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Navigating the Minefield of Trade Secrets Protection in China

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Navigating the Minefield of Trade Secrets Protection in China

*Daniel C.K. Chow**

ABSTRACT

Many Multinational Companies (MNCs) now consider trade secrets to be the most important intellectual property right in China, ahead of patents, trademarks, and copyrights. While trade secrets have become more valuable than ever as a business asset in China, many MNCs also find that the protection of trade secrets in China is full of pitfalls and traps. Unlike in the case of patents, trademarks, and copyrights, China has no unified law governing trade secrets, but has disjointed provisions scattered throughout various laws. The pitfalls are also created by a high evidentiary burden in proving a theft of a trade secret that many MNCs find difficult to meet. China places an emphasis on documentary proof of the theft of the trade secret, which can be difficult to obtain. A comparison of the enforcement of trademarks in China with the enforcement of trade secrets illustrates how much more difficult it is to enforce trade secrets. In addition, MNCs that attempt to enforce their trade secrets can find themselves caught in risky and dangerous entanglements with Chinese enforcement authorities. These enforcement authorities often demand illegal payments as a price of enforcement. While these enforcement problems admit of no easy solutions given the realities of China's current trade secrets legal regime, many of these problems can be avoided altogether if MNCs implemented some simple advanced planning and preventative measures. MNCs should invest in these preventative measures that, if carefully implemented, can avoid the traps in China's murky enforcement regime while at

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the same time protect valuable confidential and propriety information of the company.

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I. INTRODUCTION

Many multinational companies (MNCs) doing business in the People's Republic of China (China) find protecting trade secrets, the commercially valuable technical and business information MNCs protect through confidentiality measures, to be a growing problem.¹ For the first time, in a recent survey of MNCs doing business in China the majority of respondents selected trade secrets as the intellectual property right of most concern, ranking trade secrets

1. See Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat'l People's Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 10 (China) (stating that "trade secret" shall mean technical information and business information that is unknown to the public, can bring economic benefits to the owner, is of a practical nature, and is protected by confidentiality measures taken by the right owner."); see also *infra* Part III(A).

ahead of trademarks, patents, and copyrights.² The recent concern with trade secrets is highlighted by a number of high profile cases. In a notorious case, General Motors (GM) discovered that Chery, a Chinese state-owned automaker, was marketing the QQ subcompact car, a nearly identical copy of GM's Chevrolet Spark. Chery, however, was selling the QQ at one-third of the price.³ GM claimed that the two cars were built based on proprietary mathematical data and formulas that were stolen from GM.⁴ GM brought a lawsuit against Chery in China but the two parties eventually settled the case.⁵ Since the settlement, Chery has announced its plans to export cars to the United States, and it is unclear how much of an advantage Chery was able to gain through obtaining access to GM's proprietary information.⁶ In a 2013 case, a former employee of the Chinese multinational pharmaceutical company Eli Lilly downloaded copies of confidential documents from Lilly's computer server with the probable intention of making them available to Lilly's competitors in China.⁷ E.I. du Pont, Corning, and American Superconductor, all U.S.-based MNCs, have recently brought cases of trade secret theft in China.⁸

2. See U.S.-CHINA BUSINESS COUNCIL, RECOMMENDATIONS FOR STRENGTHENING TRADE SECRET PROTECTION 2 (2013) (providing data drawn from USCBC member company surveys). Forty percent of respondents selected trade secrets, while 27 percent selected trademarks, 20 percent selected patents, and 8 percent selected copyright. See *id.* (summarizing data drawn from 2013 survey responses).

3. See Marisa Anne Pagnattaro, *Protecting Trade Secrets in China: Update on Employee Disclosures and the Limitations of the Law*, 45 AM. BUS. L.J. 399, 400 (2008) (discussing the litigation and eventual settlement between GM and Chery).

4. See *id.* ("As U.S. Commerce Secretary Donald Evans stated, '[t]his incident defies an innocent explanation. The QQ and the Spark are twins because both cars were built from the same DNA—proprietary mathematical data and formulas—that were stolen from GM Daewoo and used to build the QQ.'").

5. See *id.* (discussing the settlement that occurred soon after GM brought suit against Chery in a Shanghai court).

6. See *id.* at 400–01 ("Most recently, Chery entered into a low-cost production venture with Chrysler Group, which includes the goal of exporting cars from China to the United States [I]t is unclear how much of an advantage Chery initially gained through misappropriation of trade secrets").

7. See Olivia Zhan, *The First Preliminary Injunction Issued by China Court in Trade Secrets Cases*, SQUIRE SANDERS (Aug. 27, 2013), <http://www.lexology.com/library/detail.aspx?g=6ba18a27-48fc-4916-93d3-6fdb07f78c1b> [<http://perma.cc/G7SS-UAL7>] (archived Aug. 31, 2014) (providing background information regarding a recent preliminary injunction granted by a Chinese court).

8. See Ryan Ong, *Trade Secret Enforcement in China: Options and Obstacles*, CHINA BUS. REV. (Jan. 1, 2013), <http://www.chinabusinessreview.com/trade-secret-enforcement-in-china-options-and-obstacles> [<http://perma.cc/AF3S-2TJU>] (archived Aug 31, 2014) (referencing several cases brought by companies against Chinese individuals or Chinese companies).

Theft of trade secrets in China is considered to be a widespread and common problem.⁹ The Chinese government recently acknowledged the importance of trade secrets; this acknowledgement reflects China's own concern that a lax environment that results in industrial espionage is detrimental to China's own long-term interests.¹⁰ On December 20, 2013, the U.S.-China Joint Commission on Commerce and Trade, a high-level government forum for dialogue on trade issues between the United States and China, announced that trade secret protection and enforcement and legislative reform would be a top priority for the Chinese government in 2014.¹¹

The recent attention to trade secrets is fueled by not only the growing importance of trade secrets as business assets for all MNCs doing business in China but also by the growing frustration of MNCs faced with the many difficulties of protecting trade secrets.¹² Enforcement of all intellectual property rights in China has long been a concern for MNCs, but trade secrets pose a special and unique set of issues for MNCs in China for at least three reasons.

First, while only some MNCs have commercially valuable trademarks, patents, and copyrights in China, the majority of MNCs doing business in China either have commercially valuable trade secrets when they enter the Chinese market or develop them in quick order.¹³ As a result, while some MNCs expend significant resources to protect their trademarks from counterfeiting and infringement, and others focus on enforcing their patent rights, almost every MNC has

9. See Marisa Anne Pagnattaro, *Protecting Know-How from Walking Out the Door in China: Protection of Trade Secrets*, 55 BUS. HORIZONS 329, 329 (2012) (hereinafter Pagnattaro, *Protecting Know-How*) ("Loss of trade secrets is perceived as a widespread problem, creating a climate that can be especially challenging for companies.").

10. See U.S.-CHINA BUSINESS COUNCIL, *supra* note 2 ("Such government actions reflect a growing understanding within the Chinese government about negative consequences of insufficient trade secrets protection.").

11. The announcement came at conclusion of the 24th annual U.S.-China Joint Commission on Commerce and Trade (JCCT). The JCCT is a body that considers trade and business issues, including intellectual property issues, between the United States and China. The U.S. delegation was headed by Penny Pritzker, the U.S. Commerce Secretary, and Michael Froman, U.S. Trade Representative, and the Chinese government was represented by Vice Premier Wang Yang. See U.S. DEPT OF COMMERCE, 24TH U.S.-CHINA JOINT COMMISSION ON COMMERCE AND TRADE FACT SHEET (2013), available at <http://www.commerce.gov/news/fact-sheets/2013/12/20/fact-sheet-24th-us-%E2%80%93china-joint-commission-commerce-and-trade-fact-sheet> [<http://perma.cc/AE79-2B6A>] (archived Aug. 31, 2014) (outlining several topics discussed during a meeting between the United States and China). The JCCT meets for several days on an annual basis to discuss trade and business issues of common concern between the United States and China.

12. See J. Benjamin Bai & Guoping Da, *Strategies for Trade Secrets Protection in China*, 9 NW. J. TECH. & INTELL. PROP. 351, 353-54 (2011) (noting the growth rate of foreign related intellectual property disputes in China to be "exponential" but also noting that the relatively few trade secrets cases have been reported due to the difficulties of proof in trade secrets cases).

13. See *infra* Part II.B.

trade secrets that need protecting.¹⁴ While this need means that every MNC needs to implement precautionary measures to protect trade secrets,¹⁵ not all do, and many MNCs do not understand all of the pitfalls that come with enforcement of trade secrets until after theft has already occurred.¹⁶ For the majority of MNCs doing business in China, there are two sources of trade secrets specific to their Chinese operations that need protecting. Some MNCs transfer technology to China protected as a trade secret, rather than protected as a patent or through some other form of intellectual property right. For example, an MNC might transfer an advanced chemical formula and process used in making industrial products, such as rubber resins, to its Chinese business entity as a trade secret.¹⁷ The chemical formula and process become the basic technology (i.e. the know-how) used by the Chinese business entity to manufacture products for the Chinese market. If a competitor were able to gain access to the trade secret and use the advanced formula, the competitor could gain a business advantage that could be highly damaging to the MNC. In other cases, the MNC's Chinese business entity might develop trade secrets in the process of using the MNC's transferred technology. While trade secrets often relate to technology contained in the product sold by the MNC, the trade secrets also include confidential business information, such as logistics, financial data, customer lists, marketing strategies, advertisement camp signs, and expansion plans that are not directly related to the manufacture of the product.¹⁸ The vast bulk of MNCs doing business in China will, over time, develop the type of information that could be harmful if leaked to a competitor.¹⁹

Second, trade secrets are notoriously difficult to enforce in China and present obstacles that are in some important respects even greater than hurdles in the enforcement of other intellectual property rights, such as trademarks.²⁰ Unlike other forms of intellectual property, such as trademarks, patents, and copyrights, which all have a uniform law, China's laws that pertain to trade secrets are scattered throughout various laws, including the Anti-Unfair

14. See *infra* Part II.B.

15. See *infra* Part IV.

16. This observation is based upon the author's analysis of trade secrets and unfair competition cases brought in China and on his own discussions with lawyers, academics, and in-house counsel in China.

17. All MNCs are required under Chinese law to establish a China business entity (i.e., a domestic Chinese company) in order to do business on the ground in China. The MNC owns the China business entity in whole or in part. See *infra* Part II.B.

