

Legal Counsel's Brief in the Trial of First Instance

(2012) Chao Xing Chu No. 82

To the Presiding Judge, Judicial Officer, and People's Assessor:

Having been retained by the plaintiff in this case, Beijing Fake Design Culture Limited, the Shanghai Gongyuan Law Firm has assigned lawyer Hu Jiongming (hereafter "plaintiff's counsel") to serve as legal counsel in litigation regarding the matter of the administrative dispute with the defendant, the Beijing Local Taxation Bureau Second Investigation Branch.

Having examined the evidentiary materials submitted by the defendant, conducted necessary investigations, and participated in the June 20 trial hearing, plaintiff's counsel maintains that the defendant's charge of "illegality" against the plaintiff has no evidence to support it and, moreover, constitutes a serious violation of legal procedure. Therefore, the administrative penalty that the defendant has issued should be annulled in accordance with the law. However, during the trial proceedings the judicial panel violated the law by restricting the plaintiff's rights to cross-examine evidence, debate, and produce evidence in accordance with the law, all under the excuse of "the trial proceedings must obey the instructions of the court." And, with no regard for maintaining public trust in the nation's adjudication bodies, it acted in flagrant opposition to relevant legal provisions and, in the name of "internal rules of the Chaoyang District People's Court," refused to provide the plaintiff and its legal counsel with the official record of the trial and turned an open trial hearing into a closed proceeding based on documents. Judicial practice tells us that if trial procedures are unfair then it will be difficult to ensure the fairness of any substantive decision.

Plaintiff's counsel considers it an anomaly that, throughout the trial process in this case, the judicial panel has never raised a single question about the circumstances of this case in order to better comprehend the truth of the case. I thus no longer dare to hope that the judicial panel will issue a fair decision. However, based on the legal principle of "taking the facts as basis and the law as criterion" and the professional standards of conduct that lawyers ought to uphold, I still submit the following written trial brief to the judicial panel:

I. Even though the defendant made a finding and issued a penalty regarding the plaintiff's "illegalities" of tax evasion and accounting with falsified tax invoices, the specific administrative actions under dispute cited bogus data and the defendant was unable to produce corresponding evidence at trial to support its charges. The penalty decision should thus be annulled in accordance with the law on grounds of lack of supporting evidence.

1.1 The defendant's documents deliberately concealed the plaintiff's construction project expenses, thereby creating mythical project profits of up to 100%. That bogus data must be brought to light in order to distinguish fact from fiction.

At the June 20 trial hearing, the defendant submitted a "Memorandum on the Calculation Methods of Taxes, Late Fees, and Penalties for Beijing Fake Design Culture Limited" (hereafter "Memorandum") to the judicial panel. On the basis of the contents of this Memorandum and the defendant's Administrative Pleading, plaintiff's counsel has compiled the chart below confirming that the defendant found that in the period from 2002 to 2008, concealed project revenue of the plaintiff for the "Boya Garden, Three Shadows Centre, and Naga projects" was 14,943,724.36 yuan.

(See attached image.)

(Note: The Defendant calculated the total revenues from the Boya Garden, Three Shadows Centre, and Naga projects to be 14,943,724.36 yuan.)

Upon further analysis of the defendant's Memorandum, plaintiff's counsel has discovered that the defendant determined the income for the Boya Garden project to be 1,107,716 yuan but found expenses to be zero, making the profit margin 100 percent and the cost margin infinite. For the Three Shadows Centre and Naga projects, it determined income to be 14,716,008.36 yuan, with expenses of only 1,047,349.39. This means a profit of 13,668,658.97 yuan, or a gross profit margin reaching 92.88 percent. Adding the 5.5 percent sales tax, the profit would be an even higher 98.38 percent. This means a cost margin of as high as 1300 percent! Such a huge profit margin is solely the invention of the defendant, as the below chart shows.

