



漢坤律師事務所
HAN KUN LAW OFFICES

Newsletter

China Practice

Global Vision



8th Edition of 2017



Legal Updates

1. Repossession of Aircraft in China: Legal Issues and Options for Lessors
2. Hong Kong's Recently Passed Ordinance on Third Party Funding and HKIAC's Consultation on Proposed Amendments to the 2013 Rules
3. PRC Court for the first time Recognizes and Enforces a Commercial U.S. Court Judgment



Legal Updates

1. Repossession of Aircraft in China: Legal Issues and Options for Lessors (Authors: Shu WANG, Jun ZHU)

While the aviation industry continues to expand quickly in the PRC market, it is still possible that things can go wrong and an individual lessee may default under a lease when it faces tough times due to various reasons. For all lessors, whether they are financial lessors or operating lessors, it is essential to have a good knowledge of their enforcement rights in the worst scenario and the actions that they can do to recover their aircraft when all other remedies have failed.

This article intends to provide an overview of the major legal and practical issues involved if a lessor seeks to repossess an aircraft leased to a Chinese operator/airline (the “**PRC Lessee**”). Considering the complexity of the repossession of aircraft, it should be noted that this article does not intend to give a detailed analysis of all issues that may come up during any aircraft repossession.

Lessor’s Repossession Rights under the PRC Law

From PRC law perspective, a lessor’s rights to repossess an aircraft may depend on the following facts:

- a. Whether the underlying lease is a financial lease or an operating lease. Under the PRC law, both a financial lessor and an operating lessor are entitled to repossess aircraft upon the PRC Lessee’s default; however, due to the nature of a financial lease being financing, their rights differ in some aspects. For example, a financial lessor is required to return the residual value of the aircraft back to the PRC Lessee after it disposes of the aircraft and pay off the debt owned by the PRC Lessee to it.
- b. Whether the lease is a cross border lease or a domestic lease. A cross border lease is usually governed by the laws of a foreign jurisdiction (such as the laws of England, New York); therefore, in addition to the statutory remedies provided by the PRC law to the lessor, the lessor may be entitled to claim the relevant rights and remedies under the governing law of the cross border lease.
- c. Whether the lease is entered into before or after 1 June 2009. The Cape Town Convention and its Aircraft Protocol (collectively, the “**Convention**”) took effect in mainland China from 1 June 2009; therefore, for those cross border leases entered into after 1 June 2009, the lessor would be entitled to claim the rights and remedies under the Convention.

Self-help Remedies in Repossession

The PRC law does not expressly accept “self-help” remedies or equivalent concepts and, when

approving the Convention, China has declared that “any remedy available to the creditor under any provision of the Convention which is not there expressed to require application to the court may be exercised only with leave of the court of the PRC”. Therefore, although lessor is permitted to exercise its rights to repossess the aircraft according to the lease and the applicable law, if the PRC Lessee does not cooperate in this respect or refuse to return the aircraft, it would be difficult for lessor to enforce the repossession right by directly taking physical possession of the aircraft.

Without the PRC Lessee’s cooperation, lessor may have to resort to the court for a judgment or verdict in favor of repossession of aircraft.

Application of Security Deposit or Money Drawn From the Security Deposit L/C or Bank Guarantee

For an aircraft operating lease, it is normal that performance of the PRC Lessee’s liabilities and obligations under the lease is secured by a cash security deposit (the “**Security Deposit**”) or a standby letter of credit (the “**Standby L/C**”) or on demand guarantee (the “**Bank Guarantee**”) issued by a commercial bank. When the PRC Lessee defaults on its payment obligations under the lease, the lessor is entitled to apply the cash Security Deposit or make drawdown under the Standby L/C or the Bank Guarantee and apply the money drawn towards any outstanding amounts under the lease.

Although the lease may provide for the conditions and the way of using the cash Security Deposit, it is worth to note that application of the cash Security Deposit or the money drawn from the Standby L/C or the Bank Guarantee may constitute a set-off of debt and would require notice from lessor to the PRC Lessee (according to the Contract Law of the PRC, a set-off is effective from the moment when a debtor was notified about the set-off), regardless of the provisions of the lease.

The PRC law also permits lessor to exercise its rights to set-off against the PRC Lessee’s bankruptcy administrator after the PRC Lessee commences bankruptcy procedures, subject to satisfaction of certain conditions.

Bankruptcy of the PRC Lessee and Its Effect on the Repossession

If the PRC Lessee’s financial condition continue to deteriorate, it is possible that the relevant court may commence bankruptcy procedures against the PRC Lessee, on voluntary or involuntary basis.

On the one hand, in accordance with the PRC Law, the PRC Lessee may file a voluntary petition for bankruptcy only if the following two conditions have been met: first, the PRC Lessee is unable to pay its debts when due; and second, the PRC Lessee lacks sufficient assets to pay the debts or it becomes apparent that the PRC Lessee has no capacity to discharge its debts. On the other hand, a creditor of the PRC Lessee may file an involuntary petition when the PRC Lessee is unable to pay its debts when due. For the involuntary petition filed by the creditor of the PRC Lessee, whether the court would require a comprehensive review of the PRC Lessee’s assets and liabilities or a non-

payment in one transaction would trigger the bankruptcy procedures is more subject to the court's discretion.

