, and, for the part the secondary debtor fails to pay off, the debtor shall assume supplementary liability. To the extent that the factor is in good faith and without any fault, the debtor and the secondary debtor shall not challenge the factor for the absence of the receivables and other defect.

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellant in the second instance): China Resources Bank of Zhuhai Co., Ltd. (hereinafter referred to as "China Resources Bank")

Collegial panel judges of the Supreme People's Court for re-trial: Zhou Lunjun, Ma Dongxu, Wang Jun (Written by: Zhou Lunjun, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_19

Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): Jiangxi Electric Power Fuel Co., Ltd. (hereinafter referred to as "Fuel Co.")
Third party: Guangzhou Dayou Coal Sales Co., Ltd. (hereinafter referred to as "Dayou Coal Co.")

2. **Procedural History**

First Trial: No. 435 [2016], Trial, Civ. Division, Nanchang Intermediate People's Court of Jiangxi Province (dated Jan. 26 of 2016)
Second Instance: No. 325 [2016], Final, Civ. Division, the Higher People's Court of Jiangxi Province (dated Aug. 5 of 2016)
Applied for Retrial: No. 359 [2017], App. Ruling, Civ. Division, the Supreme People's Court of the People's Republic of China (dated Mar. 27 of 2017)
Retrial: No. 164 [2017], Retrial, Civ. Division, the Supreme People's Court (dated Jun. 28 of 2017)

3. **Cause of Action**

Dispute of factoring contract

Essential Facts

On September 17, 2013, China Resources Bank and Dayou Coal Co. signed the Omnibus Credit Facility Agreement, stipulating that China Resources Bank will provide the highest omnibus credit line of RMB 200 million to Dayou Coal Co., for which Zhushui Energy Resource Group Co., Ltd, Li X (A) and Li X (B) will provide surety of joint and several liabilities for Dayou Coal Co. On November 6, 2013, subject to the above-mentioned Omnibus Credit Facility Agreement, China Resources Bank and Dayou Coal Co. signed the Domestic Factoring Business Contract with a financing line of RMB 200 million in the type of disclosed factoring with recourse. In order to handle the factoring finance business, Dayou Coal Co. altered and submitted to China Resources Bank a Coal Sales Contract signed with Fuel Co., which, after alteration, specified that the quantity of the coal to be sold was 95,000 tons at a price of RMB 46,115,344.70, and that Dayou Coal Co. shall assign to China Resources Bank the accounts receivable of RMB 46,115,344.70 to be paid by Fuel Co. under the contract. On October 24, 2013, personnel from both China Resources Bank and Dayou Coal Co. went to Fuel Co. to check the authenticity of the accounts receivable related to the factoring business involved in the case. The Confirmation of Assignment of Accounts Receivable and the Confirmation of Notice of Assignment of Accounts Receivable is affixed with the common seal of Fuel Co. and signed by the then party secretary, Zeng X, confirming the account payable to Dayou Coal Co. in the amount of RMB 46,115,344.70 by stating that "the trade background is truthful, lawful and valid, and it is agreed to assign the accounts receivable to China Resources Bank". On November 8, 2013, subject to

the above-mentioned Domestic Factoring Business Contract, China Resources Bank issued 4 bank acceptance bills to Shanxi Jinyun Energy Co., Ltd. for Dayou Coal Co., with a total acceptance amount being RMB 36.8 million and date of maturity being April 8, 2014. When the above-mentioned acceptance bills fall due, China Resources Bank incurred advance payment for the above-mentioned acceptance bills because the funds of Dayou Coal Co. are not in place. On April 25 and June 24, 2014, China Resources Bank entrusted Guangdong Victor Law Firm to issue a Lawyer's Letter to collect the accounts receivable of RMB 46,115,344.70 due on March 22, 2014 and its interest to Fuel Co., who confirmed the receipt of the Lawyer's Letter, but refused to pay on the ground of simulated contract. China Resources Bank filed a lawsuit against the co-defendants of Dayou Coal Co., Fuel Co., Zhushui Energy Group Co., Ltd., Li X (A) and Li X (B), requesting them to repay the factoring finance of RMB 36.8 million and interest thereof. The Intermediate People's Court of Zhuhai, Guangdong Province dismissed China Resources Bank's lawsuit against Fuel Co. and ruled that Dayou Coal Co., Zhushui Energy Group Co., Ltd., Li X (A) and Li X (B) be liable for the payment of RMB 36.8 million and interest thereof. China Resources Bank filed this lawsuit against Fuel Co., requesting Fuel Co. to pay accounts receivable of RMB 46,115,344.70 and interest thereof.

The court of first instance rendered a judgment on January 26, 2016, dismissing the claim of China Resources Bank. Unsatisfied with the judgment of the court of first instance, China Resources Bank lodged an appeal and the court of second instance rendered a judgment on August 5, 2016, dismissing the appeal and sustaining the original judgment.

China Resources Bank applied to the Supreme People's Court for retrial.

Issues

1. Whether the defect in the underlying creditor's rights as claimed by Fuel Co. can be used to challenge China Resources Bank;
2. Whether the right claimed by China Resources Bank against Dayou Coal Co. in a separate lawsuit is right of recourse or reverse assignment of creditor's rights, and whether it has the right to continue to require Fuel Co. to pay off its debt.

Holding

After the retrial, the Supreme People's Court holds that:

When being verified of the authenticity of the accounts receivable by China Resources Bank, Fuel Co. directly confirmed by affixing its common seal the authenticity of the accounts receivable of RMB 46,115,344.70, rather than truthfully stating the actual performance of the Coal Sales Contract, so the altered Contract with

the subject matter of 95,000 tons should be held to be false manifestation of intent between Dayou Coal Co. and Fuel Co. by collusion, which, despite invalidity between the two parties, cannot be claimed by Fuel Co. against China Resources Bank because China Resources Bank has exercised the duty of due care and diligence.

China Resources Bank's claim against Dayou Coal Co. in a separate lawsuit does not constitute manifestation of intent for reverse assignment of creditor's rights, but exercise of the right of recourse, which, therefore, can coexist with the right of recovery claimed by Fuel Co..

The Supreme People's Court, in its retrial judgment, ruled to reverse the judgments of the first and second instances, and that Fuel Co. pay RMB 36.8 million and interest thereof within the range of RMB 46,115,344.70 and interest thereof to China Resources Bank.

Comment on Rule

1. **Legal nature of factoring contract and its application of law**

The factoring contract is not a nominate contract as stipulated in China's contract law, and there is no independent factoring contract in civil causes of action. As defined by the International Institute for the Unification of Private Law in the *Convention on International Factoring*, a factoring contract is "a contract concluded between one party (the supplier) and another party (the factor) pursuant to which the supplier may or will assign to the factor receivables arising from contracts of sale of goods made between the supplier and its customers (debtors) other than those for the sale of goods bought primarily for their personal, family or household use; the factor is to perform at least two of the following functions: finance for the supplier, including loans and advance payments; maintenance of accounts (ledgering) relating to the receivables; collection of receivables; protection against default in payment by debtors." According to the definition of factoring contract and factoring business in practice, factoring contract is a mixed contract of nominate and innominate contracts, which usually includes 3 major basic legal relations, i.e., factoring finance relation between the factor and debtor, underlying trading relation between the debtor and secondary debtor, and assignment relation of creditor's rights between the debtor and factor, and also involves the guaranty relation between the guarantor and the factor, etc.

Considering that the factoring contract is a mixed contract, pursuant to Article 124 of the *Contract Law*, which stipulates that "where there are no explicitly provisions in the Specific Provisions of this Law or in any other law concerning a certain contract, the provisions in the General Provisions of this Law shall be applied, and reference may be made to the provisions in the Specific Provisions of this Law or in any other law that most closely relate to such contract", dispute over a factoring contract shall be settled by direct application of the relevant provisions in the General Provisions of the

Contract Law, and application by analogy of the most similar nominate contract. At the same time, since contract is an agreement among natural persons, legal persons or other organizations as equal parties for the establishment, modification, termination of a relationship involving the civil rights and obligations of such entities, i.e., the law between the parties, to the extent that a contract is formed and takes effect pursuant to the General Provisions of the *Contract Law*, the economic purpose of the contract and the intention of the parties, and further the rights and interests of the parties shall be determined pursuant to the provisions of the contract.

2. **Co-existence of the factor's right of recovery and right of recourse**

According to the general theory in civil law system, the legal nature of the assignment contract of creditor's rights included in the factoring business with recourse is not a pure assignment of creditor's rights, but should be recognized as an indirect payment contract with the function of guaranteeing fulfillment of obligation. According to the agreement between the two parties in the Domestic Factoring Business Contract and the legal theory of indirect payment, the factor should first seek compensation from the secondary debtor, and, failing which, he can claim rights against the debtor. The right of recourse is functionally equivalent to guarantee by the debtor to the secondary debtor's ability to satisfy the debts, and such guarantee function is equivalent to the general guarantee of abandoning the benefit of discussion. Referring to the legal provisions on general guaranty in the Guarantee Law, the secondary debtor shall assume the primary liability for satisfaction of its obligations, and the debtor shall assume the supplementary liability for the part that cannot be satisfied.

As to whether the factor's right of compensation against the secondary debtor and its right of recourse against the debtor can be concurrently supported, the nature of the above-mentioned factoring contract indicates that factoring with recourse is a combination of loan and indirect payment, whereby the essence of the factor's claiming right of compensation against the secondary debtor based on the receivables is to request the secondary debtor to satisfy the new debt, and, in case the right of compensation cannot be satisfied, the essence of the factor's claiming right of recourse against the debtor is to request the debtor to satisfy the old debt, therefore, the old and new debts can coexist. As for the relationship between new and old debts, since the two claims claimed by the factor are both for the economic purpose of recovering the financing, in order to avoid double compensation by the factor, it should be clear that the obligations of satisfaction by the debtor and secondary debtor can be mutually offset, i.e., any party's satisfaction or partial satisfaction against the factor shall correspondingly relieve the other party from its obligation of satisfaction.

3. **Whether defect in the underlying creditor's rights can be used against the factor**

Pursuant to the basic principles of civil law, false manifestation of intent by the parties through collusion will be absolutely void between the parties. However, between the party making false manifestation of intent and the third party, different legal consequences will result depending on whether the third party knows or should know

such false manifestation of intent: the voidness of the false manifestation of intent can be used against the third party if the third party knows the false manifestation of intent between the parties, and the voidness of the false manifestation of intent cannot be used against the third party if the third party does not know the false manifestation of intent between the parties.

Shanghai Tailong Real Estate Development Co., Ltd. & Shen X v. Hainan Qianbo Lecheng Development Co., Ltd. & Jiang X (Dispute over Equity Transfer)—Identification of Multiple Actions in Civil Litigation

Bo He

Rule

1. Prohibition of multiple actions means that the parties shall not file an action for the same subject matter of an action that has already been filed. The identification and handling of multiple actions shall take into account and balance the protection of the right to sue, the purpose of the civil litigation system and the purpose and regulation of prohibition of multiple actions. Whether the parties and subject matter are identical in the former and later actions is a general criterion for determining whether it constitutes multiple actions.
2. Where the parties enter into an equity transfer agreement as a guarantee for private lending, if the lender requests performance of the equity transfer agreement when the borrower cannot repay the loan upon maturity, the people's court shall trial the case pursuant to the legal relationship of private lending. The people's court shall explain to the party on the change of the claim, and rule to dismiss the action if the party refuses to change. If after the case is tried pursuant to the legal relationship of private lending and the judgment rendered takes effect, the borrower fails to perform the monetary obligation as determined by the effective judgment, and the lender can apply for the auction of the subject matter of the equity transfer contract to repay the debt. The borrower or the lender has the right to claim return of or compensation for the difference between the proceeds of the auction and the principal and interest of the loan payable.

Collegial panel judges of the Supreme People's Court for re-trial: He Bo, Sun xiangzhuang, Jia Jingsong (Written by: He Bo, Supreme People's Court; Translated by: Niu Benlin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_20

Case Information

1. Parties

Applicant in the re-trial (Plaintiff in the first instance, Appellee in the second instance): Shanghai Tailong Real Estate Development Co., Ltd. (hereinafter referred to as "Tailong Real Estate")
Applicant in the retrial (Plaintiff in the first instance, Appellee in the second instance): Shen X
Respondent in the retrial (Defendant in the first Instance, Appellant in the second instance): Hainan Qianbo Lecheng Development Co., Ltd. (hereinafter referred to as "Hainan Qianbo")
Defendant in the first instance: Jiang X

2. Procedural History

First Trial: No. 1–3 [2015], Trial, Civ. Division, Shanghai Higher People's Court (dated Jul. 8 of 2015)
Second Instance: No. 315 [2016], Final, Civ. Division, the Supreme People's Court (dated Nov. 28 of 2016)
Applied for Retrial: No. 855 [2018], App. Ruling, Civ. Division, the Supreme People's Court (dated May 17 of 2018)

3. Cause of Action

Dispute over equity transfer

Essential Facts

Shen X provided a loan of RMB 240 million to Jiang X by remitting to a company related to Jiang X pursuant to the requirements of Jiang X. On April 8, 2010, Tailong Real Estate and Xingruitai signed a Land Use Right Transfer Contract, stipulating that Xingruitai shall transfer the land use right (No. 0879) under its name to Tailong Real Estate, and after the signing of the Contract, Tailong Real Estate shall pay a deposit of RMB 50 million to Xingruitai, and that, by April 30, 2012, Jiang X shall return by installments a loan of RMB 240 million and interest of RMB 75 million to Shen X; and the Land Use Right Transfer Contract signed by Tailong Real Estate and Xingruitai will be dissolved and Xingruitai shall return within the prescribed time limit the deposit of RMB 50 million and the fund occupation fee of RMB 10 million. On August 10, 2012, the parties involved in the case signed a Supplementary Agreement and a Memorandum, stipulating that (1) Hainan Qianbo shall establish two wholly-owned project limited liability companies (A and B project companies) by means of 100% independent investment with No. 5 and No. 7 plots located at Lecheng Island Development Zone, Bo'ao Town, Qionghai City, Hainan Province, with the land use rights covering an area of 129.6 mu and 137.87 mu, and Hainan Qianbo will transfer 100% equity of the above two companies to Shen X, who is

willing to accept the two wholly-owned companies established by Hainan Qianbo as agreed in this agreement; (2) After A Company and B Company were established and obtained the business license, Hainan Qianbo's equity transfer price for A company and B company amounts to RMB 185,446,600; and (3) The relevant parties to this Agreement agree that the equity transfer price as determined in Article 2 of this Agreement shall be used to offset the principal and interest of Jiang X to Shen X and the deposit and fund occupation fee of Xingruitai to Tailong Real Estate.

After the parties involved in the case signed the Memorandum, they signed a Supplementary Agreement II, stipulating that: (1) Shen X and Tailong Real Estate agree that the repayment date of the unpaid RMB 100 million by Jiang X, Xingruitai and Hainan Qianbo is postponed to one-time payment on October 31, 2012; (2) In order to compensate for the actual loss caused by postponed payment to Shen X and Tailong Real Estate: (1) Jiang X, Xingruitai, Hainan Qianbo and the guarantor Shanghai Qianbo undertake to pay as compensation RMB 30 million to Shen X and Tailong Real Estate on December 20, 2012; (2) The difference of RMB 31.361 million between the revised equity transfer price as stipulated in the original supplementary agreement and the total transfer price of the two project companies in the original Supplementary Agreement shall be paid by Jiang X, Xingruitai, Hainan Qianbo, and the guarantor Shanghai Qianbo to Shen X and Tailong Real Estate on December 20, 2012. On February 8, 2013, the parties involved in the case also signed the Repayment Agreement, stipulating that (1) Jiang X, Xingruitai and Hainan Qianbo will voluntarily transfer the equity of A and B companies and the interests of the two plots as agreed in the original Supplementary Agreement and Memorandum to Shen. X, and Tailong Real Estate (specifically, the Supplemental Agreement and Memorandum shall prevail) to offset the debts owed by Jiang X and Xingruitai to Shen X and Tailong Real Estate; (2) On the basis of Article 1 of this Agreement, Jiang X confirms that he will unconditionally pay Shen X RMB 235 million in four installments before May 20, 2013, which includes, but is not limited to, the principal, interest, liquidated damages, loss of expected profits, etc. However, it is irrelevant to the above-mentioned amount offset by Jiang X, Xingruitai and Qianbo Lecheng against equity transfer payment of A and B companies and the interests on the two plots owned by A and B companies.

The Plaintiff Tailong Real Estate and Shen X appealed to the Higher People's Court of Shanghai on May 22, 2015 on the ground that Hainan Qianbo and Jiang X failed to go through relevant formalities for equity transfer pursuant to the Supplementary Agreement, Supplementary Agreement II, Memorandum, Repayment Agreement and the Execution Settlement Agreement, requesting the court to order: (1) To transfer the equity of the project company involved in the state-owned land use right under No. 3487, 3489, and 3490 plots located in Bo'ao Town, Qionghai City, Hainan Province to the name of Shen X and Tailong Real Estate, otherwise Hainan Qianbo and Jiang X shall return RMB 153,815,000 to Shen X and Tailong Real Estate, and also assume the liability to compensate 150% of RMB 153,815,000, i.e., RMB 230,722,500; (2) To Compensate Shen X and Tailong Real Estate RMB 10 million; (3) To bear litigation fee, costs of preservation and all other costs in this case.

The court of first instance ruled to dismiss the objection of Hainan Qianbo to the court's jurisdiction over the case on the ground that it had jurisdiction over the case. Unsatisfied with the judgment of the first instance, Hainan Qianbo appealed to the Supreme People's Court. On the ground that this action filed by Shen X and Tailong Real Estate constitutes multiple actions, the court of second instance ruled: (1) To revoke the ruling of the first instance; and (2) To dismiss the action filed by Shen X and Tailong Real Estate.

Shen X and Tailong Real Estate applied to the Supreme People's Court for retrial, requesting to revoke the Civil Ruling (No. 315 [2015], Final, Civ. Division); and sustain the Civil Ruling of the Higher People's Court of Shanghai ([2015] Trial 1–3, Civ. Division 2).

In its retrial, the Supreme People's Court also finds that on August 23, 2013, Shen X filed an action with the court on the ground that Jiang X, Hainan Qianbo, Xingruitai and Shanghai Qianbo violated the aforementioned Supplementary Agreement, Supplementary Agreement II and the Repayment Agreement, as well as dispute over private lending. On April 23, 2014, the Shanghai No. 1 Intermediate People's Court rendered a civil judgment (No. 3 [2013], Trial, Civ. Division): 1. To order Jiang X to return the loan of RMB 128 million within 10 days from the effective date of the judgment; 2. To order Jiang X to pay Shen X the overdue interest from May 21, 2013 to August 8, 2013 within 10 days from the effective date of the judgment (calculated on the principal of RMB 148 million at the loan interest rate of the People's Bank of China for the same period and same type of loans); 3. To order Jiang X to pay Shen X the overdue interest till August 9, 2013 within 10 days from the effective date of the judgment (calculated on the principal of RMB 138 million at the loan interest rate of the People's Bank of China for the same period and same type of loans); 4. To order Jiang X to pay Shen X the overdue loan interest from August 10, 2013 to the effective date of the judgment within 10 days from the effective date of the judgment (calculated on the principal of RMB 128 million at the loan interest rate of the People's Bank of China for the same period and same type of loans); 5. To order Xingruitai, Hainan Qianbo and Shanghai Qianbo to be jointly and severally liable for the above-mentioned loan principal and interest; and 6. To dismiss other claims of Shen X. Unsatisfied with the judgment, Jiang X and Shanghai Qianbo lodged an appeal. The court of second instance dismissed the appeal and sustained the original judgment. During execution, the parties involved signed an Execution Settlement Agreement on May 14, 2015, stipulating the repayment obligation of Jiang X and Hainan Qianbo, and that any dispute shall be submitted to Shanghai No. 1 Intermediate People's Court for handling pursuant to law.

Issues

1. Whether filing an action by Tailong Real Estate and Shen X on the ground that Hainan Qianbo and Jiang X failed to fulfill the Supplemental Agreement and the Execution Settlement Agreement constitutes multiple actions;

2. Whether the parties signed the equity transfer agreement as a guarantee for private lending.

Holding

Shen X and Tailong Real Estate applied to the Supreme People's Court for retrial, which ruled to dismiss the application for retrial by Shen X and Tailong Real Estate.

After the trial, the Supreme People's Court holds that:

1. **On whether this court shall accept the request of Tailong Real Estate and Shen X regarding the change of equity**

The dispute over the private lending between Shen X and Jiang X based on the Agreement, Supplemental Agreement, Supplement Agreement II, Repayment Agreement and Memorandum signed by Jiang X and Shen X for the repayment of the loan from Shen X to Jiang X in the amount of RMB 240 million and relevant interest arising therefrom has been tried by Shanghai No. 1 Intermediate People's Court and Shanghai Higher People's Court, who have rendered effective judgments. During the execution of the effective judgment, the parties reached an Execution Settlement Agreement involved in the case. It is agreed in the Agreement that Hainan Qianbo shall establish two companies with the land use rights of No. 5 and No. 7 plots located at Lecheng Island Development Zone, Boao Town, Qionghai City, Hainan Province, and transfer 100% equity of the above two companies to Shen X, who is willing to accept the two wholly-owned companies established by Hainan Qianbo as agreed in this agreement; and that the equity transfer price totaling RMB 185,446,600 shall be used to offset the principal and interest of Jiang X to Shen X and the deposit and fund occupation fee of Xingruitai to Tailong Real Estate. However, the Supplementary Agreement II, Repayment Agreement, Memorandum and Execution Settlement Agreement thereafter signed by the parties all clarified that Hainan Qianbo and Jiang X chose to repay the debt in the form of repayment, rather than setoff relevant debt with equity transfer payment. The current action filed by Tailong Real Estate and Shen X for the implementation of the Execution Settlement Agreement is still intended to repay the loan involved in the case of private lending dispute. In light of the agreements signed and the intentions of the parties in this case, the court has tried the dispute as legal relationship of private loan and rendered an effective judgment. Because the borrower Hainan Qianbo and Jiang X failed to fulfill the monetary debt as determined by the effective judgment, the creditor Tailong Real Estate and Shen X may apply to offset relevant debt with the equity transfer payment as agreed by both parties, instead of filing this action. It is not inappropriate for the court of second instance to rule that the action filed by Shen X and Tailong Real Estate constitutes multiple actions.

2. **On the non-justiciablity of the Execution Settlement Agreement involved in the case**

The Execution Settlement Agreement in its head clarifies the conditions for signing the Agreement. In Article 4, Jiang X undertakes to be separately jointly and severally liable to Tailong Real Estate for the equity transfer payment and registration of equity transfer on No. 5 Plot Company A and No. 7 Plot Company B between the Tailong Real Estate and Hainan Qianbo. At the same time, Paragraph 3 of Article 3 of the Agreement stipulates that Tailong Real Estate and Shen X agree that, after Hainan Qianbo fulfilled as scheduled its obligation (repayment obligation) as stipulated in Article 2 of this Agreement on behalf of Jiang X, Hainan Qianbo will no longer be jointly and severally liable for other claims and debts between Tailong Real Estate and Shen X on the one hand and Jiang X on the other hand other than the land use right of two plots as agreed in Article 4 of the head of this Agreement. It can be seen that the parties, based on the performance of the Execution Settlement Agreement, have made reasonable arrangement as to the equity transfer payment and registration of equity transfer on No. 5 Plot Company A and No. 7 Plot Company B between the Tailong Real Estate and Hainan Qianbo. Pursuant to Article 466 of the *Judicial Interpretation on Civil Procedure Law*, which stipulates that "if the execution creditor and execution debtor reach a settlement agreement and request to suspend execution or withdraw the execution application, the people's court may decide to suspend execution or terminate execution", the defendants sued by Tailong Real Estate and Shen X include Hainan Qianbo and Jiang X, and whether Hainan Qianbo shall assume the obligation of equity transfer registration is involved in the Execution Settlement Agreement. The court of second instance has legal basis to rule that Tailong Real Estate and Shen X may apply to Shanghai No. 1 Intermediate People's Court to resume execution of the effective judgment of another case pursuant to Article 230 of the *Civil Procedure Law*, which stipulates that "if one party fails to perform the settlement agreement, the people's court may, upon the application of the other party, resume the execution of the original effective legal document."

3. **On whether the court of second instance can dismiss the action based on the party's objection to the jurisdiction**

Whether the case falls under the scope of acceptance by the people's court is within the discretion of the people's court. In this case, the Supreme People's Court's finding upon review that the case was already handled in the Execution Settlement Agreement of another case and ruling to dismiss the action pursuant to law are in compliance with Article 124 of the *Civil Procedure Law* and do not violate the legal procedures. In summary, Shen X and Tailong Real Estate's application for retrial is not in compliance with Items (2), (6) and (11) of the *Civil Procedure Law*. Pursuant to Paragraph 1 of Article 204 of the *Judicial Interpretation on Civil Procedure Law*, and Paragraph 2 of Article 395 of the *Interpretation of the Supreme People's Court on the Application of the Civil Procedure Law*, the Supreme People's Court rules to dismiss the application of Shen X and Tailong Real Estate for retrial.

Comment on Rule

The core dispute in this case is that where the parties enter into an equity transfer agreement as a guarantee for private lending, if the lender requests performance of the equity transfer agreement when the borrower cannot repay the loan upon maturity, the people's court shall trial the case pursuant to the legal relationship of private lending. The people's court shall explain to the party on the change of the claim, and rule to dismiss the action if the party refuses to change. If after the case is tried pursuant to the legal relationship of private lending and the judgment rendered takes effect, the borrower fails to perform the monetary obligation as determined by the effective judgment, and the lender can apply for the auction of the subject matter of the equity transfer contract to repay the debt. The borrower or the lender has the right to claim return of or compensation for the difference between the proceeds of the auction and the principal and interest of the loan payable. Therefore, the conclusion of the adjudication in this case is essentially the handling of the issue of the ownership assigned as guarantee and presents itself procedurally as the identification of multiple actions.

1. **On multiple actions**

Prohibition of multiple actions means that the parties shall not file an action for the same subject matter of an action that has already been filed, otherwise the court shall rule to dismiss the action. It takes as its main standard that whether the subject matters of the former and later actions are identical. The definition and treatment of multiple actions should take account of and balance the norms in prohibiting multiple actions and diversified purposes of the civil litigation system such as protection of private rights, resolution of disputes and the maintenance of judicial order. Article 122 of the *Civil Procedure Law* stipulates that "the people's court shall safeguard a party's lawful right to file an action." The civil litigation system should not only protect the lawful exercise of the parties' right to sue and the realization of relevant substantive rights and procedural interests, but also appropriately expand the function of the litigation system to resolve disputes, striving to resolve to the largest extent related disputes through one trial procedure. This will not only avoid conflicting adjudication, but also realize litigation economy, and save and rationally allocate judicial resources in the era of litigation explosion. Therefore, in the trial practice, when the main dispute or the basic facts claimed in the former and later lawsuits are identical, the judge should shoulder the tasks of interpreting change of claim, addition of claims, and counterclaim, providing the parties with a reasonable trial procedure and avoiding substantive and procedural detriment to the parties.

(1) Relationship among prohibition of multiple actions, non bis in idem and res judicata. The positive effect of non bis in idem is that one court cannot accept

and try the case which another has tried and the judgment on which has taken effect, and the negative effect is that the parties cannot re-file an action for the same case, and, even it is filed, the court will not accept it. The effect of res judicata is that the judgment that has already taken effect excludes other courts to accept and adjudicate the case, while the prohibition of multiple actions completely excludes the possibility of adjudication and judgment by other courts.[1] The negative effect of res judicata is prohibition on repetition, i.e., the parties may no longer dispute the case that has been sentenced, which is represented institutionally as prohibiting the parties from filing the case anew, or dismissing the case even if the party files the case anew; and the positive effect is avoiding contradictions, i.e., the court should be bound by the judgment of the former case when handling the latter case, which is represented institutionally as handling the latter case based on the determination of the subject matter of litigation as ascertained in the former judgment, and the contradiction (if any) between the latter judgment and the former determination could serve as a cause for latter judgment in the retrial.[2] The superimposed effect of non bis in idem and res judicata is the negative effect of res judicata, i.e., the parties cannot re-file an action for the same case, and, even it is filed, the court will not accept it.

Prohibition on multiple actions and non bis in idem are different. The purpose of the principle of prohibiting multiple actions is to facilitate the parties' resolution of dispute in the same litigation and to rationally allocate judicial resources, with its focus on litigation economy and prevention of contradictions; while non bis in idem refers to that one court cannot accept and try the case which another has tried and the judgment on which has taken effect, and the parties cannot re-file an action for the same case, and, even it is filed, the court will not accept it. The jurisprudential basis for prohibiting multiple actions is mainly reflected in the following three aspects: First, prohibiting the parties from lodging multiple actions can protect the procedural interests of the parties, and avoid multiple actions by the parties for the same dispute. Procedural interests are interests obtained in time, expense, and effort due to simplification of procedures or avoidance of cumbersome and unhelpful procedures. The principle of "protecting procedural interests" is a basic jurisprudential principle that civil procedure law should follow. With regard to multiple actions, although the plaintiff can use the right to protect interests through litigation proceedings, it should not file two lawsuits for the same dispute, resulting in detriment to the defendant; and the defendant's failure to lodge a counterclaim in the action in chief, rather than filing a separate action will lead to procedural detriment to the plaintiff. Second, prohibiting parties from lodging multiple actions can enable the courts to make reasonable use of judicial resources. Civil litigation is a system in which the state uses public power to resolve private disputes. The limited judicial resources of the state should be reasonably distributed among various litigation cases to prevent the court from repeating trials for the same case, resulting in

[1] Zhang [1].

[2] Shao [2].

waste of judicial resources. Third, prohibiting the parties from lodging multiple actions can help maintain judicial authority and avoid conflicting judgments on the same dispute. Protecting the procedural interests of the plaintiff and defendant, rationally using judicial resources, and preventing conflicting judgments are not only the norms of the principle of prohibiting multiple actions, but also the function and purpose of the system of prohibiting multiple actions.

(2) On judging criteria for multiple actions. The reason why the principle of prohibiting multiple actions becomes an academic point of contention and an unsolved problem in theory and practice is mainly because it might be difficult to constitutes reach a consensus on the judging criteria of what constitutes "multiple actions". The author believes that we can determine the existence of multiple actions from the following aspects.

(i) Whether the parties are identical. Determining whether the former action and the latter action are "repetitive", we must first see whether the parties to the two actions are identical, which is the subject element of multiple actions. Under normal circumstances, it is easier to determine whether the parties are identical in the former action and the latter action. In addition, when the current action is a joint action, as long as some of the co-plaintiffs or co-defendants are parties to the latter action, it can constitute multiple actions.[3]In this case, the former action is Shen X v. Jiang X, Hainan Qianbo, Xingruitai & Shanghai Qianbo (dispute over private lending), and the latter action is Tailong Real Estate & Shen X v. Hainan Qianbo & Jiang X (dispute over equity transfer). Shen X is the legal representative of Tailong Real Estate, and Jiang X is the legal representative of Hainan Qianbo. The Agreement signed by Shen X (creditor), Jiang X (debtor), Tailong Real Estate, Xingruitai, Shanghai Qianbo and Hainan Qianbo on February 21, 2012 specifies that Shen X shall (through Tailong Real Estate provide a loan of RMB 240 million in three installments to Jiang X by remitting to a company related to Jiang X pursuant to the requirements of Jiang X. Moreover, the disputes of the former action and latter action involve the relevant matters as agreed in the Agreement signed on February 21, 2012. Therefore it is obvious that the parties of the former and latter actions are identical and the subject matters of the actions are identical.

(ii) Whether the subject matters are identical. The subject matter theory is one of the core issues in civil procedures and has been controversial for a long time. The identical subject matters constitute the object element of multiple actions. Taking this case as an example, upon review, it is found that the former court accepted the case of dispute over private lending by Shen X against Jiang X, Hainan Qianbo Xingruitai and Shanghai Qianbo, in which Shen X requested the court to order Jiang X, Hainan Qianbo, Xingruitai and Shanghai Qianbo to repay Shen X the loan and the deposit in the amount of RMB 128 million on the ground that Jiang X and other defendants violated the aforementioned Supplementary Agreement, Supplementary Agreement II and Repayment Agreement, and Jiang

[3] [Japan] Nakamura [3].

X also indicated that the equity dispute at issue will be handled in a separate case, which will not be claimed in this case. In this case, Tailong Real Estate and Shen X filed a case with this court on May 22, 2015, requesting the court to order the defendants to transfer the equity of the project company involved in the state-owned land use right under No. 3487, 3489, and 3490 plots located in Boao Town, Qionghai City, Hainan Province to Shen X and Tailong Real Estate on the ground that Hainan Qianbo and Jiang X failed to go through corresponding formalities for equity transfer as agreed. During the trial of the case, it is find that it is agreed in the Agreement that Hainan Qianbo shall establish two companies with the land use rights of No. 5 and No. 7 plots located at Lecheng Island Development Zone, Boao Town, Qionghai City, Hainan Province, and transfer 100% equity of the above two companies to Shen X, who is willing to accept the two wholly-owned companies established by Hainan Qianbo as agreed in this agreement; and that the equity transfer price totaling RMB 185,446,600 shall be used to offset the principal and interest of Jiang X to Shen X and the deposit and fund occupation fee of Xingruitai to Tailong Real Estate… However, the Supplementary Agreement II, Repayment Agreement, Memorandum and Execution Settlement Agreement thereafter signed by the parties all clarified that Hainan Qianbo and Jiang X chose to repay the debt in the form of repayment, rather than setoff relevant debt with equity transfer payment. The current action filed by Shen X and Tailong Real Estate for the implementation of the Execution Settlement Agreement is still intended to repay the loan involved in the case of private lending dispute. In light of the agreements signed and the intentions of the parties in this case, the court has tried the dispute as legal relationship of private loan and rendered an effective judgment. Because the borrower Hainan Qianbo and Jiang X failed to fulfill the monetary debt as determined by the effective judgment, the creditor Shen X and Tailong Real Estate may apply to offset relevant debt with the equity transfer payment as agreed by both parties, instead of filing this action.

(3) On the handling of multiple actions. In China, multiple actions in action dependence are handled by legislation and judicial interpretation mainly in the following ways:

(i) Handled as jurisdictional issues. Article 35 of the *Civil Procedure Law* stipulates that "when two or more people's courts have jurisdiction over an action, the plaintiff may institute an action in one of such people's courts; and if the plaintiff institutes actions in two or more people's courts that have jurisdiction, the people's court which dockets the case first shall have jurisdiction over the action." The foregoing circumstance is concurrent jurisdiction from the perspective of the court, and is alternative jurisdiction from the perspective of the parties. In the case where the courts having jurisdiction over the case are not unique, the parties have the right to institute actions in two or more courts, but the courts may not docket or try the case repeatedly, and shall rule to transfer the case to the court which dockets the case first if the case is docketed. The

author holds that mandatory consolidation of different claims for the same case reflects the spirit of prohibiting multiple actions.

(ii) Change of claim. In the event of coincidence of liabilities for breach of contract and tort, the parties are given the right to file an action based on either one. Article 122 of the *Contract Law* stipulates that "in case that the breach of contract by one party infringes upon the personal or property interests of the other party, the aggrieved party is entitled to request the breaching party to assume liabilities for breach of contract in accordance with the *Law*, or to request the breaching party to assume liabilities for infringement in accordance with other laws." Article 30 of the *Judicial Interpretation on the Contract Law* further stipulates that "where the creditor has made choice when filing an action with the people's court pursuant to Article 122 of the *Contract Law*, but changes claim before the commencement of the trial of first instance, the People's Court shall allow such change. In the event the other party objects to the jurisdiction and upon review such objection is sustained, the people's court shall dismiss the action."

(iii) Reflect the principle of good faith. Article 13 of the *Civil Procedure Law* adds that "in civil procedures, the principle of good faith shall be adhered to." If the party files multiple actions by maliciously abusing the right to sue and in violation of the principle of good faith, the court will not accept the action. If the action is accepted but no judgment is made, the action shall be dismissed; and if a judgment is made, it shall enter the retrial in the name of the president's discovery, and the original judgment shall be revoked and the action shall be dismissed.

In summary, the dispute over private lending arising from such agreements as the Supplementary Agreement, Supplementary Agreement II and Repayment Agreement among Shen X, Jiang X and Hainan Qianbo was adjudicated by Shanghai No. 1 Intermediate People's Court and Shanghai Higher People's Court, and an effective judgment was rendered. During the execution of the effective judgment, the parties reached the Execution Settlement Agreement. The current action is filed by Shen X and Tailong Real Estate due to the performance of the Execution Settlement Agreement is identical in the main parties to the aforementioned two cases concerning the dispute over private lending; and the subject matters of the two cases are the rights and obligations of the parties based on such agreements as the Supplementary Agreement, Supplementary Agreement II and Repayment Agreement. The claim in the current case essentially has the effect of negating the judgments of the aforementioned private lending cases. According to Article 247 of the *Judicial Interpretation on Civil Procedure Law*, which stipulates that "where a new action is filed by the parties during the litigation or after the judgment takes effect for the same issue that has been raised in an action, and at the same time meets the following conditions, they constitute multiple actions: (1) They are identical in parties; (2) they are identical in subject matter; (3) they are identical in claims, or the claim of the latter action substantially denies the judgment of the former judgment. The court shall rule not to accept if the parties file multiple actions; or shall rule to dismiss the action if it has

been accepted, unless otherwise stipulated by law and judicial interpretation", filing this action by Shen X and Tailong Real Estate constitutes multiple actions, which should be dismissed pursuant to law.

2. **On ownership assigned as guarantee**

With the continuous development of China's economy and finance, civil laws have become more developed. Traditional methods of guarantees have been unable to meet the needs of ever-changing and evolving economic exchanges due to complicated procedures and high costs. In the judicial practice of private lending, new forms of guarantee have emerged. In order to increase the debtor's ability to pay debts and avoid the inability of the debtor to repay the loan, creditors will usually sign a sales contract, equity transfer contract, etc. (in the trial practice, the house sales contract and equity transfer are usually the main forms of expression) when signing a private lending contract with the borrower, providing that when the debtor cannot repay the loan, the debtor will sell or transfer the house, equity, etc. to the creditor in the form of performing the sales contract or equity transfer contract to terminate the loan contract relationship. The key issue to handle such disputes is to consider the true intentions of the parties in signing the sales contract—to provide guarantee for the loan legal relationship, or to provide consideration for performance of the real estate sales contract or equity transfer agreement. In this regard, if it is found that after (or before) the parties involved in the case signed the private lending contract, they also signed the real estate sales contract or equity transfer agreement in order to ensure the performance of the private lending contract, providing that when the debtor cannot repay the debt, it needs to transfer the subject matter of the guarantee, i.e., the right to the real estate or the company's equity, to the creditor, then it shall be determined that the parties' signed of the sale contract or equity transfer agreement is to provide guarantee for the private lending contract, and not to actually realize the purpose of the sale contract or equity transfer contract. Therefore, the legal relationship formed between the parties involved in the case is ownership assigned as guarantee.

Ownership assigned as guarantee means the right by which the debtor or the third party assigns the overall right (usually ownership) of the subject matter of the guarantee to the creditor to guarantee satisfaction of the debt, and resumes the overall right of the subject matter after the debt is satisfied, or if the debt is not satisfied upon maturity, the creditor has right to claim priority in satisfaction over the collateral. The differences between this form of guarantee and the traditional forms of guarantee are that this form of guarantee not only transfers the right to the subject matter of the guarantee, but such right is a complete right rather than a restricted right, and this form of guarantee includes a redemption clause. As an independent guarantee, ownership assigned as guarantee has the following basic characteristics:

(1) The ownership assigned as guarantee is an atypical guarantee. As determined by whether it is provided for in the civil code, real guarantee can be divided into typical guarantee and atypical guarantee. The mortgage, pledge and lien stipulated in the civil code are typical guarantees; and other real guarantees newly developed in social transactions and not stipulated in the civil code are atypical guarantees. The ownership assigned as guarantee is a kind of guarantee

that is confirmed by the precedents in practice and falls under atypical guarantee. Compared with typical guarantee, it has the following basic differences:

(i) Difference in legal composition. In terms of legal composition, the ownership assigned as guarantee is transfer of the right itself, while the typical guarantee is the establishment of servitude. In other words, the traditional typical guarantee is a kind of servitude, without assigning the overall right of the collateral, especially the ownership; while ownership assigned as guarantee is to assign the overall right of the collateral to the creditor, which means the guarantor's loss of ownership of the collateral (at least conceptually).

(ii) Difference in publicity. Publicity is usually necessary for typical guarantee, but not for ownership assigned as guarantee, for which agreement by the parties will suffice. Therefore, the typical guarantee has the exclusive right of subrogation, while ownership assigned as guarantee is a kind of right falling somewhere between the creditor's right and the property right—property right that can be claimed against a third person if it is registered; or creditor's right if not registered. In fact, ownership assigned as guarantee is to cover the content of the property right with the appearance of the creditor's right, while a typical guarantee is a restricted property right established in the form of obligation.

(iii) Difference in implementation. A typical guarantee is a right of realization, strictly prohibiting the parties from stipulating direct fluidity of collateral in the terms of the contract, i.e., to prohibit liquidity clause; while ownership assigned as guarantee is not subject to such restrictions, which can take the forms of realization and liquidity.

(2) The ownership assigned a guarantee is an agreed guarantee. Pursuant to the reasons for the occurrence of the security interest, it can be divided into statutory guarantee and agreed guarantee. Statutory guarantee occurs as a matter of law, such as liens, priority and statutory mortgages; while agreed guarantee occurs according to the agreement of the parties, such as general mortgage right and pledge right. Ownership assigned as guarantee is an agreed guarantee, the establishment of which is based on the agreement of the parties. Statutory guarantee has the effect of maintaining the equality of creditor's rights, and its nature of subordination is particularly strong; while agreed guarantee has the function of financing, and its nature of subordination has gradually decreased. Therefore, the law is different in its design as to the reasons for the establishment and effects of these two kinds of guarantees, so different methods shall be accorded for specific treatment.

(3) Ownership assigned as guarantee is a form of guarantee established by case law. Ownership assigned as guarantee is the product of confirmation by case law, and there is no statutory law in all countries around the world. Because ownership assigned as guarantee is a perverted and irregular guarantee, so the traditional civil law has no clear stipulations on its trust-type guarantee system and has questioned its legality, which was finally affirmed for its value and developed as

a form of guarantee through case law and jurisprudence. Other forms of property security are regulated by statutory law, with some in the civil code, and some in the special law.

In addition, the retention of ownership as a non-typical guarantee differs from the ownership assigned as guarantee mainly as follows:

(i) Different scope of application. The scope of ownership assigned as guarantee is more extensive, while retention of ownership applies only to the sale and purchase relationship, and generally only applies to installment purchase and purchase and lease.
(ii) Different subject matter. The subject matter of the ownership assigned as guarantee may be either the debtor's property or the property of a third party, while the subject matter of retention of ownership can only be the subject matter of the sale and purchase between the parties.
(iii) Difference in change of possession. The ownership assigned as guarantee generally adopts the method of change of possession, which does not directly transfer the possession of the subject matter, while the subject matter of retention of ownership shall be transferred to the buyer by the seller.
(iv) Difference in the use of the subject matter. For the use of the subject matter, the ownership assigned as guarantee is usually used by the guarantee setter, while the retention of ownership is used by the buyer.

In the trial practice, the handling of the issue of ownership guarantee is not uniform. The correct handling of such cases concerns not only the adjudication uniformity of the court cases, but also whether the legitimate rights and interests of the parties can be protected by law.

Article 24 of the *Judicial Interpretation on Private Lending* stipulates that where the parties enter into a sales contract as a guarantee for private lending contract, if the lender requests performance of the sales contract when the borrower cannot repay the loan upon maturity, the people's court shall trial the case as the legal relationship of private lending, and explain to the party to change claims. If the party refuses to change, the people's court shall rule to dismiss the action. If after the case is tried pursuant to the legal relationship of private lending and the judgment rendered takes effect, the borrower fails to perform the monetary obligation as determined by the effective judgment, and the lender can apply for the auction of the subject matter of the sales contract to repay the debt. "The borrower or the lender has the right to claim return of or compensation for the difference between the proceeds of the auction and the principal and interest of the loan payable." This article to some extent fills a gap in the law, which is to confirm restrictively in the form of judicial interpretation a large number of agreements on ownership assigned as guarantee in civil and commercial legal activities. This judicial interpretation plays a positive guiding role for today's civil and commercial legal activities. First of all, the premise of the application of this clause is that the parties sign a sales contract as a guarantee for the loan contract, i.e., the signing of the sales contract by both parties is not intended to be the subject matter of the sales contract, but merely takes the subject matter of the sales

contract as a guarantee for the debt in the lending contract. Therefore, the underlying legal relationship existing between the two parties should be recognized as the legal relationship of private lending, and the sales contract as a form of guarantee only has a subordinate status and is subordinate to the major legal relationship of private lending. Secondly, this article does not deny nor confirm the validity of the sales contract. When the borrower fails to fulfill the monetary debt as determined by the effective judgment, the lender cannot directly obtain the ownership of the subject matter of the guarantee, but should apply for the auction of the subject matter to repay the debt, i.e., the guarantee effect of the subject matter of the guarantee is affirmed. Finally, if the lender requests to perform the sales contract, the people's court shall explain to the party to change the claim. If the party refuses to change, the people's court shall rule to dismiss the action, which is a procedural dismissal of the action, rather than a direct substantive loss. This article actually confirms restrictively in the form of judicial interpretation a large number of agreements on ownership assigned as guarantee in civil and commercial legal activities, which has to some extent fill a gap in current law, and exerts positive guiding significance for current civil and commercial legal activities.

In light of the merits of the case, although the parties involved in this case agree in the Agreement that Hainan Qianbo shall establish two companies with the land use rights of No. 5 and No. 7 plots located at Lecheng Island Development Zone, Boao Town, Qionghai City, Hainan Province, and transfer 100% equity of the above two companies to Shen X, who is willing to accept the two wholly-owned companies established by Hainan Qianbo as agreed in this agreement; and that the equity transfer price totaling RMB 185,446,600 shall be used to offset the principal and interest of Jiang X to Shen X and the deposit and fund occupation fee of Xingruitai to Tailong Real Estate… However, from the Supplementary Agreement II, Repayment Agreement, Memorandum and Execution Settlement Agreement thereafter signed by the parties, it can be concluded that the real intention of the parties in agreeing on the equity transfer payment is not intended to be change of equity, but merely takes the equity transfer payment as a guarantee for the debt in private lending. Therefore, the underlying legal relationship existing between the two parties should be recognized as the legal relationship of private lending, and the equity transfer payment in equity change as a form of guarantee only has a subordinate status and is subordinate to the major legal relationship of private lending. i.e., when the borrower Hainan Qianbo and Jiang X fail to perform the monetary debt as determined by the effective judgment, the lender Tailong Real Estate and Shen X cannot directly obtain the equity transfer payment in the equity change, but should obtain the equity transfer payment in equity change through legal proceedings so as to repay the debt. In other words, if the debtor Jiang X fails to pay the principal and interest of the loan, the creditor Shen X may auction or realize the subject matter, and get the payment from the proceeds thereof. If proceeds from the auction or realization exceeds the principal and interest of the loan, the excessive part shall be returned to the debtor Jiang X; Similarly, if proceeds from the auction or realization is not enough for the principal and interest of the loan, then the creditor Shen X can still claim compensation from the debtor Jiang X.

This case is not an independent equity transfer relationship, but a part of claim and debt relationship in private lending. This case of Tailong Real Estate and Shen X falls under violation of the principle of good faith, abuse of the right to sue, and multiple actions. The court, in ruling to dismiss the action filed by Tailong Real Estate and Shen X, prohibits multiple actions and takes account of fairness and justice.

The case occurred before the introduction of the *Judicial Interpretation on Private Lending*, and now with Article 24 of the *Judicial Interpretation on Private Lending*, it is believed that the line of thoughts in ruling similar cases will be clearer than the ruling of this case.