18. See *id.*

19. See *id.*

20. See *infra* Part III.C.

Competition Law,²¹ the Labor Law,²² the Labor Contract Law,²³ the Company Law,²⁴ the Contract Law,²⁵ and the Criminal Law.²⁶ In addition, there does not appear to be any impetus in China for creating a unified trade secrets law in the near future, and vested political interests may prevent the creation of such a law. Moreover, an analysis of these laws indicate that, compared with other intellectual property rights, trade secrets present an especially high evidentiary burden on plaintiffs and could involve a complex procedure that could create many traps for an MNC.²⁷ One major hurdle is that, unlike trademarks and patents, trade secrets are not subject to a registration system in China so there is no documentary evidence, such as a registration certificate officially issued by the PRC authorities, of the ownership of the trade secret by the plaintiff. Enforcing trade secrets involving intangible knowledge, without any supporting documentary evidence, becomes a difficult, if not insurmountable, problem because Chinese government authorities have a strong preference for documentary evidence in all cases.²⁸ Documentary evidence is practically the only form that is given

21. See *Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa* (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat'l People's Cong., Sept. 2, 1993, effective Dec. 1, 1993), arts. 2, 10, 25 (China) (describing what constitutes infringing upon another's trade secret and the penalty for infringing); see also discussion *infra* Part III(A).

22. See *Zhong Hua Ren Min Gong He Guo Lao Dong Fa* (中华人民共和国劳动法) [Labor Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., July 5, 1994, effective Jan. 1, 1995) (China) (defining when a non-competition provision may be included in an employment contract); see also *infra* Part III(A).

23. See *Zhong Hua Ren Min Gong He Guo Lao Dong He Tong Fa* (中华人民共和国劳动合同法) [Labor Contract Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., June 29, 2007, effective Jan. 1, 2008) (China) (establishing employee liability for trade secret infringement beyond general liability for breach of employment contract); see also *infra* Part III(A).

24. See *Zhong Hua Ren Min Gong He Guo Gong Si Fa* (中华人民共和国公司法) [Company Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., Oct. 27, 2005, effective Jan. 1, 2006), arts. 149–50 (China) (prohibiting the disclosure of company secrets by directors or senior managers); see also *infra* Part III(A).

25. See *Zhong Hua Ren Min Gong He Guo He Tong Fa* (中华人民共和国合同法) [Contract Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., Mar. 15, 1999, effective Oct. 1, 1999) (China) (setting out the guidelines for technology transfer contracts); see also *infra* Part III.A.

26. See *Zhong Hua Ren Min Gong He Guo Xing Fa* (中华人民共和国刑法) [Criminal Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., Mar. 14, 1997, effective Oct. 1, 1997) (China) (establishing criminal liability in certain instances of trade secret infringement); see also *infra* Part III.A.

27. See *infra* Part III.C.

28. See ORRICK, HERRINGTON & SUTCLIFFE LLP, *EMPLOYMENT LAW YEARBOOK* 865 (Timothy J. Long, Andrew R. Livingston, & Joshua C. Vaughn, eds., 2012) (discussing evidence collection in trade secrets cases)

significant weight in Chinese courts; oral testimony is often regarded as of little probative value.²⁹ The use of documentary evidence in enforcement of intellectual property rights can be crucial because it is often difficult to obtain. Several examples, further discussed below, will illustrate this difficulty.³⁰ Since trade secrets and trademarks are both considered to be part of the law of unfair competition, later parts of this Article will compare the enforcement of trade secrets and trademarks in China.³¹ As this Article will show, obtaining enforcement of trademark rights in China can be a straightforward process; an enforcement action can be obtained from Chinese administrative authorities in some cases immediately on application,³² whereas obtaining enforcement of trade secrets can be a long and arduous process, full of pitfalls. Part of this explanation lies in China's strong preference for documentary evidence, which is easily obtainable in trademark cases but often difficult in trade secrets cases.³³ Not surprisingly, Chinese enforcement authorities are wary of acting outside the scope of their powers. Chinese authorities are therefore especially cautious when dealing with claims of theft of trade secrets that are not supported by both documentary proof of the ownership of the trade secret as well as documentary proof of its subsequent theft.³⁴

Third, the protection of trade secrets can provide advantages to an MNC that are not available in the case of trademarks, patents, and copyrights, but the MNC must exploit these advantages or lose an important opportunity to protect its trade secrets, made all the more significant by the difficulties of enforcement once the trade secret is stolen. These advantages are that the protection of trade secrets is under greater control by the MNC or its Chinese business entity than the protection of other forms of intellectual property rights.³⁵ In the case of trademarks, once the branded product enters the stream of commerce, nothing prevents pirates and infringers from producing counterfeits and knock-offs. The owner of a patent or

29. See *id.* ("Documentary evidence is practically the only form of evidence that carries significant weight in a Chinese court. Oral testimony, while admissible, usually has little or no probative value.").

30. See *infra* Part III.C.1.

31. See *id.*

32. While enforcement of trademarks can be obtained expeditiously, the problem of deterrence is a different issue. Enforcement of trademarks against infringers often carries few consequences and does not deter infringers from repeating their offenses. See Daniel Chow, *Anti-Counterfeiting Strategies of Multinationals in China: How a Flawed Approach is Making Counterfeiting Worse*, 41 GEO. J. INT'L L. 749, 757 (2010) [hereinafter Chow, *Anti-Counterfeiting*] (advocating that MNCs ought to shift focus toward achieving long-term deterrence as opposed to focus on short-term enforcement).

33. See *infra* Part III.C.1.

34. See *id.* (explaining that proof of ownership of a trade secret and its theft are part of the burden of proof in trade secrets cases).

35. See *infra* Part IV.

copyright also loses control over the ability of others to make unauthorized copies once the trademark enters the stream of commerce. The owner of trade secrets, however, has the ability to protect the trade secret cases from disclosure to unauthorized third parties by making sure that the trade secret remains confidential.³⁶ The need to protect trade secrets is further increased by the effect of two factors. One is the problem of effective enforcement once the theft of the trade secret has already occurred.³⁷ The second factor that creates incentives for implementing effective preventative measures is that, for MNCs, the theft of trade secrets tends to occur in cases when current or former employees of the MNC's Chinese business entity are involved.³⁸ One of the most common scenarios involving theft of trade secrets is when a former employee is lured to work for a competitor. For example, Microsoft brought multiple lawsuits when a high-level executive in Microsoft's Chinese operations was hired by Google to head Google's Chinese operations.³⁹ While Microsoft was a high-profile case that drew widespread media coverage, former management-level employees with access to proprietary know-how and confidential information are often lured to work for competitors in China.⁴⁰ These developments would indicate that MNCs should invest significant resources in developing internal preventative measures that focus on current employees since the MNC's leverage and negotiating power is at its highest while the employee is still currently working at the MNC's Chinese business entity.⁴¹ Once the employee leaves, the relationship between the employer and the former employee could deteriorate or become hostile, and it then becomes necessary to proceed with civil litigation or criminal proceedings.⁴² As noted earlier, there are significant evidentiary and institutional barriers to enforcing trade secrets in China, but if the

36. See *infra* note 90. There is an important qualification to this point: discovery of a trade secret through reverse engineering of a product is lawful. If the owner of a trade secret creates a product using ingredients or through a process that can be discovered by a competitor through an analysis of the product, so-called "reverse engineering," then the trade secret has become disclosed and is no longer protected.

37. See *infra* Part III.C.

38. See US-CHINA BUSINESS COUNCIL, *supra* note 2, at 9 ("[A] considerable amount of trade secrets theft stems from incidents of misappropriation caused by current or former employees.").

39. See Pagnattaro, *Protecting Know-How*, *supra* note 9 (discussing the litigation between the two companies and noting that the case was eventually settled outside the courtroom).

40. See *id.* ("Primary threats to the disclosure of proprietary information include deliberate actions of current and former employees, as well as loss of trade secrets in the context of joint ventures or other business arrangements." (citation omitted)).

41. See *infra* Part IV.

42. This observation is based on the author's own working experience in China. Former employees tend to become uncooperative and hostile when confronted with claims of misappropriation once they leave employment.

MNC has invested in a significant compliance program, the program could greatly increase the ability of the MNC to protect its trade secrets.⁴³

This Article will develop and examine these themes in three parts. Part II of this Article discusses technology transfer and the importance of trade secrets to MNCs doing business in China. The majority of MNCs that do business in China will need to transfer technology, embodied in intellectual property rights, to their Chinese business entities; as part of this technology transfer agreement, the MNC should have provisions that pertain to trade secrets even if the main subject matter of the technology transfer agreement is another intellectual property right, such as trademark or patent rights. Part II will also explain why, even if the MNC does not transfer trade secrets to its Chinese business entity at the inception, the business entity will almost inevitably develop trade secrets that the MNC will wish to protect in the future. Part III of this Article will discuss the fragmented legal framework in China that applies to trade secrets. Unlike trademarks, patents, and copyright, which all have unified, comprehensive laws, trade secrets are subject to a patchwork of different laws and are still dominated by the Anti-Unfair Competition Law of 1993. Part IV of this Article focuses on preventative measures that MNCs might take to protect their trade secrets. Given the difficulties of the enforcement of trade secrets, and the bureaucratic and institutional interests that might resist change, the most prudent course of action for most MNCs is to invest in preventative measures under the present legal regime. It might be overly optimistic or even naïve to think that China will enact a unified trade secrets law in the near future that will reduce or eliminate the problems in enforcement.⁴⁴ It is more realistic to accept the limitations of the present legal regime and to invest in preventative measures, which appears to be the most promising area in which MNCs can invest their resources to protect their trade secrets.

II. TECHNOLOGY TRANSFER AND TRADE SECRETS IN CHINA

The majority of MNCs that do business in China will need to engage in technology transfer, that is the licensing of intellectual property rights by the owner of the technology to a licensee in China

43. See *infra* Part IV.

44. For example, in a related area, the United States and China have been engaged in dialogue over how to improve the enforcement climate against trade counterfeiting in China for over a decade. However, the counterfeiting problem has not improved and may have gotten worse. See generally Chow, *Anti-Counterfeiting*, *supra* note 32.

that is usually owned in part or in whole by the MNC.⁴⁵ The discussion below considers technology transfer, the relevant laws applicable to technology transfer, and the relevant role of trade secrets.

A. *Technology Transfer in China*

MNCs that intend to conduct business operations on the ground in China are required by Chinese law to first establish business entities in China.⁴⁶ For example, in order to establish a manufacturing facility in China, an MNC must first establish a foreign-invested enterprise (FIE) that qualifies as a Chinese company under domestic law.⁴⁷ The MNC cannot directly own and operate the manufacturing facility. Under Chinese law, the FIE must own and operate the facility, but the MNC can own the FIE in whole or in part.

