Local Courts as Legislators? Judicial Lawmaking by Subnational Courts in China

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Abstract:

The focus of this article is on an important, albeit understudied, aspect of the rising judicial creativity in China, that is, the evolving nonadjudicative, legislative role of the local courts. The article argues that Chinese subnational courts, in particular the provincial-level courts, have lived in a constant tension between the long-standing aversion to local courts' engagement in the business of judicial lawmaking on the one hand, and on the other, the demand for rules to fill the gap caused by inadequate responsiveness to local economic affairs on the part of the national-level lawmaking agencies. One surviving strategy that local courts have developed is to enact much-needed legal rules in the hope of ensuring consistent outcomes in factually similar cases. Due to ideological and institutional constraints, however, the local courts have attempted to downplay this lawmaking role that they have developed and portray it as part of their routine, quotidian, dispute-resolution function. This inevitably creates a gap between the reality of judicial lawmaking and the official rhetoric denying judicial lawmaking a place in the formal legal order in China.

Rezumat:

Obiectivul acestui articol este asupra unui aspect important al creativității judiciare în creștere în China, nestudiat, respectiv rolul legislativ în evoluție, neafirmat, al instanțelor locale. Articolul invocă faptul că instanțele naționale chineze, în particular instanțele provinciale, au funcționat într-o constantă tensiune între vechea aversiune față de angajamentul instanțelor locale în activitatea de legiferare judiciară, pe de o parte, și, pe de altă parte, cererea pentru norme, în vederea umplerii golului cauzat de răspunsul inadecvat la afacerile economice locale, din partea autorităților legiuitoare la nivel național. O strategie de supraviețuire pe care instanțele locale au dezvoltat-o este aceea de a aplica normele juridice, atât de necesare, în speranța de a asigura rezultate coerente în situații de fapt similare. Urmare a constrângerilor ideologice și instituționale, instanțele locale au încercat să minimalizeze acest rol de legiferare pe care l-au dezvoltat și să înfățișeze funcția de soluționare a litigiilor ca parte din rutina

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lor, cotidiană. Astfel, s-a creat în mod inevitabil un decalaj între realitatea de legiferare judiciară și retorica oficială de a nega legiferării judiciare un loc în ordinea juridică internă din China.

Keywords: judicial creativity, judicial lawmaking, Chinese courts

Introduction: Statute Law and Judge-Made Law through the Comparative Lens

The relationship between the roles of the legislature and of the judiciary in the development of law in a legal system is a subject of enduring interest. The traditional comparative law scholarship regards the different relationship between statute law and judge-made law, and in particular the different roles of the judge, as ones of the 'characteristic differences' between the common law and the civil law traditions.[2] In the conventional view, civil law is mostly a codified system where the role of the judge is primarily to interpret and apply a written body of statutes, whereas common law is made and developed in large part by judges through judicial precedents, not legislators.[3] This traditional dichotomy between common law as judge-made law and civil law as code law plainly 'oversimplifies and misrepresents,'[4] and it has been challenged by a large and growing literature. It is true that the interrelationship between legislation and judge-made law differs from one jurisdiction to another; so does the role of the judge in the creation, formation and development of legal rules. This difference is, however, more of degree than of fundamental nature.

We consider briefly some of the major Western jurisdictions. In the US legal system, there is a strong recognition of the lawmaking role of judges, and 'the proposition that changing the law is properly and exclusively the function of the legislature runs counter to [the American] tradition.'[5] As Posner forcefully puts it, 'appellate judges are *occasional legislators.*'[6] By contrast, in the French legal system, the official emphasis is predominantly on statute law. The most foundational premise of the French legal order is, according to Lasser, that 'the legislature, and the legislature alone, is supposed to lawmaking power. Judges *must not*... usurp this legislative lawmaking power, on which the legislature possesses a monopoly.'[7] Despite this official hostility toward judicial lawmaking, French judges are known to have played 'a highly significant role in the elaboration, development, and modification of normative rules' to the extent of developing a vast body of *jurisprudence*, the French equivalent to case law.[8]

[2] K Zweigert and H Kotz *Introduction to Comparative Law* (3rd edn Oxford University Press 1998).

[3] J Goldsworthy The Sovereignty of Parliament: History and Philosophy (Clarendon Press 1999).

[4] JH Merryman and R Pérez-Perdomo *The Civil Law Tradition: An Introduction to the Legal Systems of Europe and Latin America* (Stanford University Press 2007) 27.

[5] PS Atiyah and RS Summers *Form and Substance in Anglo-American Law: A Comparative Study in Legal Reasoning, Legal Theory, and Legal Institutions* (Oxford University Press 1987) 136–37.

[6] RA Posner *How Judges Think* (Harvard University Press 2008).

[7] MDS-O-L'E Lasser Judicial Deliberations: A Comparative Analysis of Judicial Transparency and Legitimacy (Oxford University Press 2004) 168–69.

[8] Some areas of French law, such as nonfault liability law and administrative law, are in essence judge-made law. See J Bell *Judiciaries within Europe: A Comparative Review* (Cambridge University Press 2006) 70–72; M Shapiro *Courts: A Comparative and Political Analysis* (University Of Chicago Press 1981) 136–44.

Indeed, jurisprudence is so significant to the French legal system that its relationship with statute law is, arguably, one of complementarity, rather than subordination.[9]

If the American legal system stands at one end of the spectrum and the French legal system, at the other, the English legal system occupies the middle ground. There is an emphasis on both legislation and common law as major sources of law. The English common law system is judge-made and continues to be developed by the judiciary.[10] Yet, legislation passed by Parliament has gradually transcended common law in its importance.[11] Case law has always been secondary to primary legislation, and legislation can change or abolish existing common law. And English courts are often reluctant to make major legal changes, and generally take the view that such changes should be left to Parliament.[12]

The Case of China

Our brief comparative survey seems to point to a gradual convergence of civil law and common law toward a mixed system where legislation and judicial lawmaking are complementary sources of law. This brings us to the case of China, which remains largely absent from the current literature on the interrelationshipbetween legislation and judge-made law. The Chinese legal system is deeply rooted in the civil law tradition.[13] The primary source of law has been national legislation enacted by the National People's Congress (NPC) and its Standing Committee, as well as the local legislation passed by local people's congresses.[14] It was not until the early 1980s that the Supreme People's Court (SPC) - the highest-level court in China - was officially allowed to issue binding interpretations of primary legislation passed by the NPC and its Standing Committee.