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China Biodiversity Conservation and Green Development Foundation v. Ningxia Ruitai Technology Co., Ltd. (Public Interest Litigation Against Environmental Pollution)—The Identification of Subject Qualification in Environmental Civil Public Interest Litigation Filed by Social Organizations

Yang Ye

Rule

Where the articles of association of a social organization do not specify the protection of environmental public interests, but its work content includes the protection of environmental elements and ecological system, it shall be determined in accordance with the provisions of Article 4 of the *Interpretation of the Supreme People's Court on Several Issues concerning the Application of Law in the Trial of Environmental Civil Public Interest Litigation* (hereinafter referred to as the "*Interpretation*") that "the tenets and main business scope determined in the articles of association of a social organization are to maintain the social public interests". The "public activities of environmental protection" stipulated in Article 4 of the *Interpretation* include not only the activities directly improving the ecological environment, but also the activities related to environmental protection that are conducive to enhancing the environmental governance system, improving the environmental governance capacity, and promoting the whole society to form broad consensus on environmental protection. If the matters involved in the suit filed by a social organization have corresponding relevance with its tenets and business scope, or have a certain connection with the environmental elements and ecological systems under its protection, it shall

Collegial panel judges of the Supreme People's Court for re-trial: Liu Xiaofei, Ye Yang and Wu Kaimin (Written by: Ye Yang, Supreme People's Court; Translated by: Duan Jing).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_21

be determined that the matters are in accordance with the provisions of Article 4 of the *Interpretation* that "shall be related to its tenets and business scope".

Case Information

1. **Parties**

Applicant in the retrial (Plaintiff in the first instance and Appellant in the second instance): China Biodiversity Conservation and Green Development Foundation (hereinafter referred to as the "CBCGDF")

2. **Procedural History**

First instance: No. 6 [2015], Trial, Civ. Division, the Intermediate People's Courts of Zhongwei City, Ningxia Hui Autonomous Region (dated Aug. 11 of 2015)
Second instance: No. 6 [2015], Retrial, Civ. Division, the Higher People's Court of Ningxia Hui Autonomous Region (dated Nov. 6 of 2015)
Application for retrial: No. 3377 [2016], Application, Civ. Division, the Supreme People's Court (dated Jan. 22 of 2016)
Retrial: No. 47 [2016], Retrial, Civ. Division, the Supreme People's Court (dated Jan. 28 of 2016)

3. **Cause of Action**

Public interest litigation against environmental pollution

Essential Facts

On August 13, 2015, the China Biodiversity Conservation and Green Development Foundation (hereinafter referred to as the "CBCGDF") filed a lawsuit in the Zhongwei Intermediate People's Court of Ningxia Hui Autonomous Region and alleged that Ningxia Ruitai Technology Co., Ltd. (hereinafter referred to as Ruitai Company) directly discharged substandard waste water to the evaporation pond in the process of production, which caused severe pollution of the Tengger Desert. Up to the time of action, the rectification work had not been completed yet. The CBCGDF asked the Court to order that Ruitai Company should (1) stop illegal environmental pollution activities; (2) eliminate the danger that causes environmental pollution; (3) restore the ecological environment or establish a special fund for the environmental restoration of desert and entrust a qualified third party to carry out the restoration; (4) for the second and third claims, the court would organize a team of the plaintiff, technical experts, legal experts, NPC deputies and CPPCC members for the inspection and examination of the restoration work; (5) compensate for the loss resulting in the

ecological function before the environmental restoration; (6) make an apology to the public on national media; (7) bear the appraisal fees, travel expenses, lawyer's fees and other reasonable expenses incurred by the CBCGDF; and (8) bear the litigation fees.

On August 19, 2015, the Zhongwei Intermediate People's Court of Ningxia Hui Autonomous Regions rendered a civil ruling that the action instituted by the CBCGDF should not be handled by the court. The CBCGDF refused to accept the ruling of the first instance and appealed to the Higher People's Court of Ningxia Hui Autonomous Region. On November 6, 2015, the Higher People's Court of Ningxia Hui Autonomous Region rendered a civil ruling to dismiss the appeal. After this ruling went into force, the CBCGDF filed an application for retrial with the Supreme People's Court. On January 22, 2016, the Supreme People's Court rendered a civil ruling that this case should be brought to trial.

Issue(s)

Whether the CBCGDF can be identified as a social organization specifically engaged in public activities of environmental protection.

Holding

The Supreme People's Court held that whether the tenets and business scope of a social organization include protecting the environmental public interests should be judged on the basis of their actual content other than simple literal expression. The articles of association of the CBCGDF conformed to the green development concept and were closely related to environmental protection, and it was within the scope of safeguarding the environmental public interests. Therefore, it can be determined that the tenets and business scope of the CBCGDF include content of protecting the environmental public interests. Public activities of environmental protection include not only such activities of directly improving the ecological environment as afforestation, protection of endangered species, energy conservation and emission reduction, and environmental restoration, but also environmental protection-related publicity and education, research and training, academic exchange, legal aid, public interest litigation, and other activities that are conducive to improving the environmental governance system, enhancing the environmental control capacity, and promoting the whole society to form broad consensus on environmental protection. The evidence submitted by the CBCGDF was able to prove that it has been actually engaged in environmental protection activities for a long time, which conformed to the provisions of the *Environmental Protection Law* and the *Interpretation*. In accordance with the provisions of Article 4 of the *Interpretation*, the public environmental interests involved in the public interest litigation instituted by a social organization should

have certain relevance with its tenets and business scope. These provisions aim at promoting corresponding relationship or relevance between the matter of environmental public interest protection as filed by a social organization and its tenets and business scope, so as to ensure that the social organization has the corresponding capacity to action. Therefore, even though the lawsuit filed by the social organization does not have corresponding relationship with its tenets and business scope, if such matter has certain relevance with the environmental elements or ecological system under its protection, the subject qualification of the social organization should be confirmed according to the standard of relevance. This environmental public interest litigation was instituted due to the pollution of the Tengger Desert. The complex and fragile desert ecological system formed in the interaction between the biotic community of desert and its environment needed much more cherishment and good care of the mankind. The CBCGDF alleged that Ruitai Company has discharged substandard waste water to the evaporation pond, which has severely damaged the already fragile ecological system of the Tengger Desert. So the protection of environmental public interests involved was included in its tenets and business scope.

Comment on Rule

1. The requirement of subject qualifications for a social organization to file public interest lawsuit against environmental pollution in civil litigation

To ensure that the public can orderly participate in environmental governance, establish and remedy the public environmental rights and interests, and investigate the torts in accordance with law, Article 55 of the *Civil Procedure Law* of the People's Republic of China provides for a system of civil environmental public interest litigation and specifies that an agency or relevant organization as prescribed by law may institute an environmental public interest litigation. Since environmental public interests are inclusive and sharable, there is no specific or direct interested party legally. It is necessary to encourage, guide, and regulate a social organization to file environmental public interest litigation according to the law, so as to bring the functions of environmental public interest litigation into play. Article 58 of the *Environmental Protection Law* provides that, "for an act polluting the environment or causing ecological damage in violation of the public interests, a social organization that satisfies the following conditions may institute an action in a people's court: (1) It has been legally registered with the civil affairs agency of the people's government at or above the districted city level; (2) It has specially engaged in public activities of environmental protection for five consecutive years or more without any recorded violation of law. Where a social organization complying with the provisions of the preceding paragraph instituted an action in a people's court, the people's court shall admit the case to be filed in court according to the law." Article 4 of the *Interpretation* further specifies the standards for checking whether a social organization "specially engaged

in the public activities of environmental protection", namely, "If a social organization's tenets and main business scope as specified in its articles of association are to safeguard the public interests and the social organization engages in public activities of environmental protection, it can be determined as "specially engaged in public activities of environmental protection" as provided in Article 58 of the *Environmental Protection Law*. The public interests involved in the action instituted by the social organization should be related to its tenets and business scope." Therefore, whether a social organization meets the requirements of "specially engaged in public activities of environmental protection" should be examined mainly from three aspects, namely, whether its tenets and business scope include safeguarding the environmental public interests, whether it actually engages in public activities of environmental protection, and whether the environmental public interests it safeguards are of relevance to its tenets and business scope. Among them "the tenets and business scope include the protection of environmental public interests" is the formal requirement, "engaging in public activities of environmental protection" is the substantive requirement, and "the environmental public interests are of relevance to its tenets and business scope" is the relevance requirement. The ruling further clarifies the judgment criteria of the above three requirements.

2. **Understanding of "the tenets and business scope include maintaining the environmental public interests"**

The formal requirement for a social organization to initiate environmental civil public interests litigation is that its tenets and business scope should include engagement of the said organization in public activities of environmental protection and maintenance of environmental public interests. The ruling of this case pinpoints that the provisions of Article 4 of the *Interpretation*, which states that "the tenets and main business scope as specified in the articles of association of a social organization are to maintain the public interests", comprises not only maintaining the environmental public interests as specified in the articles of association, but also the work content of protecting the environmental elements and the ecological system.

To accurately determine whether a social organization is qualified as the subject of environmental public interests litigation, the key is to see whether this organization takes the protection of environmental public interests as its tenets and goal of carrying out relevant activities. The articles of association of social organizations are the basis for it to carry out activities. In accordance with the Regulation on the Administration of the Registration of Social Organizations *Regulation on the Administration of the Registration of Social Organizations*, the *Interim Regulations on Registration Administration of Private Non-enterprise Units* and the *Regulation on Foundation Administration*, the articles of association of three types of social organizations should include such matters as the name, tenets and business scope, and should be approved by the registration agency before it takes effect. Therefore, the articles of association are the basis to determine whether a social organization can be identified as a social organization "specially engaged in the public activities of environmental protection" as prescribed in Article 58 of *Environmental Protection Law*. From the perspective of practice, the tenets and business scope stipulated in the

articles of association of social organizations often cover broader. It is not conducive to giving full play to the system function of environmental public interests litigation, if the activities of social organizations are confined to those safeguarding the environmental public interests, which is too strict. Therefore, Article 4 of the *Interpretation of Environmental Civil Public Interest Litigation Case* has moderately eased up the demands for social organizations within the scope of judicial interpretation. In other words, it is not required that their sole tenets and business scope is to safeguard environmental public interests, as long as one or several of them are to do so.

The common interests enjoyed by the public to live and develop in a healthy, comfortable, and beautiful environment are diversified in forms. Therefore, whether the tenets and business scope of a social organization include safeguarding the environmental public interests should be judged on the basis of their actual content other than simple literal expression. If the articles of association of a social organization directly states "to safeguard the social public interests" or have similar expressions, it certainly meets this requirement. Where the articles of association of a social organization do not specify safeguarding the environmental public interests, but its work content includes the protection of environmental elements and the ecological system, it shall be determined that it conforms to the condition stated in the provisions of Article 4 of the *Interpretation*. The first instance ruling, was based on the literal meaning of whether the articles of association of CBCGDF explicitly specified matters as safeguarding environmental public interests, rather than on its work content to see whether it covers the protection of environmental public interests. It was an inflexible understanding of Article 4 of the *Interpretation*, which constituted an error in the application of the law.

The meaning of "the work content includes protection of environmental elements and the ecological system" concerns the understanding of environment. Environment refers to the total body of all natural elements and artificially transformed natural elements affecting human existence and development. It includes natural environment and artificial environment. Article 2 of the *Environmental Protection Law* specifically refers to the environmental elements as atmosphere, water, ocean, land, mineral resources, forests, grassland, wet land, wildlife, natural relics, cultural relics, natural reserves, scenic spots, and cities and villages. Therefore, if the tenets and business scope provided in the articles of association of the social organization contain one or more specific environmental elements, or if it doesn't protect those in the environmental elements specifically named above, but those "within the scope of protecting various natural elements impacting the survival and development of mankind and those subject to artificial modification", it may be determined that the tenets and business scope include maintaining the environmental public interests.

With respect to the relationship between biodiversity conservation and environmental protection, it was provided in the *Convention of the United Nations on Biological Diversity* signed by China in 1992 that biodiversity referred to ecological complexes consisting of lands, oceans, and other aquatic ecological systems, including diversity in one species, among different species, and in the whole ecological system. Article 30 of the *Environmental Protection Law* provides that "exploitation and utilization of natural resources shall be developed in a rational way that protects

biological diversity and safeguards ecological security, and the relevant ecological protection and restoration plans shall be developed and implemented according to the law. For the introduction of alien species and the research, development, and utilization of biotechnologies, measures shall be adopted to prevent any damage to biodiversity". It can be seen that the protection of biological diversity is an important content of environmental protection and also a major part of safeguarding the environmental public interests. In this case, as specified in the articles of association of the CBCGDF, its tenets were to "widely mobilize the whole society to show concern for and give support to the cause of biodiversity protection and green development, protect the national strategic materials, promote the building of ecological civilization and harmony between man and nature, and build a better home for humanity", which met the requirements of the *Convention on Biological Diversity* and the *Environmental Protection Law* for protecting the biological diversity. Therefore, it should be determined that the tenets and business scope of the CBCGDF include content of safeguarding the environmental public interests, which conforms with the condition stated in the provisions of Article 4 of the *Interpretation* that "the tenets and main business scope determined in the articles of association of a social organization are protecting social public interests".

3. **Understanding of "engage in public activities of environmental protection"**

Social organizations actually engaging in environmental protection public activities is the formal requirement for judging whether they are specially engaged in environmental protection public activities. The ruling determines that, "public activities of environmental protection" as prescribed in Article 4 of the *Interpretation* include not only activities of directly improving the ecological environment, but activities related to environmental protection that are conducive to improving the environmental governance system, enhancing the environmental governance capacity, and promoting the whole society to form extensive consensus on environmental protection.

In accordance with the provisions of Article 58 of the *Environmental Protection Law*, the social organizations which specially engage in the public activities of environmental protection can institute an action. It is understood that the purpose of this provision is to ensure that the social organizations that file civil environmental public interest litigation have certain professional skills and rich practical experience, so as to maintain environmental public interest through civil environmental public interest litigation. Therefore, Article 4 of the *Interpretation* not only requires that the tenets and main business scope of social organizations are to safeguard public interests, but also the social organizations to "engage in public activities of environmental protection". Given that environmental public interest litigation is still a new form of litigation, and considering that environmental protection activities, whether direct or indirect, are the reflection of social organizations' professional ability, the "public activities of environmental protection" prescribed by law and judicial interpretation should be broadly understood. Public activities of environmental protection not only include such activities of directly improving the ecological environment as afforestation, protection of endangered species, energy conservation and emission

reduction, and environmental restoration, but environmental protection-related publicity and education, research and training, academic exchange, legal aid, public interest litigation, and other activities that are conducive to improving the environmental governance system, enhancing the environmental governance capacity, and promoting the formation of extensive consensus on environmental protection in the whole society.

In this case, although such relevant evidentiary materials submitted by the CBCGDF in the trial of first instance, trial of second instance, and retrial as historical evolution, photographs of public activities, and notice on case-filing and acceptance of an environmental public interest litigation were not cross-examined, at the stage of case-filing and review, they were sufficient to show that since its establishment, the CBCGDF had been actually engaged in environmental protection activities including hosting environmental protection seminars, organizing ecological investigations, launching environmental protection publicity and education, and instituting civil environmental public interest litigations for a long time, and it conformed to the provisions of the *Interpretation*.

4. Understanding of "the environmental public interests involved shall be related to its tenets and business scope"

In order to encourage social organizations to make better use of their experience and professional skills to promote the orderly and effective environmental civil public interest litigation, Article 4(2) of the *Interpretation* provides that "the public interests involved in the action instituted by a social organization shall be related to its tenets and business scope". This is the judging requirement of whether a social organization has the subject qualification for filing environmental civil public interest litigation. The ruling of this case specifies that the judging requirements include not only the corresponding relevance between the matters instituted by a social organizations and its tenets and business scope, but also the certain connection between the matters and the environmental elements and ecological systems protected by the social organization.

As for the relevance requirement in judicial practice, it is believed that only a certain degree of connection is required. The reason is that the relevance is required mainly to ensure that the plaintiff has sufficient professional competence. It is fair to say that social organizations undoubtedly have strong professional competence in their specialized field of environmental protection. However, if the specialized field is taken as a benchmark and is compared with the field involved in the case, the more distant the two are, the less relevance and the weaker the professionalism of the social organization in the field involved in the case. If there is little or no relevance, it can be presumed that the social organization does not have the professional competence in the particular field involved in the case. Thus the social organization does not have the subject qualification. However, it's just an idealized deduction. Practically speaking, the current social organizations in China do not have such ideal division in their work of professional fields. In some fields, there are no social organizations specially engaged in relevant protection activities, and the so-called professional ability is only professional to the general public rather than professional science

and technology in the strict sense. Therefore, if the relevance requirements are too strict, it may lead to the absence of proper litigation subjects, which is not conducive to the development of public interest litigation. In addition, in practice, even if the articles of association do not have relevance, social organizations can change their articles of association to achieve the relevance with the case. Therefore, at this stage, relevance shall include a lower degree of relevance. For example, when migrating, migratory birds need to rest, feed and reproduce in the forests, rivers, lakes, wetlands and even towns inhabited by human beings. In this process, they also need sufficient food sources such as fish, insects, plant fruits and so on. These elements should all be considered as relevant with the protection of migratory birds. When a social organization, with its tenets and business scope of wetland protection, institutes an environmental civil public interests litigation to protect migratory bird, the People's Court should determine that these two are relevant.

This environmental public interest litigation was instituted due to the pollution of the Tengger Desert. The complex and fragile desert ecological system formed in the interaction between the biotic community of desert and its environment needed much more cherishment and good care of the mankind. The CBCGDF alleged that Ruitai Company discharged substandard waste water to the evaporation pond, which severely damaged the already fragile ecological system of the Tengger Desert. The environmental public interests in this case are the interaction between the biotic community of the desert and its environment, which is closely relevant with such content as "promote the building of ecological civilization", "harmony between man and nature", and "build a better home for humanity" in CBCGDF's tenets and business scope, conforming to the relevance requirement in the *Interpretation*.

5. Conclusion

The legal and judicial interpretation of relevant provisions in the environmental civil public interest litigation subject identification system is the process of transforming the abstract characteristics of the eligible subject being in the nature of public welfare and professionalism into specific rules. In the process of transformation, on the one hand, due to the limitations of text expression, it is inevitable to have omissions or vague areas. Thus the decision maker needs to hold the legislation goal accurately to carry on the judgment. On the other hand, the process of transformation is inevitably affected by the social development. For example, the normative requirements of laws and regulations on social organizations and the development status of social organizations in China are factors that must be taken into consideration when making rules. Under the circumstance that the enhancement of ecological civilization has become a national strategy with the cause of environmental protection developing rapidly in China, the legal and judicial interpretations should be properly interpreted in combination with the social development and the protection needs of environmental public interests, so as to maximize the function of the environmental civil public interest litigation system.

Environmental Protection Association of Taizhou City, Jiangsu Province v. Taixing Jinhui Chemical Engineering Co., Ltd. (The Public Interest Litigation for Compensation for Environmental Pollution Tort)—Judgement of Environmental Pollution Tort Regarding Environmental Medium with Self-Purification Capability

Huihui Liu

Rule

In cases of environmental pollution, manufacturers of hazardous chemicals and chemical products should perform stricter duties of care for their main products and by-products. They should comprehensively understand whether the main products and the by-products generated in the production of main products are highly hazardous and whether they would cause environmental pollution. The manufacturing, sale, transportation, storage, and disposal of their main products should comply with the relevant legal provisions; and the manufacturing, sale, transportation, storage, and disposal of their by-products should comply with the relevant legal provisions as well, avoiding damage to the ecological environment or bringing about major risks of damage to the ecological environment. Although rivers have a certain degree of self-purification capability, the environmental capacity is limited. The dumping of by-product acids into rivers will definitely cause serious damage to the water quality, aquatic animals and plants as well as the eco-environment of the beds, banks and lower reaches of the rivers. In addition, if the damage cannot be repaired in a timely

Collegial panel judges of the Supreme People's Court for re-trial: Lin Wenxue, Wei Wenchao, Liu Xiaofei, Wang Zhanfei, Wu Kaimin (Written by: Liu Huihui, Supreme People's Court; Translated by: Duan Jing).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_22

manner, the accumulation of the pollution will definitely exceed the load-bearing capacity of the environment, eventually causing the irreversible environmental damage. Hence, polluters shall not be exempt from the liability of repairing the environment on the ground that the water quality of part of the water bodies has been restored.

Case Information

1. **Parties**

Applicant in the retrial (Defendant in the first instance and Appellant in the second instance): Taixing Jinhui Chemical Engineering Co., Ltd. (hereinafter referred to as "Jinhui Company")
Respondent in the retrial (Plaintiff in the first instance, Appellee in the second instance): Environmental Protection Association of Taizhou City

2. **Procedural History**

First instance: No. 00001 [2014], Trial, Civ. Division, the Intermediate People's Courts of Taizhou City, Jiangsu (dated Sep. 10 of 2014)
Second instance: No. 00001 [2014], Retrial, Civ. Division, the Higher People's Court of Zhejiang Province (dated Dec. 29 of 2014)
Retrial: No. 1366 [2016], Retrial, Civ. Division, the Supreme People's Court (dated Feb. 1 of 2016)

3. **Cause of Action**

Disputes over compensation for environmental pollution tort

Essential Facts

In 2014, the Plaintiff, Taizhou City Environmental Protection Association, filed a lawsuit in the Intermediate People's Court of Taizhou City of Jiangsu Province, and alleged that from January 2012 to February 2013, defendant Jiangsu Changlong Agrochemical Co., Ltd. (hereinafter referred to as Changlong Company), Jinhui Company, Jiangsu Shimeikang Pharmaceutical Co., Ltd. (hereinafter referred to as Shimeikang Company), Taixing Shenlong Chemical Engineering Co., Ltd., Taixing Fu'an Chemical Engineering Co., Ltd., and Taixing Zhenqing Chemical Engineering Co., Ltd., (the six altogether are hereinafter referred to as "the six defendant enterprises"), delivered a total of over 25,000 tons of hazardous waste hydrochloric acid and waste sulfuric acid generated in the process of production to Taizhou Jiangzhong Chemical Engineering Co., Ltd. (hereinafter referred to as "Jiangzhong Company")

and other relevant companies without the qualification of treating hazardous wastes at a price ranging from RMB 20 to 100 per ton. The hazardous wastes were secretly discharged into two waterways of Rutai Canal of Taixing City and Gumagan River of Gaogang District, Taizhou City, causing serious water pollution. Taizhou City Environmental Protection Association requested the court to order that the six defendant enterprises should pay the environmental restoration fee of over RMB 160 million and the appraisal and evaluation fee of RMB 100,000.

The court of first instance, held that: Taizhou City Environmental Protection Association, as a legally-established non-profit social organization engaging in the cause of environmental protection, had the right to institute the environmental public interest litigation. The six defendant enterprises delivered the by-product acids to companies without treatment qualification and capabilities at a price much lower than the expense required by the legal treatment of such by-product acids, thus dumping a great volume of untreated by-product acids into rivers and causing serious environmental pollution. Therefore, they should compensate for losses caused thereby and restore the ecological environment. The dumping of over 20,000 tons of by-product acids into rivers would inevitably cause serious environmental pollution. As the rivers flew, even though the water quality at the location of dumping took a turn for the better, it did not mean that the ecological environment of the rivers had been fully restored and it still needed restoration. Under the circumstance that it was difficult to calculate the restoration costs, the ecological environment restoration costs should be calculated by adopting the virtual treatment costs method. Therefore, the court rendered a judgment that the six defendant enterprises should pay the environmental restoration costs totaling over RMB 160 million and bear the appraisal and evaluation fee of RMB 100,000 as well as the litigation costs.

The court of second instance held that Taizhou City Environmental Protection Association had the qualification for legally instituting environmental public interest litigation as plaintiff and the trial procedure in the first instance was legal. There was causal relationship between the disposal of by-product acids by the six defendant enterprises and the environmental pollution of Gumagan River and Rutai Canal. In the judgment of first instance, the amount of compensation determined was correct and the method for calculating the restoration costs was appropriate. The six defendant enterprises should legally assume the tort liabilities for the environmental pollution caused thereby. The judgment of second instance affirmed the lower court's ruling in terms of payment of the environmental restoration costs of over RMB 160 million and adjusted the ways to perform the obligations. If the six defendant enterprises could recycle by-product acids through technical renovation, significantly decrease environmental risks, and would not be punished due to illegal activities detrimental to the environment within one year, the technical reform costs already paid could be deducted up to 40% thereof after acceptance check. Three defendant enterprises have actively performed the entire judgment of second instance.

Jinhui Company, Changlong Company and Shimeikang Company refused to accept the judgment of second instance and filed an application for retrial with the Supreme People's Court one after another. But Shimeikang Company and Changlong Company then withdrew their applications for retrial upon the approval of Supreme

People's Court since they had completed their technical reform and passed the examination of their environmental protection projects which were put into operation, thus solving their environmental problems fundamentally.

Issues

1. Whether the six defendant enterprises have disposed of the by-product acids?
2. Whether ecological restoration is needed after the disposal of by-product acids?
3. Whether the cost of ecological restoration is properly calculated?

Holding

The Supreme People's Court held that in cases of environmental pollution, manufacturers of hazardous chemicals and chemical products should perform stricter duties of care for their main products and by-products. They should comprehensively understand whether the main products and the by-products generated in the production of main products were highly hazardous and whether they would cause environmental pollution. The manufacturing, sale, transportation, storage, and disposal of their main products should comply with the relevant legal provisions and the manufacturing, sale, transportation, storage, and disposal of their by-products should comply with the relevant legal provisions as well, avoiding damage to the ecological environment or major risks of damage to the ecological environment. Although water flows with a certain degree of self-purification capability, the capacity of the environment is limited. The dumping of by-product acids into rivers will definitely cause serious damage to the water quality, aquatic animals and plants as well as the eco-environment of the beds, banks and lower reaches of the rivers. In addition, if the damage cannot be repaired in a timely manner, the accumulation of the pollution will definitely exceed the load-bearing capacity of the environment, eventually causing the irreversible environmental damage. Hence, polluters shall not be exempt from the liability of repairing the environment on the ground that the water quality of part of the water area has been restored. The Supreme People's Court also affirmed the court of second instance's innovation in performance methods, which was the result of making full use of judicial wisdom and judicial means, properly balancing the interests of all parties, and upholding the concept of prioritizing protection and emphasizing restoration in accordance with the requirements of the *Environmental Protection Law*. The Supreme People's Court finally dismissed Jinhui Company's application for retrial.

Comment on Rule

1. **Determination of causal relationship regarding water pollution**

According to the provisions of Articles 65, 66 of the *Tort Law* of the People's Republic of China, the tort of environmental pollution applies the principle of non-fault liability, where any damage is caused by environmental pollution or ecosystem disruption, the tortfeasor, faulty or not, shall assume the tort liability. The reverse onus or the shifting of the burden of proof does not mean that the plaintiff in environmental civil litigation does not need to bear any burden of proof, but does not bear the burden of proof for the causal relationship between the behaviour and the damage. The burden of proof of the plaintiff is completed after closing the burden of proof of the existence of both damage and the pollution behaviors on the part of the defendant. After that, the burden of proof is on the defendant, which means the defendant must prove that there is no causal relationship between the pollution-emission activities and the damage, otherwise the defendant will assume the tort liabilities.

2. **Determination of the responsibility for the ecological environment restoration**

Although rivers have a certain degree of self-purification capability, the capacity of the environment is limited. The water pollution will definitely cause serious damage to the water quality, aquatic animals and plants as well as the eco-environment of the beds, banks and lower reaches of the rivers. If the damage cannot be repaired in a timely manner, the accumulation of the pollution will definitely exceed the load-bearing capacity of the environment, eventually causing the irreversible environmental damage. Hence, polluters shall not be exempt from the liability of repairing the environment on the ground that the water quality has been restored.

In this case, an expert assistant was brought in to give expert opinions on how to calculate the repair cost of water pollution damage, and he also appeared in court for questioning by both parties. In foreign countries, putting the assisting expert on the stand is called the expert witness system, which is one of the most important systems in Anglo-American law. It is one of the most advantageous weapons for both sides of the prosecution and defence under the mode of adversary system. Expert witness is a witness with better professional skills and knowledge than ordinary people in a particular field. Article 61 of *Some Provisions of the Supreme People's Court on Evidence in Civil Procedures* provides that "The parties concerned may apply to the People's court to have one or two persons with professional knowledge to appear in court to make accounts of the specialized questions relating to the case. If the People's Court approves such applications, the relevant expenses shall be borne by the party that makes the application. The judges and parties concerned may interrogate the persons with professional knowledge that appear in court. Upon the approval of the People' court, the persons with professional knowledge as applied for by each party concerned may cross-examine the issues concerned in the case. The persons with professional knowledge may inquire of the authenticators". This is the first time

that China has established the expert witness system in civil litigation in normative documents. Lv Xiwu, Professor of the Southeast University School of Energy and Environment, expresses his opinions in the trial as an assisting expert that the dumping of hazardous wastes into water directly results in the damage of regional eco-environmental functions and natural resources. Both the cost of repairing the damage to the ecological environment and resources of the Yangtze River and the cost of manual intervention to reduce the risk of pollution to an acceptable level will far exceed the cost of direct treatment of pollutants. As the rivers flows with the capabilities of self-purification, even though the water quality at the location of dumping could be re-purified, the damage to the ecological environment of the rivers cannot be denied. The court of first instance adopted the expert's opinion and held that: it is explained from the professional perspective of assisting expert Lv Xiwu that the dumping of by-product acids into rivers will definitely cause serious damage to the water quality, aquatic animals and plants as well as the eco-environment of the beds, and the repair cost will far exceed the normal treatment cost.[1] The water environment is fluid, and pollution occurs instantaneously, so the damage site cannot be recovered. The ecological environment restoration costs should be calculated by adopting the virtual treatment costs method, according to the *Recommended Method for Calculating the Amount of Damage of Environmental Pollution* (hereinafter referred to as "the *Recommended Method*") (the First Version) under the circumstance that it was difficult to calculate the restoration costs. There is no essential difference concerning the regulations of the virtual treatment costs method between the First Version and the Second Version of the *Recommended Method*. Therefore, it was not inappropriate for the court of second instance to determine by the assessment report that the restoration costs should be the treatment cost of by-product acids and the amount of dumping multiplied by 4.5, the lower limit of the recommended multiples of the environmental function sensitivity of type III surface water (ranging from 4.5–6 times). At present, relevant cases including environmental pollution are indeed highly professional that need the support of expert opinions. However, not all cases are necessarily identified by authentication institutions. If experts appear in court to express their opinions, based on which the cases can be solved, both the litigation costs and time could be saved. This requires that we first change our mindset of over-reliance on authentication. In essence, the authentication is also part of the evidence to increase the judge's conviction. If there is no authentication, the judge can also obtain the conviction through the expert opinion, and directly make the judgment.

[1] Civil Judgment of Jiangsu Higher People's Court (No. 00001 [2014], Retrial, Civ. Division).

Chongqing Branch of China Orient Asset Management Co., Ltd. v. Lerentang Investment Group Co., Ltd. and Beijing Zhongkun-Jinxiu Real Estate Development Co., Ltd. etc. (Dispute over the Enforcement Applicant's Objection to Enforcement)—Conflict Between Priority of Compensation with Mortgaged Property and Expectant Right of Real Right

Nian Huang

Rule

The sale of mortgaged houses is one of the typical forms of lawsuit regarding objection to enforcement. Articles 28 of the *Enforcement Objection and Reconsideration* specify four requirements to be met if the buyer would raise objection regarding the real property registered under the name of the party against whom enforcement is sought to exclude enforcement of monetary claim. Whether the above requirements are met in the specific case is the focus of the review. Meanwhile, the mortgagee's prevention and risk control of the mortgagor's loss of trust, the transferee's duty of care for the right guarantee of him/herself and the mortgagee when making the contract should also be considered during the trial.

Collegial panel judges of the Supreme People's Court for the second instance: Huang Nian, Pan Yongfeng, Guo Zaiyu (Written by: Huang Nian, Supreme People's Court; Translated by: Duan Jing).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_23

Case Information

1. Parties

Enforcement applicant (The defendant in the First Instance, the appellant in the Second Instance): Chongqing Branch of China Orient Asset Management Co., Ltd. (hereinafter referred to as "Chongqing Branch of Orient Asset Company")
The party not involved in the enforcement proceeding (Defendant in the first instance, Appellee in the second instance): Lerentang Investment Group Co., Ltd. (hereinafter referred to as "Lerentang Investment Company")
Enforcement respondent (Defendant in the first instance, Appellee in the second instance): Beijing Zhongkun-Jinxiu Real Estate Development Co.,Ltd. (hereinafter referred to as "Zhongkun-Jinxiu Company")
Enforcement respondent (Defendant in the first instance, Appellee in the second instance): Beijing Zhongkun Investment Group Co., Ltd. (hereinafter referred to as "Zhongkun Investment Company")
Enforcement respondent (Defendant in the first instance, Appellee in the second instance): Beijing Zhongkun-Changye Real Estate Development Co., Ltd. (hereinafter referred to as "Zhongkun Changye Company")
Enforcement respondent (Defendant in the first instance, Appellee in the second instance): Huang X

2. Procedural History

First Instance: No. 123 [2017], Trial, Civ. Division, Chongqing Higher People's Court (dated Sep. 26 of 2017)
Second Instance: No. 215 [2018], Final, Civ. Division, the Supreme People's Court (dated May 25 of 2018)

3. Cause of Action

Lawsuit of enforcement applicant's objection to enforcement

Essential Facts

On April 20, 2015, the Higher People's Court of Chongqing rendered a civil judgment (No. 55 [2014], Civil, First Instance, Chongqing) that Chongqing Branch of Orient Asset Company was entitled to priority of compensation in receiving repayment of the debt of RMB 200 million and the interest thereof with the mortgaged real estate and land as numbered in the *Certificate of the Mortgagee's Rights to the Mortgaged House Property* (No. 170289, No. 170288, No. 170290 and No. 158973) and the *Certificate of the Mortgagee's Rights to the Mortgaged Land* (No. 00062 and No. 00063, 2012). After the judgement came into force, Chongqing Branch of Orient Asset Company filed an application for enforcement, which was accepted and enforced on March 11,

2016. In the enforcement proceeding, the HPC of Chongqing Municipality issued an enforcement ruling (No. 15-1 [2016] resumption of enforcement, Chongqing) on August 22, 2016 to continue to seize the relevant properties registered under the name of Zhongkun-Jingxiu Company including the houses and parking stalls involved in the case. After hearing the news, Lerentang Investment Company filed a written objection with the HPC of Chongqing on the ground that it was the actual owner of the houses and parking stalls involved in the case, requesting the removal of seizure measure. On June 28, 2017, the HPC of Chongqing rendered a ruling of enforcement (No. 18 [2017], objection to enforcement, Chongqing) to suspend the enforcement of the houses and parking stalls involved in the case. The property involved in the case has been registered under the name of Zhongkun-Jinxiu Company and have been mortgaged for the loan from Chongqing Branch of Orient Asset Company.

Chongqing Branch of Orient Asset Company filed a lawsuit with the court and requested the court to (1) revoke the ruling of enforcement (No. 18 [2017], objection to enforcement, Chongqing); (2) continue the enforcement of the houses and parking stalls involved. Zhongkun-Jinxiu Company, Zhongkun Investment Company, Zhongkun-Changye Company and Huang X did not submit their replies.

The court of first instance rendered a judgment on September 26, 2017, dismissing all the claims of Chongqing Branch of Orient Asset Company.

Chongqing Branch of Orient Asset Company refused to accept the judgment, and filed an appeal to the Supreme People's Court.

Issue(s)

Whether Lerentang Investment Company is entitled to raise objection regarding the real property registered under the name of the party against whom enforcement is sought, so as to exclude the enforcement of the houses and parking stalls involved in the case.

Holding

In the retrial, the Supreme People's Court held that first, a legal and effective written purchase contract of the houses and parking stalls involved had already been signed between Lerentang Investment Company and Zhongkun-Jinxiu Company and the online signing procedures also completed before the court seized the property. Based on the *Certificate of the Mortgagee Approving the Sale of the Mortgaged House*, Lerentang Investment Company had no fault in buying the houses and parking stalls involved. Second, the evidence provided by Lerentang Investment Company including the supporting document of property management company receipts of property management fees, utility fees, and heating sufficed to prove that it had actually possessed and used the real property involved before the court seized it. Third, the

Payment Details clarified that most of the payments by Sinopharm Group Lerentang Medicines Co., Ltd. were made on behalf of its shareholder Lerentang Investment Company, and it was not unusual to have some of the money paid one day before the date of contract signing for the sale of the real property. Such evidence as purchase invoices and bank slips sufficed to prove that Lerentang Investment Company paid the full price as agreed. Fourth, Lerentang Investment Company, based on the *Certificate of the Mortgagee Approving the Sale of the Mortgaged House*, had reasonable confidence in the transfer without knowing the regulatory agreement and the specific account. Therefore, it had fulfilled the corresponding duty of care, and not processing transfer registration was not due to its fault. The judgment of first instance was clear in fact-finding and correct in application of law and it should be affirmed. The Supreme People's Court finally ruled to dismiss all the claims of Chongqing Branch of Orient Asset Company for retrial.

Comment on Rule

As regards the controversy in this case, the following questions should be considered: whether Lerentang Investment Company and Zhongkun-Jinxiu Company had signed a legal and valid written sales contract before the seizure; whether the houses and parking stalls involved in the case had been legally possessed before the seizure; whether the price involved in the case was paid in full and whether it was reasonable to make some of the payments one day before the date of contract signing; how to determine that not processing the transfer registration was not due to the buyer's own reasons.

The sale of mortgaged houses is one of the typical forms of lawsuit regarding objection to enforcement. In the development of real estate, due to insufficient development and construction funds, it is necessary to raise funds by mortgaging the land used for construction and the project under construction. When the project meets the requirement for sale, the sales income would be used to pay back the funds raised by mortgaging, and this requires the mortgagee to modify the realization form of the right of guarantee accordingly. If all parties conduct transactions in strict accordance with the provisions of Article 191 of the *Property Law*, it is a trading activity that is beneficial to all parties. However, if the developer is not honest and conduct false sales or sales in a low price, or transfer sales income secretly, it will lead to failure in the realization of the rights of the mortgagee, thus causing conflicts of rights between the mortgagee and the buyer. In order to resolve such contradictions and disputes, the Supreme People's Court has issued relevant judicial interpretations. Article 27 of the *Provisions of Enforcement Objection and Reconsideration* provides that "where the enforcement applicant enjoys the priority of compensation including collateral rights over the subject matter of enforcement to confront the party not involved in the enforcement proceeding, the people's court shall not support the latter's objection to enforcement, except as otherwise prescribed by law or judicial interpretations". Generally speaking, the objection to enforcement of the subject matter proposed by

the party not involved in the enforcement proceeding is not supported because the enforcement applicant enjoys the priority of compensation including the real right granted by guarantee. However, Articles 28 and 29 of the relevant *Judicial Interpretation* have specified exceptions. Article 28 provides: "in the enforcement of a monetary claim, when the buyer raises objection regarding the real property registered under the name of the party against whom enforcement is sought, the people's court should support the buyer and exclude the enforcement if it is within the court's power in the following circumstances: (1) A legal and valid written sales contract has already been signed before the people's court seizes the property; (2) The real property has been lawfully possessed before the people's court seizes the property; (3) The purchase price has been paid in full, or the purchase price has been partially paid as agreed upon in the contract and the residual price would be paid for enforcement as required by the people's court; (4) Not processing transfer registration of the real property is not due to the buyer's personal reasons. The buyer's expectant right of real right that meets the above four requirements stipulated in this article may exclude the enforcement applied by the enforcement applicant who enjoys the priority of compensation. Whether the rights of Lerentang Investment Company can exclude the enforcement of the Chongqing Branch of Orient Asset Company regarding the real property involved in the case needs to be investigated from these four aspects.

1. **Whether a legal and valid written sales contract has been signed before the seizure**

The sales contract of real estate is generally written. The main controversy of its validity and legality is that whether it is a preliminary agreement or whether it is a forgery, etc. Once the facts are found out, the judgment can be made according to the standardized examination procedures of the substantive law. Normally, the controversy point of this issue in judicial practice is whether the time of contract signing is before the court's seizure of the real property. In this regard, the transferee should first bear the burden of proof to prove that the legal and valid written sales contract is signed before the seizure. If the enforcement applicant disagrees with the transferee's evidence, he should bear the burden of reverse proof such as applying for judicial expertise to determine whether it is a backdating contract, etc., except for the situation where the real estate sales contract has been filed in the housing administration bureau. In this case, the court of first instance seized the houses and parking stalls involved on October 29, 2014. Lerentang Investment Company signed the *Sales Contract of Commercial Residential Houses in Beijing* regarding the real property involved with Zhongkun-Jinxiu Company and completed the online signing procedures on March 19, 2013. The sales contract in this case shall be lawfully valid for it is a genuine manifestation of both parties' intent without violating the mandatory provisions of the law and administrative regulations. Although the real estate project completed mortgage registration before the sale, Lerentang Investment Company had no fault in purchasing the houses and parking stalls since the Chongqing Branch of Orient Asset Company provided the *Certificate of the Mortgagee Approving the Sale of the Mortgaged House*, which was also attached as the appendix to the

sales contract by Zhongkun-Jinxiu Company, to the Urban and Rural Construction Committee of Haidian District and the Housing Administration Bureau of Haidian District on November 5, 2012. The Chongqing Branch of Orient Asset Company appealed without submitting corresponding evidence that the transactions of the real property were untrue, thus the grounds for appeal could not be established.

2. **Whether it has been legally possessed before the seizure**

Lawful possession is a factual state of being in actual control of the real state with a legal basis. Investigating whether the possession occurs before the people's court's seizure is the backtracking of the past factual state. There is often much controversy in the lawsuits because of suspicious malicious collusion in the transfer procedures of the houses between the enforcement respondent and the transferee or in the supporting evidence provided by the property management company, which requires relatively objective third-party evidence such as receipts of property management fees, utility fees and heating fees, etc. In this case, the evidence including the supporting materials of the property management company, receipts of property management fees, utility fees and heating fees provided by Lerentang Investment Company sufficed to prove that it had been in actual possession of the houses and parking stalls since March 2013 and July 2014. The Chongqing Branch of Orient Asset Company did not submit rebuttal evidence to negate the aforementioned evidence, so the grounds for the appeal were untenable and could not be established.

3. **Payment**

Whether the payment has been paid in full is the core issue of whether the transferee can enjoy the expectant right of real right that is sufficient enough to exclude enforcement. If the transferee makes the payment to the account under the name of the enforcement respondent through bank transfer, then there would be no dispute over the facts of the payment. The issue lies in whether the money paid is for purchasing the real estate in the sales contract and the enforcement applicant shall bear the burden of proof if he/she has objection to it. If the transferee pays the money to the account under the name of a third party by bank transfer, the transferee should submit evidence that the payment is made for the purchase of the real estate in the sales contract involved in the case. Since it concerns the substantive rights of the third party, it is often necessary for the third party to participate in the litigation proceeding to testify the relevant facts by appearing in court or other ways. If the transferee only has the receipt and claims payment by cash, he/she shall provide sufficient evidence of his/her economic capability, changes in his/her property, the time and place of the purchase, and the information of the payment recipient etc., so that the people's court can make a judgement on a comprehensive basis. In this case, although most of the money was paid by the Sinopharm Group Le-Ren-Tang Medicines Co., Ltd.to Zhongkun-Jinxiu Company by bank transfer, the former provided the *Payment Details* on March 20, 2013, stating clearly that the above payment was made to purchase the real property on behalf of its shareholder, Lerentang Investment Company; It was not unusual to have some of the money paid one day before

the date of contract signing for the sale of the houses and parking stalls. Evidence such as purchase invoices and bank slips provided by Lerentang Investment Company sufficed to prove that it had paid the full price of the real property involved as agreed to Zhongkun-Jinxiu Company. Chongqing Branch of Orient Asset Company did not submit the rebuttal evidence to negate the aforementioned evidence, and its claims of Lerentang's evidence being insufficient to prove the full payment of the real property were untenable and thus could not be established.

4. **Reasons for not processing transfer registration of the real property**

Article 191 of the *Property Law* provides that "Where a mortgagor transfers the mortgaged property during the mortgage term with the consent of the mortgagee, the money generated from the transfer shall be used for the early repayment of debts to the mortgagee or be submitted to a competent authority for safekeeping. A mortgagor may not transfer the mortgaged property during the mortgage term without the mortgagee's consent, unless the transferee settles the debts on behalf of the mortgagor thus terminating the mortgage right". Since the mortgage registration has the validity of publicity and credibility, there are two criteria to determine that not processing transfer registration of the real property under mortgage registration is not out of the buyer's personal reasons: the mortgagee's consent to the mortgagor's transferring of the mortgaged property, or the transferee settling the debts on behalf of the mortgagor thus terminating the mortgage right. Without the mortgagee's consent, he/she is not obliged to cancel the mortgage registration unless the transferee settles the debts on behalf of the mortgagor thus terminating the mortgage right. If the mortgagee consents to transfer the mortgaged property, it is the mortgagor, not the buyer, that is the subject of duty to repay the debts to the mortgagee in advance using the money generated from the transfer or submit it to a competent authority for safekeeping. Where the mortgagor does not use the money generated from the transfer for the early repayment of debts to the mortgagee or submit it to a competent authority for safekeeping, he/she shall still undertake corresponding guarantee liabilities. The mortgagee has the responsibility to cancel the mortgage registration of the real property unless the mortgagee has an agreement with the buyer or the mortgagee has a relevant statement known to the buyer. In this case, the mortgagee Chongqing Branch of Orient Asset Company provided the *Certificate of the Mortgagee Approving the Sale of the Mortgaged House* to the Housing Administration Bureau and the mortgagor Zhongkun-Jinxiu Company also attached the *Certificate* to the sales contract. Lerentang Investment Company had reasonable confidence in the transfer of the houses and parking stalls involved. Although the Chongqing Branch of Orient Asset Company and Zhongkun-Jinxiu Company signed a *Regulatory Agreement* to supervise the sales refund, it was unknown to Lerentang Investment Company, the buyer of the property involved. Moreover, the regulatory account was not agreed as the payment account in the contract between Lerentang Investment Company and Zhongkun-Jinxiu Company. Zhongkun-Jinxiu Company did not pay off its debts to Chongqing Branch of Orient Asset Company with the money incurred from the transfer in advance or submit it to a competent authority for safekeeping, which was a violation of the contract and a serious breach of

faith. Meanwhile, this was also the contract risk that Chongqing Branch of Orient Asset Company should assume. Lerentang Investment Company had no fault in it. Therefore, as a transferee, Lerentang Investment Company had already fulfilled its corresponding duty of care in the process of purchasing the houses and parking stalls involved in the case, and it was not due to its fault that the transfer registration was not processed. The Supreme People's Court did not support all the claims of Chongqing Branch of Orient Asset Company for retrial.

This case aims to remind that the mortgagee and the transferee in the transaction of mortgaged real property should pay full attention to the mortgagor's breach of faith. The mortgagee should be careful about the things like the payment method or the regulatory account, which should be notified of to the transferee by such ways as specifying relevant information in the certificate of approving the sale, so as to avoid the loss of the money generated from the transfer of the mortgaged real property. Meanwhile, the transferee should also pay attention to the way of guaranteeing the rights of the mortgagee when signing the contract, and readily provide relevant evidence of contract signing, possession and use, and payment in order to ensure the legal protection of the expectant right of the real right.

Dalian Deyun Real Estate Development Co., Ltd. v. Dalian Yachen Real Estate Development Co., Ltd. and Dalian Shengxin Construction Group Co., Ltd. (Lawsuits of Revocation by a Third Party)—The Application Conditions for Lawsuits of Revocation by a Third Party

Dian Luo and Chengpeng Xing

Rule

In order to realize the monetary claims, the enforcement applicant files a third-party revocation action regarding the judgement of a dispute over the construction project contract in a separate case involving the subject matter of the enforcement. Whether the enforcement applicant meets the prescribed conditions for prosecution should be examined comprehensively in terms of the subject qualification, substantive conditions and the possibility of sham litigation. As regards subject qualification, the enforcement applicant of monetary claims is neither the developer nor the contractor of the project involved in the case and thus does not have the independent substantive right to the subject matter of the lawsuit. Therefore, he is not a third party with the independent right to claim the subject matter. Objectively, the enforcement applicant's monetary claims may be affected because the contractor enjoys priority in receiving the payment of the construction project, but the pure fact-based and economic influence does not affect his legal interests so he is not a third party without the independent right to claim the subject matter. Under the circumstance that the monetary claims have entered the stage of enforcement auction, the creditor has the right to apply for enforcement, but it cannot be determined based on this that he has

Collegial panel judges of the Supreme People's Court for the second instance: Miao Youshui, Luo Dian, Pang Jie (Written by: Luo Dian and Xing Chengpeng, Supreme People's Court; Translated by: Duan Jing).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_24

the exclusive creditor's right or real right to the subject matter of enforcement. If the enforcement applicant of monetary claims cannot prove that the developer and the contractor have conducted things like malicious collusion and sham litigation, which injure the interests of creditors, then the creditor's rights that have entered the enforcement proceeding shall not challenge the compensation priority of the contractor in receiving the payment of the construction project.

