Administrative Litigation Bill of Complaint

Plaintiff: Fake Design Culture Limited
Address: No. 258 Caochangdi Village, Cuigezhuang Township, Chaoyang District, Beijing
Legal Representative: Lu Qing

Defendant: Beijing Local Taxation Bureau Second Investigation Branch
Address: Block C3, No. 12 Yumin Road, Chaoyang District, Beijing
Legal Representative: Guo Zhuming

Litigation claims:

1. We request that the Beijing Local Taxation Bureau Second Investigation Branch Taxation Administrative Penalty Decision (Er Ji Shui Ji Fa [2011] No. 56) issued by the defendant be annulled in accordance with the law; [and]

2. That litigation costs associated with this case be borne by the defendant.

Facts and Reasons:

Following a tax inspection by the defendant of the plaintiff's tax-related matters from November 29, 2000, to December 31, 2010, the defendant issued Beijing Local Taxation Bureau Second Investigation Branch Taxation Administrative Penalty Decision (Er Ji Shui Ji Fa [2011] No. 56) (hereafter "Penalty Decision"). After administrative review, the administrative review authority has ruled to uphold the original decision.

The plaintiff believes that the defendant's Penalty Decision was issued in error, with specific regard to the following reasons:

I. The main evidence is inadequate

1. The evidence is inadequate to substantiate the defendant's findings of fact

Evidence is lacking for the defendant's finding of fact regarding insufficient payment of stamp duty, sales tax, urban maintenance and construction tax, education surtax, and enterprise income tax by the plaintiff.

(1) The defendant found that the plaintiff "earned a total of 15,823,724.36 yuan in taxable income" under items "Boya Garden," "Three Shadows Centre," and "Naga" but "did not record it in the accounts" and "never made a tax declaration." Based on this, the defendant demanded that the plaintiff pay 4,344,497.64 yuan in enterprise income tax and, in its Penalty Decision, issued a "fine of 150 percent" against the plaintiff. However, there is no evidence that shows that the defendant's findings regarding these items have any direct relationship to the plaintiff's income.

(2) The defendant directly used figures recorded in the account books to derive the sales tax, urban maintenance and construction tax, and education surtax that the plaintiff should pay, without ever verifying the corresponding facts. The account books are a manual record or log, and the figures recorded therein should not be used

directly as evidence without the corresponding original vouchers to serve as corroboration.

(3) The defendant overlooked the plaintiff's true costs, leading to serious inaccuracies in the figures. In carrying out an "audit collection," the defendant should have verified the plaintiff's true costs. But the defendant instead neglected to collect evidence beneficial to the plaintiff.

(4) In its Penalty Decision, the defendant notified the defendant of the penalty amount without ever making its calculation process clear, leaving the plaintiff only to know what it should do without knowing why. Such a penalty is most unconvincing!

2. Evidence collected by the defendant is inadmissible because of procedural violations

According to the Supervision Form for Serious Tax Violation Cases (Jing Di Shui Ji Du [2011] No. 7) issued to the defendant by the Beijing Local Tax Bureau on April 6, 2011, the tax case against the plaintiff had been transferred from the public security organ for handling by the tax authority. Therefore, after April 6, 2011, the public security agency should not have intervened further in this administrative case concerning taxation. Evidence collected by the public security agency, as an improper body [for handling this case], should not be used as evidence in the defendant's Penalty Decision against the plaintiff. However, the evidence relied upon by the defendant in making its Penalty Decision against the plaintiff did indeed include records of the public security agency's interrogation of the plaintiff's shareholder, Liu Zhenggang, and accountant, Hu Mingfen, that were carried out after April 6, 2011. Therefore, said documents are inadmissible as evidence and cannot be used as a basis for the tax authority's administrative action.

Even with respect to materials collected by the public security organ before April 6, 2011, according to Article 70 of the Supreme People's Court's Regulations Concerning Several Questions of Evidence in Administrative Litigation (Fa Shi [2002] No. 21) ("Facts confirmed in an effective people's court decision or ruling by an arbitration body may be used as the basis of a determination."), the defendant cannot use as the basis of its determination any materials collected or produced by the public security organ, an investigatory authority, without those materials being first confirmed by a people's court.

3. There are no original documents for any of the evidentiary materials used as the basis of the defendant's specific administrative actions

On July 14, 2011, the defendant held a penalty hearing in this case. The plaintiff requested to check documents against the originals, but the the defendant was unable to make them available.

On March 27, 2012, the plaintiff went to the administrative review authority to review the evidentiary materials used as the basis of the defendant's Penalty Decision, but all the documents were photocopies.

The defendant made a specific administrative action based solely on photocopies, but it is impossible for the plaintiff to confirm the authenticity, legitimacy, or relevance of the evidence.

II. Laws and regulations were applied in error

Given that the defendant lacked evidence for its finding of fact, laws and regulations were of course applied in error upon this false factual basis. Even from the level of legal technicalities, there were the following errors:

1. Errors in applying the Tax Administration Law

(1) Errors involving retroactive application of the law

The Tax Administration Law of the PRC (hereafter "Tax Administration Law") currently in force was promulgated as Presidential Decree Number 49 on April 28, 2001, and it took effect on May 1, 2001. Article 84 of the Legislation Law of the PRC (hereafter "Legislation Law") states: "National law, administrative regulations, local decrees, autonomous decrees and special decrees, and administrative or local rules do not have retroactive force, except where a special provision is made in order to better protect the rights and interests of citizens, legal persons and other organizations." According to the principle that "the law has no retroactive force," the aforementioned Tax Administration Law can only be applied to tax collection and payment from May 1, 2001, onward.

In Part 1(2) of the defendant's Penalty Decision, the period is given as "November 29, 2000, to December 31, 2010," but the legal basis cited is the Tax Administration Law that took effect on May 1, 2001, which results in direct application of the Tax Administration Law that took effect after May 1, 2001, being directly applied in Part 2(2) of the Penalty Decision.

The Tax Administration Law first took effect on January 1, 1993, and was revised twice on February 28, 1995, and April 28, 2001. However, the defendant applied the Tax Administration Law that only took effect on May 1, 2001, and applied it during the period from November 29, 2000, to April 30, 2001.

(2) Errors involving limitation periods

The Administrative Penalty Law of the PRC falls under the category of ordinary law, whereas the Tax Administration Law falls under the category of a special law. According to Article 29 ("Where an illegal act is not discovered within two years of its commission, administrative penalty shall no longer be imposed, except as otherwise prescribed by law.") of the Administrative Penalty Law and Article 86 ("If any violation of the laws or administrative regulations on tax collection which deserves administrative penalties is undetected for five years, no administrative penalties shall be imposed any longer.") of the Tax Administration Law, according to the principle that a special law takes precedence over an ordinary law, penalties for "any violation of the laws or administrative regulations on tax collection" should apply the statute of limitation for penalties under the special law (namely, the "five years" provided for in Article 86 of the Tax Administration Law), whereas for illegal acts other than "any violation of laws and administrative regulations on tax collection," unless said act is covered by special-law provisions, the statute of limitation for penalties under ordinary law should be applied (namely, the "two years" provided for in the Administrative Penalty Law.