Since then, the SPC has started to play a pivotal role in the development of the Chinese law. The SPC has deployed its interpretative powers in ways that enable it to fill the gap left by primary legislation.[15] This 'legislative' role, though controversial, has been embodied in the making of judicial interpretations that are regarded to have the same force as law, at least in court proceedings. A less obvious manifestation of the SPC as an occasional legislator is its creation of judicial 'precedents' - traditionally by publishing selected cases in the SPC Gazette[16] and, more recently, by introducing a 'guiding cases' system[17] - to which lower courts tend to pay close attention and, perhaps, follow.

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[9] E Steiner *French Law: A Comparative Approach* (Oxford University Press 2010) 104–10.

[10] '[J]udges make and change the law. The whole of common law is judge-made and only by judicial change in the law is the common law kept relevant in a changing world.' *Kleinwort Benson* v. *Lincoln City Council* [1999] 2 AC 349 at 358 (Lord Browne-Wilkinson).

[11] R Ward and A Akhtar *Walker & Walker's English Legal System* (11th edn Oxford University Press 2011); K Malleson and R Moules *The Legal System* (4th edn Oxford University Press 2010).

[12] Atiyah and Summers, above n 4 at 134–50; 'Editorial' (2011) Statute Law Review 32, iii.

[13] A Chen *An Introduction to the Legal System of the People's Republic of China* (4th edn LexisNexis 2011); J Chen *Chinese Law: Context and Transformation* (Martinus Nijhoff Publishers 2008).

[14] PH Corne 'Creation and Application of Law in the PRC' (2002) AJCL 50, 369.

[15] R Peerenboom *Courts as Legislators: Supreme People's Court Interpretations and Procedural Reforms* (The Foundation for Law, Justice and Society 2007).

[16] N Liu "Legal Precedents' with Chinese Characteristics: Published Cases in the Gazette of the People's Republic of China' (1991) Journal of Chinese Law 5, 107.

[17] See Stanford Law School newly launched China Guiding Cases Project, available at https://cgc.law.stanford.edu/ (accessed 10 January 2012).

The Chinese experience has important implications for the comparative literature on the interrelationship between legislation and judge-made law. Even in a jurisdiction where the emphasis is predominantly on legislation as the primary source of law, judicial lawmaking, both at the national and subnational levels, is inevitable in areas of law in which legislation fails to meet the rising demands for legal rules.

Whereas the SPC assumes an active judicial lawmaking role at the national level, a distinctive feature of the Chinese economy - economic decentralization - dictates that attention also be given to judicial creativity of the Chinese *local* courts. It has been widely accepted that governance in post-Mao China is characterized by a combination of political centralization and economic decentralization.[18] On the one hand, the Chinese central government has maintained highly centralized control over political and personnel matters, whereas on the other hand, it has adopted a relatively hands-off approach toward the administration of the economy. On a practical level, this has resulted in local authorities playing a dominant role in local economic affairs, including the protection of property rights and the resolution of economic disputes, in their jurisdiction.

Traditionally, local courts are tasked only to apply existing laws, regulations, and the SPC rules in a passive and mechanical fashion. The fast-increasing volume, complexity, and ever-changing nature of local economic activities has, from time to time, given rise to novel legal issues that fall outside the expected parameters of the tasks of such local courts. At the national level, the less-than-sophisticated legal framework fails to contemplate ex ante or to respond in an effective and efficient manner ex post to these issues, and thus local courts gradually come to assume a role in the formation of legal rules by addressing issues of significance in their particular locality. Local courts at almost all levels have engaged in judicial innovation in their routine handling of individual cases, a practice that has become the subject of an emerging literature.[19]

An important, albeit understudied, aspect of the rising judicial innovation is the evolving *nonadjudicative*, *legislative* role of local courts. The focus of this article is on the judicial creativity taking place outside of the courts' routine judicial decision-making process. It takes the form of normative documents that interpret the national-level legislation and, more significantly, create legal rules with only vague, and sometimes virtually no, statutory basis. These documents are typically enacted by the provincial-level higher people's court (HPC), and sometimes by lower courts. They tend to be highly authoritative for, and, in effect, binding on, all courts within the issuing HPC's jurisdiction, including the HPC itself. The SPC has disapproved of this particular form of judicial innovation, aut

[18] See PF Landry *Decentralized Authoritarianism in China: The Communist Party's Control of Local Elites in the Post-Mao Era* (Cambridge University Press 2008); C Xu 'The Fundamental Institutions of China's Reforms and Development' (2011) The Journal of Economic Literature 49, 1076.

[19] BL. Liebman 'Innovation through Intimidation? An Empirical Account of Defamation Litigation in China' (2006) Harvard International Law Journal 47, 33; W Chenguang 'Law-making Functions of the Chinese Courts: Judicial Activism in a Country of Rapid Social Changes' (2006) Frontiers of Law in China 4, 524; TE Kellogg '"Courageous Explorers"?: Education Litigation and Judicial Innovation in China' (2007) Harvard Human Rights Journal 20, 141; NC Howson 'Corporate Law in the Shanghai People's Courts, 1992–2008: Judicial Autonomy in a Contemporary Authoritarian State' (2010) East Asia Law Review 5, 303.

of concerns about, according to the official rhetoric, 'unity and uniformity of the legal system,' that is, the risks associated with decentralization in the lawmaking role. Yet, notwithstanding the SPC's aversion to local judicial lawmaking, both the number and the frequency of HPC-enacted normative documents governing economic affairs (e.g. contract, company, and labor issues) have been on the rise in actuality. With particular reference to court-made rules on corporate law matters prior to China's sweeping legislative reform in 2005, the following section demonstrates the practices of local judicial lawmaking in China.

Local Judicial Lawmaking on Corporate Law Matters: A Narrative

The pre-2005 Company-Law regime in China sets a perfect stage for local judicial lawmaking. National-level lawmaking agencies, in particular the Standing Committee of the NPC, did not achieve much in devising and developing sophisticated corporate law rules before 2005. The 1993 Company Law, China's first national company legislation, was designed to oil the wheels of the state-owned enterprise (SOE) reform[20] and has been widely criticized for its primitiveness, generality, vagueness, and obscurity. Many of its provisions were not readily enforceable, and loopholes were easily discernable. To be fair to the SPC, it made a serious attempt to close the legislative gaps almost a decade after the enactment of the 1993 Company Law. In November 2003, the SPC released a draft judicial interpretation for public consultation. The SPC document was entitled the Regulations on Several Issues Concerning the Adjudication of Cases Involving Company Disputes (I) ('2003 Draft Interpretations').[21] The 2003 Draft Interpretations were scheduled to be adopted for formal implementation in 2004. This did not happen, presumably because of the unanticipated NPC decision in 2004 to elevate the long-awaited revision of the 1993 Company Law to the top of the legislative agenda.[22]