Case Information

1. **Parties**

Appellant in second instance (Plaintiff in the first instance,): Dalian Deyun Real Estate Development Co., Ltd. (hereinafter referred to as "Deyun Company")
Appellee in second instance (Defendant in the first instance): Dalian Yachen Real Estate Development Co., Ltd. (hereinafter referred to as the "Yachen Company")
Appellee in second instance (Defendant in the first instance): Dalian Shengxin Construction Group Co., Ltd. (hereinafter referred to as the "Shengxin Company")

2. **Procedural History**

First Instance: No. 5 [2017], Trial, Civ. Division, the Higher People's Court of Liaoning Province (dated Oct. 30 of 2017)

Second Instance: No. 235 [2018], Final, Civ. Division, the Supreme People's Court (dated Apr. 28 of 2018)

3. **Cause of Action**

Lawsuits of Revocation by a third-party

Essential Facts

In the lawsuit filed by Deyun Company, it was stated that there were true loan relationships between Yachen Company and Tang X, then Tang X won the case by judgement of the court and applied for enforcement. Later Deyun Company acquired the creditor's right of RMB 10 million from Tang X through transfer and became the enforcement applicant upon the ruling by the court. After Deyun Company applied for the enforcement of Yachen Company's land and buildings in seizure and completed the auction procedures, Shengxin Company brought an action in court, requesting Yachen Company to pay the price of the construction fees first and claiming priority in receiving the payment of the construction project. The date of filing the case was June 27, 2016. Before the judgement was announced, Deyun Company voluntarily

applied for participating in the litigation as a third party. Intermediate People's Court of Dalian City listened to Deyun Company's opinions but did not accept it as the third party. In the judgment of first instance, the court ordered the termination of the contract and Yachen Company should pay the construction project price of RMB 30 million to Shengxin Company. Shengxin Company appealed to the court and requested to have priority of compensation regarding the construction project price.

The civil judgement by the Higher People's Court of Liaoning Province (No. 1049, 2016, Final, Civ. Division, Liaoning Higher People's Court) modified that of the first instance: Shengxin Company should not only get the payment of the construction project price of RMB 30 million by Yachen Company but also should enjoy the priority of compensation within the range of the arrears of RMB 30 million in the construction project involved. The judgment impaired the lawful rights and interests of Deyun Company because the lands and buildings involved in the case had already been seized and the date of Shengxin Company filing the case was after the time limit of the priority. Deyun Company held that Shengxin Company's application should not be supported and that the case involving Yachen Company and Shengxin Company was sham litigation. Deyun Company requested to revoke the civil judgement (No. 1049, 2016, Final, Civ. Division, Liaoning Higher People's Court).

The court of first instance rendered a ruling on October 30, 2017 and dismissed the claims of Deyun Company. After that, Deyun Company refused to accept the ruling of first instance and appealed to the Supreme People's Court.

Issue(s)

Whether Deyun Company meets the application conditions to bring a lawsuit of revocation as a third party.

Holding

The Supreme People's Court held upon review that Deyun Company was ineligible for filing a third-party revocation action. Deyun Company did not have the independent substantive right to the subject matter of the case (No. 1049, [2016], Final, Civ. Division, Liaoning Higher People's Court). Deyun Company was not related to the outcome of the case in terms of legal interests, rights and obligations (No. 1049, [2016], Final, Civ. Division, Liaoning Higher People's Court). Thus Deyun Company was ineligible for filing a third-party revocation action. In principle, the monetary claims made by Deyun Company was not included in the civil rights and interests that should be protected by third-party revocation lawsuits. Objectively speaking, Deyun Company's creditor's rights could be affected after Shengxin Company got the compensation priority in receiving the payment of the construction project, but

the pure fact-based and economic influence did not justify "affecting the third party's legal interests". The evidence provided by Deyun Company was insufficient to support its claims that Yachen Company and Shengxin Company deliberately raised the construction fees in order to avoid the debts through malicious collusion and sham litigation. In summary, the grounds of appeal given by Deyun Company were untenable. The judgment of first instance was clear in fact-fining and correct in application of law. In the end, the Supreme People's Court ruled to dismiss Deyun Company's application for retrial.

Comment on Rule

Unlike the ordinary civil actions, the conditions for filing a lawsuit of revocation by a third party shall comply with the provisions in Article 56 of the *Civil Procedure Law of the People's Republic of China* and Article 292 of the *Judicial Interpretations of the Civil Procedure Law*.[1] According to the aforesaid law and judicial interpretations, the system of third-party revocation litigation aims to protect the rights and interests of the third party who did not appear in the original trial and whose interests may be harmed by mistaken effective judgment. Meanwhile, this litigation right should not be abused so as to ensure the stability of the already effective judgement in judicial practices. Since the third-party revocation litigation is an ex post facto remedy proceeding, its standards of plaintiff's subject qualification and scope is stricter than those of

[1] According to the provisions of Article 56 of the *Civil Procedurel Law of the People's Republic of China*, if a third party considers that he has the independent right to claim the subject matter of the action of both parties, he shall have the right to bring an action. If a third party does not have the independent right to claim the subject matter of the action of both parties but the outcome of the case will affect his legal interest, he may file a request to join the litigation or the people's court may notify him to join the litigation. If a people's court holds a third party to bear a civil liability, such a third party shall be entitled to the rights and obligations as a party to litigation. If a third party as mentioned in the preceding two paragraphs fails to participate in an action, which is not attributed to his own fault, but there is evidence that a legally effective judgment, ruling or mediation statement is entirely or partially erroneous and causes damage to the third party's civil rights and interests, the third party may, within six months from the day when he knows or should have known that his civil rights and interests have been damaged, institute an action in the people's court which rendered the judgment, ruling or mediation statement. If, after trial, the third party's claims are tenable, the people's court shall modify or revoke the original judgment, ruling or mediation statement; or if the third party's claims are untenable, the claims shall be dismissed.

Article 292 of the *Judicial Interpretations of the Civil Procedure Law* provides that "where a third party files a revocation lawsuit against an effective judgment, ruling, or mediation statement of a people's court, he shall, within six months from the date when he knows or should have known that his civil rights and interests have been damaged, institute an action in the people's court which rendered the effective judgment, ruling or mediation statement, and provide the evidentiary materials to prove the existence of the following circumstances: (1) The third party fails to participate in an action for reasons that cannot be attributed to his own fault; (2) The legally effective judgment, ruling or mediation statement is entirely or partially erroneous; (3) The errors in the contents of the legally effective judgment, ruling or mediation statement cause damage to the third party's civil rights and interests.

participating in the litigation as a third party in the aspect of determining "affecting the legal interest". It not only requires the outcome of the original case must affect a third party's legal interest, but also must meet the substantive requirement that the mistaken effective judgment in the original trial harm the rights and interests of the third party. Therefore, in this case, when it comes to the judgement of whether Deyun Company meets the prescribed conditions to initiate a revocation lawsuit as a third party, it is necessary to examine whether Deyun Company meets the subject qualification of the third-party revocation litigation, and also appropriately examine whether Deyun Company meets the substantive conditions of the third-party revocation litigation.

1. **Whether Deyun Company met the subject qualification of a revocation action by a third party**

In accordance with the provisions of Paragrah1, Paragraph 2 of Article 56 of the *Civil Procedure Law* the plaintiff that has the right to bring an action to revoke an effective judgement of others' case as a third party should be a third party who has an independent right to claim or does not have an independent right to claim. In this case, Deyun Company is neither the developer nor the contractor of the construction project involved in the contract disputes between Yachen Company and Shengxin Company. Deyun Company acquired the alleged creditor's rights of Yachen Company by means of transfer from Tang X. The legal relation in the construction project contract between Yachen Company and Shengxin Company is different from that in the private lending between Tang X and Yachen Company. Deyun Company does not have the independent substantive right to the subject matter of the civil case (No. 1049, [2016], Final, Civ. Division, Liaoning Higher People's Court). Therefore, Deyun Company is not a third party with the independent right to claim. The judging standards of a third party without the independent right to claim should be strictly restricted, requiring that he should not be related to the outcome of the case in terms of legal interests, rights and obligations. The third party without the independent right to claim is usually divided into three kinds: the auxiliary third party, the defendant-type third party and plaintiff-type third party. The auxiliary third party purely assists the court in ascertaining the facts of the case and prevents unfavorable outcome without bearing civil liabilities; The defendant-type third party is actually a third party who shall participate in the lawsuit and ultimately need to bear part or all of the civil liabilities; The plaintiff-type third party is one who participats in the lawsuit as a third party plaintiff and enjoys the same interests as the plaintiff dose in the original trial. In this case, Deyun Company, not attach to any party in the contract disputes between Yachen Company and Shengxin Company , was not the subject of rights and obligations to the subject matter in the lawsuit of contract disputes; nor did it play any supporting role in ascertaining the facts of the case, thus it was not an auxiliary third person either. Meanwhile, Deyun Company did not assume any civil liabilities in the case (No. 1049, [2016], Final, Civ. Division, Liaoning Higher People's Court), so it was not the defendant-type third party. In the construction contract disputes with Yachen Company, Shengxin Company, as the contractor, enjoyed the compensation priority over the construction project fees, which has no legal relationship with Deyun

Company's creditor right to Yachen Company. Deyun Company then did not meet the qualification of plaintiff-type third party. Therefore, Deyun Company was not a third party without the independent right to claim, either. In summary, Deyun Company did not have the subject qualification to bring a revocation action as a third party.

2. **Whether the effective legal document infringed upon the civil rights and interests of Deyun Company**

In accordance with Article 56 (3) of the *Civil Procedure Law*, the substantive requirements of revocation litigation by a third party is that there is evidence that the effective judgment is erroneous and infringes on to the third party's civil rights and interests. This requirement essentially means that the content of the effective judgement would affect the third party's legal interests. First, the question was that whether the claim made by Deyun Company that there were errors in the court's judgement (No. 1049, [2016], Final, Civ. Division) of supporting Shengxin Company's compensation priority over the construction project involved was tenable. In the original case, the project involved had been suspended since June 30, 2013, and Shengxin Company had not completely withdrawn. From June 30, 2013 to June 12, 2016, Yachen Company confirmed with signature the amount of workload loss of the equipment during the shutdown of Shengxin Company, and there existed the fact that it used the housing properties to offset the construction cost and raise funds. The two parties did not negotiate or unilaterally proposed to terminate the contract until Shengxin Company brought the action, and thus there was no starting day of the compensation priority over the payment of construction. Accordingly, the civil judgement (No. 1049, [2016], Final, Civ. Division, Liaoning Higher People's Court) in the first instance was not inappropriate in determining that the compensation priority should be counted from the day of contract termination. Second, the question was that whether the civil judgement (No. 1049, [2016], Final, Civ. Division, Liaoning Higher People's Court) infringed upon the civil rights and interests of Deyun Company. The "civil rights and interests" often refer to those provided in Article 2 of the *Tort Law* including the right to life, the right to health, the right to name, the right to reputation, the right to honour, right to self image, right of privacy, marital autonomy, guardianship, ownership, usufruct, collateral right, copyright, patent right, exclusive right to use a trademark, right to discovery, equities, right of succession, and other personal and property rights and interests. In addition, the law clearly specifies that the creditor's rights under special protection may be applied to revocation litigation by a third party. These are: the creditor's rights with legal priority as provided by law such as the priority over construction project fees and maritime lien; the creditor's rights with legal revocation right as prescribed by law, mainly including the creditor's right to revocation and the revocation right of bankruptcy claims. In principle, the monetary claims do not apply to lawsuits of revocation by a third party. In this case, the monetary claims made by Deyun Company were not included in the civil rights and interests that should be protected by third-party revocation lawsuits. In addition, what was special in this case was that Deyun Company's claiming of creditor's rights had entered the enforcement stage. If the judicial auction went unsold, the debts should be compensated with the property auctioned without the intervention of other rights.

If a deal was reached in the auction or the legal ruling determined that the debts should be compensated with the property, the ownership of the subject matter should be transferred the moment when the ruling of auction deal was sent to the buyer or the ruling of compensating debts with property was sent to the creditor. In this case, Deyun Company was the enforcement applicant of the houses involved, but it could not be determined based on this that it had exclusive creditor's right or real right to the houses. Objectively speaking, Deyun Company's creditor's rights could be affected after Shengxin Company got the compensation priority in receiving the payment of the construction project, but the pure fact-based and economic influence did not justify "affecting the third party's legal interests". In summary, Deyun Company did not meet the substantive requirement for filing a third-party revocation action.

3. **Whether Yachen Company and Shengxin Company harmed the interests of Deyun Company through sham litigation**

In principle, ordinary creditor's rights shall not be protected by revocation lawsuits by a third party. However, if the third party files a lawsuit of revocation on the ground that his monetary claims are infringed upon and there are evidence to prove the existence of sham litigation in the original trial, the case shall be accepted. In the disputes over construction project contract, when the construction price settled according to the actual construction work is inconsistent with the contracted construction price, if there is evidence to prove that the two parties have changed the contractual workload, the final construction price should be based on the actual workload. In accordance with the aforesaid circumstances, the court of first instance, taking into account the evidence and actual construction workload, determined in the civil judgement (No. 1049, [2016], Final, Civ. Division, Liaoning Higher People's Court) that the Construction Project Contract between Yachen Company and Shengxin Company which specified the construction price of RMB 36 million was legal and valid. This judgement was appropriate and conformed to the criterion of "Preponderance of High Degree of Probability" in civil procedure evidence. In this case, Deyun Company stated that the price of the construction project involved in this case as specified in the contract was RMB 16.96 million consistent with the bid winning notice issued by the Tender and Bid Administration Office of Wafangdian City, Liaoning Province. Whereas the price in the certificate for undertaking construction issued by the Urban and Rural Planning Department of Wafangdian City, Liaoning Province was RMB 17 million, so Deyun Company claimed that the contract price of RMB 30 million provided by Yachen Company and Shengxin Company to the court of first instance was forged, and that Yachen Company and Shengxin Company maliciously colluded to use false contract in litigation and increase the price of the construction project to deliberately damage the interests of Deyun Company. However, the evidence provided by Deyun Company was insufficient to support his claims that Yachen Company and Shengxin Company deliberately raised the construction price to avoid the debts and maliciously collude to conduct sham litigation. In summary, the evidence provided by Deyun Company was insufficient to prove the existence of sham litigation.

Guizhou Antaen Renewable Resources Technology Co., Ltd. and Guiyang Branch of Bank of Chongqing Co., Ltd., etc. v. Hefei Midea Refrigerator Co., Ltd. (Dispute over Objection to Jurisdiction)—The Confirmation of the Place where the Result of a Tort Occurs

Huizhuo Liu

Rule

In the case of the overlap of contractual liabilities and tort liabilities, according to the principle of autonomy of will, choosing the basis of the claim is the right and responsibility of the party, and the court should respect the choice of the party. The jurisdiction of civil procedures shall follow the principle that the defendant's locality prevails over that of the plaintiff. The jurisdiction of a tort action is the place where a tort is committed, the place where the result of a tort occurs and the place where the defendant's domicile is located. In the existing judicial interpretations, there are no other specific provisions except for the special provisions on network infringement and infringement upon right to reputation, where the plaintiff's domicile can be treated as the place where the result of a tort occurs. Thus according to the existing legal provisions of jurisdiction, it is not proper to make extensive explanation of the place where the result of a tort occurs.

Collegial panel judges of the Supreme People's Court for the second instance: Liu Huizhuo, Yang Lichu, Liu Jingchuan (Written by: Liu Huizhuo, Supreme People's Court; Translated by: Duan Jing).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_25

Case Information

1. **Parties**

Appellant (Defendant in the first instance): Guizhou Antaen Renewable Resources Technology Co., Ltd. (hereinafter referred to as "Antaen Company")
Appellant (Defendant in the first instance): Guiyang Branch of Bank of Chongqing Co., Ltd. (hereinafter referred to as "Guiyang Branch of Bank of Chongqing")
Appellant (Defendant in the first instance): Guizhou Huachuang Securities Broker Co., Ltd. (hereinafter referred to as "Huachuang Company")
Appellee (Plaintiff in the Trial): Hefei Midea Refrigerator Co., Ltd. (hereinafter referred to as "Midea Company")

2. **Procedural History**

First instance: No. 53 [2016], Trial, Civ. Division, Anhui Higher People's Court (dated Feb. 16 of 2017)
Second Instance: No. 224 [2017], Final, Civ. Division, the Supreme People's Court (dated Aug. 10 of 2017)

3. **Cause of Action**

Objection to jurisdiction

Essential Facts

Midea Company signed a directional contract of RMB 300 million with Huachuang Company after it was offered relevant information of Antaen Company and Guiyang Branch of Bank of Chongqing by the personnel of Huachuang Company, since Midea Company, after conducting field investigation, believed that Guiyang Branch of Bank of Chongqing provided guaranty for Antaen Company and had acquired the approval of the head office of the Bank of Chongqing, which met the requirements of its financial management business. Huachuang Company therefore signed a single trust management contract with Lujiazui International Trust Co., Ltd., and Lujiazui International Trust Co., Ltd. then signed a *Trust Loan Contract* with Antaen Company. After receiving the funds of RMB 300 million, Antaen Company used RMB 30 million to repay in advance the loan from Guiyang Branch of Bank of Chongqing. Most of the other funds were immediately withdrawn and illegally possessed. Midea Company filed a lawsuit in Anhui Higher People's Court and claimed that Antaen Company, Guiyang Branch of Bank of Chongqing and Huachuang Company had jointly committed a tort and should be jointly and severally held liable for the compensation of a total of RMB 300 million including RMB 265 million principal and the interest thereof. Antaen Company, Guiyang Branch of Bank of Chongqing and Huachuang Company raised an objection to jurisdiction and counter claimed that this case should be subject to jurisdiction of Guizhou Higher People's Court.

In the judgment of first instance, Anhui Higher People's Court held that it had jurisdiction over the case because in the tort action brought by Midea Company against Huachuang Company, the place where the result of the tort occured was Hefei City, the place where the bank account through which Midea Company remitted the RMB 300 million involved in the case was located. Therefore, the Court ruled to dismiss the objection to jurisdiction.

Antaen Company, Guiyang Branch of Bank of Chongqing and Huachuang Company refused to accept the ruling and appealed to the Supreme People's Court.

Issue(s)

Whether there is an overlap of tort liability and liability for breach of contract in this case, and how to determine the place where the result of a tort occurs.

Holding

After the retrial, the Supreme People's Court held that:

1. **Whether Midea Company was entitled to require the tortfeasor to assume the tort liability**

First, in this case, Midea Company signed the *Huangchuang Hengfeng No. 86 Directional Asset Management Plan Contract* with the subject matter of RMB 300 million with Huachuang Company based on its trust of the *Commitment Letter* issued by Guiyang Branch of Bank of Chongqing to provide guarantee for the financing of RMB 300 million of Antaen Company. Huachuang Company therefore signed the *Single Trust Management Contract* with Lujiazui International Trust Co., Ltd., after which the latter signed the *Trust Loan Contract* with Antaen Company. This series of contractual facts that Huachuang Company disbursed RMB 300 million remitted by Midea Company to Antaen Company through Lujiazui International Trust Co., Ltd. resulted in the failure to recover the investment. Midea Company held that Antaen Company, Guiyang Branch of Bank of Chongqing and Huachuang Company committed a series of fraudulent and dishonest acts leading to its huge financial losses. Some of the tortuous acts claimed by Midea company were embodied in the form of signing and performance of the contracts, which constituted the overlap of tort liabilities and contractual liability. At this point, the party is entitled to require the claims that they believe are beneficial to the realization of their rights, and the court should also respect the choice of the party. Whether the claims would be established is the issue of entity review. Therefore, the claims of the appellant Antaen Company and Huachuang Company that this case was a contractual dispute instead of the overlapping of tort liability and liability for breach of the contract and that the application of law by the court of first instance was incorrect were untenable.

2. **Determination of the place where the result of a tort occurs**

The facts based on which Midea Company filed the lawsuit were: Midea Company remitted RMB 300 million to the special account of Huachuang Company on March 21, 2016 after signing the *Directional Asset Management Contract* with Huachuang Company. On March 22, 2016, Huachuang Company disbursed the funds to Antaen Company through Lujiazui International Trust Co., Ltd., and then Antaen Company used RMB 30 million to repay the bank loans in advance. The remaining funds flowed to related enterprises or individuals with most of the funds being withdrawn. It could be seen that Midea Company believed that Huachuang Securities was a joint tortfeasor. However, determining that the actual losses of Midea Company occurred after the funds reached Antaen Company was more in conformity with the objective situation. It was far-fetched for the court of first instance to determine the place of the outward remittance as the place where the result of a tort occurred. It was appropriate that this case should be tried by Guizhou Higher People's Court.

Comment on Rule

1. **Basis for requiring the tortfeasor to assume the tort liability**

This case is an appeal case regarding objection to jurisdiction. It is necessary to determine the basis for the party to require the tortfeasor to assume the tort liability in the first place so as to determine the correct court of jurisdiction. Therefore, in this case, we must first examine whether Midea Company was entitled to bring an action against the three defendants to require them to assume the tort liabilities. First, Midea Company claimed in the court of first instance that Antaen Company, Guiyang Branch of Bank of Chongqing and Huachuang Company had jointly committed a tort that resulted in its huge financial losses, requiring Antaen Company to compensate for the losses and Guiyang Branch of Bank of Chongqing and Huachuang Company to assume joint liabilities. The action was based on the following facts: Midea Company signed the *Huangchuang Hengfeng No. 86 Directional Asset Management Plan Contract* with the subject matter of RMB 300 million with Huachuang Company, and then Huachuang Company signed the *Single Trust Management Contract* with Lujiazui International Trust Co., Ltd., after which Lujiazui International Trust Co., Ltd. signed the *Trust Loan Contract* with Antaen Company. Guiyang Branch of Bank of Chongqing issued the *Commitment Letter* to provide guarantee for the financing of Antaen Company. Huachuang Company then disbursed RMB 300 million remitted by Midea Company to Antaen Company through Lujiazui International Trust Co., Ltd. Midea Company did not know that it was cheated until it found the *Commitment Letter* was a fake one. The Public Security Bureau was conducting criminal investigation into the suspected act of contract fraud. It could be seen that Midea Company believed that its huge financial losses were caused by a series of false and fraudulent acts of Antaen Company, Guiyang Branch of Bank of Chongqing and Huachuang Company, which fell under the circumstances as prescribed in the provisions of Article 2 of the *Tort Law* where the property interests were infringed upon and the party

was entitled to require the tortfeasor to assume tort liability. Secondly, some of the tortuous acts claimed by Midea company were embodied in the form of signing and performance of the contracts. The tort liability and the liability for breach of contract were based on the same facts and the same subject matter among the same parties, which met the requirements for civil liability of more that two kinds, thus forming the overlapping of tort liabilities and liabilities for breach of contract. Finally, in accordance with the provisions of Article 122 of the *Contract Law*, when there is an overlap of tort liabilities and liability for breach of contract, the victim is entitled to require the claims that they believe are beneficial to the realization of their rights, and the court should also respect the choice of the party. Whether the claims would be established is the issue of entity review. In this case, the judgment of first instance was not inappropriate in determining that Midea Company was entitled to petition for the tortfeasor's assumption of tort liability. Therefore, the claims of the appellant Antaen Company and Huachuang Company that this case was a contractual dispute instead of the overlapping of tort liability and liability for breach of contract and that the application of law by the court of first instance was incorrect were untenable.

2. **Determination of the place where the result of a tort occurs**

In accordance with the *Civil Procedure Law* and the relevant provisions of judicial interpretations, an action instituted for tort shall be under the jurisdiction of the people's court in place where the tort took or in the place of the defendant's domicile. The place where the tort took place includes the place where a tort is committed and the place where the result of a tort occurs. At the same time, the tort result should be divided into one that has directly occurred and one that has actually occurred. But in practice, there is often a process from the committing of the tort to the occurrence of its result, especially in the case where the property rights are infringed upon. The victim's remitting the money does not necessarily result in the loss of control over the money, and the loss of control over the money does not necessarily lead to the occurrence of damage. Generally, the actual occurrence of the tort result should be determined by the fact that the tortfeasor has got actual control over the money. In this case, Midea Company believed that Huachuang Securities was a joint tortfeasor, but the actual loss of Midea Company happened after the payment reached Antaen Company, which was more in conformity with the objective situation. It was far-fetched for the first instance court to determine the place of the outward remittance as the place where the result of a tort occurred. In addition, according to the existing laws and judicial interpretations regarding jurisdiction, the jurisdiction in civil procedures should facilitate the litigation of the parties as well as the people's court to ascertain the facts. Generally, it should follow the principle that the defendant's locality prevails over that of the plaintiff. If there is no special provision to specify that the plaintiff's domicile should be treated as the place where the result of a tort occurs, the above mentioned principle should be followed. If, without sufficient evidence, the case treated the place where the plaintiff remitted the money or the place where he lost control of the money as the place where the result of a tort occurred, it was in fact another way of taking the plaintiff's domicile as the place where the result of a tort occurred, which did not comply with the existing regulations and was inconvenient for the court proceedings.

Anhui Yonghe Property Co., Ltd. v. Anhui Guoxin Construction Group Co., Ltd. (Case Concerning Supervision over Enforcement)—After the Bankruptcy Liquidation Application is Accepted, the Money Enforced into the Court Account but not Disbursed in the Enforcement Proceeding Shall be Handed over to the Court that Accepts the Bankruptcy Case

Guohui Xiang

Rule

Before the money enforced is actually paid to the enforcement applicant, if the people's court has accepted the application for bankruptcy liquidation of the enforcement respondent, the money enforced shall not be paid to the enforcement applicant, and shall be handed over to the court or administrator that accepts the bankruptcy case.

Collegiate panel of the enforcement supervision procedures of Supreme People's Court: Xiang Guohui, Huang Jinlong, Xiong Jinsong (Written by: Xiang Guohui, Supreme People's Court; Translated by: Duan Jing).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_26

Case Information

1. Parties

Petitioner (Enforcement respondent): Anhui Yonghe Property Co., Ltd. (hereinafter referred to as "Yonghe Company")
Enforcement Applicant: Anhui Guoxin Construction Group Co., Ltd. (hereinafter referred to as "Guoxin Company")

2. Procedural History

Enforcement objection proceeding: No. 42 [2017], Trial, Civ. Division, the Intermediate People's Court of Hefei City, Anhui Province (dated Apr. 17 of 2017)
Enforcement reconsideration proceeding: No. 28 [2017], Retrial, Civ. Division, the Higher People's Court of Hefei City, Anhui Province (dated Jun. 19 of 2017)

3. Cause of Action

Supervision over enforcement

Essential Facts

On May 4, 2015, the Intermediate People's Court of Hefei City, Anhui Province rendered a Civil Ruling and notice of assistance in enforcement for the case between Guoxin Company and Yonghe Company regarding disputes over a construction project contract as follows: freezing the land transfer fees of RMB 13.32 million in Land and Resources Bureau of Feixi County, Anhui province that should be refunded to Yonghe Company. On June 25, 2015, the Civil Mediation Statement (No. 00198 [2015], Civil, First Instance) of this district court determined: "1. Yonghe Company should pay Guoxin Company RMB 13,910.094 (including a return deposit of RMB 10 million compensation of RMB 3,320,000 and a payment of overdue interest of RMB 590,094 from April 8, 2015 to the signing date of this agreement) in a lump sum before July 8, 2015; 2. If Yonghe Company fulfils the obligations of the first agreement as scheduled, the disputes over the construction project contract between the two parties shall be completed at this point, and neither party may claim any other rights to the other party in this case; If Yonghe Company fails to pay the above amount in full, it shall pay the overdue money at an interest rate 4 times that of the loan interest rate of the People's Bank of China during the same period until the sum is paid off. Guoxin Company can immediately apply for enforcement."

As Yonghe Company failed to fulfil the obligations set out in the above Civil Mediation Statement, Guoxin Company filed an application with the enforcement division of people's court, the Intermediate People's Court of Hefei City, Anhui Province on July 15, 2015. On October 20 of the same year, this court rendered an Enforcement Ruling and Notice of Assistance in Enforcement (No. 401 [2017]),

which were sent to Public Finance Bureau of Feixi County, Anhui province and Land and Resources Bureau of Feixi County, Anhui province to extract land transfer fees of RMB 13.32 million. On December 11, 2015, Public Finance Bureau of Feixi County transferred the land transfer fee of RMB 13.32 million to the court's enforcement account.

Because there are still many enforcement cases in proceeding in the Feixi County People's Court of Anhui Province involving the enforcement respondent Yonghe Company, on December 7, 2015, the Feixi County People's Court of Anhui Province submitted to the Intermediate People's Court of Hefei City, Anhui Province the letter of application for distributing the executed money among the concerned cases. On January 18, 2016, Hefei Intermediate People's Court delivered a letter to the Feixi County People's Court, notifying that the property involved would be distributed according to the order of freezing. Within 30 days from the date of receipt of the notice, other creditors of Yonghe Company could apply for bankruptcy to the people's court located in the place where they had their domicile. On January 22, 2016, according to the application of the creditor Zhang X, the Feixi County People's Court of Anhui Province rendered a civil ruling (Civ. No. 2 [2016]), and accepted the application for bankruptcy liquidation of Yonghe Company.

On January 5, 2017, the Intermediate People's Court of Hefei City, Anhui Province issued the notice (No. 00524 [2016]), deeming that the land transfer fee of RMB 13.32 million enforced from Yonghe Company should belong to Yonghe Company and it should be transferred to the bankruptcy court for disposal. Guoxin Company refused to accept and filed an objection to the court, claiming that the money enforced to the court account should not be treated as bankrupt property. According to the reply letter from the Supreme People's Court, with regard to the property subject to enforcement, the people's court had taken corresponding enforcement measures, thus the property was no longer under the debtor's actual control and should be deemed to have been delivered to the obligee, and the property should not be classified as a part of the bankruptcy assets. Based on this Guoxin Company requested to have the abovementioned money enforced to its account.

According to the *Interpretations of the Supreme People's Court on the Application of the Civil Procedure Law,* "In the enforcement proceeding where the enterprise legal person, as the enforcement respondent, falls under the circumstances as set forth in paragraph 1, Article 2 of the *Enterprise Bankruptcy Law*, the enforcement branch of the court shall, with the consent of one of the enforcement applicants or the enforcement respondent, render a ruling to suspend the enforcement against the respondent and transfer the documents related to the enforcement case to the people's court in the place where the enforcement respondent has his domicile. Where the people's court in the place where the enforcement respondent has his domicile rules to accept the bankruptcy case, the enforcement branch of court shall terminate the measures of preservation of the enforcement respondent's property." Hefei Intermediate People's Court of Anhui Province held that when the bankruptcy case was accepted by the court in the place where the respondent had his domicile, the enforcement case of the court should be suspended and the land transfer fee of RMB 13.32 million enforced to the court account should be transferred to the

court that accepted the bankruptcy case. The land transfer fee that had been enforced to the court account was not actually delivered to the enforcement applicant, thus the enforcement proceeding was not completed and the ownership of the money enforced still belonged to the enforcement respondent Yonghe Company. Guoxin Company's claims that the money was no longer under the actual control of the debtor and should be deemed to be delivered to the obligee did not comply with the provisions that the real right over movable property should be transferred at the time of delivery. Therefore, its objection application was not accepted. Hefei The Intermediate People's Court of Hefei City, Anhui Province rendered an enforcement ruling (Enforcement Objection. No. 42 [2017]) and dismissed the Guoxin Company's objection application.

Guoxin Company refused to accept the ruling and filed an application for reconsideration in the Higher People's Court of Anhui Province, requesting the revocation of the civil ruling (Enforcement Objection, No. 42 [2017]) of the Intermediate People's Court of Hefei City, Anhui Province.

Anhui Higher People's Court held that, the enforcement of the court made based on effective legal documents and the application of the applicant complied with the relevant provisions and the money that had been enforced should be given to the creditor. In the enforcement proceeding by the enforcement branch of the court, Yonghe Company's land transfer fee was extracted from the Finance Bureau of Feixi County Anhui Province to the enforcement account of the court. The money enforced in essence was held in escrow by the enforcement branch of the court for the enforcement applicant, no longer under the debtor's actual control, which was deemed to have been delivered to the obligee. Anhui Higher People's Court rendered the enforcement ruling (Enforcement Resumption No. 28, 2017) and revoked the ruling (Enforcement Objection. No. 42, 2017) of Hefei Intermediate People's Court.

Yonghe Company claimed that there was error in the application of law in the enforcement ruling (Enforcement Resumption No. 28, 2017) of the Higher People's Court and thus it should be dismissed. Yonghe Company petitioned to the Supreme People's Court.

Issue(s)

After the bankruptcy liquidation application is accepted, the money that has been enforced into the court account in the enforcement proceeding but not disbursed to the enforcement applicant shall be given to the enforcement applicant or handed over to the court that accepts the bankruptcy case.

Holding

The Supreme People's Court holds that: After the bankruptcy liquidation respondent of enforcement respondent is accepted by the people's court, the money that has been enforced into the court account in the enforcement proceeding but not disbursed to the applicant shall be handed over to the court that accepts the bankruptcy case. According to Article 16 and Article 17 of the *Guiding Opinions Concerning the Transfer of Enforcement Cases to Bankruptcy Review*, the money enforced that has already been transferred, remitted, or paid in cash to the enforcement applicant no longer belongs to the enforcement respondent since the ownership of the property has been changed. The money such as bank deposit that has been enforced into the enforcement account of the court but not yet transferred, remitted, or paid in cash to the enforcement applicant is still the property of the enforcement respondent because the ownership of the property has not been changed. The enforcement branch of the court shall hand the money over to the bankruptcy court or administrator without disbursing it to the enforcement applicant after after receiving the ruling of acceptance by the court to which the case is transferred. On December 29, 2017, Supreme People's Court rendered an enforcement ruling (Enforcement Supervision No. 422 [2017]): "1. revoke the enforcement ruling (Enforcement Resumption No. 28 [2017]) of Anhui Higher People's Court; 2. maintain the enforcement ruling (Enforcement Objection. No. 42 [2017]) of Hefei Intermediate People's Court.

Comment on Rule

In this case, Hefei Intermediate People's Court of Anhui Province and Anhui Higher People's Court hold different views regarding the ownership of the money that has been enforced to the court account but not yet disbursed to the enforcement applicant. Hefei Intermediate People's Court believes that the land transfer fee of RMB 13.32 million that has been enforced to the court account but not actually delivered to the enforcement applicant should still belong to the enforcement respondent Yonghe Company since the enforcement proceeding has not been completed yet. Whereas Anhui Higher People's Court holds that the money shall be deemed to have been delivered to the obligee based on the fact that it is in essence held in escrow by the enforcement branch of the court for the enforcement applicant and is no longer under the debtor's actual control. In this case, it should be handed over to the court that accepted the bankruptcy case.

First, according to Article 16[1] and Article 17[2] of the *Guiding Opinions Concerning the Transfer of Enforcement Cases to Bankruptcy Review*, The money such as bank deposit that has been enforced into the enforcement account of the court but not yet transferred, remitted, or paid in cash to the enforcement applicant is still the property of the enforcement respondent because, the ownership of the property has not been changed. The enforcement branch of the court shall hand the money over to the bankruptcy court or administrator without disbursing it to the enforcement applicant after receiving the ruling of acceptance by the court to which the case is transferred.

Second, *The Reply of the Supreme People's Court to the Request for Instructions on How to Understand Article 68 of the Judicial Interpretation of the Supreme People's Court on the Bankruptcy Law* (Civ. No. 52, hereinafter referred to as the *Reply*) should no longer be used as the legal basis for dealing with relevant issues. The *Reply* specifies two situations where the property should not be classified as the property in bankruptcy: "1. Where, in addition to a valid enforcement ruling rendered in the ongoing enforcement proceeding, necessary appraisal and auction procedures have been conducted for disposal of the property subject to enforcement, and the relevant party has paid a consideration, the property enforced shall be deemed to have been delivered to the applicant and the enforcement proceeding completed although the transfer registration has not been processed, for which the relevant party is not at fault. Therefore, the property shall not count as the property in bankruptcy. 2. Where the people's court has taken corresponding enforcement measures as to the property enforced, and the property is no longer under the debtor's actual control, then the property should be deemed to have been delivered to the obligee and the enforcement proceeding completed. The property shall not count as the property in bankruptcy." The first situation mainly concerns the real property that needs transfer registration. The second situation mainly investigate whether the property enforced is no longer under the debtor's actual control so as to determine whether or not the property would count as property in bankruptcy. There is no distinction in terms of the property type Anhui Higher People's Court's ruling that the money enforced was already delivered to the obligee was mainly based on the fact that the money involved is no longer under the debtor's actual control, which was basically consistent with the guidance of the *Reply*. However, the *Reply* didn't conform to the content of the *Property Law* and the *No.1 Judicial Interpretation of Property Law.* Besides, the *Reply* was made on December 22, 2004. Its idea of determining whether the property enforced

[1] Article 16 of the *Guiding Opinions Concerning the Transfer of Enforcement Cases to Bankruptcy Review* provides that "After the court to which the case is transferred rules to accept it, the enforcement branch of the court shall, within seven days, transfer to the bankruptcy court or administrator property of the enforcement respondent including the bank deposit enforced to the court account, the movable property in seizure and securities."

[2] Article 17 of the *Guiding Opinions Concerning the Transfer of Enforcement Cases to Bankruptcy Review* provides that "When the enforcement branch of the court receives the ruling of acceptance rendered by the court to which an enforcement case is transferred, the property that shall not be transferred include the property which has been disposed of and delivered to the buyer through auction, the property which is used to repay the debts and the ruling of it has been delivered to the creditor, and the money enforced that has already been transferred, remitted or paid in cash because the ownership of it has been changed and it no longer belongs to the enforcement respondent."

was delivered to the obligee based on "whether or not it was under the debtor's actual control" was not consistent with the guidance of the *Judicial Interpretation of Civil Procedure Law* implemented on February 4, 2015 and *the Guiding Opinions Concerning the Transfer of Enforcement Cases to Bankruptcy Review* promulgated by the Supreme People's Court on January 20, 2017. Thus it should not be used as the legal basis for dealing with relevant issues.

Finally, from the perspective of value orientation, the value orientation of property distribution should be tilted to all creditors to facilitate the resolution of contradictions and disputes since the start of bankruptcy proceeding. According to the provisions of the Article 19 of the *Bankruptcy Law*, the enforcement proceeding shall be suspended with the start of bankruptcy proceeding, and neither the enforcement respondent nor the people's court shall liquidate the individual claims. If it is determined that the money enforced into the people's court or a third party account can continue to be delivered to the enforcement applicant due to previous enforcement, then it is illegal enforcement against the above provisions of the *Bankruptcy Law*. Therefore, after the court accepts the bankruptcy application, the money enforced to the court account or a third-party account but not disbursed to the enforcement applicant shall be deemed as the debtor's property and included in the property in bankruptcy after the debtor declares bankrupt, and then the court shall make a fair distribution according to the bankruptcy proceeding.[3] The relevant provisions of the *Judicial Interpretation on the Civil Procedure Law* and the *Guiding Opinions Concerning the Transfer of Enforcement Cases to Bankruptcy Review* all reflect the spirit of fair liquidation for creditors.

Reference

1. Wang Fubo, "The Understanding and Application on the Guiding Opinions of the Supreme People's Court on Several Issues concerning the Transfer of Enforcement Cases for Bankruptcy Review", *People's Judicature (Application)*, 11, 2017, p. 51.

[3] Wang [1].

Zhang X v. Lei X and Zhao X (Disputes over Copyright Infringement)—Necessary Scenes and Limited Means of Expression in Works with the Same Historical Theme are not Protected by Copyright Law

Rong Li

Rule

The historical theme works created on the same theme is the common wealth of society, falls under the category of thoughts and can't be monopolized by individuals. Everyone is entitled to use and create works in his own way. The necessary scenes unavoidably taken for the creation of such works are not protected by copyright law. The plot embodying the author's thoughts and feelings belongs to the category of expression, and the plots with originality are protected by copyright law.

Case Information

1. **Parties**

Applicant in the retrial (Plaintiff in the first instance, Appellant in the second instance): Zhang X
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): Lei X
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): Zhao X

Collegial panel judges of the Supreme People's Court for re-trial: Yu Xiaobai, Luo Dian, Li Rong (Written by: Li Rong, Supreme People's Court; Translated by: Sun Lin, Zheng Yi).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_27

Defendant in the first instance, Appellee in the second instance: Shandong Aishuren Audio and video books Co., Ltd. (hereinafter referred to as "Aishuren Audio and video books Company")

2. **Procedural History**

First instance: No. 84 [2011], Trial, Civ. Division, the Intermediate People's Court of Jinan City, Shandong Province (dated Jul. 13 of 2011)
Second instance: No. 194 [2012], Trial, Civ. Division, the Higher People's Court of Shandong Province (dated Jun. 14 of 2012)
Application for retrial: No. 1049 [2014], Retrial, Civ. Division, the Supreme People's Court (dated Nov. 28 of 2014)

3. **Cause of Action**

Dispute over copyright infringement

Essential Facts

On December 3, 1999, Zhang X obtained the right to produce and adapt the TV series *Source of Snowfield* ("Xue Yu He Yuan"). In January 2000, he completed the script of 20 TV series *Plateau Cavalry Company* ("Gao Yuan Qi Bing Lian"). On August 17, 2000, Zhang X, on behalf of the Association for International Friendly Contact of Shandong Province, entered into an agreement with Lei X, on behalf of the Television Art Center of Political Department of Military Region in Lanzhou, to cooperate in the shooting of TV series. Zhang X possesses the copyright and related rights and interests of the *Plateau Cavalry Company* ("Gao Yuan Qi Bing Lian"). From May 17 to May 21, 2004, *Plateau Cavalry Company* ("Gao Yuan Qi Bing Lian") was broadcasted in CCTV-8 in the morning.

In 1996, Zhao X's novel *Travelling with Gun on the Horse* ("Qi Ma Kua Qiang Zou Tian Ya") was published in Vol. 12 (Total Vol. 512) of the *PLA Literature and Art (PLA: People's Liberation Army)*. In April 2001, the novel *Boundless Sky* ("Tian Cang Mang") was published in the PLA Literature and Art Press. On April 24, 2003, Lei X, on behalf of the Television Art Center of Political Department of Military Region in Lanzhou, entered into a contract with Shi X to obtain the right of adaptation of the TV series *Boundless Sky* ("Tian Cang Mang"). On July 21, 2003, Lei X, on behalf of the Television Art Center of Political Department of Military Region in Lanzhou, concluded an agreement with Zhao X about the revision of *The Last Cavalry* ("Zui Hou De Qi Bing"), inviting Zhao X to revise the TV series *The Last Cavalry* ("Zui Hou De Qi Bing") adapted by Lei X based on Shi X's novel *Boundless Sky* ("Tian Cang Mang"). From May 19 to May 29, 2004, *The Last Cavalry* ("Zui Hou De Qi Bing") was broadcasted in CCTV-1 in prime time at night.

In 2010, Zhang X filed a first-instance lawsuit on the ground that *The Last Cavalry* ("Zui Hou De Qi Bing") infringed on the copyright of the script and TV series of

Plateau Cavalry Company ("Gao Yuan Qi Bing Lian"). In March 2011, Copyright Protection Committee of Copyright Protection Center of China ruled that *The Last Cavalry* ("Zui Hou De Qi Bing") and *Plateau Cavalry Company* ("Gao Yuan Qi Bing Lian") were partly similar in the characterization of the protagonists and relations as well as the clues. The plots were partly identical or similar, but the specific expressions of these plots were basically different except for one expression of words. Upon the above appraisal conclusion, the court of first instance found that *The Last Cavalry* ("Zui Hou De Qi Bing") has not infringed on the related rights and dismissed Zhang X's claim. Unsatisfied with the judgment of first instance, Zhang X filed an appeal and the Court of Second Instance rendered a judgment, dismissing the appeal and affirmed the original judgment. Unsatisfied with the judgment of second instance, Zhang X appealed for a retrial.

Issue(s)

Whether the script and TV series of *The Last Cavalry* ("Zui Hou De Qi Bing") infringed on the copyright of the script and TV series of *Plateau Cavalry Company* ("Gao Yuan Qi Bing Lian").

Holding

Upon close examination, the Supreme People's Court holds that:

1. **Regarding Zhang X's claim on the same theme of *The Last Cavalry* and *Plateau Cavalry Company***

Through a comparison of *The Last Cavalry* with *Plateau Cavalry Company*, it can be found by this court that the main theme and clues of *The Last Cavalry* originated from *Travelling with Gun on the Horse*. Through a comparison of *Plateau Cavalry Company*, *The Last Cavalry*, *Traveling with Gun on the Horse* and *Boundless Sky*, it can be concluded that four works are all thematic works about the military troops based on the main line of the withdrawal (or contraction) of manning quotas in the cavalry units during the streamlining and reorganization in the mid-1980s. Belonging to the category of thoughts and creativity, the theme line is the common wealth of society and cannot be monopolized by individuals and should not be protected by copyright law. The authors of the four works are entitled to express and make use of such themes in their own way. Therefore, even though the theme lines of *The Last Cavalry* and *Plateau Cavalry Company* have certain similarities, because the theme lines are not protected by the copyright law, it cannot be ruled that *The Last Cavalry* has infringed upon the copyright of the scripts and TV plays of *Plateau Cavalry Company*.

2. **With regard to Zhang X's claim on the same character settings and relations of *The Last Cavalry* and *Plateau Cavalry Company***

Apart from the limitation of the length of the short story and the absence of triangular love relationship or military-civilian relations in *Travelling with Gun on the Horse*, the other three works all contain the character settings and relations, such as relations of triangular love, military partnership, officers and soldiers, and military-civilian relations. Such processing methods are inevitably necessary scenes and limited expressions for military works and should not be protected by copyright law.

3. **Regarding Zhang X's claim on the same language expressions and story plots of *The Last Cavalry* and *Plateau Cavalry Company***

From the perspective of language expression, the expression of 'being a free Jeep Wrangler Rubicon' in *The Last Cavalry* is basically same as that of 'being a Jeep Wrangler Rubicon' in *Plateau Cavalry Company*. Because this part of expression originates from the movie 'Jeep Wrangler Rubicon', it is not the original expression in *Plateau Cavalry Company*. From the perspective of the plot, the plot used to reflect the author's thoughts and feelings falls under the category of expression, and the original plot should be protected by copyright law. However, the fact that only part of the elements in the story are identical and similar, cannot lead to the conclusion that the stories are same and similar accordingly. After watching the two TV series of *Plateau Cavalry Company* and *The Last Cavalry* respectively, and reading the two novels of *Travelling with Gun on the Horse* and *Boundless Sky*, the identical and similar parts are mostly public domain materials or materials lacking originality. There are similarities only in some elements in the story plots, but the specific content and expression meaning of the plot are not the same. On the whole, *The Last Cavalry* and *Plateau Cavalry Company* are different in the specific plots, the emphasis of description, the character of the protagonist and the ending. The identical or similar plots take up a low proportion in two works, only a secondary position in the whole plot. Thus they did not constitute the main part of *The Last Cavalry*, and will not lead the readers and the audience to have the same and similar appreciation experience of the two works. Thus, it cannot be concluded that the two works are substantially similar.

Therefore, according to provisions in Article 15 of *Interpretation of Copyright Disputes*, *The Last Cavalry* and *Plateau Cavalry Company* are works created by different authors on the same theme which have originality and enjoy independent copyright. Thus, the Supreme People's Court dismissed Zhang X's application for retrial.

Comment on Rule

1. The background for settling the copyright disputes of film and television works in China

In recent years, with the rapid development of China's film and television industry, the infringement on film and television works on the copyright of the original creator has become increasingly prominent. How to strengthen the protection of the copyright of the original creator has become an important issue for the judicial trial of copyright of the people's court.