The plaintiff maintains that in order to use "five years" as the statute of limitations, a judgment must first be made as to whether the Ministry of Finance's (1993) Decree No. 6, Invoice Management Measures of the PRC (hereafter "Invoice Management Measures"), quoted by the defendant constitutes a "law or administrative regulation on tax collection."

The current Invoice Management Measures were approved by the State Council on December 12, 1993, and promulgated by the Ministry of Finance on December 23, 1993, as Decree No. 6. On December 20, 2010, they were revised by the State Council Decision on Revising the Invoice Management Measures of the PRC. According to the provisions of the Law on Legislation, the Invoice Management Measures prior to December 20, 2010, are categorized as departmental rules, whereas the Invoice Management Measures as revised on December 20, 2010, fall under the category of administrative regulations. Therefore, regardless of whether or not the content of the Invoice Management Measures concerns "tax collection," the Ministry of Finance (1993) Decree No. 6—namely, the Invoice Management Measures prior to revision on December 20, 2010—do not fall under the category of "laws or administrative regulations" and, thus, cannot be categorized as "laws or administrative regulations on tax collection." Therefore, ordinary law (namely, the two-year statute of limitation on penalties in the Administrative Penalty Law) should of course apply to the "illegal acts" set out in the Invoice Management Measures prior to the December 20, 2010, revision.

In Part 1(3) of the defendant's Penalty Decision, the period is given as "November 29, 2000, to December 31, 2010," and the basis for its finding is the Ministry of Finance's (1993) Decree No. 6, as is the basis for the penalty in the corresponding Part 2(3) of the Penalty Decision. Therefore, according to the "Identification Report Issued by the Taxation Authority" submitted by the defendant, the defendant's finding that the plaintiff "obtained invoices not in accord with regulations" concerns acts all prior to January 31, 2010. According to the principle of "the law has no retroactive force," the Invoice Management Measures from before their revision on December 20, 2010 (namely, the Ministry of Finance's [1993] Decree No. 6), should be applied. Thus, the statute of limitation on penalties for the defendant's so-called "obtained invoices not in accord with regulations" should be "two years," but the "November 29, 2000, to December 31, 2010" recorded in the Penalty Decision actually covers a period of more than 10 years.

(3) Errors in Finding of Fact

It is clear from the documents that the defendant submitted to the administrative review authority that the defendant was never able to collect in a comprehensive or clear manner relevant cost information or income and expense vouchers said to be related to the plaintiff. According to Article 35 ("Should a taxpayer fall into one of the following cases, the tax authorities shall have the right to assess the amount of tax payable: [. . .] [4] Although account books are kept, account entries are messy and information of costs, and vouchers on income and expenses are incomplete, making account inspection difficult.") of the Tax Administration Law and Article 3 ("Should a

taxpayer fall into one of the following cases, assessment will be carried out of enterprise income tax: [. . .] [4] Although account books are kept, account entries are messy and information of costs, and vouchers on income and expenses are incomplete, making account inspection difficult.") of the (Trial) Measures for Verification Collection of Enterprise Income Tax (Guo Shui Fa [2008] No. 30), the defendant should have used the method of "assessment collection" instead of mistakenly using "audit collection."

Under the method of "assessment collection," the defendant should not have penalized the plaintiff under Article 63 of the Tax Administration Law. According to Article 63 of the Tax Administration Law: "Tax evasion means that a taxpayer forges, alters, conceals or, without authorization, destroys accounting books or vouchers for the accounts, or overstates expenses or omits or understates incomes in the accounting books, or, after being notified by the tax authorities to make tax declaration, refuses to do so or makes false tax declaration, or fails to pay or underpays the amount of tax payable. Where a taxpayer evades tax, the tax authorities shall pursue the payment of the amount of tax he fails to pay or underpays and the surcharge thereon, and he shall also be fined not less than 50 percent but not more than five times the amount of tax he fails to pay or underpays." In making its finding about the amount of tax evaded by a taxpayer, the defendant should provide sufficient evidence to show that the taxpayer carried out the methods of tax evasion listed in Article 63 of the Tax Administration Law. The defendant should also investigate to determine whether the plaintiff concealed income and what amount of income was concealed or whether the taxpayer made a false statement of costs and, if so, how high was the amount of falsely stated costs or expenses. No matter whether it is proof of concealed income or reasoning about falsely stated costs or expenses, it all requires direct evidence to confirm it properly. If evidence is lacking or it is difficult to form an effective chain of evidence between the pieces, making it impossible to make proper confirmation of concealed income or falsely stated costs or expenses, it will be difficult to make a finding of so-called tax evasion. Tax determined under the method of assessment collection has the potential to be either more or less than the taxpayer's actual unpaid or underpaid tax. But, clearly, said tax is not the same as the taxpayer's actual unpaid or underpaid tax. Considering the impossibility or difficulty that the defendant has in providing sufficient evidence to prove that the defendant did not pay or underpaid tax and show the amounts involved, then it is clearly difficult to apply Article 63 of the Tax Administration Law and, of course, the penalty issued against the plaintiff lacks a legal basis.

According to Article 37 of the Tax Administration Law: "Where a taxpayer engaged in production or business operation without tax registration in accordance with the regulations and a taxpayer temporarily engaged in business operation, the tax authorities shall assess the amount of tax payable thereof and order the taxpayer to pay tax; and where tax remains unpaid, the tax authorities may detain the commodity or goods thereof in a value to the equivalent of the amount of tax payable." Naturally, an unregistered taxpayer that engages in business operations does not file tax returns

or pay tax on the income derived from production or business operation, but the Tax Administration Law only provides for assessment of the taxable amount under said circumstances of unpaid or underpaid tax and does not provide for the imposition of late fees or penalties. Even if coercive measures are taken against a taxpayer who refuses to pay the tax assessed, those coercive measures are only taken against commodity or goods in a value to the equivalent of the amount of tax payable and do not even include late fees. From this, one can see extremely clearly that the legislative intent of the Tax Administration Law does not involve late fees or penalties for assessments of payable tax.

Even in tax investigation cases, assessments are still approved after the fact. For example, Article 3 of the Guide to After-the-Fact Assessments of Enterprise Income Tax and Tax Assessments of Enterprise Income Tax Penalties and Late Fees issued by the Guangzhou Local Taxation Bureau (Sui Di Shui Fa [2006] No. 192) states: "Method for after-the-fact assessment of enterprise income tax in each of the circumstances covered in Article 5 of Guangdong Local Taxation Bureau Provisional Measures for Assessment of Enterprise Income Tax (Sui Di Shui Fa [2005] No. 297) (hereafter, "Provisional Measures"): (1) If the circumstances of Point 1 of Article 5 of the Provisional Measures are met (namely, 'Failure to set up account books in accordance with laws and administrative regulations.') then issue a penalty in accordance with Article 60 of the Tax Administration Law of the PRC (hereafter, "Tax Administration Law") and assess late fees; (2) If the circumstances of Point 2 of Article 5 of the Provisional Measures are met (namely, 'Unauthorized destruction of account books or refusal to provide tax documents.') then issue a penalty under reference to the relevant provisions of Articles 60 and 62 of the Tax Administration Law and assess late fees; (3) If the circumstances of Point 3 of Article 5 of the Provisional Measures are met (namely, 'Though account books have been set up, the accounts are disorganized or cost documents, income invoices, and expense invoices are so incomplete that it is difficult to check the accounts, including: 1. Only total revenues can be accounted accurately, or total revenues can be verified but costs and expenses cannot be accurately accounted; 2. Only costs and expenses can be accounted accurately, or costs and expenses can be verified but total revenues cannot be accounted accurately; 3. Neither total revenues nor costs and expenses can be accounted accurately and true, accurate, and complete tax documents cannot be provided to the responsible tax authority such that investigation is difficult; ') then, if the invoices and relevant documents are incomplete, a penalty may be issued in accordance with Article 60 of the Tax Administration Law and late fees assessed; if the accounts are merely disorganized, a penalty is not required and issue only late fees; (4) If the circumstances of Point 3.4 of Article 5 of the Provisional Measures are met (namely, 'Even though account books are set up and the accounting is in accord with regulations, relevant account books, invoices, and tax documents have not been kept.') then issue a penalty in accordance with Article 60 of the Tax Administration Law and assess late fees; (5) If the circumstances of Point 4 of Article 5 of the Provisional Measures are met (namely, 'Failure by a public institution, social organization, or private non-enterprise unit to account costs, expenses, and losses