Thus, local courts were left in a position where they had to apply the 1993 Company Law without having much guidance from the SPC, even though the 2003 Draft Interpretations provided a somewhat useful reference point on certain issues. A number of HPCs had risen to the challenge of legal lacunas. They enacted their own normative documents, setting out more detailed corporate legal rules prior to the sweeping 2005 company law reform. These include the Opinions Concerning Several Issues on the Adjudication of Cases Involving the Application of the Company Law (On Trial Application),[23] issued by Jiangsu HPC in 2003 (hereinafter, 2003 Jiangsu Opinions), Opinions Concerning Several Issues on the Adjudication of Company Related Cases,[24] issued by Shanghai HPC in 2003 (hereinafter, 2003 Shanghai Opinions I), and Guiding Opinions

[20] RC Art and M Gu 'China Incorporated: the First Corporation Law of the People's Republic of China' (1995) Yale Journal of International Law 20, 274; D Clarke 'Corporate Governance in China: An Overview' (2003) China Economic Review 14, 494.

[21] Guanyu shenli gongsi jiufen anjian ruogan wenti de guiding (yi) (zhengqiu yijian gao), promulgated by the SPC at its own official web site on 3 November 2003 and at the People's Court Daily and the China Securities News on 5 November 2003.

[22] L Ye *Gongsifa yanjiu* [*Studies on Company Law*] (Renmin University Press 2008) 112.

[23] *Guanyu shenli shiyong gongsifa anjian ruogan wenti de yijian (Shixing)*, passed by the Adjudication Committee of the Jiangsu Provincial HPC on 3 June 2003.

[24] *Guanyu shenli sheji gongsi susong anjian ruogan wenti de chuli yijian*, issued on 12 June 2003.

Concerning Several Issues on the Adjudication of Company Disputes (On Trial Implementation),[25] issued by Beijing HPC in 2004 (hereinafter, 2004 Beijing Opinions).

Not all pre-2005 local normative documents on company law matters were issued in the name of the provincial HPC. Some were issued by the HPC's Second Civil Division - the court chamber responsible for the adjudication of company law cases. For instance, in 2002, the Second Civil Division of the Zhejiang HPC made the Understandings Concerning Several Issues on the Application of the Company Law[26] (hereinafter, 2002 Zhejiang Opinions) for 'internal reference' by local courts in Zhejiang Province. Following the 2003 Shanghai Opinions I, the Second Civil Division of the Shanghai HPC promulgated two supplementary documents in December 2003 (hereinafter, 2003 Shanghai Opinions II) and in March 2004 (hereinafter, 2004 Shanghai Opinions), respectively.

These normative documents differ considerably in length and scope. The 2003 Jiangsu Provisions is by far the most comprehensive one. Consisting of 79 articles, it covers a large number of issues ranging from the general principles for adjudicating company-related disputes, to the classification of company disputes, to more specific aspects of company law. At the other end of the spectrum lies the 2004 Shanghai Opinions, which contains merely eight articles dealing with concrete issues. The normative documents also vary considerably in their treatment of substantive legal issues. The 2003 Jiangsu Opinions is relatively formal in format, and it gives clear, unambiguous and direct instructions on how certain legal issues are to be handled. On the other hand, the 2002 Zhejiang Opinions is featured with its contextualized account of the rationales behind its provisions and, interestingly, references are explicitly made to comparative experience in other jurisdictions to justify some of its provisions.

On a closer look, the provisions in these normative documents serve different purposes and require varying levels of creativity. Judging by their functionality and their degrees of novelty, these provisions can be broadly categorized into four discrete, and to some extent overlapping, types: (i) provisions that determine the applicable law for certain legal issues; (ii) provisions that ascertain the meaning of an obscure or equivocal statutory rule; (iii) provisions that fill the gaps in the company legislation, and (iv) provisions that create new rules with no express statutory backing, to which we now turn to.

A small number of provisions in the HPCs' normative documents are little more than a suggestion as to which law to apply in a particular circumstance. An example is Article 55 of the 2003 Jiangsu Opinions, which makes a not very creative statement that, in determining the validity of share transfer transactions, the 1986 General Principles of Civil Law, the 1999 Contract Law, and the 1993 Company Law shall apply and that reference is allowed to be made to administrative rules pertaining to the 1993 Company Law.[27] There are, of course, more sophisticated

[25] *Guanyu shenli gongsi jiufen anjian ruogan wenti de zhidao yijian (shixing)*, passed by the Adjudication Committee of the Beijing HPC on 9 February 2004.

[26] *Guanyu gongsifa shiyong ruogan yinan wenti de lijie*, in D Jiang (ed) *Gongsifa Baogao (Er)* [*Company Law Report (Vol II)*] (CITIC Publishing House 2003) 457.

[27] It is fair to point out that Art. 55 is followed by a set of more specific rules on ascertaining the validity of share transfer contracts.

rules on the issue of applicable law. Article 21 of the 2004 Beijing Opinions, for instance, deals with an issue that has created controversies in practice: the applicability of the 1993 Company Law to foreign investment enterprises (FIEs). For many reasons, China has created and continues to sustain a separate legal regime for FIEs, independent of and parallel to the company legal framework. There are discernable inconsistencies and contradictions between the two regimes.[28] Article 18 of the 1993 Company Law provided that the Law applied to 'limited-liability companies with foreign investment' and that FIE laws shall prevail if FIE laws provide otherwise. It was uncertain as to whether the 1993 Company Law should apply if FIE laws are silent, and in practice, some government agencies opted not to apply the 1993 Company Law to FIEs at all.[29] Article21 of the 2004 Beijing Opinions clarifies that in the absence of FIE laws, the 1993 Company Law shall apply.

Making interpretation of equivocal provisions in the company legislation is the second important function of these normative documents. Article 60(3) of the 1993 Company Law provided that the company's directors and executives shall not give the company's property in security for the personal debts of either the company's shareholder or any third parties. Clearly, it was not within an individual director's power to enter into a security agreement under which a security interest is given over the corporate assets in favor of the shareholder or a (typically, connected) third party. One could interpret Article 60(3) to mean that the board of directors also did not have the power to bind the company with such a security agreement, as the board is, after all, composed of individual directors whose hands are tied by Article 60(3). This was the SPC's reading of Article 60(3) in a widely reported case adjudicated by the SPC in 2001.[30] An alternative interpretation was that Article 60(3) only prohibited directors from acting individually to create a security interest in the shareholder's favor and that the directors acting collectively as the board have the power to so act as they see fit, perhaps subject to approval by the shareholders. Ironically, this alternative understanding of Article 60(3) was subsequently adopted in 2004 by the SPC in a factually similar case.[31] In the face of this dilemma, Article 5 of the 2003 Shanghai Opinions II opts for the latter interpretation. It clearly stipulates that ex ante approval by the shareholders' meeting would enable directors or executives to attach a security interest to corporate assets to satisfy the personal debts of the shareholder.

