

CPI's Asia Column Presents:

New Developments in Trade Secret Protection in China

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There have recently been a few positive developments in the trade secret protection regime in China. For instance, the threshold for initiating criminal prosecution against trade secret theft has been lowered, and rules for shifting the burden of proof to those accused of trade secret infringement in civil cases have also been introduced. All these new changes are expected to make trade secret protection in China easier.

I. Latest Legislative Activities on Trade Secret Protection in China

In 2019 and 2020, China launched a series of legislative efforts related to trade secret protection, partially as a result of the U.S.-China trade negotiations. But more importantly, it reflects the inherent need to better protect local innovation and ensure a healthy market competition environment in China. Below is a brief summary of the new rules, including some of the newer drafts.

A. New Rules on Trade Secret Protection that Have Come into Effect

On April 23, 2019, the 2019 Amendment of the PRC Anti-Unfair Competition Law (the “2019 Amendment”)¹ came into effect. The Amendment emphasized the illegality of stealing trade secrets by means of “electronic intrusion,” as well as the illegality of aiding, abetting, or facilitating another party’s misappropriation of trade secrets. Most importantly, Article 32 of the Amendment conditionally shifts the partial burden of proof from the trade secret owner to the accused infringer.

Subsequently, on January 15, 2020, the China-U.S. Phase One Trade Deal (the “Trade Deal”)² was signed. Article 1.4 (defining the Scope of Prohibited Acts Constituting Trade Secret Misappropriation) and Article 1.5 (elaborating the Burden-Shifting in a Civil Proceeding) of the Trade Deal are also present under the revisions in the 2019 Amendment. Obviously, the revisions in the 2019 Amendment had reflected the consensus reached in the previous China-U.S. trade negotiations.

To implement its commitment in the Trade Deal, China has also released several judicial interpretations and other regulations to strengthen trade secret enforcement accordingly.

- 1) The Provisions of the Supreme People’s Court on Several Issues Concerning the Application of Law in the Trial of Civil Cases Involving Infringements upon Trade Secrets³ has come into force since September 12, 2020. What is notable is that the judicial interpretation clarifies the method of determining whether the trade secret used by the accused infringer is materially the same as that owned by the rights holder, confirms the illegality of using others’ trade secrets after improving under certain circumstances, and responds to the issues of convergence between current and past laws. In addition, Article 15 of the judicial interpretation elaborates the application of preliminary measures and injunctions in trade secret cases, directly echoing Article 1.6 of the Trade Deal, i.e. the Provisional Measures to Prevent the Use of Trade Secrets. Prior to the formal judicial interpretation, there was a draft version providing detailed instructions on how to apply preliminary injunctions (behavior preservations in Chinese legal jargon) in trade secret misappropriation cases. However, compared with the wording found in the former draft version, Article 15 in the formal interpretation deletes the detailed guidance and keeps only the general rule, which has disappointed many trade secret rights holders.

- 2) On September 14, 2020, the Interpretation (III) of the Supreme People's Court and the Supreme People's Procuratorate of Several Issues Concerning the Specific Application of Law in the Handling of Criminal Cases Involving Infringements upon Intellectual Property Rights (the "Interpretation III")⁴ came into effect. The major focus is trade secret-related crime. As a significant improvement, this Interpretation (III) lowers the threshold for initiating criminal prosecution from RMB 500,000 to RMB 300,000 and elaborates the criteria for "great losses" suffered by the trade secret right holder. What's more, Interpretation III further clarifies the possibility of criminal prosecution against someone solely for obtaining the trade secrets by illegal means, without actual disclosure or use. Previously, the mainstream theory held that simply obtaining others' trade secrets by illegal means is rarely considered a crime, since the rights holder's losses are difficult to quantify.⁵ However, Article 5.1 (a) of this interpretation explicitly stipulates that the losses incurred from illegally obtaining others' trade secrets can be calculated by referring to the reasonable royalties of the trade secrets. By providing this method of calculation, the interpretation removes the difficulties in quantifying losses and makes it possible to hold the aforementioned infringer criminally liable. Besides, the interpretation provides that when determining the rights holder's great loss, the cost of remedial measures shall be considered, which echoes Article 1.7 of the Trade Deal, i.e. the Threshold for Initiating Criminal Enforcement.
- 3) On September 17, 2020, the Supreme People's Procuratorate and the Ministry of Public Security issued the Decision on Amending the Criteria for Launching Formal Investigation into Criminal Cases of Infringement upon Trade Secrets (2020).⁶ The Decision was made to ensure consistency with the abovementioned Interpretation III on the threshold for initiating criminal prosecution in trade secret misappropriation cases, and the criteria for determining "great losses" suffered by the trade secret rights holder.

B. Other Pending New Rules on Trade Secret Protection

There are more draft laws and regulations proposed to improve trade secret protection in China from different angles, again as part of the effort to implement the Trade Deal. These are still at the stage of seeking public comments and are expected to be officially passed later this year or early next year.