Years	Project(s)	Project Revenues	Total Costs	Profit Margin	Cost Margin
2002-2003	Boya Garden	¥1,107,716	¥0	100%	∞
2006-2008	Three Shadows Centre, Naga	¥14,716,008.36	¥1,047,349.39	92.88%	1300%

(See attached image)

(Note: Adding 5.5 percent sales tax for the Three Shadows Centre and Naga projects yields a profit margin of 98.38 percent. However, expenses represent a mere 1.62 percent as a proportion of revenue. Such a high profit margin based on such low expenses is something unmatched in today's international or domestic commodity trading market. Even smuggling or trafficking in drugs cannot match this level of profit. No person on earth with a brain would believe these high profit figures, so how should judges with high IQs believe them?)

Only by relying on such a mistakenly high profit margin was the defendant able to find that the plaintiff evaded 4,701,885.48 yuan in enterprise income tax, adding late fees of 2,748,189.82 yuan and a penalty of 5,996,892.56 yuan for a total income tax amount due of 13,446,967.86 yuan. If 5.5 percent sales tax is added, that would be equivalent to all project revenues. What country in the world has such a high tax burden? The key question posed by plaintiff's counsel is: how was such a high profit margin arrived at?

1.2 In inspecting the plaintiff's project revenues and expenses, the defendant applied a double-standard of completely recognizing the former and completely rejecting the latter. Under the premise of concealing project expenses, the defendant directly invented a high profit margin for the plaintiff and paved the way for penalizing the plaintiff.

Plaintiff's counsel draws the judicial panel's attention to the fact that among the evidence that the defendant submitted is a "Three Shadows Centre" Construction Project Contract and a "Three Shadows Arts Centre Construction Project Statement" (hereafter, "Project Statement") in the amount of 4,920,796.81 yuan. But any project revenues must have project expenses, and the scope of construction in the "Three Shadows Centre" Construction Project Contract included: "New construction of a 2500m² two-story brick house (each story 3-8m high), with boiler room, electricity distribution room; provision of outdoor conduits for drainage, electricity and heating for the original building; construction of a reception office; waterproofing of the roof and renovation of the facade

of the old building; and construction of outdoor walkways, landscape lighting, a surrounding wall, and a surveillance system.” Even excluding water, electricity, and heating, the costs of constructing a 2500m² brick building of two stories, each 3-8m high, would involve expenses of more than 3 million yuan, and the Project Statement not only specifies the total price but also notes the unit price of materials as well.

According to Article 5 of China’s Enterprise Income Tax Law, an enterprise’s taxable income should be calculated as follows: Revenues – Direct Expenses (labor, materials, equipment costs, site management fees, etc.) – Expenses Associated with Finances and Project Management – Sales Taxes and Surcharges = Amount of Taxable Enterprise Income. The defendant should calculate the plaintiff’s taxable income amount according to the legal provisions above. However, the defendant violated these legal provisions by ignoring expenses in the Boya Garden and other two projects, calculating 1,047,349.39 yuan in costs for the “Three Shadows Centre and Naga” projects with a total price of 14,716,008.36 yuan and no costs for the Boya Garden project with a total price of 1,107,716 yuan. Therefore, plaintiff’s counsel can responsibly say that the profit margin of nearly 100 percent attributed to the Boya Garden and other two projects was “invented” by the defendant through violations of the Enterprise Income Tax Law and related regulations on accounting system and practice issued by the Ministry of Finance, as well as the use of a double-standard. The only possible purpose is to pave the way for increasing the fine. Therefore, the defendant’s administrative penalty that was based on the aforementioned data should be annulled in accordance with the law.

1.3 The defendant claims to have identified 58 falsified invoices belonging to the plaintiff. It produced a “Tax Authority Identification Report,” finding that the plaintiff engaged in illegal behavior with regard to falsified invoices, and issued a penalty. However, it is unable to provide the court with the corresponding 58 falsified invoices or the legal basis for its definition. On this point, the judicial panel should find that the specific administrative action lacks a basis in evidence.