The bulk of provisions in the normative documents serve to fill the gaps in the 1993 Company Law. The 1993 Company Law (Articles 43 and 104) conferred a duty upon the board to convene the shareholders' meeting under the circumstances and in the manner prescribed by the Company Law and the articles of association. The Law was, however, silent as to remedies available. Article 13 of the

[28] A Yuan 'Foreign Direct Investments in China - Practical Problems of Complying with China's Company Law and Laws for Foreign-Invested Enterprises' (2000) Northwestern Journal of International Law and Business 20, 475.

[29] Ibid, 485.

[30] *Fujian Province Zhongfu Industrial Joint Stock Ltd Co* v. *Industrial and Commercial Bank of China, Fuzhouv Municipality Mindu Subbranch* (2000) Jingzhong zi No 186. The judgment was issued by the SPC on 17 November 2001.

[31] *China Construction Bank, Fuzhou Municipality Chengbei Subbranch* v. *Yunsheng (Shanghai) Industrial Joint Stock Ltd Co & Fujian Province Zhongfu Industrial Joint Stock Ltd Co* (2003) Min'er Zhongzi No 199. The judgment was delivered by the SPC on 19 March 2004.

2003 Jiangsu Opinions closed in part the loophole by providing that shareholders may petition the court to cause the meeting to be held and that the defendant in the proceeding would be the company.

The most significant aspect of the normative documents is their creation of new legal rules with only vague, and sometimes virtually no, statutory foundation. As will be demonstrated below, local courts tend to rely on general legal doctrines and principles when developing these new rules. The most salient examples are the rules on veil piercing and on derivative actions.

(A) Local Judicial Rules on Piercing the Corporate Veil

Limited liability is a bedrock principle of modern corporate law.[32] Shareholders of a corporation are generally not liable for the obligations of the corporation beyond their investments in the corporation. Limited liability has never been, however, as absolute as it purports to be. Creditors of insolvent corporations may ask courts to, under a judicially developed doctrine known as 'piercing the corporate veil' or 'lifting the corporate veil,' disregard the corporate form and hold a shareholder personally responsible for the corporation's obligations. The doctrine of piercing the veil exists as a check on the principle of limited liability, and it prevents shareholders from using limited liability to achieve illegitimate ends.

Prior to the enactment of the 2003 Draft Interpretations, the SPC had developed some judicial rules under which the shareholders of a company who violate the statutory registered capital rules and capital maintenance rules could be held personally liable for the debts of the company. These rules are, however, not in a strict sense veil-piercing rules, as the shareholder's liability under these rules is, in most cases, not beyond the extent of their stated investments. Only in very limited circumstances can shareholders defrauding the company's creditors be held liable for the company's debts beyond their stated investments in the company, that is, the registered capital.[33]

The 2003 Draft Interpretations marked a major step forward in the SPC attempt to develop a more fully fledged veil-piercing regime. A test of separateness was laid down in determining whether or not the privilege of limited liability has been abused. More specifically, under the 2003 Draft Interpretations, the company and its controlling shareholder would be seen to have no separate existence and, consequently, the shareholder 'bears joint liability' for the corporate debts under three circumstances. First, the corporate income is not separated from the controlling shareholders' own income, thus resulting in the commingling of accounts. The second circumstance is where the company and its controlling shareholder commingle business funds with personal funds, and they continuously use the same accounts. The third circumstance is that there is a constant commingling of corporate business and personal business, and the company's business transactions are under complete control of the controlling shareholder.[34]

Some HPCs also developed their own veil-piercing rules prior to and, perhaps independent of, the 2003 Draft Interpretations. Shanghai HPC is among the first that made rules holding abusive shareholders directly liable for the obligations of the company. The 2003 Shanghai Opinions I provides for a cause of action for the company's creditors

[32] R Kraakman and others *The Anatomy of Corporate Law: A Comparative and Functional Approach* (2nd edn Oxford University Press 2009) 5.

[33] C Xi 'Piercing the Corporate Veil in China: How Did We Get There?' (2011) JBL 55, 413.

[34] *Ibid.*

against shareholders whose acts constitute an abuse of the corporate form and, consequently, result in the company being unable to fulfill its obligations in full.[35] The Opinions proceeds to canvas four circumstances where the court could hold shareholders personally liable for the company's acts.[36] The first three circumstances are no more than a restatement of the SPC's preexisting rules described above. The provision for the fourth circumstance bears, however, an innovative element: Where there is a commingling of the shareholder's assets or business with the corporate assets or business, the corporation's personality is deemed to have been 'merged' with that of the shareholder and no longer separately exists. Under this circumstance, the shareholder shall bear joint and unlimited liability for the company's debts and other obligations.[37] Apparently, this provision does not derive from any preexisting statutory provision or SPC judicial interpretations - the 2003 Draft Interpretations was only publicized a few months later. In justifying this innovative legal rule, the Opinions label, perhaps mistakenly, the commingling of corporate and shareholder assets and business as a form of (unlawful) 'connected transaction.' This mischaracterization was soon rectified by the Shanghai HPC in its subsequent 2003 Opinions II. Here, the Court indicated that the basis for holding the controlling shareholder[38] liable for the corporate acts is the doctrine of bona fide and the doctrine of abuse of rights, two doctrines that are enshrined in the 1986 General Principles of Civil Law.[39]

The 2002 Zhejiang Opinions represents another attempt made by HPCs to develop veil-piercing rules with little guidance from the primary company legislation and the SPC. Article 19 - the veil-piercing provision in the Opinions - starts with a statement on the doctrinal foundation for imposing personal liability on shareholders: 'Separate corporate legal personality is a fundamental precondition for a company to engage in civil activities. And disregarding corporate personality is indeed an identification and confirmation of the fact that [a company] has already lost its status of a separate legal person. Where the existence of [a company's] separate personality contradicts the intent and purpose of granting personality [to the company] in the first place, justice, as embodied in the law, necessarily requires piercing the corporate veil of the company that already has no independent existence.'