related to taxable income separately from costs, expenses, and losses related to non-taxable income according to regulations, and the amount of taxable revenue cannot be calculated according to the apportionment method or other reasonable methods.') then it is unnecessary to issue a penalty and issue only late fees; (6) If the circumstances of Point 5 of Article 5 of the Provisional Measures are met (namely, 'If a taxpayer with an obligation to pay enterprise income tax fails to complete the taxation registration according to statute but engages in production or business.') then issue a penalty in accordance with Article 62 of the Tax Administration Law and assess a late fee; (7) If the circumstances of Point 6 of Article 5 of the Provisional Measures are met (namely, 'If there is a tax obligation but failure to file a tax return within the statutory period or, having been given a deadline by the tax authorities to file a return, failing to file the return by the deadline.') then issue a penalty in accordance with Article 62 of the Tax Administration Law and assess a late fee; (8) If the circumstances of Point 7 of Article 5 of the Provisional Measures are met (namely, 'The tax basis reported by the taxpayer is obviously low, without good reason.') and none of the other circumstances of Article 5 of the Provisional Measures are met, no penalty should be issued or late fees assessed for the time being at the time of the first after-the-fact assessment and the taxpayer ordered to rectify the problem. If the same circumstances are again found to have occurred, the case should be transferred to the investigation authorities for handling."

First, this document clearly points out that assessments may be made beforehand; that is, after the taxpayer makes annual applications, verification of the taxpayer's income tax assessment method is made and an assessment is approved according to the taxable income rate. At the same time, the document also clearly stipulates, and moreover in accordance with Article 1 ("These measures are hereby enacted in order to further standardize the work of assessing enterprise income tax and strengthening management of assessments of enterprise income tax and in accordance with the Tax Administration Law of the PRC [hereafter 'Tax Administration Law'] and its implementation measures [hereafter, 'Tax Administration Law Implementation Measures'], the Provisional Enterprise Income Tax Regulations of the PRC [hereafter, 'Regulations'] and its implementation rules [hereafter, 'Implementation Rules'], and the State Administration of Taxation's Provisional Measures on the Assessment of Enterprise Income Tax [hereafter, 'Assessment Measures'] [Guo Shui Fa (2000) No. 38], combined with the specific circumstances in our city."), Article 3 ("Assessment of enterprise income tax can be categorized according to the relative position of the act of assessment with respect to the tax period as either before-the-fact assessment, current assessment, and after-the-fact assessment."), and Article 4 ("Before-the-fact assessment refers to an assessment of the current year's monthly (or quarterly) tax by the tax authorities based on a taxpayer's previous monthly or annual circumstances. Current assessment refers to an assessment of tax made by the tax authorities for a taxpayer who has recently obtained certain income and requests that the tax authorities issue a tax invoice but the relevant income or expense invoices are not complete. After-the-fact assessment refers to an assessment by the tax authorities after the tax period is concluded when it is discovered through examination or inspection

that the taxpayer meets one of the circumstances in Article 5 of these measures.") of Guangzhou Local Taxation Bureau Provisional Measures on the Assessment of Enterprise Income Tax (Sui Di Shui Fa [2005] No. 297), approved assessments may also be made after-the-fact; that is, after the end of the tax period, if the tax authorities discover during an investigation that an assessment needs to be made against a taxpayer, the assessment may be made after the fact.

Next, this document clearly stipulates that when an assessment is made in the after-the-fact manner, when a penalty is imposed in accordance with Article 60 of the Tax Administration Law ("Where a taxpayer commits one of the following acts, he shall be ordered by the tax authorities to rectify within a time limit and may be fined not more than RMB 2,000 yuan; if the circumstances are serious, he may be fined not less than 2,000 yuan but not more than 10,000 yuan."), the maximum penalty may not exceed 10,000 yuan. In other words, when after-the-fact assessment is employed, the provisions on tax evasion in Article 63 of the Tax Administration Law may not be applied and neither, of course, may corresponding penalties be imposed.

The plaintiff maintains, first of all, that assessment of taxes may occur both before the fact and after the fact. Next, regardless of whether the assessment is made before the fact or after the fact, the bases for its legal enforcement are the Provisional Measures of the PRC on Enterprise Income Tax, the Enterprise Income Tax Law of the PRC (hereafter, "Enterprise Income Tax Law"), regulatory documents of the State Administration on Taxation regarding assessment of enterprise income tax, and various local taxation authorities' implementation rules for the assessment of enterprise income tax; there are no separate legal bases applicable for before-the-fact and after-the-fact assessments. Finally, when after-the-fact assessment is employed, since the governing law cited by each locality is the same, the legal basis for enforcement in each locality should be identical. For the same act, there should not be a situation in which a fine of no more than 10,000 yuan is imposed in the south whereas in the north a so-called 150 percent fine of as much as 6,733,716.36 yuan is imposed in the north.

2. Errors in the application of the Administrative Penalty Law

In Page 3, Paragraph 2, of the Penalty Decision, the defendant states: "Your company is required to submit payment to the Beijing Municipality Chaoyang District Branch Treasury Office within 15 days of receipt of this decision. If payment is not made by this deadline, our bureau may impose an additional fine of 3 percent of the penalty for each day in accordance with Article 51.1 of the Administrative Penalty Law.

According to the provisions of Supreme People's Court Reply Concerning Whether to Calculate Additional Fines During the Litigation Period (SPC [2005] Xing Ta Zi No. 29): "According to the relevant provisions of the Administrative Procedure Law of the PRC, additional fines imposed for failing to fulfill the obligations of an administrative penalty decision fall under the category of enforcement penalties and should not be calculated during the litigation period."

First, this judicial interpretation is applicable to all administrative penalty

decisions made by administrative organs, regardless of whether said administrative organ is a taxation authority.