According to Item 3 of the defendant’s evidence, Tax Authority Identification Report (hereafter “Identification Report”): “Invoices obtained by the plaintiff include falsified invoices and invoices in which the issuer and purchaser do not match, which falls under the category of illegally obtaining invoices without following the regulations. Invoices that have been obtained without following the regulations may not serve as proof of pre-tax deduction, so the amount of taxable income should be adjusted for calculation of enterprise income tax and an administrative penalty should be levied.”

The taxation authorities have the power to penalize a party that uses falsified invoices, but that same party also has the right to cross-examine the evidence of so-called falsified invoices. But as of the trial hearing on June 20, the defendant has been unable to produce the so-called 58 falsified invoices to the court. Plaintiff’s counsel wants to point out that the Identification Report is a report that was produced after screening a sample (in this case, 58 falsified invoices), and so this basis is itself a sample. This is a clear case of “if there is no skin, what does the hair stick to?” If the defendant is unable to produce the so-called 58 falsified invoices to the court and can only put forward an Identification Report, it cannot but cause one to doubt the existence of the 58 falsified invoices claimed by the defendant.

Plaintiff’s counsel maintains that in accordance with Article 32 (“The defendant shall have the burden of proof for a specific administrative act it has taken and shall provide evidence and regulatory documents on which the act has been based.”) of China’s Administrative Procedure Law and Article 1(1) (“Based on Articles 32 and 43 of the Administrative Procedure Law, the defendant shall have the burden of proof for a specific administrative action it has taken and shall provide all evidence and regulatory documents on which the act has been based within 10 days of receiving a copy of the complaint. If the defendant does not provide or delays without good reason in providing

said evidence, the specific administrative action in dispute shall be seen to lack corresponding evidence.”) of the Supreme People’s Court’s Regulations Concerning Several Issues Regarding Evidence in Administrative Litigation (hereafter “SPC Evidence Regulations”), the defendant’s inability to produce the 58 invoices upon which the Identification Report was issued by the time of the June 20 court hearing should be treated as a lack of corresponding evidence to substantiate the defendant’s administrative penalty against the plaintiff and thus its Penalty Decision should be annulled in accordance with the law.

1.4 Although the defendant has meticulously constructed the Fake Company Tax Evasion Tower, the foundation of this tower is not facts but, rather, the seemingly solid ice of the bogus high profits and the non-existent, so-called falsified invoices. And the bogus high profits were set up on a foundation of concealed project costs, so that as soon as the facts are revealed, it’s like sunshine that will quickly melt the ice and cause the Tax Evasion Tower to come crashing down.

In order to visualize the unsubstantiated nature of the defendant’s tax evasion case, plaintiff’s counsel has used data cited in the defendant’s Memorandum to compile the following chart for the reference of the judicial panel.

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(See attached image)

The above chart shows that the tax evasion case against Fake Company is just like a tower, one that has been constructed primarily from the 4,701,885.48 yuan in enterprise income tax evaded by the plaintiff, the 2,748,189.82 yuan in late fees, and the penalty of 5,996,892.56 yuan. But its foundation is located on the 92.88 to 100 percent bogus profit margins of the Boya Garden, Three Shadows Centre, and Naga projects, the 58 non-existent falsified invoices, and the project expenses that have been deliberately concealed. But as of the trial hearing on June 20, the defendant has been unable to produce the so-called 58 falsified invoices, so plaintiff’s counsel can only believe that those 58 falsified invoices do not exist. And can construction projects have such absurdly high profit margins? Plaintiff’s counsel checked out China’s leading construction company—China State Construction (stock code: 601668)—and found that its profit margin for housing construction in 2011 was only 7.6 percent. As for developers, which have a much higher profit margin than construction companies, Huayuan Property Company (stock code: 600743) only had a 29.48 percent profit margin in 2011. This is sufficient to prove that the high profit data maintained by the defendant is bogus and does not exist in the real world. According to the calculation methods used by the defendant, nearly 100 percent of state-owned and private enterprises would be found to have evaded enterprise income tax. These numbers simply do not inspire any confidence, so how can the judicial panel believe them?