At the early stage of the promulgation of copyright law in China, the awareness of copyright was relatively slight. If the people's court judges rule strictly the cases of copyright disputes in film and television works, a large number of works would be identified as infringement. Therefore, under the then special background, the people's court took an appropriately lenient attitude when deciding whether film and television works constituted infringement. For example, in the case of *Beijing Jiuge Tailai Film and Television Culture Co., Ltd. v. The Chinese People's Liberation Army General Political Department of Drama Group* and other copyright infringement disputes in 2004, the Higher People's Court of Beijing City held that *Years of Burning Passion* did not constitute an infringement on *I am the Sun*, even though the former was identical with the latter in 63 places. With the rapid development of China's film and television works and the promulgation of copyright law for more than two decades, people's awareness of copyright has been enhanced. In the case that film and television works infringe upon the copyright of the original authors more and more prominently, it is necessary for the people's courts to strengthen the protection of the copyright of the original creators. We should take a strict attitude when determining whether the works constitute infringement. That is to say, when judging whether a work constitutes a 'substantial similarity', we can adopt a more stringent method to the degree of similarity, which can better protect the copyright of the original author. For example, in the case of copyright infringement disputes between Chen X (Qiong Yao for her pseudonym) and Yu X heard by the Higher People's Court of Beijing City, 21 plots and consecution of the script *Plum Blossom Scar* ("Mei Hua Lao") advocated by Chen X can be reflected into the plot deduction of the script *Palace 3: The Lost Daughter* ("Gong Suo Lian Cheng"). If only all the plots in the script *Palace 3: The Lost Daughter* are taken into account, the proportion of the above plots in *Plum Blossom Scar* is not high, but the plot setting it contains already accounts for a sufficient proportion of *Palace 3: The Lost Daughter*), and it is enough for the audience to feel that the above plots in *Palace 3: The Lost Daughter* originate from *Plum Blossom Scar*, and the above plots are the vast majority of the contents of *Plum Blossom Scar*. Therefore, the court found that the script *Palace 3: The Lost Daughter* and *Plum Blossom Scar* was substantially similar as a whole, resulting in infringement.

In the case of *Zhang X v. Lei X* and other copyright infringement disputes, the main theme and overall thread of works created on the same historical theme fall under the category of ways of thoughts. Excluding the category of thoughts of necessary

scenes and public domain which are not protected by copyright in our country, the same and similar plots in *The Last Cavalry* and the *Plateau Cavalry Company* take up a very low proportion, and they are insignificant in the whole plot, which will not give the readers and the audience the same and similar sense of appreciation. Even under strict control, it is still impossible to draw a conclusion that the two works are essentially similar in composition.

2. Factors to be considered by the people's courts when hearing the copyright infringement cases of film and television works

First of all, it is necessary to judge whether the author of the disputed infringing works has reached the works that the obligee claims to protect. According to Article 15 of the *Interpretation of Copyright Disputes*, if the failure to prove that the author of the disputed infringing works has reached the works that the obligee claims to protect, even if the disputed infringing works are substantially similar to the works that the obligee claims to protect, it is still possible to conclude that the disputed infringing works do not constitute the copyright of the infringer who claims to protect the works. The two works mentioned above are unique and enjoy the copyright respectively.

Secondly, in case the author of the disputed infringing works has reached the works that the obligee claims to protect, it is necessary to judge whether the disputed infringing works have essential similarity to the works of obligee. According to Article 2 of the *Regulations on the Implementation of the Copyright Law*, works protected by copyright law must meet the following four requirements: (1) they must be intellectual creations in the fields of literature, art and science; (2) they must be original; (3) they must be able to be reproduced in tangible form; (4) the form of expression of the works should conform to the provisions of the law. Works with original expressions are protected by China's *Copyright Law*, that is, the expression of thoughts or emotions, while it does not protect creativity, ideas for creating works, public domain information, creation forms, necessary scenes, and unique or limited expression forms. In the comparison of the two works, we should make a comparison of the original expression of the works, make a comparison of whether the author's choices, arrangements and designs in the works are identical or similar, and should not do that from perspectives of thoughts, emotions, creative ideas and objects. Considering China's *Copyright Law* does not protect ideas, even if the two works are identical or substantially similar in thoughts, infringement shall not be decided.

Thirdly, the plots reflecting the author's thoughts and feelings belong to the category of expression, and the original plots are protected by the copyright law. If some elements in the story are identical in two works, but the specific content and meaning are not, the identical and similar parts are few and insignificant, and they are in a secondary position in the whole story line, which will not cause the readers and the audience to have the identical and similar sense of appreciation experience for the two works, then it cannot be determined that the two works constitute substantial similarity.

Cao X v. Yunnan Xiaguan Tuocha Tea (Group) Co., Ltd. (Dispute over Infringement of Trademark Rights)—The Relationship Between the Registered Trademark Protection and the Popularity of Trademarks for the Disputed Infringing Commodities

Yanfang Wang

Rule

The trademark owner has not only the right to use his/her registered trademark on his/her commodities or services, to establish a connection between the trademark logo and the source of his/her commodities or services in the public, but also has the right to prohibit others from using the registered trademark for the identical or similar commodities. The puzzle and confusion of the public includes mistaking the commodity with the disputed infringing mark as the commodity of the trademark owner or having some connection with the trademark owner, and confusing the commodity of the trademark owner as the commodity of the sued infringer or mistaking the trademark owner as having some connection with the sued infringer. The opinion that the higher popularity of the disputed infringer's registered trademark enables the infringer to use his/her registered trademark arbitrarily will prevent the registered trademark from playing its basic function of identifying the source of commodities and cause substantial damage to the exclusive right in using the registered trademark.

Collegial panel judges of the Supreme People's Court for re-trial: Wang Yanfang, Du Weike, He Peng (Written by: Wang Yanfang, Supreme People's Court; Translated by: Sun Lin, Zheng Yi).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_28

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellee in the second instance): Cao X
Respondent in the retrial (Defendant in the first instance, Appellant in the second instance): Yunnan Xiaguan Tuocha Tea (Group) Co., Ltd. (hereinafter referred to as "Xiaguan Tuocha Tea Company")

2. Procedural History

First Instance: No. 01 [2016], Trial, Civ. Division, the Intermediate People's Court of Kunming City, Yunnan Province (dated Aug. 17 of 2016)
Second Instance: No. 738 [2016], Final, Civ. Division, the Higher People's Court of Yunnan Province (dated Dec. 29 of 2016)
Retrial: No. 273 [2017], Retrial, Civ. Division, the Supreme People's Court (dated Sep. 20 of 2017)

3. Cause of Action

Dispute over infringement of trademark rights

Essential Facts

Cao X brought a lawsuit to the Intermediate People's Court of Kunming City, claiming that he was the owner of the registered trademark *Military Hardware* ("Jin Ge Tie Ma") bearing No. 5492697, Xiaguan Tuocha Tea Company used the sign of *Military Hardware* ('Jin Ge Tie Ma') on the products during its production and sales of products, which violated Cao X's exclusive right to use the registered trademark. Therefore, Cao petitioned to the court that: (1) Xiaguan Tuocha Tea Company shall cease the infringement; (2) it shall also apologize publicly and eliminate the influence; (3) it shall make a compensation of RMB 1,260,000 yuan; (4) it shall make a compensation for attorney's fees and other reasonable expenses in the amount of RMB 63,990 yuan; and (5) The litigation cost and expenses in this case shall be borne by the defendant.

On June 14, 2009, Cao X obtained the No. 5492697 registered trademark, which is a combination of characters and graphics. The character "Jin Ge Tie Ma" ("金戈铁马") is a horizontal arrangement of traditional Chinese, and there is a leaf pattern under the word "Jin Ge Tie Ma". The commodities approved for use under this trademark are Category 30: tea, etc. The sued Xiaguan Tuocha Tea Company obtained two trademarks through registration on January 21, 2010 and September 7, 2014 respectively, namely, the combination trademark consisting of the pattern of "Song He Yan Nian" ("松鹤延年") + circle(s) + crane and the word trademark of "Xiaguan Tuocha Tea". The approved commodities are classified as the 30th Category including tea. In 2014 (the Lunar Year of Horse), Xiaguan Tuocha Tea

Company used the words "Jia Wu Jin Ge Tie Ma Tie Bing" ("甲午金戈铁马铁饼") on the packaging of its golden print series products. The characters are simplified, among which the characters "Jia Wu" ("甲午") and "Tie Bing" ("铁饼") are smaller, while the character "Jin Ge Tie Ma" ("金戈铁马") is larger and is located in a prominent position in the outer and inner packaging of tea cakes. A running horse is also arranged beside the word "Jin Ge Tie Ma" ("金戈铁马"). At the same time, Xiaguan Tuocha Tea Company has marked "Song He Yan Nian" registered trademark and Xiaguan Tuocha Tea in the inner and outer packages of the above-mentioned tea cakes produced by Xiaguan Tuocha Tea Company, and has marked the name of the disputed Xiaguan Tuocha Tea Company on the inner and outer packages. In February 2015, Cao X's principal agent sent a lawyer's letter to demand that Xiaguan Tuocha Tea Company immediately stop infringement, compensate for losses and make apologies. During the trial, Xiaguan Tuocha Tea Company recognized that the commodities sued of infringement were produced by the Company and that they were sold in Kunming.

Established on March 14, 1995, Xiaguan Tuocha Tea Company is mainly engaged in tea production and sales. Cao X is the legal representative of Yunnan "Jin Ge Tie Ma" Tea Co., Ltd, which was founded on February 6, 2007, mainly engaging in sales of tea, side-line products and local specialties. Yunnan Jinge Tiema Tea Co., Ltd. has used the No. 5492697 registered trademark "Jin Ge Tie Ma" on many products such as "Jing Mai Gu Shu Tea" and "Jing Mai Tuo Tea".

The Intermediate People's Court of Kunming City, Yunnan Province rendered in the judgment of the first instance that Xiaguan Tuocha Tea Company should stop selling the infringing commodities marked with "Jin Ge Tie Ma"; Xiaguan Tuocha Tea Company should compensate Cao X RMB 200,000 yuan for economic losses; and dismiss other claims raised by Cao X.

Xiaguan Tuocha Tea Company filed an appeal to the Higher People's Court of Yunnan Province, the judgment of the second instance stated that the judgment of first instance was revoked, and all the claims raised by Cao X were dismissed. Thus, Cao X appealed to the Supreme People's Court for a retrial.

Issue(s)

Whether the disputed infringing mark and the registered trademark are similar, and whether it is easy to bring about confusion among the public.

Holding

Upon retrial, the Supreme People's Court held that in this case, the No. 5492697 registered trademark by Cao X was approved to be used the Category 30 of commodities, which include tea, honey, sugar, coffee, etc., while the disputed infringing commodities were tea, belonging to the same kind of commodities as the registered trademark held by Cao X. Meanwhile, the comparison was made between the mark

used by Xiaguan Tuocha Tea Company and the visual effect of a registered trademark held by Cao X. From the constituent elements of the trademark, there are certain similarities in the two constituent elements. Although Xiaguan Tuocha Tea Company claims that it uses the marks of "Jia Wu Jin Ge Tie Ma Tie Bing" ("甲午金戈铁马铁饼") as a whole, however, after examination, the fonts of "Jia Wu" ("甲午") and "Tie Bing" ("铁饼") are smaller, while the font of in "Jin Ge Tie Ma" ("金戈铁马") is larger, and it is located in a prominent position on the outer package and inner package of the tea cake. Although Cao X's registered trademark is a composition of words and figures, the words "Jin Ge Tie Ma" ("金戈铁马") are more prominent in the constituent elements of Cao X's registered trademark, while Xiaguan Tuocha Tea Company highlights the "Jin Ge Tie Ma" ("金戈铁马"). Although the fonts are different, the pronunciation and meaning of the words are the same, so the two forms are similar, and it is easy to confuse the public when the words are used on the same tea commodity.

Finally, the Supreme People's Court entered a judgment to reverse the judgment of second instance and sustained the judgment of first instance.

Comment on Rule

Article 57 of *Trademark Law* provides that any of the following acts shall be an infringement upon the right to exclusive use of a registered trademark: (1) using a trademark which is identical with or similar to the registered trademark on the same kind of commodities or similar commodities without a license from the registrant of that trademark; (2) using a trademark which is similar to the registered trademark on the same kind of commodities or similar commodities without a license from the registrant of that trademark, or using the same or similar trademark as its registered trademark on similar commodities, which may easily lead to confusion. Article 10 of the *Interpretation on Dispute of Trademark* provides for the principle of judging whether two trademark symbols are identical with as or similar to each other, that is (1) ordinary attention of the relevant public shall be adopted as the criterion; (2) it is imperative to make an overall comparison of the trademark symbols and a comparison of the main parts of the trademark symbols under the conditions where the objects under comparison are isolated from each other; (3) to judge whether a trademark is similar, the prominence and popularity of the registered trademark shall be considered. According to the *Trademark Law* and the aforementioned judicial interpretation, the key to the determination of infringement of trademark rights in this case is whether the sued infringing marks and registered trademarks are similar, and whether it is possible to confuse the public concerned.

In determining whether they are similar, there are two improper points in the application of the judicial interpretation of the preceding article in the judgment of second instance: 1. the court ignores the fact that as the composition trademark of words, "Jin Ge Tie Ma" is the main part of the trademark due to naming habits and other factors. 2. according to the provisions of third paragraph of judicial interpretation of the preceding article, the determination of whether the trademarks are similar

shall take into account the popularity and significance of the registered trademark, rather than the popularity of the sued infringing trademark.

Firstly, the people's court should examine and decide the facts on the basis of examining the evidence provided by the parties, rather than on deduction. Even if it is necessary to deduce the relevant intention of the parties according to the preponderant evidence of the case, it must be combined with the facts identified by the relevant evidence. In the absence of evidence to prove that the trademark of Xiaguantuo Tea (No. 12201774) enjoys a higher popularity, the deduction of the court of the second instance that it is not necessary for the sued infringing commodities to attach the trademark to improve their popularity is lacking in factual basis.

Secondly, as a kind of authentication to distinguish the source of commodities or services, authentication is its basic attribute. Although "Jin Ge Tie Ma" ("金戈铁马") is a common term in literary works, its registration is significant in the Category 30 of tea, honey, sugar, coffee and other commodities, thus can play a role in identifying the source of commodities. Cao X's rights to register the trademark is not different from the generally registered trademark because of the terms frequently used in literary works.

Finally, even if the trademark of Xiaguan Tuocha Tea Company enjoys higher popularity than the trademark in dispute, and there is a certain possibility for the court to rule, it is not necessary for the disputed infringing commodities to attach the trademark in the case to improve their popularity, but the deduction ignores the registered trademark as an identifying civil right, the trademark owner has the right not only to prohibit others from using the registered trademark logo on the same or similar commodities, but also to use its registered trademark logo to establish a connection between the trademark logo and the source of the commodities in the public concerned. The puzzle of the public includes mistaking the commodity using the disputed infringement mark as the commodity of the trademark owner or having some connection with the trademark owner, and confusing the commodity of the trademark owner as the commodity of the sued infringer or mistaking the trademark owner as having some connection with the sued infringer, thus preventing the trademark owner from exercising his exclusive right to use the registered trademark, and then substantially preventing the registered trademark from playing the role of authentication. Therefore, the opinion that the higher popularity of the sued infringer's registered trademark enables the infringer to use other's registered trademark arbitrarily, will prevent the registered trademark from playing its basic function of identifying the source of commodities and cause substantial damage to the exclusive right in using the registered trademark.

Shenzhen Ellassay Garment Co., Ltd. v. Wang X (Disputes over the Infringement of Trademark Rights)—Malicious Acquisition and Exercise of Trademark Rights are not Protected by Law

Shu Tong

Rule

The principle of good faith is the basic principle that all market participants should follow, and it shall be observed in civil litigations. Any act that violates the legal purpose and spirit, aims at impairing the legitimate rights and interests of others and maliciously acquires and exercises trademark rights, constitutes the abuse of rights, and relevant claims cannot be protected and sustained by law.

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellee in the second instance): Wang X
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): Shenzhen Ellassay Garment Co., Ltd. (hereinafter referred to as "Ellassay Garment Company")
Defendant in the first instance: Hangzhou Yintai Century Department Store Co., Ltd. (hereinafter referred to as "Hangzhou Yintai Department Store Company")

Collegial panel judges of the Supreme People's Court for re-trial: Wang Yanfang, Zhu Li, Tong Shu (Written by: Tong Shu, Supreme People's Court; Translated by: Sun Lin, Zheng Yi).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_29

2. **Procedural History**

First Instance: No. 362 [2012], Trial, IP Division, the Intermediate People's Court of Hangzhou City, Zhejiang (dated Feb. 1 of 2012)
Second instance: No. 222 [2013], Final, IP Division, the Higher People's Court of Zhejiang Province (dated Jun. 7 of 2013)
Retrial: No. 1320 [2013], Retrial, Civ. Division, the Supreme People's Court (dated Nov. 30 of 2013)
Review: No. 24 [2014], Review, Civ. Division, the Supreme People's Court (dated Aug. 14 of 2014)

3. **Cause of Action**

Dispute over infringement of trademark rights

Essential Facts

Established on November 18, 1996, Shenzhen Ellassay Garment Design Co., Ltd. was one of the shareholders (initiators) of Ellassay Garment Company in this case. The trademark of No. 1348583 Ellassay was registered by Shenzhen Ellassay Garment Design Co., Ltd. and approved to be used on the Category 25 of clothing and other commodities. It was registered in December 1999 upon the verification and approval. Now the ownership of the trademark is Ellassay Garment Company. The trademark of No. 4225104 "ELLASSAY" was registered by Shenzhen Ellassay Garment Industry Co., Ltd. and was approved for use on Category 18 commodities such as wallets and handbags. The trademark No. 7925873 Ellassay (hereinafter referred to as the "Ellassay") was registered in June, 2011 upon the verification and approval, and its registrant, Wang X, was approved for use on Category 18 commodities such as wallets and handbags. On July 7, 2004, the trademark No. 4157840 Ellassay Ji Tu ("歌力思及图") filed an application for registration. Upon preliminary approval and announcement, Shenzhen Ellassay Garment Design Co., Ltd. filed an application for suspension within the legally recognized suspension period. On April 2, 2014, the Beijing Higher People's Court decided in the second instance that the trademark of No. 4157840 had impaired the prior trade name rights enjoyed by Ellassay Investment and Management Co., Ltd., and should not be approved for registration. Since September 2011, Wang X has purchased leather bags with the slogan "Brand Chinese Name: Ellassay, English Name: ELLASSAY" through notarization procedure at "ELLASSAY" counters in Hangzhou City, Nanjing City, Shanghai City and Fuzhou City.

On March 7, 2012, Wang X filed a lawsuit on the ground that the production and sale of the aforementioned bags by Ellassay Garment Company and Hangzhou Yintai Department Store Company constituted an infringement on Wang X's trademark rights of Ellassay and Ellassay Ji Tu, claiming that Wang X had been engaged in the production and sale of women's bags for a long time and had always used "Ellassay" as the brand of women's bags. Knowing that Wang X has the ownership of the trademark of No. 4157840 and No. 7925873, Ellassay Garment Company still uses the

above-mentioned registered trademark acquired by Wang X on women's handbags and other commodities. The wide scope and the large quantity on infringement had seriously impaired the legitimate rights and interests of Wang X. Hangzhou Yintai Department Store Company sold commodities that infringed upon the exclusive rights of registered trademarks. To sum up, the acts of Ellassay Garment Company and Hangzhou Yintai Department Store constitute an infringement on the trademark rights of No. 4157840 and No. 7925873 owned by Wang X.

On February 1, 2013, Hangzhou Intermediate People's Court made a civil judgment (No. 362 [2012], Trial, IP Division), holding that the production and sale of the sued infringing commodities by Ellassay Garment Company and Hangzhou Yintai Department Store infringed on Wang X's exclusive right of the registered trademark, and deciding that Ellassay Garment Company and Hangzhou Yintai Department Store to stop the infringement, compensate for Wang X's economic losses and reasonable expenses in total of RMB 100,000 and eliminate the impact. Unsatisfied with the judgment, Ellassay Garment Company appealed. The Higher People's Court of Zhejiang Province rendered a civil judgment (No. 222 [2013], Final, IP Division) to dismiss the appeal and sustain the original judgment. Both the Ellassay Garment Company and Wang X refused to accept the judgment and applied to the Supreme People's Court for retrial. The Supreme People's Court decided to review this case.

Issue(s)

Whether the act of using commercial marks by Ellassay Garment Company on disputed infringing commodities has infringed on Wang X's exclusive right of registered trademarks.

Holding

The Supreme People's Court held upon reviewing the case that the principle of good faith is the basic principle that all market participants should observe. On the one hand, good faith encourages and supports people to accumulate wealth and create social value through honest labor, and protects the property rights and interests formed on this basis, as well as the freedom and rights to dispose of the property rights and interests for legitimate and proper purposes; on the other hand, it also requires people to pay attention to honesty in market activities, and to pursue their own interests without impairing the legitimate interests of others, public interests and market order. The principle of good faith shall also be observed in civil litigations. On the one hand, the principle ensures the parties can exercise and dispose of their own civil rights and litigation rights as prescribed by law; On the other hand, it also requires the parties to exercise their rights in good faith and prudently without impairing the interests of others and the public. Any act that violates the purpose and spirit of the law, aims at impairing the legitimate rights and interests of others,

maliciously acquires and exercises rights, and disturbs the order of fair competition in the market is presumed to be abuse of rights, and its related claims should not be protected and supported by the law.

Because the trademark of No. 4157840 Ellassay Ji Tu has not been approved for registration so far, Wang X has no right to sue others for infringement on trademark rights. As to whether the acts of Ellassay Garment Company and Hangzhou Yintai Department Store Company have infringed on the trademark right of No. 7925873 Ellassay held by Wang X, first of all, Ellassay Garment Company has the legal basis of prior rights. Ellassay Garment Company and its affiliated enterprises first used Ellassay as their enterprise tradename in 1996 and first obtained the exclusive right of registered trademark Ellassay in clothing and other commodities in 1999. After long-term use and extensive publicity, as an enterprise tradename and registered trademark, Ellassay has already gained high market popularity, and Ellassay Garment Company enjoys legal prior right for the aforesaid commercial logo. Secondly, the use of Ellassay Garments Company in this case is based on the legitimate basis of rights, the use method and the nature of the conduct are legitimate. From the point of the place of sale, the display and sale of the disputed infringing commodities by Ellassay Garment Company were completed at the Ellassay Counter in Hangzhou Yintai Department Store. Marking the trademark "ELLASSAY" of Ellassay Garment Company, the "ELLASSAY" Counter in the Department Store clearly indicated the provider of the disputed infringing commodities, by doing so the ordinary consumers would not mistake the commodities with those from Wang X. From the specific usage of Ellassay Garment Company, the trademark "ELLASSAY" is clearly marked on the outer package and prominent parts of the disputed infringing commodities, while the words "Chinese Brand name: Ellassay" is only presented on the tag. Since Ellassay itself is the business name of Ellassay Garment Company and has a mutual referential relationship with the "ELLASSAY" trademark, it is not obviously inappropriate for Ellassay Garment Company to use Ellassay to refer to the commodity producer on the tag of the disputed infringing commodities. There is no subjective intention of clinging to the popularity of trademark of Wang X's Ellassay, nor will it create obstacles for the ordinary consumers to correctly identify the source of the disputed infringing commodities. On this basis, the conduct of selling the disputed infringing commodities by Hangzhou Yintai Department Store is not prohibited by law. Finally, it is hard to justify Wang X's acquisition and exercise of the trademark right of Ellassay. The trademark Ellassay consists of the Chinese character "歌力思", which is exactly the same as the enterprise tradename previously used by Ellassay Garment Company and the character composition of the previously registered trademark Ellassay. As a fictional word without intrinsic meaning, the word Ellassay manifests an inherent characteristic of distinctiveness. Judging by the common sense, it is less likely to have identical registrations due to coincidence without any access to the knowledge. As an operator with close geographical proximity and high degree of business scope correlation, it is less likely for Wang X to be completely unaware of the name and trademark of Ellassay. Under such circumstances, it is difficult to justify Wang X's application for the registration of Ellassay trademark on handbags, wallets and other commodities. Wang X's action for infringement on the legitimate use of Ellassay

Garment Company by means of trademark rights obtained in bad faith constitutes abuse of rights. Therefore, a judgment is entered to dismiss the judgments of the first and the second instance, and all claims raised by Wang X.

Comment on Rule

This case is innovative for the people's court in the trademark trial practices. From the essential factual information, this case is nothing more than a case of infringement on trademark rights in general sense. The plaintiff is the owner of the trademark Ellassay which was initially approved for use in wallets, handbags and other commodities. The accused Ellassay Garment Company used the words Ellassay on the tags of the handbags it sells. If it is analyzed from the literal meaning of the first paragraph of Article 52 of the *Trademark Law*, the defendant has undoubtedly infringed on the plaintiff's trademark rights. Therefore, the judgments by the first and second instance are made in strict accordance with the legal provisions. However, in the retrial process, the Supreme People's Court put it on trial and eventually dismissed all the plaintiff's claims, out of the following considerations:

1. **Application of the principle of good faith in trademark infringement cases**

As the "fundamental principle" within the framework of civil and commercial law, the principle of good faith plays an important role in guiding civil and commercial trial practices, which is also a starting point for analyzing whether the conduct of the defendant constitutes an infringement. The principle of good faith is the basic principle that all market participants should observe. On the one hand, it encourages and supports people to accumulate wealth and create social value through honest labor, and protects the property rights and interests on this basis, as well as the freedom and rights to dispose of the property rights and interests for legitimate purposes; on the other hand, it also requires people to pay attention to honesty in market activities, and to pursue their own interests without impairing the legitimate interests of others, public interests and market order. The principle of good faith shall also be observed in civil litigations. On the one hand, the principle guarantees the parties to exercise and dispose of their own civil rights and litigation rights as prescribed by law; on the other hand, it also requires the parties to exercise their rights in good faith and prudently without impairing the interests of others and the public. Any conduct that violates the purpose and spirit of the law, aims at impairing the legitimate rights and interests of others, maliciously acquires and exercises rights, and disturbs the order of fair competition in the market is presumed to be abuse of rights, and the claims therefrom shall not be protected and supported by law.

Consideration of the principle of good faith is reflected in two aspects: one is whether the plaintiff's registration violates that principle. Obviously, when the plaintiff applied for the registration of the Ellassay trademark, the defendant's Ellassay brand and the "Ellassay" trademark registered on clothing and other commodities already have a high popularity. Considering the geographical and industrial factors,

it is difficult to eliminate the subjective malice of the plaintiff's registered trademark. The second aspect is whether the use of Ellassay Garment Company itself violates the principle of good faith. As has been analyzed in the judgment, it is difficult to identify the defendant's subjective malice in terms of the place and method of use, and the legitimacy of the source of his rights. Therefore, considering the above factors, the Supreme People's Court has analyzed and judged the conduct of the plaintiff and the defendant not only from the literal meaning of the legal provisions, but has made a comprehensive consideration from the legitimacy of the foundation of rights and the use conduct, thus exploring substantive justice to the greatest extent.

2. Substantive settlement of disputes in civil and administrative cross-claim case

Under the framework of China's intellectual property legal system, action for affirming the rights in trademark and patent law has been well instituted. Under certain conditions, the parties can initiate relevant administrative and judicial procedures to challenge the effectiveness of the patents and trademark rights that have been granted. As a result, in many cases of infringement of patents and trademarks, the initiation of rights affirmation procedure in order to fundamentally overthrow the plaintiff's basis of a certain right has become an important litigation strategy for the defendant. Based on the fact that "the case must be handled on the basis of the judgment of another case" is the cause of suspension provided in Article 150 of the *Civil Procedure Law* of China, and it is not rare that patent rights and trademark rights are eventually invalidated in practice, therefore, once the defendant applies for invalidation and requests the court to suspend the trial of infringement cases, the court will be faced with the dilemma of whether to suspend the trial: once suspended, the trial of infringement cases may be suspended for many years due to the complexity and long process of affirming rights; If not suspended, it will face the risk that the rights will be invalidated after the infringement is confirmed. In this case, there is also trademark ownership dispute between the two parties regarding the affirmation of rights for the trademark in dispute. However, the court did not passively wait for the outcome of the rights confirmation. Rather, on the basis of comprehensively considering the facts found out in this case and some effective judgments, the court made certain comments on the legitimacy of trademark registration in dispute, and dismissed the plaintiff's claims accordingly. This practice not only embodies the necessary respect of judicial decisions for the administrative review right of trademark confirmation cases, but also guides the trial of confirmation cases to a certain extent, so as to give full play to the leading role of civil procedure in the dispute settlement of civil and administrative cross-claim case, and ultimately conducive to the substantive settlement of such disputes.

Eli Lilly and Company v. Changzhou Watson Pharmaceutical Industries Ltd. (Dispute over the Infringement upon Patent for Invention)—Identification of the Preparation Process of the Disputed Infringing Drug

Rong Wu

Rule

In handling the dispute of patent infringement on the drug preparation process, it shall be presumed that the preparation process for the disputed infringing drug filed in the drug regulatory department is its actual preparation process in the absence of evidence to the contrary. In case that there is evidence to prove that the filing process of the sued infringing drug is untrue, the technical source, production regulations, production records, and filing documents of the disputed infringing drug shall be fully reviewed, and the actual preparation process of the disputed infringing drug shall be determined in accordance with law. Regarding the complex technicality involved in the preparation process of the disputed infringing drug, it can be comprehensively identified by various means such as technical investigators, expert assistants, judicial identification (forensic science expertise), and scientific and technical experts.

Case Information

1. Parties

Appellant (Plaintiff in the first instance): Eli Lilly and Company (AKA "Elily Company")

Collegial panel judges of the Supreme People's Court for re-trial: Zhou Xiang, Wu Rong, Song Shuhua (Written by: Wu Rong, Supreme People's Court; Translated by: Sun Lin, Zheng Yi).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_30

Appellee (Defendant in the first instance): Changzhou Watson Pharmaceutical Industries Ltd. (hereinafter referred to as "Watson Pharmaceutical Company")

2. **Procedural History**

The first instance: No. 0002 [2013], Trial, Civ. Division, the Higher People's Court of Zhejiang Province (dated Oct. 14 of 2013)
The second instance: No. 1 [2016], Final, Civ. Division, the Supreme People's Court (dated May 31 of 2016)

3. **Cause of Action**

Dispute over the infringement upon patent for invention

Essential Facts

On July 25, 2013, Eli Lilly and Company claimed to the Higher People's Court of Jiangsu Province that Eli Lilly and Company enjoys the patent right for invention bearing No. 91,103,346.7, and the method is applied for producing a new drug named Olanzapine. By using the preparation method, Watson Pharmaceutical Company produces the drug Olanzapine and sells to the market, which constitutes infringement on the right of patent for invention method of Eli Lilly and Company. Watson Pharmaceutical Company alleges that it has been producing Olanzapine with the process filed in the State Drug Administration since 2003. Upon the commission by the Higher People's Court of Jiangsu Province, the Shanghai Science and Technology Consulting Service Center has conducted experimental operations in accordance with the procedures described in the *Research Materials and Documentation of Raw Material Medicine Production Process* filed by Watson Pharmaceutical Company. The result indicate that the raw material Olanzapine could not be obtained in this way. The Technical Expertise Report EXP. No. 19 (2010) has been issued for the conclusion that the filing production process is not feasible because the key reaction steps of the raw material drug Olanzapine in the record of Watson Pharmaceutical Company is short of authenticity. Watson Pharmaceutical Company agrees with the conclusion, but alleging that the identification is not feasible because some of the contents involving trade secrets are not included in the filing materials. However, Watson Pharmaceutical Company does not further prove the actual preparation of Olanzapine, so the Higher People's Court of Jiangsu Province ruled that the Eli Lilly and Company's infringement allegation shall be established on the basis that Watson Pharmaceutical Company failed to make the proof, therefore rendered the civil judgment (No. 0002 [2014], Civ. Division, dated October 14, 2014): (1) Changzhou Watson Pharmaceutical Company shall compensate Eli Lilly and Company the economic loss and the reasonable expenses for stopping the infringement expenses, at RMB 3,500,000 in total; (2) Other claims by Eli Lilly and Company shall be dismissed. The case handling fees and expenses shall be RMB 809,744, of which RMB

161,950 shall be borne by Eli Lilly and Company while RMB 647,794 by Changzhou Watson Pharmaceutical Company. Both Eli Lilly and Company and Watson Pharmaceutical Company refused to accept the judgment and filed an appeal to the Supreme People's Court.

Upon the investigation by the Supreme People's Court, it is confirmed that: the *Technical Contract* entered into on October 28, 1999 between the Watson Pharmaceutical Company and the Institute of Materia Medica stated that the anti-schizophrenia drug Olanzapine and its preparations developed by the Institute of Materia Medica shall be transferred to the Watson Pharmaceutical Company and the Institute of Materia Medica is responsible for completing the pre-clinical approval information and applying for clinical application in Beijing; it also points out that acceptance criteria and methods are taken in accordance with the approval criteria for new drugs, and the inspection shall use clinical approval documents and new drug certificates. And both parties make an agreement on the approval of the new drug certificate and production in other terms.

On November 9, 1999, the Beijing Health Bureau has made a *New Drug Development Site Assessment Report Form* for the application of the new drug clinical research application of the Institute of Materia Medica. The on-site assessment conclusion column states that "The institution meets the conditions for the development of this raw material, the original records and experimental materials are basically complete and the contents are true."

In June 2001, the Institute of Materia Medica and the Watson Pharmaceutical Company have jointly submitted the "Certificate and Production Application Form of New Drug" to the National Medical Products Administration [(2001) Sub. Pro. No. 019]. In terms of the application, the Jiangsu Medical Products Administration has issued the "Report Form for New Drug Development Site Assessment Report" on October 22, 2001. The on-site assessment conclusion column states that "After on-site assessment, the original records of sample preparation and inspection are basically complete, and the conditions for the inspection instruments are basically available, the research unit has no raw material production workshop at this moment, and is thus applying for a new drug certificate for this product."

According to the application of Watson Pharmaceutical Company, on May 21, 2009, the Jiangsu Medical Products Administration has issued a letter to entrust Changzhou Food and Drug Administration of Jiangsu Province to inspect the production site of the Olanzapine of the Watson Pharmaceutical Company and obtain the samples. Then, Jiangsu Medical Products Administration issued the "Report on the Inspection of Drug Registration Production Sites" (Acceptance No. CXHB0800159) for the inspection and sampling in which the inspection results stated: "According to the relevant requirements for on-site inspection of drug registration, the first inspection of the production site of the variety was carried out on July 7, 2009. The company's organization and personnel, production and inspection facilities can meet the production requirements. The materials are traceable, the main raw materials are provided according to the specified amount, and the production process is carried out according to the submitted process. On August 25, 2009, according to the relevant requirements for on-site inspection of drug registration, the batch production records,

inspection records, raw material use and inventory records of 70309001, 70309002 and 70309003 are sampled according to sampling requirements. In the Comprehensive Assessment Conclusions column, it stated that "according to the comprehensive assessment, the on-site inspection conclusion is qualified."

On March 5, 2015, the Science and Technology Consulting Center of Jiangsu has been entrusted by Shanghai Fangda (Beijing) Law Firm to issue *Technical Examination Report* (*EXA*. No. 02. 2014). And its examination conclusion part is: (1) The preparation process of Olanzapine filed by Watson Pharmaceutical Company in 2008 to the National Medical Products Administration is feasible. (2) Comparing the Olanzapine preparation process filed by Watson Pharmaceutical Company with the National Medical Products Administration in 2008 and the Eli Lilly and Company's method patent No. 91103346.7, the original materials of both are secondary amides, but the preparation process methods are different as follows: (1) The key intermediates produced in process are different; (2) The reaction steps are different: Watson Pharmaceutical Company is a four-step method, Eli Lilly and Company is a two-step method; (3) Conditions of reaction are different: in the substitution reaction, Watson Pharmaceutical Company adopts Dimethyl formamide (DMF) as a solvent, and Eli Lilly and Company uses a mixed solvent of dimethyl sulfoxide and toluene as a solvent.

Issue(s)

Whether the Olanzapine preparation process of the Watson Pharmaceutical Company falls within the scope of patent protection, among which the key lies in the determination of the preparation process of the disputed infringing drug.

Holding

Upon review, the Supreme People's Court holds that the preparation process of Olanzapine of Watson Pharmaceutical Company does not fall within the patent scope of protection of Eli Lilly and Company. And the Supreme People's Court rendered the civil judgement (No. 1 [2016], Final, Civ. Division): (1) To set aside the civil judgement of the Jiangsu Higher People's Court. (No. 0002 [2013], Trial, Civ. Division); (2) To reject the claims of Eli Lilly and Company. The first and the second instance case handling fees are RMB 809,744, among which RMB 323,897 shall be borne by Eli Lilly and Company, and RMB 1,295,591 by Changzhou Watson Pharmaceutical Company.

Comment on Rule

1. Determination of the preparation process of the disputed infringing drug

The general idea in the trial concerning patent infringement disputes of drug preparation process is to ascertain the protection scope of the patent for invention involved firstly, and then to determine the preparation process of the disputed infringing drug, and finally to make the infringement comparison, and to decide whether the preparation process of the infringing drug shall be found within the protection scope of the patent right involved in the case. During the trial process of such cases, due to the existence of the patent authorization text and the positive attitude for providing evidence of the patentee, the scope of protection of the patent right involved in the case is relatively easy to determine. However, for the preparation process of the sued infringing drug, its forms are usually the filed materials in drug registration, production records, production regulations, etc. And it needs to conduct on-site inspection and requires technology in a higher bar, so the preparation process may show differences in various evidences, and most of the evidence is used by the sued infringer, who often lacks positivity to prove evidence. Therefore, it's often difficult to ascertain the facts of the preparation process of the sued infringing drug.

As a special product relating to human life and health, the production and sales of medicine are subject to strict institutional supervision. The premise of drug to the market is to obtain the corresponding administrative licensing. When submitting a registration application, the drug manufacturer must submit the development and experiment materials of the drug, which record the preparation process of the drug. For the approved drugs, the registration and filed materials have been strictly examined and approved by the drug regulatory authorities, including procedures for research and production site verification, and test run of drug samples. Therefore, the preparation process recorded in the drug registration materials has a high credibility and can generally be regarded as the actual preparation process of the disputed infringing drug. However, due to historical problems and supervision omissions, etc., the actual production of drug manufacturers may not follow or not exactly follow the process filed in the drug regulatory authority. In this case, the Olanzapine filed process of Watson Pharmaceutical Company in 2003 is identified as infeasible in the second instance. Therefore, the effective judgment of the previous case finds that Watson Pharmaceutical Company does not use the filed process to prepare Olanzapine in the actual production process. So, Watson Pharmaceutical Company further submits evidence of its Olanzapine batch production records and production procedures in the first instance. The actual drug production records and production procedures formed in the actual production process of the drug are the most direct evidence of the actual preparation process of the drug. However, as a long time has passed by, other documents in the case should be combined for review for their authenticity and probative value. In addition, for the production record of the drug, there is a process to find the technical fact from the related records, such as the original materials of the drug, the reaction route, the preparation step, and the preparation parameters. Specifically, the production records and production procedures should be

reviewed combined with the drug registration and filed materials, and the similarities and differences among the technical sources, raw materials, preparation processes recorded in the filed materials and the production records and regulations shall be examined. What's more, it is necessary to review the production records and procedures for years, and to clarify the technical accumulation and technical improvement process, it is also necessary to examine the inheritance and continuity of the relevant records, so as to accurately find the raw materials, reaction routes and preparation steps for the actual production of the sued infringing drug and to establish a good foundation for the subsequent infringement judgment. In this case, upon review of the batch production records, production procedures and filed registration materials of Watson Pharmaceutical Company for many years, the second instance judgment finds that Watson Pharmaceutical Company has been using its reaction route of the supplementary filed process in 2008 to produce Olanzapine from 2003 to the patent expiry date. Watson Pharmaceutical Company only adjusts the reaction conditions and the production details of the solvent on the basis of maintaining the reaction route. In this way, it can be found that the Olanzapine preparation process of Watson Pharmaceutical Company does not fall within the scope of patent protection.

2. **The identification mechanism of technical facts**

Technical cases such as patents, new plant varieties, and layout designs of integrated circuits manifest the characteristics of professionalism and technicality. The identification of technical facts is difficult in such cases. In order to improve the identification for the technical facts in a scientific, professional and neutral way, the judicial practice includes the facts identification mechanism, namely, assessors with technical knowledge, technical investigators, expert assistants, judicial identification and scientific and technical experts. Since the *Interim Provisions on Trial Provisions of the Supreme People's Court on Several Issues Concerning the Participation of Technical Investigation Officers of Intellectual Property Courts in Litigation Activities* was issued on December 31, 2014, the technical investigator system in China has been established. Although the system is a supporting system for intellectual property courts, Article 10 provides: "when other people's courts review the cases listed in Article 2 of this provision, they may refer to the application of this provision. Therefore, other people's courts may also assign technical investigators to participate in litigation in the course of reviewing the technical cases. The technical investigator is a quasi-judicial assistant who does not have the adjudicative power, but can participate in investigating and obtaining evidence, inquests, and preservation. He can also appear in court to assist the judge to identify the technical facts. With the permission of the judge, he can ask questions related to the technology to the parties, agents ad litem, witnesses, appraisers, inspectors, and expert assistants, and technical review opinions written by the said personnel about the technical issues involved in the case can serve as reference for the judge to determine the technical facts. The challenge raised by the parties against for the technical investigator shall count on the relevant provisions regarding judges in procedural laws. The patent in dispute in the present case falls within the scope of medical chemistry, which comprises complex technical issues, such as the interpretation of the claims for patent rights involved in the case,

and the determination of the preparation process of the disputed infringing drugs. In order to accurately identify the technical facts, the court has assigned the technical investigation officer to participate in the proceeding who has appeared in the court to assist the judge in the investigation of the technical issues, which ensures the fair and efficient trial of the case. The system of expert assistants can be found in Article 79 of the *Civil Procedure Law*: the parties may apply to the court to notify the person with special knowledge to appear in court, and provide opinions on the appraisal opinions or professional issues made by the appraisers. And the 'the person with special knowledge' here means the expert assistants. According to Article 122 and Article 123 of the Judicial Interpretation of *Civil Procedure Law*, expert assistants can only participate in the trial of professional issues, and their opinions on the technical issues involved in the facts of the case are regarded as the statements of the parties. With the permission of the judge, the parties may inquire the expert assistants who appear in court. According to the application of Elly Lilly and Company, the judge has informed the expert assistants to appear in court to put forward opinions on the professional protection of the scope of patent protection and the preparation process of the disputed infringing drug, which ensures the objectivity and fairness of the relevant technical facts.

It should also be noted that various specific methods in the above-mentioned fact-finding mechanism have different limitations and advantages to a certain extent: the participation of assessors and technical consultants may be limited by such factors as time, but their objectiveness and neutrality can be guaranteed and applied to a wide range of technical fields; the technical opinions of the expert assistants may fall short of neutrality, but they can fully guarantee the legitimate rights and interests of the litigants; judicial identification costs are higher and identification longer, but their probative value is stronger; the deeper technical investigator participates in the case, the higher degree of credibility technical opinion will be, but its appointment and management are still in the exploratory stage. Therefore, in the specific application of the fact-finding mechanism, the said methods complement each other and form an organic whole. As to an individual case, one or several methods can be selected according to the actual situation of the case to accurately identify the technical facts.

3. **Noticeable issues during the application of law by reference**

In this case, to determine the preparation process of the disputed infringing drug calls for emphasis on ascertaining the corresponding technical characteristics on the basis of legally determining the burden of proof, combining with the patent claims involved in the case, subject to the evidence and comprehensive consideration of drug registration filed materials, batch production records, production procedures, and technology sources and accumulation processes. There is also a question about the sources of evidence. For the distribution of the burden of proof for the actual preparation process of the sued infringing drug, Article 57(2) of the *Patent Law* provides that "if a patent infringement dispute involves the patent for invention of a new product manufacturing method, the unit or individual which manufactures the same product shall provide that manufacturing method which is different from the proof of the patented method." The principle of reversing the burden of proof shall be applied

when the disputed infringing drug is a new product. The sued infringer shall bear the burden of proof that the preparation process of the disputed infringing drug shall not fall within the scope of protection of the patent right for invention. In this case, both parties agree that the Olanzapine shall be a new product in accordance with the *Patent law*. Watson Pharmaceutical Company shall bear the burden of proof for its Olanzapine preparation process, and how it is different from the patent method. Because Watson Pharmaceutical Company fails to submit evidence of the actual preparation process of the disputed infringing drug, the previous judgment becomes evidence for the failure of the Watson Pharmaceutical Company to supply the actual drug preparation process, thus constitutes the impossibility to bring forth the evidence, so the court's determination of such impossibility constituting infringement stands. However, in the patent infringement dispute of the drug preparation process, if the drug in dispute is not a new product, it shall apply the general principle of "the burden of proof rests on the party who alleges". The burden of proof shall still be borne by the patentee for the actual preparation process of the disputed infringing drug being within the scope of protection of the patent right. However, the reality is that the registration and filing materials of the disputed infringing drugs are filed in the drug regulatory department, and the evidence of production records and production procedures is owned by the sued infringer. If the patentee is required to provide such evidence, it is obviously not conducive to find out the facts. The patentee may petition to the court based on *ex officio* to obtain the registration and filing materials of the disputed infringing drug under this circumstance. When the patentee can prove that the sued infringer has produced the same drug as that in the patent, and he has made reasonable efforts to prove the preparation process of the infringer to produce the drug, and combining the known facts and daily life experience, the patentee can find that the drug is highly likely to be produced by a patented method, the transfer of burden of proof can be applied in accordance with the relevant provisions of the judicial interpretation of judicial evidence, which means the patentee is no longer required to provide further evidence, and the sued infringer shall provide evidence that the preparation process of the drug is different from the patented method. In addition, in the case that the actual preparation process of the sued infringing drug is different from the registration and filing process of the drug regulatory department, the actual preparation process is used for the infringement comparison, and whether the sued infringer should bear the relevant administrative responsibility does not affect the decision of infringements in civil litigation.

Zhongshan Longcheng Daily Products Co., Ltd. v. Hubei Tongba Children's Products Co., Ltd. (Dispute over the Infringement of Utility Model Patent Right)—Whether the Prior Agreement Between the Patentee and the Infringer Can Serve as the Basis for Ascertaining the Amount of Damages for Infringement

Peng He

Rule

The prior agreement of the rights-holder and the infringer on the amount of compensation for infringement damages will not constitute a transaction contract between them. Therefore, the liability borne by the infringer shall only be categorized as the infringement liability, which does not fall within the concurring infringement liability and the liability for breach of contract provided in Article 122 of the *Contract Law*.

The prior consent or agreement on the amount of compensation for damages is to be regarded as a calculation method reached by the holder of rights and the infringer in advance for the loss suffered by the holder of rights due to the infringement and for the benefit gained by the infringer due to the infringement occurring in the future. The people's court may directly regard the prior consent or agreement reached between the holder of rights and the infringer as the basis for calculating the amount of damages for infringement, if law has not made it null and void.

Collegial panel judges of the Supreme People's Court for re-trial: Wang Chuang, Zhu Li, He Peng (Written by: He Peng, Supreme People's Court; Translated by: Sun Lin, Zheng Yi).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_31

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellant in the second instance): Zhongshan Longcheng Daily Products Co., Ltd. (hereinafter referred to as "Longcheng Daily Products Company")
Respondent in the retrial (The accused in the first instance, Appellant in the second instance): Hubei Tongba Children's Products Co., Ltd. (hereinafter referred to as "Tongba Baby Products Company")

2. Procedural History

The first instance: No. 467 [2011], Trial, IP Division, the Intermediate People's Court of Wuhan City, Hubei Province (dated Oct. 24 of 2011)
The second instance: No. 86 [2012], Final, Civ. Division, the Higher People's Court of Hubei Province (dated May 11 of 2011)
Application for retrial: No. 116 [2013], Review, Civ. Divsion, the Supreme People's Court (dated Dec. 7 of 2013)

3. Cause of Action

Dispute on the infringement of utility patent

Essential Facts

Longcheng Daily Products Company is the patentee of the utility model patent (hereinafter referred to as the disputed patent) named "Front Wheel Alignment Device". In April 2008, Longcheng Daily Products Company brought a lawsuit against Tongba Baby Products Company to the Intermediate People's Court of Wuhan City on the ground that Tongba Baby Products Company infringed on the patents. The court found that Tongba Baby Products Company shall stop the infringement and compensate for the losses. Tongba Baby Products Company is not satisfied with the judgment and filed an appeal. During the second instance, the two parties have reached a mediation agreement and the Higher People's Court of Hubei Province has produced a Civil Mediation Agreement (numbered No. 42 [2009], Final, Civil/Mediation), which records that: Tongba Baby Products Company shall guarantee that it will no longer infringe upon the patent rights of Longcheng Daily Products Company. In case of a violation of the utility model patent rights of Longcheng Daily Products Company, Tongba Baby Products Company will voluntarily compensate Longcheng Daily Products Company for RMB 1,000,000. But after that, Longcheng Daily Products Company finds that Tongba Baby Products Company was still engaged in the business operation of infringing patent rights. Longcheng Daily Products Company

files a lawsuit against Tongba Baby Products Company to the Intermediate People's Court of Wuhan City in May 2011, requesting the court to order Tongba Baby Products Company to compensate Longcheng Daily Products Company for RMB 1,000,000 and to bear litigation cost and expenses. During the trial of the first instance, upon interpretation by the court, Longcheng Daily Products Company has clarified that the case shall be based on patent infringement and contract breach does not apply, but makes a petition to the court to calculate the amount of the infringement in accordance with the standards agreed on by both parties. The court of the first instance holds that: if the liability of infringement and the liability for breach of contract overlap, the injured party has the right to make choices in accordance with the provisions of Article 122 of the *Contract Law*. Longcheng Daily Products Company has filed a lawsuit for infringement and shall determine the amount of compensation in accordance with the *Tortious Liability Law*. If the compensation standard follows the provisions of the previous civil mediation agreement, it will violate the above provisions of the *Contract Law*. Longcheng Daily Products Company files the lawsuit in the name of infringement, hence the lawsuit for breach of contract cannot be within the scope of the court's investigation and debate. Therefore, the court does not need to make judgments on breach of contract and liability for breach of contract, so it is not appropriate to apply the liquidated damages agreed upon by the parties. The court of the first instance shall apply the statutory compensation judgment to order Tongba Baby Products Company to make a compensation of RMB140,000 for Longcheng Daily Products Company. Longcheng Daily Products Company is not satisfied and files an appeal. The second instance of the Higher People's Court of Hubei Province holds that whether the infringement is established is the basis of the rights and obligations of the parties in this case. In the previous case, the model of the infringing baby stroller product is different from the model of the infringing baby stroller product in the case. Therefore, the amount of compensation agreed on in the mediation agreement cannot be applied to the case. The court has dismissed the appeal and affirmed the original judgment of the first instance. Longcheng Daily Products Company is still dissatisfied and applies to the Supreme People's Court for retrial.