- 1) On August 14, 2020, the Department of Justice issued the Guiding Opinions on Strengthening the Protection of Trade Secrets and Confidential Business Information in the Administrative Licensing Process (draft for comments). It focuses on the performance of Article 1.9 of the Trade Deal, i.e. Protecting Trade Secrets and Confidential Business Information from Unauthorized Disclosure by Government Authorities. The Guiding Opinions are intended to regulate the behavior of administrative agencies during the process of administrative permission. This is a step towards better protection of the enterprises' trade secrets and confidential commercial information.
- 2) On October 21, 2020, Amendment XI to the Criminal Law (second draft for review) ("Amendment XI") was made open for public comments. Most importantly, the amendment has revised the original threshold for the crime of trade secret misappropriation, i.e. from "causing great losses to the rights holder," to "under serious circumstances." As the existing criminal rule provides the crime of trade secret misappropriation as a consequential offense, this revision makes it possible to change the

crime into a behavioral offense. This fundamental change has taken the relevant enterprises several years of advocacy. Given the fact that Amendment XI is still open for soliciting comments, it is unknown whether the formal version will keep the change or not. Even if the final version adopts the revision, more detailed official interpretations are still in need to clarify the meaning and scope of “serious circumstance.” Therefore, it is uncertain whether the crime of trade secret misappropriation will eventually be changed from consequential offense to behavioral offense.

- 3) On October 18, 2020, the State Administration for Market Regulation issued the Provisions on the Protection of Trade Secrets (Draft for Comments), aiming at refining and clarifying the key aspects of investigation and handling of suspected trade secret misappropriation acts and relevant legal liabilities. Although the Anti-Unfair Competition Law has empowered the administrative agencies to regulate the trade secret infringement acts, the implementation of such rights is rarely heard of. That is mainly because it is hard to determine the existence of such infringing acts given the difficulties of investigating and handling trade secret infringement cases and the lack of technical support for administrative law enforcement officers. The issuance of the Provisions for the Protection of Trade Secrets (Draft for Comments) reflects the willingness of administrative agencies to play a more important role in the protection of trade secrets. Meanwhile, the provincial and municipal administrative agencies for market regulation are also actively encouraging technical experts to participate in the law enforcement proceedings on trade secret protection.

II. Implications for the Industry

All these new rules, including the pending drafts, are very encouraging to the industry and should make IP owners feel more confident about protecting their trade secrets in China.

First, where necessary, companies can be more aggressive than before in taking legal actions to enforce their trade secrets, particularly by taking advantage of the positive amendment of the law. For a long time, it has been a common impression among rights holders that it is very difficult to enforce their trade secrets in China. The new laws and regulations mentioned above have reduced the burden of proof for the trade secret rights holders and also lowered the criminal threshold among others. Certainly, these revisions need to be tested in real cases in order to confirm they can really work to establish a reliable and stable system for trade secret protection in China. By reviewing more cases, Chinese courts and legislators can further improve upon the rules for trade secret protection.

Second, companies should be mindful of taking proper confidentiality measures for their trade secrets which is a precondition for legal protection in China. In some unsuccessful cases the rights holders' trade secrets were found unprotectable, mainly because their confidentiality measures failed to meet the requirements stipulated in the relevant laws. For instance, merely signing a broad general non-disclosure agreement is often considered not sufficient. Rather, the rights holders need to prove that restrictions have been put in place to limit access and prevent leakage of the specific trade secrets in question.

Third, companies should also improve their risk control system. The dramatic lowering of the criminal threshold for trade secret protection will have a series of impacts. On one hand, it

makes criminal enforcement easier, but on the other hand, it also means higher potential risks when a company hires employees from competitors, especially those with sensitive information. Hence, companies not only need to do careful pre-hiring background checks on their new employees, but also should ensure proper clearance for any sensitive technical or commercial information submitted by their employees during the employment period.

To conclude, there are significant improvements to the trade secret protection regime in China, which should benefit both local and international companies. While it may take some time to see how the new rules play out in real cases, the overall trend is positive. For instance, Dow and Johnson Matthey recently released a joint statement about a landmark victory they obtained in a trade secret case in Jiangsu Province, China just before the local defendant's home court. It is recommended that companies gain more confidence about enforcing their trade secrets in China, while at the same time also paying attention to risk management.

¹ Anti-Unfair Competition Law of the People's Republic of China (2019 Amendment).

² ECONOMIC AND TRADE AGREEMENT BETWEEN THE GOVERNMENT OF THE PEOPLE'S REPUBLIC OF CHINA AND THE GOVERNMENT OF THE UNITED STATES OF AMERICA ("China-U.S. Trade Deal Phase I").

³ Provisions of the Supreme People's Court on Several Issues Concerning the Application of Law in the Trial of Civil Cases Involving Infringements upon Trade Secrets, Interpretation No. 7 [2020] of the Supreme People's Court.

⁴ Interpretation (III) of the Supreme People's Court and the Supreme People's Procuratorate of Several Issues Concerning the Specific Application of Law in the Handling of Criminal Cases Involving Infringements upon Intellectual Property Rights, Interpretation No. 10 [2020] of the Supreme People's Court.

⁵ *People v. LIU Zhongyan* ("Mingyang case"), (2020) Yue 52 Xing Zhong No. 203, which is the only case in the public domain where the court held the act of simply obtaining the trade secrets without using constitutes the crime of trade secret misappropriation.

⁶ Notice by the Supreme People's Procuratorate and the Ministry of Public Security of Issuing the Decision on Amending the Criteria for Launching Formal Investigation into Criminal Cases of Infringement upon Trade Secrets (2020).