Second, since enforcement penalties should not be calculated during the litigation period, additional fines during the reconsideration period are also enforcement penalties and should not be calculated during the reconsideration period. In the article "Additional Fines for Administrative Penalties Should not be Calculated During the Litigation Period," published in the 11th issue of 2008 of *People's Judiciary*, the presiding judge of the Administrative Litigation Division of the Supreme People's Court, Cai Xiaoxue, clearly states that were additional fines on an administrative penalty to continue to be calculated during the litigation period, it would potentially cause the amount of additional fines payable by the administrative counterparty to exceed the amount of the original penalty itself, thereby discouraging the administrative counterparty from pursuing administrative litigation and resulting in failure to give adequate protection to the administrative counterparty's right to appeal. This would clearly not be in keeping with the goal of the Administrative Procedure Law to safeguard the administrative litigation rights of citizens, legal persons, and other entities. Were a party to choose to bring a lawsuit directly to a People's Court, then there would be no additional fines calculated, based on the provisions of the Supreme People's Court Reply Concerning Whether to Calculate Additional Fines During the Litigation Period (SPC [2005] Xing Ta Zi No. 29). Were a party to choose to request administrative reconsideration by the taxation authority, and additional fines continued to be calculated during the administrative reconsideration period, it would similarly discourage the administrative counterparty from requesting administrative reconsideration, impede the fair exercise of the party's rights to judicial choice, and render completely meaningless the options provided for in Article 88(2) of the Tax Administration Law. Therefore, if the defendant mechanically cites Article 55.1 of the Administrative Penalty Law without distinguishing whether administrative reconsideration has been requested or an administrative lawsuit filed, it inevitably deviates from the Administrative Reconsideration Law's goal of "preventing and setting right illegal or inappropriate specific administrative acts, protecting the lawful rights and interests of citizens, legal persons and other entities, and ensuring and supervising the performance of functions and powers by administrative organs in accordance with the law."

3. The defendant relied upon a regulatory document concerning taxation that lacks legitimacy

The plaintiff maintains that the State Council Notice Regarding Questions About Violations of Stamp Duty Regulations (Guo Shui Fa [2004] No. 15), upon which the defendant based its Penalty Decision, lacks legitimacy and the People's Court should not admit it.

Part 2(1) of the defendant's Penalty Decision states: "In accordance with Article 64(2) of the Tax Administration Law of the PRC and Article 1 of the State Administration of Taxation Notice Regarding Questions About Violations of Stamp Duty Regulations (Guo Shui Fa [2004] No. 15), your company is fined 300 percent,

or 13,106.01 yuan, for failure to affix duty stamps in accordance with regulation."

The aforementioned basis, namely the State Administration of Taxation Notice Regarding Questions About Violations of Stamp Duty Regulations (Guo Shui Fa [2004] No. 15) states: "Since the re-revision and promulgation of the Tax Administration Law of the PRC (hereafter "Tax Administration Law"), and the Implementation Regulations for the Tax Administration Law of the PRC (hereafter "Tax Administration Law Implementation Regulations"), portions of Article 13 of the PRC Provisional Measures for Stamp Duty (hereafter, "Stamp Duty Provisional Measures") and Articles 39, 40 and 41 of the Implementation Rules for the PRC Provisional Measures for Stamp Duty (hereafter "Implementation Rules for Provisional Measures for Stamp Duty") are no longer applicable. In order to strengthen management of stamp duty collection and handle violations of applicable stamp-duty regulations in accordance with the law, based on the relevant provisions of the Tax Administration Law and the Tax Administration Law Implementation Regulations, the fines for violations of the regulations concerning stamp duty are clarified as follows: when a person obligated to pay stamp duty commits one of the following, the tax authority shall impose a penalty according to the severity of the circumstances: 1. For failure to affix or affixing an insufficient amount of tax stamps to a taxable invoice, or failing to cancel or cross tax stamps that have already been affixed to a taxable invoice, apply penalties in accordance with Article 64 of the Tax Administration Law."

The plaintiff maintains that the "Guo Shui Fa (2004) No. 15" document lacks legitimacy. The reasoning is as follows:

(1) It violates provisions of the Legislation Law.

In fact, the "Guo Shui Fa (2004) No. 15" document holds that, because of the promulgation of a new law and new regulations, certain provisions of an administrative regulation (PRC Provisional Measures for Stamp Duty [hereafter, "Stamp Duty Measures"]) and departmental rules (Implementation Rules for the PRC Provisional Measures for Stamp Duty [hereafter "Implementation Rules for the Stamp Duty Measures"] that are still in force contravene the provisions of legislation of a higher level or there are inconsistencies between the provisions of administrative regulations, and there are some provisions that are no longer appropriate. However, in the following three circumstances, the State Administration of Taxation lacks the authority to make changes to administrative rules and regulations:

A. When legislation of lower levels contravenes legislation of upper levels. Of the legislation cited in the State Administration of Taxation Notice Regarding Questions About Violations of Stamp Duty Regulations (Guo Shui Fa [2004] No. 15), the Tax Administration Law is legislation of upper levels compared to the Stamp Duty Measures and the Implementation Regulations for the Tax Administration Law of the PRC (hereafter, "Tax Administration Law Implementation Regulations") is legislation of upper levels compared to the Implementation Rules for the Stamp Duty Measures.

If legislation of lower levels is found to contravene legislation of upper levels, then according to Article 87 (“Under any of the following circumstances, laws, administrative regulations, local regulations, autonomous regulations, separate regulations or rules shall be altered or annulled by the organ concerned in accordance with the limits of power prescribed in Article 88 of this Law: . . . [2] where provisions of the legislation of lower levels contravene those of the legislation of upper levels;”) and Article 88 (“The limits of power for altering or annulling laws, administrative regulations, local regulations, autonomous regulations, separate regulations or rules are as follows: . . . [2] The Standing Committee of the National People's Congress has the power to annul any administrative regulations which contradict the Constitution and laws, to annul any local regulations which contradict the Constitution, laws or administrative regulations, and to annul any autonomous regulations or separate regulations which have been approved by the standing committees of the people's congresses of the relevant provinces, autonomous regions or municipalities directly under the Central Government but which contravene the Constitution or the provision of Article 66(2) of this Law; [3] The State Council has the power to alter or annul any inappropriate rules of the departments and of local governments.”) of the Legislation Law, the organ with authority to alter the Stamp Duty Measures should be the Standing Committee of the National People's Congress and not the State Administration of Taxation, which issued the “Guo Shui Fa (2004) No. 15” document.

B. When there are inconsistencies between the provisions of administrative regulations. The Tax Administration Law Implementation Regulations and the Stamp Duty Measures are classified as administrative regulations of the same level, and, according to Article 85 (“Where there is inconsistency between the new general provisions and the old special provisions in different administrative regulations governing one and the same matter and it is hard to decide which provisions shall prevail, a ruling shall be made by the State Council.”) of the Legislation Law, if there are inconsistencies between the two a ruling should be issued by the State Council and not the State Administration of Taxation, which issued the “Guo Shui Fa (2004) No. 15” document.

C. The provisions of administrative rules are found to be inappropriate. The Implementation Rules for the Stamp Duty Measures fall under the category of departmental rules, and according to Article 87 (“Under any of the following circumstances, laws, administrative regulations, local regulations, autonomous regulations, separate regulations or rules shall be altered or annulled by the organ concerned in accordance with the limits of power prescribed in Article 88 of this Law: . . . [4] where the provisions of rules are considered inappropriate and should therefore be altered or annulled.”) and Article 88 (“The limits of power for altering or annulling laws, administrative regulations, local regulations, autonomous regulations, separate regulations or rules are as follows: . . . [3] The State Council has the power to alter or annul any inappropriate rules of the departments and of local governments.”) of the Legislation Law, if Articles 39, 40 and 41 of the Implementation Rules for the Stamp Duty Measures are found to be inappropriate, then they should be altered or

annulled by the State Council and not the State Administration of Taxation, which issued the "Guo Shui Fa (2004) No. 15" document.