Issue(s)

How to determine the liability of Tongba Baby Products Company? That's to say, whether the prior agreement between the patentee and the infringer can be used as the basis for determining the amount of compensation for infringement damages?

Holding

After the retrial, the Supreme People's Court finds that:

1. **The validity of the mediation agreement reached between the parties**

Since the mediation agreement is voluntarily entered into by both parties, and the terms only concern the disposition of private rights, not the public interests those of the third. In addition, there is no invalidity circumstances as provided for in the law. The Higher People's Court of Hubei Province made a civil mediation agreement after reviewing and confirming the mediation agreement. Therefore, the mediation agreement reached by the two parties in the previous judgment is legal and valid.

2. **Whether the method for calculating the amount of the compensation agreed upon in the mediation agreement can be applied**

Firstly, the civil liability of Tongba Baby Products Company in this case is not an overlap of infringement liability and breach of contract liability. The legally required essential elements for the overlap of the infringement and breach of contract liability as provided in Article 122 of the *Contract Law*, "the breach of contract by one party has infringed on another party's personal and property rights." As for the said provision, the premise of the overlap of the breach of contract liability and the tort liability is that there is a basic contractual relationship between the parties. Based on the contract, once one party violates the obligations stated in the contract, and the breach of contract violates the rights of the other party, thus constituting tort liability. Therefore, the breach of contract in this regulation shall be referred as the violation of the obligations stated in the basic transaction contract, and the breach of contract also infringes the rights of the other party, which does not mean a breach of the agreement on how the party is liable for damages after the infringement has occurred. From the content of the mediation agreement, the agreement is not an underlying transaction contract between Longcheng Daily Products Company and Tongba Baby Products Company. Instead, it is an agreement on how to assume liability for infringement (including calculation method and amount) after the infringement occurs. Therefore, the civil liability of Tongba Baby Products Company in this case is not the infringement liability and breach of contract liability as provided in Article 122 of the *Contract Law*. Secondly, Tongba Baby Products Company in this case shall bear the liability of tort. On the one hand, as mentioned above, there is no basic contractual relationship between Longcheng Daily Products Company and Tongba Baby Products Company; On the other hand, the legal significance and effect of the mediation agreement is not to provide for the contractual transaction obligations of Tongba Baby Products Company, but to make an agreement on how to bear the tort liability. Even without a mediation agreement, Tongba Baby products Company has the obligation of non-infringement based on legal provisions. Both parties have reached on the specific compensation method and amount for the future infringement of Tongba Baby Products Company in mediation agreement, only to agree on how the tort liability should be borne when Tongba Baby Products Company infringed again. Finally, the *Tort Liability Law* and the *Patent Law* did not prohibit the infringed and the infringer in advance for the methods of infringement and the amount of infringement compensation. The essence of the agreement is a simple calculation and determination method that the two parties have reached upon

in advance for the loss suffered by the right holder due to the infringement in the future, or the benefit obtained by the infringer due to the infringement in the future. The parties can agree on the amount of infringement compensation within the scope of private law because of the difficulties in proof and time-consuming litigation, and the agreement not only targets on a subsequent agreement after the infringement, but also on a prior consent/agreement. Therefore, the method for determining the amount of compensation agreed on by the parties in the mediation agreement in this case does not violate the relevant provisions of Article 65 of the *Patent Law*. To sum up, method for calculating the amount of compensation agreed by Longcheng Daily Products Company and Tongba Baby Products Company in the previous mediation agreement can be applied in this case.

3. **How the method for calculating the amount of the compensation agreed upon in the mediation agreement can be applied**

In this case, how to apply the method for determining the amount of compensation agreed on in the mediation agreement shall depend on the interpretation of the following article in the mediation agreement: "If it finds that Tongba Baby Products Company infringes on the utility model patent of Longcheng Daily Products Company, Tongba Baby Products Company shall voluntarily compensate RMB 1,000,000". According to the ascertained facts, the Civil Mediation Agreement (numbered No. 41 [2009], Final, Civil/Mediation) and the Civil Mediation Agreement (numbered No. 42 [2009], Final, Civil/Mediation) are concerned with the compensation for infringement of utility model patent rights. However, in the mediation agreement numbered No. 42 [2009], Final, Civil/Mediation, Tongba Baby Products Company may not infringe on the contents both of the design and utility model patents of Longcheng Daily Products Company. So this court considers the cases of patent infringement disputes between Longcheng Daily Products Company and Tongba Baby Products Company, and the opinions expressed by the two parties on this issue during the trial, and finally finds that the agreement in the mediation agreement that Tongba Baby Products Company shall not infringe and the corresponding compensation amount is a "package" agreement. That means: firstly, the "infringement" in the above-mentioned agreement is not limited to the specific type of infringing stroller involved; secondly, the 'infringement' in the above-mentioned agreement is not limited to the patent right thirdly, the 'infringement' refers to the act of infringing a patent right of Longcheng Daily Products Company. Therefore, in this case, Tongba Baby Products Company shall compensate Longcheng Daily Products Company for RMB 1,000,000. The reason of the application for a retrial of Longcheng Daily Products Company is justified and shall be sustained. The court of the second instance is erroneous in the application of law on how to determine the liability of Tongba Baby Products Company, which is to be corrected. Upon retrial, the judgment of Supreme People's Court reverses the original judgments of the first and second instance, and order Tongba Baby Products Company to compensate Longcheng Daily Products Company for RMB 1,000,000.

Comment on Rule

1. **What is the nature of the mediation agreement signed by Longcheng Daily Products Company and Tongba Baby Products Company?**

First of all, the mediation agreement is voluntarily singed by Longcheng Daily Products Company and Tongba Baby Products Company, which is true manifestation of mutual assent of both parties. The content only involves the private rights of both parties, not social public interests and third party interests, and there is no invalidity circumstances as provided for in the law. Moreover, the Higher People's Court of Hubei Province also produced a civil mediation agreement after reviewing the reconciliation agreement. Therefore, the mediation agreement signed by Longcheng Daily Products Company and Tongba Baby Products Company is legal and valid. Secondly, the mediation agreement has legal effects in two aspects. On the one hand, according to the mediation agreement, Tongba Baby Products Company, which was sued of infringement, has obtained the understanding of the patentee Longcheng Daily Products Company. In the case of the third judgment (numbered No. 42 [2009], Final, Civil/Mediation) in infringement of utility model patent, Tongba Baby Products Company only needs to bear the liability of RMB 55,000; On the other hand, according to the mediation agreement, Tongba Baby Products Company may take a huge liability for compensation when such infringement on the patent rights of Longcheng Daily Products Company recurs.

2. **Whether the responsibility for the re-infringement of Tongba Baby Products Company is the overlap of infringement liability and breach of contract liability as provided in Article 122 of the *Contract Law*.**

Article 122 of the *Contract Law* provides that "where the breach of contract by one party infringes upon the other party's personal or property rights, the aggrieved party is entitled to choose to claim the assumption by the violating and infringing party of liabilities for breach of contract according to this Law, or to claim the assumption by the violating and infringing party of liabilities for infringement according to other laws". In the provision of this article, the legal requirement for the concurrence of tort liability and breach of contract liability is "the breach of contract by one party infringe(ing) upon the other party's rights of the person or property". In the daily legal operations, there may occur such situation as the existence of defect in the delivered good from the seller to the purchaser, resulting in infringement to the buyer's personal and other property rights. Then, the buyer may choose to request the seller to bear the liability for breach of contract because of nonconformity of the subject matter, or choose to request the seller to bear the tort liability. It can be seen that, the premise of concurrence or overlap of the breach of contract liability and the tort liability is that there is a basic transactional contract relationship between the two parties, based on which one party violates the contractual obligations and the breach of contract violates the rights of the other party, thus making liability for infringement. In this case, there is no basic transactional contract relationship between Longcheng Daily Products Company and Tongba Baby Products Company. The mediation agreement

signed by the two parties does not belong to the contract with transactional content. The legal significance and effect of the mediation agreement is not to agree on the transactional contractual obligations of Tongba Baby Products Company, but to make an agreement on how to bear the tortious liability. Both parties conclude the specific compensation method and amount in the future infringement into the mediation agreement, which is just to facilitate further clarification of how the tort liability should be borne when such infringement of the Tongba Baby Products Company recurs. Therefore, in this case, the civil liability of Tongba Baby Products Company shall be the tort liability, and shall not be the concurrence of infringement liability and breach of contract liability as provided in Article 122 of the *Contract Law*.

3. **Whether the prior agreement between Longcheng Daily Products Company and Tongba Baby Products Company can be used as the basis for determining the amount of infringement damages.**

The *Tort Liability Law* and the *Patent Law* do not prohibit the infringed and the infringer from making an agreement in advance regarding tort liability and the amount of tort compensation. The legal nature of such an agreement can be determined as a simple calculation and determination method that the two parties have reached in advance for the loss suffered by the right holder due to the future infringement or the infringer's benefit due to the future infringement. The parties can fully agree on the amount of infringement compensation within the scope of private law autonomy due to the difficulties in burden of proof and time-consuming and laborious litigation, and the agreement includes not only a subsequent agreement after the infringement, but also a prior consent before the infringement. Therefore, the method for determining the amount of compensation agreed on by the parties in the mediation agreement in this case does not violate the relevant provisions of Article 65 of the *Patent Law*. It shall be noticed also that Article 25(3) of the *Interpretation of Copyright Disputes* provides that the agreement on the amount of compensation for the actual loss of the right holder or the illicit income of the infringer agreed on by both parties is to be allowed by the court. This can be regarded as an ascertainment by the people's court of what both parties to the dispute have agreed on after the event as to the amount of compensation. Therefore, in this case, the prior consentment between Longcheng Daily Products Company and Tongba Baby Products Company can be used as a basis for determining the amount of infringement damages.

Grohe AG. v. Zhejiang Jianlong Sanitary Ware Co., Ltd. (Dispute over Infringement of the Design Patent Right)—Determination of Patent Design Features and Functional Design Features of Authorized Designs and Its Considerations in Infringement Judgments

Rong Wu

Rule

If the disputed infringement design does not comprise an authorized design and is distinctive from all the design features of the existing design, it can be generally assumed that the disputed infringement design is not similar to the authorized one. For the purpose of making a determination of design features, the patentee shall prove the design features claimed by him/herself and allow the third party to provide counter-evidence to overturn them. On the basis of hearing the opinions of the parties, the people's courts shall fully examine the evidence and determine the design features of the authorized design in accordance with law. The identification of functional design features does not lie in whether the design is not selectable due to the limitation of function or technical conditions, but from the perspective of general consumers whether the design is only determined by a certain specific function, without evaluating the aesthetic value of the design.

Collegial panel judges of the Supreme People's Court for re-trial: Zhou Xiang, Wu Rong, Song Shuhua (Written by: Wu Rong, Supreme People's Court; Translated by: Sun Lin, Zheng Yi).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_32

Case Information

1. Parties

Applicant in the retrial (Defendant in the first instance, Appellee in the second instance): Zhejiang Jianlong Sanitary Ware Co., Ltd. (hereinafter referred to as "Jianlong Sanitary Ware Company")
Respondent (Plaintiff in the first instance, Appellant in the second instance): Grohe AG

2. Procedural History

First Instance: No. 573 [2013], Trial, Civ. Division, the Intermediate People's Court of Taizhou City, Zhejiang Province (dated Mar. 5 of 2013)
Second Instance: No. 255 [2013], Final, IP Division, the Higher People's Court of Zhejiang Province (dated Sep. 27 of 2013)
Retrial: No. 23 [2015], Retrial, Civ. Division, the Supreme People's Court (dated Aug. 11 of 2015)

3. Cause of Action

The dispute over infringement of design patent right

Essential Facts

In November 2012, Grohe AG brought a lawsuit against Jianlong Sanitary Ware Company for producing and selling the "丽雅" ("Lia") series of sanitary products in violation of its design patent right applied to the hand-held shower heads produced by Grohe AG requests the court to decide that Jianlong Sanitary Ware Company shall immediately stop the infringement, shall destroy the infringing products in stock and the molds to the production of infringing products, and compensate Grohe AG Company for economic losses of RMB 200,000.

The disputed patent involved is the design patent of "Hand held Shower Heads" (NO. A4284410X2) possessed by Grohe AG, the application date is on June 23, 2009, the date to be granted the patent is May 19, 2010, and the patent number is ZL200930193487.X. The design patent remains legal and valid till now. In the first instance, through comparison, the similarities between the disputed infringing products of Jianlong Sanitary Ware Company and the design patents involved in the case of Grohe AG are found out as follows: two kinds of products fall within the same category, and from the whole perspective, they are composed of two parts: the head of the nozzle and the handle. The shape of the head water surface of the disputed infringement product is the same as the patent involved. Both of them show that the water outlet holes are distributed in the rounded and intermediate rectangular regions at both ends, and the edges are arc-shaped. The differences between the two are: (1) The head of the nozzle of the disputed infringing product is inclined around the head,

and is inclined from the back to the water outlet. The main view of the patent and the left view show that the head of the nozzle is surrounded by a circular arc surface; (2) The water surface of the head of the disputed infringing product is separated only by a line, and the water surface of the patent head involved in the case is separated from the panel by two lines; (3) The distribution pattern of the outlet holes in the head water surface of the disputed infringing product is slightly different from the patented products; (4) The handle of the patented product has a long oval switch design, while the disputed infringing product does not have the parallel design; (5) In the patented product, although the connection between the head and the handle has a certain oblique angle, the angle is small, almost a straight connection, the angle between the head of the disputed infringing product and the handle produces a larger angle of inclination; (6) From the bottom view of the patented product, the bottom of the handle is round, and the bottom of the disputed infringing product is a curved fan shape. The lower end of the patented handle is a cylinder, and gradually shrinks into a flat ellipsoid in the direction of the joint with the head. The lower end of the handle of the disputed infringing product is a fan cylinder, and the transition to the joint with the nozzle is a fan cylinder, and the middle portion of the handle in the transition has a convex protrusion; (7) The bottom end of the handle of the disputed infringing product has a curved decorative line, and the bottom end of the handle is integrated with the back of the product. The bottom end of the handle of the patented product is not designed like this; (8) The length ratio of the patented head and handle is different from those of the disputed infringing product. There is also a difference in the arc surface of the joint between the head and the handle.

On March 5, 2013, the Intermediate People's Court of Taizhou City, Zhejiang Province made the civil judgment (No. 573 [2013], Trial, Civ. Division) and dismissed the claims of Grohe AG. Grohe AG felt dissatisfied with the outcome and appealed. The Higher People's Court of Zhejiang Province makes a civil judgment on September 27, 2013 (numbered No. 255 [2013], Final, IP Division, the Higher People's Court of Zhejiang Province) and it stated, (1) The Civil Judgment of the Intermediate People's Court of Taizhou, Zhejiang Province (numbered No. 573 [2013], Trial, Civ. Divisionis to be revered); (2). Zhejiang Jianlong Sanitary Ware Company shall immediately stop manufacturing, promising to sell and selling products that have infringed on the design patent rights of the 'Hand Held Shower Heads' owned Grohe AG, and destroys the infringement products in stock; (3) Zhejiang Jianlong Sanitary Ware Company shall compensates Grohe AG. for economic losses (including reasonable expenses incurred by Grohe AG in order to stop the infringement) of RMB 100,000; and (4) Other claims from Grohe AG shall be dismissed.

Zhejiang Jianlong Sanitary Ware Company refused to accept the judgment, and filed an application to the Supreme People's Court for retrial.

Issues

Whether the design of the disputed infringement falls within the scope of patent protection? It mainly concerns: the determination of the design features of the authorized

design, whether the push button on the handle involved in the authorized design can be judged as a functional design feature and on that basis, whether the design of the disputed infringement and the authorized design of the case are identical or similar.

Holding

Upon review, the Supreme People's Court finds that the design of the disputed infringing product produced, promised to be sold or sold by Zhejiang Jianlong Sanitary Ware Company and the authorized design of the disputed product manufactured by Grohe AG are neither identical nor similar, which thus is not the subject matter covered in the protection of the design patent rights. The production, promised sales, sales of the disputed infringing products in Zhejiang Jianlong Sanitary Ware Co., Ltd. do not constitute an infringement of the patent rights of the company Grohe AG. On August 11, 2015, the Supreme People's Court makes judgement (No. 23 [2015], Retrial, Civ. Division) that, (1) the civil judgment (numbered No. 255 [2013], Final, IP Division, the Higher People's Court of Zhejiang Province) is to be reversed; (2) the civil judgment of the Intermediate People's Court of Taizhou City, Zhejiang Province (No. 573 [2013], Trial, Civ. Division) is to be affirmed.

Comment on Rule

1. **The design features of the authorized designs**

After the amendment of the *Patent Law* in 2008, the design for which the patent right is authorized must be innovative, i.e. the design features mentioned in Paragraph 2 of Article 23 of the *Patent Law* "compared with the existing design or the combination of existing design features, it shall have obvious difference", which is called the design features of the authorized design. Reflecting the designer's creative contribution to the existing design, the design features are the basis for the attaining the protection of the design patent right. Regarding the ways to determine the design features in patent infringement judgment, Article 11(2) (ii) of the *Interpretation of Patent Infringement Disputes*, which was implemented on January 1, 2010, provides that compared with other design features of authorized design, the design features of authorized design, which are different from existing design, usually have more influence on the overall visual effect of the design. The reason is that the design feature has distinction among the authorized design and the existing design or the combination of existing design features, which makes it easy for the general consumer to distinguish the authorized design from the existing design, so the design features imposes a significant impact on the overall visual effect of the design product. Thus, in case of that, if the disputed infringing design does not contain all the design features that are different from the existing design, then the part of the design features not contained will make it

obviously different from the authorized design in the overall visual effect. In this case, it can be generally presumed that the disputed infringing design and the authorized design do not constitute an approximation.

Since the design features of authorized designs have a greater weight in the determination of infringement, the determination of design features thus often becomes one of the focuses of dispute among all parties involved in disputes over infringement of design patents. In general, the patentee knows best the design features of his authorized design, and he often claims that the design of the disputed infringing design adopts the design features of the authorized design. In this regard, according to the general rules of evidence "the burden of proof rests on the party who alleges", the patentee should first bear the burden of proof for the design features of the authorized design. In addition, the design features of the authorized design may be recorded in the relevant application and review documents of the patent authorization process, such as the brief description of the patent application document, or the document of the invalidation request review decision, etc. These documents are important for the determination of design features. Meanwhile, due to the limitations of the search database, the limitations of the search capabilities, etc., the design features in the record may not be derived from the search of the entire existing design. Therefore, in the case of any objection by the other party, they should be allowed to provide counter-evidence. In this case, Grohe AG has claimed that the design features of the runway-shaped water surface shall be its design patents, the petition for announcing null and void the design patent in the case was made by a comparison with the existing design document recorded in the documents, Grohe AG holds the view that their feature enjoys the patent right for the design in dispute. But the Jianlong Sanitary Ware Company disagrees. However, upon repeated request by the court, Jianlong Sanitary Ware Company still fails to submit evidence that the runway surface is its current design. Therefore, after hearing the opinions of the parties, the court thoroughly examines the evidence in the case and determines in accordance with the law and that the runway-like water surface is the design feature of the patent design.

2. **Issue on functional design features of the design**

In patent law, the design is based on industrial products, which must first meet specific functional requirements. Therefore, the design will be subject to the specific functions required for industrial products, resulting in functional design features. For functional design features, Article 11(1) of the *Interpretation of Patent Infringement Disputes* provides that when the people's court finds whether the designs are identical or similar, the design features determined by technical functions shall not be considered. Accordingly, in a dispute over infringement of a design patent, the sued infringer often claims that one of the distinguishing design features between the disputed infringing design and the authorized design in dispute is a functional design feature, which will not be considered in the infringement comparison. In general, there are two forms of functional design features of a design. One is a design that is only determined by a specific function, which is not related to aesthetics and not selective in terms of decoration. The other is one of many designs that can realize specific functions. Although the design is optional in decoration, it is determined by the

specific functions to be realized by the product and is also independent of aesthetics from the perspective of the general consumers for design products. Therefore, the functional design feature is not determined by whether the design is not selective due to functional or technical constraints, but rather that it does not seem to be decorative for the general consumer for design products. According to the above judicial interpretation, the above-mentioned two forms of functional design features are not included in the scope of the infringement comparison.

In judicial practice, there is another design feature that is closely related to functional design features, which is the most aesthetically pleasing design chosen by the designer in a variety of designs that implement product-specific features, based on a certain aesthetic need. From the view of the general consumer of design products, this design feature not only realizes the specific functions of the products, but also meets the visual aesthetic needs. Therefore, this design feature is related to aesthetics and does not belong to functional design features. This functional and decorative design feature shall be included in the scope of the infringement comparison. When determining the influence of functional and decorative design features on the overall visual effect of design products, the strength of decoration should be considered: the stronger the decoration, the greater the influence on the overall visual effect; the weaker the decoration, the smaller the impact on the overall visual effect. In this case, the court of the second instance determines the runway-like push button set on the handle of the authorized design product as a functional design feature, which will not be considered in infringement comparison. And this determination has ignored the decorative attention of the general consumers who buy the shower head when they see the push button. The designer of the authorized design chose to design the push button of the handle position as a racetrack so as to coordinate with the runway-like water surface to increase the overall aesthetics of the product. Therefore, the push button should be regarded as a functional and decorative design feature. In the infringement comparison, the influence of the decorative visual strength on the overall visual effect of the shower head product is judged according to the decorative strength.

3. **Issues Worthy of Mention During the Application**

Article 11 of the *Interpretation of Patent Infringement Disputes* provides that when the people's court finds whether the design is identical or similar, it shall make a comprehensive judgment based on the overall visual effect of the design in accordance with the design features of the authorized design and the design of the disputed infringement. If there is no difference in the overall visual effect between the design of the disputed infringement and the authorized design, the people's court shall find that the two are identical with each other; if there is no substantial difference in the overall visual effect, the two should be considered similar. In case of that, in the trial of patent infringement disputes of design patents, the principle of infringement comparison of "holistic observation and comprehensive judgment" shall be strictly adhered to. The above considerations for the innovative design features and functional design features of the design in the infringement judgment are to determine the weight of the feature on the overall visual effect of the design product,

and whether the disputed infringing design and the authorized design constitute the same or approximate judgment should still be based on the principle of "holistic observation and comprehensive judgment".

It shall also be noted that in the design infringement comparison principle, the objective of "holistic observation" is the overall design features of the design, including innovative and non-innovative design features. The distinctive design features of the disputed infringing design and the authorized design other than the innovative design features not claimed by the patentee and the non-innovative design features should be considered. But different design features have different weights in 'comprehensive judgment". For example, innovative design features have a more significant impact on the overall visual impact of the design product. And the appearance of the product displayed by the authorized picture are based on the design patent protection, and functional design features are excluded from the consideration of "comprehensive judgment". Finally, on the basis of examining the influence of all design features on the overall visual effect of the design, the difference or substantive difference of the overall visual effect of different design is judged comprehensively, so as to make the determination of infringement. The second instance judgment of this case focuses on the innovative design features of the runway-like surface of the authorized design, but the main reason for its erroneous application of law is that other innovative design features of the authorized design, as well as the different design features of the disputed infringing design and the authorized design, which are easily directly observed in other parts of shower nozzle products during normal use, are not considered. In addition, it shall be pointed out that as the design is based on industrial products, the improvement of its design level shall depend on the influence of aesthetics and the advancement of industrial technology. With the improvement of the technology, more and more design options can be selected to achieve specific functions, leaving design space larger and larger. Therefore, the specific design features of a particular product may develop from functional technical features to functional and decorative design features under different technical conditions. The court may make a different determination when considering the impact on the overall visual effects of the design products.

Beijing Long-Young Technology Co., Ltd. v. Wuhan Sanyuan Special Building Materials Co., Ltd. (Disputes over Unfair Competition)—The Difference Between "Unique Name of a Well-Known Commodity" and "Distinctiveness of a Trademark"

Xia Luo

Rule

The requirement of Article 9 of the *Trademark Law* about the distinctiveness in applying for a registered trademark is that it can be the source to identify the commodity. In the Article 5(2) in the *Anti-Unfair Competition Law* (in this article it refers to the *Anti-Unfair Competition Law* before amendment in November 4, 2017), the name specifiability of a well-known commodity means the reality to distinguish the source of commodities. And It emphasizes that the name, packaging, and decoration have played a role in distinguishing the source of goods through commercial use. The focus of the review is on the actual commercial use. The identification of the exclusive right to use a trademark does not necessarily prove that the logo has obtained the distinctiveness or the specificity as provided in Article 5(2) of the *Anti-Unfair Competition Law*.

Collegial panel judges of the Supreme People's Court for re-trial: Zhou Xiang, Luo Xia and Tong Shu (Written by: Luo Xia, Supreme People's Court; Translated by: Sun Lin, Zheng Yi).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_33

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellant in second instance): Beijing Long-Young Technology Co., Ltd. (hereinafter referred to as "Long-Young Technology Company")
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): Wuhan Sanyuan Special Building Materials Co., Ltd. (hereinafter referred to as "Sanyuan Special Building Materials Company")

2. Procedural History

First Instance: No. 03179 [2015], Trial, IP Division, the Intermediate People's Court of Wuhan (dated Jul. 17 of 2015)
Second instance: No. 00621 [2016], Final, Civ. Division, the Higher People's Court of Hubei (dated Jun. 9 of 2016)
Application for retrial: No. 3693 [2017], Retrial, Civ. Division, the Supreme People's Court (dated May 22 of 2017)

3. Cause of Action

The dispute over unfair competition

Essential Facts

The FS101 and FS102 underground rigid composite waterproof technology has been reported as the core content of this project has not been reported at home or abroad by the Science and Technology Information Center in Heilongjiang Province on September 12, 2006. On September 30, 2006, Beijing Urban Construction Science and Technology Promotion Association provided an evaluation conclusion as follows: "The technology is the first innovation and at the leading level in China thus can be applied". On December 14, 2006, it was incorporated into the *National Science and Technology Achievements Promotion Project of the National Construction Industry in 2006 by the Ministry of Construction Science and Technology Development Promotion Center*, and is subsequently included in the "Technology and Commodity Selection Manual" of the "Eleventh Five-Year Plan for Construction Project". On February 28, 2008, Long-Young Technology Company obtained all the intellectual property rights and other related rights of the technology and FS101 mortar waterproofing agent and FS102 concrete waterproofing and compacting agent. After that, the technology was incorporated into the *National Building Energy Efficiency Project Summary and New Technology and New Product Selection Manual*, and was awarded 'Building Energy Conservation Recommended Brand', which was promoted as the national real estate development unit and architectural design unit, and also listed in *Selection Catalogue*

of National Green Building Materials during the Twelfth Five-year Plan and *2014 National Engineering Construction Standard Technology and Product Application Catalogue*. The national standard of the People's Republic of China, *Technical Code for Waterproofing of Underground Works* (GB50108-2008) and *Acceptance of Construction Quality of Underground Waterproof* (GB50208-2011) have recorded and introduced the said technology. The FS102 concrete waterproofing and compacting agent products produced and sold by Long-Young Technology Company, which have won the "National Real Estate General Engineer Architectural Design Selection and Selection Brand in 2009" "Shanghai World Expo Construction Project Energy Conservation and Environmental Protection New Materials (System) in 2010" "The National Real Estate General Manager's preferred brand products in 2010", "National Real Estate General Manager's Preferred Brand Products in 2011" and other honorary titles, are included in the "Property Housing Construction Materials Parts Purchasing Information Platform" by the Housing and Urban-Rural Development Department Housing Industrialization Promotion Center. Long-Young Technology Company has signed a distribution agreement with several building materials companies for FS101 mortar waterproofing agent and FS102 concrete waterproofing agent. Established on May22, 2001, Sanyuan Special Building Materials Company manufactures and sells concrete admixtures, mortar, concrete waterproofing and waterproof building materials, meanwhile it contains technology promotion services. Sanyuan Special Building Materials Company uses the registered trademarks No. 3624234 and No. 9527424 on products it produces and sells. On September 2014, at the site of the renovation project of a shantytown in Songshuping, Enshi, a large number of products was found to be produced by Sanyuan Special Building Materials Company which are printed and sold with the words FS101 waterproof cement mortar. On the same day, in the commercial production site of Yuxin Building Materials Co., Ltd., Qifeng Building Materials Co., Ltd. and Qilong Building Materials Co., Ltd., a large number of products FS102 compact concrete waterproofing agent were produced and sold by Sanyuan Special Building Materials Company.

Then, Long-Young Technology Company has brought a lawsuit to the court and request Sanyuan Special Building Materials Company to immediately stop the unfair competition by using the product name of FS101 waterproof mortar, FS102 compact concrete waterproofing agent, and to stop selling the products containing the product name, and to destroy all packaging materials and other materials and articles containing the name of the commodity, and to publish a statement in the national well-known media, acknowledging the infringement and making apologies to Long-Young Technology Company, and to compensate for economic losses of RMB 3,150,000. Sanyuan Special Building Materials Company argued that: FS101 mortar waterproofing agent and FS102 dense concrete waterproofing agent have become the generic name of waterproofing agent in the industry. Sanyuan Special Building Materials Company sells its own commodity, which does not constitute an infringement on the unique name of Long-Young Technology Company.

The court of the first instance rendered a judgment on July 17, 2015, dismissing all the claims of Long-Young Technology Company. Not satisfied with the judgment

of the court of first instance, Long-Young Technology Company lodged an appeal and the court of second instance rendered a judgment on June 9, 2016, dismissing the appeal and affirming the original judgment.

Long-Young Technology Company then appealed to the Supreme People's Court for retrial.

The main reasons for Long-Young Technology Company to apply for retrial are as follows: The first and second instances have determined that FS101 mortar waterproofing agent and FS102 concrete waterproofing agent do not constitute well-known commodities, and FS101 and FS102 do not constitute unique names, which are erroneous in fact-finding. The use of FS101 and FS102 trade names on mortar and concrete waterproofing agent products by Sanyuan Special Building Materials Company is a counterfeit to the unique name of Long-Young Technology Company. The acquisition of the registered trademarks of FS101 and FS102 by Long-Young Technology Company on April 29, 2016 can prove that FS101, FS102 and FS are distinctive and can distinguish commodities. Without permission, Sanyuan Special Building Materials Company has used the same unlicensed trademarks and registered trademarks of Long-Young Technology Company on the same products prominently as Long-Young Technology Company, which constitutes an infringement of trademark rights. To sum up, Long-Young Technology Company filed a petition, pleading the Court to dismiss the judgment of the court of second instance, to issue an order for retrial, and to find in favor of its claims.

Issue(s)

Whether Sanyuan Special Building Materials Company has conducted the unfair competition conduct of unauthorized use of the unique name of another well-known commodity? The key is to determine whether the name of the commodity has the exclusive right to to be used on the granted trademark can mean that the name is a unique name, or whether that is sufficient to prevent others from using the name.

Holding

Upon review, Supreme Court holds that the acquisition of trademark registration by Long-Young after the second instance judgment can not be brought to a direct conclusion that FS101 and FS 102 can satisfy the conditions of protection for the unique names of well-known commodities. The acquisition of identification of the trademark right itself cannot prove that the logo has obtained the distinctiveness of Article 5(2) of the *Anti-Unfair Competition Law* through use. The indistinguishable using method of FS101 and FS102 as technical names or product names by Long-Young Technology Company, prevents the public from establishing a connection between

the product name and the specific producer or provider. In the case where a plurality of producers provide corresponding commodities suitable for implementing the promotion of technology, the product names of FS101 and FS102 cannot identify or correspond to the specific producer, thus distinguishing from similar products of other operators. The conclusions of the first and second instance courts that FS101 and FS102 do not constitute a unique name are correct and shall be affirmed. Sanyuan Special Building Materials Company used its No. 9527424 graphic trademark and No. 3624234 text and graphic combination trademark in FS101 waterproof cement mortar and FS102 compact concrete waterproofing agent it produces and sells. And the methods of use clearly point to the producer of the commodities. Long-Young Technology Company alleged to Sanyuan Special Building Materials Company that Sanyuan it has taken advantage of the reputation of Long-Young Technology Company, intentionally causing confusion or misunderstanding among the consumers, the claim is impossible to support due to the malicious behavior of the conductor. The judgments made in the first and second instances that Long-Young Technology Company's allegations of unfair competition against Sanyuan Special Building Materials Company are untenable, and the conclusions are correct and shall be affirmed. In the end, the Supreme People's Court rules to dismiss the application for retrial of Long-Young Technology Company.

Comment on Rule

1. **The influence of well-known technology on determing a well-known commodity**

In terms of the characteristics of intellectual property, the International Association for the Protection of Industrial Property divides the intellectual property into creative and discerning mark rights, and the latter dealing with trademarks, trade names, geographical indications and the right to identify marks in the *Anti-Unfair Competition Law*. The identification mark refers to the external manifestation of the enterprise and its commodities (services). The identification mark is intended to recognize its own entity through its distinctive appearance characteristics and personality, and to convey clear information to the public and other companies, thus distinguishing from other enterprises and their activities and commodities (services).[1] There are regulations of the counterfeiting of commercial marks by trademarks and commercial subject marks respectively in Article 5(1)(i), (ii), and (iii) of *China's Anti-Unfair Competition Law*, and the subsection (ii) refers to the name of the commodities, packaging, decoration, that is, the terms of the dispute in this case. In general, a commodity with certain reputation, its unique name packaging and decoration may establish contact with the provider and manufacturer of the commodity, and distinguish it from other commodities and services, with the role of distinguishing the source of commodities.

[1] Xie Xiaoyao: *On the Protection of Competition Law for Identification Marks*, in *Law Review*, Vol. 3, 2000.

The special name, packaging and decoration of these commodities with the function of identification the source of the commodity can be protected to prevent counterfeiting. Being well-known is an important threshold for applying Article 5(2) of the *Anti-Unfair Competition Law*. Pursuant to provisions of the *Interpretation of Unfair Competition Civil Cases*, when determining the popularity of the commodities, it is necessary to consider the time, region, object and sales of the commodities, and the duration, extent and scope of territory. Determining the popularity means the certain popularity among the public but not requiring the relevant public to be widely known. In comprehensively judging these factors, when a factor is sufficient to prove the popularity of the commodity, it can be determined in accordance with this factor on whether it constitutes a well-known commodity, and it is not necessary to consider all the factors. With certain popularity among the relevant public, the technology was used to produce corresponding commodity. The popularity of the technology will inevitably reflect the cognition of the relevant public on the popularity of the commodity because the commodity can reflect the specific technology. In this case, the underground rigid composite waterproof technology of Long-Young Technology Company has certain popularity, based on which, the commodities have specific composite waterproof technology performance. Moreover, in the publicity report on the promotion and application of this technology, the corresponding commodities are FS101 mortar waterproofing agent and FS102 concrete waterproofing and compacting agent requested for protection by Long-Young Technology Company in this case. Therefore, the correspondence between technology and commodities, a technical scheme and physical objects, enables the fact that technology has popularity to be mapped to the popularity of commodities. After comprehensive identification, the commodities that Long-Young Science and Technology Company requests protection should be identified as well-known commodities.

2. **Potential problems caused by abuse of technical names and commodity names**

The popularity of technology will generally drive the great sales of the corresponding commodities. Therefore, the promoters of the technology often use the name of the commodities and the name of the technology in business, so as to accelerate the popularity and the sales of the commodities. However, this business strategy has potential legal risks when claiming that the name of commodity is unique. In this case, FS101 and FS102 underground rigid composite waterproof technology is a technology with certain popularity. And Long-Young Technology Co., Ltd. has invested a large amount of capital in research, development, evaluation, declaration, transfer and promotion of the technology. Long-Young Technology Co., Ltd. holds that the product related to the technology is a well-known commodity and the name of the commodity is a unique name. And it also claims that the unauthorized use of the well-known name of a well-known commodity constitutes an unfair competition. After review, although Long-Young Technology Co., Ltd. once marks the 'Han Wu Si Da' registered trademark on its products for production and sales, in the subsequent operations, it does not intend to distinguish the name of the rigid composite waterproof technology from the name of the goods involved. A large amount

of evidence submitted by Long-Young Technology Co., Ltd. to prove the promotional materials, honors and sales of the unique names of well-known products show that: there are mixed or alternative use in the actual operation among FS101 mortar waterproofing agent, FS102 concrete waterproofing agent trade name and FS101, FS102 underground rigid composite waterproof technology. In the distribution contract between Long-Young Technology Co., Ltd. not being a party in the case, there are also the facts that the technical names FS101 and FS102 refer to FS101 mortar waterproofing agent and FS102 concrete waterproofing agent respectively. Long-Young Technology Co., Ltd. also continues to advocate when applying for retrial, FS101, FS102 is the abbreviation of FS101 mortar waterproofing agent and FS102 concrete waterproofing agent. The facts of this case prove that Long-Young Technology Co., Ltd. has not intended to distinguish the product name from technical name in the production and operation, and it has intentionally mixed the two. The dispute in this case was caused by the way of using it. Therefore, the key aspect for the review is to determine whether no distinction between the name of technology and the name of commodities in actual business operations can have certain effect on the distinctiveness of the source of the product.

(1) The holder of the new technology does not have exclusive rights to the name of the technology.

The promotion and application of new technologies will help the promotion of the transformation of scientific and technological achievements into real productivity, provide technical support for economic and social development, and achieve a better market effect. In the promotion and application of technology, the holder of the technology does not have exclusive rights to the name of the technology. In the production and operation, the technical implementer cannot reasonably mark, explain, and express the objective requirements of the technical name. In this case, the FS101 and FS102 underground rigid composite waterproof technology, through the positive promotion by Hanwusida Company and Long-Young Technology Co., Ltd., it was listed as the National Construction Industry Science and Technology Achievement Promotion Project by the Ministry of Construction Science and Technology Development Promotion Center as early as December 14, 2006. The above-mentioned technologies have been recorded and introduced in the national standards related to the underground engineering waterproofing technology and the engineering quality acceptance specifications, and the relevant departments have also notified the qualified regions and engineering projects to give priority to the use of this technology. As in usual, manufacturers who wish to use FS101 and FS102 underground rigid composite waterproof technology must express or mention the name of the technology in actual operation. On the one hand, it is necessary to accept the quality inspection of the relevant departments. On the other hand, it is necessary to inform public that the products implementing the technology are different from the existing products and have performance. Therefore, the promotion of the underground rigid composite waterproofing technology of FS101 and FS102 has led to the emergence of the

objective behavior of the technical implementer to mark and express the technical name, which will inevitably make it difficult to correspond to a specific commodity producer only by the technical name.

(2) The identification function of the product name shall be weakened or even be offset because of the use of the identical name by an unspecified number of technical implementers

To determine the distinctiveness of a commercial identity, it usually takes into account the understanding of the public in the use of the commodity. If the public identifies the product name as a kind of commodity, and when the commodity is provided by a plurality of producers, it is difficult for the public to distinguish the source of the commodity only by the name of the commodity. The name of the technology and its product name are mixed and used alternatively, which leads to difficulties in the popularity of the technology and a weakening of the identification function of the product name, which means that the two are inversely proportional to each other. The wider the scope of technology being promoted and applied, the more difficult it is for the public to rely on the name of the product to match a specific producer or provider, and to establish a connection with the source of the commodity. For example, in this case, the public's knowledge of the names of FS101 and FS102 is not only a waterproof product with excellent performance brought by a new type of technology, but also a key technical project for promotion and application in the industry. With the promotion and application of FS101 and FS102 underground rigid composite waterproof technology, a manufacturer of Long-Young Technology Co., Ltd. implements the composite waterproof technology, and the market structure for producing and selling relative products has changed. In the case that a plurality of producers provides the commodities suitable for implementing the promotion technology, the product names that rely solely on FS101 and FS102 cannot be identified and matched with the specific producer, and are distinguished from similar products of other operators. Through a review of the facts in this case, it is to be recognized that the indistinct use method of Long-Young Technology Co., Ltd. for FS101 and FS102 as technical names or product names, reduces the recognition function of FS101 and FS102 as commodity names, and impedes the public from linking the name of the product to a particular producer or provider, loses the meaning of being unique as a well-known commodity.

3. Whether the fact of obtaining trademark registration exert any influence upon the well-known commodities' peculiarity

Standards for determining the identification of the peculiarities are specified in Article 5(2) of the *Anti-Unfair Competition Law*, this peculiarity is the distinctiveness or distinction of name, packaging, and decoration. It emphasizes the peculiarities that can be used to indicate a particular source of business through commercial use. If a mark that is significant in itself has not been used commercially, it cannot be proved that it has become a unique name for a well-known product. Thus, the protection cannot be granted by citing the provisions of Article 5(2) of the *Anti-Unfair Competition Law.* China's trademark registration system adopts the first application first

system. The *Trademark Law* does not require trademark applicants to submit evidence for actual use when submitting an application for registration. Therefore, there is a difference in the determination of the factual basis between the distinctiveness of the trademark and the specificity of the unique name of the well-known commodity. The requirement of Article 9 of the *Trademark Law* for a registered trademark to be distinctive lies in the fact the source of the commodity can be identified. The specificity provided in Article 5(2) of the *Anti-Unfair Competition Law* means the reality to distinguish the source of goods, which emphasizes that through commercial use of the name, packaging, and decoration, the source of the commodity can be distinguished objectively. And therefore, the focus for the court's review is on the actual commercial use. Therefore, the identification of the trademark right itself does not prove that the logo has obtained the specificity or peculiarity provided in Article 5(2) of the *Anti-Unfair Competition Law*. In the present case, Long-Young Technology Co., Ltd. submits the trademark registration certificate of FS101 and FS102 after the judgment of the second instance and thus claims that the product name has its own peculiarity. And the Supreme People's Court does not maintain Long-Young Technology's claim that FS101 and FS102 product names are peculiar or specific.

Beijing Qihoo Technology Co., Ltd. v. Tencent Technology (Shenzhen) Co., Ltd. and Shenzhen Tencent Computer System Co., Ltd. (Dispute over the Abuse of Market Dominant Position)—Analysis Methods and Ideas for the Definition of the Relevant Markets and the Abuse of Market Dominant Position in the Internet Environment

Li Zhu

Rule

In the lawsuit involving abuse of market dominance position, the definition of the relevant market is a tool for assessing the market power of the operator and the impact of the alleged monopolistic behavior on the competition. And the definition of the relevant market is not the purpose in or of itself. If the direct evidence can be given to exclude or obstruct the competition and the market position of the operator and the market impact of the alleged monopolistic behavior can be assessed, then there is no need to clearly define the relevant market in every case of abuse of market dominance position.

Hypothetical Monopolist Test (HMT) is a generally applicable analytical approach to define the relevant markets. In practice, Hypothetical Monopolist Test (HMT) can be performed by *Small but Significant Non-transitory Increase in Price* (SSNIP) or *Small but Significant Non-transitory Decrease in Product Quality* (SSNDQ). The free features of Internet instant messaging services make users sensitive to a high price. As a test method of rising prices will lead to a broad definition of the relevant market,

Collegial panel judges of the Supreme People's Court for re-trial: Wang Chuang, Wang Yanfang, Zhu Li (Written by: Zhu Li, Supreme People's Court; Translated by: Sun Lin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_34

the qualitative analysis should be conducted by using a hypothetical monopolist test with reduced quality.

As for the low cost and high coverage of Internet instant messaging services, when defining the relevant geographical market, comprehensive assessment should be carried out according to such factors as the actual area of the commodity selected by the demander, the provisions of laws and regulations, the status of overseas competitors and the timeliness of entering the relevant geographical market.

In the Internet sector, market share is only a rough and potentially misleading indicator for judging market dominant position. Its position and role count on the specific circumstances of the case when determining the market dominance.

Case Information

1. **The Parties**

Appellant (Plaintiff in the first instance): Beijing Qihoo 360 Technology Co., Ltd. (hereinafter referred to as the "Qihoo Technology Company")
Appellee (Defendant in the first instance): Tencent Technology (Shenzhen) Co., Ltd. (hereinafter referred to as the "Tencent Technology Company")
Appellee (Defendant in the first instance): Shenzhen Tencent Computer System Co., Ltd. (hereinafter referred to as the "Tencent Computer Company")

2. **Procedural History**

First instance: No. 2 [2013], Trial, Civ. Division, the Higher People's Court of Guangdong Province (dated Mar. 20 of 2013)
Second instance: No. 4 [2014], Final, Civ. Division, the Supreme People's Court (dated Oct. 8 of 2014)

3. **Cause of Action**

Dispute over the abuse of market dominant position

Essential Facts

The Qihoo Technology Company claimed in the first instance: The Tencent Technology Company and the Tencent Computer Company had a market dominant position concerning instant messaging software and service market. On November 3, 2010, the Tencent Technology Company and the Tencent Computer Company released the *Letter to QQ Users*, explicitly prohibiting their users from using the 360 software developed by the Qihoo Technology Company. Otherwise it would stop such users from accessing QQ software services, or would refuse to provide related software services to 360 users, so as to force users to delete 360 software, and adopt technical means to prevent users who have installed the 360 Security Browser from

accessing QQ space. During this period, a large number of users deleted the software developed by the Qihoo Technology Company. The above behaviors of the Tencent Technology Company and the Tencent Computer Company constituted a restriction on transaction. In addition, the Tencent Technology Company and the Tencent Computer Company prohibited the Tencent PC Manager (previously named the "QQ software manager") with its instant messaging software QQ, and forced users to install QQ Doctor in the name of upgrading the Tencent PC Manager, thus forming a bundling sale. The Tencent Technology Company and Tencent Computer Company jointly abused their market dominant position, which caused damage to the Qihoo Technology Company, so the two companies should bear joint and several liabilities. To sum up, Plaintiff requested the Tencent Technology Company and the Tencent Computer Company: 1) to immediately stop the alleged monopolistic behavior; 2) to jointly compensate the Qihoo Technology Company for an economic loss of RMB 150,000,000; 3) to apologize to the Qihoo Technology Company; and 4) to assume the reasonable expenses of RMB 1,000,000 that the Qihoo Technology Company has paid for rights protection.

The Tencent Technology Company and the Tencent Computer Company jointly made a defense that Qihoo Technology Company misdefined the relevant market because the two defendants did not have a market dominant position in the instant messaging service market. So the alleged monopolistic behavior did not constitute an act of abusing the market dominant position, nor did it have the effect of restricting competition. Therefore, the two defendants requested the Court to dismiss all claims of Qihoo Technology Company.