Here, the Zhengjiang HPC seemed to suggest that (i) the fundamental principle of justice, on its own, allows courts to disregard the separateness of the company and its shareholders if the circumstances warrant it and (ii) courts do not have to rely on any particular statutory doctrines in so ruling. In defense of this novel approach to veil piercing, the Court added that 'disregarding corporate legal personality has become a legal doctrine commonly recognized by many civil law and common law jurisdictions.'

(B) Local Judicial Rules on Derivative Actions

When directors, management, or others in control of a company are in breach of their duties and legal obligations owed to the corporation and thus injure the company, litigation can be instituted against wrongdoers to remedy the injury.

[35] Art. 4(1), 2003 Shanghai Opinions I.

[36] Art. 4(2), 2003 Shanghai Opinions I.

[37] *Ibid.*

[38] 'Controlling shareholders' is defined as 'shareholders who are actually involved in the corporate operation and management, and can influence major corporate decision-making,' and controlling shareholders 'can be, but are not limited to, shareholders who control the majority of the votes.' Art. 5(1), 2003 Shanghai Opinions II.

[39] Arts. 4 and 7.

The litigation decision is usually left to the board of directors or the shareholders as a whole, which may, because of either self-interest or neglect, not pursue litigation against alleged wrongdoers even it is in the best interest of the company to do so. Judicial rules have developed since 1843, when the *Foss* v. *Harbottle*[40] principle was formulated, to give individual shareholders the standing to pursue litigation on behalf of the company. Derivative suits have been seen as an important remedial and deterrent device to rectify and prevent management abuses and to protect minority shareholders.[41]

There was no express statutory basis for derivative lawsuits under Chinese law prior to the 2005 company law reform.[42] In 1994, the SPC issued a circular under which a party to a Sino–foreign equity joint venture was given the standing to bring an action derivatively on behalf of the joint venture in order to enforce a claim that the board of directors refused to enforce. Despite its limited applicability, the circular has been seen as an indication that the SPC would allow some form of derivative litigation in narrowly tailored circumstances.[43] The 2003 Draft Interpretations introduced a more fully fledged derivative suits system. Individual shareholders, subject to certain safeguards,[44] are given the standing to pursue litigation on behalf of the company against (i) directors, supervisors, managers, or other members of senior management who have infringed their duty of loyalty, damaged the interests of the corporation, and caused losses to the corporation, and (ii) controlling shareholders who have abused their controlling position and caused injury to the corporation.[45]

Again, some local courts went ahead of the SPC in 'codifying' the derivative claim into their normative documents. Zhejiang HPC, in its 2002 Zhejiang Opinions, affirmed that a shareholder might bring a derivative lawsuit, notwithstanding the provision made in Article 63 of the 1993 Company Law that the right to enforce a claim against wrongdoing directors, supervisors, and managers belonged to the corporation, not its shareholders.[46] The rationale underlying the provision is, as the Court rightly pointed out, that the wrongdoers often have control over the corporation and are most unlikely to seek relief against themselves. It appears that the Court was fairly sympathetic to derivative claims: It suggested that 'derivative lawsuits have only very recently emerged in China, qualification imposed on derivative suit plaintiffs should not be overly burdensome.' All existing shareholders can bring an action derivatively, and it is not required under the 2002 Zhejiang Opinions that they have been a shareholder at the time of the alleged wrongdoing as under the rule of contemporaneous ownership.[47] In order to bring a derivative suit, the plaintiff shareholder would only need to prove that the corporation has refused to enforce its cause of action on its own behalf.

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[40] (1843) 67 ER 189.

[41] JH Choper, JC Coffee Jr, and RJ Gilson *Cases and Materials on Corporations* (7th edn Aspen Publishers 2008) 825.

[42] J Deng 'Building an Investor-Friendly Shareholder Derivative Lawsuit System in China' (2005) Harvard International Law Journal 46, 347 at 355–65.

[43] Ibid, 365.

[44] Arts. 44, 45, and 47, 2003 Draft Interpretations. For a more thorough examination of these safeguards, see *Ibid.*

[45] Art. 43, 2003 Draft Interpretations.

[46] Art. 15, 2002 Zhejiang Opinions.

[47] Choper and others, above n 40 at 870.

The 2003 Shanghai Opinions I contains a more compressive set of rules on derivative claims. The Opinions first provides that the court accept cases brought by shareholders derivatively on behalf of the company against the controlling shareholders or senior officers whose misconduct has caused damage to the corporation.[48] Individual shareholder access to courts must not be denied, the Opinions reiterates, on the sole basis that the shareholders have no direct interest in the corporation's cause of action.[49] Like the 2002 Zhejiang Opinions, the Shanghai Opinions I requires that the plaintiff be an incumbent shareholder and that the wrongdoing controlling shareholders, officers, and interestingly, the counterparty to the challenged transactions be made defendants.[50] In deciding whether the claim is successful, five factors need to be considered by the court. First, whether actual damage has been caused to the corporation. Secondly, whether there is misconduct on the part of the defendant. Thirdly, whether there is a causal relationship between the corporation's loss and the defendant's misconduct. Fourthly, in the case that the counterparty to the transaction into which the corporation entered is made a defendant, whether the counterparty was acting in good faith. Lastly, whether the corporation refused to sue on its own behalf as it was controlled by the wrongdoers.[51] A derivative suit may not be settled, the Opinions further stipulates, without judicial approval. The court has to investigate whether the proposed settlement harms the corporation and its shareholders and, if so, rule against the settlement. With respect to the reimbursement of expenses, the court may order the corporation to indemnify the plaintiff shareholders against reasonable expenses incurred in connection with the lawsuit.

Local Judicial Lawmaking: Institutional Constraints and Incentives

The significance of local judicial corporate lawmaking, as described in the previous section, needs to be understood against the proclaimed position of the SPC in relation to local judicial lawmaking. The SPC has displayed an antipathy to the local courts' attempts to engage in the business of interpreting laws and regulations. One of the first manifestations of the SPC's disapproval of local judicial lawmaking can be found in a 1987 SPC Reply.[52] The Reply concerns a normative document adopted by the HPC of the Guangxi Autonomous Region, setting out the Court's policies on certain issues of real estate laws. While the Reply discusses at some length the inconsistency of some of these policies with the then-prevailing laws and policies, the emphasis is unambiguously on the more general issue of Guangxi HPC's practice of enacting and publicizing its own interpretations of laws and regulations. The Reply states: [This Guangxi HPC's document] possesses the characters of the SPC judicial interpretations, and it is inappropriate for local courts at any level to adopt [documents of this nature].

As to the practical need for the HPCs to address in a systematic manner novel, difficult, or complex legal issues, a proper

[48] Art. 5(1), 2003 Shanghai Opinions.

