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Wei Cui

Allard School of Law at the University of British Columbia, cui@allard.ubc.ca

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DOES JUDICIAL INDEPENDENCE MATTER? A STUDY OF
THE DETERMINANTS OF ADMINISTRATIVE LITIGATION IN
AN AUTHORITARIAN REGIME

Wei Cui*

Lawsuits against the government form a part of the regular functioning of legal systems in democratic countries, and responding to such lawsuits an unavoidable part of governance. However, in the context of authoritarian regimes, administrative litigation has been viewed as a distinctively valuable institution for promoting the rule of law and individual rights. Moreover, the judiciary is portrayed as the keystone to this institution and to the rule of law in general: the more powerful and competent is the judiciary, the more it is able to “constrain government” through judicial review. Through empirical and comparative analyses of over two decades of administrative litigation in China against one of the state’s essential branches, tax collection, I challenge the utility of this normative conception of administrative litigation. Using conceptual tools that apply across legal systems and regulatory areas, I show that while litigant behavior as well the regulatory environment offer useful explanations of litigation patterns such as case volume and the plaintiff win rate, the relevance of judicial quality is barely discernible. This highlights the intuitive idea that judicial review can operate only when private parties bring suit, and whether and when they will do so cannot be taken for granted. In countries with weak legal systems, the rule of law may fail in certain basic ways that even a competent and well-subsidized judiciary cannot remedy.

Key words: administrative litigation, judicial review, rule of law, tax litigation.

TABLE OF CONTENT

* Associate Professor, Allard School of Law, University of British Columbia. Author email: cui@allard.ubc.ca. I am grateful to Eric Hou and Xiang Fangfang for excellent research assistance and to Zhiyuan Wang for assistance with statistical analysis. I have benefited from comments by Cheng Jie, He Haibo, Liu Yue, Pitman Potter, Wang Yaxin, and audiences at the Sydney Chapter of the Australian Branch of the International Fiscal Association, Northwestern University Law School, and the Canadian Law and Economics Association Annual Meeting in 2014, on earlier drafts. All errors remain my own.

INTRODUCTION2

I.BASIC FACTS: CASE VOLUME, PLAINTIFF WIN RATE, AND RATE OF
ADJUDICATION IN CHINESE TAX LITIGATION8

II.INSTITUTIONAL DETERMINANTS: EXHAUSTION OF ADMINISTRATIVE
REMEDIES AND SETTLEMENTS DURING LITIGATION 15

 A. Settlement Prior to and as a Result of Administrative
 Appeal.....15

 B. Settlement during Litigation20

III.EVIDENCE FROM A SYSTEMATIC REVIEW OF CASE LAW23

 A. The Sample23

 B. The Findings26

 1. Does tax litigation involve aberrant behavior?27

 2. Evidence of selection effects30

 3. Evidence for information asymmetry between plaintiffs
 and defendants32

 4. Legal standards and judicial bias34

 C. Summary.....40

IV.THE REGULATORY ENVIRONMENT: THE HEART OF THE STORY41

V.ADMINISTRATIVE LITIGATION AND THE RULE OF LAW47

CONCLUSION.....51

INTRODUCTION

In democracies with strong traditions of the rule of law, litigation against the government, while generating important bodies of case law for various areas of government activity, is not itself viewed as a yardstick for evaluating the performance of legal systems. In the United States, a probably widely-shared view about litigation against government agencies is expressed by Professors Theodore Eisenberg and Henry Farber: “We suspect that, on average, the federal government is less fearful of litigation than are private litigants. Government is, after all, as permanent a secular institution as we have and has been litigating for hundreds of years. Litigation to enforce laws and defend against attacks on laws and government policies is part of its routine. Government is so large relative to most other litigants that it, more than the average litigant, knows substantial litigation will be a part of its existence.”¹ In other words, the occurrence of litigation to resolve disputes between the government and citizens is an epiphenomenal consequence of the

¹ Theodore Eisenberg & Henry S. Farber, *Government as Litigant: Further Tests of the Case Selection Model*, 5 AM. L. & ECON. REV. 94, 109 (2003).

general functioning of the legal system and the (wide) scope of government activities. One need not think of it as a distinct institution with a distinct purpose in itself.² In countries with civil law traditions, a special judicial branch is often created to adjudicate lawsuits against the government: a special recognition for disputes between the government and private parties can thus be said to be institutionalized, somewhat in contrast with the U.S. and other common law countries.³ The existence of an administrative law branch of the judiciary, however, is not itself regarded as differentiating countries characterized by the rule of law from those that are not.

In countries subject to authoritarian rule, by contrast, lawsuits against government agencies can assume a special symbolic status: they may be seen as providing rare instances of institutionalized constraint on the exercise of authoritarian power.⁴ Well-justified

² Correspondingly it need not constitute a distinct subject of study. Thus in numerous quantitative studies of U.S. litigant behavior, lawsuits with government defendants are simply included as one type of litigation among many others. See Peter Siegelman & John J. Donohue III, *The Selection of Employment Discrimination Disputes for Litigation: Using Business Cycle Effects to Test the Priest-Klein Hypothesis*, 24 J. LEGAL STUD. 427 (1995); Peter Siegelman & Joel Waldfogel, *Toward a Taxonomy of Disputes: New Evidence through the Prism of the Priest/Klein Model*, 28 J. LEGAL. STUD. 101 (1999); Daniel Kessler et al., *Explaining Deviations from the Fifty- Percent Rule: A Multimodal Approach to the Selection of Cases for Litigation*, 25 J. LEGAL STUD. 233 (1996). In the large empirical literature studying judicial attitudes, lawsuits against government agencies offer particularly germane material for the examination of the ideological leanings of judges (e.g. whether they are pro- or anti-government). For a review, see FRANK B. CROSS, *DECISION MAKING IN THE U.S. COURTS OF APPEALS* (2007). But the fact that these lawsuits are brought to courts in the first place are taken for granted.

³ See, generally, ZAIM M. NEDJATI & J.E. TRICE, *ENGLISH AND CONTINENTAL SYSTEMS OF ADMINISTRATIVE LAW* 35 (1979); Dominique Custos, *Independent Administrative authorities in France: Structural and Procedural Change at the Intersection of Americanization, Europeanization and Gallicization*, in *COMPARATIVE ADMINISTRATIVE LAW* 278 (Susan Rose-Ackerman & Peter L. Lindseth ed., 2010); Katharine Thompson & Brian Jones, *Administrative Law in the United Kingdom*, in *ADMINISTRATIVE LAW OF THE EUROPEAN UNION: ITS MEMBER STATES AND THE UNITED STATES* 177 (3d ed., René Seerden ed., 2012).

⁴ See, e.g. Kevin J. O'Brien & Lianjiang Li, *Suing the Local State: Administrative Litigation in Rural China*, 51 CHINA J. 75, 90-91 (2004); Tom Ginsburg, *Administrative Law and the Judicial Control of Agents in Authoritarian Regimes*, in *RULE BY LAW: THE POLITICS OF COURTS IN AUTHORITARIAN REGIMES* (Tom Ginsburg & Tamir Moustafa ed., 2008) (accessible at <http://ssrn.com/abstract=2006538>, all page citations below to this chapter are by reference to the SSRN version).

antipathy towards oppressive regimes that frequently trample rule of law norms has led legal professionals, scholars, the media and citizens in general to applaud lawsuits against the government (frequently labeled as “administrative litigation”) as a good thing in itself.⁵ Administrative litigation is thus strongly promoted by those who aspire to limit the power of bad government, especially when few other mechanisms of such constraint are available.⁶ Conversely, administration litigation has also been conceived as a distinct device with which the principals in an authoritarian regime can monitor their agents.⁷ Once such positive valence, or at least distinct institutional purpose, is attached to administrative litigation, it also becomes instinctive to view the quantity of such litigation as well as litigation outcomes as meaningful indicators of how well the institution is serving its purpose. In particular, lower-than-expected case volume and plaintiff win rates against the government are taken to reflect judicial weakness vis-a-vis the executive branch.

As natural as such reasoning may seem, it faces some serious theoretical and methodological difficulties. To begin, there is no generally accepted theory predicting the quantity of litigation in a given jurisdiction, i.e. explaining why some countries are more “litigious than others”.⁸ Consequently, it can be difficult to justify the implicit benchmarks used in making judgments such as that the volume of litigation or the rate of plaintiff wins in a country is “too low”. In addition, with respect to the plaintiff win rates, the most compelling existing theory posits that the key determinant of such rates is the rate of settlement among litigants, which is itself determined by the abilities of litigants to predict judicial outcomes,

⁵ O’Brien and Li, *supra* note 4, at 103 (administrative litigation is a form of “rightful resistance”, which is “a form of popular contention that operates near the boundary of authorized channels, employs the rhetoric and commitments of the powerful to curb the exercise of power, hinges on locating and exploiting divisions within the state, and relies on mobilizing support from the wider public”).

⁶ *Id.* (administrative litigation has led many “to reconsider their relationship to authority, while posing new questions, encouraging innovative tactics, and spurring thoughts about political change.”)

⁷ Ginsburg, *supra* note 4.

⁸ For recent discussions, see Theodore Eisenberg et al., *Litigation as a Measure of Well-Being* (Cornell Law Faculty Working Papers No. 99/Apr. 8, 2012), available at http://scholarship.law.cornell.edu/clsofs_papers/99; Mark Ramseyer & Eric B. Rasmusen, *Are Americans More Litigious? Some Quantitative Evidence*, in *THE AMERICAN ILLNESS* 66 (Frank Buckley ed., 2013).

the cost of litigation, and the stakes the parties have in the disputes.⁹ Plaintiff win rates, in other words, by themselves do little to answer questions about whether the judiciary tends to side with the government, or whether the legal standard in a given area of dispute is otherwise too favorable to the government.

This Article explores these challenges facing the interpretation of the outcomes of administrative litigation in authoritarian regimes through an in-depth case study. I focus on one country, China, and litigation in one fundamental area of government activity, taxation. Because of its authoritarian government and weak rule of law,¹⁰ administrative litigation in China has long been held as an emblem of instruments for constraining government. Ever since the 1980s, both Chinese and foreign scholars have resorted to the study of administrative litigation as a way of assessing the development of China's legal system.¹¹ Various authors have also held forth putative evidence of low case volumes and low plaintiff win rates as confirming the lack of independence on the part of the Chinese

⁹ George L. Priest & Benjamin Klein, *The Selection of Disputes for Litigation*, 13 J. LEGAL STUD. 1 (1984); Joel Waldfogel, *The Selection Hypothesis and the Relationship Between Trial and Plaintiff Victory*, 103 J. POL. ECON. 229 (1995); Joel Waldfogel, *The Selection of Cases for Trial*, in 3 THE NEW PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW 419 (Peter Newman ed., 1998); Keith N. Hylton & Haizhen Lin, *Trial Selection Theory and Evidence: A Review*, in 8 ENCYCLOPEDIA OF LAW AND ECONOMICS 487 (2d ed., Chris Sanchirico ed., 2012).

¹⁰ PITMAN POTTER, CHINA'S LEGAL SYSTEM 192-93 (2013); Benjamin J. Liebman, *China's Courts: Restricted Reform*, 191 CHINA Q. 620 (2007); RANDALL PEERENBOOM, CHINA'S LONG MARCH TOWARDS RULE OF LAW 247, 513 (2002); Stanley Lubman, *Bird in a Cage: Chinese Law Reform after Twenty Years*, 20 NW. J. INTL L. & BUS. 383, 385, 408 (2000); KEVIN J. O'BRIEN, REFORM WITHOUT LIBERALIZATION: CHINA'S NATIONAL PEOPLE'S CONGRESS AND THE POLITICS OF INSTITUTIONAL CHANGE 13, 20 (2008).

¹¹ See, e.g., Pitman Potter, *The Administrative Litigation Law of the PRC: Judicial Review and Bureaucratic Reform*, in DOMESTIC LAW REFORMS IN POST-MAO CHINA (Pitman Potter ed., 1994); Minxin Pei, *Citizens v. Mandarins: Administrative Litigation in China*, 152 CHINA Q. 832 (1997); David Weller, *The Bureaucratic Heavy Hand in China: Legal Means for Foreign Investors to Challenge Agency Action*, 98 COLUM. L. REV. 1238 (1998); O'Brien & Li, *supra* note 4; Donald Clarke et al., *The Role of Law in China's Economic Development*, in CHINA'S GREAT ECONOMIC TRANSFORMATION 375 (Thomas Rawski & Loren Brandt ed., 2008); Ji Li, *Suing the Leviathan – An Empirical Analysis of the Changing Rate of Administrative Litigation in China*, 10 J. EMPIRICAL LEGAL STUD. 815; Margaret Y.K. Woo, *Law and Discretion in Contemporary Chinese Courts*, in THE LIMITS OF THE RULE OF LAW IN CHINA 163, 174, 183, 190 (Karen G. Turner et al. ed., 2000); Lubman, *id.*, at 392.

judiciary.¹² While Chinese tax litigation has generally attracted little attention to date, when instances of such litigation are reported in the media, they are also quickly portrayed as responding to oppressive government actions (and reflecting Chinese courts' general inability to constrain such actions).¹³ Overall, both popular and academic discussions of Chinese administrative litigation display a high degree of consensus with respect to two claims. First, both the volume and outcome of administrative litigation are chiefly functions of the distribution of powers between the Chinese judiciary and the executive branch—in short, of judicial independence.¹⁴ Second, administrative litigation is a good thing in itself, and judicial institutions should be reformed to deliver a greater amount of that good.

By examining empirical information relating to Chinese tax litigation spanning over two decades, I come to conclusions that challenge this consensus. I present four sets of findings, obtained from applying different devices of empirical and comparative analysis. First, certain instinctive judgments in reaction to seemingly

¹² Xin He & Yang Su, *Do the "Haves" Come Out Ahead in Shanghai Courts*, 10 J. EMPIRICAL LEGAL STUD. 120 (2013); Ji Li, *Dare You Sue the Tax Collectors? An Empirical Study of Tax-Related Administrative Lawsuits in China*, 23 PAC. RIM L. & POLY J. 57 (2014); He Haibo (何海波), *Kundun de Xingzheng Susong (困顿的行政诉讼) [The wearied state of administrative litigation]*, 2012 HUADONG ZHENGFA DAXUE XUEBAO (华东政法大学学报) [JOURNAL OF THE EAST CHINA UNIVERSITY OF POLITICAL SCIENCE AND LAW] no. 2.

¹³ See James Fallows, *More on the Detained Chinese Lawyer*, THE ATLANTIC (Aug. 1, 2009), available at <http://www.theatlantic.com/technology/archive/2009/08/more-on-the-detained-chinese-lawyer/22546>; Evan Osnos, *Where is Xu Zhiyong?* THE NEW YORKER (Jul. 31, 2009), available at <http://www.newyorker.com/news/evan-osnos/where-is-xu-zhiyong>; Ben Blanchard & Yoko Nishikawa, *China demands Ai Weiwei pay \$1.85 million in taxes, fines*, REUTERS (Jun. 28, 2011, 8:29 AM), available at <http://www.reuters.com/article/2011/06/28/us-china-artist-idUSTRE75L3U520110628>; Andrew Jacobs, *Chinese Artist Is Barred From His Own Hearing*, THE NEW YORK TIMES (Jun. 20, 2012), http://www.nytimes.com/2012/06/21/world/asia/supporters-take-up-chinese-artist-ai-weiwei-s-cause-at-court.html?_r=3&ref=world; Sui-Lee Wee, *Chinese Court Upholds Fine Against Dissident Ai Weiwei*, REUTERS (Sep. 27, 2012, 10:21 AM), available at <http://www.reuters.com/article/2012/09/27/us-china-dissident-idUSBRE88P0J720120927>.