Most MNCs that do business in China choose to establish FIEs through either a joint venture or a wholly foreign-owned enterprise (WFOE).⁴⁸ A joint venture is a Chinese business entity formed by an MNC, the foreign investor, and a local partner, often a Chinese state-owned enterprise.⁴⁹ The joint-venture partners each contribute equity in the form of cash or in-kind contributions (e.g., land use rights) and obtain equity ownership interests in the joint venture in proportion to the equity contribution of each.⁵⁰ If the MNC invests 60 percent of the equity in the joint venture and the Chinese state-owned enterprise invests 40 percent of the equity, then the MNC has a 60 percent equity interest in the joint venture and the Chinese partner has a 40 percent interest.⁵¹ The joint venture is a distinct and separate legal

45. See DANIEL C.K. CHOW & THOMAS J. SCHOENBAUM, *INTERNATIONAL BUSINESS TRANSACTIONS: PROBLEMS, CASES, AND MATERIALS* 324 (2d ed. 2010) (discussing international technology transfer and emphasizing “the importance of technology transfer in modern international business transactions”).

46. See DANIEL C.K. CHOW & ANN M. HAN, *DOING BUSINESS IN CHINA: PROBLEMS, CASES, AND MATERIALS* 85 (2012) (discussing business and legal issues that foreign investors seeking to conduct business operations in China must consider).

47. See *id.* (introducing FIEs available to MNCs seeking to conduct business operations in China).

48. See CHOW & SCHOENBAUM, *supra* note 45, at 489–90 (discussing the advantages and disadvantages of joint ventures and WFOEs).

49. See CHOW & HAN, *supra* note 46, at 88 (“A joint venture is a business entity that is formed by an MNC and a local Chinese business entity, generally either a state-owned enterprise or a private company.”).

50. See *id.* at 90 (“Under all joint ventures, both the foreign partner and the Chinese partner are required to make capital contributions in the form of cash or in kind as part of the start-up costs of the joint venture Once all of the requirements are met, the profits can be divided between the two investors in proportion to their capital contributions.”).

51. See *id.* at 102 (“The contribution of registered capital by each joint venture partner represents its ownership or equity interest in the new company.”).

entity from each of the joint-venture partners, which are separate corporate entities in their own right.⁵² The joint venture is capable of incurring its own separate debts and legal liabilities. By contrast, a WFOE is wholly-owned by the MNC without any participation by a Chinese entity.⁵³ The MNC will invest the entirety of the capital necessary to establish the WFOE. Similar to the joint venture, the WFOE is also a distinct and separate legal entity.⁵⁴ The WFOE is considered to be a Chinese company under domestic law that is owned by the MNC, a foreign investor. Both the joint venture and the WFOE continue to be popular business vehicles among MNCs in China.

At the point when the MNC establishes the joint venture or WFOE in China, it is a legal entity that is otherwise an empty shell. The MNC will inject capital, often in the form of cash, and the local partner will also inject capital, in cash or in-kind contributions of land, buildings, or equipment, to the joint venture.⁵⁵ This capital may be used to acquire or purchase land-use rights, buildings, machinery, equipment, and power inputs, such as electricity, water, gas, and steam.⁵⁶ At this point, even though the FIE has all of the necessary physical structures necessary to operate, the FIE will still lack the know-how, knowledge, or technology necessary to produce the goods.

Take the example of an MNC in the consumer products industry that establishes a joint venture to be a manufacturing facility for producing laundry detergent that will be sold in China. Even though the joint venture may have the necessary physical structures (i.e. buildings, equipment, machinery, and power), the joint venture will be unable to manufacture the MNC's laundry detergent unless the MNC gives access to its proprietary know-how and intellectual property to the joint venture. In order to sell the laundry detergent in China, the MNC will need to allow the joint venture to have access to both the MNC's chemical formula for the laundry detergent as well as use of the MNC's trademarks and know-how.

In a typical case, the MNC will first register any trademarks in China in its own name and then will license the use of its trademarks

52. See *id.* at 88–89 (“[I]n a true joint venture, the end result is that there are three companies: Company A (the MNC), Company B (the Chinese partner), and Company C, the joint venture.”).

53. See *id.* at 91 (“[T]he wholly foreign-owned enterprise (WFOE) is a legal business entity that is owned entirely by the foreign investor with no participation from a Chinese partner.”).

54. See CHOW & SCHOENBAUM, *supra* note 45, at 490 (comparing joint ventures and WFOEs).

55. See CHOW & HAN, *supra* note 46, at 101 (“Registered capital can be contributed by the parties in cash or in kind, in the form of buildings and equipment. It is common for MNCs to contribute cash and for the local partner to contribute in kind.”).

56. See *id.* at 100 (explaining the ways in which registered capital can be used to meet the start-up costs of a joint venture).

to the joint venture.⁵⁷ This license agreement is a form of technology transfer whereby the owner of the patents and trademarks gives access to the proprietary technology under a licensing agreement to a third party, the joint venture.⁵⁸ MNCs use a license agreement because, under such an agreement, the MNC remains the owner of the intellectual property rights, and the licensee has been merely authorized to use the licensed technology.⁵⁹ To establish its ownership, the MNC will first register the trademark or patent in its own name with the Chinese authorities.⁶⁰ The MNC then licenses or gives permission to the joint venture or WFOE to use the intellectual property.⁶¹ The joint venture or WFOE is permitted by the MNC to use the intellectual property rights, but the MNC remains the owner of the rights.⁶² The MNC's ownership rights are established by its official registration certificate for the patent or trademark.⁶³ If, for any reason, the joint venture or WFOE terminates, the licensing agreement also terminates, and the MNC remains the owner of the intellectual property rights.⁶⁴

B. Technology Transfer and Protection of Trade Secrets

In some cases, the MNC will choose to transfer know-how as a trade secret. The requirements for a patent include novelty, nonobviousness, and utility, and might be difficult to satisfy.⁶⁵ There

57. See *id.* at 321 (discussing the “proper procedure” for acquisition and licensing of intellectual property rights).

58. See *id.* at 320–21 (describing MNCs as owners of intellectual property rights, and FIEs as licensees of intellectual property rights).

59. See *id.* at 321 (“The licensees have a right to use the licensed intellectual property, but they acquire no ownership rights.”).

60. See *id.* (explaining that an MNC first acquires intellectual property rights in China under its own name).

61. See *id.* (providing that after acquiring intellectual property rights in its own name, an MNC licenses intellectual property rights to an FIE).

62. See *id.* (differentiating the rights of MNC owners from the rights of FIE licensees).

63. See *id.* at 102 (“Once the joint venture is established, it will issue a certificate to each of the joint venture partners stating their equity interests. This certificate also serves as proof of the ownership interest of each partner in the joint venture.”).

64. See *id.* at 321 (“If, for any reason, the licensing agreements between [the MNC] and its China FIEs are terminated, [the MNC] remains the undisputed owner of the technology.”).

65. See Patent Law of the PRC (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 27, 2008, effective Oct. 1, 2009) (China) (providing that novelty, creativity, and practical use are required under Chinese law); see also 35 U.S.C. §§ 102–03 (2006) (providing that novelty, nonobviousness, and utility are required under U.S. law). Although China's terms differ slightly from those used by the United States, they are deemed to be equivalent. Both U.S. and Chinese law are implementations of the requirements that are set forth in the Agreement on Trade-Related Intellectual Property Rights (TRIPs), a mandatory obligation of the World Trade Organization. Article 27 of TRIPs provides that “patents shall be available for

may also be reasons why an MNC will choose trade secret protection for its proprietary know-how even if the know-how qualifies for patent protection. Assume, for example, that an MNC uses a complex chemical formula to produce an industrial product, like the rubber resin used in making tires for automobiles.⁶⁶ Or, suppose that the MNC uses proprietary mathematical data and formulas for a design of an advanced truck axel for trucks that can haul very heavy loads.⁶⁷ The MNC might choose to protect the know-how as a trade secret as opposed to using patent law because a patent has a maximum term of protection of under U.S. and Chinese law of twenty years, after which the know-how enters the public domain.⁶⁸ A trade secret, however, can be protected indefinitely, so long as it is not disclosed to the public.⁶⁹ To protect its proprietary technology for an indefinite and unlimited period, the MNC might chose to treat the technology as a trade secret. One of the most famous examples of know-how that is protected as a trade secret is the formula for Coca-Cola.⁷⁰ Business executives at Coca-Cola made the decision to forgo patent protection

inventions . . . [that] are new, involve an inventive step, and are capable of industrial application." An accompanying footnote states that "the terms 'inventive step' and 'capable of industrial application' may be deemed by a Member to be synonymous with the terms 'non-obvious' and 'useful' respectively." All WTO members, including China and the United States, must include these requirements as a condition of patentability.

66. This observation is based upon the author's experience serving as an expert witness in an intellectual property dispute involving an MNC doing business in China.

67. This observation is based upon the author's experience serving as a consultant for an MNC doing business in China.

68. The Agreement on Trade-Related Intellectual Property Rights (TRIPs), a mandatory obligation of the World Trade Organization, requires a minimum patent protection term of twenty years that must be implemented by all of its members, which includes China and the United States. See 35 U.S.C. § 154 (2012) (providing for the contents and terms of patents); Patent Law of the PRC art. 10 ("If a Chinese unit or individual intends to transfer the right to apply for a patent or patent rights to a foreigner, foreign enterprise or other foreign organization, it or he shall perform the procedures in accordance with the provisions of relevant laws and administrative regulations."); Agreement on Trade-Related Intellectual Property Rights art. 33, Apr. 15, 1994, 1869 U.N.T.S. 299, 33 I.L.M. 1197 [hereinafter TRIPs] ("The term of protection available shall not end before the expiration of twenty years counted from the filing date.").

69. See *Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa* (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat'l People's Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 10 (China) (describing what amounts to infringement of a trade secret and what qualifies as a trade secret); see also Li Mi, *Trade Secrets and Patents Compared*, CHINA LAW & PRACTICE, <http://www.chinalawandpractice.com/Article/3253061/Channel/7576/Trade-secrets-and-patents-compared.html> [<http://perma.cc/TV82-BUD6>] (archived Aug. 31, 2014) (2013) ("[T]he duration of trade secret protection is indefinite.").