[49] Pre-2005 Chinese law required that in order to institute a lawsuit, a plaintiff must have a 'direct interest' in the claim. 1991 Civil Procedure Law.

[50] Art. 5(2), 2003 Shanghai Opinions I.

[51] *Ibid.*

[52] *Zuigao renmin fayuan guanyu defang geji fayuan buyi zhiding sifa jieshi xiangzhi wenjian wenti de pifu* [SPC Reply Concerning the Inappropriateness for Local Courts at Various Levels to Adopt Documents of the Nature of Judicial Interpretation], issued on 31 March 1987.

way forward, the Reply suggests that it is for the HPCs to present their preferred positions in the form of scholarly writings, such as journal articles, to which reference can be made where necessary. The Reply also identifies the practice of holding closed-door seminars for the purposes of building consensus on legal issues of local concern, as desirable.[53]

Despite the Reply, the practice of HPCs enacting interpretative, binding documents has continued to bloom.[54] China's accession to the World Trade Organization (WTO) in 2001 afforded the SPC an opportunity to assert greater control over local judicial lawmaking. With a view to ensuring compliance with China's commitments under the WTO, the central authorities orchestrated a nationwide campaign to have all preexisting laws, regulations, and rules thoroughly reviewed and, where necessary, revamped. As part of this campaign, the SPC issued a circular in 2001 instructing a 'cleaning up' by the local courts of the preexisting normative documents they enacted as to how given legal provisions should be applied.[55] In Tianjin, the HPC reportedly mobilized a massive, multistaged review of all preexisting documents issued by the three levels of local courts. Inconsistencies and contradictions were identified between some of these documents on the one hand and national laws, regulations, and judicial interpretations on the other. In enacting some of the documents under review, it was admitted, local courts had actually encroached on the legislative authority of the SPC. Consequently, among the 500-odd interpretative documents reviewed at the first stage, 94 were repealed.[56] In Ningxia Autonomous Regime, a similar exercise resulted in 10 local-court-made normative documents being revoked.[57]

The SPC's continued disapproval of local judicial lawmaking was clearly and unambiguously expressed by Justice Shen Deyong, Executive Vice-President of the SPC, in his recent address to presidents and other senior members of all HPCs at an SPC annual strategy conference held in December 2011. Justice Shen reportedly reiterated that subnational courts should refrain from enacting normative, binding documents interpreting laws and regulations. As for those documents already in existence, local courts were instructed to 'take the initiative to clean them up.'[58]

The SPC's long-standing aversion to local courts' enactment of general rules guiding the local application of laws seems to derive primarily from concerns about the 'unity and uniformity' of the legal system. Judge Wu Zhaoxiang, a senior judge in the SPC Research Office, remarked that subnational courts'

[53] *Ibid.*

[54] F Li 'Difang fayuan wuquan fabu sifa jieshixing wenjian' [Local Courts Do Not Have the Authority to Issue Judicial Interpretative Documents] *Fa xue* [*Legal Science*] (1998:2) 59 (suggesting that, in practice, HPCs enacted a large volume of judicial interpretative documents).

[55] *Guanyu qingli defang fayuan zixing zhiding de falu shiyong guifanxing wenjian de tongzhi* [*SPC Circular Concerning Cleaning Up Normative Documents on Application of Laws Enacted by Local Courts on Their Own Initiatives*].

[56] X Zhang and X Li 'Tianjin fayuan qingli falu shiyong guifanxing wenjian' [Tianjin Cleared up Normative Documents on the Application of Laws] *Zhongguo qingnian bao* [*China Youth Daily*] 10 May 2002.

[57] S Yang and B Wei 'Ningxia fayuan quanmian wancheng falu shiyongxing wenjian qingli gongzuo' [Ningxia Courts Fully Completed the Clearing Up of Normative Documents on the Application of Laws] *Ningxia Ribao* [*Ningxia Daily*] 22 March 2002.

[58] D Yuan 'Zuigaofa yaoqiu mingnian 8yuedi qian wancheng sifa jieshi jizhong qingli renwu' [SPC Ordered the Completion of Cleaning Up the Judicial Interpretations by August Next Year] *Fazhi Ribao* [*Legal Daily*] 24 December 2011.

interpretations of the same legal provision can vary greatly from one local court to another and that outright contradictions among these interpretations were not uncommon.[59] Thus, decentralization of judicial lawmaking to subnational courts, according to Judge Wu, can bring significant risks of 'undermining the authority of the law and the uniformity of the judiciary.'[60]

This gives rise to an intriguing question: What explains active engagement by some HPCs in judicial corporate lawmaking notwithstanding the SPC's expressed disapproval? An official report (Survey Report) by the Beijing HPC on the findings of its survey of all company law cases adjudicated by the three levels of local courts in Beijing between 2000 and 2003 offers a rare glimpse into the issue. Published in the *China Civil and Commercial Trial*, the SPC Second Civil Division's official periodical publication,[61] the Survey Report constitutes the very basis for the 2004 Beijing Opinions[62] and informs our discussion that immediately follows.

One plausible reason for the HPC's 'activism' in corporate lawmaking is the rising *demand* for corporate legal rules. Indeed, a key factual finding of the Beijing Survey was the sharp increase in the number of corporate disputes brought before the courts in Beijing between 2000 and 2003.[63] In 2000, local courts in Beijing accepted merely 56 corporate law disputes.[64] The company caseload started to rise exponentially to 132 in 2001, 427 in 2002, and 819 in 2003, representing an annual increase rate of 136, 223, and 92 per cent, respectively.[65] The caseload, despite its dramatic growth, does not seem to warrant the level of attention and efforts the Beijing HPC has demonstrated. After all, the company law caseloadb in 2000 (56 cases) represented only a negligible proportion (0.04 per cent) of the 139,629 civil and economic cases that first-instance courts in Beijing heard that year.[66] Even in 2003, when the number of company cases rose to close to the rank of 1000, it amounted to but a very modest 0.46 per cent of the total civil and commercial caseload in Beijing.[67]

The statistically insignificant company law cases posed, however, a great challenge that courts in Beijing had struggled hard to meet. Uncommon as they were before 2000, company law cases brought about a host of novel legal issues that local courts had not previously encountered. Judges, from time to time, found themselves in an awkward position,

[59] Z Wu 'Guanyu sifa jieshi gongzuo de guiding de lijie yu shiyong' [Interpretation and Application of the Regulations on the Work of Judicial Interpretations] *Renmin Sifa* [*People's Judicature*] (2007: 5) 29.