The Guangdong Provincial Higher People's Court of Guangdong Province made a judgment on March 20, 2013. The Court made a judgment: (1) The issue of the defining the relevant market. The Qihoo Technology Company claimed that the comprehensive instant messaging services constituted an independent commodity market and that the relevant geographical market in this case should be the Chinese mainland market, which cannot be established. The relevant commodity market involved in this case far exceeded the comprehensive instant messaging service market, and the relevant geographical market should be the global market. However, the Higher People's Court of Guangdong Province did not clearly define the scope of the relevant commodity market. (2) The issue of the determination of market dominant position. Because the Qihoo Technology Company mis-defined the relevant commodity market in this case, the evidence provided was insufficient to prove that the Tencent Technology Company and the Tencent Computer Company had a monopoly position in the relevant commodity market. (3) Because it was impossible to prove that the Tencent Technology Company and the Tencent Computer Company had a monopoly position in the commodity market, the claim raised by Qihoo Technology Company that the Tencent Technology Company and the Tencent Computer Company abused their market dominant position lacked factual and legal basis, so it cannot be established. The Court decided to dismiss all claims of the Qihoo Technology Company.

The Qihoo Technology Company refused to accept the judgment of first instance and filed an appeal. The Supreme People's Court on October 8, 2014 rendered a judgment to dismiss the appeal and affirm the original judgment.

Issues

(1) How to define the relevant market in this case?
(2) Whether the Tencent Technology Company and the Tencent Computer Company had a market dominant position? and,
(3) Whether the Tencent Technology Company and the Tencent Computer Company constituted such abuse of market dominant position as prohibited by the *Anti-Monopoly La*w?

Holding

Upon review, the Supreme People's Court holds that:

1. **Ways to define the relevant market**

(1) The court of first instance did not have a clear determination about whether the definition of the relevant commodity market was true. In the case trial of abusing market dominant position, defining the relevant market is a tool for assessing the market influence of operators and the impact of the alleged monopolistic behavior on competition, rather than the end. It is not the case in determining the abuse of market dominant position that the relevant market has to l be clearly and definitively defined. In this case, the court of first instance has actually tried to define the relevant commodity market. However, due to the ambiguous boundary of the relevant market, the court of first instance only analyzed the possibility of its boundary without giving a clear definition. So we cannot say that the court of first instance made an improper determination about the basic fact.
(2) Whether the case was suitable for using the method of "hypothetical monopolist test" (hereinafter referred to as the "HMT") to define the relevant market and whether the HMT was applied correctly by the court of first instance. As an analytical approach to defining the relevant market, the HMT has a universal applicability. Under the background where the free Internet-based instant messaging service has long existed and became a popular business model, users have a very high sensitivity to price, so changing the free strategy to charge even a small amount of fees may result in a large loss of users. In this case, adopting the HMT which is based on a relative price increase is likely to include commodities that do not have a substitution function into the scope of the relevant market, rendering the definition of the relevant market a rather broader concept. Therefore, the application of the HMT which is based on a relative price increase was not suitable in this case. Therefore, that the court of first instance directly used the SSNIP test which features a relative price increase was improper.
(3) Whether non-comprehensive instant messaging services such as text, audio and video should be included in the relevant commodity market in this case. From

the perspective of product characteristics, instant messaging services with only one or two functions have almost the same characteristics as the comprehensive instant messaging services. Based on the Internet, both kinds of services are free and capable of detecting user's online position, and carrying out instant communication and private communication. From the perspective of the availability of commodity, three services are easily available for free from the Internet. From the perspective of the functional use of commodity, they all have at least one totally identical function. From the perspective of supply substitution, operators providing non-comprehensive instant messaging services can easily switch to providing comprehensive and integrated instant messaging services. Therefore, non-comprehensive instant messaging services such as text, audio and video should be included in the scope of relevant commodity market in this case.

(4) Whether mobile instant messaging services should be included in the scope of relevant commodity market. When the alleged monopolistic behavior in this case occurred, the mobile instant messaging services and the personal computer instant messaging services became basically identical in terms of product characteristics, quality, functional use, access channels, etc., and mobile instant messaging services were prospering and formed a relatively large scale. So the mobile instant messaging services should be included in the scope of relevant commodity market in this case.

(5) Whether social networking sites and Weibo services should be included in the scope of relevant commodity market. When compared with social networking sites and Weibo, instant messaging has significant differences in terms of product characteristics. Social networking sites and Weibo are mainly aimed at open group communication among a large number of users, so their requirement for instantaneity is relatively low, while instant messaging pays more attention to bilateral private communication or internal communication of small groups, which is a closed circle to some extent, so instant messaging has a relatively high requirement for instantaneity. When compared with social networking sites and Weibo, instant messaging is also different in terms of main functions. The main function of instant messaging is for chatting, while social networking sites and Weibo features a more prominent social function. From the perspective of demanders, instant messaging is more of a complementary tool to social networking sites and Weibo, rather than a substitution. The court of first instance determined that social networking sites and Weibo should be included in the scope of relevant commodity market in this case, which was an error. Actually, social networking sites and Weibo should not be included in the scope of relevant commodity market in this case.

(6) Whether the mobile phone messaging and e-mail should be included in the scope of relevant commodity market. There is a relatively big difference in the functions and feature between the instant messaging and the mobile phone messaging for the instant messaging is free, while the mobile phone messaging charges a fee. E-mail and instant messaging have great differences in terms of core functions and feature. E-mail does not have the instantaneity of communication, nor does it have the function of notifying the online position of users. The

instantaneity of communication is the core of instant messaging services and the function that is most attractive to uses. Therefore, there is no close substitute relationship among instant messaging, e-mail and mobile phone messaging, so mobile phone messaging and e-mail should not be included in the scope of relevant commodity market in this case. It was correct that the determination of the court of first instance about that mobile phone messaging and e-mail should not be included in the scope of relevant commodity market scope in this case.

(7) Whether the relevant commodity market in this case should be determined as the Internet application platform. The Supreme People's Court held that, it should be concerned whether the appellee used its possible market dominant position in the field of instant messaging to exclude and restrict competition in the field of Internet security software, and extended its possible market dominant position in the field of instant messaging to the field of security software, in which the competition occurred more for free clients. Therefore, the Supreme People's Court would no longer consider the competitive characteristics of Internet platform during the process of defining the relevant market in this case, but would consider it when identifying the market position and market power of the operators.

(8) Issues of defining the relevant geographical market. First of all, most users in the Chinese mainland choose to use instant messaging services provided by operators in the scope of the Chinese mainland. Secondly, China implements an administrative licensing system for value-added telecommunications services, such as instant messaging. Foreign operators usually cannot directly enter into the Chinese mainland and operate relevant business, but need to obtain the corresponding administrative license and enter the Chinese market in the form of Sino-foreign joint ventures. Thirdly, before the alleged monopolistic behavior happened, most major international instant messaging operators have entered the Chinese mainland market in the form of joint ventures. Finally, it is difficult for overseas instant messaging service operators to enter the Chinese mainland in a short period of time (such as one year) and develop to the size big enough to restrict the development of domestic operators. Based on the above-mentioned factors, the relevant geographical market in this case should be the Chinese mainland market. The definition of the court of first instance about the relevant geographical market in this case was not proper and should be corrected.

(9) Whether defining the relevant market in the case needs to consider the relevant market conditions and technological development trends after the occurrence of the proceeding. Since competition, especially in the cyber space, is characterized by dynamic factors, when defining the relevant markets, it is necessary to consider the market response and change that are really possible to happen in the foreseeable future, in order to correctly judge whether the competition in the relevant market is subject to the restriction of competition from operators in another field. In this case, the court of first instance considered the development position and future trends of Weibo and social networking sites when analyzing whether Weibo and social networking sites belong to the scope of

relevant commodity market in this case. This thread of such ideas itself was not inappropriate.

To sum up, the relevant market in this case should be defined as the instant messaging service market in the Chinese mainland, including PC instant messaging services and mobile instant messaging services, and comprehensive instant messaging services and non-comprehensive instant messaging services such as text, audio and video.

2. **Whether the Tencent Technology Company and the Tencent Computer Company were in a market dominant position**

In this case, although the Tencent Technology Company and the Tencent Computer Company had a market share of more than 80% in both the PC and mobile instant messaging service markets, it was too early to draw a conclusion based solely on their market share. Other factors need to be considered.

(1) Issues of the competition in the field of instant messaging in the Chinese mainland. When the alleged monopolistic behavior happened, there were dozens of instant messaging tools in the field of instant messaging in the Chinese mainland, and the stability and services of these products was becoming more mature as users are growing. Around that time when the alleged monopolistic behavior happened, more and more companies with different backgrounds and technologies have entered the field of instant messaging. In particular, the mobile instant messaging developed rapidly. With the new mobile instant messaging service operators continuously entering the market, new impetus was brought to the instant messaging industry. The competition in the field of instant messaging presented the distinctive features of innovative competition and dynamic competition, and platform competition was becoming increasingly acute. It could be seen that the market competition in the field of instant messaging was relatively sufficient.

(2) Issues of the capacity of the Tencent Technology Company and the Tencent Computer Company to control commodity price, quantity or other transaction conditions. First of all, since the instant messaging services provided by the instant messaging service operators to the users were free of charge and the users lacked the willingness to pay a fee, it was impossible for any instant messaging service operator to have the ability to control the price charging from the users. Secondly, the Tencent Technology Company and the Tencent Computer Company did not have the ability to control the service quality. If the appellee lowered the quality of service, a large number of users would have switched to other instant messaging services. In addition, the competition characteristics of Internet platform also restricted the ability of the appellee to control the service quality. Finally, the Tencent Technology Company and the Tencent Computer Company also did not have the ability to control the commodity quantity and other transaction conditions. To sum up, the Tencent Technology Company and the Tencent Computer Company had a relatively

vulnerable ability to control the commodity price, quality, quantity or other transaction conditions.

(3) Issues of the financial and technical conditions of the Tencent Technology Company and the Tencent Computer Company. Many competitors in the field of instant messaging in the Chinese mainland had a strong strength in finance and technology, and were powerful enough to influence the leading market role of the Tencent Technology Company and the Tencent Computer Company. In addition, the innovation in the field of instant messaging was active, while the demands for technology and cost were relatively low. So the impact of technical and financial conditions on market power was not significant. Therefore, the financial and technical conditions of the Tencent Technology Company and the Tencent Computer Company had a very limited impact on their market power.

(4) Issues of the degree of dependence of other operators on the Tencent Technology Company and the Tencent Computer Company. The Tencent QQ developed by the Tencent Technology Company and the Tencent Computer Company was not a necessity for users when needing instant messaging services. There were many types of instant messaging software that could be selected by users, and the cost of acquiring instant messaging software and services was low, so there were no significant economic or technical obstacles that prevented users from selecting or switching instant messaging services. Even if the Tencent Technology Company and the Tencent Computer Company accounted for a relatively high market share, it was difficult to force the users to rely on the two companies. Actually, the customer stickiness in the field of instant messaging had not significantly increased the users" reliance on the Tencent Technology Company and the Tencent Computer Company.

(5) Issues of the ease or the difficulty of other operators entering the relevant market. Firstly, what was important, when determining whether the Tencent Technology Company and the Tencent Computer Company had a market dominant position, was to determine the ease of entering the relevant market and expanding the market share. A low market share did not surely imply a relatively weak restriction on market competition. As long as the market could be quickly entered and effectively expanded, then the company enjoying the dominant position would be effectively restricted by the competition from other competitors. Secondly, the evidence in this case showed that during the time when the Tencent Technology Company and the Tencent Computer Company had a relatively high market share, a large number of domestic operators who met the administrative licensing conditions entered the field of instant messaging every year, and many of them quickly established a market share in a short time large enough to support their development. These actual examples of successful entry strongly proved that the instant messaging service market where the Tencent Technology Company and the Tencent Computer Company were engaged in was relatively easy to enter for other operators.

(6) Issues of whether the behaviors of the Tencent Technology Company and the Tencent Computer Company for enabling their services incompatible with the services provided by other companies and forcing users to make "either-or

choice" meant that the company had a market dominant position. The Supreme People's Court held that the "either-or choice" implemented by the Tencent Technology Company and the Tencent Computer Company lasted only one day, which led to their competitor MSN growing more than 23 million users that month and more other competitors competed for the instant messaging service market. This fact was a powerful proof to illustrate that the Tencent Technology Company and the Tencent Computer Company did not have a significant market dominant position in the instant messaging market.

In sum, the evidence available in this case was insufficient to support the conclusion that the Tencent Technology Company and the Tencent Computer Company had a market dominant position.

3. **Whether the behavior of the Tencent Technology Company and the Tencent Computer Company constituted an abuse of market dominant position, which is prohibited by the *Anti-Monopoly Law***

Judging whether the behavior of operators constitutes an abuse of market dominance position requires a comprehensive assessment of the behavior's negative effects and possible positive effects on consumers and competition. The concern of the *Anti-Monopoly Law* is not the interests of individual operators, but the possibility of distorting or destroying the healthy market competition mechanism.

(1) Issues of whether the behavior of enabling their "products incompatible" (forcing users to make either-or choice) implemented by the Tencent Technology Company and the Tencent Computer Company constituted a restriction on transaction, which was prohibited by the *Anti-Monopoly Law*. First, the motivation for the Tencent Technology Company and the Tencent Computer Company to adopt a behavior of enabling their "products incompatible" with the products provided by other companies in order to exclude and restrict the competition in the instant messaging service market was not obvious. Second, the behavior of the Tencent Technology Company and the Tencent Computer Company implementing the policy of enabling their "products incompatible" lasted for only one day, but they have brought more active competition to the instant messaging service market, and the negative impact on the security software market was extremely minimal. This fact showed that the behavior of enabling their "products incompatible" implemented by the Tencent Technology Company and the Tencent Computer Company did not constitute an abuse of market dominant position prohibited by the *Anti-Monopoly Law*. It also supported the conclusion that the Tencent Technology Company and the Tencent Computer Company did not have a market dominant position.

(2) Issues of whether the behavior of the Tencent Technology Company and the Tencent Computer Company constituted a bundling sale prohibited by the *Anti-Monopoly Law*. First, there was no reliable evidence to prove that the alleged bundling sale has enabled the Tencent Technology Company and the Tencent Computer Company to extend its leading position in the instant messaging market to the security software market. Second, the package installation of

instant messaging software QQ and Tencent PC Manager could be understood to some extent. By installing the instant messaging software QQ and the Tencent PC Manager in a package and achieving a function integration of QQ, users could better manage their QQ and ensure their account security, thereby improving the performance and value of the instant messaging software QQ. Therefore, the behavior of the Tencent Technology Company and the Tencent Computer Company did not constitute a bundling sale prohibited by the *Anti-Monopoly Law*.

The grounds for the Qihoo Technology Company to appeal regarding the Tencent Technology Company and the Tencent Computer Company abusing their market dominance position cannot be established and were not be supported.

In summary, although the facts determination of the court of first instance had flaws, its application of law was correct and the holding was appropriate. And the appellant's grounds for appeal were partially established, but these grounds did not have effect on the holding in this case. So the Supreme People's Court dismissed the appeal and affirm the original judgment.

Comment on Rule

This is the first case about monopoly adjudicated tried by the Supreme People's Court, which involved the determination of the monopolistic behavior of abusing market dominant position in the cyber space. Now the key issues surrounding the Rule are reviewed as follows:

1. **Issues of the analytical methods in cases of abusing market dominant position and whether defining the relevant market is a mandatory step**

Prior to the final judgment of the case, the dominant analytical paradigm used by the European and American courts in similar cases of abusing market dominance position was "Relevant market—Market power—Competitive effect" (R-M-C), in which accurately defining the relevant market is the premise of determining the market dominance position.[1] This idea is proper to some certain. Because competitive behaviors all occur and develop within a certain market, defining the relevant market can clarify the market scope of competition among operators and the competitive restraints they face. In cases of abusing market dominant position, we should reasonably define the relevant market, correctly determine the market position of operators, analyze the influence of the operators "behavior on market competition, and judge whether the

[1]The related precedents in the US and European courts all attached great importance to the role of defining the relevant market. Take the following cases as examples, United States v. Aluminum Co. of America, 148, F. 2d 416 (2nd Cir.), 1945; and two cases from the EU, that is, Case 6/72 *Continental Can v. Commission*[1973] ECR 215 and Case 27/76 *United Brands v. Commission* [1978] ECR 207. They all emphasized the importance of defining the relevant market and market share in identifying monopoly power.

operators" behavior is illegal and what kind of legal responsibility they should bear if their behavior is illegal. Such key issues are of great significance. Therefore, in the trial of anti-monopoly cases, defining the relevant market is often an important analytical step. However, based on the development of theories and practices, the Supreme People's Court ultimately did not admit the opinion that defining the relevant market is a necessary step in cases of abusing market dominant position. First of all, from the perspective of theoretical origin, in the trial of abusing market dominant position, the purpose of defining the relevant market is to assess the market power of the operator and the impact of the alleged monopolistic behavior. In order to achieve this purpose, in addition to indirectly assessing the tool of the relevant market, we can directly assess the market position of the alleged operator and the possible market impact of the alleged monopolistic behavior based on the actual evidence that is used to prove the alleged operator has excluded or hindered market competition. Therefore, defining the relevant market is only one of the ways to evaluate the market power of operators and the effect of their alleged monopolistic behaviors on competition, but not the only way. Second, from the perspective of practice, whether the relevant market can be clearly defined depends on the specific circumstances of the case, especially such factors as the evidence of the case, the availability of related data, and the complexity of competition in relevant fields. In particular, in the network environment, the boundary among relevant markets is more blurred due to the popularity of attention competition, platform competition and cross-border competition, so defining the relevant market not only becomes more difficult, but is more likely to be erroneous.[2]Therefore, we have to maintain the necessary vigilance towards the analytical method of "Relevant Market-Market Power-Competitive Effect", and in turn focus on using direct evidence to identify the market power of operators.

Therefore, the Court proposed a statement in the judgment that "even if the relevant market is not clearly defined, the market position of the alleged operator and the possible market impact of the alleged monopolistic behavior may be assessed by the direct evidence that is used to prove the alleged operator has excluded or hindered market competition". The statement essentially puts forward two new analytical paradigms. One is to evaluate the market power of operators through direct evidence, and then to evaluate the impact of the operators 'behaviors on market competition. This paradigm can be called the analytical method of "Market Power—Competition Effect" (M–C). The other is to assess the actual or potential effect of the operators' behavior on market competition through direct evidence. This paradigm can be called the analytical method of "Conduct—Competition Effect" (C–C). The latter method that attaches importance to assessing the competition effect with direct evidence further enriches and develops approaches to analyzing the cases of abusing market dominant position. This is one of the important contributions of the judgment made in this case.

[2]See Li [1].

The Court analyzed in detail in the judgment of this case the definition of the relevant market and the determination of market power, and drew the conclusion that the Tencent Technology Company did not have a market dominant position. And the Court did not just stop there. Instead, the direct evidence was used to comprehensively evaluate the actual or potential effects of the alleged monopolistic behavior on market competition, and a final judgment was made based on the basis. Actually, this is the specific application of the analytical methods of "Market Power—Competitive Effect" (M–C) and "Conduct—Competitive Effect" (C–C).

2. **Flexible application of the HMT in the cyber space**

The HMT is an analytical method commonly used by countries and regions when defining the relevant market. Based on this idea, with the help of economic tools to analyze the relevant data obtained, we can determine the minimum commodity collection and territory scope that the hypothesis monopolist can maintain the price above the competitive price level, thereby defining the relevant market. Generally, the HMT first defines the relevant commodity market, for which the specific idea is: First, regarding the commodity (target commodity) provided by the operator in the monopoly case, we assume that the operator is a monopolist who considers the profit maximization as his business target (the hypothetical monopolist). Then, in the case where the sales conditions of other commodities remain unchanged, we consider whether the hypothetical monopolist can increase the price of the target commodity in a small amount (generally 5%–10%) for a long time (generally one year) (the so-called *Small but Significant Non-transitory Increase in Price* Test, that is, the "SSNIP" test). The price increase of the target commodity will cause the demander to switch to other commodities that can substitute the price-growing commodity, thereby resulting in the sales of the hypothetical monopolist to decline. If the price of the target commodity increases, even if the hypothetical monopolist's sales decline, he is still making profits. Then the target commodity constitutes the relevant commodity market.[3]This traditional test method has been in a leading position in this

[3] Article 10 of the *Guide of the Anti-Monopoly Committee of the State Council for the Definition of the Relevant Market* (May 24, 2009) regulates the basic idea of the HMT test.

The HMT test is an analytical approach to define the relevant market, which can help resolve uncertainties that may arise when defining the relevant market, and is currently widely borrowed when countries and regions develop their anti-monopoly guidelines. Based on this idea, with the help of economic tools to analyze the relevant data obtained, we can determine the minimum commodity collection and territory scope that the assumed monopolist can maintain the price above the competitive price level, thereby defining the relevant market.

The HMT test generally defines the relevant commodity market first. First, regarding the commodity (target commodity) provided by the operator concerned in the monopoly case, we assume that the operator is a monopolist with the profit maximization as his business target (the assumed monopolist). Then the problem to be analyzed is that, in the case where the sales conditions for other commodities remain unchanged, whether the assumed monopolist can increase the price of the target commodity in a small amount (generally 5–10%) for a long time (generally one year). The price increase of the target commodity will cause the demander to switch to other commodities that can substitute the price-growing commodity, thereby resulting in the sales of the assumed monopolist to decline. If the price of the target commodity increases, even if the assumed monopolist's sales

case until the Court made a judgment. The court of first instance used this method to define the relevant commodity market in this case.

But the HMT based on price increase has encountered difficulties in the Cyber space. When using the HMT which is based on price increase, the implied precondition is that the homogenization characteristics of commodities in the relevant market are relatively obvious, and price competition is a rather important form of competition. However, if there is a significant difference in products, and non-price competitions, such as quality competition, service competition, innovation competition, and consumer experience competition, become important forms of competition, then adopting the so-called SSNIP test has great difficulties. Particularly, adopting the SSNIP test is difficult when the market equilibrium price of a specific commodity sector is zero. This is because, when using the SSNIP test, it is necessary to carry out a price increase of 5%–10% based on a benchmark price that is set by a fully competitive market, and then determine the demander's response. If the benchmark price is zero, the price will remain zero even if the price increases by 5%–10%. And if the price is raised from zero to a smaller positive price, it means the price increases infinitely, which indicates the product characteristics or business model have undergone major changes. Under this circumstance, it is difficult to perform the SSNIP test. For the competition in the cyber space, Internet service providers tend to compete for quality, service and innovation rather than price. Usually their business model is to use free basic services to attract and accumulate a large number of users, and make profit by utilizing the huge user resources to operate value-added services and advertising, and in turn support the survival and development of free

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decline, he is still making profits. Then the target commodity constitutes the relevant commodity market.

If the price increase causes the demander to turn to other commodities as substitutes, and the assumed monopolist's behavior of increasing price is unprofitable, the substitute commodity needs to be added into the relevant commodity market, which means the substitute commodity and the target commodity form a commodity collection together. Next, we need to analyze whether the monopolist is profitable if the price of the commodity collection is raised. If the answer is yes, then the commodity collection constitutes the relevant commodity market. Otherwise, the above analysis process needs to be continued.

As the commodity collection becomes larger and larger, the chance that the goods within the collection be replaced by the goods outside the collection becomes smaller and smaller, and eventually a commodity collection of this kind will appear, in which the monopolist can always make profits by raising the price. Therefore, we define a commodity collection of this kind as the relevant commodity market.

The idea of defining the relevant geographical market is the same as defining the relevant commodity market. First, starting from the territory (target territory) of the operator's business activities that the anti-monopoly review focuses on, the problem to be analyzed is that, given the sales conditions in other territories unchanged, whether it is profitable if the assumed monopolist persistently increase the price within the target territory in a small amount (generally 5–10%) for a long time (generally one year). If the answer is yes, the target territory will constitute the relevant geographical market. If other geographical markets can easily substitute the target territory, which then makes the price increase in the target territory unprofitable, it is necessary to expand the geographical scope until the behavior of price increase is finally profitable. And then the territory obtained is the relevant geographical market.

services with profits obtained from value-added services and advertising. Therefore, the HMT based on the relative price increase is not suitable for use in this case.

After correcting the mistake made by the court of first instance that directly used the HMT which is based on price increase, the Supreme People's Court further developed the analytical method for the HMT, and clarified the flexible application method for using the HMT in the cyber space. The Court pointed out in the judgment that in practice, there are many analytical methods for the HMT, such as the *Small but Significant Non-transitory Increase in Price Test* (SSNIP) and the *Small but Significant Non-transitory Decrease in Product Quality Test* (SSNDQ). Moreover, as an analytical idea or thinking method, the HMT can be carried out by a qualitative analytical method or a quantitative analytical method when conditions permit. Although the HMT based on the relative price increase is improper to apply in this case, a flexible form of the test can be taken, such as an HMT based on quality degradation. Since the degree of quality degradation is difficult to assess and the relevant data is difficult to obtain, the HMT based on quality degradation can adopt the qualitative analysis rather than the quantitative analysis. This is an important advancement for the analytical methods of the HMT.

3. Issues of the definition method of the relevant geographical market in the cyber space

Defining the relevant geographical market also follows the general approach of defining the relevant commodity market. It is generally believed that under the framework of the HMT, the main factor to be considered when defining the relevant geographical market is whether the operators from other territories can form an effective competition restriction on the hypothetical monopolist of the target territory when competitive factors, such as price or quality, change. From the perspective of demand substitution, the main considerations are such factors as the evidence that the demander turns to or considers to purchase commodity from other territories because of the change of commodity price or other competitive factors, the transportation cost and commodity characteristics, the actual regions where most demanders buy the commodity, the commodity distribution of main operators, the trade barriers among territories, and the preferences of demanders in a specific region. From the perspective of supply substitution, the main considerations are the evidence that the operators in other territories have made reaction to the changes in the competitive factors such as the commodity price, and the timeliness and feasibility of operators from other territories supplying or selling the relevant commodity.

In this case, the court of first instance used such important arguments as that the overseas operators can provide instant messaging services to users in the Chinese mainland, the appellee also provide services to users around the world, and a certain number of overseas users are using the instant messaging services provided by the appellee, thereby determining that the relevant geographical market should be the global market. Actually, this analytical method deviates from the above-mentioned analytical methods, because while considering the global and low-cost characteristics of the Internet, it ignores such restraints as the legal barrier among territories and preferences of specific consumers. The Supreme People's Court pointed out in the

judgment that the Internet-based instant messaging service can reach or cover the whole world at a low expense and cost without additional transportation cost, price cost or technical obstacles worthy of attention. When defining the relevant geographical market, the main considerations are the actual regions where most consumers buy the commodity, the provisions of laws and regulations, the status of overseas competitors and the timeliness of their entry into the relevant geographical market. Since no factor above was not decisive, a comprehensive assessment should be carried out based on these factors. Since most users in the Chinese mainland choose to use instant messaging services provided by operators in the Chinese mainland, China's administrative regulations and rules on the Internet stipulate clear requirements and conditions for the operation of instant messaging services. we implement the administrative licensing system for value-added telecommunications services such as instant messaging, so foreign operators usually cannot be unable to enter the Chinese mainland directly for operation, but need to enter in the form of Sino-foreign joint ventures and obtain the corresponding administrative licensing. And it is difficult for overseas instant messaging service operators to enter the Chinese mainland in a short period of time (such as in one year) and develop to the size enough to restrict domestic operators. Therefore, the relevant geographical market in this case should be the Chinese mainland market. This method of defining the relevant geographical market considered not only the characteristics of the cyber space, but also the actual restraints such as laws, consumer habits and so on to the Internet service market, which had important guiding significance for defining the relevant geographical market in the cyber space.

4. Issues of the influence of market share possessed by operators in internet on the determination of market power

In the traditional field, there is a strong positive correlation between the market share of operators and their market power, that is, the larger the market share, the greater the possibility of having a stronger market power. For a long time, the anti-monopoly laws traditionally have taken market share as the most important indicator of market power. China's *Anti-Monopoly Law* is based on this kind of correlation between market share and market power, and stipulates the method of presuming the market power through market share.[4]

However, due to the characteristics of the cyber space, this correlation between market share and market power has been weakened. Firstly, the ambiguity of market

[4] Article 19 of the *Anti-Monopoly Law* stipulates that under any of the following circumstances, a business operator may be presumed to have a market dominant position: (1) The market share of one business operator accounts for 1/2 or more in the relevant market; (2) The joint market share of two business operators accounts for 2/3 or more in the relevant market; or (3) The joint market share of three business operators accounts for 3/4 or more in the relevant market. Under the circumstance prescribed in Item 2 or 3 of the previous paragraph, if any of the business operators has a market share of less than 1/10, that business operator shall not be considered to have a market dominant position.

A business operator that has been presumed to have a market dominant position shall not be considered as having a market dominant position if the operator can provide opposite evidence.

boundaries in the cyber space has weakened the role of market share played in market power. Differentiated competition in the cyber space is more obvious than in the traditional field. Even if the functions and uses of the products are the same, the consumer experience is very different. This differentiation makes the boundaries among relevant markets more ambiguous. At the same time, the platform competition in the cyber space has further exacerbated the ambiguity of market boundaries. Since the core of the Internet lies in the attention of users, there is often some degree of competition among platforms that are very different in usage or performance. Compared with the traditional field, the unclear market boundary in the cyber space leads to certain randomness when determining the market share in the network environment, so the indication effect of market share on market power will be affected to some extent. Second, the innovation competition in the cyber space has also weakened the correlation between market share and market power. Market share and market power can be acquired and maintained for a number of reasons, and companies may maintain their high market share through continuous competition and continuous innovation. For example, although Google has a large market share in the global search engine market, Google is innovating all the time. The market share obtained due to continuous innovation does not mean that Google has a strong market power. In this way, the role of market share as an indicator of market power is weakened. Finally, even in the case of possessing a relatively high market share, it is still necessary to consider a variety of factors when judging whether the operator has a substantial market power, such as how competitors or customers react to price increase (or lower quality), how easy it is to enter the relevant market. Based on this, the judgment in this case pointed out that in the cyber space, market share is only a rough and potentially misleading indicator for judging market dominant position. Its position and role played when determining market power must rely on the specific circumstances of the case.

5. **Other issues worthy of mention**

(1) The universality and individuality of the analytical methods used for cases of abusing market dominant position

Based on the analytical method of "Relevant Market-Market Power-Competitive Effect" that is used in the case of abusing market dominant position, the judgment of this case further applies and develops the two analytical methods of "Market Power-Competitive Effect" and "Conduct—Competitive Effect", forming a much more complete analytical method system for cases of abusing market dominant position. Commonly these three analytical methods can be used in cases of abusing market dominant position. However, when applying the judicial orientation and the generally applicable rules embodied in the judgment of this case to other similar cases, attention must be paid to correctly distinguishing the general rules with the features of individual cases, and using the general rules flexibly based on individual cases, skillfully but not mechanically. In any case, people's courts should be flexible to choose the appropriate analytical method according to the circumstances of the case. When defining the relevant market in the case is difficult, but the direct evidence

used to prove that the operator has market power or his behavior has impact on market competition is sufficient, courts can choose the analytical methods of "Market Power-Competitive Effect" or "Conduct—Competitive Effect", and do not need to clearly define the relevant market. If the evidence is sufficient to define and determine the relevant market and market share, courts can choose to apply the analytical method of "Relevant Market-Market Power-Competitive Effect". But in the cyber space, courts should be cautious about the indication role of market share based on the characteristics of network competition, and focus on such evidence as the market entry, market behavior and economic effects of the corresponding market in the individual case.

(2) The correct application of economic analytical method in monopoly cases

Judging whether the monopolistic behavior is legal often requires the application of economic analytical method. One of the important contributions of the judgment in this case is that it enriches and develops the application of economic analytical method used to define the relevant market in the cyber space. Nevertheless, the monopolistic behavior, according to its very nature, ultimately should be determined by a legal judgment, while the economic analysis is only one of the tools used to achieve the correct legal judgment. Judges cannot transfer the power of making judgment to economists. Therefore, in the trial of anti-monopoly cases, it is necessary to combine legal judgment with economic analysis creatively, and correctly use the conclusion obtained from the economic analysis to improve the accuracy of legal judgment when determining a monopolistic behavior. To use the economic analytical method correctly and rationally, courts should first adopt the right economic analytical method and fully understand the data limitations and condition restraints. Regarding the economic analytical methods and conclusions, courts should neither be arrogant nor be biased. For judges and others who work at the judicial level, it is necessary for them to achieve the rational use of economic analytical methods, and avoid being misled by the mistake of choosing the wrong economic analytical method, and by the data limitations and condition restraints. In addition to the necessary economic knowledge, more importantly judges should adhere to the effect-oriented principle and focus on the actual or potential impact of the alleged monopolistic behavior on competition. As long as the nature that the monopolistic behavior has actual or potential negative impact on competition is clear, and is properly applied the results of economic analysis through the effect-oriented direct evidence, a more accurate, realistic and reasonable legal recognition of monopolistic behavior can thus be confirmed.

Reference

1. Zhu Li, "Legal Boundaries of Competition in the Area of Internet: Challenges and Judicial Responses", *Competition Policy Research*, 1, 2015, pp. 1–12.

Wu X v. Shaanxi Broadcast & TV Network Intermediary (Group) Co., Ltd. (Bundling Transaction Dispute)—The Authentication of Market Dominant Position Possessed by Operators

Yanfang Wang

Rule

As the only operator in a specific region that legally operates the cable TV transmission business and a centralized broadcaster of TV programs, the Shaanxi Broadcast & TV Network Intermediary (Group) Co., Ltd. (hereinafter referred to as the "Shaanxi Broadcast & TV Group") had advantages in terms of market access, market share, business position and operation scale, thereby it could be determined as the operator that owns the market dominant position.

The operator took advantage of its market dominant position to bind the digital TV basic maintenance fee and the digital TV paid program fee together to collect from consumers, which has infringed on the consumers' right of consumption choices. And the conduct of the Group was not conducive to other service providers to enter the digital TV service market. Even if there were exceptions that the operator sometimes collected the fees for the two services separately, it is not enough to deny that the conduct constituted a bundling sale as prohibited by the *Anti-Monopoly Law*.

Collegial panel judges: Wang Yanfang, Qian Xiaohong, Du Weike (Written by: Wang Yanfang, Supreme People's Court; Translated by: Sun Lin).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_35

Case Information

1. Parties

Retrial Applicant (Plaintiff in first instance, Appellee in second instance): Wu X
Retrial Respondent (Defendant in first instance, Appellee in second instance): Shaanxi Broadcast & TV Network Intermediary (Group) Co., Ltd. (hereinafter referred to as the "Shaanxi Broadcast & TV Group")

2. Procedural History

First instance: No. 00428 [2013], Trial, Civ. Division, the Intermediate People's Court of Xi'an City, Shaanxi Province (dated Jan. 5 of 2013)
Second instance: No. 38 [2013], Final, Civ. Division, the Higher People's Court of Shaanxi Province (dated Sep. 12 of 2013)
Application for retrial: No. 98 [2016], Retrial, Civ. Division, the Supreme People's Court (dated Apr. 28 of 2016)

3. Cause of Action

Monopoly dispute

Essential Facts

On May 10, 2012, Wu X went to the Shaanxi Broadcast & TV Group to pay the basic digital TV subscription and maintenance fee, but he was informed that the minimum standard for the fee was raised from RMB 25 to RMB 30 a month. Wu X paid the basic digital TV subscription and maintenance fee of RMB 90, which was the fee from May 10 to August 9, 2012. The special invoice issued by the Shaanxi Broadcast & TV Group to Wu X stated that the basic digital TV subscription and maintenance fee was only RMB 75 and another RMB 15 was the digital TV paid program fee. Later, Wu X consulted the issue with the customer service center of Shaanxi Broadcast & TV Group (service call "96766"), and was told that the Shaanxi Broadcast & TV Group has upgraded a number of its programs to be paid programs, and there were different packages, among which the basic subscription fee of the minimum package is RMB 360 per year and users should pay a minimum of 3 months at a time. Shaanxi Broadcast & TV Group was the only operator authorized to do the cable TV transmission business in Shaanxi Province and the only centralized broadcaster of TV programs approved by the Shaanxi Provincial Government. The Shaanxi Broadcast & TV Group admitted that it has dominated the cable TV transmission business in Shaanxi Province.

In addition, the *Interim Measures for the Administration of Basic Cable TV Broadcasting Maintenance Fees* issued by the National Development and Reform Commission and the State Administration of Radio, Film and Television on December 2,

2004 provides that the basic TV subscription and maintenance fees shall be subject to government pricing, and the charging standards shall be formulated by the relevant competent pricing agencies. On July 11, 2005, the State Administration of Radio, Film and Television issued *Some Opinions of the State Administration of Radio, Film and Television on Promoting the Overall Transform of Cable TV Digitization by Pilot Entities (for Trial Implementation),* which provides that all pilot entities shall, in the process of promoting the overall transformation, attach importance to popularizing such new services as paid channels, and provide users with the right of free choice and voluntary orders. The Shaanxi Provincial Price Bureau on May 29, 2006 issued *Notice on the Standards for Basic TV Broadcasting Maintenance Fees in Shaanxi Province,* stating that the unit of charge on basic digital TV subscription and maintenance fee is based on the one receiving terminal that used for one TV set by resident users. The urban resident users above the county level in the province will pay RMB 25 per main terminal per month. The cable digital TV users may voluntarily choose to pay the basic subscription and maintenance fee on a monthly, quarterly or annual basis according to actual conditions. The National Development and Reform Commission and the State Administration of Radio, Film and Television on August 25, 2009 issued the *Notice on Strengthening the Management of Cable TV Charges and Other Issues,* pointing out that the basic cable TV subscription and maintenance fee is subject to government pricing and the fees for cable TV value-added services and digital TV paid program are determined by the cable operator.

In the second instance, the Shaanxi Broadcast & TV Group provided four copies of special invoices for tolls, which proved that the business hall of Shaanxi Broadcast & TV Group received a monthly service fee of RMB 25 around May 10. Since there was no original invoice, Wu X did not need to make cross-examination. Upon review, the Shaanxi Broadcast & TV Group provided three originals of the invoices, and both parties conducted relevant verification and confrontation. The invoices showed that the annual payment amount was RMB 300, that is, RMB 25 per month. The Shaanxi Broadcast & TV Group provided the originals of five invoices, indicating that the payment all happened at Xianyang City, and the three of them were provided in the first instance. In this way, the Shaanxi Broadcast & TV Group intended to prove that the Group has provided a monthly service fee of RMB 25 around May 10.

During the retrial, the Shaanxi Broadcast & TV Group submitted a screenshot to show its website charging package in 2016, a notice on the issuance of the *Notice of the Implementation Measures for Mass Business in 2016 (for Trial Implementation)*, and some charging invoices in 2016.

The Intermediate People's Court of Xi'an City, Shaanxi Province made the judgment of first instance to: (1) confirm that the conduct that Shaanxi Broadcast & TV Group collected the fee of RMB 15 for the digital TV paid program from Wu X is invalid; (2) order that the Shaanxi Broadcast & TV Group shall return Wu X RMB 15. The Shaanxi Broadcast & TV Group filed an appeal, and the Higher People's Court Shaanxi Province made the judgment of second instance to: (1) reverse the judgment of first instance; (2) dismiss the lawsuit claims raised by Wu X.

Wu X refused to accept the judgment of second instance and applied to the Supreme People's Court for retrial.

Issues

1. Whether the Shaanxi Broadcast & TV Group was in a market dominant position in the cable TV transmission service market in Shaanxi Province?
2. Whether the conduct that the Shaanxi Broadcast & TV Group bound the digital TV basic subscription service with the digital TV paid program service to sell to Wu X violated the provisions of Article 17(1)(v) of the *Anti-Monopoly Law*?

Holding

The Supreme People's Court after the trial held that the Shaanxi Broadcast & TV Group had a market dominant position in the cable TV transmission service market in Shaanxi Province, and the behavior that it bound the digital TV basic subscription service with the digital TV paid program service to sell to Wu X violated the provisions of Article 17(1)(v) of the *Anti-Monopoly Law*. Wu X requested in retrial to confirm that the conduct of Shaanxi Broadcast & TV Group to charge RMB 15 for its digital TV program fee is null and void and to order the Group to return the fee of RMB 15, which were well established. The Supreme People's Court rendered the judgment numbered No. 98 [2018], Retrial, Civ. Division, Supreme People's Court to, (1) reverse the judgment of second instance; (2) affirm the judgment of first instance.

Comment on Rule

1. **Whether the Shaanxi Broadcast & TV Group had the market dominance position**

In China, lawsuits against monopolistic behaviors and lawsuits concerning the abuse of the market dominant position have accounted for quite a large proportion.[1] The premise of regulating the abuse of market dominant position by operators is to judge whether the operators have the market dominant position. Although laws in different countries or anti-monopoly theories have different definitions and determinations of market dominant position, the common ground is that the determination of market dominant position is the premise and basis of regulating behaviors of abuse. In this regard, Article 17(2) of the *Anti-monopoly Law* provides that the market dominance position refers to the market position relying on which operators will have the ability to control commodity prices, quantities or other trading conditions in the relevant market, or to hinder or affect the ability of other operators to enter the relevant market.

[1]Ministry of Commerce of the People's Republic of China Department of Treaty and Law [1], p. 156.

In this case, the Shaanxi Broadcast & TV Group clearly recognized in the defense of first instance that it was "the only operator legally operating cable television transmission business in Shaanxi Province approved by the Shaanxi Provincial Government. As the only TV program centralized broadcaster in Shaanxi Province, undoubtedly the Shaanxi Broadcast & TV Group had the market dominant position in the cable TV market of Shaanxi Province. The Group has encouraged users to choose more abundant cable TV packages, but it has not abused the market dominance position, nor has it imposed on users to consume services beyond the basic subscription business. In the second instance, the Shaanxi Broadcast & TV Group did not recognize its market dominant position, but did not put forward the corresponding evidence to prove this denial. In the process of retrial review, the Shaanxi Broadcast & TV Group did not object to the determination made by the courts of first instance and second instance that the Group had a market dominant position. In view of the fact that the Shaanxi Broadcast & TV Group is the sole operator of cable TV transmission business in Shaanxi Province and the sole centralized broadcaster of TV programs in Shaanxi Province, the courts of first instance and second instance, on the basis of ascertaining the facts, found that the Shaanxi Broadcast & TV Group had advantages in market access, market share, operation position and operation scale in the cable TV transmission market, so it was not improper for the courts to assume that the Group had a market dominant position.

2. **To decide whether the Shaanxi Broadcast & TV Group constituted a bundling sale when providing services to Wu X**

The bundling sale refers to the fact that the business operators, by using their market dominant position, sell or provide, in violation of the purchaser's free will, another kind of commodities or services that the purchaser does not need.[2]

Paragraph 1(5) of Article 17 of China's *Anti-Monopoly Law* provides that operators with market dominant position are prohibited from implementing bundling sales or imposing other unreasonable trading conditions without any justifiable causes at the time of trading. The characteristics of bundling sales include: (1) bundling two or more products together to sell; (2) violating the free will of the purchaser; and (3) without a justifiable reason.

According to the aforementioned facts and the fact that the Shaanxi Broadcast & TV Group issued a special invoice to Wu X, which recorded the charges of RMB 75 for basic digital TV maintenance and RMB 15 for digital TV paid programs, it can be determined that the Shaanxi Broadcast & TV Group actually bound the basic digital TV programs and digital TV paid programs together to sell to Wu X, and did not tell Wu X whether he can purchase the basic digital TV subscription service only. In addition, the reply from the customer service center of Shaanxi Broadcast & TV

[2]Ministry of Commerce of the People's Republic of China Department of Treaty and Law [1], p. 230.

Group (service call 96766) can also prove that the Shaanxi Broadcast & TV Group collects the basic digital TV subscription and maintenance fee and the digital TV paid program fee together and provides the services together. Although the Shaanxi Broadcast & TV Group submitted relevant invoices in the second instance to prove that it charged the basic digital TV subscription and maintenance fee from other users separately, the evidence only proved that there were exceptions other than the package stated by the customer service center when the Shaanxi Broadcast & TV Group collected the fee. In the retrial, the Shaanxi Broadcast & TV Group did not reasonably explain the exceptions other than the package stated by the customer service center. And the invoices submitted by the Shaanxi Broadcast & TV Group to prove that it once has collected the relevant fees separately also occurred after the lawsuit in this case, which was not enough to illustrate the situation when the lawsuit happened. Therefore, the evidence shall not be admitted by the people's court. Therefore, the existence of exceptions other than the package stated by the customer service center was not enough to deny the general practice of Shaanxi Broadcast & TV Group to collect the basic digital TV subscription and maintenance fee and the digital TV paid program fee together. The court of second instance found that the Shaanxi Broadcast & TV Group not only provided bindling services, but also provided basic services, but the determination lacked sufficient evidence and shall be corrected. Therefore, the existing evidence cannot prove that ordinary consumers can only pay the basic TV maintenance fee or the digital TV paid program fee, that is to say, no evidence can prove that consumers have the right make free choices. The court of the second instance directly considered the case as a violation of consumers" right to know, in which the Group did not inform consumers of their right to choose, but there was no evidence to prove that the customers have the right to choose. On this basis, it can be concluded that the conduct of Shaanxi Broadcast & TV Group did not constitute a bundling sale without justifiable reasons as regulated by the *Anti-monopoly Law*. Actually, The determination made by the court of second instance lacked sufficient facts and legal basis, which shall be corrected.

According to the facts ascertained, the basic digital TV subscription and maintenance fee and the digital TV paid program fee belong to two separate services. In the lawsuit, the Shaanxi Broadcast & TV Group did not prove that providing the two services together was in conformity with the trading customs for providing digital TV services. At the same time, if the digital TV basic maintenance fee and the digital TV paid program fee were collected separately, there was no evidence to prove that the performance and use value of the two services would be impaired. And the Shaanxi Broadcast & TV Group did not make justifiable reasons about the above-mentioned behavior. In this case, the Shaanxi Broadcast & TV Group, taking advantage of its market dominant position, collected the basic digital TV subscription and maintenance fee and the digital TV paid program fee together, which objectively affected consumers to choose the relevant digital paid programs provided by other

service providers, which was not conducive to other service providers entering the television service market, causing adverse effects on market competition. Therefore, it is proper that the court of first instance found that the conduct of Shaanxi Broadcast & TV Group violated the provisions of Article 17(1)(v) of the *Anti-monopoly Law*.

Reference

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Yuan X v. the People's Government of Jiangsu Province (Government Information Disclosure)—Determination of the Necessity to Protect Rights in Administrative Lawsuit Concerning Government Information Disclosure

Baojian Geng and Qin Yin

Rule

An application for the disclosure of government information shall be submitted to the government information disclosure institution attached to an administrative organ in a prescribed form. If the applicant sends a letter to the legal representative of the administrative organ and the content of the letter is not in conformity with the prescribed form, and if an administrative organ fails to reply or treats it as a complaint via letters and visits, and so the applicant files a lawsuit on the grounds that the administrative organ fails to perform its duty of disclosing government information, the people's court shall rule against filing the case or dismiss the case directly. Whereas if the content of the letter is basically in conformity with the prescribed form, the date which the information disclosure institution receives the forwarded application in reality or the date has been ascertained by the applicant shall be regarded as the "date of receipt of the application", and in accordance with which the relevant reply term shall be calculated.

The collegiate panel judges of the Supreme People's Court for retrial: Geng Baojian, Bai Yali and WangJun (Written by: Geng Baojian and Yin Qin, Supreme People's Court; Translated by: Li Jinyan).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_36

Case Information

1. **Parties**

Applicant in the retrial (Plaintiff in the first instance, Appellant in the second instance): Yuan X
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): People's Government of Jiangsu Province

2. **Procedural History**

The First Instance: No. 00022 [2015], Trial, Adm. Division, the Intermediate People's Court of Yangzhou City, Jiangsu Province (dated Dec. 15 of 2015)
The Second instance: No. 229 [2016], Final, Adm. Division, the Higher People's Court of Jiangsu Province (dated Jun. 27 of 2016)
Retrial: No. 17 [2017], Retrial, Adm. Division, the Supreme People's Court (dated Feb. 28 of 2017)

3. **Cause of Action**

Government information disclosure

Essential Facts

On May 7, 2014, Yuan X mailed to the Governor of People's Government of Jiangsu Province an *Application Letter for Information Disclosure on Land Expropriation, Land Use and Afforestation Compensation to the People's Government of Jiangsu Province*, requesting the People's Government of Jiangsu Province to disclose the requisition and the use of land and the compensation related to the construction of Taizhou Airport Expressway, or the People's Government of Jiangsu Province to instruct the local government to disclose the the said information. After receiving the application letter on May 8, 2014, the People's Government of Jiangsu Province transferred it to Yiling Town, Jiangdu District, Yangzhou City as a complaint via letters or visits. Yuan X filed an administrative lawsuit on May 20, 2014, claiming that the People's Government of Jiangsu Province shall perform its statutory duty of disclosure the relevant government information.