70. See Gene Qinn, *Vault with Coca Cola Trade Secret Formula on Public Display*, IPWATCHDOG, <http://www.ipwatchdog.com/2012/01/06/vault-with-coca-cola-trade-secret-formula-on-public-display/id=21588/> [<http://perma.cc/4X3R-BUH6>] (archived Aug. 31, 2014) (describing the measures that have been taken to keep the Coca-Cola formula a secret).

for the formula for Coca-Cola, protecting it as a trade secret in order to be able to protect the formula indefinitely.⁷¹

If an MNC protects its basic technology through trade secrets law, the MNC should license the trade secrets to the FIE. Note the basic difference between the licensing by an MNC of its trademarks and patents to an FIE, and the licensing of its trade secrets to an FIE in China. When an MNC licenses its trademarks or patents, the MNC first obtains a registration of the trademark or patent in China, and then licenses the right in a separate agreement to the joint venture or WFOE. The registration is official documentary evidence of ownership of the intellectual property right by the MNC. In the case of trade secrets, the MNC cannot register the trade secrets in China as there is no mechanism under Chinese law for such registration.⁷² Under China's present legal regime, the MNC has no mechanism under Chinese law that conclusively establishes that the Chinese government recognizes that the MNC is the owner of a trade secret before Chinese courts, administrative, or other enforcement authorities.⁷³ The inability to obtain an official documentation of ownership leads to traps in the enforcement process as discussed further in the next part of this Article.⁷⁴

The MNC should nevertheless enter into a written licensing agreement for its trade secrets with its Chinese FIEs. This licensing agreement will help to establish that the MNC is the owner of the trade secrets and will dispel any confusion that the joint venture or the WFOE has any ownership rights in the trade secrets. Under Chinese law, the licensing agreement must be in writing to be valid.⁷⁵ The licensing agreement should also set out the chemical formulas, as discussed in the examples above, and any other trade secrets in detail so the MNC has a full written record of its trade secrets. Otherwise, without a written record of the trade secrets, it will become much more difficult to argue before the Chinese authorities that the MNC's trade secrets have been stolen. If the MNC does not have a licensing agreement with a detailed written record of the trade secrets, the MNC will likely face higher evidentiary burdens in order to satisfy

71. Coca-Cola's formula has been protected as a trade secret since 1886. *See id.* (explaining that Coca-Cola's formulation has been kept a close secret since its invention by Dr. John S. Pemberton).

72. The author and the library research staff at the Moritz College of Law has done an exhaustive search of China's legal system and found no official government registration system for trade secrets.

73. *See id.*

74. *See infra* Part III(B)-(C).

75. *See* Zhong Hua Ren Min Gong He Guo He Tong Fa (中华人民共和国合同法) [Contract Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., Mar. 15, 1999, effective Oct. 1, 1999), art. 342 (China) (defining technological transfer contract and stipulating that such a contract must be in writing).

the demands of Chinese authorities that the MNC prove that it owns trade secrets.

A written licensing agreement between the MNC and its FIE can help to resolve any disputes over which entity owns the trade secret. Returning to the earlier example involving laundry detergent, suppose that the MNC gives access to its proprietary detergent formula to its joint venture but does not have a written licensing agreement protecting the formula as a trade secret. The local partner in the joint venture, a Chinese state-owned enterprise, might use the proprietary formula to improve the quality of its own detergent products under its own brand name that it manufactures separately from the joint venture. Such an act could lead to tensions between the MNC and the Chinese state-owned enterprise because the MNC might see this action as a breach of trust.⁷⁶ From the local partner's perspective, however, nothing has been stated about the proprietary nature of the know-how, and the local partner believes that obtaining access to advanced technology is one of the major reasons why it entered into the joint venture in the first place. A written licensing agreement could prevent this type of incident and the hostilities that might ensue. A licensing agreement provides a written record of who owns the trade secret and the scope of the covered trade secret so there is no doubt about the illegality of a separate use by the local partner.

Even in cases where the MNC has not transferred a basic technology as a trade secret to its FIE in China as part of establishing the joint venture or wholly foreign-owned enterprise, it is all but inevitable that the MNC's Chinese FIEs will develop confidential information that the MNC will want to protect as trade secrets in the course of doing business over a period of time in China. Returning to the example of a joint venture producing laundry detergent, the joint venture will manufacture products that will be sold under the trademarks licensed to the FIE by the MNC. In order to succeed in any competitive sector, such as the consumer products market, the MNC's Chinese business entities will need to engage in strategic business decisions, such as marketing and advertising, product promotions, logistics, strategies for dealing with competitors, and overall strategies for the Chinese market.⁷⁷ Over the course of several years, management-level business executives could accumulate a

76. This incident is based upon the author's own work experience in China. The tensions that ensued as a result of the local partner's use of the MNC's proprietary technology led to the termination of the joint venture.

77. See Mi, *supra* note 69 ("Virtually any business information can be protected as a trade secret provided appropriate measures are taken to keep it confidential. Trade secrets can include technical information such as formulae, patterns, processes, devices, designs, drawings, programs, new product information before market launch and commercial information like actual or potential supplier or customer lists, management techniques, marketing, sales and advertising strategies.").

great deal of valuable confidential information: financial data, customer lists, new product development, and new marketing strategies.⁷⁸ Similarly, in most competitive industries in China, the vast majority of MNCs doing business in China develop valuable confidential information that the MNC will wish to protect even if the trade secret is not part of the basic technology that was transferred under the original licensing agreement when the joint venture or WFOE was first established.

The importance of trade secrets to MNCs doing business in China raises the question of whether rights in trade secrets can be effectively enforced in China. The next part of this Article examines China's legal framework for enforcing trade secrets and the issues that can arise.

III. CHINA'S LEGAL FRAMEWORK FOR PROTECTING TRADE SECRETS

Unlike trademarks, patents, and copyrights, trade secrets in China are not governed by a unified law but are subject to scattered provisions in different laws.⁷⁹ This fragmented legal framework creates a host of problems for MNCs that seek to enforce their trade secrets, make amendments to the laws, or create a unified law. The fragmentation is due to vested interests by different authorities interested in protecting their own sphere of authority. Although there are many possible explanations for the lack of a comprehensive law, and a detailed examination of such causes is beyond the scope of this Article, one possible explanation is that, unlike the other major forms of intellectual property, trade secrets do not enjoy substantial protections in the World Trade Organization (WTO).⁸⁰ Under the WTO, all member countries, including the United States and China, are obligated to provide substantial protections for trademarks, patents, and copyrights.⁸¹ Comprehensive international treaties governing trademarks, patents, and copyrights have existed for over

78. See *id.* ("Any technology, know-how or business information that has been kept confidential will constitute a trade secret.").

79. See *infra* Part III.A.

80. The WTO is the world's most important multilateral organization dealing with international trade. The WTO has major treaties dealing with the trade in goods, services, and intellectual property. The WTO treaty dealing with international property is TRIPs.

81. Becoming a member of TRIPs is mandatory at the same time that a country becomes a member of the WTO. See CHOW & SCHOENBAUM, *supra* note 45, at 589 (The effect of TRIPs . . . is that all WTO members must now enact IP laws that meet the minimal substantive standards of TRIPs . . ."). TRIPs Articles 9–14 create obligations related to copyrights, TRIPs Articles 15–21 create obligations related to trademarks, and TRIPs Articles 27–34 create obligations related to patents.

one hundred years.⁸² These treaties have now been incorporated, in substantial part, into the WTO. This incorporation creates mandatory obligations for all WTO members.⁸³ The WTO, however, contains only one provision relating to the protection of trade secrets with which China seems to be in compliance.⁸⁴ Prior to joining the WTO in 2001, China spent years revising its patent, trademark, and copyright laws in order to comply with TRIPs but did not make any revisions to the 1993 Anti-Unfair Competition Law, the major legislation applying to trade secrets. It is possible that China's lack of a comprehensive law on trade secrets can be traced to a lack of substantial treaty obligations relating to trade secrets.⁸⁵ The reality is that for now, and for the near future, China has a number of provisions scattered throughout its laws that relate to trade secrets. It is important to

82. See Paris Convention on the Protection of Industrial Property, Mar. 20, 1883, 21 U.S.T. 1538, 828 U.N.T.S. 11851 [hereinafter Paris Convention] (last revised July 14, 1967) (applying to patents and trademarks); see also Berne Convention for the Protection of Literary and Artistic Works, Sept. 9, 1886, 1161 U.N.T.S. 18338 [hereinafter Berne Convention] (last revised July 24, 1971) (applying to copyrights).

83. TRIPs Article 2 incorporates Articles 1–12 and Article 19 of the Paris Convention applicable to patents and trademarks, and TRIPs Article 9 incorporates Articles 1–21 of the Berne Convention applicable to copyright. See TRIPs, *supra* note 68, arts. 2, 9.

84. See *id.* art. 39 (providing for the protection of undisclosed information). The sole provision in TRIPs related to trade secrets is contained in Article 39, which provides in relevant part as follows:

(2) Natural and legal persons shall have the possibility of preventing information lawfully within their control from being disclosed to, acquired by, or used by others without their consent in a manner contrary to honest commercial practices so long as such information:

(a) is secret in the sense that it is not, as a body or in the precise configuration and assembly of its components, generally known among or readily accessible to persons within circles that normally deal with the kind of information in questions;

(b) has commercial value because it is secrets; and

(c) has been subject to reasonable steps under the circumstances, by the person lawfully in control of the information, to keep it secrets.

(3) Members, when requiring, as a condition of approving the marketing of pharmaceutical or of agricultural chemical products which utilize new chemical entities, the submission of undisclosed test or other data, the origination of which involves a considerable effort, shall protect such data against unfair commercial use. In addition, Members shall protect such data against disclosure, except where necessary to protect the public, or unless steps are taken to ensure that the data are protected against unfair commercial use.

Id. Outside of the WTO, there is no major international convention comparable to the Paris Convention (applicable to patents and trademarks) or the Berne Convention (applicable to copyright) that applies to trade secrets.

85. See *id.* (standing alone as the sole TRIPs provision relating to the protection of trade secrets).

understand this fragmented legal framework in order to plan how to best protect trade secrets in China.