¹⁴ Ginsburg, *supra* note 4, at 24 (“the administrative litigation scheme can become an effective arena of political contestation. However, the regime may also seek to tighten control over the courts to inhibit them from becoming a major locus of social and political change.”)

low case volume and plaintiff win rates in Chinese tax litigation are hard to justify, in light of available cross-country comparative information.¹⁵ Second, I situate Chinese tax litigation in the context of a multi-year, multi-agency study of what disputes against the government are brought to Chinese courts and result in judicial decisions.¹⁶ Cross-agency comparisons furnish credible evidence that Chinese plaintiffs tend to encounter particularly adverse outcomes in litigating against tax agencies; but this may be the result of both information asymmetry between plaintiffs and defendants and adverse legal standards based on statutes, and need not indicate judicial bias favoring tax agency defendants. Third, I assembled the largest set of published Chinese judicial decisions in tax cases to date,¹⁷ and systematically analyzed the content of the decisions.¹⁸ I argue, based on such a comprehensive review, that the available evidence is consistent with the view that the Chinese judiciary is (and has been for some time) able to adjudicate tax disputes with competence and reasonable neutrality.¹⁹ Fourth and finally, a

¹⁵ This argument is informed by comparative tax dispute resolution information generated by both scholarly studies and a variety of professional sources. For scholarly studies in the U.S., see, e.g. Leandra Lederman, *Which Cases Go to Trial?: An Empirical Study of Predictors of Failure to Settle*, 49 CASE W. RES. L. REV. 315 (1999); Leandra Lederman & Warren B. Hrungr, *Do Attorneys Do Their Clients Justice? An Empirical Study of Lawyers' Effects on Tax Court Litigation Outcomes*, 41 WAKE FOREST LAW REV. 1235 (2006); in Canada, see Benjamin Alarie & Andrew Green, *Policy Preferences and Expertise in Canadian Tax Adjudication*, 62 CANADIAN TAX J. 985 (2014); in Japan, see J. Mark Ramseyer & Eric B. Rasmusen, *Why the Japanese Taxpayer Always Loses*, 72 S. CAL. L. REV. 571 (1999); in Israel, David Gliksberg, *Does the Law Matter? Win Rates and Law Reforms*, 11 J. EMPIRICAL LEGAL STUD. 378 (2014). Additional scholarly and professional sources are cited in Part I infra.

¹⁶ The details of the study are set out in Wei Cui & Zhiyuan Wang, *The Selection of Disputes against Government Agencies: Evidence from a Civil Law System* (paper presented at the 2015 Annual Meeting of the Italian Law and Economics Association; on file with the author).

¹⁷ The case sample size is, to my knowledge, the largest among existing studies in English that analyze Chinese administrative litigation decisions, whether generally or within specific regulatory areas.

¹⁸ Mark A. Hall & Ronald F. Wright, *Systematic Content Analysis of Judicial Opinions*, 96 CAL. L. REV. 63 (2008). All decisions in the sample were coded intensively, using a score sheet of over 30 questions. The content analysis performed captures a large number of features of the decisions, providing a rich set of information about the substantive and procedural aspects of the cases.

¹⁹ The details of this study are fully reported in Cui Wei (崔威), *Zhongguo Shuiwu Xingzheng Susong Shizheng Yanjiu* (中国税务行政诉讼实证研究) [An

separate study of Chinese tax administration, which forms the essential background of dispute resolution on tax matters, was carried out.²⁰ That study suggests that the low level of tax litigation in China can well be explained by the organization of Chinese tax administration, which permits a high frequency of informal interactions among taxpayers and tax collectors. This explanation implies, however, that the volume of litigation may remain low regardless of improvements in the Chinese judiciary.

Collectively, these findings imply that inferences about the power of the judiciary vis-à-vis the executive branch on the basis of litigation volume and judicial outcomes are highly unreliable, because these observable patterns are determined primarily by other factors. This conclusion would not itself be very remarkable if reached in the context of a developed legal system. In the U.S., for example, the dominant approach to analyzing civil litigation patterns is to assume that they are driven by litigants' rational choice.²¹ However, scholars have succumbed to the temptation to depart from this approach when engaging with the legal system in authoritarian countries. I argue that portraying administrative litigation as a self-standing institution imbued with a distinct purpose (i.e. offering opportunities for plaintiffs and courts to constrain otherwise unconstrained government)²² has limited benefits, particularly given its risk of generating spurious explanations.

The Article proceeds as follows. Part I provides background information regarding patterns of Chinese tax litigation and discusses how these patterns are inadequately explained by prevailing views of Chinese administrative litigation. Part II first considers the procedural features of Chinese tax litigation that may explain some of the litigation patterns. It then presents evidence of a correlation between the settlement rate during litigation and plaintiff win rate,

Empirical Study of Tax Litigation in China], 2015 QINGHUA FAXUE (清华法学) [TSINGHUA UNIVERSITY LAW JOURNAL] no.3, 135.

²⁰ For a preliminary exposition, see Wei Cui, *Administrative Decentralization and Tax Compliance: A Transactional Cost Perspective*, 65 U. TORONTO L.J. 186 (2015).

²¹ See especially the sources cited in note 9 *supra*. See also STEVEN SHAVELL, *FOUNDATIONS OF ECONOMIC ANALYSIS OF LAW PART IV* (2004); Kathleen Spier, *Litigation*, in 1 *HANDBOOK OF LAW AND ECONOMICS* 259 (A. Mitchell Polinsky & Steven Shavell ed., 2007).

²² See Ginsburg *supra* note 4, at 24 (“administrative litigation...will tend to constrain the government, even if...regime opponents are [often] not successful in their particular lawsuits.”)

which suggests that the “trial selection theory” of disputes widely applied in studying litigation outcomes in the U.S. may also apply to China. According to this theory, non-independent (or incompetent) courts are only one among several equally plausible explanations of plaintiffs’ poor odds in tax litigation. Part III then investigates the strength of evidence for attributing taxpayer’s poor chances to an underperforming judiciary. I describe select findings based on the extensive content analysis of case law, and argue that neither qualitative nor quantitative evidence supports the hypothesis of judicial non-independence. Statutory biases and information asymmetries between litigants are at least equally good explanations of low plaintiff win rates. Part IV then explains how the main cause of low tax litigation volume may lie in the structure of Chinese tax administration. Part V reviews the implications of these findings for the discourse associating administrative litigation with the promotion of the rule of law. A brief Conclusion follows.

I. BASIC FACTS: CASE VOLUME, PLAINTIFF WIN RATE, AND RATE OF ADJUDICATION IN CHINESE TAX LITIGATION

Interest in tax litigation has grown among Chinese tax and legal professionals in the last few years.²³ As a result of Chinese courts’ recent extraordinary practice of publishing all decisions that are not politically sensitive,²⁴ a massive amount of case law of all varieties has come to the public light in the last few years, and tax litigation is no exception. Chinese tax practitioners are discussing case law much more so than they ever did previously, and tax advisors are beginning to advise clients to consider the litigation option where they have not before.²⁵

²³ The first administrative law case that China’s Supreme People’s Court (SPC) has tried after a much-anticipated revision of the Administrative Litigation Law in 2014 was a lawsuit against the local tax bureau. Luo Shuzhen (罗书臻), *Zuigao Renmin Fayuan Gongkai Kaiting Shenli Xin Xiugai Xingzheng Susong Fa Shishi Hou Diyi Qi Xingzheng Anjian* (最高人民法院公开开庭审理新修改行政诉讼法实施后第一起行政案件) [*The first Administrative Litigation Case tried in a public hearing at the Supreme People’s Court after the implementation of the newly amended Administrative Litigation Law*], RENMIN FAYUAN BAO (人民法院报) [PEOPLE’S COURT DAILY], Jun. 30, 2015, at 1.

²⁴ See notes 76-82 *infra* and accompanying text.

²⁵ For the prior reluctance of foreign investors to challenge the actions of Chinese tax agencies, see Wei Cui, *Foreign Administrative Law and International*

However, lest one hastens to the conclusion that this growing interest is attributable to a rising wave of tax litigation, some sobering statistics should be considered. According to data published by China's Supreme People's Court (SPC),²⁶ the quantity of first-instance tax litigation in China experienced a significant decline since the late 1990s: close to 2000 cases a year were brought at the beginning of this period; the number declined to around 1000 a year by 2004, and to around 300 by 2007; they have stayed around 400 a year more recently (see Chart 1). SPC data indicates that the ratio of tax litigation to the total volume of (first instance) administrative litigation in China also declined from 2.4% in 2000 to 0.3% in 2013. While tax disputes became rarer during this period, administrative litigation as a whole grew.



Thus in both absolute and relative terms, the volume of Chinese tax litigation may seem low in some intuitive ways. The absolute number of cases a year (around 400) seems low relative to China's population and the size of its economy. The U.S. Tax Court alone sees around 30,000 cases docketed a year.²⁷ India, a country with

Taxation: a Case Study of Tax Treaty Implementation in China, 64 ADMIN. L. REV. 191 (2012).

²⁶ For a discussion of the nature of the SPC data, see Cui and Wang, *supra* note 16. Since the late 1980s the data has appeared in the annual China Law Yearbook (中国法律年鉴). Unless otherwise indicated, all data regarding the quantity of administrative litigation and manners in which such cases are disposed provided in this Article comes from this source.

²⁷ HAROLD DUBROFF & BRENT J. HELLWIG, *THE UNITED STATES TAX COURT: AN HISTORICAL ANALYSIS* (2014). Unlike the U.S. and a small number of other countries, China has no specialized tax courts. (Given the small quantity of

comparable population size to China, also sees over 20,000 first instance tax cases a year.²⁸ China's tax litigation volume is more comparable to Japan's, which legal scholars have treated as a low-litigation jurisdiction.²⁹

However, these crude comparative figures need to be viewed with caution: since comparative tax litigation data is not generally available, it is difficult to know which countries constitute the norm and which countries the outliers. Even the U.S.' and India's tax litigation volumes are dwarfed by the number of tax cases in Italy³⁰ and Brazil.³¹ Thus perhaps a more persuasive assessment would refer to the fact that the Chinese tax bureaucracy employs more than 10% of China's civil servants, and tax administration clearly touches on the everyday operation of every Chinese business.³² Given the size of the tax branch of the Chinese administrative state, even the 2.4% of tax cases in 2000 relative to the total volume of litigation against the government seems disproportionately low, not to mention the 0.3% found in recent years.³³

tax litigation each year, creating such a court would be hard to justify.) Tax cases, along with other types of administrative litigation, are tried by administrative law tribunals that can be found in most courts at various levels across the country.

²⁸ PRICEWATERHOUSECOOPERS, *NAVIGATING TAX CONTROVERSY IN INDIA* 15 (2005).

²⁹ Ramseyer & Rasmusen, *supra* note 15, reports that there were 189 and 154 cases of tax litigation (including appeals) in Japan in 1989 and 1994, respectively. See also Akihiro Hironaka, et al., *Japan, in TAX DISPUTES AND LITIGATION REVIEW* 162, 164 (2d ed., Simon Whitehead ed., 2014) (294 tax lawsuits were reported in 2013 in Japan). It is worth noting, however, that in recent years the Canadian Tax Court has received on average only 600 cases a year, even though Canada does not have a reputation for being a "low litigation" jurisdiction. Alarie & Green, *supra* note 15, at 996.

³⁰ 247,911 tax cases decided by and 510,236 tax cases pending at the Court of First Instance in 2013, See Roma Giugno, *Appendici Statistiche E Guida Alla Relazione Sul monitoraggio Dello Stato Del Contenzioso Tributario e Sull'Attività Delle Commissioni Tributarie* 45 (2014), available at <http://www.piscino.it/file/bilancio/ctr-06-1.pdf>.

³¹ See Lourdes Garcia-Navarro & Paula Moura, *Brazil: The Land of Many Lawyers And Very Slow Justice*, NATIONAL PUBLIC RADIO (Nov. 05, 2014, 2:15 PM), available at <http://www.npr.org/sections/parallels/2014/11/05/359830235/brazil-the-land-of-many-lawyers-and-very-slow-justice> (1,660,000 cases in progress in the court that deals with tax avoidance in the city of Sao Paulo alone).

³² Cui, *supra* note 20, at 225.

³³ Figures given by Ramseyer & Rasmusen, *supra* note 15, suggest that tax litigation comprises between 20% and one third of all civil lawsuits against the government in Japan.

Equally striking, of course, is the decline in tax litigation in the last 10 years. There are different hypotheses that would explain this decline, none of which can at the present be confirmed. One is that Chinese tax administration practice has possibly improved in terms of greater conformity to rule of law norms.³⁴ Changing administration practices may also be relevant. It has been reported that tax agencies have in recent years adopted more “collaborative” forms of tax collection and applied penalties less frequently.³⁵ Tax disputes may be predicted to decrease as a result.³⁶ Another hypothesis for explaining the decline of tax litigation, with a different thrust, is that the revision in 2000 of the Law on the Administration of Tax Collection,³⁷ the general procedural statute for tax administration, significantly expanded the powers of tax agencies, legitimized certain agency practices that had previously been controversial, and otherwise made it more difficult for lawsuits against tax agencies to be brought.³⁸ Yet another hypothesis is that it was the high volume of tax litigation in the late 1990s that was abnormal, attributable possibly to the rapid changes in the organization of tax administration in China during that time.³⁹ The

³⁴ The Chinese police also saw a substantial decline in both the absolute and relative quantities of lawsuits brought against it (a drop of 1/3 and over 80%, respectively) in the same period, and some Chinese scholars have been willing to attribute this to improved policing practice. He, *supra* note 12, at 88.

³⁵ Whether an agency adopts a collaborative or adversarial approach to regulation arguably has no direct implications for the assessment of the agency under rule of law norms. For a discussion of Chinese tax agencies’ experiments in recent years with more collaborative approaches to tax collection, see Qian Junwen (钱俊文) & Wei Guoqing (韦国庆), *Nashui Pinggu de Hefa Xing Zhengyi Jijue* (纳税评估的合法性争议及其解决) [*The controversy of legal status of tax assessment and its solution*], 2013 SHUIWU YANJIU (税务研究) [TAXATION RESEARCH] no. 1, 72. For analysis of the adoption of such collaborative forms in other Chinese regulatory agencies, see, e.g. Carlos Wing-Hung Lo et al., *Changes in Regulatory Enforcement Styles among Environmental Enforcement Officials in China*, 41 ENVIRON. PLAN. A 2706 (2009).

³⁶ Note that accepting this explanation can affect one’s view of what level of litigation is “too low:” one should be less inclined to view the current level of tax litigation as abnormally low, if its decline from a previously more “normal-looking” level has a ready explanation.

³⁷ *Zhonghua Renmin Gonghe Guo Shuishou Zhengshou Guanli Fa* (中华人民共和国税收征收管理法) [Law on the Administration of Tax Collection] (promulgated by the Standing Comm. Nat’l People’s Cong., Sep. 4, 1992, effective as amended May 1, 2001) [hereinafter referred to as “LATC”].

³⁸ See notes 134-136 *infra*.

³⁹ See Cui, *supra* note 20, at 201.

steady, lower level of tax litigation in recent years merely represents a reversion to the mean. Because of the lack of information about Chinese tax litigation in the 1990s,⁴⁰ it is difficult to confirm or disconfirm any of these hypotheses. Note, though, none of these hypotheses refers to the quality of Chinese courts at all.

Fluctuations in litigation levels are unique neither to tax agencies nor to China. In countries enjoying high levels of rule of law, both the level at any given time and fluctuations over time in administrative litigation volumes simply remain esoteric facts: they are rarely noticed and even more rarely highlighted as demanding explanation.⁴¹ However, when administrative litigation is held to symbolize mechanisms of constraining authoritarian power, its volume becomes imbued with significance. Moreover, instead of offering hypotheses like the ones just described, scholars of Chinese law who find the level of administrative litigation lower than they expect often take such low case volume to impugn the court system.⁴² Such commentary displays two implicit assumptions: first, the actions or inactions of courts are the primary determinants of observed litigation patterns; second, since administrative litigation is a good thing, a lower-than-expected level of such litigation indicates under-performance or even malfunction of the courts.⁴³ Yet at least in the tax context, these assumptions fit uncomfortably with the data. If they were held onto, declining litigation volume would imply that Chinese judiciary became less independent vis-à-vis tax agencies over time, and/or that tax agencies became more powerful relative to

⁴⁰ See note 88 *infra*.