[60] *Ibid.*

[61] See Beijing Higher People's Court 'Guanyu shenli sheji gongsi jiufen anjian de diaocha yanjiu' [A Survey and Research on Adjudication of Cases Involving Company Related Disputes] in X Xi (ed) *Zhongguo Minshang Shenpan* [*China Civil and Commercial Trial*] (China Law Press 2006) 216.

[62] See Second Division of the Beijing Higher People's Court 'Beijingshi gaorenmin fayuan guanyu shenli gongsi jiufen anjian ruogan wenti de zhidao yijian (shixing) de shuoming' [Explanatory Note on the Guiding Opinions Concerning Several Issues on the Adjudication of Company Disputes (On Trial Implementation)] in X Xi (ed) *Zhongguo Minshang Shenpan* [*China Civil and Commercial Trial*] (China Law Press 2007) 23. [Hereinafter, Explanatory Note.]

[63] On the relationship between caseload change and socioeconomic conditions in the context of China, see H Xin 'The Recent Decline in Economic Caseloads in Chinese Courts: Exploration of a Surprising Puzzle' (2007) China Quarterly 190, 352.

[64] Survey Report, above n 60 at 216.

[65] *Ibid.*

[66] *2001 Beijing Nianjian* [*2001 Beijing Annals*] (Beijing Annals Press 2001) 163. This consisted of 112,120 civil cases and 27,509 economic disputes cases.

[67] *2004 Beijing Nianjian* [*2004 Beijing Annals*] (Beijing Annals Press 2004) 133. This comprised civil and commercial cases.

where the existing body of laws was utterly silent on some of those issues, examples of which included shareholders' derivative actions and piercing the corporate veil.[68] Nor was the existing scholarly research particularly helpful, as many of the issues were understudied.[69] Thus, courts in Beijing came to label company law cases as belonging to the class of 'difficult cases,' and some courts were not shy from admitting that they had insurmountable difficulties in handling company law cases.[70]

Facing the rising tide of company law cases, courts in Beijing labored to resolve newly emerging legal issues, mostly on their own and in an uncoordinated manner.[71] This led to what the Beijing HPC identified as a systemic problem: inconsistencies, and sometimes contradictions, between individual courts' approaches to the same legal issue. For instance, on the issue of the validity of a share transfer contract, the performance of which results in a company having fewer than two members,[72] some courts in Beijing held the contract to be valid, whereas other courts ruled it to be invalid.[73] Such marked instances of courts giving inconsistent and, even worse, contradictory verdicts on the same matter, the Survey Report rightly cautions, only served to undermine the authority of the courts.[74]

Thus, company legal rules that are capable of being readily identified and consistently applied by the local courts in resolving company law cases were evidently in demand. Consider the various possible ways in which these rules can be supplied. Amour and others, in examining the evolutionary trajectory of hostile takeover regimes in the United States, the United Kingdom, and Japan, identify four possible ways through which the demand for business law development can be accommodated: primary legislation, judicial decisions, regulation by government agencies, and private agreement among market actors.[75] Of immediate relevance to our analysis here are, first, the company law legislation by the Standing Committee of the NPC (NPCSC) and, second, the company law judicial interpretation by the SPC, to which we now turn.

To be sure, revision of the 1993 Company Law was one of 89 items in the five-year (1998–2003) legislative blueprint of the Ninth NPCSC. However, only relatively minor legislative changes were adopted in 1999. Revision of the 1993 Company Law was reintroduced to the 10th NPCSC's five-year legislative plan (2003–08). However, it was not until 2004, and indeed after the 2004 Beijing Opinions were issued, that the NPC decided to move the overhaul of the 1993 Company Law to the top of its legislative agenda.[76] In the absence of a legislative overhaul, the 1993 Company Law was not regarded as a source of corporate legal rules that fit the newly emerged and swiftly changing realities. The 1993 Company

[68] Survey Report, above n 60 at 218.

[69] *Ibid.*

[70] *Ibid.*

[71] Of course, an issue of judicial independence, that is, independence of the lower-level courts from the higher-level courts, is involved. See, generally, Randall Peerenboom (ed) *Judicial Independence in China: Lessons for Global Rule of Law Promotion* (Cambridge University Press 2010).

[72] Before the 2005 amendments to the 1993 Company Law, it was required that a company should have no fewer than two members, except for wholly state-owned limited-liability companies. Art. 20, 1993 Company Law. See, generally, Gu Minkang *Understanding Chinese Company Law* (2nd edn Hong Kong University Press 2010).

[73] Survey Report, above n 60 at 218–19.

[74] Survey Report, above n 60 at 219.

[75] J Armour, JB Jacobs, and CJ Milhaupt 'The Evolution of Hostile Takeover Regimes in Developed and Emerging Markets: An Analytical Framework' (2011) Harvard International Law Journal 52, 219.

[76] L Ye, above n 21 at 112.

Law was, rather, to be held responsible for the legitimacy-threatening problem of inconsistencies in court rulings on company law matters, the Survey Report boldly put.[77]

The role of supplying the much-needed corporate legal rules then fell on the SPC. Noting the failure of the 1993 Company Law to give much guidance to judges in their handling of company law cases,[78] the SPC responded by enacting its own rules in the form of judicial interpretations to fill the gap. Consisting of 53 articles, the 2003 Draft Interpretations included a comprehensive set of provisions addressing what were perceived as 'thorny' company legal problems that judges ran into with frequency.[79] These included issues in connection to derivative actions and piercing the corporate veil.[80]

Given that the SPC had, in response to legislative inaction, already assumed the role as a leading provider of corporate legal rules, it is puzzling that the HPCs also allowed themselves to become a player in the corporate rule-making arena. This might be less of an issue for the HPCs that made rules (e.g. 2002 Zhejiang Opinions and 2003 Shanghai Opinions) prior to the SPC's promulgation of the 2003 Draft Interpretations in November 2003; they were only but to fill the gap in the intervening time. Yet, the Beijing Survey was carried out about the same time the 2003 Draft Interpretations was being drafted, and the Beijing Opinions was issued only two months after the SPC closed its public consultations on the 2003 Draft Interpretations. This all gives the impression that the Beijing HPC was engaged in a race with the SPC for corporate lawmaking.

That impression is a false one. Indeed, the Beijing HPC took painstaking efforts to avoid being seen as competing with the SPC for the rule-making authority. This is manifested in the Beijing HPC's Explanatory Note accompanying the 2004 Beijing Opinions.[81] In the Explanatory Note, the Beijing HPC emphatically stated that it had carefully refrained from making rules on the issues already addressed by the 2003 Draft Interpretations. In what appears to be a tactful understatement of the innovative nature of the 2004 Beijing Opinions, the Beijing HPC added that the scope of the Opinions was confined only to 'procedural matters' and that the Opinions did not venture beyond the boundary of the then-existing laws.