A. Existing Laws Applicable to Trade Secrets

The most important law governing trade secrets is the 1993 Anti-Unfair Competition Law (AUCL). Article 10 of the AUCL states in relevant part:

“[T]rade secret” shall mean [1] technical and business information that is unknown to the public, [2] can bring economics benefits to the owner to the right owner, [3] is of a practical nature and is protected by confidentiality measures taken by the rights owner.⁸⁶

Under this definition, trade secrets can include scientific processes, methods, recipes, or business information. Business information can include marketing and advertising strategies, new product development strategies, customer lists, financial data, and terms and prices.⁸⁷ As noted earlier, the vast bulk of MNCs doing business in China have information that falls into these categories when they enter the Chinese market or develop such information after doing business in China for any period of time.⁸⁸ Article 10 of the AUCL further proscribes the following acts of infringing upon trade secrets:

- (1) obtaining a trade secret by theft, promise of gain, duress or any other unfair means;
- (2) disclosing, using, or permitting others to use a right owner’s trade secret that was obtained by any of the means set forth in the preceding item; or
- (3) disclosing, using, or permitting others to use a right owner’s trade secret in that operator’s possession, thus violating an agreement or the right owner’s requirement to keep the trade secret confidential.⁸⁹

An important decision of the Supreme People’s Court has supplemented the AUCL. In 2006, the Supreme People’s Court issued the “Interpretation on Certain Issues Concerning the Application of Law in the Trial of Civil Cases Involving Unfair Competition” (2007 SPC Interpretation).⁹⁰ When the Supreme People’s Court issues

86. See *Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa* (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat’l People’s Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 10 (China) (defining what a trade secret is under the law).

87. See *Mi*, *supra* note 69 (“Trade secrets can include . . . commercial information like actual or potential supplier or customer lists, management techniques, marketing, sales and advertising strategies.”).

88. See *supra* Part II(B).

89. See Anti-Unfair Competition Law of the PRC, art. 10 (defining specific infringing activities).

90. See Interpretation of the Supreme People’s Court on Some Matters About the Application of Law in the Trial of Civil Cases Involving Unfair Competition (promulgated by the Supreme People’s Court, Jan. 12, 2007, effective Feb. 1, 2007)

interpretations of laws, it is exercising legislative power and its interpretations are considered to be authoritative and binding on lower courts.⁹¹ Referring specifically to Article 10 of the AUCL set forth above, the 2007 SPC Interpretation clarified several key elements in the AUCL definition of trade secrets,⁹² including what types of measures satisfy the requirement under the AUCL that the trademark owner has adopted confidentiality measures to protect the trade secret:

[A] right owner has taken confidentiality measures if the right owner has done any of the following and it is sufficient to prevent the confidential information from being disclosed under normal circumstances:

- (1) Restricted the scope of personnel who may know of the confidential information and disclosing the content thereof only to the relevant personnel who must know of it;
- (2) Locked up the carrier of the confidential information or taken other precautionary measures;
- (3) Placed a confidentiality mark on the carrier of the confidential information;
- (4) Encrypted or encoded the confidential information;
- (5) Entered into a confidentiality agreement;
- (6) Restricted the visitors from entering the machinery areas, premises, workshops, and other sites related to the confidential information or subjected visitors to confidentiality requirements; and
- (7) Taken other reasonable measures to ensure the confidentiality of the information.⁹³

Note that of the measures set forth above, a written confidentiality agreement is alone sufficient to satisfy the requirement that the trade secrets owner has taken “confidentiality measures” to protect the trade secret as required by Article 10 of the AUCL. The 2007 SPC Interpretation also confirmed that customer lists can qualify as trade secrets,⁹⁴ and a trade secret that is obtained

(China) [hereinafter 2007 SPC Interpretation], available at <http://www.wipo.int/edocs/lexdocs/laws/en/cn/cn104en.pdf> [<http://perma.cc/YV79-7WBZ>] (archived Sept. 28, 2014) (providing interpretative guidance to the lower courts on how to apply the AUCL).

91. See DANIEL C.K. CHOW, *THE LEGAL SYSTEM OF THE PEOPLE'S REPUBLIC OF CHINA* 179 (2d ed. 2009) [hereinafter CHOW, *LEGAL SYSTEM OF CHINA*] (“The SPC acts as a legislative body when it issues legislative interpretations that supplement and elaborate on existing laws.”).

92. See 2007 SPC Interpretation, *supra* note 90, art. 11 (stating explicitly that it is clarifying the meaning of “confidentiality measures as stipulated in Paragraph 3 of Article 10 of the Anti-Unfair Competition Law”).

93. *Id.*

94. See *id.* art. 13 (“The name list of clients among business secrets generally refers to the special client information that is different from related public information.”).

through independent development or reverse engineering is lawful and does not constitute a violation of the AUCL.⁹⁵

In addition to the AUCL, several other laws apply to trade secrets. Article 43 of the Contract Law generally prohibits a party from disclosing the trade secrets that are made known during contract negotiations regardless of whether a contract is concluded.⁹⁶ Section 3 of Chapter 18 has several provisions regulating technology licensing, including trade secrets.⁹⁷ Among other obligations, the licensee must maintain confidentiality,⁹⁸ cannot exploit the trade secret beyond the scope permitted in the licensing agreement,⁹⁹ and cannot disclose the licensed trade secret to third parties.¹⁰⁰ Article 149 of the Company Law provides that directors or senior management personnel of a Chinese company are prohibited from disclosing trade secrets¹⁰¹ and are liable for damages for breach of this obligation.¹⁰²

Article 22 of the 1995 Labor Law provides that the parties can include a stipulation in the labor contract that the employee will maintain the employer's trade secrets.¹⁰³ Article 102 of the 1995 Labor Law states that if the employee breaches a confidentiality obligation specified in the employment contract, and causes economic

95. *See id.* art. 12 ("As regards obtaining business secrets through development and research by itself or reverse engineering, it shall not be ascertained as an infringement upon business secrets.")

96. *See* Zhong Hua Ren Min Gong He Guo He Tong Fa (中华人民共和国合同法) [Contract Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., Mar. 15, 1999, effective Oct. 1, 1999), art. 43 (China) (prohibiting the disclosure of trade secrets obtained during contract negotiation regardless of whether or not a contract is formed).

97. *See id.* arts. 342-43, 347-49, 351-54 (describing the requirements for a technological transfer contract and the penalties in place for infringing on another party's trade secrets).

98. *See id.* arts. 348, 350 (establishing the duty of maintaining confidentiality of a company's trade secrets when entering into a contract with that company).

99. *See id.* art. 351 (establishing liability when a party discloses another company's trade secrets or in some other fashion breaches the duty of maintaining confidentiality).

100. *See id.* (establishing liability when a party allows a patent to be exploited or a technical secret to be used by a third person).

101. *See* Zhong Hua Ren Min Gong He Guo Gong Si Fa (中华人民共和国公司法) [Company Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., Oct. 27, 2005, effective Jan. 1, 2006), art. 149(7) (China) (barring directors or senior managers from disclosing company secrets).

102. *See id.* art. 150 (making directors and senior managers who disclose company secrets liable for company losses resulting from the disclosure).

103. *See* Zhong Hua Ren Min Gong He Guo Lao Dong Fa (中华人民共和国劳动法) [Labor Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., July 5, 1994, effective Jan. 1, 1995), art. 22 (China) (providing for the inclusion of provisions in an employment contract safeguarding a company's trade secrets).

harm to the employer, the employee is liable for damages.¹⁰⁴ Article 23 of the 2008 Labor Contract Law provides that the employer and employee can include both a confidentiality clause and a non-competition clause in the labor contract.¹⁰⁵ Under a confidentiality clause, the employee is bound to keep trade secrets confidential. Under the non-competition clause, the employer is allowed to prevent the employee, after termination of employment, from working for a business that manufactures products similar to that of the former employer or that competes with the former employer.¹⁰⁶ Through the non-competition clause, the employee is also prohibited from establishing his or her own business that manufactures similar products or otherwise competes with the former employer.¹⁰⁷ Under the 2008 Labor Contract Law, a non-competition agreement has a maximum term of two years¹⁰⁸ and must be supported by the payment of monthly compensation.¹⁰⁹ Since the majority of trade secrets cases involve current or former employees who are induced to work for a competitor, the provisions of the 2008 Labor Contract Law are especially important in supplementing the AUCL and will be the subject of an extended examination in a later section of this Article.¹¹⁰

B. Enforcement Authorities

Several different enforcement authorities have jurisdiction over trade secrets cases under the AUCL and other laws. The Administration of Industry and Commerce (AIC), an administrative

104. See *id.* art. 102 (establishing liability for laborers who revoke labor contracts under specified circumstances).

105. See *Zhong Hua Ren Min Gong He Guo Lao Dong He Tong Fa* (中华人民共和国劳动合同法) [Labor Contract Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., June 29, 2007, effective Jan. 1, 2008), art. 23 (China) (allowing for a non-competition provision in an employment contract provided that the employer continues to pay employee during the non-compete term).

106. See *id.* art. 24 (outlining who may be subject to a non-competition provision and defining activities prohibited during the term).

107. See *id.* (“[A] person shall be subject to non-competition provisions in terms of his working for a competing Unit that either reproduces the same type of products or is engaged in the same type of business as his current Unit, or in terms of his establishing his own business to produce products or engage in business competing with his current Unit’s products or business . . .”).

108. See *id.* (stating that the term of a non-competition clause “shall not exceed two years”).

109. See *id.* art. 23 (“If a laborer has an obligation to maintain the confidentiality of his Unit’s trade secrets, the Unit may agree with the laborer on the inclusion of non-competition provisions in the labor contract or a separate confidentiality agreement, and stipulate that the Unit shall pay economic compensation to the laborer on a monthly basis during the term of non-competition after the termination of the labor contract.”).

110. See *infra* Part IV (discussing preventative strategies that the MNC can take to ensure trade secrets protection).

body, has the authority to seize products or documents, order the infringer to cease the infringing activity, and to impose a fine of between roughly 1,700 to 33,000 U.S. dollars.¹¹¹ The AICs, however, have no authority to order compensatory damages or to issue permanent injunctions.¹¹² The advantage of an administrative proceeding before the AIC is speed. The AICs will, if presented with satisfactory evidence, act in a matter of days or even immediately. In the case of trademark counterfeiting over which the AICs also have authority, the AICs have been known to act immediately within as little as fifteen to thirty minutes when presented with evidence of counterfeits.¹¹³ The plaintiff can also bring an action to enforce trade secrets in a People's Court. The courts have the authority to issue evidence preservation orders, issue injunctions, and award compensatory damages.¹¹⁴ An evidence preservation order is important because the order, usually administered directly by the judge in person against the defendant on the suspect premises, can preserve evidence that the defendant would otherwise likely destroy and, as noted earlier, all Chinese authorities find, in general, that only documentary evidence has probative value.¹¹⁵ The disadvantage of proceeding in court in China is that there is no system of discovery similar to that available under the U.S. civil litigation system. If the plaintiff seeks an evidence preservation order, the plaintiff will need to know, in advance of the order, about the existence of the evidence. If the confidentiality clause protecting trade secrets is contained in an employment contract, the case can also be brought in a labor arbitration commission with an appeal to a People's Court.¹¹⁶ If the employee is the plaintiff, the employee will often choose to bring the

111. See *Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa* (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat'l People's Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 25 (China) ("In case a business operator violates the provisions of Article 10 of this law and infringes upon trade secrets, the supervision and inspection department shall order the ceasing of the illegal acts and may impose a fine of not less than 10,000 yuan but not more than 200,000 yuan in light of the circumstances.").