(2) It violates provisions of the Administrative Penalty Law regarding the enactment of administrative penalties. According to Article 9 ("Different types of administrative penalty may be created *by law*."), Article 10 ("Administrative penalties, with the exception of restricting freedom of person, may be created *by administrative rules and regulations*."), Article 11 ("Administrative penalties, with the exception of restriction of freedom of person and revocation of business license of an enterprise, may be created *in local regulations*."), Articles 12(1) and 12(2) ("The ministries and commissions under the State Council may, *in the rules they enact*, formulate specific provisions within the limits of the acts subject to administrative penalty and the types and range of such penalty as prescribed by laws and administrative rules and regulations. With regard to violations of administration order against whichnno laws or administrative rules and regulations have been enacted, the ministries and commissions under the State Council may create administrative penalty of disciplinary warning or a certain amount of fine in the rules they enact, as stipulated in the preceding paragraph. The specific amounts of fine shall be laid down by the State Council."), Article 13 ("The people's governments of provinces, autonomous regions, and municipalities directly under the Central Government, of the cities where the people's governments of provinces and autonomous regions are located, and of the larger cities approved as such by the State Council may, within the limits of the acts subject to administrative penalty and the types and range of such penalty as prescribed by laws and regulations, formulate specific provisions *in the rules they enact*."), and Article 14 ("*No administrative penalties shall be created in any other regulatory documents* in addition to the ones as stipulated in Articles 9, 10, 11, 12 and 13 of this Law.") of the Administrative Penalty Law, other than law, regulation (including administrative regulations and local regulations), or rules (including departmental rules and local rules), no "other regulatory documents," including "regulatory documents concerning taxation," shall create any administrative penalties. Administrative tax penalties are a type of administrative penalty, so of course they may not be enacted through "regulatory documents concerning taxation."

Furthermore, according to Article 12(3) of the Administrative Penalty Law ("The State Council may authorize the departments directly under it that have the power of administrative penalty to formulate provisions on administrative penalty in accordance with the first and second paragraphs of this Article."), the State Administration of Taxation, as a department directly under the State Council, may only enact administrative tax penalties through the provisions of "rules" with clear authorization from the State Council and may not enact them through provisions of "regulatory documents concerning taxation" issued by the tax authority.

However, the "Guo Shui Fa (2004) No. 15" document, as a "regulatory document concerning taxation" and despite having no authority to enact administrative tax penalties, clearly contains provisions to the effect of "when a person obligated to pay

stamp duty commits one of the following, the tax authority shall impose a penalty according to the severity of the circumstances." Therefore, it violates the provisions of the Administrative Penalty Law regarding jurisdiction to enact administrative penalties. On this point, Article 5 ("Regulatory documents concerning taxation *shall not enact* provisions on matters of commencing or stopping the collection of tax, reducing tax, exemption from tax, tax refund, or additional tax payment; administrative licensing, administrative approvals, *administrative penalties*, administrative enforcement, or administrative service fees; or any other matters that shall not be enacted by regulatory documents concerning taxation, with the exception of matters such as tax reduction or tax exemption as approved for enactment by the State Councila.") of the Measures for the Administration of Drafting of Regulatory Documents Concerning Taxation (Decree No. 20 of the State Administration of Taxation) also makes a clear prohibition.

III. Violations of legal procedure

According to Article 54(2) ("[After hearing a case, the court may] rule to revoke or partially revoke a specific administrative act, or else rule the defendant to make a new administrative act if a specific administrative act has been taken in one of the following circumstances: . . . 3. it violated legal procedures; 4. it was made through exceeding authority; or 5. it was an abuse of authority.") of the Administrative Procedure Law of the PRC (hereafter "Administrative Procedure Law") and Article 24 ("When carrying out an inspection, evidence that can confirm the facts of the case shall be collected in accordance with legal limits on authority and procedures.") of the Tax Inspection Work Procedures (Guo Shui Fa [2009] No. 157), a penalty decision taken against the plaintiff by the defendant should have sufficient evidence, and said evidence should be lawful in nature, which includes having been obtained through legal procedures. If the defendant collects evidence in violation of legal procedure, said evidence should not be used as the factual basis of a specific administrative action. At the same time, if there are violations of legal procedure at the time that the defendant is carrying out a specific administrative action, that specific administrative action should be annulled in accordance with the law. As for the defendant in this case, its enforcement of the law involved serious violations of legal procedure, exceeding of authority, and abuses of power, and its penalty decision should of course be annulled in accordance with the law.

1. Seriously unlawful procedures [including] early intervention by the public security department, joint action by public security and taxation [agencies], and arresting before carrying out an audit

(1) Facts

The plaintiff first received the defendant's Tax Inspection Notice on April 8, 2011; however, prior to this, the plaintiff's employees Ai Weiwei, Wen Tao, and Hu Mingfen had already been detained by public security organs. After April 8, 2011, the public security organs detained the plaintiff's shareholder Liu Zhenggang and employee Zhang Jinsong. Specific facts are as follows:

On the morning of April 3, 2011, Ai Weiwei was taken away by the police at the Capital International Airport before completing border-exit formalities. Up until June 22, when Ai Weiwei was "released on bail pending further investigation" and returned home, his family never received any official notification and were unable to know the charges alleged, what coercive measures had be taken, or where he was in custody.

At 12 noon on April 3, 2011, the Beijing Public Security Bureau carried out a search lasting nearly 12 hours on the house of Ai Weiwei located at No. 258, Caochangdi, Chaoyang District, seizing 127 items including computers, portable hard drives, CDs and books. The inventory of items seized was issued in the name of the Chaoyang District Branch of the Beijing Public Security Bureau. Ten people from Ai Weiwei Studio were brought to Nan'gao Police Station for questioning until the early morning [of the next day].

At 2 p.m. on April 3, 2011, Ai Weiwei's assistant Wen Tao was forced into a black Buick by four men in civilian clothes and taken away. Having lost contact with him, his family went to the Nan'gao Police Station responsible for the area where the incident occurred and reported a case of kidnapping. On the evening of June 24, Wen Tao was sent home by Beijing public security officers, who demanded that he not discuss details of his detention publicly or have any contact with Ai Weiwei. During Wen Tao's disappearance, his family members did not receive any paperwork. Wen Tao himself still does not know why he was detained for 83 days.

At approximately 11:30 p.m. on April 6, 2011, the defendant and the Beijing Public Security Bureau went to Beijing Huxin Financial Accounting Services Co., Ltd. (hereafter "Huxin Company"), which had been entrusted to keep the plaintiff's accounts, and seized the original vouchers, accounting vouchers, tax vouchers, balance sheets, income statements and other accounting documents of the plaintiff [dating] from 2000 to February 2011. At 12:47 a.m. [on April 7], Xinhua News Agency issued a report in English, stating: "Ai Weiwei is being investigated according to law on suspicion of economic crimes."

On April 7, 2011, the Beijing Economic Crime Investigation Unit brought the plaintiff's accountant, Hu Mingfen, who had been visiting relatives in Lanzhou, back to Beijing, at which point Hu Mingfen lost contact with family. Until June 13, when she was "released on bail pending further investigation," her family never received any official paperwork [regarding her whereabouts].