An immediate question that arises is why the Draft Interpretation did not make provisions for these 'procedural matters.' Ignorance or information asymmetry could be one of the reasons. Anecdotal evidence suggests, however, this is not likely to be the case. The Beijing HPC had been closely involved in the drafting process of the 2003 Draft Interpretations. The Beijing HPC was among the seven HPCs that the SPC contacted in March 2003 with a view to gaining a fuller understanding of local judicial practices.[82] Relatedly, the Beijing HPC submitted to the SPC a report on the findings of a

[77] Survey Report, above n 60 at 216.

[78] See the SPC Circular accompanying the 2003 Draft Interpretations.

[79] D Wang 'Gongsifa sifa jieshi zhunbei gongzuo dashi ji' [Major Events in the Preparation Work of the 2003 Draft Interpretations of the Company Law], available at http://www.zwmscp.com/list.asp?unid=17 (accessed 15 June 2009).

[80] For detailed analysis of the 2003 Draft Interpretations in relation to its provisions on derivative actions and piercing the corporate veil, see J Deng, above n 41; and C Xi, above n 32, respectively.

[81] Above n 61.

[82] D Wang 'Gongsifa sifa jieshi zhunbei gongzuo dashiji' [Milestones in the Preparation Work for the Judicial Interpretation of the Company Law], available at http://www.zwmscp.com/list.asp?unid=17 (accessed 15 June 2009).

survey that the District Court of the Haidian District conducted on the company law disputes it tried.[83] Judges from the Beijing HPC were also invited to attend the SPC closed-door seminar convened in August 2003, which vetted the initial draft of the 2003 Draft Interpretations.[84] In all likelihood, the SPC must have been adequately knowledgeable about those 'procedural matters' on which the Beijing HPC subsequently made rules on its own.

Another possible reason can be that these 'residual' matters were intentionally left out from the 2003 Draft Interpretations, maybe because they were perceived not be of national significance. This proposition is not based on mere speculation. For example, in the context of intellectual property lawmaking, Justice Jiang Zhipei, then Chief Justice of the SPC Third Civil Division, articulated the SPC's stance toward the making of judicial interpretations:[85] 'On the matter of judicial interpretations, local courts have placed very high expectations on the SPC, hoping that judicial interpretations can be enacted with a highest possible frequency, and that their provisions can be laid out with a greatest possible degree of clarity and detail. Nevertheless, judicial interpretations tend to carry with them important policy implications, and it is important that they can stand the test of time and remain stable. Thus, judicial interpretations shall be enacted only on issues… concerning national interests and of universal significance.'

To the extent that these matters were of limited significance to economic activities in the whole nation, the Beijing HPC could hardly elect to ignore them. All of the 23 issues tackled by the 2004 Beijing Opinions 'derived from company law cases adjudicated by different levels of courts in Beijing' and were ones that local judges 'commonly encountered.'[86] The Beijing HPC would be bound to see its lower courts continue to hand out inconsistent and, even worse, contradictory rulings, had it failed to supply the much-needed guidance on those matters. It has emerged, self-consciously or involuntarily, as a de facto subnational legislator on corporate affairs, even though it can find for itself no place in China's formal legislative framework.

Conclusion

Subnational Chinese courts, in particular the HPCs, have recently lived in constant tension between the SPC's long-standing aversion to local courts' engagement in the business of judicial lawmaking on the one hand, and on the other, the demand for rules to fill the gap caused by regulatory unresponsiveness to local economic affairs on the part of the national-level lawmaking agencies. This tension is inevitable; it is fundamentally one between the official rhetoric of *centralization* of law/rule-making authority and the hard truth of economic *decentralization* in the era of economic reforms. A manifestation of the tension is highlighted in this Article. Disputes between members of the company, which were channeled through the court system, increased greatly both in number and in complexity, creating what was perceived

[83] *Ibid.* There was a concentration of company law cases in the Haidian District. The District Court alone handled 20% of all company law cases in Beijing. See Survey Report, above n 60 at 216.

[84] D Wang, above n 78.

[85] Z Jiang 'Zai quanguo fayuan zhishi chanquan shenpan gongzuo zuotanhui shang de zongjie jianghua [Concluding Remarks at the National Court Colloquium on Intellectual Property Adjudication Work] (20 January 2007). These remarks were made with endorsement from Justice J Cao, then Executive Vice-President of the SPC and, presumably, can be regarded as an embodiment of the SPC's general policy preferences.

[86] Explanatory Note, above n 61 at 24.

by local courts to be an irresistible demand for corporate legal rules that the national-level lawmaking agencies, in particular, the NPCSC and the SPC, were barely able to meet in an effective manner.

One surviving strategy that local courts - in particular, the HPCs - have developed is to make much-needed corporate legal rules, despite the SPC's expressed disapproval, in the hope of ensuring consistent outcomes in factually similar cases. These rules vary greatly in their functionality and the degree of novelty, ranging from rules that serve to determine the applicable law for certain legal issues, to rules that help to fill the gap in company law, and to rules that are so novel that it is difficult to trace their legislative roots. However, the local courts attempt to downplay the rule-making nature that they have developed and portray it as part of their routine, quotidian, dispute-resolution function.

Local corporate judicial lawmaking serves an important function in China's economic development. It helps to fix a structural defect in Chinese formal lawmaking, that is, the inability of the national lawmaking agencies to respond adequately to demand for rules arising from constantly changing economic activities at the local level. Thus, local judicial lawmaking improves the responsiveness of the legal system as a whole to economic development in the era of economic reforms.

The Chinese experience has important implications for the comparative literature on the interrelationship between legislation and judge-made law. Even in a jurisdiction where the emphasis is predominantly on legislation as the primary source of law, judicial lawmaking, both at the national and subnational levels, is inevitable in areas of law in which legislation fails to meet the rising demands for legal rules. Innovative courts, even though they actually assume a legislative role, may be reluctant to admit that they have in fact played that role, due largely to ideological and institutional constraints. This only serves to create a gap between the reality of judicial lawmaking and the official rhetoric denying judicial lawmaking a place in the formal legal order.

Nota redacției: Articolul a fost publicat inițial în *Statute Law Review* 34(1), 39–57, 2013, Revista Forumul Judecătorilor primind permisiunea autorului și a revistei britanice în vederea republicării exclusive a studiului în România.