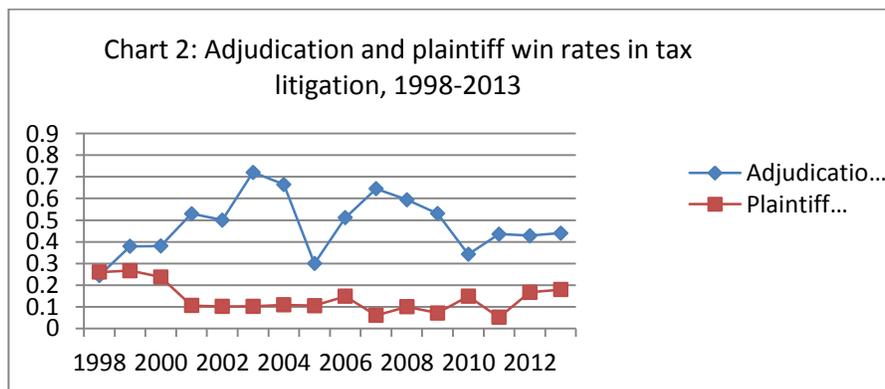
⁴¹ In U.S. tax scholarship, I am aware of only instance of such attention. See Yehonatan Givati, *Resolving Legal Uncertainty: The Unfulfilled Promise of Advance Tax Rulings*, 29 VA. L. REV. 137, 146 (2009) (noting a greater than 50% drop of tax cases filed in the U.S. between 1996 and 2000 and complete recovery in the years afterwards, and stating that such fluctuation “calls for further research”).

⁴² See, e.g. He, *supra* note 12, at 88 (suggesting that the low level of tax litigation also signals a failure of the public remedy system); Rachel E. Stern, *The Political Logic of China's New Environmental Courts*, 72 CHINA J. 53 (2014) (noting an inadequate quantity of environmental litigation and suggesting that courts must do more to increase such quantity). A recent study argued that the level of tax litigation confirms a “shared understanding [among commentators on Chinese law] that local courts do not normally adjudicate administrative lawsuits against government agencies impartially and judicial bias is presumably more serious when powerful agencies, such as tax bureaus, are sued.” Li, *supra* note 12 at 58 (footnotes omitted).

⁴³ Li, *supra* note 11, at 840.

other agencies over time. But there is no independent reason to embrace or even consider such claims.

Another implicit assumption of previous commentary on Chinese administrative litigation is that plaintiff win rates serve as a specific mechanism through which the actions of Chinese courts may affect litigation volume. More specifically, plaintiff win rates reflect judicial attitudes, and low plaintiff win rates, reflecting judicial bias in favor of government defendants, could deter litigation.⁴⁴ What do we know about plaintiff win rates in tax litigation? The SPC also offers information about the ways in which tax cases are disposed, which can be classified into plaintiff wins and losses. Using this information, I calculate two rates, the “plaintiff win rate” and the “adjudication rate”, for each year. Chart 2 maps the evolution of both the plaintiff win rate and the adjudication rate for tax litigation over the course of 16 years. It can be seen that the adjudication rate has largely followed an inverse-U-shaped development (with a blip in 2005-6), going from a low of 24.4% in 1998 to a high of 67.5% in 2004 and back to 32.1% in 2010. Plaintiff win rates went from a high point of 26% in 1998 down to 9.5% in 2001 and back to 16.7% in 2012. Thus in the late 1990s, when more lawsuits were brought against tax agencies, both the rate of withdrawal of lawsuits and the rate of plaintiff wins were also higher.



Are Chinese taxpayer plaintiffs’ odds of winning too low, and could this be why few lawsuits are brought? Cross-country comparative information again offers no support for these assessments. Plaintiff win rates in U.S. tax and district courts have

⁴⁴ He & Su, *supra* note 12, at 139; Li, *supra* note 12.

been reported to range from 15%⁴⁵ to 29%,⁴⁶ which are not much higher than China's.⁴⁷ While higher plaintiff win rates have been reported for other countries, those countries do not always have higher (per capita) litigation volumes.⁴⁸ Although such comparative information is quite limited, it still warns us that, with no further theory, we should have little confidence that judicial biases and judicial capacity offer even *relevant* explanations of case volume and observed litigation outcome, let alone the most important ones.

The next Part will examine a number of features of Chinese dispute resolution institutions that *are* clearly relevant to understanding case volume and litigation outcome. Each of these features is shared by Chinese institutions with those of many other countries, although some combination of features may be more unique. One such feature is the availability of administrative remedies: in China as in many other countries, the appeal of the action of a government agency within the executive branch before a dispute is brought to courts is either a requirement or a right that is commonly exercised. This may systematically reduce litigation volume, and also indirectly affect observed plaintiff win rates. Similarly, any cost to the pursuit of formal dispute resolution—such as the requirement Chinese taxpayers face to pay the disputed tax liability before bringing even an appeal within the executive branch—could also suppress litigation volume and affect that outcome of cases that are brought to courts. More generally, the costs of dispute resolution may lead to settlements at different points after a dispute arises, conditional upon the litigants' respective

⁴⁵ Daniel M. Schneider, *Using the Social Background Model to Explain Who Wins Federal Appellate Tax Decisions: Do Less Traditional Judges Favor the Taxpayer?* 25 VA. TAX REV. 201, 224 (2005) (calculation based on 1292 randomly sampled tax cases in the Federal circuit courts between 1996 and 2000).

⁴⁶ Daniel M. Schneider, *Assessing and Predicting Who Wins Federal Tax Trial Decisions*, 37 WAKE FOREST L. REV. 473, 519 (2002) (a study of 482 randomly sampled cases for the Tax Court and from District Courts during the 1979-1998 period).

⁴⁷ One professional article reports that taxpayers in Germany also win only 20% of the first instance cases. See Michael Hendricks, *Germany*, in TAX DISPUTES AND LITIGATION REVIEW 101, 102 (2d ed., Simon Whitehead ed., 2014).

⁴⁸ Alarie & Green, for example, report a close-to-50% taxpayer win rate in the Canadian Tax Court, but the volume of tax litigation is low in Canada compared to the U.S. and to other countries with lower reported win rates (e.g. Italy). See notes 15 and 30, *supra*, for litigation volume in Canada and Italy. Italy's taxpayer's win rate was between 30% and 40% in 2013. See ROMA GIUGNO, *supra* note 30.

expectations and degrees of uncertainty. Litigants' rational choices in light of these costs and subject to these information constraints could easily reduce or eliminate the effect of judicial bias (or capacity) on observed litigation outcome.⁴⁹ It is only by taking these institutional factors into account—as urged by some of the most influential contemporary theories about legal systems—that one can begin to make inferences from litigation patterns.

II. INSTITUTIONAL DETERMINANTS: EXHAUSTION OF ADMINISTRATIVE REMEDIES AND SETTLEMENTS DURING LITIGATION

A. Settlement Prior to and as a Result of Administrative Appeal

The option to pursue administrative appeals prior to litigation is an important feature distinguishing administrative litigation from other types of civil litigation. It implies the existence of an institutionalized procedure for resolving disputes between private parties and the government, before the disputes reach courts. Just as settlements during litigation reduce the number of cases tried by judges, appeals within the executive branch reduce the number of cases docketed with courts in the first place. While negotiations prior to potential plaintiffs' decisions to bring suit also lead to settlements and reduce the number of cases docketed in other types of civil disputes, administrative appeal, as a public institution, often requires the government to record the quantity of disputes between it and private parties and the manners in which they are resolved pre-litigation. This type of pre-litigation settlement, therefore, may be more observable than in other areas.

In China, the administrative remedy that is available to citizens as an alternative to, or an option prior to, seeking judicial remedies is called administrative reconsideration (AR).⁵⁰ For tax disputes, AR possesses special significance, because in all disputes regarding the

⁴⁹ Law and economic analysis of the outcomes of civil litigation in the United States generally demonstrate—or assume—the elimination of such effects of judicial biases. See Hylton & Lin, *supra* note 9; SHAVELL, *supra* note 21.

⁵⁰ Zhonghua Renmin Gongheguo Xingzheng Fuyi Fa (中华人民共和国行政复议法) [Administrative Reconsideration Law] (promulgated by the Nat'l People's Cong., Apr. 29, 1999, effective Oct. 1, 1999) (Lawinfochina) (China); see also Zhonghua Renmin Gongheguo Xingzheng Fuyi Fa Shishi Tiaoli (中华人民共和国行政复议法实施条例) [Regulation on the Implementation of the Administrative Reconsideration Law] (promulgated by the St. Council, May 29, 2007, effective Aug. 1, 2007) (Lawinfochina) (China).

assessments of deficient tax payments, AR is a remedy that must be exhausted before judicial review is available.⁵¹ But not all disputes with tax agencies go through AR first. For disputes regarding the imposition of a civil penalty, an enforcement action or a seizure to secure tax payment, the taxpayer may choose either to apply for AR or directly to bring a complaint to court. Actually litigated cases thus involve a mixture of disputes that have gone through the AR process and those that have not. Previous studies based on limited case samples suggest that tax cases litigated that are preceded by AR represent over 35% of all tax lawsuits.⁵² This is higher than the proportion of litigation preceded by AR in the overall population of administrative litigation, which has been estimated to be around 20%.⁵³ The difference reflects the fact that, unlike the United States, where the exhaustion of administrative remedies is a general administrative law doctrine broadly applicable across most agencies,⁵⁴ the requirement is imposed in China only on less than a handful of agencies and subject areas other than tax agencies and the assessment of tax deficiencies.

Could this fact be relevant to understanding why the volume of tax litigation is distinctly low relative to total administrative litigation? Suppose two agencies, A and B, face the same amount of potential disputes, but disputes against A can go to court directly while disputes against B must go through AR first. If AR is able to resolve many disputes, the number of lawsuits against B should be much lower than the number of lawsuits against A.

Unfortunately, this factor explains fairly little. In a previous study, I calculate that among tax disputes that are brought to AR, around 14% go on to be litigated.⁵⁵ This implies that only about

⁵¹ LATC, *supra* note 37, art. 88. Shuiwu Xingzheng Fuyi Guize (税务行政复议规则) [Rules for Tax Administration Reconsideration] (promulgated by the St. Admin. of Tax'n, Feb. 10, 2010, effective Apr. 1, 2010) (Lawinfochina) (China) (defining procedures of administrative appeals against all tax agencies).

⁵² See Cui, *supra* note 19, at 141; Huang Qihui (黄启辉), *Xingzheng Susong Yishen Shenpan Zhuangkuang Yanjiu* (行政诉讼一审审判状况研究) [A Study of First Instance Adjudication of Administrative Lawsuits], 4 QINGHUA FAXUE (清华法学) [TSINGHUA UNIVERSITY LAW JOURNAL] 73 (2013), at 80.

⁵³ See Xin He, *Administrative Reconsideration's Erosion of Administrative Litigation in China*, 2 CHINA J COMP LAW 1, 10 (2014).

⁵⁴ See generally, 2 RICHARD J. PIERCE, JR., ADMINISTRATIVE LAW TREATIES (5TH ED., 2015) (Chapter 15 Exhaustion, Finality, and Ripeness).

⁵⁵ This computation is based on knowledge of the ratio of the total number of ARs brought against tax agencies to the total number of lawsuits brought against

1,000 AR procedures a year are pursued by Chinese taxpayers,⁵⁶ which seems a miniscule number in light of the sheer size of Chinese tax administration and the prominence taxation holds for most businesses. To understand low case load in courts, therefore, one must understand why taxpayers do not tend to seek administrative review of tax agencies' assessments of deficiencies to begin with.

For those who are inclined to explain litigation outcomes in terms of features of judicial institutions, one explanation may come to mind. Perhaps Chinese taxpayers believe that anyone in the executive branch reviewing a tax agency action during an AR proceeding is likely to be biased in favor of the government.⁵⁷ If they also believe that courts tend to rule in favor of tax agencies, then they may not initiate any AR proceeding at all: the pursuit of dispute resolution would be futile. Therefore, (perceived) judicial bias could indirectly reduce the volume of AR (and, mechanically, the volume of tax litigation). However, this explanation implies that those who do end up initiating AR proceedings should be prepared to litigate, since the complainant is unlikely to acquire new information about the biases of courts in the AR proceeding itself. But this is not the case. While an estimated 14% of tax AR cases continue to litigation, a far higher proportion of complainants receive unfavorable determinations at the end of AR proceedings.⁵⁸ Such a high rate of

the same tax agencies; the information is available only for a part of China's tax bureaucracy and only for a few years. The estimate is consistent with the result of a government study in 2007. See Cui, *supra* note 19. Note that this percentage itself is not too different from the U.S. Lederman, *supra* note 15, at 329, note 62, reports that IRS "settles approximately 90% of the cases it considers".

⁵⁶ Currently no reliable statistic is independently available concerning the total number of AR proceedings against tax agencies. The number must therefore be inferred. If one assumes that 35% of litigated tax cases have gone through AR, and that these represent just 14% of all tax AR proceedings, then at 400 litigated cases a year, there are about 1,000 AR tax procedures.

⁵⁷ Such a belief would be well-justified, given that the rate of affirmation of agency actions during AR proceedings in general has consistently been greater than 50% He, *supra* note 53, at 8. No information is currently available regarding the breakdown of types of dispositions for tax AR proceedings specifically.

⁵⁸ A 2007 government report claimed that complainants in tax AR proceedings were able to obtain a favorable ruling or a settlement 62% of the time—which would be markedly higher than the outcome for AR proceedings in general. See Lin Hong (蔺红), *Guojia Shuiwu Zongju Fahui Fuyi Zhineng Cujin Zhengce Wanshan* (国家税务总局发挥复议职能促进政策完善) [*The State Administration of Taxation Used Administrative Reconsideration to Improve Tax Policymaking*], *ZHONGGUO SHUIWU BAO* (中国税务报) [CHINA TAXATION NEWS],

attrition at the end of AR proceedings would be inexplicable if complainants made decisions to pursue AR after already having taken into account possible judicial bias.

What else, then, might explain the low volume of tax AR proceedings? Notably, when a taxpayer is required to apply for AR before bringing a lawsuit (e.g. in all disputes regarding deficiency assessments), it must also first remit the tax amount as determined by the tax authority, or provide corresponding guaranty, as a condition for opening an AR proceeding.⁵⁹ Such a requirement is not totally exceptional in comparative perspective,⁶⁰ but it does seem to erect a barrier to the pursuit of a dispute. It could do so in two ways. First, if the tax paid is later ruled to be over-assessed, but no interest is paid on the over-collected amount, the payoff to litigation is reduced, since the tax refunded in the future is worth less now given the foregone interest. This may induce settlement.⁶¹ However, such an effect is significant only if the expected duration of litigation is long, the rate of foregone interest is high, or the amount in dispute is very large.⁶² Second and more significantly, it is possible that the defendant's negotiation position generally changes after an AR is brought: the government is easier to negotiate with before a formal dispute is instigated, but toughens its position once a dispute is

Feb. 5, 2007, at 2. Yet even this high number implies 38% of complainants receiving unfavorable rulings.

⁵⁹ LATC, *supra* note 37, art. 88. In disputes where AR is not a precondition for seeking judicial remedies, such prior payment (e.g., of the penalty) also is not required. *Id.*

⁶⁰ The OECD reports a large number of countries authorizing the collection of disputed tax during both AR and judicial review, although tax agencies in some country may refrain from exercising such authority while a dispute is pending. OECD, *TAX ADMINISTRATION 2013: COMPARATIVE INFORMATION ON OECD AND OTHER ADVANCED AND EMERGING ECONOMIES* 324-325, 345-347 (2013). Some countries (including Japan and the UK) explicitly impose a requirement to pay assessed deficiencies before disputing an assessment in court. *Id.* Other countries require the provision of a guaranty for the tax amount disputed. See Aurora Ribes, *Spain*, in *COURTS AND TAX TREATY LAW* 333, 336 (Guglielmo Maisto ed., 2007).

⁶¹ Under current Chinese law, there is no clear provision requiring the government to compensate for interest on tax refunded after AR or litigation.