At 3 p.m. on April 8, 2011, the defendant and Beijing public security organs went to the plaintiff's accounts office and searched and seized all financial and accounting documents, contracts and seals and other items from 2005 to 2010. At this time, the defendant made a record of its questioning of Zhang Jinsong, Ai Weiwei's driver, and for the first time issued the plaintiff a Tax Inspection Notice and Inquiry Notice, and the plaintiff's legal representative, Lu Qing, was required to go to the Beijing Local Taxation Bureau on April 12 for questioning.

At 7 p.m. on April 9, 2011, Liu Zhenggang, a shareholder of the plaintiff, was forcibly taken away by four men in civilian clothes from his residential community in Haidian District and taken to an unknown location. His wife then reported a kidnapping case to the Dazhongsi Police Station in Haidian District. On June 11, when Liu Zhenggang was "released on bail pending further investigation," his family members had not yet received any official paperwork [concerning his whereabouts].

At 1 a.m. on April 10, 2011, Zhang Jinsong lost contact after leaving his friends. His family went to Nan'gao Police Station in Chaoyang District to report his disappearance. On June 23, Zhang Jinsong was "released on bail pending further investigation." Prior to that, his family members did not know his whereabouts and never received any official paperwork.

At 9:30 a.m. on April 12, 2011, only after three raids and the "disappearance" of five persons did the defendant conduct its first questioning of Lu Qing, the plaintiff's legal representative.

On May 20, 2011, Xinhua News Agency issued a news brief, saying, "Xinhua News Agency reporters have learned from Beijing public security organs that, after further investigation of the case of Ai Weiwei's suspected economic crimes, the public security organs have initially identified that Fake Design Culture Development Ltd., which is actually controlled by Ai Weiwei, has committed criminal activity such as evasion of huge amounts of taxes and intentional destruction of accounting documents."

On the evening of June 22, 2011, after detention of 81 days, Ai Weiwei was "released on bail pending further investigation" without any official explanation to the family. At 10:15 that night, Xinhuanet issued a short news item in both Chinese and English, saying: "Reporters have learned from the Beijing public security organs that the public security organ carried out an investigation of Ai Weiwei in accordance with the law on suspicion of economic crimes and discovered that Beijing Fake Cultural Development Limited, which is actually controlled by him, carried out criminal acts such as evasion of a large amount of tax and intentional destruction of accounting documents. In light of Ai Weiwei's good attitude in admitting his crimes and the fact that he suffers from chronic illness, combined with his multiple expressions of willingness to pay the taxes owed, Ai Weiwei has been released on bail pending further investigation in accordance with the law."

The above facts show that the close cooperation between the defendant and the public security organs is directly related to the plaintiff's tax case.

(2) Procedural error 1: Early intervention in the tax evasion case by the public security organs

According to Article 201(1) ("Where any taxpayer files false tax returns by cheating or concealment or fails to file tax returns, and the amount of evaded taxes is relatively large and accounts for more than 10 percent of of the taxes owed, he shall be sentenced to fixed-term imprisonment not more than three years or penal detention, and be fined; or if the amount is huge and accounts for more than 30 percent of the taxes owed, he shall be sentenced to fixed-term imprisonment not less than three years but not more than seven years, and be fined") and Article 201(4) ("Where any taxpayer who committed the act as described in Paragraph 1 has made up the payable taxes and paid the late fine after the tax authority sent down the notice of tax recovery according to law, he shall not be subject to criminal liability if he has already been administratively punished; however, an exception will be made for any person who has already been criminally punished in five years for evading tax payment or who has been administratively punished by the tax authorities two or more times") of the Criminal Law of the People's Republic of China (hereafter "Criminal Law") as amended on February 28, 2009, administrative sanction by the tax authorities has become a prepositional condition for the public security organs to initiate a judicial procedure.

According to Article 57(1) of the Notice of the Supreme People's Procuratorate and the Ministry of Public Security on Issuing the Provisions (II) of the Supreme People's Procuratorate and the Ministry of Public Security on the Standards for Filing Criminal Cases under the Jurisdiction of the Public Security Organs for Investigation and Prosecution, promulgated on May 7, 2010: "Tax evasion cases (Article 201 of the Criminal Law): For any tax evasion involving one of the following circumstances, a case will be filed for investigation and prosecution: (1) A taxpayer files false tax returns through cheating or concealment or fails to file tax returns, the amount of evaded taxes is more than 50,000 yuan and accounts for more than 10 percent of the taxes owed and, after the tax authority issues a notice of tax recovery according to law, fails to make up the taxes owed or pay the late fine or refuses to be administratively punished; (2) A taxpayer has already been criminally punished in five years for evading tax payment or has been administratively punished by the tax authorities two or more times, and has evaded taxes, with the amount of evaded taxes being more than 50,000 yuan and accounting for more than 10 percent of the taxes owed; (3) A withholding agent fails to pay or fails to pay in full the withheld or collected taxes by cheating or concealment, and the amount is more than 50,000 yuan." The plaintiff was established on November 29, 2000, had no record of criminal or administrative punishment before this tax case, did not commit the action of "after the tax authority issues a notice of tax recovery according to law, failing to make up the taxes owed or pay the late fine or refusing to be administratively punished," and thus did not meet the above standard for filing a case by the public security organs. Therefore, the defendant's cooperation in the early intervention by the public security organs and auditing the accounts through seizure of people are excessive, power-abusing, and serious illegal acts, the evidence obtained in violation of legal procedures is unlawful, and the defendant's Penalty Decision made in violation of

legal procedure should be annulled.

(3) Procedure error 2: Joint handling of the case by tax authorities and public security organs

The joint handling of the case by the defendant and the public security organs is not only a formal error; it is also a serious blurring of the boundary between administrative and judicial authority and a complete deviation from the provisions of the Criminal Procedure Law of the PRC regarding strict procedures for the filing of criminal cases and encourages an ordinary administrative body like the defendant to arrogate to itself powers to restrict personal liberty and carry out searches that the Tax Administration Law has never given to tax authorities. If all administrative organs are allowed to handle cases "jointly" with public security organs, then any administrative organ effectively has the power to deprive individuals of their liberty.

2. Before the tax inspection, the defendant did not fulfill notification obligations in accordance with the law

According to Article 22(1) of the Tax Inspection Work Procedures (Guo Shui Fa [2009] No. 157): "Before inspection, the target of the inspection shall be informed of the inspection time and necessary materials to prepare, unless prior notice would impede the inspection."

However, late at night on April 6, 2011, when there was no obstacle to inspection, the defendant failed to inform the plaintiff according to legal procedures and went ahead to the plaintiff's entrusted bookkeeper, the Huxin Company, and retrieved the plaintiff's accounting documents [covering the period] from the founding of the company in 2000 until February 2011.

3. The defendant failed to issue a tax inspection certificate or Tax Inspection Notice in accordance with the law

According to Article 59 of the Tax Administration Law ("When conducting tax inspection, the officials sent by the tax authorities shall produce tax inspection permit and tax inspection notice, and shall have the duty to protect the confidentiality of the persons under inspection; when the tax inspection permit and tax inspection notice are not produced, the persons subject to inspection shall have the right to refuse to accept the inspection.") and Article 22(2) of the Tax Inspection Work Procedures (Guo Shui Fa [2009] No. 157) ("The inspection shall be executed by two or more inspectors, who should show a tax inspection permit and Tax Inspection Notice to the target of the inspection."), it is necessary legal procedure for tax inspectors to show permits and legal tax documents to the target of an inspection.