Commencement of bankruptcy procedures will have profound legal implications to lessor's rights to repossess the aircraft, including:

- a. The PRC law imposes an automatic stay during the pendency of the bankruptcy procedure of the PRC Lessee, which means that:
 - i. the PRC Lessee is not allowed to pay rent and other amounts to an individual lessor under the lease;
 - ii. any lawsuit against the PRC Lessee can only be commenced in the same people's court that accepts the bankruptcy petition;
 - iii. any civil lawsuits or arbitration proceedings or enforcement procedures initiated prior to the commencement of the bankruptcy case are suspended;
 - iv. interest on unmatured debts (including default interests on unpaid rent) stop accruing as of the date the court grants the bankruptcy petition;
 - v. the PRC Lessee's creditor is prohibited from enforcing its rights against the property of the PRC Lessee after the bankruptcy petition is accepted by the court.
- b. The PRC law authorizes the court to avoid, upon request of the bankruptcy administrator, certain fraudulent conveyances of the PRC Lessee's property within one (1) year prior to the date the court accepts the bankruptcy petition, and any payment made for the benefit of a creditor within the six (6) months period prior to the date the court accepts the bankruptcy petition if the debtor was insolvent at the time, which means that the court may scrutinize the payments made by the PRC Lessee to the lessor within the above period.
- c. The bankruptcy administrator of the PRC Lessee is authorized to terminate or continue to perform pre-bankruptcy contracts if there are obligations to be performed by each contracting party, which means that the bankruptcy administrator of the PRC Lessee may terminate the lease with the lessor.

If bankruptcy proceedings have commenced with respect to the PRC Lessee, and the lease has not been terminated either by the PRC Lessee's bankruptcy administrator or the lessor, then the rights of the lessor under the lease will continue as against the PRC Lessee's bankruptcy estate. The aircraft on lease shall not be included in the PRC Lessee's bankruptcy estate.

China has made a declaration to the Convention that the entirety of Alternative A of article XI of the Protocol shall apply. This means that, for those leases that the Convention applies, the PRC Lessee's bankruptcy administrator is obliged to return possession of the aircraft to the lessor within sixty (60) calendar days.

Interim Measures

Under the PRC law, the aircraft may be arrested in China before or after a case is filed to the PRC court, if the lessor can convince the PRC court that the arrest meets statutory criteria for a property preservation measure. When the lessor applies for property preservation measure against the aircraft, the court has the power to demand counter-security from lessor in the form of cash or bank guarantee depending on the court's discretion.

If the Convention applies to the lease, lessor is entitled to the interim reliefs under the Convention from a PRC court pending final judgment of its claim and to the extent that the PRC Lessee has at any time so agreed, including: (a) preservation of the aircraft and its value; (b) possession, control or custody of the aircraft; (c) immobilization of the aircraft; (d) lease or management of the aircraft and the income therefrom; (e) sale of the aircraft and application of the income therefrom. In accordance with the declarations made by China at the time of accession to the Convention, for the remedies specified in subparagraph (a), (b) or (c), the PRC Court shall giving a ruling within ten (10) days after receiving an application and immediately enforce it; for the remedy specified in subparagraph (d) or (e), the PRC Court shall giving a ruling within thirty (30) days after receiving an application and immediately enforce it.

Enforcement of Repossession Judgment/Award in Favor of Lessor Made by Foreign Court or Arbitral Tribunal in China

To date, it is still difficult in practice for a foreign lessor to enforce a foreign court interim order or an arbitral award to arrest and repossess aircraft leased to a PRC Lessee.

If a foreign lessor has obtained a final and conclusive foreign court judgment in respect of its repossession of the aircraft, it may apply to enforce such judgment before a PRC court without re-examination or re-litigation, provided that China and the country of the court have concluded a judicial assistance treaty or judgments of courts of the PRC receive reciprocal treatment in the courts of such foreign country. To date, there is no bilateral treaty between China and the U.S. or the England on recognition and enforcement of foreign court judgments. In June 2017, there has been a case that a court in Wuhan, Hubei Province issued a court order (Order No.: 2015 E Wuhan Zhong Min Shang Wai Chu Zi Di 00026 Hao) which recognized and enforced a judgment made by an U.S. court. This is the first court order ever in China that confirms the existence of "reciprocal treatment" relationship between China and U.S. However, as China does not have the legal principle of *stare decisis*, it remains to be seen whether the other PRC courts will follow this view.

In the event that a final arbitral award in respect of foreign lessor's repossession of the aircraft is obtained from an arbitral tribunal, such award would be recognized and enforced in the PRC by the People's Courts according to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("**New York Convention**") if the award is made in a contracting state of the New York Convention (or if the arbitral award is rendered in Hong Kong, according to the Arrangement of

Supreme People's Court on Mutual Enforcement of Arbitration Awards between the Mainland and the Hong Kong Special Administration Region).