⁶² My review of the sample of published tax cases discussed in Part III indicates that the average duration for a dispute to be decided by a first instance court is less than two years. While the opportunity cost of funds for average taxpayers or the cost of financing (for cash constrained taxpayers) is a more complex matter, it should be noted that the interest cost of owing tax is also high: Chinese tax law provides for an interest rate of over 18% per annum for overdue tax amounts. LATC, *supra* note 37, art. 32.

governed by formal legal procedures.⁶³ This may happen, for example, if the government's negotiating position after entering into a formal dispute is based closely on law and estimates of the likelihood of prevailing during AR and litigation, whereas before entering a formal dispute, it is influenced more by ongoing interactions with the taxpayer and considerations of revenue targets, or is more open to the discretion of particular revenue agents.

This second possibility, however, implies that even if there is no requirement to pay tax before bringing an AR complaint against a tax agency, taxpayers may prefer to reach settlements instead of going into AR. In other words, the incremental cost of paying tax first before pursuing formal dispute resolution may not exert a significant independent effect. In any case, existing AR statistics does not offer evidence that the requirement to pay tax as a precondition for AR induces more pre-AR settlement.⁶⁴ If there is greater pre-AR settlement in tax, it should follow that the rate of settlement during a tax AR proceeding should be lower than AR proceedings in general: the tax cases that can be settled are more likely to have already been settled. However, this appears not to be the case. Previous authors suggest that between 16% and 18% of all AR cases continue to litigation.⁶⁵ These percentages are actually higher, or at least not very different from, the estimated figure of 14% for tax AR cases that

⁶³ One can imagine the tax agency's position toughening once an AR proceeding opens, and toughening even further once a lawsuit is launched.

⁶⁴ In the U.S., Tax Court cases represent 95% of all first-instance tax cases brought to federal courts. This has been explained by reference to the fact that for a dispute with an IRS tax assessment to be accepted by the Federal Court of Claims or a District Court, the tax assessed has first to be paid (thus these latter courts only accept lawsuits for refunds of tax paid). Leandra Lederman, *What Do Courts Have To Do With It? The Judiciary's Role in Making Federal Tax Law*, 65 NATL. TAX J. 899 (2012). However, there the observed effect of the requirement to pay tax before bringing a dispute is on the choice between alternative venues, not on whether to bring a dispute at all. Moreover, other aspects of Tax Court practice, such as the availability of informal procedures, the commonality of pro se cases, may all make the U.S. Tax Court a more attractive choice to most taxpayers. See generally, *Id.* Lederman also mentions the fact that IRS notices of deficiency only inform taxpayers of the option to challenge the notice in the Tax Court, and not of other choices. *Id.*

⁶⁵ He, *supra* note 53, at 9, 12 (providing an estimate of 19% for 2009, and citing an earlier study that estimate an average of 16-17%). These percentages still reflect a relatively high rate of attrition from dispute resolution, even after receiving unfavorable AR determinations. *Id.*, at n7.

continue to litigation. Taxpayer complainants drop out of dispute resolution no less frequently than other complainants.⁶⁶

In summary, while pre-litigation procedures for tax disputes are distinctive relative to other areas of disputes with Chinese government agencies, they do not seem to explain the low volume of tax litigation. Moreover, the limited information available regarding taxpayers' use of these procedures seems to reject the relevance of judicial quality: the quality of the Chinese judiciary appears unlikely to be a primary or even significant factor explaining observed low case volume.⁶⁷

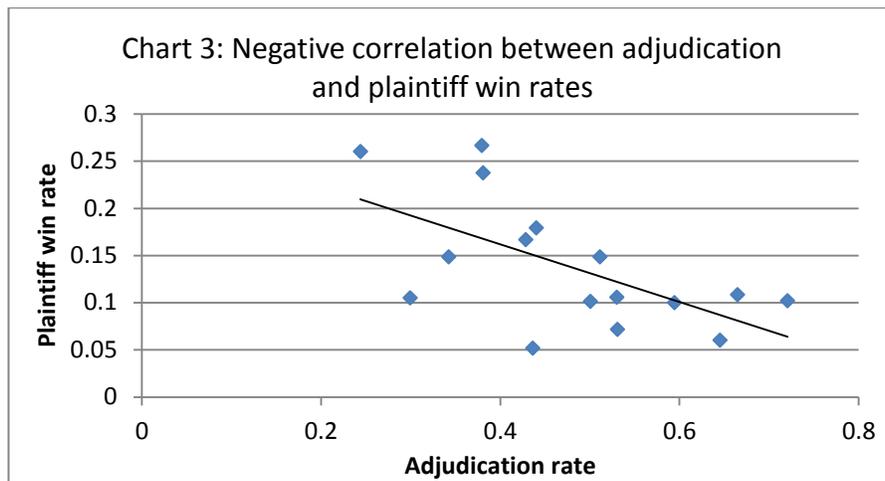
B. Settlement during Litigation

One might expect judicial quality to matter more once disputes are brought to courts. However, it turns out that an important determinant of plaintiff win rate in Chinese tax litigation is the rate of withdrawal from litigation before courts issue their decisions. Using the same data as Chart 2, Chart 3 illustrates a negative correlation between the rates of adjudication (which is basically the complement of the rate of withdrawal) and the plaintiff win rates observed over 16 years. This correlation implies that, in any given year, the more disputes reached the stages where courts issued decisions (i.e. the less often the plaintiffs settled with tax agencies or otherwise dropped their lawsuits), the less likely plaintiffs are to win in court.⁶⁸

⁶⁶ Moreover, limited information on settlement before a decision is issued at the end of an AR proceeding suggests that this type of settlement does not occur less frequently in tax than in other areas. See Cui, *supra* note 19, at 142, for more detailed discussion.

⁶⁷ However, pre-litigation procedures may well have effects on other observed litigation patterns. For example, the disputes not resolved during the AR process and subsequently brought to courts may settle less frequently during litigation than cases that are directly brought to courts. One can expect this substitutive effect between earlier and later settlements because the disputes that are more amenable to settlement are likely to have been settled earlier. The lower settlement rates for lawsuits preceded by AR also implies that disputes preceded by AR may be over-represented in published court verdicts relative to its proportion in all lawsuits, since only cases that are not settled receive judicial verdicts. See note 108 *infra* and accompanying text.

⁶⁸ More advanced statistical analysis confirms the significance of the correlation observed in Chart 3. See Cui & Wang, *supra* note 16.



This finding is important in several ways. First, it implies that the cases that are decided by courts do not form a random and representative sample of all disputes that are litigated. If decided cases were such a sample, the rate of plaintiff win should remain roughly the same regardless of what proportion of disputes is adjudicated; but this is clearly not the case. Thus, as low as Chinese taxpayers' chances of winning in court seem from decided cases (see Chart 2 *supra*), their frequency of winning would be even lower if more cases were adjudicated. Second, a statistically significant correlation between the rates of adjudication and plaintiff wins, when observed in the U.S. context, is generally taken by existing scholarship to be strong evidence for the “trial selection theory” of civil litigation.⁶⁹ According to this theory, rational litigants go to trial when the difference in their expected values of the payoff from litigation is greater than the aggregate cost of litigation for both parties.⁷⁰ When the differences in expected value of litigation are smaller than the collective cost of litigation, the parties can achieve a mutually beneficial outcome by settling the dispute instead. This rational choice model of litigant behavior also predicts that, all other things equal, plaintiffs are less likely to win where defendants (i) have greater stakes in litigation than plaintiffs, and/or (ii) have

⁶⁹ See Hylton & Lin, *supra* note 9, for a recent review of this body of theory, which was pioneered by Priest & Klein, *supra* note 9.

⁷⁰ Differences in expectations arise from different estimations of the probability of plaintiff prevailing, due to uncertainty and asymmetrical information.

significant private information about the matter in dispute.⁷¹ In other words, insofar as the trial selection theory is applicable to a particular context,⁷² it tells us that litigation outcomes should be traced as much to the choices of litigants as to the behavior of judges.

Using a sophisticated analytical tool like the trial selection theory indeed allows one to make a number of refined judgments about Chinese tax litigation patterns. For example, a cross-agency comparison shows that the plaintiff win rate in tax disputes tends to be lower than the majority of other agencies.⁷³ The trial selection theory typically explains such patterns by reference to several factors. For example, different degrees of information asymmetry among litigants may be relevant. Any information advantage of the defendant is predicted by the selection theory to generate lower plaintiff win rates (holding other things equal). In comparing litigation outcomes against different Chinese government agencies, it can indeed be seen that in tax and certain other areas of regulation (such as policing, public health, environmental protection, and family planning), the plaintiff win rates are lower. One explanation, consistent with the selection theory, is that these agencies' primary roles are to enforce the law. They may thus be much more familiar with the details of the law to be enforced and how the law is generally applied than the subjects of enforcement. This amounts to a form of information asymmetry between plaintiff and defendants. By contrast, a number of other agencies that lose more often as defendants (such as land management and urban planning bureaus) face plaintiffs that are real estate developers, or who bring class action suits. These are precisely types of plaintiffs who suffer less from information disadvantages.

Another relevant factor is differences in statutory standards. It is conceivable that the Chinese government has written the law in such

⁷¹ When both the stakes and information are symmetrical between plaintiffs and defendants, then as legal uncertainty goes down and the cost of litigation goes up, the adjudication rate tends towards zero, and the plaintiff win rate, famously, tends to 50%. Priese & Klein, *supra* note 9.

⁷² The novelty of finding evidence for the trial selection theory in the Chinese context lies in the fact that very few legal scholars have so far explored whether that theory holds in civil law jurisdictions. For further discussion, see Cui & Wang, *supra* note 16.

⁷³ *Id.* Taxpayer plaintiffs seem to fare considerably better when suing certain other types of government entities, including township governments, land management bureaus, urban planning bureaus, and agricultural bureaus, although they tend to fare equally bad or even worse when suing family planning agencies and public health bureaus.

a way as to give greater power to its most coercive branches, such as taxation, family planning, and public security. In this case, holding all other things equal, plaintiffs should be less likely to win. By contrast, it seems very unlikely that the distribution of power of the judiciary relative to different government departments can explain the variation in plaintiff win rates. There is no reason to have even thought that family planning agencies are more powerful vis-à-vis the judiciary than township governments, or that public health officials are more powerful than those managing land use and issuing building permits. Other factors, unrelated to judicial quality, must be at play.

As with the discussion of factors that may explain the decline of the volume of tax litigation in Part I, establishing the relevance of these factors empirically requires good data. In the next Part, I will summarize the findings from a unique collection of tax disputes that bear on these questions of information asymmetry and legal standards. In addition, having noted that judicial quality is unlikely to explain variations of plaintiffs' chances when litigating against different agencies, I will also examine whether there is evidence for judicial bias in published tax case law.

III. EVIDENCE FROM A SYSTEMATIC REVIEW OF CASE LAW

Parts I and II analyzed aggregate data on Chinese tax litigation. To evaluate the determinants of administrative litigation patterns, and specifically to assess how the quality of judicial institutions may affect both litigation outcome and whether private parties decide to bring suit in the first place, it is of course helpful to study the disputes themselves. This Part will discuss some findings from analyses of the most comprehensive collection of judicial decisions resulting from tax litigation in China.⁷⁴

A. The Sample

Because China has a civil law system in which most decided cases have no precedential value,⁷⁵ for a long time there were no institutional mechanisms or rationales for Chinese courts to publish their decisions systematically. Consequently, the publication of

⁷⁴ For a fuller exposition, see Cui, *supra* note 19.

⁷⁵ See DANIEL C.K. CHOW, *THE LEGAL SYSTEM OF THE PEOPLE'S REPUBLIC OF CHINA IN A NUTSHELL* (2015).

judicial decisions on administrative lawsuits was both highly haphazard and highly selective.⁷⁶ However, case publication practices of Chinese courts went through a radical transformation in recent years. In 2009, China's Supreme People's Court urged all courts to promote judicial transparency by placing cases online.⁷⁷ Simultaneously with this announcement (and in some places even before), several jurisdictions, including the province of Henan and the City of Shanghai, began to release a large amount of judicial verdicts on the internet.⁷⁸ At the end of 2013, the SPC launched its own website publishing judicial decisions rendered by courts across China,⁷⁹ while issuing guidelines regarding what types of decisions should be made public.⁸⁰ Since then, an extraordinary amount of judicial decisions has become accessible. Although restrictions are placed on the publication of several categories of decisions, administrative litigation is not one of them.⁸¹ Existing examinations

⁷⁶ Some decisions were published in textbooks for judge training, or otherwise as results of one-time efforts by judges, scholars, or others interested in administrative litigation to depict judicial practice. The cases that became publicly accessible in this manner were probably unrepresentative due to editor bias.

⁷⁷ Zuigao Renmin Fayuan Yingfa Guanyu Sifa Gongkai de Liuxiang Guiding he Guanyu Renmin Fayuan Jieshou Xinwen Meiti Yulun Jiandu De Ruogan Guiding de Tongzhi (最高人民法院印发《关于司法公开的六项规定》和《关于人民法院接受新闻媒体舆论监督的若干规定》的通知) [Supreme People's Court's Notice on the Publication of Six Measures on Judicial Openness and Certain Provisions on People's Court Accepting News Media Supervision] (promulgated by the Sup. People's Ct., Dec. 8, 2009).

⁷⁸ For a discussion of such initiatives in Henan, see Benjamin Liebman, *Leniency in Chinese Criminal Law? Everyday Justice in Henan* 6-13 (Columbia Public Law Research Paper No. 14-406/Aug. 7, 2014), available at <http://ssrn.com/abstract=2491889>. By early 2014 more than 600,000 cases has been posted online in Henan. *Id.*, at 8. For a discussion of similar initiatives in Shanghai, see He & Su, *supra* note 12, at 126. More than 100,000 decisions had been made available in Shanghai by 2009. Note that these numbers pertain to all varieties of judicial verdicts allowed to be published and not just administrative litigation.

⁷⁹ See ZHONGGUO CAIPAN WENSHU WANG (中国裁判文书网) [JUDICIAL OPINIONS OF CHINA], available at <http://www.court.gov.cn/zgcpwsw/>.

⁸⁰ Zuigao Renmin Fayuan Guanyu Renmin Fayuan Zai Hulanwang Gongbu Caipan Wenshu de Guiding (最高人民法院关于人民法院在互联网公布裁判文书的规定) [Provisions of the Supreme People's Court on the Issuance of Judgments on the Internet by the People's Courts], ZHONGGUO FAYUAN WANG (中国法院网) [CHINA COURT WEB] (Nov. 12, 2013).

⁸¹ See Liebman, *supra* note 78, at 7-8, 65.

of recent court case publication practices suggest that the scope of publication in non-restricted areas is reasonably comprehensive.⁸²

The sample of tax cases discussed below was made possible by this recent change in publication practice.⁸³ The sample includes 233 original or edited court documents published between 1987 and 2012, some of which combine first-instance and second-instance (regular appeals) decisions. Because Chinese appellate decisions tend to excerpt first-instance decisions extensively, close to 400 court judgments are reflected in the sample.⁸⁴ The number of verdicts per year in the sample increased over time—not, we know, because the volume of tax litigation increased,⁸⁵ but only because of better publication practice of courts. Similarly, the geographical distribution of the sample is uneven.⁸⁶ The sample thus shares the geographical bias displayed by other recent scholarly attempts to analyze large quantities of Chinese case law.⁸⁷ On the other hand, for 2010, the decisions included in the sample comprise over 20% of all tax decisions rendered in China in that year. This relatively high rate of publication—remarkable for a civil law country where published decisions do not yet fulfill any legal function—was also observed in 2011 and 2012.⁸⁸

⁸² See Liebman, *supra* note 78, at 10-11; He & Su, *supra* note 12, at 127-8.

⁸³ However, case gathering ended in May 2013. The sample thus does not include tax cases that have come to the public light after that time.

⁸⁴ The 233 documents we collected map onto 190 lawsuits, with the latter individuated by reference to whether the same set of parties and facts was involved. For several factors we examine in coding the cases, it is not the number of decisions, but the number of lawsuits, that are relevant.

⁸⁵ See Chart 1 in Part I *supra*.

⁸⁶ The city of Shanghai and the province of Henan contribute almost half of the documents, while all but 3 of the other 28 provinces each contributed fewer than 10. However, the predominance of Henan and Shanghai cases in the sample holds only for the years 2009-2011, and has waned by 2012. It is also worth noting that there is presently no information about the geographical distribution of tax litigation across China, so how unrepresentative the sample is in this regard remains unknown.