However, late on the night of April 6, 2011, when retrieving accounting materials from Huxin Company, the defendant violated legal procedure by failing to produce a tax inspection permit and Tax Inspection Notice.

4. The defendant committed a serious violation of legal procedure in retrieving the plaintiff's accounting documents

According to Article 25 of the Tax Inspection Work Procedures (Guo Shui Fa [2009] No. 157), "When retrieving account books, accounting vouchers, statements and other relevant information, a Notice for Retrieving Account Books and Documents should be issued to the target of the inspection and an Inventory of Retrieved Account Books and Documents completed for the target's signature after being checked and confirmed." According to Article 26 of the same procedures, "When it is necessary to retrieve original documents as evidence, a Dedicated Receipt for Retrieval of Evidence should be issued to the relevant party, who should check it and confirm with a signature," "when it is necessary to take an issued invoice for inspection, an Invoice Exchange Receipt should be issued to the work unit or individual who is being inspected," and "when it is necessary to take blank invoices for inspection, a Blank Invoice Retrieval and Inspection Receipt should be issued to the work unit or individual who is being inspected."

However, when retrieving accounting materials from Huxin Company and the plaintiff, the defendant failed to issue a Notice for Retrieving Account Books and Documents or complete an Inventory of Retrieved Account Books and Documents to be given to the plaintiff for checking and confirmation. When retrieving original documents as evidence and examining invoices from the Huxin Company and the plaintiff, the defendant never issued a Dedicated Receipt for Retrieval of Evidence, a Invoice Exchange Receipt, or a Blank Invoice Retrieval and Inspection Receipt.

5. The accounting materials of the plaintiff retrieved by the defendant were not returned within the statutory time limit

According to Article 86 of Rules for the Implementation of the Tax Administration Law of the PRC ("A taxation authority exercising its powers of office provided under the provisions of item [1] of Article 54 of the Tax Administration Law may do so at the business premises of a taxpayer or tax-withholding agent. If deemed necessary and subject to approval by the head of a taxation authority at county level or above, the taxation authority may also demand that the taxpayer's or tax withholding agent's account books, accounting documentation, statements and other relevant documents of the previous accounting year be submitted for examination. In so doing, however, the taxation authority must provide the taxpayer or tax withholding agent with a detailed list of the items taken and shall return them intact within three months; in special cases, the taxation authority may return the taxpayer's or tax withholding agent's account books, accounting documentation, statements and other relevant materials of the current accounting year for examination, which must be returned by the taxation authority within 30 days.") and Article 25(2) of the Tax Inspection Work Procedures (Guo Shui Fa [2009] No. 157) ("Retrieval of the taxpayer's or tax withholding agent's account books, accounting documentation, statements and other relevant documents of the previous accounting year shall be approved the head of a taxation authority and [the documents] shall be returned within

three months; retrieval of the taxpayer's or tax withholding agent's account books, accounting documentation, statements and other relevant documents of the current accounting year shall be subject to approval by the head of a taxation authority at city and autonomous prefecture level or above and they must be returned within 30 days."), any of the plaintiff's prior-year accounting documents retrieved by the defendant should have been returned intact within three months; any of the plaintiff's current-year accounting documents retrieved by the defendant should have been returned within 30 days.

However, the defendant did not return all the retrieved accounting documents in accordance with the law at the time that the aforementioned statutory time limit expired, and, moreover, has to date not yet returned them, which not only seriously affects the plaintiff's production and business activities, but also substantially impedes the defendant's rights to reconsideration.

6. The defendant's penalty hearing procedure was illegal

According to Article 42 ("An administrative organ, before making a decision on administrative penalty that involves ordering for suspension of production or business, revocation of business permit or license or imposition of a comparatively large amount of fine, shall notify the party that he has the right to request a hearing; if the party requests a hearing, the administrative organ shall arrange for the hearing: [3] The hearing shall be held openly, except where state secrets, business secrets or private affairs are involved.") of the Administrative Penalty Law and the provisions of Chapter II ("Penalty Procedures"), Section 3 ("Hearing Procedures") of the Provisional Measures for Management of Administrative Penalties Related to Taxation issued by the Beijing Local Taxation Bureau (Jing Di Shui Fa [2001] No. 488), hearings are a necessary procedural part of administrative penalties related to taxation and, if the plaintiff requests it, the defendant should arrange a hearing to be held in accordance with procedures and requirements. If the hearing itself violates regulations and procedures, it will inevitably result in the administrative penalty related to taxation being itself a "violation of statutory procedure" and, on this basis, the corresponding administrative penalty related to taxation should be annulled. Though the defendant held a hearing in this case, the hearing procedures seriously violated the law.

(1) The hearing was not held openly in accordance with the law

According to Article 53 ("When target of the inspection or other party related to the tax matter requests a hearing, a hearing shall be held and conducted by a hearing officer. The hearing should be carried out in accordance with the relevant regulations of the State Administration of Taxation.") of the Tax Inspection Work Procedures (Guo Shui Fa [2009] No. 157), and Article 2 ("Hearings on Administrative Penalties Related to Taxation abide by the principles of legality, fairness, openness, timeliness, and convenience.") and Article 11 ("Hearings on Administrative Penalties Related to Taxation shall be carried out openly, except when state secrets, business secrets, or

private affairs are concerned. In cases where there are open hearings, an announcement shall be made beforehand of the names of the parties and investigators in the case, the matter at hand, and the time and location of the hearing. Members of the public shall be allowed to observe open hearings. Observing members of the public may make comments with the prior permission of the hearing officer. In cases where hearings are not open, the reason for not opening the hearing shall be announced.") of the Implementation Measures for the Procedure for Hearings on Administrative Penalties Related to Taxation (Guo Shui Fa [1996] No. 190), except when state secrets, business secrets, or personal affairs are involved, hearings on administrative penalties related to taxation should be held in public.

On June 29, 2011, the plaintiff submitted a written application for a hearing. In response to the defendant's decision to "close the hearing" on the grounds of the "business secrets" of a third party, the plaintiff twice submitted written objections, but the defendant refused to explain its reasoning. During the hearing on July 14, 2011, the defendant failed to produce to the plaintiff any application from a third party requesting protection of secrecy.

Open hearings are a procedural requirement for administrative penalties related to taxation. If the hearing in this case concerned the business secrets of a third party, then the defendant should make clear the third party's written application for protection of secrets. However, according to interpretations of business secrets in the Criminal Law and the Anti-Unfair Competition Law of the PRC, the meaning of business secrets is "technical or business information which is of a practical nature, is unknown by the public, can bring economic profits to the person who enjoys the rights, and for which the person who enjoys the rights has taken steps to protect as secret." The defend157ant has no proof of third party information that simultaneously satisfies the aforementioned characteristics of "unknown by the public," "can bring economic profits to the person who enjoys the rights," "is of a practical nature," and "for which the person who enjoys the rights has taken steps to protect as secret," and the claim of "business secrets" is completely groundless.