Deregistration of the Aircraft

China maintains an operator-based aircraft registry, which means the operator of the aircraft is entitled to apply for the registration of the aircraft. In order for the PRC Lessee to operate the aircraft in China, the aircraft must be registered with the Civil Aviation Administration of China (the "CAAC"). For purpose of remarketing the aircraft in international aviation market and facilitating the next lessee's registration of the aircraft in other relevant jurisdiction after repossession of the aircraft, the lessor needs to ensure that the aircraft will be deregistered from the aircraft registry maintained by CAAC upon its repossession of the aircraft.

According to the rules of CAAC, normally CAAC only accepts the deregistration application filed by the PRC Lessee of the aircraft in the capacity of "operator". CAAC's rules do not expressly permit a lessor being owner of the aircraft to deregister an aircraft by virtue of a deregistration power of attorney issued by the PRC Lessee in advance upon leasing of the aircraft.

For those leases that the Convention applies, the lessor may rely on an Irrevocable De-Registration and Export Request Authorisation (the "IDERA") recorded with CAAC to deregister the aircraft. It should be noted that even if the PRC Lessee has a duly recorded IDERA, it still needs to present "a document issued by a PRC court confirming that the Authorized Party is entitled to possession of the aircraft under the Convention" to CAAC in the deregistration application.

Export of the Aircraft

After the aircraft is repossessed, the lessor may have to deal with export of the aircraft, obtaining permission to ferry flight the aircraft out of China and tax/customs clearance.

To export the aircraft out of China, the lessor will have to file a customs declaration and other necessary documents. As the customs authority normally only deals with the PRC Lessee for import and export of the aircraft, lessor may not be familiar with the relevant customs procedures and may need assistance from an experienced customs declaration agency if the lessor wants to export the aircraft by itself. To date, the PRC customs authority has not issued any special rules on export of an aircraft by using an IDERA.

The lessor may lease the repossessed aircraft to another operator in the PRC. In such case, if the PRC Lessee is still cooperative, the aircraft may be possibly transferred to the new operator by way of lease novation, which may not necessarily cause physical export of the aircraft (necessary procedures still need to be done with the customs authority to reflect the change of lessee).

The ferry flight of the aircraft would be subject to the confirmation of the Airworthiness Department of CAAC as a matter of procedure as to the airworthiness of the aircraft.

According to the rules of CAAC, the authorized party under a duly recorded IDERA is entitled to apply to the airworthiness certification department of CAAC to obtain export certificate of airworthiness before its application to deregister the aircraft.

Other Practical Issues

To our experience in precedent repossession cases, in addition to the above legal issues, lessor is very likely to encounter the following practical issues in repossession of aircraft from the PRC Lessee:

- Other third parties with competing claims in respect of the aircraft and/or the PRC Lessee, including airports, fuel and other suppliers, maintenance facilities and etc.
- Airports and maintenance facilities who may claim possessory lien over the aircraft
- Status of ownership registration of the aircraft with CAAC
- Priority of the international interests and other registrable interests in respect of the aircraft on the International Registry
- CAAC's order to ground the aircraft
- Airport to grant access to aircraft
- Translation of the lease documents written in English into Chinese in order to be used in the relevant procedures in the PRC Court
- Experienced technical team readily available to inspect the aircraft and ensure airworthiness
- Qualified crew to operate and fly the aircraft
- Insurance arrangement after repossession of the aircraft
- The lessor's capability of remarketing the aircraft

According to our experience in the previous aircraft repossessions, it usually take a substantial long period of time to liaise with the relevant parties (including airport, fuel supplier, MRO, air traffic control, local CAAC agency, court, bankruptcy administrator, potential lessee) to coordinate the whole repossession process. This will be challenging to lessor, and to complete a successful and efficient repossession, lessor would need strong and timely support from its business, technical, remarketing and legal teams.

=====

2. Hong Kong's Recently Passed Ordinance on Third Party Funding and HKIAC's Consultation on Proposed Amendments to the 2013 Rules (Authors: Bonita CHAN, Rio LI)

In this June, a long-awaited law was passed and enacted by the Hong Kong Legislative Council, clearing the way for third parties to fund arbitration in Hong Kong.

What Does the New Law Say?

Under the new law, a third party funder is allowed, under a funding agreement in writing, to provide arbitration funding to a funded party, in return for the funder receiving a financial benefit only if the arbitration is successful within the meaning of the funding agreement.

Certain issues are worth noting, amongst other things, that:

- a. the parties will have to define what is a “successful” outcome within the meaning of the funding agreement. Particularly, the parties should specify what would happen in case of negotiation for settlement – it will not be rare that the funder wants to settle sooner whereas the funded party may be inclined to press on with the arbitral proceedings until a better sum is offered;
- b. while the new regime does not preclude the possibility that law firms act as funders, lawyers who act for any party to the arbitration are not allowed to fund those proceedings. In other words, contingency fees arrangement is still not open for arbitration sits in Hong Kong;
- c. The funded party must disclose the existence of the funding agreement, and the funder's name to the other side of the arbitral proceedings and to the tribunal. While failure to comply with this requirement does not render any person liable to judicial or other proceedings, the tribunal can take the failure into account if it is relevant to a question being decided in the arbitration.

Consultation on Proposed Amendments to the 2013 Administered Arbitration Rules

On 29 August, the HKIAC Rules Revision Committee commenced the public consultation process on proposed amendments to the 2013 HKIAC Administered Arbitration Rules¹.