On December 18, 2015, the court of the First Instance rendered an administrative judgment, numbered No. 00022 [2015], Trial, Adm Division, dismissing Yuan X's claim. On June 27, 2016, the court of the Second Instance issued an administrative judgment, numbered No. 229 [2016], Final, Adm Division, dismissing the appeal and upholding the decision of the first instance.

After the judgment came into effect, Yuan X applied to the Supreme People's Court for a retrial, claiming to set aside the judgment of the appellate court, to confirm of the illegal action of Jiangsu Provincial Government committed an act of omission, and to order the Jiangsu Provincial Government to make a reply to the public in accordance with the requirements of the *Application Letter*.

Issues

1. Whether mailing letters to the legal representative of an administrative organ can be deemed as an application for government information disclosure;
2. Whether the Jiangsu Provincial Government has the legal duty to disclose government information;
3. Whether the case falls within the scope of administrative litigation.

Holding

The Supreme People's Court reviewed the case and held that the Jiangsu Provincial Government has established and improved the government information disclosure system. Under such circumstances, citizens, legal persons or other organizations applying for government information disclosure to the Jiangsu Provincial Government should submit the application to the government information disclosure office affiliated with General Office of the Jiangsu Provincial Government in accordance with the requirements and *Guidelines for the Government Information Disclosure*. In this case, the applicant in the retrial, Yuan X wrote a letter to Li X, whom is the legal representative of Jiangsu Provincial Government, reporting that the lower-level administrative authorities had not disclose the information as applied for and requesting the Jiangsu Provincial Government to disclose the said information or instruct the local government to disclose the said information. However, the letter does not conform to the formal requirements of the government information disclosure application, nor does it propose to the handling institution in accordance with the *Regulations on Information Disclosure* and the *Guidelines on Information Disclosure*. According to the contents of this letter, The Jiangsu Provincial Government treated it as a complaint via letters and visits instead of an application for government information disclosure, which did not violate the laws or regulations. Based on the contents of Yuan X's letter, the information that Yuan applied for publicity mainly involves information on land requisition, land use, afforestation compensation, and related payment and usage. Such information is obviously not made or kept by the Jiangsu Provincial Government, who is not obligated to disclose such information. And, the Higher People's Court of Jiangsu Province, No. 00180 [2016], Final, Adm Division, has determined that Yuan X has actually obtained the contents of the government information. For the reason that the letter mailed by Yuan is not in conformity with the formal requirements of the government information disclosure application, and the relevant information is not made or preserved by the Jiangsu Provincial Government, the Jiangsu Provincial Government does not have the statutory duty to disclose the government information applied by Yuan. For an application that is obviously not in conformity with the formal requirements of the government information disclosure application and is not submitted to the government information disclosure organization in accordance with the law and the application resembles

a complaint via letters or visits, the government's failure to reply in time or treat it the way a complaint via letters or visits was handled, thus resulting in an administrative lawsuit on the ground that the government fails to perform the statutory duty of government information disclosure, does not constitute a cause of action, and the claim raised by the applicant may not amount to the point when the necessity to protect the rights involved in the administrative litigation. If the applicant insists on pursuing the cause, the people's court shall not allows the case to be filed in the court or may enter a ruling as a direct dismissal of a case.

Comment on Rule

"The law is the manifestation of various conflicts of interests in society as well as the arrangement and balance of various conflicting interests."[1] In general theory, the applicant's interests are protected by the *Regulations on Government Information Disclosure* as "the right to know".[2] The right to know is presented to be basic right and is the premise for citizens to exercise their rights of participation, political right and right of supervision. The pattern of interest in government information disclosure is more represented by the fact that the special interest of the applicant is absorbed by the public interest, while balance of interest in government information disclosure will eventually become a game between the public interest of promoting the disclosure of public information and the public interest of supporting non-disclosure of public information.[3] Different from the confrontation between the right to know and the interests of the third party and state secrets, the practice of information disclosure by the Chinese government in recent years also reflects another kind of confrontation, which is the confrontation between the increase in administrative and judicial costs and the decrease of marginal effects caused by the right to know and frivolous applications. At the level of legal interpretation, the judges of this case have made an endeavor to work out a better type of expressing the intention in the application form for the government information disclosure, which is more in line with the legislative

[1] Philip [1].

[2] Hereto, Zhang Qiong, the deputy director of the Legislative Affairs Office of the State Council by then, answered questions at press conference and pointed out that, "The full implementation of the regulations is conducive to ensuring citizens, legal persons or other organizations to obtain government information and realizing the people's right to know, participate in and supervise governmental work." See Cao Kangtai, editor-in-chief, *Regulation of the People's Republic of China on the Disclosure of Government Information*, Beijing, People's Publishing House, 2007, p. 12. *The Outline of the State Council on Comprehensively Promoting Administration by Law* (No. 10 G.F. [2004]) also stipulates that "the implementation of administrative practice, administrative organs shall disclose and listen to the opinions of citizens, legal persons and other organizations information other than those involving state secrets, trade secrets and personal privacy protected by law. Administrative organs shall strictly follow statutory procedures and protect administrative counterparts and interested parties' right to know, and the right of participation and relief in accordance with the law."

[3] Wang [2].

intent, and made an attempt to figure out a way to determine the necessity to protect rights involved in government information disclosure.

1. Understanding of "Application" in government information disclosure of application

Although modern administrative law is centred on administrative acts, the purpose of an administrative act is still to form the relationship of rights and obligations in administrative law. To make administrative act according to the application, both parties have a process of meaning exchange on the specific issue of granting benefits, which is in common with the offer and acceptance system in civil law in form. Supply act by administration, a kind of right-and-obligation relationship in public law, consists of several manifestations of will after what are formed between the applicant and the administrative organ. In other words, although the supply act by administration also has certain high rank of power and discretion, on the premise of the exchange of intention expression between the administrative counterpart and the applied organ, if the administrative counterpart does not express the application intention to the administrative organ, or its application intention expression is incomplete, the administrative organ cannot make the corresponding beneficial act.

The legal relationship of government information disclosure belongs to the legal relationship of supply act by administration. Through the expression of the application, the applicant requests the administrative organ to have access to certain government information. The administrative organ can only decide whether to supply in accordance with the legal provisions in the event of full understanding of the applicant's meaning and intention in the application. Therefore, whether the application intention is full and complete is the key to obtain the government information.

According to the discretionary theory, the applicant can generally decide the meaning of application according to his or her free will. However, in order for the administrative organ to learn of the intention of the applicant at a lower cost and to disclose the government information in a more convenient way, the law generally has more specific provisions for the applicant and his/her application. Article 20 of the *Regulations on the Disclosure of Government Information* provides that, "Citizens, legal persons or other organizations applying to administrative organs for obtaining government information shall use the written form (including data message)." It also states, that "an application for government information disclosure shall include the following: (1) the name or designation, and contact information of the applicant; (2) a detail description of the government information to be disclosed; (3) the formal requirements for government information to apply for disclosure." *The Opinions of the General Office of the State Council on Conducting the Disclosure of Government Information upon Requests* (No. 5 G. F. [2010]) also states that, "in practice, sometimes there is an application for disclosure of government information produced or stored by multiple administrative organs, and some applications involve diverse types and items of information. If the administrative organ handling the case cannot provide such information as required, or there is difficulty to specify which information is nonexistent or belongs to which administrative organ, the efficiency of handling would be affected. Thus, in order to improve the work efficiency and the convenience for applicants to gain access to the disclosure information as soon as possible,

if some application requires multiple items to be disclosed, the administrative agency handling the application may ask the applicant to adjust the application according to the principle of "one item, one application"; that is, a government information disclosure application only corresponds to one information item. At the same time, if the government information disclosure in the application is divided far detailedly, that is the applicant submits several applications with similar information disclosure contents to the same administrative organ for a specific matter, the administrative organ needs to split such existing information before replying, then the accepting organ may ask the applicant to merge the applications in a proper way. "In addition, some local government regulations may provide for more details on how to express relatively clear and specific intentionin in the application submitted by applicants.[4]

Legislation requires applicants to express the intention clearly and specifically in the application. Its essence is to seek a balance between protecting citizens' rights to know and reducing unnecessary costs incurred by administrative organs. However, that should be interpreted from the perspective of giving full play to the function of the government information disclosure system, which should not be an excuse for administrative organs to refuse to disclose government information.

2. Understanding how the expression of intention is communicated to the administrative agency ("Reach")

In general, "reach" of intention expressed upon the administrative agency (how the expression of intention is communicated) is a vital element or a prerequisite for its legal effect. Two theories in the civil law have been looked on as criteria to determine the "reach" of expressing the intention, namely the space domination by the recipient and the reasonable expectation of knowing. That is to say, the expression of intention has to reach the space domain where the recipient can exercise his or her domination, so that the said expression of intention can be known or can be expected to learn the contents under ordinary circumstances.[5] That judgmental standard for the reach of intention expressed can also be grafted in the field of government information disclosure. For some certain information disclosure application, the written application documents, the carrier of the applicant's intention, reach the administrative agency in printed paper documents or corresponding data messages, and accordingly the administrative organ can be expected to know the possible reach.

Regarding the possibility of knowing, Article 4 of the *Regulation on the Disclosure of Government Information* in accordance with which the people's governments at all levels and the people's governmental departments at or above the county level

[4]For example, Article 21, Paragraph 1 of the *Regulations on Information Disclosure of Shanghai Municipal Government* stipulates that, "If citizens, legal persons or other organizations apply to an administrative organ for disclosure of government information in accordance with Article 13 of the *Regulations on Disclosure of Government Information*, it shall submit an application stating the following contents: (1) the name or designation and contact information of the applicant; (2) specific government information contents, including the name, document number or other characteristic descriptions of the document that can pointed out; (3) methods and formality of obtaining such government information."

[5]Zhu [3].

shall establish and improve the government information disclosure system of their respective administrative organs, and designate agencies to be responsible for the daily work of government information disclosure. Article 19 also provides that the administrative agency shall compile and publish guidelines and catalogues for the disclosure of government information and update them in a timely manner. A guide to the disclosure of government information shall include the classification, arrangement system and access to government information, as well as the relative agencies' name, office address, work hours, telephone number, fax number, e-mail address, etc. Therefore, unless the applicant agrees that the transmission of the application for government information disclosure to the designated equipment or e-mail box of the administrative agency in the form of data message is to be deemed "reach" and the administrative agency is aware of it, if the people's governments at all levels have designated the relevant working organization as the specialized agency for government information disclosure and announced the name, office address, office hours, telephone number, fax number and e-mail box of the working organization to the public through various means, the printed paper form of the application documents for information disclosure shall be deemed to reach the administrative agency and have the possibility of getting learned or known by the said agency; if an administrative agency has designated a specialized agency but the application for government information disclosure reaches other agencies within other administrative agencies, it shall be deemed that the administrative agency has the possibility of knowing when the other agencies transfer the application to the specialized agency; if a government information disclosure institution is not designated, the application for government information disclosure shall be deemed that there is the possibility of getting known when it reaches the administrative organ.

If an application for information disclosure is directly mailed to the legal representative of an administrative organ, can it be regarded as being known to the administrative organ? It is generally believed that administrative law includes both the law about administrative organization and the law concerning administrative action. The former regulates all levels of administrative organization structure, jurisdiction (authority), branch divisions, allocation of responsibilities, staffing and internal discipline, while the latter regulates the operation of administrative organizations and the rights and obligations with the people.[6] Generally speaking, the law about administrative organization is concern with the internal power operation of the administrative agency, while the law regulates administrative action is chiefly concerned with the external power operation of the agency. The gain and loss change of the administrative legal relationship is caused by the administrative agency exercising its administrative power externally, which belongs to the scope of the law regulating the administrative action. The legal representative of the administrative agency and the departments, offices, sections and offices within the administrative agency all belong to the internal components of the agency, unless laws and regulations clearly provide that they can become the administrative subject. Article 62 of the *Organic Law of the Local People's Congresses at All Levels and Local People's Governments at All Levels* states

[6]Wu [4].

that, "local people's governments at all levels shall implement the accountability system respectively for governors, mayors, and heads of provinces and municipalities, heads of cities, of counties, of districts, of townships and towns including autonomous regions, and whom shall preside over the work of local people's governments at all levels". Such provisions should be understood as a hierarchical supervisory and administrative relationship based on the principle of division of labour within the administrative agencies, without any direct legal effect to the public, and the legal representative of the administrative agencies cannot generally make decisions and express them in his own name. In the current framework of administrative litigation in our country, the internal hierarchical supervision and administration regulated by the law concerning the administrative organization is generally not within the scope of administrative litigation. "The general administrative organization is formed by a pyramid system of hierarchical structure (hierarchical system) through appropriate distribution of authority. In this hierarchy, the important principles for administrative agencies to exercise their authority are the principle of authority distribution and the principle of command and supervision with the characteristics of bureaucracy."[7] In principle, all acts directed towards the public are carried out in the name of the agency before they come into force."[8] Therefore, to mail the application for government information disclosure to the legal representative of the administrative agency instead of the legally designated government information disclosure organization can only produce the legal effect of internal supervision and management by the legal representative of the administrative agency in terms of the law concerning administrative agency's actions, but cannot directly produce the legal effect exerted by the reach of the intention expressed upon the administrative agency, that is to say, the status of the legal representative of an administrative agency enjoyed in accordance with the organic law and the status of the said legal representative enjoyed in accordance with the law concerning administrative action has been confused.

Under the circumstances that *Regulation on the Disclosure of Government Information* and local government regulations have designated the corresponding agencies of the people's governments at all levels as the agencies for government information disclosure, only mailing the application for government information disclosure to the legal representative of the administrative agency instead of the agencies for government information disclosure cannot be deemed that as the administrative agency has learned of the application. However, for applications that have met the formal requirements and fallen within the scope of government information disclosed by the administrative organ, even if the applicant submit an application to the legal representative and other internal organizations instead of the government information disclosure organization, the administrative organ shall still forward the application to the corresponding government information disclosure organization based on the principle of timely protection of the right to know and reduction of the burden on the applicant. In such case, the relevant reply period shall also be calculated on the day

[7] Ichihashi et al. [5].

[8] Wu [4].

when the designated government information disclosure agency actually receives the forwarded application.

3. Understanding of the "Frivolous Application" in the government information disclosure

As a restriction on the exercise of private rights, the principle of prohibiting abuse of rights is the result of social development and the conceptual changes of legal rights. The principle of prohibiting abuse of rights requires that if the right holder exercises his rights in an unfair way, such exercise of rights is wrong and should therefore be prohibited. According to the *Encyclopedia of International Comparative Law*, there are mainly six types of abuse of rights, namely intentional damage, lack of legitimate interests, choice of harmful ways to exercise rights, the damage caused by the exercise of rights is greater than the benefits obtained, violation of the purpose of rights and violation of the general principles of tort law. In this regard, Article 13(1) of the *Civil Procedure Law* also provides that civil proceedings shall follow the principle of good faith.

The principle of prohibiting abuse of rights requires that applicants government information disclosure should not be "frivolous" or vexatious. Frivolous applications, also known as entangled applications, nuisance applications, abuse of the right to apply for government information and abuse of the right to know, were defined in a guiding outline provided by Scotland's Information Disclosure Commissioner to public institutions in 2012. It is stated that: such application would impose a significant burden on public institutions, while (1) the application has no serious purpose or value; or (2) its purpose is to harass or trouble public institutions; or (3) it would cause disturbance to the normal work of the public institutions in effect; or (4) the application in or of itself is unreasonable or out of proportion to a person with basic rationality.[9] Article 14 of the *British Freedom of Information Act* stipulates that if an applicant's application is found to be unreasonable or vexatious, public agencies are not required to fulfill their obligation to provide the applicant with the applied information.

When the *Regulations on Disclosure of Government Information* was enacted, the government information disclosure system was mainly oriented to towards promoting the administration of administrative agencies according to law, and further enhancing the public's awareness. There was no clear provisions for the abuse of the right to know. In practice, when the public questioned the legality of administrative action, they tend to choose applying for the information disclosure.[10] Researches suggest that the abnormal application for the disclosure of government information in our country includes the following situations: applicant may (1) intentionally repeatedly apply for disclosure due to dissatisfaction with compensation and resettlement for land acquisition and relocation; (2) seek some illegitimate benefits or vent personal emotions by applying for information disclosure; (3) intend to solve the problems left over by the past through the disclosure of government information; (4) intend

[9] Wang [6].
[10] Hou [7].

to get self-promotion in the name of public interest; (5) name as the application for government information disclosure but consultation and complaint in the name of application for disclosure via letters and visits; (6) apply for disclosure of government information already obtained.[11] In principle, right to know is exercised is regardless of the subject, or the motivation and purpose, or the object and content, or the number of times. The purpose of regulating frivolous applications is to ensure that valuable resources of public institutions are not wasted or allocated disproportionately. Therefore, the administrative agency should still prudently determine whether the applicant has made a frivolous application, and bear the corresponding obligation to explain the reasons and the burden of proof.

4. Necessity of right protections in administrative litigation of government information disclosure

In consideration of judicial resources, costs and expenses incurred to the parties, and the limit of jurisdiction, it is not always necessary for the court to hear and adjudicate all the claims raised by the parties, or the court is able to hear and adjudicate all these claims.[12] Thus, the prerequisites for initiating a legal action and requests any trial have to be premised on the determination of the necessity to protect the rights in the lawsuit. "The necessity to protect rights involved in the lawsuit, is to determine a beneficial, efficient, timely and legitimate opportunity for right and remedy."[13]

It is generally believed that the following kinds of important situations are short of benefits of litigation and thus not worthy of rights protection: (1) the purpose can be achieved or has been achieved through other simpler ways; (2) the purpose of the lawsuit could not have been realized due to legal or factual reasons, or winning the lawsuit has no practical significance; (3) the purpose of the lawsuit is to cause damage to the other party or the third party, or the plaintiff contradicts himself/herself because of some prior act, or the limitation of action has expired.[14] China's administrative procedure law does not specify the necessary provisions for the rights protection, in *Li X v. the People's Government of Chaoyang District* and others such, the Supreme People's Court held that, "in accordance with Article 1 of the *Administrative Procedure Law*, the primary purpose of the people's court in hearing administrative cases is to protect the legitimate rights and interests of citizens, legal persons or other organizations. Article 2 of this law therefore provides that citizens, legal persons or other organizations have the right to bring an administrative lawsuit to the people's court if they believe that the administrative action of administrative agencies and the executive staff infringe upon their legitimate rights and interests. Accordingly, *Administrative Procedure Law* is first and foremost the legal remedies for damage to the rights. The premise for bringing an administrative lawsuit is the possibility

[11] Li [8].
[12] Zhang [9].
[13] Wang [10].
[14] Friedhelm [11].

that the sued administrative action infringes upon the plaintiff's legitimate rights and interests."[15]

In the administrative lawsuit of government information disclosure, the right to know is the interest of the lawsuit itself.[16] To judge whether the plaintiff's suit is necessary for the protection of rights, one can judge whether the disclosure of his application information is an abuse of the right to know and whether the purpose of suit is to realize the right to know. If the administrative agency can prove that the applicant made the application frivolously, or the court found that the purpose of the plaintiff was to obviously and unreasonably consume administrative and judicial resources upon examination, it can be considered that there is no necessity to protect the right. For example, if the applicant has obtained the corresponding information through government information disclosure and applies repeatedly, or requests the administrative agency to provide government bulletins, newspapers, magazines, books and other public publications, and the administrative agency refuses to do so, the lawsuit has no interest in litigation. However, according to Item 2, Article 12 of the *Provisions on Hearing Administrative Cases of Government Information Disclosure*, if the government information applied for disclosure has already been made public and the defendant has informed the applicant of the ways and means to obtain such public government information, the people's court shall rule to dismiss the plaintiff's claim. Therefore, if the government information has been made public and the applicant files a lawsuit, the distinction on whether the litigation has any interest lies to whether the applicant files an application in good faith rather than frivolously. If the applicant objectively does not know that the administrative agency has voluntarily made public or does not know the ways and means to obtain the such information, then there has the necessity of rights protection when the applicant brings the corresponding administrative lawsuit. In this case, the interests of a lawsuit not only have the negative function of denying the lawsuit, but also have the positive function of confirming the right.

At the level of judicial policy, the Supreme People's Court does not require strict enforcement of unified interest standards for government information disclosure proceedings without exception, but rather recognizes the objective orientation of its proceedings. Because the peculiarity of the right to know is that it serves not the interests of individuals, but the public interests in participating in politics and supervising administration by law. Thus, the court should still hold a more cautious attitude to the requirement of interests in the public litigation of government information. In information disclosure litigation, although the interest of litigation is an issue of procedure, it still contains comprehensive considerations on the protection of subjective public rights, participation in politics, supervision of administration by law, maintenance of public interests, and effective allocation of administrative and judicial resources and the enhancement of their marginal utility.

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[15] See the administrative ruling (No. 3007 [2016], Retrial, Adm. Division, SPC).

[16] Shen [12].

5. Conclusion

By grafting the concept of government information disclosure as a general supply act of application with the concept of the expression of will in civil law, the application intention, the arrival of the expression of will and its legal effect in government information disclosure applications can be analyzed into more details. Besides, the relevant provisions of the *Regulations on Government Information Disclosure*, local government regulations on information disclosure applications, information disclosure specialized agencies, etc. can also be interpreted in a targeted manner.

However, the administrative agency cannot reject any application for information disclosure that has not been formulated in accordance with the law or has not been submitted to a legal specialized agency. Instead, it should try its best to safeguard the public interest implied by the right to know and make a more favorable judgment and treatment for the applicant. Furthermore, only when the plaintiff based on frivolous application and suit, obviously unreasonable consumption of administrative and judicial resources, can it be deemed that there is no necessity of rights protection.

The judgment of this case has established a correct way to apply to the administrative agency for government information disclosure, and has clarified the disposal principles and examination standards for applications that obviously do not conform to the statutory application form and fail to pass the government information disclosure organization in accordance with the law.

First, it is the right of citizens, legal persons or other organizations to obtain government information according to law. Administrative agencies should actively perform their duties of government information disclosure according to law to protect citizens, legal persons and other organizations' right to know. However, when citizens, legal persons or other organizations apply for the disclosure of government information, they shall submit the application to a specific administrative government information disclosure organization in a statutory form consistent with the provisions of laws and regulations. For applications of government information disclosure that do not meet the formal requirements of government information disclosure applications or not submit to the designated government information disclosure agencies, the administrative agency could give proper response in accordance with the contents of the letters.

Second, for applications that meet the formal requirements of the application and fall within the scope of government information disclosure by the administrative agency, even if the applicant does not apply to the specific government information disclosure institution, but to the legal representative or other internal organization, the administrative agency shall still forward such application to the government information disclosure institution of the administrative agency based on the principle of timely protection of the right to know and reduction of the burden on the applicant. Under such circumstances, the date of receipt of the forwarded application or the date of confirmation with the applicant shall be taken as the date of receipt of the application by the information disclosure agency.

Third, if the application for government information disclosure does not meet the formal requirements, and does not fall within the scope of the designated government information disclosure, and which has not been mailed to the government information disclosure institution in accordance with law, the administrative agency could handle the application not as a government information disclosure application. If the applicant thus brings an administrative lawsuit on the ground that the administrative agency does not perform its duty of disclosure of government information, the people's court may consider that there is no necessity to protect the rights in the administrative proceedings and can rule against filing the case in the court, or dismiss the cause.

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Chen X and Zhao X v. The People's Government of Yimen County, Yunnan Province—The Grant of the Certificates by the Administrative Agency, though Flawed Procedurally, May not be Revoked Necessarily

Yonghai Wan and Wenfei Liu

Rule

The administrative registration of the housing or housing property is the ascertainment or the confirmation of the transfer or the alteration of the title to the housing property. As both parties wish to make the housing purchase, the housing registration authority may inquire into matter from the both parties, then after prudent examination, make a determination that both parties have reached mutual intention to handle the administrative registration of the title to the housing property. In accordance with the application filed by one party for the registration of housing ownership, the housing registration authority had issued the certificate of ownership to the party who filed the application. Although procedural flaws are being detected, it has not yet reached the level of revocation.

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellee in the second instance): Chen X and Zhao X

Collegial panel judges of Supreme People's Court for re-trial: Wan Yonghai, Pan Yongfeng, Yang Kexiong (Written by: Wan Yonghai and Liu Wenfei, Supreme People's Court; Translated by: Peng Bo).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_37

Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): People's Government of Yimen County, Yunnan Province (hereinafter referred to as "Yimen County Government")
Respondent in the retrial (Third party in the first instance, Appellant in the second instance): Xu X, Pu X

2. **Procedural History**

First instance: No. 7 [2015], Trial, Adm. Division, the Intermediate People's Court of Yuxi City, Yunnan Province (dated May 9 of 2016)
Second instance: No. 165 [2016], Final, Adm. Division, the Higher People's Court of Yunnan Province (dated Nov. 18 of 2016)
Retrial Review: No. 181 [2017], Retrial, Adm. Division, the Supreme People's Court (dated Apr. 28 of 2017)

3. **Cause of Action**

Housing administrative registration

Essential Facts

Chen X and Zhao X are married couple, so are Xu X and Pu X. On June 26, 2015, Chen X, Zhao X and Xu X, Pu X signed Real Estate Transaction Contract of Yimen County. The contract agrees that Chen X and Zhao X is to sell their own houses (with a construction area of 7119.35 m^2 and house ownership certificate No. 0021711-1 and 0021711-2) located at Yun' an street, 6th street, Yimen county to Xu X and Pu X, with a transaction price of RMB 14,000,000 yuan. The contract also agrees that both parties shall submit the application for the transfer of housing ownership to the city or county housing registration authority where the house is located. Both parties shall also submit the following files: the *Yimen County Real Estate Transaction Contract*, the housing ownership certificate, the tax payment certificate and other relevant materials. On the same day, Chen X and Xu X signed a supplementary agreement on housing sale and purchase in, which both parties agree that Chen X shall return the money owed to Xu X from the date of signing the purchase agreement until August 16, 2015. In case of Chen X's failure to return the money due, Xu X will follow the relevant provisions of housing purchase in accordance with the law. On the same day, Real Estate Trading Center of Yimen County had verified the contract. The Housing Administration Office of Yimen County had inquired both parties about the registration of the house transaction and made a written record the inquiry into. The contract was registered with registration number 139 (2015). On August 17. 2015, the Yimen County Real Estate Trade Center, entrusted by Xu X and Pu X, had made a surveying and mapping of the housing area, and then issued *Housing and Building Area Surveying and Mapping Report of Yimen County Real Estate Trade Center* (Yimen Surveying No. 2015-298). On the same day, Xu X and Pu X had completed the tax

payment on the amount of RMB 1,129,764.28 yuan, including business tax, deed tax and other taxes. They had filled out the form of *Housing Ownership Application of Yimen County* and submitted it to the Housing Administration Office of Yimen County. The Office had inquired into the relevant information of housing ownership transfer and made a written record of *Inquiry into Housing Registration*. On August 18. 2015, after examination of the relevant documents including *Certificate of Housing Ownership*, *Real Estate Transaction Contract*, *Inquiry of Housing Transaction Registration*, as well as the copies of deed tax invoice and the *Housing and Building Area Surveying and Mapping Report of Yimen County Real Estate Trade Center* which were provided by Xu X and Pu X, Yimen county government had completed the registration of housing ownership under the names of Xu X and Pu X, and issued the housing ownership certificates (Yimen County Zi No. 0022517-1 and No. 0022517-2). On the next day, Pu X had collected the two house ownership certificates as mentioned above. On September 8. 2015, Yimen County Real Estate Registration Center has been established. The administrative function of housing registration of Yimen County Housing Administrative Office has been transferred to Yimen County Real Estate Registration Center.

On December 11. 2015, Chen X and Zhao X filed a lawsuit, requesting to revoke the housing ownership certificates No. 0022517-1 and No. 0022517-2 issued by Yimen county.

The first instance judgment of the Yuxi City Intermediate People's Court, Yunnan province, holds that the housing ownership certificates of Yimen county No. 0022517-1 and No. 0022517-2 issued by the government of Yimen county are to be revoked.

Yimen county government, Xu X and Pu X appealed against the decision. The second instance judgment of the Higher People's Court of Yunnan province holds that "(1) No.7 Adm. Trial of Intermediate People's Court of Yuxi city, Yunnan Province (2015) is revoked; (2) the action initiated by Chen X and Zhao X is dismissed."

Chen X and Zhao X appealed to the Supreme People's Court for a retrial.

Issues

After the Housing Administrative Office of Yimen County inquired into the transaction between Chen X, Zhao X and Xu X, Pu X and completed the housing registration, People's Government of Yimen County issued the certificate of ownership to Xu X, Pu X in accordance with the registration application filed by them and the inquiry into only one party. Therefore the issue of the case is that whether it is lawful for the People's Government of Yimen County to issue the certificate of ownership to Xu X and Pu X, and whether the issued certificate shall be revoked.

Holding

The main reasons for Chen X and Zhao X's retrial application to the Supreme People's court are: (1) There is no legal basis for the court of second instance to exclude *the Provisional Regulations on Real Property Registration* in its application of law, resulting in an error in citing the law; (2) There is no evidence in the judgment of second instance to prove that the retrial applicant has manifests "the intention to register the transfer of housing ownership". Thus, Chen X and Zhao X requested the Supreme People's Court to reverse the judgment of the second instance and affirm the judgment of the first instance.

The Supreme People's Court held in accordance with provisions of Article 12 (1) of the *Real Right Law*, Articles 12 and 18 of *Housing Registration Measures*, and Article 14 (1) of the *Provisional Regulations of the People's Republic of China on Real Property Registration*, both parties shall file an application when registering real property (including housing registration), and the registration authority shall inquire into both parties. The above laws and regulations are made for the reasons that real estate registration is a prudent and serious administrative act; it is to be ascertained that the applicants have manifested true and real intention to register the transfer and alteration of real estate property. It should be pointed out that the *Provisional Regulations of the People's Republic of China on Real Property Registration* comes into force on March 1, 2015. As the administrative organ which performs the duties of real estate registration, the Housing Administration Office of Yimen County can undoubtedly apply these regulations for real property registration. The court of second instance's decision is improper to exclude the application for the reason that the registration date of the case involving housing property lags behind the establishment of the Real Property Registration Center of Yimen County. In this case, Chen X, Zhao X and Xu X, Pu X signed *Real Estate Transaction Contract of Yimen County* to express the mutual intention of agreeing on matters related to the housing transaction. The Housing Administration Office of Yimen county inquired both parties about the issues about housing transaction and registration, and made a written record of *Inquiry of the Housing Transaction Registration,* then completed the registration of their contract. The inquiry and registration not only mean the confirmation of the authenticity of the housing transaction, but also the confirmation of matters on the agreement of housing ownership transaction reached by both parties and so on. After investigation, compared with *Inquiry of Housing Transaction Registration*, *Inquiry of Housing Registration* only presents 6 more items, that is, "whether there is any objection to the area of the housing to be registered". The two records are highly identical in contents. Therefore, it can be determined that *Inquiry of Housing Transaction Registration* can manifest the true intention of Chen X and Zhao X to transfer the case involving housing property to Xu X and Pu X. At the same time, in *Inquiry of Housing Transaction Registration*, Chen X, Zhao X and Xu X, Pu X all confirmed the authenticity of the relevant documents submitted to the Housing Management Office of Yimen County. The housing administrative registration is the confirmation of property changes of the real ownership such as

the housing transfer and alteration. Therefore, after inquiring into the transaction registration between Chen X, Zhao X and Xu X, Pu X, the People's Government of Yimen County issued the certificate of ownership to Xu X, Pu X in accordance with the registration application filed only by Xu, Pu and the inquiry into only one party between the buyer and seller. Although flaws have been detected in the procedure, this can not be said to amount to the degree that the issued certificate has to be revoked. As for the supplementary agreement for the housing purchase and sale signed by Chen X and Xu X on June 26, 2015, though it has not been submitted to Housing Administrative Office of Yimen County, it can't be used as a legal basis for judging whether the act of issuance of certificate by the People's Government of Yimen County is lawful. To sum up, although the act of issuance of the certificate by the People's Government of Yimen County is flawed in the procedure, this can not be said to amount to the degree that the issued certificate has to be revoked necessarily. Article 91 of the *Administration Procedural Law* can be applied to the application submitted by Chen X and Zhao X. In accordance with Article 101 of *Administrative Procedure Law*, and Article 204 (1) of *Civil Procedural Law*, it is to be decided that the application submitted by Chen X and Zhao X be dismissed.

Comment on Rule

1. **Relevant laws and regulations provide that, the housing registration authority shall register the transfer of ownership in accordance with a joint application by both parties in a housing transaction, for the purpose that the application for registration manifests the true and real intention of the applicants**

Article 14 (1) of the *Provisional Regulations of the People's Republic of China on Real Property Registration* provides, "where an application for real property registration is made for sale or mortgage, both parties of the transaction shall file a joint application." Article 12 of (1) *Housing Registration Measures* (Order No. 168 of the Ministry of Construction of the People's Republic of China) provides: "the application for housing registration shall be jointly applied by both parties, unless provided otherwise." The above-mentioned administrative laws, regulations and provisions are made for protecting the vital and legitimate interests of the parties, and ascertaining the manifestation of the true and real intention of the real property registration. More specific and operational provisions for this matter are found in other laws and regulations. For example, Article 12 (1) of the *Real Right Law* provides: "the registration authority shall perform the following duties: (1) Examine and verify ownership certificate and other necessary materials provided by the applicant; (2) Inquire the applicant about relevant registration matters…". Article 18 (1) of *Housing Registration Measures* also provides that "the housing registration authority shall examine application materials for registration, and shall also inquire applicant about the following registration application matters based on different types of registration:

whether the registration application is a manifestation of true and real intentions of the applicant, whether the housing to be registered is co-owned, whether the property holder agrees on the transfer or the alteration, and whether other relevant matters in the application materials need to be further clarified. The result of inquiry shall be signed by the applicant and be kept on file."

2. **The legitimacy for the housing registration authority to issue a housing ownership certificate by the registration application submitted by only one party has to be examined or reviewed procedurally**

In accordance with the laws and regulations, when housing registration authority handles ownership registration, it shall receive a joint application from both parties, and after examining or verifying the application documents, it shall also inquire applicants in accordance with the law, the purpose of which is to make sure of the manifestation of the true intentions of applicants. In this case, after Chen X, Zhao X and Xu X, Pu X signed *Real Estate Transaction Contract of Yimen County*, the Housing Administrative Office of Yimen County inquired about relevant matters of the housing transaction registration and then made the written record of *Inquiry of Housing Transaction Registration.* Then that, the said Office has the transaction contract registered. The registration processes conducted by the Office can be deemed a confirmation that the manifestation of mutual intention of both parties has been achieved to conduct the housing transaction. Generally, if the validity of the house transaction can be confirmed, it can be found that the seller and the buyer have manifested their true intention to have the transfer of the title to the housing ownership registered. This is further proved by the fact that the records of *Inquiry of Housing Registration* and *Inquiry of Housing Transaction Registration* produced by the Housing Administrative of Yimen County are identical. Thus, the present collegiate panel holds, though the issuance of certificates by the People's Government of Yimen County, does not strictly conform to the laws and regulations, in view of the fact that the transaction was handled in the interim period before new laws comes into effect, and that the new real estate transaction institution is yet to be formed in Yimen County, and that the registration of the housing ownership transfer manifests the true and real intention of both parties, the failure of one party to be present when the registering of the housing ownership transfer may constitute a procedural flaw, but that procedural flaw may not amount to the degree that the registration has to be revoked necessarily revoked.

3. **The supplementary agreement not submitted to the housing registration authority or Yin-Yang Contract can not serve as a legal basis to determine the legality of the housing ownership registration**

In practice, because of the different purposes on behalf of the applicants, the transaction contract submitted to the housing registration authority is inconsistent with the contents of its actual transaction, such significant changes as contract price registration of the housing ownership are even found in the contract. In the case at hand, Chen X, Zhao X and Xu X, Pu X signed *Real Estate Transaction contract of Yimen County*, after that they signed a *A Supplementary Agreement of Housing Sale and Purchase*.

As such clauses or attitudes as liquidation about the assignment security are contained in the Supplementary Agreement, the said agreement may not be deemed as a contract of sale. The collegiate panel also pointed out in the review process that the manifestation of mutual intention of both parties in registering the housing ownership has to be prudently determined. Upon further examination and confirmation, it is found that when applying for registration of the housing ownership, no supplementary agreement has been submitted to the Housing Administration Office of Yimen County, who has also no knowledge of the existence of the said agreement. Therefore it cannot be used as a basis to decide whether the Yimen county government's issuance of the certificate is legal. Whether the supplementary agreement will affect the rights and obligations of both parties can be resolved separately in accordance with the law.

In sum, the housing registration authority have confirmed the manifestation of mutual intention of ownership registration from both parties by examining the submitted documents and inquiring both parties in the transaction. The administrative act in reliance upon the application of a single party to the housing ownership registration constitutes a procedural fault or defect, yet that procedural defect on fault may not amount to the extent that the issuance of the certificate itself has to be revoked altogether.

The Compensation Agreement by the People's Government of Haitang District, Sanya City, Hainan Province (Dispute over the Conclusion of Compensation Agreement for Government Taking)—The Conclusion of Administrative Agreements Shall be Within the Scope of Administrative Agency's Discretion

Xiujiang Guo

Rule

Any act that violates laws, administrative regulations, local regulations, legal and effective rules and according normative documents, can be verified as an illegal administrative act. When signing an administrative agreement, the administrative organ shall proceed within the scope of its discretion. It shall neither infringe upon the interests of the nation, the public and the lawful rights and interests of others, nor damage the lawful rights and interests of the counterparty in the name of signing administrative agreement.

An signed administrative agreement will not necessarily be revoked or nullified if the act of signing is held illegal. If the violation of administrative agreement procedures is immaterial but and without infringement of the lawful rights and interests of the plaintiff, or, if the revocation will infringe the national and public interests, then the signing act shall be ruled as the violation of law, at the same time the agreement shall not be revoked, and the court shall sustain the legal effect of its relevant provisions.

Collegial panel judges of Supreme People's Court for re-trial: Guo Xiujiang, Gong Bin, Wang Yuying (Written by: Guo Xiujiang, Supreme People's Court; Translated by: Peng Bo).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_38

Case Information

1. **Parties**

Applicant in the retrial (Defendant in the first instance, Appellant in the second instance): People's Government of Haitang District, Sanya City, Hainan Province (hereinafter referred to as "Haitang District Government")
Respondent in the retrial (Plaintiff in the first instance, Appellee in the second instance): Zhai X (A)
Respondent in the retrial (Plaintiff in the first instance, Appellee in the second instance): Liu X
Respondent in the retrial (Plaintiff in the first instance, Appellee in the second instance): Zhai X (B)
Respondent in the retrial (Plaintiff in the first instance, Appellee in the second instance): Li X
Respondent in the retrial (Plaintiff in the first instance, Appellee in the second instance): Zhai X (C) [former name: Zhai X (D)]

2. **Procedural History**

First Instance: No. 185 [2016], Trial, Adm. Division, the Intermediate People's Court of Sanya City, Hainan Province (dated Jun. 12 of 2016)
Second instance: No. 422 [2016], Final, Adm. Division, the Higher People's Court of Hainan Province (dated Nov. 22 of 2016)
Application for Retrial: No. 5250 [2017], Retrial, Adm. Division, the Supreme People's Court (dated Aug. 25 of 2017)

3. **Cause of Action**

The conclusion of the agreement on compensation for expropriation (government taking) and the failure to perform the legal duties of resettlement in accordance with the law

Essential Facts

Zhai A and other respondents are originally from Henan Province. In 1994, with the approval of the Committee of Zhuangdacun Village, Haitang District, Sanya City (hereinafter referred to as Zhuangdacun Village Committee), and the permission of local public security administration, the Zhai's emigrated to the first village group under Zhuangdacun Village Committee. They had been granted a tract of land to build the house where the family still live in. On November 22, 2007, due to the construction needs of the project of Haitangwan Tourism and Holiday Development Zone and relevant Roads Zhai X (A) and other respondents' residential land and

housing were expropriated. Zhai X (A) and others signed *Compensation and Resettlement Agreement for Land Expropriation and Demolition in Zhuangdacun Village* with Haitang District Government, agreeing to stipulated resettle in the form of apartment as in provisions in the document bearing Sanya Gov. Doc. No. 107 (2007). After the agreement was signed, both parties did not perform the agreement. On July 17, 2012, People's Government of Sanya City (hereinafter referred to as "Sanya Government") approved the implementation of *Compensation and Resettlement Plan for Land Expropriation and Demolition in Haitangwan Town* (hereinafter referred to as "the 2012 Resettlement Plan"). In order to implement the resettlement, in 2013 Haitang District Government issued *Detailed Rules for the Resettlement in Haitangwan town* (hereinafter referred to as "the 2013 Resettlement Rules"), further clarifying the principles of individual resettlement, the conditions for determining resettlement targets, the procedures for determining individual resettlement and targets, as well as the specific resettlement methods. In the 2013 Rules for Resettlement, Article 2 states that the expropriated shall be resettled by "households"; the resettlement target is directed at the expropriated and their family members who own legal real property within the expropriation and demolition area, and entitled with rights and undertake obligations inside the collective economic organization. Article 3 states that Haitangwan area will provide a style of row house scenery town for resettling. The village (residential) committees shall resettle the farmers whose lands or houses are expropriated for Haitangwan Project in the nearby scenery town in unit according to residential conditions. The row house in the town has four models including 150, 200, 250 and 300 m^2. The resettlement standard is 50 m^2 for each person. If the number of a household exceeds the number determined by the resettlement standard for the largest size, the exceeding number will be resettled in the apartment building with a standard of 60 m^2 per person. As the expropriated residents, Zhai X (A)'s family have a total of five persons who meet the resettlement requirements in his household, namely Zhai X (A), Liu X, Zhai X (B), Li X and Zhai X (C). In 2009, 2010 and 2015, Zhai X (A) and other respondents filed three lawsuits because Zhuangdacun Village Committee did not distribute the same compensation amount for expropriation to Zhai X (A) as other villagers received. Sanya Intermediate People's Court and Sanya Suburban People's Court made the judgements including No. 60 [2009], Final, Civil Division, the Intermediate People's Court of Sanya City, No. 615 [2010], Trial Civil Division, the Suburban People's Court of Sanya City, No. 262 [2015], Final, Civil Division, the Intermediate People's Court of Sanya City. All these civil judgments confirm that Zhai X (A) and other respondents have the membership of the first village collective economic group of Zhuangdacun Village Committee. Zhuangdacun Village Committee shall give the proper compensation to Zhai and other respondents as the same amount given to other villagers. On September 7, 2015, in order to expedite the hydrographic system construction in the central area of Haitang district, Haitang District Government signed *Compensation and Resettlement Agreement for House Expropriation and Demolition in Haitang District* (hereinafter referred to as "the 2015 Compensation Agreement"). The main contents of the agreement are as follows: Zhai X (A)'s expropriated house size is 143.91 m^2, and the number of person

for resettlement is five. The resettlement is carried out by means of property replacement. The house for resettlement is in an apartment building in Linwangbei Town with an area of 120 m^2. After the agreement was signed, Haitang District Government demolished Zhai X (A)'s house on September 8 and 9, 2015. On November 5, 2015, Zhai X (A) and other respondents applied to Haitang District Government for an illegal resettlement, but Haitang District Government did not reply. On January 11, 2016, Zhai X (A) and other respondents filed an administrative lawsuit for this case, claiming that the 2015 Compensation Agreement was signed under intimidation and against their true intent. They request to make the 2015 Compensation Agreement invalid and be compensated a 250 m^2 row house in Linwangbei town in accordance with the 2013 Rules for Resettlement.

The First Instance Court made the judgment on June 12, 2016 which determine that a 120 m^2 house in apartment building given to Zhai and other respondents by Haitang District Government in the 2015 Compensation Agreement is invalid. Haitang district government shall give Zhai a 250 m^2 row house in Linwangbei town for resettlement in accordance with the 2013 Rules for Resettlement. Haitang District Government are dissatisfied with the judgment and appealed to the Second Instance Court which later uphold the judgment of the First Instance Court to dismiss the appeal on November 22, 2016.

Haitang District Government appealed to Supreme People's Court for retrial.

Issues

1. The accreditationn of Zhai X (A) and other respondents as members of the collective economic group;
2. Review for the effectiveness and lawfulness of the administrative agreements;
3. Application of normative documents in determining administrative case by people's courts.

Holding

Upon review, the Supreme People's Court's holds that in accordance with Article 70 of *Rules of Evidence in Administrative Litigation,* the facts determined by the effective people's court's judgment can be used as admissible evidence. In this case, Judgments numbered No. 60 [2009], Final, Civil Division, the Intermediate People's Court of Sanya City, No. 615 [2010], Trial, Civil Division, the Suburban People's Court of Sanya City, and No. 262 [2015], Final, Civil Division, the Intermediate People's Court have verified the fact of Zhai X (A) and other respondents as members of the collective economic group of Zhuangdacun village, as well as the fact that Zhai X (A) and other respondents' participation in the democratic election of

the Village Committee, compliance with the one-child policy propagated by the Village Committee, donation to the village road rebuilding construction, and engaging in individual medical services for villagers to fulfill their obligations as members of the collective economic group. According to the facts determined in those three effective civil judgments mentioned above, the judgments by the First and Second Instance Court have verified the accreditation of Zhai X (A) and other respondents as members of the collective economic group of Zhuangdacun village, they have fulfilled relevant obligations, which all conform to the rules of admissibility of evidence in administrative litigation. Haitang District Government claimed that the First and Second Instance judgments lack evidences to prove the accreditation of Zhai X (A) and other respondents as the target for resettlement, and there is no evidence to prove that Zhai X (A) and other respondents have fulfilled their obligations as members of the collective economic group. However, Haitang District Government did not introduce enough relevant evidences to deny the facts determined in those three effective civil judgments, and it shall not be upheld by Supreme People's Court since its claim has no factual basis.

Article 63 of *Administrative Procedure law* provides that the people's courts shall try administrative case in accordance with laws, administrative regulations, local regulations and rules. The third paragraph of the first part of *Summary of the Symposium on Administrative Cases* states that although the practice of administrative trails usually take references from, specific explanations to the application of the law and other normative documents formulated by relevant departments to guide the implementation of laws or administrative measures, these specific application explanations and normative documents are not formal sources of law, hence there's no binding force on people's courts. However, after examination, if the people's court believes that specific explanations to the application of the law and other normative documents for administrative act under litigation is if legal, effective, reasonable and appropriate, then the ruling shall be also taken as valid. Administrative agreement cases concern the performance of administrative functions and the realization of public management objectives, the legality of which thus must be reviewed in accordance with the rules and provisions of *Administrative Procedure Law*. Any act that violates laws, administrative regulations, local regulations, legal and effective rules and normative documents under those rules, can be verified as an illegal administrative act. When signing administrative agreement, the administrative organ shall proceed within the scope of its discretion, lest it infringe upon the interests of the nation, the public and the lawful rights and interests of others, nor damage the lawful rights and interests of the counterparty in the name of signing administrative agreement. In this case, the 2013 Resettlement Rules is not against peremption, which means it did not violate the in a higher legislative hierarchy law. So, it is legal and effective that can be used as the basis for determining the nature of 2015 Compensation Agreement signed between Zhai X (A) is and Haitang District Government, and whether it is legitimate for Haitang District Government not performing its legal obligation. From the comparison between the 2015 Compensation Agreement and the 2013 Resettlement Rules, it is obviously inconsistent with the relevant provisions of the 2013 Resettlement Rules regarding the resettlement measures, this seriously harms Zhai X (A)'s

legal rights to receive compensation and resettlement in accordance with the relevant laws and rules. Haitang District Government has the responsibility and obligation to resettle Zhai X (A)'s household in accordance with the 2013 Resettlement Rules. Therefore, the judgments of the First and Second Instance are appropriate and correct in denying the validity of the contents of compensation and resettlement for Zhai X (A) and other respondents in the 2015 Compensation Agreement signed by Haitang District government, and ordered Haitang District Government to resettle Zhai X (A)'s household in a 250 m^2 housing in Linwangbei town in accordance with the 2013 Resettlement Rules. It should be pointed out that, to invoke Article 52 of *the Contract Law* to determine the invalidity of the 2015 Compensation Agreement are unnecessary, because there are corresponding judgment standards in the *Administrative Procedure Law* and relevant administrative legal norms. The Supreme People's Court hereby points out and corrects it. Since that law citation did not affect the legality of the judgments of the first and second instance, the case will not be retried.