In summary, plaintiff’s counsel maintains that under Articles 32 and 43 of China’s Administrative Procedure Law, the defendant has the burden of proof for a specific administrative action it has taken. Moreover, according to Article 26(2) (“The defendant shall provide all evidence and regulatory documents on which the specific administrative act has been based within 10 days of receiving a copy of the complaint. If the defendant does not provide or delays without good reason in providing said evidence, the specific administrative action in dispute shall be seen to lack corresponding evidence or basis.”) of the Supreme People’s Court’s Interpretation Concerning Several Issues Regarding Evidence in Administrative Litigation (hereafter “SPC Interpretation”), since the defendant has not provided the judicial panel with the so-called 58 falsified invoices, therefore the penalty that it issued for those invoices is unsubstantiated by evidence and should be annulled in accordance with the law. And according to Article 68(5) (“The court may directly make

findings of the following facts: . . . Facts derived from a presumption based on a rule of thumb rooted in daily life.”) of the Supreme People’s Court Regulations Concerning Several Issues Regarding Evidence in Administrative Litigation, the judicial panel should make its presumption about the likelihood of nearly 100 percent profit margins for the Boya Garden and two other projects based on a rule of thumb rooted in daily life, and it should rest its determination about whether the defendant [sic] evaded such a large amount of enterprise income tax upon the facts deriving from that presumption. If the judicial panel cannot accept profit margins in this case that far exceed those for smuggling and trafficking in drugs, then the defendant’s administrative penalty decision against the plaintiff for evasion of enterprise income tax should also be annulled in accordance with the law.

II. In trying this case, the judicial panel illegally deprived the plaintiff of its right to submit evidence and violated the principle of fairness in restricting the plaintiff’s rights to cross-examine evidence and debate. These actions must be rectified.

2.1 After receiving the plaintiff’s Application to Obtain Evidence and evidence leads, the judicial panel not only did not obtain any evidence that was not beneficial to the defendant but also illegally deprived the plaintiff of its right to produce evidence.

In the course of calculating the plaintiff’s enterprise income, the defendant only calculated project revenues and did not calculate expenses, resulting in the anomaly of enterprise income tax nearly reaching 100 percent profit margin. But because all of the plaintiff’s account ledgers were seized by the public security organ, the plaintiff has no way to produce evidence. Therefore, on June 7, 2012, the plaintiff submitted an Application to Obtain Evidence to the judicial panel and provided the panel with precise leads, requesting that the judicial panel procure in accordance with the law relevant evidence that was not beneficial to the defendant. But after receiving the application, the judicial panel did not act according to Article 25 of the SPC Evidence Rules (“The People’s Court shall examine an application of a party to procure evidence and, if it meets the conditions for procuring evidence, decide to procure the evidence right away; if it does not meet the conditions for procuring evidence, the court shall give written notice to the party or its legal counsel explaining the reason for not approving the procuring of evidence.”), neither examining the plaintiff’s application to decide whether or not to obtain the relevant evidence nor giving notice to the plaintiff explaining the reasons why the relevant evidence could not be procured.

Plaintiff’s counsel made an effort and, on the morning of June 20, went to the Three Shadows Centre to collect evidence sufficient to overturn the defendant’s specific administrative action in dispute. Prior to and during the court hearing on the afternoon of June 20, I attempted to submit the evidence three times, but was refused each time by the judicial panel on the grounds that the deadline for producing evidence had passed. Plaintiff’s counsel believes that the judicial panel’s actions are a serious violation of statutory procedure and a deprivation of the plaintiff’s right to produce evidence. The reasons are as follows:

(1) The judicial panel only informed the plaintiff’s legal representative Lu Qing orally about the deadline for producing evidence. But according to Article 1 (“After an administrative lawsuit has been examined for filing and transferred for adjudication, prior to hearing the trial the litigants should each be sent a notice of litigation . . .”) and Article 2 (“The notice of litigation should list the following: . . . [3] Scope and deadline for producing evidence for the litigants, as well as the legal consequences for providing evidence beyond the deadline. If there is a legitimate reason why a litigant cannot produce evidence by the deadline, it may apply for an extension to produce evidence.”) of the Beijing High Court’s Procedural Regulation for First-Instance Administrative Trials (hereafter “Beijing High Court Procedural Regulations”), it is a violation of the Beijing High

Court Procedural Regulations for the judicial panel to give only oral notification of the deadline for producing evidence.

(2) The defendant [sic] submitted a written Application to Obtain Evidence to the judicial panel prior to the deadline for producing evidence that was communicated orally. Though Article 25 of the SPC Evidence Regulations has no provision regarding a deadline for the court's examination of the application, the judicial panel continually set aside the plaintiff's application and provided no written or oral response.

(3) According to Article 6 of the SPC Evidence Regulations ("The plaintiff may provide evidence to prove the illegality of the specific administrative action in dispute"), the plaintiff has a right to produce evidence. After receiving the plaintiff's application to obtain evidence, the judicial panel continually avoided it. But when, through the efforts of plaintiff's counsel, on the morning of June 20 relevant evidence was obtained that is sufficient to overturn the specific administrative action in dispute, the judicial panel refused to admit it. This deprivation of the plaintiff's right to produce evidence is clearly a violation of statutory procedure and support for the defendant's mistaken penalty decision.

2.2 In order to cover up the illegality of the specific administrative action in dispute, during the trial proceedings in this case the judicial panel restricted the plaintiff's right to cross-examine the defendant's evidence on the grounds of "the trial proceedings must obey the instructions of the court." This is a violation of the legal statute providing that "evidence shall be produced in court and cross-examined at trial."

During cross-examination of the defendant's evidence in this case, the judicial panel first required the defendant to read the nearly 2,000 pages of disorganized evidence all at once and required the plaintiff to cross-examine all at once without providing the plaintiff with any catalog of evidence. The defendant was most cooperative, reading the evidence more quickly than a CCTV presenter. When the plaintiff objected that this manner of presenting evidence made it impossible to cross-examine, the judicial panel announced that "the trial proceedings must obey the instructions of the court" and said that if cross-examination could not be carried out in accordance with the judicial panel's requirements, it would be seen as abandonment of the right to cross-examine.

Under these circumstances, the plaintiff raised a challenge to the court's ruling. After nearly an hour, the judicial panel agreed to provide a catalog of evidence and changed from cross-examination of 2,000 pages of evidence all at once to cross-examination by groups (nine groups in total, each group with about 200 pages), but only five minutes would be given to cross-examine each group. The plaintiff again raised an objection, but the judicial panel again used the excuse of "the trial proceedings must obey the instructions of the court" and announced that exceeding the five-minute rule would amount to automatic abandonment of the right to cross-examine but that cross-examination opinions could be submitted in writing after the hearing.

Plaintiff's counsel maintains that the Administrative Procedure Law gives the defendant the burden of proof for a specific administrative action it has taken, but the plaintiff has the right to cross-examine the defendant's evidence to show whether or not the evidence possesses the relevance, objectivity, and legality required by law. At the same time, according to Article 35 ("Evidence shall be presented at court and cross examined during the trial. Any evidence not cross-examined during the trial may not serve as the basis for deciding the case.") of the SPC Evidence Regulations, evidence should be presented at court and cross-examined during the trial. By requiring the plaintiff to cross-examine the defendant's evidence in writing, the judicial panel both deprives the plaintiff of its right to cross-examine and violates state law. Therefore, plaintiff's counsel requests that a new hearing be held so that the relevant evidence may be cross-examined at trial.