The proposed amendments include, amongst other things:

- a. a new provision on the funded party's duty to disclose information of the funding agreement in the Notice of Arbitration or Answer (where applicable) or within 15 days after the funding agreement is made or terminated, if such agreement is entered into after the arbitration commences (see Proposed Article 44);
- b. an amended confidentiality provision to allow disclosure of arbitration information to a third party funder (see Proposed Article 45.3(e)).

The Committee also seeks views on whether an express provision should be added to allow the

¹ See <http://www.hkiac.org/news/revision-2013-administered-arbitration-rules>

arbitral tribunal to award costs of third party funding as part of costs of arbitration. The public can submit their views to HKIAC by Monday, 2 October.

It is expected that HKIAC's proposed amendments to the 2013 Rules in relation to third party funding will be welcomed by the arbitration community. Further, an express provision should be added to allow the tribunal to award costs of third party funding as part of costs of arbitration so as to avoid any doubts. After all, tribunal will have a general power to decide the issue of costs in the arbitral proceedings.

Summary

The new law and HKIAC's proposed amendments are essential for Hong Kong to keep abreast with its common law jurisdiction fellows, such as UK, Australia and Singapore, and maintain itself as a leading arbitration seat in the world.

By removing the obstacle for third party funding in arbitration, many of the professional investment funders will look into the Hong Kong market for potential investment opportunity. This will also provide great assistance to party who has a strong case but limited resources.

As for law firms, it is anticipated that significant activities and instruction opportunities will emerge in this area. Further, law firms may serve as an ideal channel to bridge the investor's and the funded party's needs.

It is therefore believed that the new law will bring various positive impacts on the stakeholders in Hong Kong's arbitration market.

=====

3. PRC Court for the first time Recognizes and Enforces a Commercial U.S. Court Judgment (Authors: Andy LIAO, Alan LIN)

On June 30, 2017, the Wuhan Intermediate People's Court ("**Wuhan Court**") issued a verdict (the "**Case**") ordering the recognition and enforcement of a commercial judgment rendered by the Los Angeles County Superior Court, California, USA ("**LA Court**"). This marks the first time for a PRC court to recognize and enforce a commercial judgment from a U.S. court², which is of landmark significance and is thus noteworthy for all law practitioners and interested parties.

Case Background

² According to *Provisions of the Supreme People's Court on the Issues Concerning the Procedures for PRC Citizens to Apply for the Recognition of Divorce Judgments by Foreign Courts*, PRC courts may recognize divorce judgments rendered by U.S. courts. In practice, PRC courts have recognized many foreign divorce judgements.

In this Case, the applicant, Li Liu (the "**Applicant**"), applied to the Wuhan Court to recognize and enforce judgment No. EC62608, rendered by the LA Court (the "**U.S. Judgment**"), against the respondents, Li Tao and Wu Tong (the "**Respondents**"), related to a dispute between them involving an equity transfer agreement. Based upon the information contained in the U.S. Judgment, the background of the Case is summarized as follows:

On September 22, 2013, the Applicant and the Respondents signed an Equity Transfer Agreement providing that the Respondents would transfer to the Applicant a 50% equity interest held in JiaJia Management Inc. for consideration of US\$ 150,000. After the Applicant paid US\$ 125,000 to the Respondents, the Respondents absconded with the money. On July 17, 2014, the Applicant filed a suit in the LA Court on the grounds that the Respondents had misappropriated the US\$ 125,000 by fabricating the equity transfer transaction. Subsequently, the LA Court, in the absence of the Respondents, rendered a judgment ordering the Respondents to refund to the Applicant the amount of US\$ 125,000 plus interest, a total of US\$147,492. However, the Respondents did not comply with the U.S. Judgment after it became effective. The Applicant therefore applied to the Wuhan Court to have the U.S. Judgment recognized and enforced since the Respondents had assets available for enforcement in Wuhan, Hubei Province.

Basis for the Wuhan Court Verdict

The Wuhan Court issued the above verdict based on the following grounds:

- a. The Applicant had submitted a certified copy of the U.S. Judgment and a Chinese translation, which satisfied the procedural requirement for applying for the recognition and enforcement of a foreign court judgment;
- b. The Applicant had submitted evidence that precedent exists of U.S. courts recognizing and enforcing civil judgments rendered by PRC courts, thereby confirming a reciprocal relationship between China and the United States for the mutual recognition and enforcement of each other's civil judgments;
- c. The U.S. Judgment aimed to resolve a dispute in relation to an equity transfer agreement between the two parties, which was not in violation of the basic principles of PRC law and did not damage national sovereignty, national security and social and public interests;
- d. Although the U.S. Judgment was made in the absence of the Respondents, the evidence submitted by the Applicant certified that the LA Court had issued summonses to the Respondents in accordance with judicial procedures. The submitted evidence included an investigation request lodged by the Applicant against the Respondents, an LA Court order requiring the summonses to be served by public notice and the notice as issued in newspapers;
- e. Since the Case was heard for the purpose of rendering judicial assistance, the PRC court's review did not involve an examination of the substantial rights and obligations of the disputed parties. As a result, the Wuhan Court did not uphold the Respondents' defense arguments that

the equity transfer agreement was legitimate and effective and that the U.S. Judgment was flawed.