⁸⁷ See Liebman, *supra* note 78; He & Su, *supra* note 12.

⁸⁸ For details, see Cui, *supra* note 19, at 144-5. By contrast, published decisions collected for earlier years represented between only 0.6% and 2.7% of actually rendered decisions. Thus for the year 2000, which witnessed the largest number of concluded tax cases (2025), only 17 decisions were found.

Existing content analyses of Chinese judicial opinions have drawn on samples from particular courts and particular years.⁸⁹ More detrimentally, studies of administrative litigation in particular have used samples that are truly small.⁹⁰ While geographical bias is still present in the sample of tax cases used here, I tried to expand the sample's coverage both geographically and over time. The longer time horizon of the sample especially permits the discovery of litigation patterns that take years to unfold.⁹¹ Finally, given the discussion in the last Part, we know that even if all or most court judgments are published, they are likely to be unrepresentative of all disputes brought to courts, because many lawsuits settle before they result in judicial verdicts. In interpreting the findings from the sample, therefore, I strive to take the biases that are predicted by trial selection theory into account.⁹²

B. The Findings

Judges have no reason to reveal their lack of independence (if that is indeed the case) in their written decisions. Conversely, even if judicial verdicts frequently end up in favor of government defendants,

⁸⁹ See, e.g., He & Su, *supra* note 12 (all cases in Shanghai courts for the years 2004-9), Liebman, *supra* note 78 (all criminal cases in one year from two courts in Henan).

⁹⁰ See, e.g. Li, *supra* note 12, at 79 (41 decisions corresponding to 19 tax disputes in one province between 2009 and 2011); Xuehua Zhang & Leonard Ortolano, *Judicial Review of Environmental Administrative Decisions: Has it Changed the Behavior of Government Agencies?* 64 CHINA J. 97, 102 (2010) (14 cases from two counties).

⁹¹ See text accompanying notes 130-133 *infra*. In the sample, the most common types of actions of tax agencies challenged in courts are assessments of deficiencies, penalties, and compulsory measures in collection or tax preservation. But challenges against a wide variety of other agency actions, such as state compensation, denial of administrative reconsideration, government inaction (e.g. failure to reward whistleblowers), government information disclosures, are also included.

⁹² I calibrate the sample in several ways. First, one recent empirical study of Chinese administrative litigation is based on a large sample of cases (not restricted to tax) directly gathered from courts, including withdrawn cases and unpublished cases. See Huang, *supra* note 52. It is thus free from publication bias, and I make use of relevant results from that study. Second, I find the proportion of two main types of defendants in tax litigation, state tax bureaus and local tax bureaus, to be roughly consistent between our sample and what is known about the underlying dispute population. Third, the types of taxes involved in the sample disputes are also consistent with the tax structure in China. For details, see Cui, *supra* note 19.

this may simply be the result of the facts of the cases and applicable law, and not of judicial attitudes. Therefore, evidence from published cases on whether judicial attitudes or judicial quality determine outcome can only be indirect. In the following, I discuss four groups of relevant evidence. First, a previous study claimed that because Chinese courts can be assumed to lack independence in tax adjudication and because potential plaintiffs fear retaliation from tax agencies, actually observed cases of tax litigation tend to involve exceptional circumstances. The prevalence of such exceptional circumstances could thus constitute indirect evidence for judicial bias. Therefore, I examine the frequency of such circumstances. Second, the trial selection theory discussed earlier suggests that litigants' rational choices with respect to settlement can mask judicial attitudes. Therefore I consider the strength of selection effects in the sample, focusing on determinants of plaintiff wins. Third, findings relating to whether there exists information asymmetry between plaintiffs and defendants in tax litigation are discussed. Fourth and finally, I discuss what residual evidence there is both for the location of legal standards in tax disputes, and for the relationship between the judiciary and tax administration.

1. Does tax litigation involve aberrant behavior?

In a previous study of tax litigation in China, Professor Ji Li asserted that it is common knowledge that Chinese courts would generally favor defendants in tax disputes, and that anyone suing tax collectors would likely face "retaliation".⁹³ Therefore, he argues, it is hardly surprising that few Chinese taxpayers "dare sue" the tax collector; what is surprising is why *anyone* would sue.⁹⁴ Professor Li postulates several types of reasons. One is that some plaintiffs are "retaliation-proof": the defendant may have limited jurisdiction over the plaintiff and therefore cannot effectively retaliate; or the plaintiff literally has "nothing to lose" (the favored example is tax whistleblowers who are unemployed social gadflies).⁹⁵ Another is that the plaintiff is politically well-connected, which forces the adjudicating court to act neutrally.⁹⁶ Yet a third reason is that "high

⁹³ Li, *supra* note 12 at 69.

⁹⁴ *Id.*, at 72.

⁹⁵ *Id.*, at 80-6.

⁹⁶ *Id.* at 99-103. Professor Li simply assumes that otherwise courts need not be neutral.

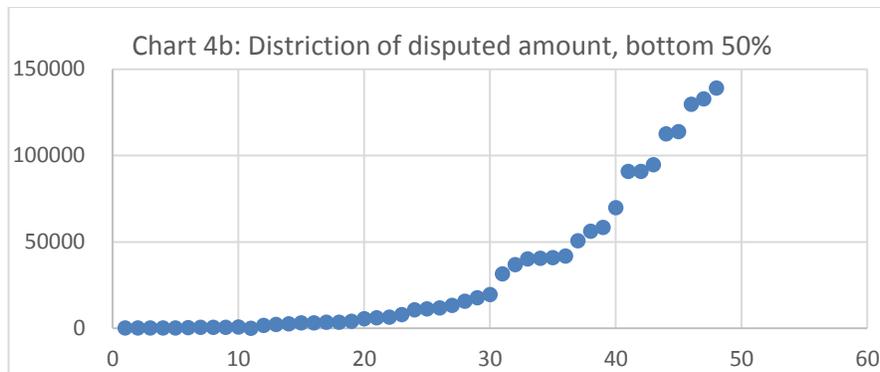
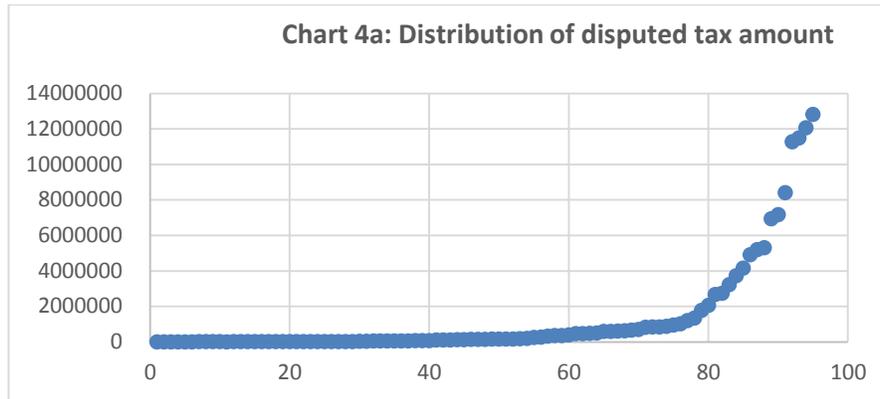
stakes” are involved and other channels of conflict resolution are closed.⁹⁷ Professor Li’s argument appears to be that unless one of these factors is present, litigating against Chinese tax collectors would be “irrational”.⁹⁸

I investigated these claims in several ways. The first is *the monetary amount in dispute*. In half of the cases in our sample, the amounts of tax payment in dispute (not including penalties) are given. The smallest such amount is 30 Chinese Yuan (CNY)—approximately 5 US dollars, while the largest amount is 12,806,105 CNY. The mean amount disputed is 1,314,541 CNY and median 138,976 CNY. The following two charts illustrate the distribution of disputed amounts. The first chart, covering the entire sample, shows that the top two deciles of cases involve disputes over RMB 2 million or more, which are substantial amounts by any standards. The second chart shows that within the bottom half of distribution of cases in terms of amount, there is still a significant spread, and once the 3rd decile is passed, the disputes amounts are already above RMB 20,000. Thus, at least judging by the published decisions, many Chinese taxpayers sue tax agencies because non-trivial sums are at stake, and not because of antagonisms unrelated to the economic value of a dispute.⁹⁹ The distribution of amount disputed is also continuous up to the top decile, with no evidence of disputes bunching at the low end (due to those plaintiffs who “have nothing to lose”) and at the high end (due to those plaintiffs with “high stakes”).

⁹⁷ Id. at 86-103. It is not clear why this explanation of the occurrence of many lawsuits would not apply generally to all legal systems, and why it explains the special pattern of litigation in China.

⁹⁸ Id. at 75. Professor Li claims to find at least one such factor in each of the 19 cases he studies.

⁹⁹ The preponderance of disputes involving small amounts at the bottom half of the distribution is also consistent with experiences in other countries. See, e.g. DUBROFF & HELLWIG, *supra* note 27, at 5034, reports that “small cases” consistently represented around 50% of all cases in the U.S. Tax Court in recent years. Small tax cases in the U.S. tax court are cases involving less than \$50,000 a year. Lederman, *supra* note 64, at 901. In Canada, more than half of Tax Court cases were brought using the informal procedure, which is available only when the amount of federal tax and penalties in dispute is \$25,000 or less. Alarie & Green, *supra* note 15, at 995-6.



Thus the majority of the cases do not involve plaintiffs “with low incomes and revenues [who] are relatively immune to the agencies' retaliation threats.”¹⁰⁰ In theory, cases with larger amounts in dispute may be more likely to go to trial,¹⁰¹ and thus the sample of published cases may not be representative of the underlying population.¹⁰² Therefore I also specifically reviewed for evidence that the plaintiff has low income or low levels of wealth, and found this to be the case only in 5 out of 190 cases.

I also tested Professor Li’s claim that potential plaintiffs in China would not sue the agencies that routinely regulate them, for fear of retaliation, and therefore that many actual lawsuits involve

¹⁰⁰ Li, *supra* note 12 at 75. Such plaintiffs presumably would not be suing for such large amounts

¹⁰¹ In the model of Priest and Klein, *supra* note 9, taking trial and settlements costs as constant, the larger the amount in dispute, the more likely that a given difference in the estimated probability of outcomes by the plaintiff and defendant will result in a sufficiently large divergence in the expected values of judgments.

¹⁰² Note that Professor Li also drew his evidence from a small number of published cases.

taxpayers and tax agencies that dealt on a one-time basis. I specifically attempted to determine whether the defendant in a case has regular jurisdiction over the plaintiff taxpayer. In the 135 cases in which it is possible to make this determination, the defendant *is* the regular tax administrator over the plaintiff in 100 cases. Thus it is overwhelmingly disputes involving locals that are adjudicated. The idea that only the “out-of-towner”, so to speak, sues the tax collector (along with local social misfits) finds no support in the sample. This appears to be a robust result since parties that deal on a routine basis should have more incentives to stay out of court or to settle during litigation. Therefore the various stages of trial selection—for the commencement of a lawsuit and for getting to a verdict—should screen out many disputes among locals and ensure that they are under-represented, instead of over-represented, in decided cases.

Finally, close to 60% of the cases in the sample studied involve individual plaintiffs. This percentage likely understates the proportion of individuals bringing suit, since individuals are more likely to withdraw a lawsuit (i.e. settle with the defendant) than other types of plaintiffs.¹⁰³ Among the plaintiffs that are entities, 72% are non-state-owned, private firms. While some individual and private firm plaintiffs may be politically well-connected,¹⁰⁴ claiming that plaintiffs would not sue tax collectors *but for* being politically well-connected seems far-fetched. Overall, political connections and plaintiff “retaliation-proofness” offer at best marginal explanations of why tax litigation happens in China.

2. Evidence of selection effects

¹⁰³ Huang, *supra* note 52, at 81. In Huang’s sample (which covers 2,767 administrative litigation cases, though only 28 of which were tax litigation) 79.5% of plaintiffs were individuals. *Id.*, at 77. The under-representation of individuals in published decisions was also a feature of the case sample analyzed in Pei, *supra* note 11.

¹⁰⁴ Some studies have suggested that politically well-connected Chinese firms are more likely to go to court in general (not just for purposes of suing government agencies). Yuen Yuen Ang & Nan Jia, *Perverse Complementarity: Political Connections and the Use of Courts among Chinese Private Firms*, 76 J. POLIT. 318 (2014). Note, however, that this may be little different from patterns observed in other countries. See B. Zorina Khan, “*To Have and Have Not*”: *Are Rich Litigious Plaintiffs Favored in Court?* (NBER Working Paper No. 20945/Feb. 2015), available at <http://www.nber.org/papers/w20945> (studying civil litigation in Maine from the Colonial period through to the Civil War, and showing that wealthier individuals engaged in litigation more).

According to trial selection theory, rational litigants will take any information regarding judicial bias into account when deciding whether to go to trial. If both the plaintiff and the defendant expect the deciding judge to be biased against the plaintiff, they will settle instead of going to trial (thus saving the cost of litigation). Consequently, the judge's bias may not end up being reflected in decided cases; any judicial bias can be observed in published decisions only where such filtering through litigants' choices fails to be effective.¹⁰⁵ Although, for reasons discussed below,¹⁰⁶ it is presently not possible to implement any quantitative measure of judicial bias for Chinese administrative litigation, it makes sense to consider whether the selection effect of litigant choices is strong enough in tax litigation that any such bias would be masked anyway.¹⁰⁷

I find some evidence for the selection effect in the case sample. As argued in Part II.A. *supra*, lawsuits preceded by administrative appeal (AR) are less likely to settle during litigation. This implies that disputes preceded by AR may be over-represented in published court verdicts relative to its proportion in all lawsuits (only cases that are not settled receive judicial verdicts). This prediction is confirmed by the sample: in 50% of the cases, the disputes either went through or an application for AR was rejected by an reviewing agency. This is significantly higher than the figure reported in a study based on a more representative sample of published and unpublished disputes, where only 36% of tax disputes were reported to be preceded by AR.¹⁰⁸

Another kind of evidence seems to confirm the selection effect of AR. Our sample captures 254 first-instance judicial decisions.¹⁰⁹

¹⁰⁵ John M. de Figueiredo, *Strategic Plaintiffs and Ideological Judges in Telecommunications Litigation*, 21 J. LAW ECON. ORGAN. 501 (2005).

¹⁰⁶ See text accompanying notes 121-126 *infra*.

¹⁰⁷ The evidence presented in Part II.B for the trial selection theory is based on aggregate data and on diachronic variations. Here I consider whether this effect is manifest in sample cases themselves.

¹⁰⁸ Huang, *supra* note 52, at 80.

¹⁰⁹ Because many decisions on appeal report the decisions of the first-instance courts, it is possible to code for some aspects of such first-instance decisions even though they are not directly available. Thus 272 first-instance dispositions are captured in the sample, included 49 summary dismissals and 18 permissions to withdraw. Consistently with the calculation described in Part I, summary dismissals are included as a kind of judicial verdict (thus in the denominator for computing plaintiff wins) but permissions to withdraw are not.

Among these, the plaintiff win rate is 18.4%.¹¹⁰ This is somewhat higher than the average rate of plaintiff wins in Chinese tax litigation over recent years.¹¹¹ In disputes involving penalties, however, the plaintiff win rate is even higher. 57 out of 190 of the lawsuits in the sample implicated penalties. First instance courts reversed the penalties in 21 cases (sustaining in part and reversing in part in 4 more.) This is a significantly higher win rate for plaintiffs than on average, and it may not be coincidental: as discussed in Section II.A, penalty decisions can be appealed to courts directly without going through AR; thus the filtering effect of AR—which suppresses observed plaintiff win rates—does not apply.¹¹²

3. Evidence for information asymmetry between plaintiffs and defendants

An interesting set of results from the analysis of published cases relates to information asymmetry between plaintiffs and defendants. Under the trial selection theory, if the defendant enjoys an information advantage regarding issues relevant to trial outcome—e.g. it possesses private information about the facts implicated in the disputes (e.g. whether the defendant was negligent), greater knowledge about judicial attitudes, and so on—it will make more informed decisions about settlement, adopt more effective strategies when bargaining with plaintiffs, etc., all of which will result in a lower observed plaintiff win rate. In tax and other administrative litigation, it is possible that the defendants systematically enjoy

¹¹⁰ 119 decisions in our sample were rendered by courts on appeals. Among these, the plaintiff win rate was 20%.