112. See *id.* Nothing in the Anti-Unfair Competition Law authorizes compensatory damages or a permanent injunction.

113. See *Chow, Anti-Counterfeiting*, *supra* note 32, at 761 (noting that if PRC authorities were already familiar with MNCs representatives, then PRC authorities will often, within "fifteen minutes to half an hour, initiate a raid").

114. See *Civil Procedure Law of the PRC* (promulgated Oct. 28, 2008, effective Apr. 1, 2008, and revised on Jan. 1, 2013), art. 100 (China).

115. See *ORRICK, HERRINGTON & SUTCLIFFE LLP*, *supra* note 28, at 865–66 (explaining that "the court may, among other things, question the respondent" and "conduct an inspection of [the] premises" to ensure evidence preservation).

116. See *Labor Arbitration Law of the PRC*, art. 5 (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 29, 2007, effective May 1, 2008) (China) (stating that if the parties are not willing to have a consultation or if the consultation fails, then they can submit an application for mediation to a mediation institute).

case in a labor arbitration commission, which is viewed as more sympathetic to employees.¹¹⁷ For the same reason, employers will usually choose to go directly to court to enforce the trade secret under the AUCL, rather than choose labor arbitration.¹¹⁸

Unlike many other countries, China also has criminal penalties for breach of trade secrets. Article 219 of the Chinese Criminal Law imposes criminal liability on anyone who discloses or acquires a trade secret by illegal means when the act causes “serious” or “exceptionally serious” losses to the owner of the trade secret.¹¹⁹ All criminal cases are initiated and conducted by the Chinese police, the Public Security Bureau (PSB).¹²⁰ Criminal cases are prosecuted in a People’s Court by a procuratorate.¹²¹ A major advantage of pursuing a criminal case is that the PSB has wide investigatory powers at its disposal in all criminal cases, including the abilities to make an inquest on site, seize documents, inspect the premises, and issue orders to the defendant to produce information.¹²² Most defendants do not feel safe ignoring PSB investigatory powers.¹²³ These powers, and the fact that trade secrets can be protected by criminal actions, are especially important in light of the lack of a discovery system in China in civil cases.¹²⁴ Bringing a criminal action, however, has other problems that are highlighted in the discussion below.

117. See ORRICK, HERRINGTON & SUTCLIFFE LLP, *supra* note 28, at 855 (“According to statistics, employees win or partially win in most labor arbitrations.”).

118. See *id.*

119. See *Zhong Hua Ren Min Gong He Guo Xing Fa* (中华人民共和国刑法) [Criminal Law of the PRC] (promulgated by the Standing Comm. Nat’l People’s Cong., Mar. 14, 1997, effective Oct. 1, 1997), art. 219 (China) (stating the different levels of punishment for infringing on business secrets, ranging from fixed-term imprisonment of no more than three years for causing “heavy losses” to fixed-term imprisonment of three to seven years for “especially serious” infringements). The statute does not further define “serious” or “especially serious” offenses, leaving it to the discretion of the Public Security Bureau.

120. See CHOW, LEGAL SYSTEM OF CHINA, *supra* note 91, at 263 (“The Ministry of Public Security, under the State Council, has overall responsibility for the police force of the PRC. At the local level, among other police functions, public security bureaus generally handle the first stages of the criminal process in the PRC.”).

121. See *id.* at 218 (“The procuratorate, modeled on the institution of the procuracy in the former Soviet Union, performs the tasks of approving arrests by the public security organs and prosecuting criminal cases . . .”).

122. See *id.* at 263–64 (discussing the powers of the police in the investigatory stage).

123. See *id.* at 263–65 (noting that these investigative powers of the PSB are backed by various coercive measures, such as detention, interrogation, and arrest).

124. See Mark Cohen, “Case Filing” in *China’s Courts and Their Impact on IP Cases*, CHINA IPR (Mar. 24, 2012) (noting the “lack of discovery type procedures for all civil cases in China”), <http://chinaipr.com/2012/03/24/case-filing-in-chinas-courts-and-their-impact-on-ip-cases> [<http://perma.cc/A9ED-FL7E>] (archived Sept. 2, 2014).

C. High Evidentiary Burden and Traps in the Enforcement Process

The 2007 SPC Interpretation of the Anti-Unfair Competition Law, discussed above, also sets forth the burden of proof in a trade secrets case:

Where a party alleges that another infringes its trade secret, the party shall bear the burden of proof [1] as to the fact that the trade secret it has possessed is in conformity to the statutory requirements, [2] that the other party's information is identical or substantially identical to its trade secret and [3] that the other party has adopted unfair means.¹²⁵

Step one in the burden of proof requires the plaintiff to prove that it owns a trade secret as defined by statutory requirements set forth in Article 10 of the AUCL.¹²⁶ Step two requires the plaintiff to prove that the defendant has the trade secret in its possession.¹²⁷ Step three requires the plaintiff to prove that the defendant has obtained the trade secret by illegal means.¹²⁸

In order to prove step one, the plaintiff must prove that it owns a trade secret by demonstrating that its information satisfies the statutory requirements of a trade secret as set forth in Article 10 of the AUCL—that there exists technical and business information unknown to the public, that the information has economic and practical value, and that the owner has taken measures to maintain confidentiality. Step one is frequently disputed.¹²⁹ The existence of technical and business information that can qualify as a trade secret is the most heavily disputed element in the AUCL statutory definition.¹³⁰ The second element, economic and practical value of the information, is almost never disputed.¹³¹ The third element can be

125. 2007 SPC Interpretation, *supra* note 90, art. 17.

126. See Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat'l People's Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 10 (China) (“Trade Secrets’ mentioned in this Article refers to any technology information or business operation information which is unknown to the public, can bring about economic benefits to the obligee, has practical utility and about which the obligee has adopted secret-keeping measures.”).

127. See 2007 SPC Interpretation, *supra* note 90, art. 17 (defining the second requirement of the burden of proof in trade secrets cases).

128. See Anti-Unfair Competition Law of the PRC, *supra* note 126 (discussing the means by which a business operator is prohibited from infringing upon trade secrets).

129. See *id.* (defining “trade secrets”).

130. See ORRICK, HERRINGTON & SUTCLIFFE LLP, *supra* note 28, at 856–57 (identifying the requirements and indicating that “requirement (2) is almost never disputed. Requirement (3) is often disputed. The most heavily disputed issue is requirement (1)”).

131. See *id.*

satisfied by a confidentiality agreement alone or other measures set forth in the 2007 SPC Interpretation.¹³²

The first issue—the existence of technical and business information that can constitute a trade secret—is heavily disputed and can be a troublesome issue for an MNC. A comparison between the enforcement of trademarks and trade secrets can be a useful guide to understanding the issue. In a trademark dispute, the owner proves its ownership of a trademark by the mere act of submitting to the enforcement authorities a copy of the trademark registration certificate issued by the China Trademark Office.¹³³ As noted earlier, China has an official registration system for trademarks. If the MNC submits a copy of the trademark certificate, the MNC submits proof that it owns the trademark. If the MNC's FIE is a licensee of the trademark, the representatives of the joint venture or WFOE may need to produce both a copy of the trademark certificate in the name of the MNC and a copy of the licensing agreement that authorizes the joint venture or WFOE to enforce the trademark on behalf of the MNC.¹³⁴ By contrast, China has no registration system for trade secrets, so proving the existence of a trade secret can be a far more difficult burden.¹³⁵ If the MNC has a written licensing agreement that sets forth the trade secret in detail, as recommended in Part II above, the MNC should submit a copy to the Chinese enforcement authorities. Chinese authorities almost always insist on documentary evidence because they are fearful of acting outside their scope of authority. If the MNC has no documentary evidence at all of the existence of the trade secret, the MNC might find that the authorities will refuse to accept the case. If the MNC has documentary evidence that is general in nature, such as a general clause in a labor contract that refers to confidential information without details about the nature of the information, the Chinese authorities might also be

132. See 2007 SPC Interpretation, *supra* note 90, art. 11(7) (“It shall be determined that a right owner has taken any confidentiality measures if the right owner has . . . (7) [t]aken other reasonable measures to ensure the confidentiality of the information.”).

133. See (中华人民共和国商标法) [Trademark Law of the PRC] (promulgated Aug. 30, 2014, effective May 1, 2014), ch. 1, art. 3 (China) (“A trademark registrant shall be entitled to the exclusive right to use the registered trademark and such right shall be protected by law.”). The revised 2014 Trademark Law amends and replaces the 2001 Trademark Law. Unless otherwise indicated, all references to the PRC Trademark Law will refer to the 2014 Trademark Law.

134. The licensing agreement should include a provision that authorizes the licensee to enforce the trademark rights on behalf of the trademark owner, the MNC. However, based on the author's own working experience in China, the author has found that the Chinese authorities usually do not even ask to see a copy of the licensing agreement. The authorities seem to assume that if the MNC owns the trademark, its joint venture or WFOE has the right to enforce the trademark on behalf of the MNC.

135. See Ong, *supra* note 8 (noting the lack of a formal registration system for trade secrets with Chinese authorities).

reluctant to move without further documentary evidence. The best scenario is to present a document, such as a licensing agreement, with details on the scope of the confidentiality obligation and with the technical or business information set forth in detail.

In some cases, even if the MNC has a written document, the Chinese enforcement authorities might still be reluctant to move forward without written certification that a trade secret violation exists from an approved state-owned technology consultancy organization.¹³⁶ This is easily understood by noting that the second element in the burden of proof set forth in the 2007 SPC Interpretation is that “the other party’s information is identical or substantially identical to its trade secret.” For example, suppose that the MNC has used a written agreement to license a chemical process to its Chinese business entity and now believes that a former employee has stolen the chemical process and has gone to work for a competitor. Suppose further that the MNC has decided to bring a criminal enforcement action through the PSB because the PSB has the power to order the defendant to produce internal documents. While the PSB is empowered to investigate economic crimes, the PSB does not have expertise in trade secrets involving advanced technology, such as a chemical process or a product design. To move forward with the trade secrets investigation, the PSB will entrust the trade secrets issue to a state-owned technology research institute or consultancy organization to determine the first two steps of the burden of proof set forth by the 2007 SPC Interpretation: (1) whether the plaintiff owns technical and business information and (2) whether the defendant has possession of the identical or substantially similar information.¹³⁷ Such a process can take months and be quite complex; the state-owned research institute may have to engage in extensive tests and analysis of the two chemical processes to determine whether they are identical or substantially the same. If the case had been brought in a civil court, instead of as a criminal case, the civil court might have to rely on the same analysis as the court may find that it lacks the expertise to make such a comparison on its own. If the state-owned technology institute determines that the first two evidentiary steps have been met—that the MNC owns technical and business information and that defendant possesses identical or substantially similar information—then the state-owned technology institute will issue a report with such a finding to the PSB. The MNC

136. For the list of approved technology appraisal organizations, see the Sup. People’s Ct., Reply to China Science and Technology Consultancy Service Center about “Report of Application for Incorporation of Judicial Appraisal Institution into the Roster” (Apr. 9, 2003).