Legal rules and practice related to recognition and enforcement by PRC courts of foreign court judgments

The provisions under PRC law related to recognition and enforcement of a foreign judgment by the PRC government mainly refer to Articles 281 and 282 of the *Civil Procedure Law of the People's Republic of China* and related judicial interpretations.

Under Article 281 of the *Civil Procedure Law*, “[i]f a legally effective judgment or ruling made by a foreign court requires recognition and enforcement by a people's court of the People's Republic of China, the party concerned may directly apply for recognition and enforcement to the intermediate people's court with jurisdiction of the People's Republic of China. Alternatively, the foreign court may, pursuant to the provisions of an international treaty concluded between or acceded to by the foreign state and the People's Republic of China, or in accordance with the principle of reciprocity, request the people's court to recognize and enforce the judgment or ruling.”

According to Article 282 of the *Civil Procedure Law*, “Having received an application or a request for recognition and enforcement of a legally effective judgment or ruling of a foreign court, a people's court shall review such judgment or ruling pursuant to international treaties concluded or acceded to by the People's Republic of China or in accordance with the principle of reciprocity. If, upon such review, the people's court considers that such judgment or ruling neither contradicts the basic principles of the law of the People's Republic of China nor violates State sovereignty, security and the public interest, it shall rule to recognize its effectiveness. If enforcement is necessary, it shall issue an order of enforcement, which shall be implemented in accordance with the relevant provisions of the Law. If such judgment or ruling contradicts the basic principles of the law of the People's Republic of China or violates State sovereignty, security or the public interest, the people's court shall refuse to recognize and enforce the judgment or ruling.”

According to Paragraph 1, Article 544 of the *Interpretation of the Supreme People's Court on the Application of the Civil Procedure Law of the People's Republic of China*, “Where a party concerned applies to a competent intermediate people's court in the People's Republic of China for recognition and enforcement of a judgment or ruling which is rendered by a foreign court and is legally effective, and the country where the court is located does not conclude or participate in any international treaty or has reciprocal relations with the People's Republic of China, the intermediate people's court shall reject such application, unless the party applies to the people's court for enforcement of a divorce judgment which is rendered by a foreign court and is legally effective.”

Based on the above provisions, since China and the United States have not reached or acceded to any international treaty related to the mutual recognition and enforcement of each other's court judgments, the recognition and enforcement of a U.S. court judgment by a PRC court may only be

conditioned upon the existence of a reciprocal relationship between the two countries. Otherwise, a PRC court would generally refuse to recognize and enforce such foreign court judgments³. However, PRC law fails to clearly specify the criteria for determining whether a reciprocal relationship exists. In judicial practice, PRC courts strictly adopt the reciprocity principle, which means that a PRC court will determine that there exists a reciprocal relationship between China and the foreign country only if the PRC court confirmed there was a precedent of the foreign country's courts recognizing and enforcing PRC court judgments. Only under this circumstance could the PRC court recognize and have enforced a judgment rendered by a court in the foreign country⁴. Thus, it is difficult in practice for PRC courts to trigger the reciprocity principle. In fact, PRC courts have quite rarely recognized foreign court judgments absent an international treaty, and have not confirmed reciprocity in order to enforce such judgments absent the foreign court's preceding recognition and enforcement of a PRC court judgment⁵.

The influence of this case on judicial practice with respect to PRC court recognition and enforcement of U.S. court judgments

In this case, the Wuhan Court determined that a reciprocal relationship existed between China and the United States for the mutual recognition and enforcement of each other's civil judgments based upon a California U.S. District Court ruling in 2009 to recognize and enforce a commercial judgment rendered by the Hubei Higher People's Court in the case *Hubei Gezhouba Sanlian Company v. Robinson Helicopter Company* ("Sanlian Case"). The Wuhan Court ruled to recognize and enforce the U.S. Judgment because of this earlier U.S. court ruling. The Wuhan Court clearly made this ruling based upon the legal provisions and the reciprocity principle described above. The significance of the Case lies in that it is the first time for a PRC court to apply the reciprocity principle to recognize and enforce a commercial judgment rendered by a U.S. court. The Case sets an example for other PRC courts for how to deal with similar matters, or it at least demonstrates that it is possible to successfully apply to a PRC court for the recognition and enforcement of a commercial U.S. court judgment. This development will encourage more efforts to seek enforcement of U.S. court judgments in China.

³ For example: According to Reply of the Supreme People's Court on whether the People's Court of PRC shall Recognize and Implement the Judgements of Japanese Courts on Credit and Debt Disputes ([1995] Min Ta Zi No. 17): "Since China and Japan have not concluded or acceded to any international treaty for mutual recognition and enforcement of each other's court rulings, and the two countries have not established reciprocal relationship in relation to such mutual recognition and enforcement ... People's Courts of the PRC shall not recognize and implement the ruling of Japanese courts."

⁴ For example, the Nanjing Intermediate People's Court accepted an application submitted by Kolmar Group AG and Sutex Group to recognize and enforce a Singapore High Court civil judgment because the court found that there was a reciprocal relationship between China and Singapore since a Singaporean court had once recognized and enforced a PRC court judgment.