¹¹¹ See Chart 2 *supra*.

¹¹² The importance of the trial selection theory is illustrated by this last discussion. Without applying such a theory, one might be tempted to explain why Chinese courts are more willing to hold against tax agencies in penalty cases than in other cases in terms of judicial attitudes or judicial quality. For example, perhaps penalty cases more often involve intuitive judgments about fairness (i.e. “Was the penalty commensurate with the taxpayer’s fault?”) And judges are perhaps less willing to defer to tax agencies in respect of such judgements than in respect of more “technical” judgments about the proper tax treatment of various transactions. Moreover, since the impositions of penalties tend to be subject to more stringent administrative procedures, judges may seem especially well positioned to safeguard procedural (as opposed to substantive) justice. However, such hypotheses about the effect of judicial quality on litigation outcome may well be spurious, given the existence of another theory that simultaneously explains a much wider range of phenomena.

information advantages. In particular, tax agencies may have good knowledge of the law regardless of whether they have attorney representation, since enforcing the law is their job. By contrast, taxpayer plaintiffs (especially those that have been assessed deficiencies) are likely to be adequately informed about the law only when they engage attorneys. This hypothesis is partially supported in the U.S. context, where it has been found that attorney representation of taxpayers in Tax Court proceedings significantly reduced the IRS recovery rate.¹¹³

In the 233 judicial documents I analyzed, plaintiffs are represented by attorneys in 113 instances, and act *pro se* in the remaining 120 cases.¹¹⁴ Two different statistical tools (crosstab and multivariate logit regression) show that plaintiff attorney representation is significantly (at the .001 level) and negatively correlated with whether the plaintiff is an individual, and significantly (at the .05 level) and positively correlated with whether the case was preceded by AR.¹¹⁵ In other words, individual plaintiffs, as well as plaintiffs who have brought suit directly instead of going through AR, are less likely to hire attorneys.¹¹⁶ Interestingly, plaintiff representation significantly (at the .05 level) increase the chance that the plaintiff will make a procedural argument in the case.¹¹⁷ There is some evidence, therefore, that hiring attorneys helps mitigate plaintiffs' information disadvantage, and the greater than half of plaintiffs who failed to hire attorneys did so to their own detriment.

¹¹³ Lederman & Hrung, *supra* note 15, at 1255.

¹¹⁴ It is conceivable that cases with plaintiff attorney representation involve more elaborate fact finding and legal interpretation, and that courts are more likely to publish elaborate cases. In combination, these factors suggest that the proportion of plaintiff attorney representation is over-stated in published cases.

¹¹⁵ In the multivariate analysis, I used two additional independent variables as controls: whether the dispute took place in an urban (as opposed to rural) area, and the monetary amount disputed. Neither of these variables turned out to have any significant correlation with either plaintiff or defendant attorney representation. The independent variables also bear no significant correlations with one another, dispelling concerns about multi-collinearity in the multivariate regressions.

¹¹⁶ This is consistent with the pattern in the descriptive statistics in Huang, *supra* note 52: entity plaintiffs are much more likely to engage attorneys than individual plaintiffs.

¹¹⁷ Plaintiff representation is also positively correlated with the outcome of an adverse ruling against the defendant using a simple crosstab measure, although this effect disappears using the more rigorous multivariate logit analysis.

Defendants' representation by lawyers turns out to be an entirely different story. In the sample, tax agencies hired attorneys more frequently than plaintiffs—in 131 of the cases. However, whether a defendant engaged attorneys shows no significant correlation with whether the lawsuit was preceded by AR or with other independent variables (e.g. the location or amount in dispute). Moreover, defendant representation by lawyers has no significant impact on the likelihood of the defendant mounting a procedural defense. Finally, defendant attorney representation even seems positively correlated (under crosstab) with an adverse ruling against the government—the governing hiring a lawyer is more likely to lead to a government loss—although a more rigorous multivariate analysis shows that it simply has no effect on case outcome. Whether external attorney offers any “value added” to tax agencies defendants, therefore, is quite unclear.

These patterns can be interpreted as evidence that tax agencies are themselves aware of the relevant procedural rules even without external legal support. In another recent empirical study of Chinese administrative litigation, the average frequency of attorney representation of defendants across agencies was 30%.¹¹⁸ This is much lower than the frequency (57%) of defendant attorney representation in our tax sample. The author of that study, Professor Huang Qihui, argued that because government agencies both have in-house lawyers and are repeat-players in litigation, they are less likely to hire attorneys than plaintiffs. In other words, external lawyers may not provide enough “value added” for government defendants. This view is consistent with the observed effect of defendant attorney representation in our sample. It could also explain why tax agencies' choice about whether to have attorney representation seems more random than that of plaintiffs.¹¹⁹

4. Legal standards and judicial bias

Notwithstanding the selection effects of both pre-litigation proceedings and settlements during litigation, and notwithstanding

¹¹⁸ Huang, *supra* note 52, at 78.

¹¹⁹ If external attorneys provide relatively little value added, there should also be little selection bias that would result in defendant attorney engagement being over-represented in case samples. This raises the possibility that tax agencies in fact engage lawyers in litigation more often than other agencies, despite (or perhaps because of) the low volume of tax litigation.

the general brevity of Chinese court decisions,¹²⁰ it is possible to glean evidence from the large sample of tax cases regarding the legal standards applicable to disputes between taxpayers and tax administrators, the judicial application of these standards, and even the reactions of the executive branch of government towards tax litigation.

At the outset, however, it is worth noting that the method for empirically studying judicial bias most commonly employed in U.S. scholarship is not feasible in China.¹²¹ In empirical tests of the “attitudinal model” of judicial behavior—particularly to test the hypothesis that the decisions of judges can be predicted from their political party affiliation or ideology—scholars usually examine the decisions of a small number of judges in a large number of cases.¹²² In this approach, the large quantity of decisions associated with each judge dilutes the effect on case outcome of the merits of particular cases. The relatively small number of judges involved, meanwhile, makes it feasible to gather personal information about each of them. The theoretical validity of this approach to testing the attitudinal model is controversial.¹²³ But even if it is valid (when properly used), it would be difficult to implement in China. Chinese judges’ role in most types of adjudication is much less individualistic than in the U.S.; the role of individual courts is much more prominent.¹²⁴ Moreover, even if relevant, the personal characteristics of judges in the thousands of lower-level courts that adjudicate almost all of the first- and second-instance lawsuits are difficult to gather.¹²⁵ Finally,

¹²⁰ The average length of decisions in the sample is fewer than 3,000 Chinese characters (the equivalent, if translated, to not much more than 2,000 English words).

¹²¹ Indeed, such method may not be deployable in most countries with civil law judiciaries and less individualistic judges.

¹²² See JEFFREY A. SEGAL & HAROLD J. SPAETH, *THE SUPREME COURT AND THE ATTITUDINAL MODEL REVISITED* (2002); CROSS, *supra* note 2.

¹²³ There is a particular acute question of whether it can be reconciled with the trial selection theory. See de Figueiredo, *supra* note 105.

¹²⁴ See, generally, Liebman, *supra* note 78.

¹²⁵ In J. MARK RAMSEYER & ERIC B. RASMUSEN, *MEASURING JUDICIAL INDEPENDENCE: THE POLITICAL ECONOMY OF JUDGING IN JAPAN* (2003), Professors Ramseyer and Rasmusen studied the Japanese judiciary, which is much smaller and more elite in composition than China’s corp of over 200,000 court employees. They provided evidence that Japanese judges could decide cases independently in tax and other subject matter areas, by using data about the judges’ promotions, demotions, and career stagnations. Such data is not available in China and thus this approach for studying judicial independence is also not feasible.

in almost all areas of administrative litigation—tax is only one most extreme example in this regard—the case volume is sufficiently low, and case publication practice sufficiently recent, that not many cases can be attributed to the same court. For example, in 2013, when all administrative lawsuits are combined, there are on average fewer than 40 cases for each of the over 3,000 Chinese basic-level courts, and there is approximately one tax case for every nine such courts.¹²⁶

The evidence we have, therefore, is circumstantial. Two types of weak evidence for judicial bias in favor of the government can be reported. First, in many cases in the sample, judges displayed strong deference to tax agencies on matters of legal interpretation, to the detriment of plaintiffs. This is especially apparent in a substantial number of decisions (69 of them) where the agency actions challenged were partially based informal agency guidance. According to the SPC's position, such guidance lacks the formal force of law and is not binding on courts.¹²⁷ In a number of these cases, plaintiffs requested the courts to disregard allegedly inappropriate informal guidance, and the courts declined to do so even though they had the power to. However, it must be recognized that judicial deference to administrative agencies in statutory interpretation is widespread even in mature legal systems, and can clearly be compatible with judicial independence.¹²⁸ Moreover, the more statutes (or law with equivalent force) delegates authority to administrative agencies to engage in rulemaking and legal interpretation, the harder it will be for courts to contravene the exercise of such delegated power. Thus it is not clear that the prevalence of judicial deference in tax cases should be blamed on judicial weakness as opposed to excessive statutory delegation.¹²⁹

¹²⁶ The decisions of 133 different courts in China are represented in the case sample studied here. Even courts that published the largest number of tax cases in the sample (two intermediate courts in Shanghai) only had 9 and 8 cases each.

¹²⁷ The legal status of informal agency guidance and the SPC's position with respect to such guidance is extensively discussed in Nicolas Howson, *Enforcement without Foundation? Insider Trading and China's Administrative Law Crisis*, 60 AM. J. COMP. 955 (2012), and Wei Cui, *What is the "Law" in Chinese Tax Administration?* 19 ASIA PAC. LAW REV. 75 (2011).

¹²⁸ See KRISTIN E. HICKMAN & RICHARD J. PIERCE JR., FEDERAL ADMINISTRATIVE LAW, CASES AND MATERIALS, CHAPTER 6 (2D ED. 2014); Kristin E., Hickman, *IRB Guidance: The No Man's Land of Tax Code Interpretation*, 2009 MICH. ST. L. REV. 239 (2009).

¹²⁹ On excess statutory delegation in Chinese tax law, see Cui, *supra* note 127. Note also that, in our case sample, there were at least 30 instances where courts ruled that tax agencies misapplied the law.

A second weak indication of judicial bias is the courts' response to procedural arguments. In 77 decisions in the sample, plaintiffs raised procedural challenges against agency actions, but this led to adverse rulings against agencies only in 13 instances. Defendants made defenses on procedural grounds also in a significant number of cases, which resulted in favorable rulings for the defendants in 2/3 of the cases (43 out of 66). However, in 7 decisions, courts spontaneously (i.e. without the plaintiffs raising relevant challenges) made adverse rulings against agencies on procedural grounds. Without studying the merits of all these procedural claims (which often require knowledge of facts not sufficiently disclosed in the decisions), the evidence is not conclusive.

On the other hand, the sample also contains cases that reflect the executive branch's view of judicial independence. Of particular interest are clusters of cases where a specific type of disputes is repeatedly brought to courts over time, and where the government appears to have changed the law in reaction to litigation. An important advantage of longitudinal coverage of the case sample assembled here is that it allows one to observe such shifts in legal standards.

One such cluster of cases relates to the treatment of innocent third parties in detected VAT fraud. A prevalent type of VAT fraud in China is the sham issuance of VAT invoices.¹³⁰ Although both criminal and civil penalties apply to those who issue sham invoices, beginning in 1995 the Chinese tax authority applied an adverse rule against buyers who receive such invoices: any invoice that is the product of a sham issuance cannot be used to claim input credits by buyers, regardless of whether the buyer is aware of the sham issuance.¹³¹ That is, even innocent buyers, who receive VAT invoices from purported sellers who signed real contracts with the

¹³⁰ For purposes other than criminal law, a sham issuance encompasses issuing, for oneself or for others, or allowing others to issue for oneself, invoices that are "inconsistent with actual business affairs". *Zhonghua Renmin Gongheguo Fapiao Guanli Banfa* (《中华人民共和国发票管理办法》) [Measures for Managing Invoices] (promulgated by the State Council, as revised by State Council Decree 587, 20 December 2010, and effective on February 1, 2011). A sham issuance is distinguished from producing forged VAT invoices—the invoice issued is authentic, it just does not correspond to actual transactions. This area of substantive Chinese tax law is discussed in ALAN SCHENK ET AL, *VALUE ADDED TAX: A COMPARATIVE PERSPECTIVE* 467-73 (2015) (Chapter 14, Section VI.C).

¹³¹ This is a punitive outcome for taxpayers even if no explicit penalty is imposed: they would need to bear a sizeable tax burden that normally would be passed on to downstream producers or consumers.

buyers, delivered the specified goods, and provided invoices that correspond perfectly with the transactions from the buyers' perspectives, are denied input credit if the invoices turn out to be issued in a sham.¹³² This controversial "buyer strict liability" regime gave rise to repeated disputes between taxpayers and tax authorities, some of which went into litigation. In our sample, four cases, litigated at different times and in different parts of China, presented such fact patterns. In all three cases tried before 2009, the plaintiffs (all innocent buyers) argued (correctly) that the tax authority's rules lacked basis in the law. In all three lawsuits, courts in the first instance and on appeal held for the government and found ways to deflect plaintiff arguments about the legal infirmities of the tax agencies' policies. One could interpret this either as a sign of the lack of judicial independence, or as a normal example of judicial deference to the executive branch. But more interestingly, the national government, when it revised the relevant VAT regulations in 2008, deliberately changed the legal standard. Whereas the old VAT regulation did not provide support for the informal policy of tax agencies regarding sham issuances, the new regulation endorsed the effectiveness of such informal policy, making it much harder for a taxpayer to challenge it. Not coincidentally, in the fourth case in our sample, the plaintiff was not able to advance this legal argument.¹³³

There are other clusters of cases in our sample that illustrate the same pattern: the government was challenged in court on the basis of the legal infirmities of some of its policies (and occasionally suffered

¹³² This could happen, for example, unknowingly to the buyer, the purported seller was not the owner of the goods sold and was simply acting on behalf of someone else (who is not able to issue VAT invoices).

¹³³ This legal issue continues to be litigated and new cases have emerged not contained in the original sample. *See* Anhui Sheng Hefei Shi Luyang Qu Renmin Fayuan Xingzheng Panjue Shu (安徽省合肥市庐阳区人民法院行政判决书) [Anhui Province Hefei City Luyang District People's Court Administrative Litigation Decision], Lu Xing Chuzi Di 00032 Hao (庐行初字第 00032 号) [Lu Administrative Trial Decision No.00032] (2014). *Jinhu Shengjin Tongye Youxian Gongsi yu Huaian Shi Guojia Shuiwu Ju Jicha Ju Xingzheng Chufa Ershen Xingzheng Panjue Shu* (金湖盛锦铜业有限公司与淮安市国家税务局稽查局行政处罚二审行政判决书) [Jinhu Shengjin Copper Company Ltd. v. Huaian City State Taxation Bureau Tax Inspection Department Administrative Penalty Second Instance Administrative Litigation Decision], Jiangsu Sheng Huaian Shi Zhongji Renmin Fayuan Xingzheng Panjue Shu (江苏省淮安市中级人民法院行政判决书) [Jiangsu Province Huaian City Intermediate People's Court Administrative Litigation Decision], Huai Zhong Xing Zhongzi Di 0139 Hao (淮中行终字第 0139 号) [Huai Intermediate Administrative Final Decision] (2014).

legal defeat); subsequently the law was amended in the government's favor to fix the previous infirmity. For instance, certain tax agency penalty practices that evolved in the late 1990s were subject to court challenges, and such practices prevailed only after being codified in statute.¹³⁴ Similarly, the authority of local tax inspection bureau to assess taxes was challenged until the late 1990s, and such authority was given statutory grounding in 2000 upon the revision of the Law on the Administration of Tax Collection.¹³⁵ Indeed, in this last set of disputes, tax authorities had seemed to be threatened with systematic defeat before the statute was changed, as the Chinese Supreme People's Court had indicated that it believed that the law was not on the government's side.¹³⁶

The claim here is not that in all these cases where the law was revised, the revision was a causal consequence of government defeats in courts or even of the government being challenged in courts. It is instead that the government could ultimately protect itself against legal vulnerabilities in court by changing the law, and this is what Chinese tax authorities have often done. In other words, there are two contrasting views regarding potential legal disputes between Chinese taxpayers and tax agencies. One is that even if the taxpayer has strong legal arguments, no good will come from bringing such a dispute to court, because Chinese courts are not independent and the defendant tax agencies will retaliate. The other is that if taxpayers have good legal arguments on a particular issue, then disputes on such issues are likely to arise often. The government may hope that it will not be sued as a result of such disputes, and that

¹³⁴ For discussion, see Wei Cui & Xiaoyu Ma, *The Option to Sue: Hainan Oriental Hotel v. Hainan Local Tax Bureau*, 6 CHINA TAX INTELLIGENCE 20 (2011).