137. See 2007 SPC Interpretation, *supra* note 90, art. 14 (setting forth the burden of proof in a trade secret case).

must then still prove the third step in the burden of proof, that the defendant obtained the information by illegal means.

1. Enforcement of Trademarks and Trade Secrets

Before examining some of the treacherous pitfalls and traps involved in this process, compare the enforcement of trademarks, also viewed as part of the law of unfair competition and covered by the AUCL,¹³⁸ with the enforcement of trade secrets. In a typical case involving either trademark counterfeiting or substantial but not identical copying, the MNC will also approach a local branch of the AIC, which has enforcement authority over trademarks, as well as trade secrets.¹³⁹ The MNC will display a copy of its trademark registration certificate issued by the China Trademark Office, conclusive proof of its ownership of the trademark. The MNC will also then give the AIC officials some samples of counterfeits or knock-offs of its trademarked product that it has purchased from some nearby location. The MNC will then state that the samples are unauthorized counterfeits or knock-offs. Note that these two simple steps allow the MNC to assert a claim of trademark counterfeiting or infringement: (1) a copy of its trademark registration certificate and (2) a statement from a representative of the MNC that the knock-offs are unauthorized.

Convincing the authorities to act is often facilitated by the use of private investigators. Many private investigators have already built a relationship with the AIC through previous enforcement actions. In many cases, especially if the private investigators know the local authorities, these simple steps, which can be accomplished in as little as half an hour, are all that is necessary to trigger a raid by the AIC of the suspected premises where the counterfeits are made. In half an hour or less after the initial discussion, AIC officials, accompanied by the private investigator and representatives from the MNC trademark owner, will get into a government vehicle, and, once in the vehicle, the investigators will give the officials directions to the suspect premises. The investigators will wait until all AIC officials are in the vehicle and en route to reveal the location in order to avoid tip-offs. Once the AIC officials reach the premises, a raid occurs in which the counterfeits or infringing products are seized.

The speed with which the enforcement action occurs is one of the major attractions of this method,¹⁴⁰ but the speed is due to two

138. Trademarks are also governed by the 2014 Trademark Law of the PRC, *supra* note 133.

139. The following procedures are based upon the author's own experience in enforcing trademarks and trade secrets while working as an in-house counsel for an MNC in China.

140. While the enforcement action is expeditious, the problem lies in the penalties. In most cases, the penalties are so light that they do not create any

factors that significantly distinguish trademark cases from trade secrets cases. First, proof of ownership of a trademark is accomplished by simply presenting a copy of the trademark registration certificate. This is not possible in the case of trade secrets since no registration system for trade secrets exist.¹⁴¹ The MNC must prove it owns trade secrets by submitting internal documents that may, or may not, be persuasive to enforcement authorities without outside verification by a state-owned technology institute. Second, the proof of an infringement of a trademark right can be accomplished by the MNC trademark owner's statement—sometimes an oral statement is sufficient—that the counterfeits or knock-offs are unauthorized copies.¹⁴² The Chinese authorities will accept the MNC's statement that the counterfeits are unauthorized copies and can, by a simple visual comparison of the counterfeits with the genuine products and the trademark certificate provided by the MNC, determine that an infringement has occurred. This simple process stands in stark contrast to the complex and time-consuming process involved in proving a trade secrets violation to the AIC or the PSB.

While the need to have the existence of the trade secrets and its infringement verified by a state-owned research institute is alone an additional and time-consuming burden, many MNCs will find that there are some additional legal risks involved in the verification process. The PSB is charged with enforcement against all crimes but always places priorities on violent crimes. The PSB may have little interest in economic crimes, unless these economic crimes result in harm to the public (e.g., counterfeit liquor or baby formula that can result in deaths to consumers) or threaten national security (e.g., smuggling). The PSB might have little interest in investigating a trade secrets case involving an MNC where the only harm is that an MNC with deep pockets is losing profits. In these cases, the PSB has been known to ask for "case fees," a cash payment of approximately 10,000 U.S. dollars, depending on the case,¹⁴³ for accepting the case. Case fees are used ostensibly to reimburse the PSB for expenses incurred in the investigation. Case fees are technically illegal under

deterrence to further illegal activity but, in fact, might have the opposite effect, inciting even more counterfeiting. See Chow, *Anti-Counterfeiting*, *supra* note 32, at 759, 765–76 (discussing flaws with the current enforcement approach and noting that "[t]he overall picture . . . is that there is a torrent of enforcement activity in China, but with little or no deterrence.").

141. See Ong, *supra* note 8 (stating that trade secrets are "not formally registered with government authorities").

142. This observation is based on the author's own experience in working with AIC enforcement authorities in China.

143. When the author was working on a trade secrets case as an in-house counsel in China, the author experienced first-hand being asked for a case fee by the PSB.

Chinese law,¹⁴⁴ although they are common when MNCs seek police help in investigating certain “victimless” economic crimes, that is crimes like counterfeiting or trade secrets where no person has been injured and the issue is one of economic losses suffered by the MNC. Given the recent heightened concern with bribery of foreign officials under the U.S. Foreign Corrupt Practices Act (FCPA), a U.S.-based MNC might also be at risk for an FCPA investigation by the U.S. Department of Justice for such a cash payment to the PSB.¹⁴⁵

Even if the PSB accepts the case, the PSB may be unwilling to proceed with the investigation unless the existence of the trade secrets and its possession of the identical or similar information by the defendant are verified by a judicial appraisal report from an approved state-owned technology appraisal consultancy organization.¹⁴⁶ In any case involving complex trade secrets, the PSB will lack the expertise to determine if a trade secret exists and has been stolen but will likely seek an expert's report. If the trade secrets need to be examined by a state-owned technology appraisal consultancy organization, the organization will also be entitled to charge an appraisal fee in accordance with Chinese law.¹⁴⁷ If the PSB accepts the case and entrusts the case to the state-owned technology appraisal consultancy organization to do an analysis of the trade secrets, the PSB, as the entrusting authority, should pay the appraisal fee.¹⁴⁸ However, in practice, the PSB will usually ask the MNC to pay the appraisal fee.¹⁴⁹ If the MNC pays a fee on behalf of the PSB that should have been paid by the PSB, then that act

144. Charging case fees is illegal under PRC law. See Article II of the Circular of the Ministry of Public Security on Prohibition of Demanding Money and Valuable from All Parties and Supporters during Criminal Case Proceeding, Notice No. 725 (1998) (“It is strictly prohibited to charge all parties during criminal processing in various names. It is not allowed to accept the case processing fee paid by the interested parties in various names for any reason. Where commission may be or is permitted during case processing as previously provided, immediate rectification shall be carried out. Any violation against provisions shall be investigated and punished strictly.”).

145. See Daniel Chow, *China Under the Foreign Corrupt Practices Act*, 2012 WIS. L. REV. 574 (2012) (highlighting the recent rise in FCPA cases involving China).

146. See Sup. People's Ct., Reply to China Science and Technology Consultancy Service Center, *supra* note 136 (offering a selected list of approved technology appraisal organizations).

147. See Decree of Ministry of Justice on General Rules on the Procedures for Judicial Appraisal, art. 8 (promulgated July 18, 2007, effective on Oct. 1, 2007) (“The judicial appraisal institutions shall uniformly charge for the judicial appraisal fees. The charging items and standards shall be subject to relevant national provisions.”).

148. See *id.* arts. 8, 11 (indicating that the technology consultancy organization can charge a fee (Article 8), that the organization must be entrusted with the appraisal (Article 11), and that the entrusting party must pay the judicial appraisal fee as it is the entrusting party that requests the appraisal).

149. This observation is based upon the author's own working experience in China.

appears to be in violation of Chinese law¹⁵⁰ and may also implicate issues under the FCPA.¹⁵¹ If the MNC refuses to pay the appraisal fee on behalf of the PSB and the state-owned research institute refuses to issue an expert's report, then the PSB will take no further action in investigating the case.¹⁵² In addition, it is possible that the research institute will pressure the MNC for additional payments beyond the regular appraisal fee in order to secure a favorable result.¹⁵³ It is also possible that both the PSB and the research institute will ask for more payments if additional, unexpected steps are required.¹⁵⁴ These considerations indicate that an MNC could become ensnared in a web of questionable legality involving repeated demands for payments once the MNC seeks help from the PSB and a technical analysis of the trade secrets and their infringement as part of its burden of proof.

2. Legal Risks in Enforcing Trade Secrets

The discussion above indicates that MNCs seeking to enforce their trade secrets are faced with some daunting risks. In a typical scenario, the MNC finds that an ex-employee, armed with trade secrets from his former employer, has accepted, or is about to accept, employment with a competitor. If the MNC chooses to use administrative authorities, the AICs have limited investigatory powers, have no authority to award compensatory damages, and have no authority to issue an injunction permanently preventing the employee from disclosing trade secrets.¹⁵⁵ If the MNC files a civil court action, the MNC will find that there is no civil discovery system,

150. See Article II of the Ministry of Public Security Notice No. 725, *supra* note 144 (stating that it is illegal for the PSB to "accept the case processing fee paid by the interested parties in various names for any reason."). If the PSB is required to pay a judicial appraisal fee and the PSB asks the MNC to pay the judicial appraisal fee in what guise, then the PSB appears to be in violation of Article II of Notice No. 725. *Id.*

151. See Chow, *China Under the Foreign Corrupt Practices Act*, *supra* note 145, at 595-96 ("The DOJ might find that MNCs are knowingly making payments to third parties who will then pass on the payments to PRC officials and might consider this practice to be an FCPA violation.").

152. This observation is based upon the author's own experience in dealing with the PSB while working in China as an in-house counsel for an MNC.

153. This observation is based upon the author's own experience working as an in-house counsel for an MNC in China when dealing with a state-owned technology consultancy service.

154. When working in China, the author found that once an MNC submits to a demand for payment, additional demands for payment often follow.