⁵ During past two years, PRC courts have relaxed somewhat on this position. For example, as stipulated in the *Several Opinions of the Supreme People's Court on the Provision of Judicial Service and Guarantee by People's Courts for the "One Belt and One Road" Construction (2015)*: "Some countries along the route that have not yet concluded a judicial assistance agreement with China, PRC courts may, based upon mutual intent to establish international judicial cooperation and the commitment of the other countries as to provide reciprocal judicial assistance, consider to take the initiative to render judicial assistance to relevant parties from the corresponding country, so as to promote the establishment of reciprocal relations between the two countries."

However, in practice, PRC courts have discretion, albeit limited, to determine whether reciprocity exists between China and the foreign country, since there are no clearly establishment criteria provided under PRC Law. Unlike under the common law system, judgments made by PRC local courts lack binding effect. Thus, we cannot theoretically rule out the possibility that a PRC court may reject an application to recognize and enforce a U.S. court judgment because the court is not bound to rely upon the Sanlian Case in determining that a reciprocal relationship exists between China and the United States, or because the court determines that the previously existing reciprocal relationship had been terminated for any reason (for example, a U.S. court had refused to recognize and enforce other PRC court judgments following the Sanlian Case).

Finally, it is worth mentioning that the reason that the U.S. court ruled to recognize and enforce the PRC court judgment was not based upon the reciprocity principle or to take the lead in establishing a reciprocal relationship. In fact, the judgment was entered primarily based on the *Uniform Foreign-Money Judgments Recognition Act*, which did not take into account the existence of a reciprocal relationship in determining whether to recognize the PRC court judgment. Therefore, we have no reason to expect U.S. courts to engage in quid pro quo or enter into a virtuous cycle of reciprocity by consistently recognizing PRC court judgments in the future. In other words, we cannot expect a more positive attitude from U.S. courts for the recognition and enforcement of commercial PRC court judgments in the future, or for a more proactive stance with respect to PRC courts.

Attachment: Applicant Li Liu applies to have recognized and enforced a civil judgment rendered by a foreign court against Respondents Li Tao, Wu Tong

People's Republic of China

Wuhan Intermediate People's Court of Hubei Province

Civil Ruling

(2015) E Wuhan Zhong Min Shang Wai Chu Zi No. 00026

The Applicant: Li Liu, female, Han nationality, born on June 15, 1979, residing at No.90 Yi Fen Chang Dormitory, Hu Bin Nong Ken Group Company, Yueyanglou District, Yueyang, Hunan

Agent ad litem: Guanlin Chen, Hunan Jinqiu Law Firm.

The Respondent: Li Tao, female, Han nationality, born on November 6, 1986, residing at Room A, 4th Floor, Building 7, Zone B.C of Wanda Plaza, Wuhan Lingjiaohu, No.15 Tang Jiadun Road, Jiangnan District, Wuhan City, Hubei Province

Agent ad litem: Hang Chen, Hubei S&H Law Firm

The Respondent: Wu Tong, male, Han nationality, born on September 12, 1977, residing at Room A, 4th Floor, Building 7, Zone B.C of Wanda Plaza, Wuhan Lingjiaohu, No.15 Tang Jiadun Road, Jiangnan District, Wuhan City, Hubei Province

Agent ad litem: Hang Chen, Hubei S&H Law Firm

With respect to application of the Applicant Li Liu, which requests to have recognized and enforced the civil judgment rendered by a foreign court against the Respondents Li Tao and Wu Tong, the court accepted the case and organized a collegial panel in accordance with law on October 19, 2015. Subsequently, the court held two hearings, respectively, on December 25, 2015 and March 15, 2016. The Applicant Li Liu, his Agent ad litem Guanlin Chen, the Respondents Li Tao, Wu Tong and their jointly appointed Agent ad litem Hang Chen attended the hearings. The trial review of this case has been completed.

The Applicant claimed that: On December 22, 2013, the Applicant and the Respondent signed an equity transfer agreement, stipulating that Respondent would transfer 50% equity interest held by her in JIAJIA MANAGEMENT INC to the Applicant, for a consideration of US\$ 150,000. After the Applicant paid US\$ 125,000 to the Respondent as agreed, the Respondent absconded with the money. After reporting the situation to the local police, who declined to pursue the case, the Applicant filed a lawsuit in Los Angeles County Superior Court of California (the "LA Court"). The LA Court passed judgment No. EC062608 (the "Judgment") on July 24, 2015, ordering Respondents to refund to the Applicant US\$ 125,000, plus interest of US\$ 20,818 incurred thereupon before the trial (during the period between September 25, 2013 to May 25, 2015), plus a trial costs equal to US\$ 1,674, for a total of US\$ 147,492. The Judgment had come into effect, but the Respondents failed to comply. The Respondents are currently residing at Room A, 4th Floor, Building 7, Zone B.C of Wanda Plaza, Wuhan Lingjiaohu, No.15 Tang Jiadun Road, Jiangnan District, Wuhan City, Hubei Province and have assets available for enforcement in Wuhan. Given that the Judgment does not violate the basic principles of national sovereignty, security and social interests of China, in order to safeguard the legitimate rights and interests of the Applicant, the Applicant hereby requests the court to rule as follows: 1. Acknowledge the Judgment rendered by the LA Court should have legal effect in China; 2. Order the Respondents to pay to the Applicant the following amounts as specified in the Judgment: US\$ 125,000, plus interest incurred thereupon equal to US\$ 20,818, plus trial costs equal to US\$ 1,674, for a total of US\$ 147,492, which is equal to RMB 940,040.26 (calculated according to the exchange rate on September 12, 2015). Besides this, the Respondents should also pay to the Applicant the overdue interest incurred during the period from 25 May 2015 to the date of enforcement of the Judgment; 3. The Respondents should bear the fees and expenses related to the enforcement.