(2) The plaintiff was illegally deprived of its rights to statement and defense

According to Article 14 ("During the hearing, the hearing officer shall state the charges of the party's illegal acts and present factual evidentiary materials.") of the (Trial) Implementation Measures for Hearings on Administrative Penalties Related to Taxation (Guo Shui Fa [1996] No. 190), when the hearing was being held the defendant should have presented the plaintiff with the evidentiary materials upon which the administrative penalty was based and provide original documents in order to allow verification of the authenticity of the evidence. But from the beginning the defendant only provided photocopies of the relevant evidence, and said photocopies were not confirmed with the plaintiff's chop. Because the defendant never provided the plaintiff with original copies for comparison, it was impossible for the plaintiff to verify the authenticity, legality, or validity of the evidence, which substantively deprived the plaintiff of its rights to statement and defense.

7. The principle of checks through division of labor failed to be realized

According to Article 5 of the Tax Inspection Work Procedures (Guo Shui Fa [2009] No. 157): "When the investigation branch investigates a case of illegality related to taxation, it should follow the principle of checks through division of labor in selection of cases, investigation, hearing, and enforcement." According to Article 3 of the (Trial) Implementation Measures for Separation Between Investigation and Penalty Decisions in Taxation Cases (Guo Shui Fa [1996] No. 190): "Investigation and retrieval of evidence in all types of taxation cases shall be the responsibility of the relevant investigation units of the taxation authority. Review of the results of the investigation of a case shall be the responsibility of a relatively detached body (hereafter referred to as the review body) assigned by the responsible person in the taxation authority." However, in its taxation investigation of the plaintiff, the defendant did not fulfill the above statutory requirements. For example, prior to conducting the penalty hearing on July 14, 2011, personnel from the Operations Section (Legal Section) had already participated in the "meeting of the Taxation Investigation Case Hearing Committee" held on June 27, 2011.

8. The defendant failed to conduct the examination and hearing in accordance with legal procedure

According to Article 40 ("In the course of an inspection, inspection personnel should produce a signed, dated Tax Inspection Working Draft to record the facts of the case and collect the relevant evidentiary documents."), Article 42 ("After the inspection is completed, a Tax Inspection Report should be produced on the basis of the Tax Inspection Working Draft and related documents and inspected by responsible persons at the inspection authority."), and Article 43 ("When an inspection is concluded, the inspection authority shall send the Tax Inspection Report, Tax Inspection Working Draft, and related evidentiary documents to the hearing body within five working days for a hearing and take care of the handover procedures.") of the Tax Inspection Work Procedures (Guo Shui Fa [2009] No. 157), the defendant should, in the course of a tax inspection, produce such legally required documents as a Tax Inspection Working Draft and Tax Inspection Report and use these as the basis of a hearing.

However, in this case, the basis for the defendant's Penalty Decision against the plaintiff lacked a Tax Inspection Working Draft and Tax Inspection Report.

IV. The defendant exceeded its authority

The "concealed income" found by the defendant includes: 1,107,716 yuan for decoration under "Boya Gardens," 928,118.36 yuan for decoration under "Naga," and 4,507,890 yuan under "Three Shadows Centre." Since the plaintiff does not have relevant qualifications in the construction industry, then even if the above decoration income belong to the plaintiff, it would qualify as operations "without obtaining qualifications." According to Article 6 ("The competent construction administrative department under the State Council shall exercise unified supervision and regulation over construction activities throughout the country.") and Article 65(3) ("[An

organization] that contracts projects without a certificate of qualification shall be banned and fined, with any illegal income confiscated.") of the Construction Law of the PRC, the authority to manage and punish income of "an organization which contracts projects without a certificate of qualification" rests with the administrative departments of construction under the State Council, instead of with tax authorities.

V. The administrative penalty was obviously unfair

In Parts 2(1), 2(2), and 2(3) of the defendant's Penalty Decision, penalties were issued in the amounts of 300 percent, 150 percent, 10,000 yuan, and 10,000 yuan.

According to the provisions of the Beijing Local Taxation Bureau's Forwarded Notice from the Beijing Municipality People's Government Regarding Supporting Systems for an Administrative Law Enforcement Responsibility System (Jing Di Shui Fa [2007] No. 349) and Article 5 ("The standardization of free discretion in administrative penalties shall be carried out according to legal goals; take full consideration of and weigh the facts, nature, circumstances, and level of social harm of an illegal act; and exclude interference by irrelevant matters. In response to similar acts of administrative illegality with basically the same facts, nature, circumstances, and level of social harm, the legal basis and the type and scale of the penalty should be basically similar.") of Beijing Municipality's Several Regulations Regarding the Standardization of Discretion in Administrative Penalties (Jing Zheng Fa [2007] No. 17), the defendant should exclude interference by irrelevant matters and apply basically the same scale of penalty for similar acts, or the scale of punishment should not be greater than that applied to acts of a more serious nature.One can see from the State Administration of Taxation's report on major tax cases (see http://www.chinatax.gov.cn/n8136506/n8136548/n8136623/8279062.html) that in June 2007 the Beijing Local Taxation Bureau carried out a full audit of the taxes of Beijing Taiyue Real Estate Development Co., Ltd, finding that the company had filed false tax returns and under-reported 1.353 billion yuan in income taxable for the purposes of sales tax, with the amount of sales tax involved at 67.6287 million yuan.The tax authorities ordered Beijing Taiyue Real Estate Development Co., Ltd, to make supplementary payments of 67.6287 million yuan in sales tax, 4.734 million yuan in urban maintenance and construction tax, and 2.0289 million yuan in education surtax, imposed 32.468 million yuan in late fees and a penalty of 36.1814 million yuan. That case involved the sensitive real estate industry and has been identified by the State Administration of Taxation as a major tax case. The amounts and impact of this case far exceed those of this case, but the scale of the penalty was only 50 percent of taxes owed. How can the defendant penalize the plaintiff between 150 and 300 percent in this case, with a maximum fine of 10,000 yuan?

Even considering Article 7 ("When formulating standards for giving heavier administrative penalties, consideration shall be given to the following circumstances: [1] Concealing or destroying evidence of illegality or other acts of interference in enforcing the law; [2] Failing to heed warnings and continuing to engage in illegal acts; [3] Flagrant illegality that results in serious consequences; [4] Compelling, luring, or inciting others to engage in illegal acts; [5] The primary party in an illegal act committed jointly; [6] Illegal acts committed multiple times after refusing to

reform; [7] Illegal acts committed during a public emergency; [8] Other circumstances in which heavier penalties may be imposed.") of Beijing Municipality's Several Regulations Regarding the Standardization of Discretion in Administrative Penalties (Jing Zheng Fa [2007] No. 17), none of the circumstances above apply to the plaintiff, so how can a heavier administrative penalty be imposed? Clearly, the administrative penalty imposed against the plaintiff by the defendant falls under the category of "obviously unfair" as established in Article 54.4 of the Administrative Procedure Law and should be annulled.

The plaintiff maintains that the Penalty Decision issued by the defendant lacks a basis in fact and in law, and it seriously infringes upon the legitimate rights and interests of the plaintiff. We hereby file suit with your court and request that the court find in favor of the plaintiff's litigation claims.

Sincerely,

Plaintiff: Fake Design Culture Development Ltd.

Legal representative: Lu Qing
April 13. 2012

Beijing Municipality Chaoyang District People's Court