¹³⁵ The evolution of this dispute is discussed in Li Gang (李刚), *Quanguo Tongyi Shuishou Zhifa Wenshu Shiyang Ruogan Wenti Yanjiu* (全国统一税收执法文书式样若干问题研究) [Investigation of Several Issues on the Style of the National Uniform Writ of Tax Collection], 12 CAISHUI FALUN CONG (财税法论丛) [FINANCE AND TAX LAW] 178, 193-99 (2012).

¹³⁶ Zuigao Renmin Fayuan Dui Fujian Sheng Gaoji Renmin Fayuan "Guanyu Fujian Sheng Difang Shuiwu Ju Jicha Fenju Shifou Juyou Xingzheng Zhuti Zige de Qingshi Baogao" de Dafu Yijian (最高人民法院对福建省高级人民法院《关于福建省地方税务局稽查分局是否具有行政主体资格的请示报告》的答复意见) [Supreme People's Court Reply to the High People's Court of Fujian Province Regarding the Inquiry of the Standing of Tax Inspection Office of Local Tax Bureau as the Administrative Body], Xing Ta [1999] 25 Hao (行他[1999]25号) [Xing Ta [1999] No. 25], (promulgated and effective on 21 October 1999).

if sued, the courts will side with it, but ultimately, disputes, lawsuits, and court defeats can be avoided only by changing the law. Overall, existing case law provides more support for the second, rather than the first, view.¹³⁷

C. Summary

To review: if a Chinese taxpayer, considering bringing a lawsuit against a tax agency, hires a good lawyer to review published decisions in tax litigation, they would find that many prior litigants are normal businesses typical of what one finds in the marketplace. They would find courts considering some fairly sophisticated legal arguments advanced by both plaintiffs and defendants. Courts hold against tax agencies with non-negligible frequency—in one fifth of the cases overall and one third of the penalty cases—but the odds of winning is evidently lower for plaintiffs than for defendants. Why the plaintiffs lose, however, are generally not mysterious: either the law simply seems not to be on their side, or tax agencies are enforcing policies and practices that are adverse to the plaintiffs, have inadequate basis in the law, but which presumably are applied to all taxpayers and not just the plaintiffs. Courts are reluctant to invalidate these informal practices (although they occasionally do precisely that). Aside from this, there is little general evidence for courts' lack of neutrality or competence. Adverse legal standards seem much more relevant than judicial attitude or quality. Finally and most importantly, if the taxpayer and his lawyer are able to conclude that they have a strong case on the merits, there is nothing in the published cases (more than half of which involved pro se plaintiffs) that implies that they should preclude the litigation option.

Why, then, do Chinese taxpayers tend not to bring suit? Are legal standards so generally adverse to taxpayers that they rarely have a good case?¹³⁸ How, then, do Chinese taxpayers normally survive? The next Part suggests what is likely to be a surprising answer to these questions.

¹³⁷ Not all disputes and litigated cases involve issues of policy implementation, of course. But when they do not, government incentives for interference with independent adjudication seem even weaker.

¹³⁸ In Part II, we saw that while some litigation procedural rules are adverse to taxpayer plaintiffs, they are probably insufficient to explain the low volume of litigation.

IV. THE REGULATORY ENVIRONMENT: THE HEART OF THE STORY

The social environment in which disputes arise clearly may affect the volume of litigation. Professors Ramseyer and Rasmussen noted, for example, that the number of pawn shops in Japan declined dramatically from 1955 to the present, and as a result the quantity of litigation pursued by Japanese creditors increased (since fewer creditors are pawnshops that could simply keep pawned objects of defaulting debtors).¹³⁹ The challenge, though, is identifying such relevant features of the social environment when one's scope of attention begins narrowly with the courts. In the case of Chinese tax litigation, such a non-obvious, but potentially key, determinant of how disputes arise and are dealt with is the structure of tax administration.

China's workforce of tax administrators comprises approximately 756,000 civil servants.¹⁴⁰ Although this is certainly the largest tax bureaucracy in the world by absolute size,¹⁴¹ it is not in per capita terms: the number of tax administrators relative to the size of the country's general workforce is much lower than the OECD average.¹⁴² Notwithstanding this fact, the organization of China's tax administration permits most business taxpayers to easily contact tax collectors. This is the result of what one might call radical "administrative decentralization".¹⁴³ The easiest way to

¹³⁹ Ramseyer & Rasmussen, *supra* note 8.

¹⁴⁰ OECD, TAX ADMINISTRATION 2015: COMPARATIVE INFORMATION ON OECD AND OTHER ADVANCED AND EMERGING ECONOMIES 84 (2015) (Table 2.4).

¹⁴¹ *Id.*

¹⁴² See Appendix in Leslie Robinson & Joel Slemrod, *Understanding Multidimensional Tax Systems*, 19 INT TAX PUBLIC FINAN 237 (2012). Robinson and Slemrod's analysis of OECD data shows that developed countries tend to have a much higher number of tax administrators relative to population than developing countries.

¹⁴³ Cui, *supra* note 20. I define "administrative decentralization" by two features of the state. First, there is a single bureaucratic hierarchy, and government functions *viz-a-viz* citizens are performed at the lowest levels of the hierarchy. By contrast, higher levels of the bureaucracy do not exercise government power with respect to citizens directly, but instead issue commands to bureaucratic subordinates. Second, the lower the bureaucratic rank, the smaller is the geographical reach of units in the rank. Decentralization thus implies that the jurisdiction of a particular, citizen-facing government unit is geographically quite limited. What is unusual about China is first, how deep (i.e. multilayered) the bureaucratic hierarchy is, and second, how resolutely the tasks of government administration are placed at the bottom ranks of the hierarchy. *Id.*, at 23.

appreciate what this means is to consider the vertical distribution of government personnel—what proportions of civil servants are employed at the various levels of government. At the national level, China’s State Administration of Taxation (SAT) houses just over 800 staff members—a mere 0.1% of the army of tax administrators. By way of contrast, in 2013 the U.S. Internal Revenue Service’s (IRS) National Office in Washington D.C. employed a staff of 4,072, out of a total IRS staff size of 86,977 (i.e. 4.68% of IRS staff work at the National Office).¹⁴⁴ At the next, provincial level, China’s tax bureaucracy has 11,000 employees. Thus even when the national and provincial offices are combined, employees at these levels represent only 1.56% of the tax administration.¹⁴⁵

Where then are China’s tax collectors? Data compiled by the SAT shows that in 2003, 16% of tax administrators working at subnational levels were posted at prefectural/municipal tax bureaus, and an overwhelming 79.5% or more work at the county level or below.¹⁴⁶ Arriving at a breakdown of personnel between the county and lower levels takes some guess work, but the latter ranks contain at least as many employees as the county rank.¹⁴⁷

Imagine what the U.S. IRS would be like if it were structured like China’s tax bureaucracy. First, there would be barely anyone in the Washington D.C. National Office. There would also be no counterparts to the seven current IRS regional offices, each of which oversees matters across several states.¹⁴⁸ Instead, the current 139 IRS district offices, which are field offices directly dealing with taxpayers, would become high-level offices giving commands to three additional layers of subordinate offices, where most personnel would be located. Most interestingly, these offices would form a dense

¹⁴⁴ In 2011, the IRS national office employed a staff of 4,569, out of the total IRS staff size of 94,709. OECD, *supra* note 140, at 83 (Table 2.4).

¹⁴⁵ *Id.* According to a recent OECD study (*id.*), which covered 35 OECD countries and 17 non-OECD countries/regions, China has by far the smallest percentage of tax administration staff working either at headquarters (i.e. national) offices, or at national and regional offices combined, among the 52 countries surveyed.

¹⁴⁶ Cui, *supra* note 20.

¹⁴⁷ Therefore, if one visualizes Chinese tax administration in a pyramidal figure with five tiers (national, provincial, prefectural, county, and sub-county), the proportions of areas of the tiers from the top to the bottom would have the ratios of 0.1:1.5:18.4:40:40. The top two tiers would be barely visible.

¹⁴⁸ IRS, *Chapter 13-1 – Exhibit 1 Regional Offices*, INTERNAL REVENUE SERVICE (Mar. 3, 2015), available at <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Chapter-13-1-Exhibit-1-Regional-Offices>.

network that is, so to speak, close to the ground. Instead of having 20 Taxpayer Assistance Centers in the entire state of New York,¹⁴⁹ for example, there would be 20 such centers just for upper Manhattan.¹⁵⁰ Instead of having just two or three hundred field offices in the entire country, there would be such a number of offices just in one metropolitan area.¹⁵¹

The sheer density of this network of “grass-root” offices implies that each of the offices that constitute the network’s nodes has a small geographical jurisdiction. Taxpayers in each such small jurisdiction is thus in easy physical proximity to an office housing tax administrators. What a local office tends to do also accentuates this proximity. Although, nominally, the role of a local tax office is fairly comprehensive,¹⁵² in reality the bulk of a local office’s staff time and resources are devoted to a range of basic compliance tasks. Relatively fine divisions of labor, for example, are found for managing taxpayer registration, ensuring the timely filing of tax returns and the very basic processing of such returns, ensuring prompt payment of taxes, dealing with refund claims, and issuing tax invoices.¹⁵³ In addition, the local office is supposed to give publicity

¹⁴⁹ IRS, *Contact My Local Office in New York*, INTERNAL REVENUE SERVICE (Aug. 17, 2015), available at <http://www.irs.gov/uac/Contact-My-Local-Office-in-New-York>. Similarly, the State of California has only 28 such centers.

¹⁵⁰ The Dongcheng District in the City of Beijing (https://en.wikipedia.org/wiki/Dongcheng_District,_Beijing), for example, has a population of 0.9 million and a geographical area of 40 square kilometers—which is roughly half the size of Manhattan in both population and area terms. It has twenty taxpayer service centers. See Beijing Shi Guojia Shuiwu Ju (北京市国家税务局) [Beijing State Taxation Bureau], *Dongcheng Qu Shuiwu Tingsuo (东城区税务厅所) [Dongcheng District Local Taxation Office]*, BEIJING SHI GUOJIA SHUIWU JU (北京市国家税务局) [BEIJING STATE TAXATION BUREAU] (Aug. 17, 2015), available at <http://www.bjsat.gov.cn/bjsat/qxfj/dc/swts/>.

¹⁵¹ OECD, *supra* note 140 (Table 2.4) states that IRS has 139 “regional offices” and 119 “local/branch offices”. The City of Beijing itself has more tax offices than this total number of 258.

¹⁵² Cui, *supra* note 20, at 203-4.

¹⁵³ See, e.g. Shenzhen Shi Nanshan Qu Difang Shuiwu Ju (深圳市南山区地方税务局) [Shenzhen Nanshan District Local Taxation Bureau], *Shenzhen Shi Nanshan Qu Difang Shuiwu Ju Shuiwu Shixiang Tiaozheng Gaozhi Shu (深圳市南山区地方税务局税务事项调整告知书) [Notice of the Shenzhen Nanshan District local taxation bureau regarding adjustments to tax-related matters]*, SHENZHEN SHI DIFANG SHUIWU JU (深圳市地方税务局) [SHENZHEN LOCAL TAXATION BUREAU] (Jul. 13, 2015), available at <http://www.szds.gov.cn/wap/tzgg/201507/07d8debf75344486a2bd6a20453e5d09.shtml> (detailing the functions and services provided by a local tax office).

to tax law, and provide taxpayer education, training, and other services.¹⁵⁴ Thus instead of mailing one's returns and writing checks to distant "return processing centers" as U.S. taxpayers do, and in addition to being able to dial up the equivalent of IRS service hotlines, Chinese taxpayers can handle their basic tax compliance and obtain taxpayer services in their neighborhoods. In short, tax administration in China possesses a "personal face" to a much greater extent than in many other countries.

The origin of this organizational structure of Chinese tax administration are complex.¹⁵⁵ Suffice it to say that the purpose of this structure is *not* to provide face-to-face taxpayer service, but to collect tax revenue in the main ways in which the government knows how to.¹⁵⁶ Moreover, by some measures this system has also worked well: close contact with taxpayers has reduced the size of the informal sector in China to one of the smallest in the world, and Chinese tax revenue has been growing at a faster pace than its GDP for almost two decades.¹⁵⁷ But it has also had many unintended implications. For our purposes here, the most important implication is for how Chinese taxpayer may choose to learn about and comply with tax law.

Like taxpayers elsewhere, a Chinese taxpayer may consult government publications, acquire professional tax advice, or inquire with taxpayer service units within the tax administration to learn about tax law. But in addition, because of the dense network of local tax offices, he is also able to consult with the tax administrators in the neighborhood, whom he deals with during routine (e.g. weekly or monthly) tax compliance, regarding the latter's view about how certain transactions should be handled.¹⁵⁸ This latter option offers

¹⁵⁴ Cui, *supra* note 20, at 204.

¹⁵⁵ It needs to be traced both to the Chinese government's attempt to build a tax system to embrace a market-based economy in the 1980s and 1990s, and to the overall structure of the Chinese state. See *id.*, at 235-6.

¹⁵⁶ In other words, physical proximity between Chinese taxpayers and tax collectors does not mean that the former get better taxpayer services than taxpayers in other countries: the primary objective of any local tax office and of most local office employees is still to collect revenue.

¹⁵⁷ *Id.*, at 194, 199.

¹⁵⁸ In many countries, only a small set of taxpayers, e.g. large corporations where audit teams from the tax agency are routinely stationed, have tax administration staff specifically assigned to them and deal with them on a routine basis. Taxpayers may have access to good taxpayer services, including having simple inquiries answered, but the government staff answering the inquiries are not the ones that will engage in audits and make tax assessments.

two significant advantages. First, it is these officials who are most likely to be conducting any examination of the transactions in question in the future. Not only may the officials' view now be a relevant predictor of their view in the future, but the officials may also feel bound to some extent by their own advice to taxpayers, or at least be more reluctant to impose severe penalties if taxpayers turn out to own additional taxes. In other words, consulting the local tax official about tax law has advantages analogous to obtaining an advanced ruling.¹⁵⁹ Second, learning the law through local tax officials is also (considerably) cheaper than hiring tax advisors. By relying on local tax officials for legal advice, taxpayers effectively convert what would have been their compliance costs into the government's administrative costs.¹⁶⁰

It is likely that many Chinese taxpayers precisely engage in such behavior. Moreover, because the grass-root offices offer low career incentives to their employees and inadequate opportunities for specialization, it is likely that local tax administrators have rather imperfect knowledge of tax law.¹⁶¹ When this is the case, and when taxpayers do not independently learn the tax law, even the most "compliant" taxpayers are only "semi-compliant": their compliance activities are blessed by local tax administrators' routine intervention and (non-binding) advice, but may still substantially deviate from the requirements of law.

Now consider a Chinese taxpayer's incentives when a dispute with the local tax office arises. First, the dispute would be viewed from both sides in the context of an ongoing, physically proximal, and frequently interactive relationship: how the dispute is resolved is likely to affect future interactions, and both sides may prefer not to be burdened with continued adverse feelings. Moreover, the prospect of future interactions also creates rooms for bargaining in settlement. Second, to litigate in court, or even to bring a dispute through a formal administrative review proceeding, both sides would need to come to terms with what the law requires. Many taxpayers, however, have precisely chosen not to do that in regular compliance. Instead, by choosing to rely on the local tax office for various compliance

¹⁵⁹ See *id.*, at 223 for a discussion contrasting this type of *ex ante* consultation and advanced rulings systems available elsewhere.