The Respondents Li Tao and Wu Tong claim that: 1. The Judgment passed by the LA Court does not have legal effect in the People's Republic of China, for the Respondents had not been served with notice to attend the trial where the adverse judgment was ruled against them; 2. the Respondents should not be required to refund the equity transfer price amount to the Applicant, since

the Equity Transfer Agreement signed between the Applicant and the Respondent is true, legitimate and effective. Thus, the Respondents request to dismiss the Applicant's application.

Upon review and consideration, this court has determined that the Respondent Li Tao and the Applicant Li Liu signed an Equity Transfer Agreement on September 22, 2013 in the United States, which provided that Li Tao would transfer to Li Liu a 50% equity interest which she held in JIA JIA MANAGEMENT INC (shares registered in California). Li Liu subsequently made two payments to the Respondent, respectively, on September 22, 2013 and September 25, totaling US\$ 125,000. According to bank account information submitted by Li Liu, a bank account owned by Wu Tong, the husband of Li Tao, was credited with US\$ 125,000 during the period between September 14 and October 16, 2013. Thereafter, Applicant Li Liu filed a lawsuit in the LA Court against the Respondents on July 17, 2014, on the grounds that the two Respondents illegally obtained the US\$ 125,000 by fabricating the equity transfer transaction. The case was entered under case no. EC062608. On October 7, 2014, the U.S. investigation company Rolan issued an investigation report with respect to the personal information and contact address of Respondents Li Tao and Wu Tong in the United States. The U.S. attorney was then entrusted by Applicant Li Liu to attempt delivery of the litigation materials to the address as stipulated in such investigation report, but the documents failed to be properly delivered to the recipients. On January 8, 2015, Judge William D. Stewart of the LA Court issued an order to permit delivery of the relevant summons and notice by making a public announcement in the SAN GABRIEL VALLEY TRIBUNE. The announcement was then published four times in the SAN GABRIEL VALLEY TRIBUNE on January 15, January 22, January 29 and February 5, 2015. On July 24, 2015, Judge William D. Stewart of the LA Court rendered the Judgment with Respondents in absentia. According to the LA Court opinion, since the LA Court served summonses to Respondents in accordance with procedures when the Respondents failed to appear before the LA Court to respond to the Applicant's complaint, the LA Court heard the case and entered the Judgment in Respondents' absence. Upon review and consideration of the case, the judge ordered Respondents Li Tao and Wu Tong to refund to Applicant Li Liu the amount of US\$125,000, plus interest incurred thereupon as of the date of Judgment equal to US\$ 20,818 (calculated from September 25, 2013 to May 25, 2015, at a daily rate of US\$ 34.24 per day), plus trial costs equal to US\$ 1,674, totaling US\$ 147,492. On the same day, the Judgment was filed by the U.S. attorney for Applicant Li Liu. According to the news report entitled the "PRC Court Ruling Recognized and Enforced in the United States for the First Time" (*China Law Journal*, January 2010 issue) submitted by the Applicant, the court confirms that a civil judgment was recognized and enforced by a U.S. court in a product infringement dispute rendered by the Hubei Higher People's Court in the case of *Hubei Gezhouba Sanlian Industrial Co., Ltd., Hubei Pinghu Travel Vessel Co., Ltd. v. United States Robinson Helicopter Co., Ltd.*

This court finds:

This case involves an application for the recognition and enforcement of a dispute ruling rendered by a foreign court. According to Article 281 of the *Civil Procedure Law of the People's Republic of*

China, “if a legally effective judgment or ruling made by a foreign court requires recognition and enforcement by a people's court of the People's Republic of China, the party concerned may directly apply for recognition and enforcement to the intermediate people's court with jurisdiction of the People's Republic of China. Alternatively, the foreign court may, pursuant to the provisions of an international treaty concluded between or acceded to by the foreign state and the People's Republic of China, or in accordance with the principle of reciprocity, request the people's court to recognize and enforce the judgment or ruling”. According to Article 282 of the same, “[h]aving received an application or a request for recognition and enforcement of a legally effective judgment or ruling of a foreign court, a people's court shall review such judgment or ruling pursuant to international treaties concluded or acceded to by the People's Republic of China or in accordance with the principle of reciprocity. If, upon such review, the people's court considers that such judgment or ruling neither contradicts the basic principles of the law of the People's Republic of China nor violates State sovereignty, security and the public interest, it shall rule to recognize its effectiveness. If enforcement is necessary, it shall issue an order of enforcement, which shall be implemented in accordance with the relevant provisions of the Law. If such judgment or ruling contradicts the basic principles of the law of the People's Republic of China or violates State sovereignty, security or the public interest, the people's court shall refuse to recognize and enforce the judgment or ruling.” In this case, the Respondents Li Tao and Wu Tong have real estate located in Wuhan, Hubei Province. This court, which is located in the place where the property subject to enforcement is situated and is within the place of habitual residence of the Respondents, has the jurisdiction over this case according to law.