Article 29 of the *Administrative Litigation Law* provides that citizens, legal persons or other organizations who have interest with the administrative act under litigation but who have not brought a lawsuit, or those who have an interest with the judgment of the case, may apply for a third party in the lawsuit or be notified by the people's court to participate in the lawsuit. Subject to Article 91(5) therein, if the original judgment omits any serious violation of legal procedures by the party, a retrial shall be conducted in accordance with the law, and the original judgment shall be reversed and retried. In this case, the administrative act in litigation is the act of Haitang District Government's signing of a rettlement compensation agreement with Zhai X (A) and other respondents, and the act of Haitang District Government's failing to perform its legal duties of settlement for Zhai X (A) in accordance with law. The First Villager group of Zhuangdacun Village Committee, in which Zhai X (A) and other respondent be part of, has no interest with these two administrative acts under litigation, and there is no relevance with the judgment of this case. The judgment denies neither rights of the First Villager Group of Zhuangdacun Village Committee, nor obligations be added. Therefore, the First Villager Group of Zhuangdacun Village Committee does not have to be a third party to participate in the Litigation. The First and Second Instance did not add it as a third party to participate in the Litigation, which does not violate the legal procedures. The reason that claimed by Haitang District Government of the First Villager Group of Zhuangdacun Village Committee having an interest with the case, is not sufficient. The court will not support the application for retrial on this ground.

To sum up, Haitang District Government's retrial application does not apply to Article 91(3,4,5) of the *Administrative Procedure Law*. In accordance with Article 74 of the *Judicial Interpretation of the Application of the Administrative Procedure Law*, the retrial application by the People's Government of Haitang District, Sanya city, Hainan Province, shall be rejected.

Comment on Rule

1. **Legal conditions for membership of collective organizations**

Article 70 of the *Rules on Evidence in Administrative Litigation* states that facts determined by the effective people's court's judgment can be used as the basis for case judgment. That is to say, the effective judgment can be used as the basis for determining citizens' membership of collective organizations However, there are three main legal conditions for determining the membership of collective organizations: first, whether the household is registered within the collective economic organization; Second, whether they enjoy the rights of members of collective economic organizations; Third, whether they fulfill the obligations of members of collective economic organizations. In this case, Zhai X (A) and his household emigrated to the First Village Group of the Zhuangdacun Village Committee and had been distributed a land to build the housing in which they had been resided until now.. Zhai X (A) and other respondents actively participated in the democratic election of Village Committees and they enjoyed the right to vote and to be elected as members of the collective economic group. At the same time, Zhai X (A) and other respondents' compliance with the one-child policy propagated by the Village Committee, donation to the village road rebuilding construction, and engaging in individual medical services for villagers are provided the fact of fulfilling their obligations as members of the collective economic group. Therefore, the effective judgment of the people's court finds that Zhai X (A) and other respondents' membership of the first village collective economic group of the village Committee is legal and valid.

2. **The review of the legality of administrative acts in the application of normative documents**

Article 63 of the *Administrative Procedure Law* provided that the people's courts shall try administrative cases in accordance of laws, administrative regulations, local regulations and rules. The third paragraph of the first part of *Symposium Minutes of Hearing Administrative Cases* states that in the practice of administrative trials, specific explanations to the application of the law and other normative documents formulated by relevant departments to guide the implementation of laws or administrative measures are often involved. These specific application explanations and normative documents are not formal sources of law and are not binding on people's courts in the sense of legal norms. However, after examination, the people's court believes that specific explanations to the application of the law and other normative documents applied by the administrative act under litigation shall be regarded as legal, effective, reasonable and appropriate, and should be also taken as valid when determining the legality of the specific administrative act. Administrative agreement cases involve the performance of administrative functions and the realization of public management objectives. As administrative cases, the legality of the administrative agreement acts under litigation must be reviewed in accordance with the rules and provisions of Administrative Litigation Law. Any act that violates laws, administrative regulations, local regulations, legal and effective rules and normative

documents under those rules, can be verified as an illegal administrative act. When signing administrative agreement, the administrative organ shall proceed within the scope of its discretion. It shall neither infringe upon the interests of the nation, the public and the lawful rights and interests of others, nor damage the lawful rights and interests of the counterparty in the name of signing administrative agreement. That is to say, legal and effective normative documents can be used as the basis for determining the legality of administrative acts In this case, the 2013 Resettlement Rules did not violate the higher-level law, which makes it legal and effective administrative normative documents. Haitang District Government shall perform its legal duties in accordance with the normative documents and compensate Zhai X (A) and other respondents with resettlement. The First and Second Instance judgments denies the validity of the compensation and resettlement for Zhai X (A) and his household in the 2015 Compensation Agreement signed with Haitang District Government, and ordered Haitang District Government to resettle Zhai X (A)'s household in a 250 m^2 housing in Linwangbei town in accordance with the 2013 Resettlement Rules. The judgments is appropriate and just.

3. **Trial rules for administrative agreement case**

As administrative case, administrative agreement case shall be tried in accordance with the provisions of the *Administrative Procedure Law*, which cannot be tried in accordance with the rules of the *Civil Procedural Law*. Therefore, the trial object of administrative agreement case can only be the acts of administrative agreement under litigation, whereas not administrative agreement disputes. The content of administrative agreement case trial can only be the legality of the acts of administrative agreement and the concurrent administrative compensation for the infringement or violation of the acts of administrative agreement, whereas not the Liability for breach of contract in contract disputes. The standard for administrative agreement case review should be administrative laws and regulations, legal and effective rules and normative documents, as well as effective agreements between the parties, whereas not civil legal norms. The judgment for administrative agreement case must be made in accordance with the relevant provisions of the *Administrative Procedure Law*, whereas not in accordance with the rules of civil substantive laws such as the *Contract Law*. In administrative agreement case, the liability of compensation for violation of the plaintiff's legal rights and interests by illegal administrative agreement acts can only be the Liability of the nation, whereas not the Liability for breach of contract or tort Liability. Administrative agreement signed by administrative organ can only be proceed within the scope of its discretion. If administrative agreement is signed beyond the scope of discretion, it can be verified as an ultra vires administrative act, which may infringe upon the interests of the nation, the public and the lawful rights and interests of the administrative counterparts. The administrative agreement shall be thereunder nullified or declared invalid in accordance with law. The contents of the agreement can't be used as a basis for determining whether the administrative agreement act is legal, nor can it be used as a basis for determining whether the administrative organ should make administrative compensation or undertake the liability of compensation.

In this case, the 2013 Resettlement Rules can be found as the compensation and resettlement plan for this collective land expropriation. The plan clearly stipulates that each person of the expropriated villagers will be resettled with 50 m^2 of row house. This agreement does not violate the *Land Administration Law* and its implementative regulations as well as other relevant laws and regulations on resettlement compensation. It does not infringe upon the interests of the nation, the public and the lawful rights and interests of others. The compensation and resettlement plan is legal and effective. Zhai X (A) and other respondents, as villagers residing in the area of the expropriated land, have the right to receive compensation and resettlement in accordance with the plan. When Haitang District Government signed the administrative agreement, it violates the legal and effective provisions of the compensation and resettlement plan, as well as the principle of equal rights of villagers. The resettlement agreement signed with Zhai X (A) and other five respondents, which only provide 120 m^2 of apartment buildings for their resettlement, thus violates the legal rights and interests of Zhai X (A) and other respondents, and it can be verified illegal to sign the agreement. The First and Second Instance judgments, which nullify the administrative agreement signed between Haitang District Government and Zhai X (A) and other respondents and ordered Haitang District Government to compensate Zhai X (A)'s household for resettlement within a time Limit in accordance with the standards provided in the compensation and resettlement plan, is not against the relevant regulations and provisions of the *Administrative Procedure Law*.

Huang X (A) and Huang X (B) v. the People's Government of Shunde District, Foshan, and National Land and Civil Construction Bureau and Water Conservancy Bureau of Shunde District, Foshan (Administrative Registration)—The *Bona Fide* Acquisition of Mortgage Constitutes an Impediment to the Cancellation of Housing Registration

Junyong Xiong and Yanjia Niu

Rule

Jus in re aliena encompasses mortgage, to which the system of *bona fide* acquisition can also be applied. The judgment of whether housing mortgages constitutes *bona fide* acquisition shall be analyzed in light of the general theory of *bona fide* acquisition and the actual situation of the case. The core element for the determination of *bona fide* acquisition is *bona fide* acquisition of mortgage by a third party with compensation. When housing mortgages is in conformity with the elements of *bona fide* acquisition, such *bona fide* acquisition may constitute a deterrent to cancellation of housing registration. Cancellation of the housing registration will affect the validity of the mortgage registration, resulting in the inability to realize the mortgage. Therefore, in the event of obtaining the mortgage in such bona fide acquisition, it shall be adjudicated that the act of housing registration is illegal, and the validity of the housing registration shall be retained.

Collegial panel judges of Supreme People's Court for re-trial: Xiong Junyong, Cao Gang, Gong Bin (Written by: Xiong Junyong and Niu Yanjia, Supreme People's Court; Translated by: Li Jinyan).

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_39

Case Information

1. Parties

Applicant in the retrial (Plaintiff in the first instance, Appellee in the second instance): Huang X (A) and Huang X (B)
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): People's Government of Shunde District, Foshan (hereinafter referred to as "Shunde District Government")
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): National Land and Civil Construction Bureau and Water Conservancy Bureau of Shunde District, Foshan (hereinafter referred to as "Shunde District Land Bureau")
Respondent in the retrial (The third person in the first instance, Appellant in the second instance): Shunde Branch of Bank of China Limited (hereinafter referred to as "Shunde Branch of Bank of China")
The third party in the first instance and the appellee in the second instance: Huang X (C)

2. Procedural History

First instance: No. 67 [2015], Trial, Adm. Division, the Intermediate People's Court of Foshan City, Guangdong Province (dated Mar. 30 of 2016)
Second instance: No. 1129 [2016], Final, Adm. Division, the Higher People's Court of Guangdong Province (dated Nov. 24 of 2016)
Application for retrial: No. 95 [2017], Retrial, Adm. Division, the Supreme People's Court (dated Apr. 28 of 2018)

3. Cause of Action

Housing administrative registration

Essential Facts

Huang X (A) and Huang X (B) are mother-child relationship. Liu X (A) applied to Guangdong Development Bank for a RMB 500,000 loan to do business in the name of Huang X (B). The collateral for the loan was the property located at No. 27 Changfeng 3rd Street, Jizhou Changfengyuan Residential District, Jizhou Village Committee, Lunjiao Sub-district Office, Shunde District, Foshan City, under the name of Huang X (A) and Huang X (B) (hereinafter referred to as "the house involved in the case") In November 2009, Huang X (C) was charged for repayment of debt due to his failure to repay the principal and interest of the loan. The Shunde District People's Court finds in its civil judgment that Guangdong Development Bank has the right of priority against proceeds from auction or sale of the house involved in the case for

the principal and interest of the loan in the amount of about RMB 450,000. In order to prevent the house involved in the case from being auctioned, Huang X (A) decided to transfer the house to his daughter Huang X(D) and applied to the bank for a loan in the name of Huang X(D) to repay the above loan. Huang X (A) and Huang X (B) have entrusted Liu X (A) in writing with full power to handle relevant formalities and transferred the property right to Huang X(D). Liu X (A) sub-entrusted Wu X to handle the above matters. Huang X (C) fully entrusted a third person Zhong X (A) (her other identity, "Zhong X (B)", was used by Liu X (A)'s daughter Zhou X) to purchase the house involved in the case and notarized the entrustment. Liu X (A) borrowed about RMB 700,000 from Li X to repay Huang X (B)'s loan principal and interest in the amount of RMB 500,000 with Guangdong Development Bank and redeemed the Housing Property Certificate involved in the case. Wu X went to Songzhu Police Station of Leizhou Municipal Public Security Bureau for the issuance of a *Household Registration Certificate* proving Huang X (C)'s former name was "Huang X(D)", and to see a staff from Shunde Branch of Bank of China for information about the loan and relevant materials. Thereafter, he returned the loan material to Liu X (B) and asked for a loan. After a loan review, Shunde Branch of Bank of China approved the loan application and signed the *Mortgage Loan Contract for House Purchase* with Huang X (C) on August 16, 2010, agreeing on that the loan of RMB 1.2 million was used for purchasing the house involved in the case and paid off with the house being collateral. On August 23, 2010, Liu X (A), representing the contract sellers Huang X (A) and Huang X (B), signed a *Real property Sales Contract* with Zhong X (A), representing the contract buyer Zhong X (A), on the sale of the house involved in the case to Huang X (C) at the price of RMB 1.632 million. On August 24 and September 3, 2010, Foshan Housing and Construction Bureau issued Guangdong *Real property Ownership Certificate* No. 0300151353 and Guangdong *Real property Mortgage Certificate* No. 0310020385 to Huang X (C) and Shunde Branch of Bank of China. At the same time, the "cancellation" seal was affixed to the inside page of the *Real property Ownership Certificate* and *Real property Co-Ownership (Common) Certificate* originally possessed by Huang X (A) and Huang X (B). On September 8, 2010, Shunde Branch of Bank of China issued a loan of RMB1.2 million to Huang X (C)'s bank account (opened by Wu X on behalf of Huang X (B)). On the same day, Li X and Liu X (A) transferred RMB 990,000 from this account to her husband Ye X's account, with the remaining deposited into Liu X (A)'s bank account and to be disposed for other purposes. Thereafter, Huang X (C) was sued by Shunde Branch of Bank of China for debt collection due to his failure to repay the remaining principal and interest after paying a total amount of RMB 121,291.59. On November 28, 2012, Shunde District People's Court issued a civil judgment (No. 19, Trial, Civ. Division), confirming the mortgage of Shunde Branch of Bank of China on the house involved in the case.

On August 27, 2015, the Shunde District People's Court rendered a criminal judgment (No. 2703, Trial, Crim. Division) that Liu X (A) was sentenced to imprisonment of one year and nine months and a fine of RMB 10,000 for the crime of defrauding loans. The court found that Liu X (A) used false household registration certificate to transfer the house involved in the case to Huang X (C), and then took the relevant

false material to defraud the bank loan. The fraud was targeted at the relevant departments handling the transfer of real property and the bank handling the loan. Finally, Liu X (A) defrauded the bank loan of RMB 1.2 million. The judgment also found that the identity of "Zhong X (A)" was false, so were the bank current account and the real property sales contract used by Huang X (C) to apply for the loan.

On November 4, 2015, Huang X (A) and Huang X (B) filed a lawsuit in this case, requesting: (1) to set aside the defendant's canceling of the *Property Ownership Certificate* with Guangdong real property certificate No. C6026635 and the *Real property Co-Ownership Common (Common) Certificate* with Guangdong property certificate No. C1467912, and to restore the original owner's property archives and property ownership certificate; (2) to revoke the *Property Ownership Certificate* issued by the defendant with Guangdong Property Ownership Certificate No. 03000151353; (3) to revoke the *Property Mortgage Certificate* issued by the defendant with Guangdong property mortgage certificate No. 0310020385.

On August 18, 2017, the Shunde District People's Court issued a civil judgment (No. 127, Trial, Civ. Division), confirming that the *Real property Sales Contract* signed on August 23, 2010 in the name of Huang X (A) and Huang X (B) was null and void.

First instance judgment of Foshan Intermediate People's Court: (1) revokes the administrative registration by the defendant of *Property Ownership Certificate* with Guangdong property ownership certificate No. 0300161353; (2) revokes the administrative registration by the defendant of *Property Mortgage Certificate* with Guangdong property certificate No. 0310020385; (3) revokes the defendant's cancellation of the administrative registration of *Property Ownership Certificate* with Guangdong property certificate No. C6026635 and the *Real property Co-Ownership (Common) Certificate* with Guangdong property co-ownership certificate No. C1467912; (4) dismisses Huang X (A)'s and Huang X (B)'s other claims. Shunde Branch of Bank of China appealed against the first-instance judgment. Guangdong Provincial Higher People's Court reversed the first instance judgment and dismissed Huang X (A)'s and Huang X (B)'s claims.

Huang X (A) and Huang X (B) applied to the Supreme People's Court for retrial.

Issues

1. The legality of housing registration authority's handling of property ownership registration of the house involved in the case;
2. The legality of mortgage registration of the house involved in the case;
3. The method of adjudication in this case.

Holding

The Supreme People's Court held that the National Land and Civil Construction Bureau of Shunde District had fulfilled its duty of prudence in examining the application materials for registration and its registration conformed with the requirements as stipulated in the *Housing Registration Measures*. However, after the housing registration, the criminal judgment made by Shunde District People's Court found that Liu X (A), in violation of the entrusted matters, provided a false *Household Registration Certificate* to the housing registration authority to prove that Huang X (C)'s former name was Huang X (D), and maliciously colluded with Huang X (C) to jointly apply for housing transfer registration for the purpose of obtaining housing registration by means of concealing the real situation and providing false materials. In this case, the housing registration authority can surely review in accordance with the provisions of Article 81 of the *Housing Registration Measures* to decide whether it is necessary to exercise its own cancellation right to cancel the registration of the housing involved in the case. When the housing registration authority itself fails to set aside the registration, the parties concerned may apply to the court to handle the legality of the registration in accordance with the law and determine the legality of the registration pursuant to the this clause. The second instance denied Huang X (A)'s and Huang X (B)'s claims for revocation of the property ownership certificate on the grounds that "Huang X (A) and Huang X (B) failed to obtain a valid judgment or arbitration ruling denying the validity of their sales contract with Huang X (C) and the validity of the mortgage right of Shunde Branch of Bank of China through civil dispute resolution, and the evidence for revocation of the property ownership certificate was insufficient". At the same time, the court also denied the claims for mortgage registration of the house. It is erroneous in the application of law. The false belief of Shunde Branch of Bank of China in the review of mortgage registration was caused by malicious collusion of Liu X (A), Huang X (C) and others in providing false materials. Moreover, the mortgage registration was also based on the trust in the credibility of the housing registration after the housing registration authority had previously made the housing transfer registration. Thus, Shunde Branch of Bank of China had no gross negligence in the mortgage registration, whose mortgage acquired was *bona fide* acquisition and shall be protected by law. The *bona fide* acquisition by Shunde Branch of Bank of China constituted a legal impediment to set aside the mortgage registration by the housing registration authority. The first instance judgment to cancel the mortgage registration is erroneous in the finding of facts and application of law. To sum up, the retrial application of Huang X (A) and Huang X (B) have been in conformity with the requirements of Article 91 (3) (iv) of the *Administrative Procedure Law*. According to Article 74 (1) (i) of the *Administrative Procedure Law* and the provisions of Article 119 and Article 122 of the *Interpretation on the Application of Administrative Procedure Law*, the court ruled to annul the judgment of the first and second instances, confirm that the *Real property Certificate* issued by Shunde District Government and Shunde District Housing and Construction Bureau with Guangdong Property Certificate No. 03000151353 is in violation of the law, and dismiss Huang X (A)'s and Huang X (B)'s other claims.

Comment on Rule

1. The Legality of housing registration authority's handling of property ownership registration of the house involved in the case

Article 11 of the *Housing Registration Measures* implemented on July 1, 2008 provides that, "when applying for housing registration, the applicant shall file an application with the housing registration authority where the housing is located and submit the application registration materials. The applicant shall submit the original of the registration materials, or, if no original can be submitted, a photocopy confirmed by the relevant authorities to be identical with the original. The applicant shall be responsible for the truthfulness, legality and validity of the application materials, and shall not conceal the fact or provide false materials to apply for housing registration." In accordance with the above provisions, the applicant shall be responsible for the truthfulness, legality and validity of the application for registration materials. Whether the examination of the registration materials by the housing registration authority is only a duty of formal examination or a duty of substantive examination is not expressly stipulated by the law, but the housing registration authority shall fulfill its duty of prudence in examination within its capabilities.[1] That is to say, when examining the registration, the housing registration authority mainly examines whether the application materials are complete and integral, and conform to the legal formality and for the truthfulness, legality and validity of the relevant materials, the registration authority shall only fulfill its duty of prudence in the examination within its scope of office duties. In practice, it did happen when some applicants obtain the housing registration by providing false registration materials maliciously and deceiving the registration authority. If the housing registration authority finds afterwards that the applicant has provided false materials.[2]

Based on the facts ascertained by the first and second instances, National Land and Civil Construction Bureau of Shunde District has fulfilled its duty of prudence when examining the application materials for registration, and its registration act conformed to the requirements of the *Housing Registration Measures*. However, after

[1] In the registration of real property rights, the control of the examination scale by the registration department is actually the issue of whether the registration institution conducts substantive examination or formal examination of the registration application submitted by the applicant. Since both of the *Real Right Law of the People's Republic of China*, entering into force on October 1, 2007, and the *Housing Registration Measures*, coming into force on July 1, 2008, do not expressly provide this issue, but exclusively specify the specific liability of registration agencies in different situations. Therefore, the current mainstream view is that differences in registration examination standards should be shelved. Housing registration agencies mainly conduct formal examination of registration applications, but they should fulfill reasonable and prudent obligations. If reasonable doubts about "consistency" and "conflict on rights" in registration conditions provided in Article 20 of the *Housing Registration Measures* are found, substantive examination should be conducted on the doubts.

[2] Article 81 of the *Housing Registration Measures* stipulates that the housing registration authority has the power to revoke the original housing registration, withdraw the housing ownership certificate or registration certificate, or announce the cancellation of the certificate.

the house has been registered, the criminal judgment made by Shunde District People's Court has found that Liu X (A), in violation of the entrusted matters, provided false household registration certificate materials to the housing registration authority, and maliciously colluded with Huang X (C) to jointly apply for housing transfer registration. It is concealing the truth, providing false materials to obtain housing registration. Under such circumstances, the housing registration authority can surely review in accordance with the provisions of Article 81 of the *Housing Registration Measures* to decide whether it is necessary to exercise its own cancellation right to set aside the registration of the housing involved in the case. Where the housing registration authority fails to set aside the registration, by itself and the parties concerned apply to the court for ruling the court shall deal with the legality of the registration act in accordance with the law, and may determine the legality of the registration act in accordance with this clause. The second instance denies Huang X (A)'s and Huang X (B)'s claims for revocation of the property ownership certificate involved in the case on the grounds that "Huang X (A) and Huang X (B) did not obtain a valid judgment or arbitration award denying the validity of their sales contract with Huang X (C) and the validity of the mortgage right of Shunde branch of Bank of China, so there is insufficient evidence to request the revocation of the *Property Ownership Certificate* (Guangdong Property Ownership Certificate No: 03000151353)" and denies the claims for mortgage registration at the same time. This is erroneous application of law. The criminal judgment with binding force has confirmed that in the process of housing registration, the litigant provided false materials, which satisfies the cause for revocation. Regarding the validity of the sales contract submitted in the registration process, it is not the only factor to be considered when determining whether the housing registration involved in the case should be set aside. Moreover, on the basis of the latest evidence submitted by Huang X (A) and Huang X (B), the valid civil judgment made by Shunde District People's Court also confirmed that the sales contract of the house involved in the case was null and void. Therefore, regarding the legality of housing registration in this case, the facts confirmed by the binding criminal judgment and the civil judgment should be used to confirm that the parties concerned have submitted false materials and obtained housing registration by illegal measures. According to Article 69 of the *Administrative Procedure Law*, if the evidence of the administrative act is conclusive, and the application of laws and regulations is correct and in conformity with legal procedures, people's court shall decide to dismiss the plaintiff's claim. The judgment of the second instance dismissing the claims against the housing registration is erroneous in its application of law, and shall be corrected.

2. **The legality of the mortgage registration of the house involved in the case**

First of all, where the housing registration authority finds afterwards that relevant parties provide false materials in the process of housing registration, it also needs to confirm whether the housing registration should be revoked through investigation. Despite no fault and responsibility on the part of the housing registration authority for such revocation, it still needs to revoke the housing registration if relevant conditions are satisfied. Secondly, what is provided here is that except *bona fide* acquisition, the

housing registration obtained by providing false materials shall be set aside. That is, in the event of *bona fide* acquisition, it will constitute the ground for the cancellation of housing registration. In general, the *bona fide* acquisition mentioned in this article refers to the acquisition of houses in good faith by a third party. Then, the issue to be further discussed in this case is when the person without the right of disposal has disposed of other people's house and completed the registration, the real owner claims to cancel the house registration, but the third person claims to obtain housing mortgages in good faith, whether that constitutes a reason for the cancellation of the housing registration.

Article 106(1) of the *Property Law* provides: "If a person without the right of disposal transfers immovable or personal property to the transferee, the owner has the right to recover it; Except as otherwise provided by law, the transferee acquires the ownership of the real property or personal property if: (1) the transferee was in good faith when accepting the real property or personal property; (2) transfer is at a reasonable price; and (3) the transferred real property or personal property that should be registered in accordance with the law has been registered, and those that do not need to be registered have been delivered to the transferee." Article 106(3) provides that, "in the event of the party's bona fide acquisition of *jus in re aliena*, reference shall be taken to the provisions of the preceding two paragraphs." As provided in the above provisions, the system of *bona fide* acquisition also applies to *jus in re aliena*, including mortgage. Indeed, whether housing mortgages constitutes *bona fide* acquisition shall be analyzed in light of the general theory of *bona fide* acquisition and the actual situation of the case.[3] Where housing mortgages conform to the factual elements of *bona fide* acquisition, the *bona fide* acquisition may also constitute a deterrent to the cancellation of housing registration.

As mentioned above the housing registration involved in the case should have been revoked by virtue of the submission of false materials and the illegal acquisition of housing registration. In this case, the effective criminal judgment has determined that Huang X (C) colluded with Liu X (A) maliciously to defraud the house registration, so Huang X (C) is not a *bona fide* third party, and there is no reason that the housing registration is cancelled due to the *bona fide* acquisition of the house by the third party. Then, the legality of the housing mortgage registration involved in the case will directly affect the judgment on whether the housing registration should be revoked. The secured creditor's rights between Huang X (C) and Shunde Branch of Bank of China were confirmed by the effective civil judgment of Shunde District People's Court. The court held that Shunde Branch of Bank of China has the mortgage on the house involved in the case in accordance with the law. Although the effective criminal judgment confirmed that Liu X (A) and Huang X (C) jointly provided false

[3]The *bona fide* acquisition system is to solve the problem of protecting the trust interests of *bona fide* third parties (assignees) without the right to dispose of them. Generally speaking, a *bona fide* acquisition must be in conformity with the following considerations: (1) the transferor has no right to dispose of it; (2) the transferee was in good faith when accepting the real property or personal property; (3) the property is transferred at a reasonable price; and (4) the transferred real property or personal property in the need of registration pursuant to the law has been registered, and those in no need of registration have been delivered to the transferee.

information to defraud the house transfer registration and mortgage registration, the Shunde Branch of the Bank of China conducted a corresponding review in the process of signing the mortgage loan contract with Huang X (C) with no gross negligence. Thus, it should be recognized as a bona fide third party. Moreover, Shunde Branch of Bank of China has issued a loan of RMB 1.2 million to Huang X (C)'s account, fulfilling its obligation to pay mortgage consideration pursuant to the loan contract. The mortgage registration of the house involved in the case made by the house registration authority is legal and valid with nothing improper.

The first instance held that Liu X (B), a staff member of Shunde Branch of Bank of China, as the business agent for setting up the mortgage, "neither contacted with Huang X (B) and Huang X (A), the sellers of the real property involved, nor examined the truthfulness of the *House Purchase and Sales Contract*, nor obtained the *Household Registration Certificate*. Under such circumstances, he recklessly believed that Huang X (C) was the legitimate buyer of the house involved in the case, and had committed gross negligence without careful examination of the loan contract and mortgage contract." "Shunde Branch of Bank of China has committed gross negligence for the consequences of Liu X (A) and Huang X (C)'s defrauding mortgage registration, and is not a *bona fide* third party." The above determination is contrary to the conclusion that the effective civil judgment has confirmed that the mortgage contract for the house involved in the case is legitimate and valid. Without initiating the trial supervision procedure to correct the effective civil judgment, this part of the facts determined in the first instance cannot be considered as the facts of the case and shall be corrected.

The bank signing the mortgage contract should actually review the relevant materials provided by the applicant with prudence in handling mortgage registration. In spite of no contact between Liu X (B) and the sellers Huang X (B) and Huang X (A), Huang X (A) and Huang X (B) entrusted Liu X (A) in writing to handle the transfer and mortgage procedures for the house involved in the case, and the entrustment procedures were notarized by the notary department. There was reason for Liu X (B) to believe that Liu X (A) was qualified as an agent. As for the examination of the *Household Registration Certificate* and the *House Purchase and Sale Contract*, when the respondent, a house registration agency, failed to find any falsification or invalidity of the above materials submitted by Liu X (A) and others in the process of registering there is no legal basis and realistic possibility to require bank staff to make more accurate judgment and higher examination efforts than government departments. The false belief of Shunde Branch of Bank of China in the review of mortgage registration was caused by malicious collusion between Liu X (A) and Huang X (C) and others in providing false materials. Moreover, the mortgage registration was also based on the trust in the credibility of the housing registration after the housing registration authority had made the housing transfer registration before. Shunde Branch of Bank of China has no gross negligence in the mortgage registration, whose mortgage acquired is *bona fide* acquisition and should be protected by law. The *bona fide* acquisition by Shunde Branch of Bank of China constitutes a legal impediment to the cancellation of mortgage registration by the housing registration

authority. The first instance judgment remanding the mortgage registration was based on unclear facts and erroneous application of law.

3. The method of adjudication in this case

Negative evaluation of the sued administrative act does not mean that the administrative act must be revoked. If the method of making judgment act as provided in Article 74(1)(i) of *Administrative Procedure Law* and[4] is to make negative evaluation on the legality of the sued administrative act without changing the legal relationship formed by the administrative act. The applicable conditions of this method of judgment include cases involving *bona fide* third parties in addition to national interests or public interests.

Article 11(3) of the *Provisions on Hearing Housing Registration Cases* provides that the even sued housing registration is illegal, if the cancellation of the judgment will cause heavy losses to the public interests or the house has been acquired in good faith by a third party, then the court finds that the sued behavior is illegal but does not revoke the registration. This case involves two administrative acts of housing registration and mortgage registration, where the mortgage registration is a right that should be protected by law. If the housing registration is cancelled, the real right basis of that mortgage registration does not exist, and the legitimate rights of the mortgagee cannot be protected, which will inevitably cause damage to the public interests. Subject to the above provisions, the housing registration should have been revoked by the judgment, but revocation will affect the effectiveness of the mortgage registration and the realization of the mortgage. Therefore, the judgment should confirm that the housing registration is illegal, retain the effectiveness of the housing registration, and reject the retrial applicant's other claims.

It shall be noted that Article 106(2) of the *Property Law* provides: "where the transferee acquires the ownership of real property or personal property in accordance with the provisions of the preceding paragraph, the original owner is entitled to claim compensation for the loss from the person without the right of disposal." In this case, Liu X (A)'s fraudulent obtaining of the loan caused Huang X (A) and Huang X (B)'s the house involved in the case to be transferred for registration and mortgaged, which did cause certain losses. However, when Huang X (A) and Huang X (B) entrusted Liu X (A) to complete the housing transfer registration and mortgage, their original intention was to deal with the execution of the previous loan by the court. After Liu X (A)'s manipulation much of the loan granted by Shunde Branch of Bank of China were repaid to the third persons who had repaid the previous loans on their behalf. Liu X (A) submitted a false household registration certificate to defraud a housing registration under the guise of Huang X (C), a person never involved in a series of criminal, civil and administrative proceedings. Huang X (A)'s and Huang X (B)'s related losses can be claimed from those without right of disposal for compensation in accordance with the relevant provisions of the *Property Law.* After finishing the

[4] Article 74 of the *Administrative Procedure Law of the People's Republic of China* stipulates that in any of the following circumstances, people's courts shall make judgment to confirm the violation of the law, but shall not revoke the administrative act: (1) The administrative act shall be revoked according to law, but revocation will cause great damage to the interests of the state and the public;…

execution procedure of the housing involved in the case, Huang X (A) and Huang X (B) can also claim the remaining funds.

In practice, some judges believe that the revocation of ownership of real property does not affect mortgage, and the corresponding judgment is made accordingly.[5] Based on this view, the court may decide to cancel the house registration, but retain the validity of the mortgage registration.[6] As for the issues involved in this case, the method of adjudication actually involves the understanding of the relationship between mortgage and real right and the way to balance the legal rights and interests of all parties. The method of adjudication in this case still needs further discussion.

[5]For example, Beijing No. 2 Intermediate People's Court, in its administrative judgment (No. 562 [2017], Final, Adm. Division), held that in the event of any evidence proving false application materials for registration of housing ownership transfer, the registration shall be revoked. The revocation judgment of the people's court does not necessarily result in the mortgage right of the third party to the house not being realized. Therefore, the registration in housing mortgages fails to constitute a legal obstacle to the revocation of the ownership registration. Judgment by Beijing No. 3 Intermediate People's Court (No. 754 [2017], Final, Adm. Division) held that the mortgage is a real right, and the legal binding of revocation of the *Property Ownership Certificate* does not affect the binding force of the mortgage in the event of lawsuit brought by the parties against the *Loan Mortgage Contract* of the civil basis of mortgage registration without support from the court and the legal mortgage registration made by the housing registration authority.

[6]In general, the consideration paid when the house is mortgaged differs from that paid when the house is transferred, and the consideration paid by the mortgagee is often less than the value of the house. Where the false housing registration is cancelled and the validity of the mortgage registration is retained, the residual value of the house will still belong to the original owner of the house after the mortgagee fulfills his mortgage, and the original owner can be protected to the maximum extent.

Zuo X v. Tongzi County People's Government of Guizhou Province and Tongzi County Education Bureau (Dispute over the Agreement on Housing Demolition and Resettlement)—The People's Court Shall Specifically Rule on the Rights and Obligations of the Parties to the Administrative Agreement

Zhiming Li

Rule

The *Administrative Procedure Law* provides that people's court handles lawsuits brought by citizens, legal persons or other organizations because they believe that the administrative organ fails to act in accordance with the law, fails to perform in accordance with what has been agreed upon or makes altercation or changes illegitimately, rescinds the government franchise agreement, land and housing expropriation compensation agreement and other agreements. The administrative agreement is reached through consultation by the administrative organ and those subject to administration out of its discretion. It is a creative combination of administrative nature, for which it is different from civil contract, and contractual nature, for which it is similar to civil contracts. In accordance with the principle of full performance required by administrative law theory, administrative organs and those subject to administration shall abide by and perform the rights and obligations set forth in the administrative agreements. Therefore, in comparison with the general administrative litigation, people's court shall make a more direct and specific ruling on the rights

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Selected Cases from the Supreme People's Court of the People's Republic of China, Library of Selected Cases from the Chinese Court,
https://doi.org/10.1007/978-981-15-0342-9_40

and obligations of the parties to the administrative litigation arising from any dispute over the administrative agreement. If the administrative organ is only ordered to make another administrative act or the parties are ordered to renegotiate and sign an agreement, circular litigation or judgment without execution will incur easily, preventing the rights of the parties from being protected substantially.

Case Information

1. **Parties**

Applicant in the retrial (Plaintiff in the first instance, Appellant in the second instance): Zuo X
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): the People's Government of Tongzi County, Guizhou Province
Respondent in the retrial (Defendant in the first instance, Appellee in the second instance): Tongzi County Education Bureau of Guizhou Province (formerly named Tongzi County Education, Science and Technology Bureau)

2. **Procedural History**

First Instance: No. 480 [2016], Trial, Adm. Division, the Intermediate People's Court of Zunyi City, Guizhou Province (dated Apr. 14 of 2016)
Second Instance: No. 652 [2017], Final, Adm. Division, the Higher People's Court of Guizhou Province (dated May 17 of 2017)
Application for Retrial: No. 4718 [2017], Retrial, Adm. Division, the Supreme People's Court (dated Sep. 26 of 2017)

3. **Cause of Action**

Disputes over housing demolition and resettlement agreement

Essential Facts

Zuo X, a retired teacher from No. 5 Middle School of Tongzi County, possesses a house with an area of 50.82 m^2 in the Railway Staff's No. 17 Family Dormitory Building, in Tiexi Village. In 2012, Because No. 5 Middle School in Tongzi County needed to occupy the Railway Staff's No. 17 Family Dormitory Building in Tiexi Village for reconstruction and expansion. Tongzi County People's Government entrusted Tongzi County Education Bureau (formerly named Tongzi County Education and Science and Technology Bureau) to carry out the resettlement and demolition work. On July 28, 2012, Tongzi County Education Bureau, as Party A, and Zuo X, as Party B, enters into the *Agreement on Demolition and Resettlement of the Railway Staff's*

No. 17 Family Dormitory Building in Tiexi Village. The agreement states that Party A shall be responsible for the simultaneous resettlement of Party B in accordance with the resettlement policies for railway worker households in Tiexi Village after the agreement was concluded. It also provides that "the subsequent similar agreements prevail over the terms of this Agreement, and Party B shall enjoy the rights thereunder" and "anyone who breaches shall bear a penalty at 2‰ of the total price per day based on then current price of the resettlement house".

In 2014, Tongzi County initiated the construction project of Rongdeshan Park's urban shanty areas. Railway Staff's Family Dormitory Building in Tiexi Village falls within the scope of the project. In order to be included in the resettlement scope of the project, Zuo X submitted applications to Tongzi County People's Government and Tongzi County Education Bureau on November 3, 2014 and October 15, 2015 respectively, requesting the conclusion of specific resettlement agreement. Zuo X filed a lawsuit the fact as the People's Government of Tongzi County and Education Bureau of Tongzi County failed to specify the resettlement or compensation for Zuo X, nor have they entered into a new agreement for returning the house to Zuo X.

On April 14, 2016, the court of first instance held that Tongzi County People's Government and Tongzi County Education Bureau shall perform the *Agreement on Demolition and Resettlement of the Railway Staff's No. 17 Family Dormitory Building in Tiexi Village* signed with Zuo X within 60 days from the effective date of the judgment. Zuo X appealed against the trial judgment. The court of second instance made a judgment on may 17, 2017, "(1) to cancel the administrative judgment numbered No. 480 [2015], Trial, Adm. Division; (2) to order Tongzi County People's Government to perform the *Agreement on Demolition and Resettlement of the Railway Staff's No. 17 Family Dormitory Building in Tiexi Village* concluded with Zuo X within 60 days from the effective date of the judgment; (3) to dismiss Zuo X's other claims against Tongzi County People's Government; (4) to dismiss Zuo X's lawsuit against Tongzi County Education Bureau.

Zuo X refused to accept the judgment of the second instance and applied to Supreme People's Court for retrial.

Issues

1. Whether Tongzi County Education Bureau is an eligible defendant in this case?
2. Whether *the Agreement on Demolition and Resettlement of the Railway Staff's No. 17 Family Dormitory Building Tiexi Village* signed by Zuo X and Tongzi County Education Bureau is legal and valid?
3. Should Zuo X's claim on housing resettlement and payment of liquidated damages be supported by the court?

Holding

After examination, the Supreme People's Court held that the issue at hand is whether Zuo X's specific claim on the housing resettlement and payment of liquidated damages should be supported. The *Agreement on Demolition and Resettlement of the Railway Staff's No. 17 Family Dormitory Building Tiexi Village* involved in this case was entered into willingly by both parties. It is legal and effective and should be fully performed in accordance with the law. Article 1 of the agreement states: "… Party A shall be responsible for providing Party B with the same demolition and resettlement as requested in the demolition and resettlement policies (plans) of Tiexi Village Railway Workers and Households of No. 4 Company of No. 2 Bureau, China Railway …" The agreement is an entrustment agreement for implementing synchronous resettlement or signing demolition and resettlement compensation agreement in the future. Although the agreement does not specify the method and the time to resettle or compensate for Zuo X's house, after the Tongzi county government implemented the "Tongzi Rongdeshan Park urban shanty areas construction project", it has already relocated Railway Staff's Family Dormitory Building in Tiexi Village. In accordance with the agreement, it is now possible to determine the resettlement area or the calculation method of the resettlement area for Zuo X based on the resettlement standards for similar households that have already received generous resettlement. The court of the second instance held that "the resettlement area requested by Zuo X cannot be determined", which was obviously inappropriate. At the same time, Article 6 of the Agreement stipulates that "anyone who breaches shall bear a penalty at 2‰ of the total price per day according to then current price of the housing". Now that the residents involved in the demolition of Rongdeshan Park's urban construction and shanty areas renovation project have been resettled, the date of commencement, payment standard or amount of liquidated damages should also be determined based on all factors of the case.

To sum up, the court of second instance only ruled that the Tongzi county government fulfill the agreement signed with Zuo X without stipulating the specific resettlement area and liquidated damages, which was not conducive to the substantive resolution of administrative disputes and easily led to circular litigation. Therefore, the case should be retried in accordance with the law. Zuo X's retrial application has met the conditions stipulated in Article 91 of the *Administrative Procedure Law*, and in accordance with Article 92(2) of the *Administrative Procedure Law* and Article 77(2) of the *Interpretation on the Implementation of Administrative Procedure Law*. An administrative ruling was made by the Supreme People's Court Numbered No. 4718 [2017], Retrial, Adm. division (1) to instruct Guizhou Higher People's Court to retry the case; and (2) during the retrial, to suspend the execution of the original judgment during the retrial.

Comment on Rule

1. Governing Laws and Comments on Core Issues Involved in the Case

(1) Regarding whether Tongzi County Education Bureau is an eligible defendant. Article 4 (1) of the *Regulations on House Expropriation and Compensation on State-owned Land* provides that the municipal and county-level people's governments are responsible for house expropriation and compensation in their respective administrative areas. In this case, although the former Tongzi County Education, Science and Technology Bureau signed *the Agreement on Demolition and Resettlement of the Railway Staff's No. 17 Family Dormitory Building, Tiexi Village* in its own name with Zuo X, it was actually entrusted by Tongzi County People's Government to carry out the demolition and resettlement work. Therefore, subject to Article 26 (5) of the *Administrative Procedure Law*, Tongzi County Education Bureau (formerly named Tongzi County Education and Science and Technology Bureau) is not an eligible defendant in this case. Tongzi County People's Government is the eligible defendant in this case.

(2) On Zuo X's demanding for 200.72 m^2 of resettlement housing. The agreement involved was an entrustment agreement for the future implementation of synchronous resettlement or the signing of a relocation compensation agreement. Therefore, the agreement did not specify specific method and the time to resettle and compensate for Zuo X's house. However, in accordance with Article 7 of the Agreement, it can be resettled based on the resettlement standards for similar households Zuo X mentioned as having received preferential resettlement.

(3) On Zuo X's claim to pay liquidated damages. Article 3 of the Agreement provided: "…Party A shall be responsible for providing Party B with the same demolition and resettlement in accordance with the demolition and resettlement policies (plans) of Tiexi Village Railway Workers and Households of No. 4 Company No. 2 Bureau China Railway…" Article 6 of the Agreement stipulated that "everyone who breaches shall bear a penalty at 2‰ of the total price per day based on the current price of the resettlement house". In accordance with the evidence provided by Zuo X, the county government agreed on October 8, 2014 to "perform the contract the same way as the implementation of Buildings No. 15 and No. 16 of Rongdeshan Park urban construction and shanty area renovation project in Tongzi county". Buildings No. 15 and No. 16 demolished in Rongdeshan Park's urban construction and shanty area renovation project were resettled in August 2014. Zuo X agreed to extend the commencing time for calculating the liquidated damages to November 30, 2014. Therefore, the statement made by the court of the second instance that "the commencing basis and time for the accumulation of liquidated damages as stipulated are not clear". The unclear Agreement contradicts with the facts.

2. Jurisprudential Analysis of the Issues Involved in the Dispute

The adoption of administrative agreements for administrative management is conducive to fully mobilizing the initiative and enthusiasm of administrative organs

and those subject to administration, improving administrative efficiency and reducing contradictions and disputes. However, for a long time, different opinions have rested on whether disputes over administrative agreement should be settled in judicial practice through civil proceedings or administrative proceedings. Civil judges mostly consider that disputes over administrative agreement are contract disputes and advocate to solve them through civil proceedings. It is so dominant in judicial practice that the most typical administrative agreement dispute - state-owned land assignment contract dispute, is defined as a civil case by the *Judicial Interpretation of Disputes over State-Owned Land Use Rights*. The revised *Administrative Procedure Law* has already made it clear that disputes over administrative agreement are within the scope of administrative litigation from May 1, 2015 and should be resolved through administrative litigation. Relevant judicial interpretations previously in conflict with the Administrative Procedure Law should no longer be applied.

(1) The dual nature of administrative agreements

Administrative agreements bear both administrative and contractual attributes. Administrative agreements are administrative in nature. First of all, one party to the administrative agreement is the administrative organ. Secondly, the conclusion of the administrative agreement aims to reach the goal of administrative management, which will inevitably cause the formation, change or termination of the administrative legal relationship. Contracts concluded by administrative organs for civil purposes are civil contracts. Finally, the administrative agreement is a kind of administrative management means, thus the administrative organ enjoys the administrative superiority. The administrative superiority is the administrative power that the law grants the administrative organ to unilaterally exercise in the administrative agreement, including the guidance and supervision over the performance of the administrative agreement, the right of enforcement against those subject to administration who fails to perform relevant obligations, the right of administrative sanction right against those subject to administration who violate the agreement, the right of modification and cancellation the administrative agreement, etc.

Administrative agreements are also contractual. First of all, consensus of the parties is the prerequisite of the conclusion of an administrative agreement. In spite of the dominant role of administrative organ in the process of entering into an administrative agreement, those subject to administration still reserve the right to decide whether to sign the agreement and to negotiate with the administrative organ on such issues as the way of performing the agreement, the time limit for performing the agreement and the way of paying the remuneration. Secondly, both parties to the administrative agreement are bound by the administrative agreement. Upon the formation and taking into effect of the administrative agreement, both parties to the agreement shall strictly perform the agreement. The administrative organ shall not abuse the administrative privilege, and those subject to administration shall not delay in performing or improperly perform the agreement. Otherwise, it will be liable for breach of contract.

Although the administrative agreement has both administrative and contractual natures and contract, the administrative agreement is a method of administration

adopted by the administrative organ to perform its statutory duties. Therefore, the nature of administrative agreement is still an administrative act.

(2) The difference between the disputant involving proceedings and administrative procedure in general

There are essential differences between administrative agreement litigation and administrative procedure in general. In general administrative procedure, when the administrative act is illegal or obviously inappropriate, people's court shall, in principle, order the administrative organ to revoke the administrative act and, depending on the circumstances, order the administrative organ to make another administrative act. Only when "the administrative punishment is obviously inappropriate or other administrative acts involving the determination and confirmation of the amount of money is incorrect" as provided in Article 77 of the *Administrative Procedure Law*, people's court may make changes for the purpose cost substantially resolving administrative disputes, and avoid the circular litigation that may result from revoking the judgment and ordering the administrative organ to make another administrative act. In the lawsuit directed at the administrative agreement, because the administrative agreement is reached by the administrative organ based on the administrative discretion and those subject to administration, it is a creative combination of administrative nature, for which it is different to civil contracts and contractual nature, for which it is similar from civil contracts, which is similar to civil contracts. The rights and obligations of the administrative parties and those subject to administration agreed in the administrative agreement must be realized and fulfilled, which is exactly what full performance means under the administrative law principles. Therefore, people's court should make a more direct and specific ruling on the rights and obligations of the parties to the administrative agreement in the administrative litigation in comparison with the administrative procedure in general.

(3) The extent to which judicial power intervenes in administrative acts when administrative organs fail to perform administrative agreements in accordance with the law

An administrative organ's non-performance or performance in consistent with the law or what has been agreed on means this said agency has failed to perform its statutory or agreed duties. When hearing such cases, the people's court shall examine whether the administrative organ has fully performed its duties and obligations in accordance with the time limit, amount, method and scope stated in the administrative agreement. If the administrative organ fails to fully perform its duties and obligations, the people's court shall confirm the legality of the act and decide whether the administrative organ shall bear the corresponding liability for compensation.

Administrative compensation in administrative agreement cases differs from ordinary administrative compensation in the applicable laws. When hearing administrative compensation cases related to administrative agreements, the people's court shall, first of all, judge the administrative organ to bear the corresponding administrative compensation liability in accordance with the legal and effective agreement; in the event of no agreement, the administrative organ shall be judged to bear

the corresponding administrative liability for compensation in accordance with the administrative legal norms and the civil legal norms alternatively. For example, with regard to liability for breach of contract, compensation for deposit and legal liability results from the invalidity of administrative agreement, the relevant provisions of civil norms can be applied in the absence of legal and valid agreement or administrative legal norms, and the administrative organ can be judged to bear the corresponding administrative liability for compensation.