2.3 The judicial panel's unreasonable time limits illegally deprive the plaintiff of its right to debate

The judicial panel, during the period of debate, limited each side to a mere 10 minutes of time to speak and said that written arguments could be presented in writing after the hearing. Plaintiff's counsel maintains that according to Article 9 ("Parties to administrative litigation have the right to debate.") of the Administrative Procedure Law, parties have a statutory right to debate.

This so-called debate means that each of the parties may, with the support of the court, present its own proposals and opinions regarding the facts of the case and issues of controversy and engage in a process of rebuttal and response with each other. With respect to both procedural questions and substantive issues in this case, the judicial panel should safeguard the rights of both parties to engage in debate. But the judicial panel gave both sides the right to debate in form only, using time to limit the right to debate of both sides, but mainly of the plaintiff. As a result, the plaintiff was unable to present its opinions sufficiently at court with regard to the procedural legality or evidentiary substantiation of the specific administrative action in dispute.

2.4 It was illegal for the judicial panel to go against legal statute in the name of "Chaoyang District Court internal rules" and refuse to allow lawyers to copy the Trial Record.

After the trial hearing had concluded on the evening of June 20, plaintiff's counsel requested to photocopy the Trial Record, but the judicial panel said that the person responsible for the photocopier had already left for the day and requested that the plaintiff return to the court at 2 p.m. on June 21, 2012, to photocopy. But at the appointed time, the judicial panel cited "Chaoyang District Court internal rules" as an excuse and refused to allow the plaintiff to photocopy the Trial Record.

Plaintiff's counsel maintains that trust is a basic tenet that has gradually formed during the course of human evolution and the basis for cohesion of groups or even nations—as the saying goes, "A person has no standing without trust." The judicial panel sacrificed its own public trust and even that of the Chaoyang District Court by using two different excuses to prevent the plaintiff from photocopying the Trial Record. Who now will dare to believe the Chaoyang District Court?! Moreover, according to Article 34 ("From the date a case is accepted by the People's Court, a lawyer who has been engaged to represent a party to the case has the right to consult, summarize, and reproduce all materials pertaining to the case he is undertaking.") of China's Law on Lawyers, the plaintiff has the right to reproduce the Trial Record in its case. Therefore, plaintiff's counsel requests that the judicial panel no longer use new excuses to prevent counsel from reproducing the Trial Record.

In conclusion, plaintiff's counsel maintains that the defendant, in finding that the plaintiff evaded enterprise income tax that it owed, failed to account for pre-tax deductions allowed by law or relevant labor expenses, materials costs, equipment expenses, management fees. Instead, it directly treated project revenues as the amount of taxable income and issued an administrative penalty to the plaintiff. Its action is a complete violation of the relevant provisions of the Enterprise Income Tax Law and the specific administrative action in dispute should be annulled in accordance with the law.

States establish administrative litigation systems in order to shine a light on the administrative actions of state organs so that if a state organ acts in error, a party may pursue judicial channels to seek a remedy. This is a form of oversight over the administrative power of state organs, one that allows them to perform their duties better. Therefore, the judicial system is the last defense of

fairness in society. When parties go to the courts with administrative litigation, it is in hope of trial at court during which they may fully express their demands and in hope that the court will issue a fair decision. But the prerequisite of a fair decision is procedural fairness. Without procedural fairness, there is no substantive fairness. This is the motivation behind the state's enactment of the Administrative Procedure Law and related judicial interpretations. Therefore, judicial oversight cannot be merely formalistic. To this end, even knowing it is impossible, plaintiff's counsel raises the violations of statutory procedure by the judicial panel in hopes that the judicial panel can fulfill its duties to obtain evidence and carry out a new cross-examination of the defendant's evidence in order that it may determine the truth and issue a fair decision. This legal brief is hereby submitted to the judicial panel for its full consideration.

Sincerely,

Legal counsel for Beijing Fake Design Culture Limited

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Shanghai Gongyuan Law Firm

June 26, 2012

TO: Beijing Municipality Chaoyang District People's Court