Together with the application to recognize and enforce the foreign court Judgment, the Applicant Liu Li also submitted a certified copy of the Judgment issued by the LA Court and the Chinese translation thereof, which satisfies the procedural requirement for applying to recognize and enforce of a judgment rendered by a foreign court. Since the United States and China have not concluded or acceded to any international treaties related to mutual recognition and enforcement of each other's civil judgments, the Applicant's application should be reviewed based on whether there exists a reciprocal relationship between the two countries. According to the evidence submitted by the Applicant, U.S. courts have established a precedent to recognize and enforce civil judgments rendered by PRC courts. Thus, it is confirmed that there exists a reciprocal relationship between the United States and China for the mutual recognition and enforcement of each other's civil judgments. In addition, the Judgment rendered by the U.S. court aimed to resolve a dispute between the Applicant and the Respondents in respect of the equity transfer contract between the two parties, which did not violate the basic principles of PRC law or breach the national sovereignty, security and social public interest. As to the Respondents' defense that they did not receive the trial notice, the court finds that the Judgment clearly provided that the Judgment was made in the absence of the Respondents. According to evidentiary documents submitted by the Applicant, including the investigation report of the Respondents, a U.S. court may permit summonses to be delivered by making public announcements, including announcements issued in newspapers, and this court

confirmed that the LA Court had issued the summonses to the Respondents in accordance with that procedure. With respect to the Respondents' claim that requiring the court to find that the Equity Transfer Agreement between the two parties is true, legitimate and effective and thereby the Respondents should not be required to refund the transfer price, the court believes that since this case was heard for purposes of judicial assistance, the court's review shall not involve the review of substantial rights and obligations of the two parties. Given that the LA Court has ruled with respect to the effectiveness of the agreement, the Respondents' claim in this regard cannot be upheld.

Therefore, the Applicant's application requesting to recognize and enforce the Judgment rendered by the LA Court is sustained by this court. However, another claim of the Applicant requesting the Respondents to pay overdue interest incurred during the period from May 25, 2015, the day when the LA Court issued the ruling, to the date of enforcement of the U.S. Judgment, is not sustained by the court, since it does not fall within the scope of review when considering an application for the recognition and enforcement of a foreign court judgment.

Upon review by the collegial panel, and in accordance with item (11), Paragraph 1, Article 154, Article 281 and 282 of the *Civil Procedure Law of the People's Republic of China*, Paragraph 1, Article 543 and Paragraph 1, Article 546 of the *Interpretation of the Supreme People's Court on the Application of Civil Procedure Law of the People's Republic of China*, this court ruled as follows:

1. The Judgment rendered by the LA Court is hereby recognized and to be enforced;
2. All other requests made by the Applicant Li Liu are hereby dismissed.

The application fee equal of RMB 100 for this case shall be borne by the Respondents Li Tao and Wu Tong.

The presiding judge: Qianxi Zhao

Judge: Jie Yu

Judge: Yanhong Xiong

Date: June 30, 2017

Clerk: Lei Xu



Important Announcement

This Newsletter has been prepared for clients and professional associates of Han Kun Law Offices. Whilst every effort has been made to ensure accuracy, no responsibility can be accepted for errors and omissions, however caused. The information contained in this publication should not be relied on as legal advice and should not be regarded as a substitute for detailed advice in individual cases.

If you have any questions regarding this publication, please contact:



Contact Us

Beijing Office

Tel.: +86-10-8525 5500
9/F, Office Tower C1, Oriental Plaza
No. 1 East Chang An Ave.
Beijing 100738, P. R. China

Estella CHEN Attorney-at-law

Tel.: +86-10-8525 5541
Email: estella.chen@hankunlaw.com

Shanghai Office

Tel.: +86-21-6080 0909
Suite 5709, Tower 1, Plaza 66, 1266 Nanjing
West Road,
Shanghai 200040, P. R. China

Yinshi CAO Attorney-at-law

Tel.: +86-21-6080 0980
Email: yinshi.cao@hankunlaw.com

Shenzhen Office

Tel.: +86-755-3680 6500
Room 2103, 21/F, Kerry Plaza Tower 3, 1-1
Zhongxinsi Road, Futian District, Shenzhen
518048, Guangdong, P. R. China

Jason WANG Attorney at-law

Tel.: +86-755-3680 6518
Email: jason.wang@hankunlaw.com

Hong Kong Office

Tel.: +00852-2820 5600
Suite Rooms 2001-02, 20/F, Hutchison
House, 10 Harcourt Road, Central,
Hong Kong, P. R. China

Dafei CHEN Attorney at-law

Tel.: +852-2820 5616
Email: dafei.chen@hankunlaw.com