¹⁶⁰ Indeed when local tax offices engage in extensive tax return processing, they may even be perceived as an adequate substitute for professional tax return preparers by many businesses.

¹⁶¹ *Id.*, at 211-4.

efforts, they have benefited from both savings on advisory and compliance costs and perhaps even direct tax savings resulting from the local tax collectors' partial ignorance (or discretionary application) of the law. Any taxpayer considering becoming a plaintiff, therefore, must be prepared to abandon this type of normal equilibrium. These two factors—the greater opportunity for settlement due to repeated interactions, and the desire that taxpayers may have for keeping to a particular type of compliance practice—may both have powerful effects in suppressing formal dispute resolution strictly based on the law.

Note that these explanations are distinct from the claim that taxpayers may hesitate to sue tax agencies for fear of retaliation. To begin, a tax agency's ability to retaliate is presumably constrained by law: if a taxpayer can sue an agency in the first place, it can sue the same agency for retaliatory actions that have no basis in law. The question, then, is whether a defendant (especially one that loses) may retaliate within the bounds of law. In China it is plausible that this is feasible, but the reason lies in the tax administrators' deep involvement with most taxpayers' normal compliance activities, and the frequency with which taxpayers benefit from such involvement. It is not enough that the agency sued retains jurisdiction over the taxpayer;¹⁶² it must be the case that it delivers benefits to taxpayers that it could withdraw after being sued. Moreover, in the repeated interactions between taxpayers and tax administrators, it is also not just the government that can act strategically, e.g. by retaliating: taxpayers can also choose different levels of cooperation in response to the government's choices. Thus it is at least as plausible to see the suppression of formal disputes as resulting from the expanded space for bargaining and reaching settlement as it is to read such suppression as a reflection of government power.

In summary, the low tax litigation volume in China may be explainable by the atomistic structure of Chinese tax administration, which creates opportunities for frequent informal actions between taxpayers and tax administrators. The logic of this explanation might extend to other regulatory areas as well. For example, it has been noted in a number of studies that in the sphere of environmental protection, the level of environmental litigation (including administrative litigation) is so low that the maintenance of specialized environmental courts, which the Chinese government

¹⁶² This is true for most other tax systems (in other countries).

created in 2011, has been difficult to justify.¹⁶³ It has similarly been noted that the penalties imposed on polluters and other violators of environmental law are far lower than can be expected from statutory provisions.¹⁶⁴ Fewer scholars have recognized that the organization of environment protection agencies in China is very decentralized, in ways not dissimilar to the decentralization of tax administration discussed above.¹⁶⁵ But it is plausible that such decentralization is also the culprit for low litigation in the environmental area.

V. ADMINISTRATIVE LITIGATION AND THE RULE OF LAW

Among Chinese policymakers and legal scholars, it is conventional wisdom that administrative litigation is not just a mechanism for resolving disputes between private parties and government entities, disputes that arise because of factual and legal disagreements and perhaps simply as a part of life. Administrative litigation instead (and perhaps even primarily) serves the function of protecting the legal rights and interests of citizens from the encroachment of the government. This imputed function implies that the government is prone to making such encroachment, and perhaps more generally, to acting in ways that significantly deviate from what is required by the law. This implied claim is certainly apt in characterizing many of the activities of the Chinese government, which is far from being tamed by the rule of law.¹⁶⁶ From this perspective, while citizens suing the government may or may not be acting purely in their own private interest, such lawsuits may generate a kind of social benefit beyond the private benefit for the plaintiffs: administrative litigation may deter the government from much unlawful activity, or at least help the government to improve

¹⁶³ Xuehua Zhang et al., *Agency Empowerment Through the Administrative Litigation Law: Court Enforcement of Pollution Levies in Hubei Province*, 202 CHINA Q. 307 (2010); Stern, *supra* note 42.

¹⁶⁴ Zhang et al, *supra* note 163.

¹⁶⁵ One scholar observed that one provincial environmental protection bureau may be too thinly staffed. Benjamin Van Rooij, *Organization and Procedure in Environmental Law Enforcement: Sichuan in Comparative Perspective*, 17 CHINA INFO. 36 (2003). This phenomenon in fact exists across provinces and across agencies. I discuss these cross-agency commonalities in Wei Cui, *The Legal Maladies of "Federalism, Chinese-Style"*, in THE BEIJING CONSENSUS? HOW CHINA HAS CHANGED THE WESTERN IDEAS OF LAW AND ECONOMIC DEVELOPMENT AND GLOBAL LEGAL PRACTICES (Weitseng Chen ed., forthcoming).

¹⁶⁶ See note 10 *supra*.

its operations through better alignment with the law.¹⁶⁷ Although public law scholars may be unfamiliar with such a formulation, the idea is that legal disputes with government agencies have strong positive externalities, as they promote a particular social good, namely the rule of law in governance.

It is very likely for this reason that the Chinese government has heavily subsidized administrative litigation. The subsidies take multiple forms. At the level of individual disputes, court fees for administration litigation are negligible (50 yuan or 8 dollars per case).¹⁶⁸ In the institutional dimension, separate tribunals with dedicated judges for hearing administrative law disputes are set up at courts at all levels, resulting in an average case load of fewer than 40 a year for such tribunals.¹⁶⁹ The judicial system also separately gathers and publishes data on administrative litigation, which made possible the analysis in Parts I and II *supra*. Moreover, a large number of Chinese legal scholars specialize in research on how to make administrative litigation more effective at promoting the rule of law, for example by modifying the Administrative Litigation Law to offer more plaintiff rights and remedies.¹⁷⁰ As a part of the judicial apparatus that receives such targeted subsidies, administrative litigation is clearly a distinct institution with a distinct purpose.

In tax and many other areas, however, what paradoxically seems to be preventing this institution from serving its purpose is the shortage of plaintiffs. Missing (often) are the very parties whose

¹⁶⁷ For the inevitable divergence between the private incentives and social cost and benefits of litigation, see SHAVELL *supra* note 21, Chapter 17.

¹⁶⁸ Susong Fei Jiaona Banfa (诉讼费缴纳办法) [Measures Regarding Payment of Litigation Fee] (promulgated by the St. Council, Dec. 19, 2006, effective April 1, 2007), art. 13(5). Attorney fees are also low. Li, *supra* note 11, at 69.

¹⁶⁹ See, Cui and Wang, *supra* note 16.

¹⁷⁰ See generally, 2 JIANG BIXIN (江必新) & LIANG FENGYUN (梁凤云), XINGZHENG SUSONG FA LILUN YU SHIWU (行政诉讼法理论与实务) [THEORY & PRACTICE ON ADMINISTRATIVE LITIGATION LAW] (2011); He Haibo (何海波) ed., *Lixiang de Xingzheng Susong Fa (理想的行政诉讼法) [The Ideal Administrative Litigation Law]* (unpublished conference proceedings on file with the author); HE HAIBO (何海波) ET AL. ED., FAZHI DE JIAOBU SHENG – ZHONGGUO XINGZHENG FA DA SHIJI (1978-2014) (法治的脚步声——中国行政法大事记(1978-2014)) [THE FOOTSTEP OF THE RULE OF LAW – THE CHRONICLE OF CHINA’S ADMINISTRATIVE LAW (1978-2014)]; LIN LIHONG (林莉红) ED., XINGZHENG FAZHI DE LIXIANG YU XIANSHI (行政法治的理想与现实) [THE IDEAL AND REALITY OF ADMINISTRATIVE RULE OF LAW] (2014).

rights and interests administrative litigation is supposed to protect. Courts cannot by themselves constrain government and promote the rule of law in the executive branch, unless private parties spontaneously bring suits. This point may seem obvious, but it is also precisely ignored when one assumes that if only courts are more neutral, competent, and particularly more independent and “powerful” vis-à-vis the executive branch, or the procedures for litigation are made more plaintiff-favorable, the lawsuits would naturally happen. The investigation carried out in this Article into the actual empirical patterns of Chinese tax litigation shows that this kind of assumption may have little justification in reality. Just as subsidizing administrative litigation hasn’t made it the institution it is intended to be, improving judicial quality and independence may not, either. The actions and choices of would-be-plaintiffs cannot be forgotten.

The empirical considerations discussed in Parts II to IV suggest two reasons why administrative litigation may be deprived of its significance. The first, more straightforward, reason is that the laws that courts would enforce may be unfavorable to would-be plaintiffs: the judiciary cannot uphold rights that private parties do not have. Thus if Chinese tax law imposes many compliance requirements on taxpayers, taxpayers who flunk such requirements cannot expect much by way of judicial remedy.

The second, more profound reason why the significance of administrative litigation may diminish is that private parties may themselves benefit from, come to terms with, and perpetuate a social order that is inconsistent with the rule of law. Most obviously, thieves, tax evaders, polluters, unscrupulous merchants and opportunistic businesses all benefit from ineffective law enforcement. But equally importantly, many private citizens may prefer to be spared the costs of learning and complying with the law, if they have the opportunity to do so. As discussed in Part IV, if a taxpayer can obtain a significant amount of free tax advice and free assistance with return preparation at a local tax office—even if offering such free services is not the intended function of such offices—they may happily follow the personal discretion of the local civil servants, particularly if they don’t end up paying more tax. Indeed, they may actively seek access to such discretion, more than they try to learn about the law. When incentives for doing so are pervasive, “constraining government” may often not be felt by citizens to be in their own interest. They may readily leave their supposed rights simply on the books.

While it may ultimately be the government's responsibility to put an end to this kind of non-rule-based social practice, it is important to recognize that the problem here is the rule of law has failed in a much more fundamental sense than unconstrained (or under-constrained) government: the failure rather lies in there being no publicly announced legal rules that are generally followed. The making and publicizing of legal rules, and achieving general compliance with these rules, form the pre-conditions of and general backgrounds to large-scale social coordination in many countries (democratic or authoritarian) in the 21st century. They are also pre-conditions of the functioning of judicial institutions in these countries. Where both the government and private citizens opt for personal discretion and informal bargaining instead of rule-based social practices, courts that are supposed to enforce legal rules may end up being little used.

Of course, it is not only Chinese policymakers and legal scholars who tend to identify judicial monitoring of executive action as the locus for promoting the rule of law. The idea of "rule of law" is frequently associated with "constraining government" in discourses around the world. This Article has shown, however, that because the very possibility of judicial monitoring is conditional upon plaintiffs bringing suit, and because whether plaintiffs bring suit in the first place may depend on whether legal rules are generally being complied with by private citizens and effectively enforced by the government—that is, whether legal rules guide social and economic life—the rule of law is far from being synonymous with "constraining government".

As mentioned in the Introduction, some scholars studying administrative litigation have also taken theoretical perspectives different from the one just described. They see administrative litigation as a distinctive institution, but not because it (purportedly) produces a distinctive public good, namely more rule of law in governance (or a more constrained government). Instead, in the context of authoritarian regimes, they see administrative litigation either as furnishing a meaningful tool for the "principals" in the regimes to monitor the actions of their "agents",¹⁷¹ or as an inadvertent opening for those who oppose the regimes to pursue political contest.¹⁷² In the former case, a narrative is then developed to predict how authoritarian regimes may choose among different

¹⁷¹ Ginsburg, *supra* note 4.

¹⁷² O'Brien and Li, *supra* note 4.

forms of monitoring. In the latter case, a new kind of normative significance, beyond the rule of law, is bestowed upon administrative litigation: such litigation may undermine authoritarianism itself.

The weaknesses of these theoretical claims, which can readily be seen purely in conceptual terms, are put into sharp relief by considering the realities of administrative litigation. The main problem with the “third-party monitoring for the benefit of dictators” story is that the objective of such monitoring is presumably catching malfeasance by agents of the authoritarian regime.¹⁷³ However, it is not clear why courts are particularly adept at catching official malfeasance, especially when administrative litigation proceedings and not criminal prosecution are involved.¹⁷⁴ Moreover, since courts are reactive, plaintiffs are needed to detect the instances of malfeasance first. The key “third party” in judicial monitoring, in other words, is the plaintiff, not the judge. It is not clear that the remedies that courts typically provide to plaintiffs in administrative litigation give distinctively strong incentives for monitoring official malfeasance. Given these facts, whistleblower or ombudsman systems with rewards appear much more suitable for the purpose of third-party monitoring from the perspective of authoritarian principals. The choice of administrative litigation for such purpose would be inexplicable.

As to the story of administrative litigation as a form of political contest, the overwhelming evidence from China is that citizens do not see things that way. As heavily subsidized as the institution of administrative litigation is, it is still infrequently used in many areas. Chinese citizens’ disinclination to challenge one of the most pervasive—and purposefully extractive—branches of the government, namely taxation, is hard to ignore. Instead of citizens using a seemingly neutral and apolitical channel—that of law—to pursue political purposes, the very functioning of administrative litigation as a legal mechanism is threatened by its disuse, for reasons that have no discernible connection with politics.

CONCLUSION

At the outset of this Article, I presented a contrast in how administrative litigation is viewed in democracies with established

¹⁷³ Ginsburg, *supra* note 4, at 11.

¹⁷⁴ They would be, if the errant agents tend to disguise their misconduct through the complexity of legal rules, but there is no reason to believe that this is the case.

rule of law, on the one hand, and in countries that are characterized either by authoritarianism or by deficient legal systems, on the other. In the former context, administrative litigation often does not stand out as a distinctive institution, but instead merges seamlessly into a background characterized by the rule of law. In the latter, administrative litigation is often portrayed as an aspirational institution, as capable of either promoting the rule of law or undermining authoritarianism. Consequently, it may be showered with subsidies (sometimes even by the governments it is supposed to reform themselves) and highlighted for political support by international rule of law initiatives. An implicit assumption underlying these different manners of (and motivations for) endorsing administrative litigation is that a weak judiciary will undermine that institution, and that to enhance it, one needs to empower the judiciary.

This Article, by analyzing the determinants of administrative litigation patterns in a context characterized by authoritarianism and a rule of law deficit, has questioned the justifiability of thus privileging the judiciary. It appears that the behaviors of litigants, as well as the laws that courts are supposed to enforce, have more explanatory power insofar as some core litigation outcomes are concerned. Moreover, by highlighting the causes of the disuse of administrative litigation, it has questioned an even deeper and more widely-held assumption, namely that the rule of law should be identified with judicial constraints on the executive.

This Article resembles previous revisionist scholarship that employs a generally applicable conceptual framework, combined with empirical analysis, to penetrate a self-enclosed, self-sustaining discourse about a particular legal system. For example, using similar methods, Professors Mark Ramseyer and Eric Rasmussen forcefully challenged “cultural models” of the Japanese legal system and common wisdom about litigation patterns in that system.¹⁷⁵ The

¹⁷⁵ See J. Mark Ramseyer & Minoru Nakazato, *The Rational Litigant: Settlement Amounts and Verdict Rates in Japan*, 18 J. LEGAL STUD. 263 (1989) (demonstrating that rational choice models used in the U.S. can explain litigation choices in Japan without resorting to “cultural” models, and that “claims that Japanese courts are so expensive, powerless, and slow that they effectively deny relief to victims of legal wrongs” are unfounded); Ramseyer & Rasmussen, *supra* note 15 (using empirical analysis of Japanese judges’ careers to demonstrate the falseness of popular wisdom that low plaintiff win rates in Japanese tax litigation is due to the government’s manipulation of the judicial apparatus to obtain decisions biased in its favor).

discourse on Chinese administration litigation studied here is similar to the discourse Professors Ramseyer and Rasmussen criticize in that the discourses' participants rarely consider whether the explanations offered can apply in other legal systems, or fare better than alternative explanations in predictive power. But the stakes in this study are higher, since the Chinese discourse about administrative litigation has been taken to inform thinking about the relationship between the rule of law and authoritarian regimes in general.¹⁷⁶

¹⁷⁶ Ginsburg, *supra* note 4.