155. See *Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa* (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat'l People's Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 10 (China) (setting forth the legal liability of the infringer where the remedies available to the supervision and inspection department do not include compensatory damages and the ability to issue permanent injunctions).

so it will be difficult to obtain documentary evidence of the theft of the trade secret in the hands of the former employee.¹⁵⁶ This lack of documentary evidence may mean that the MNC will be unable to meet its high burden of proof in trade secret cases.¹⁵⁷ If the MNC files a criminal case with the PSB, the MNC may be faced with demands for an illicit case fee.¹⁵⁸ In either a civil case or a criminal case, the authorities may require a report from an approved state-owned research institute since the enforcement authorities themselves lack the technical expertise concerning the trade secret. When a state-owned research institute is used, the Chinese authorities who should pay the fee may pass on the payment to the MNC and the consulting organization may demand additional payments beyond authorized fees to issue a report. All of these actions leave the MNC embroiled in a web of illegal acts for which it may face civil and criminal liability under both Chinese and U.S. law.

These daunting problems can be traced, in part, to the high evidentiary burden in trade secrets cases. The plaintiff is required to satisfy three steps, all by the use of documentary evidence: (1) the plaintiff owned a trade secret; (2) the defendant has obtained, or is using, the identical or substantial similar trade secret; and (3) the defendant obtained the trade secret through illegal means.¹⁵⁹ Any document evidence of elements (2) and (3) are likely to be within the possession of the defendant, but Chinese civil law does not permit the use of discovery to obtain such evidence.¹⁶⁰ The courts will likely accept only documentary evidence and will not accept witness testimony to prove these elements.¹⁶¹ These evidentiary hurdles leave some MNCs with no choice but to seek the help of the PSB.¹⁶² State-

156. See CHOW, LEGAL SYSTEM OF CHINA, *supra* note 91, at 288 (discussing the minimal discovery procedures available to litigants in China).

157. See *supra* Part III.C (discussing the high evidentiary burdens and traps in the enforcement process).

158. See *id.*

159. See 2007 SPC Interpretation, *supra* note 90, art. 14 (stating the burden of proof set forth by the 2007 SPC Interpretation).

160. See CHOW, LEGAL SYSTEM OF CHINA, *supra* note 91, at 288 (“Pre-trial discovery in civil litigation in China is minimal as compared with the United States. . . . There is little, if any, exchange of evidence between the parties and PRC litigants do not have access to coercive measures such as interrogatories, depositions, and document requests . . .”).

161. See ORRICK, HERRINGTON & SUTCLIFFE LLP, *supra* note 28, at 865–66 (explaining where there is conflicting witness testimony in a case, both will be disregarded, and where an employer invites a current employee to testify against a former employee, the testimony is also disregarded because the current employee is deemed to have an interest related to his employer).

162. This observation is based upon the author’s own experience working in China with the PSB.

owned research institutes are also known to demand illegal payments.¹⁶³

While China has pledged to consider legislative reforms for trade secrets in 2014,¹⁶⁴ MNCs would be ill-advised to expect that these reforms will eliminate the major problems in enforcing trade secrets. While U.S. companies have made recommendations for legislative reform,¹⁶⁵ there is, of course, no guarantee that the Chinese government will accept these recommendations. In addition, one major reason why enforcing trade secrets is full of traps is government corruption, which is a pervasive problem that affects MNCs in all areas of doing business in China and can be traced to the fundamental political issue of the concentration of power in China's government and ruling Communist Party.¹⁶⁶ Although China has announced a serious crackdown on government corruption and bribery, many are skeptical that the Communist Party will enact any fundamental reforms that will erode its power.¹⁶⁷ The best strategy is to accept the existing legal framework and to develop a strategy to protect trade secrets in light of existent legal limitations. The next Part of this Article focuses on how MNCs can protect their trade secrets under the present legal framework.

IV. PREVENTATIVE MEASURES

The evidentiary burdens involved in proving a trade secrets case and the risks of involving the PSB and a state-owned technology appraisal consultancy organization make the effective use of preventative measures even more important in all trade secrets

163. This observation is based upon the author's own experience in China working with technology consulting organizations.

164. This announcement was made at the conclusion of the meeting of the high-level U.S.-China Joint Commission on Commerce and Trade. See U.S. DEP'T OF COMMERCE, *supra* note 11 ("The United States and China commit to cooperate in 2014 on proposals to amend the trade secret law and on related legislative and policy issues. China shall give serious consideration to U.S. legislative reform proposals.").

165. See U.S.-CHINA BUSINESS COUNCIL, *supra* note 2, at 2-3 (discussing recommendations for enforcing agreements through drafting a unified trade secret law and prioritizing revisions to the AUCL).

166. See generally Daniel C.K. Chow, *Why China's Crackdown on Commercial Bribery Threatens U.S. Multinational Companies Doing Business in China*, 31 ARIZ. J. INT'L & COMP. L. (forthcoming 2014).

167. See William Wan, *China's New Leaders Discuss Fight Against Corruption, but Some are Skeptical of Action*, WASH. POST (Dec. 28, 2012), available at http://www.washingtonpost.com/world/asia_pacific/chinas-new-leaders-focus-on-fighting-corruption/2012/12/27/9953e00a-4f77-11e2-950a-7863a013264b_story.html [<http://perma.cc/N7Q4GSQ>] (archived Sept. 2, 2014) (noting that real change requires creating new institutions that put "checks and balances" into the political system but that there has been little appetite for such move within the government).

cases.¹⁶⁸ Once the MNC finds that a trade secret has been stolen, the MNC will find meeting the evidentiary burdens in China to be time-consuming, frustrating, and potentially involving questionable cash payments. A preventative strategy should implement measures that anticipate these problems and avoid them, if possible. Since trade secrets cases in China commonly involve theft by existing or former employees, the MNC should plan its preventative strategies with a focus on employer-employee relations.

A. Licensing and Confidentiality Agreement

An MNC should sign a written licensing agreement with its FIE.¹⁶⁹ This agreement should set forth, in detail, the nature and scope of the trade secrets.¹⁷⁰ The purpose of the licensing agreement is to establish documentary evidence of the existence and ownership of the trade secret by the MNC, the first step in the burden of proof of any trade secrets case.¹⁷¹ The licensing agreement should be drafted to set out the scope of the trade secret in technical detail. Detail will help avoid any doubts about whether the stolen information falls within the protected knowledge if a dispute arises.¹⁷²

An MNC should then require that all existing employees with access to any confidential information sign a confidentiality agreement.¹⁷³ The agreement can be referenced in the labor contract, but a separate detailed confidentiality agreement should be signed in addition to the labor contract. Use of a written confidential

168. For a similar recommendation, see Bai & Da, *supra* note 12, at 365–71 (recommending confidentiality policies and confidentiality and non-competition agreements as preventative measures for the protection of trade secrets in China).

169. See *id.* at 368 (“Due to the high evidentiary burden in China, written agreements are vital in protecting trade secrets and confidential information.”).

170. See *id.* (“Whenever possible, confidentiality agreements should clearly identify the information that the employer deems as confidential.”).

171. See *supra* text accompanying note 169; see also Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat’l People’s Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 10 (China) (prohibiting business operators from infringing upon trade secrets in various ways); 2007 SPC Interpretation, *supra* note 90, art. 14 (setting forth the burden of proof in trade secrets cases).

172. See Bai & Da, *supra* note 12, at 365 (recommending that companies establish confidentiality policies “[c]learly spelling out the consequences of any unauthorized, improper use, or disclosure of confidential information.”).

173. See Zhong Hua Ren Min Gong He Guo Lao Dong He Tong Fa (中华人民共和国劳动合同法) [Labor Contract Law of the PRC] (promulgated by the Standing Comm. Nat’l People’s Cong., June 29, 2007, effective Jan. 1, 2008), art. 23 (China) (“[T]he Unit may agree with the laborer on the inclusion of non-competition provisions in the labor contract or a separate confidentiality agreement.”); Bai & Da, *supra* note 12, at 366 (recommending that a company “[r]equire all key personnel who have knowledge of trade secrets to sign confidentiality agreements”).

agreement is important even though an analysis of the laws governing trade secrets in Part III of this Article indicates that the obligation of confidentiality may exist for employees even without a confidentiality agreement. This would occur, for example, if the employer uses other measures specified by the 2007 SPC Interpretation, such as passwords or marking information as confidential.¹⁷⁴ The Company Law indicates that senior management employees have a fiduciary duty to keep trade secrets confidential.¹⁷⁵ A similar duty may be the basis for the obligation of a lower-level employee to keep information confidential when other confidentiality measures are used. However, under the Company Law, the senior management employee's duty to keep information confidential exists only when the employee continues to work for the employer;¹⁷⁶ once the employment is terminated, the duty of confidentiality ends since the fiduciary duty to the employer also ends.¹⁷⁷ The same should hold true for lower-level employees: the duty of confidentiality created by protective measures taken by the employer ends when employment ends. The only way to extend the confidentiality obligation after the termination of employment is through the use of a confidentiality agreement.¹⁷⁸ This is what distinguishes the confidentiality agreement from all of the other measures set forth in the 2007 SPC Interpretation. None of the other confidentiality measures set forth in the 2007 SPC Interpretation have any effect after termination of employment. Moreover, the confidentiality agreement does not require any compensation to be paid to the employee in order to be enforceable,¹⁷⁹ and the agreement can extend the confidentiality

174. See 2007 SPC Interpretation, *supra* note 90, art. 11 (listing different means an employer may use to protect company information, including tagging classified information or adopting passwords or codes on classified information).

175. See *Zhong Hua Ren Min Gong He Guo Gong Si Fa* (中华人民共和国公司法) [Company Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., Oct. 27, 2005, effective Jan. 1, 2006), arts. 148–49 (China) (discussing fiduciary obligations of a director and the various acts in which a director or senior manager is not allowed to participate).

176. See *id.* (providing restrictions on senior management employee conduct).

177. See *id.* (apparently restricting senior management employee conduct only throughout the duration of said employment).

178. See Bai & Da, *supra* note 12, at 368 (“Chinese law does not prescribe any fixed term during which an employee must keep the trade secret confidential, but a court may prolong the obligation until the general public is aware of the trade secret. Therefore, employers should consider specifying a reasonable time limit for maintaining confidentiality obligations post-termination in all IP agreements, consultant agreements, and service agreements that the companies may have with its employees, contractors, and subcontractors, etc.”).

179. See Labor Contract Law of the PRC, art. 23 (“If a laborer has an obligation to maintain the confidentiality of his Unit's trade secrets, the Unit may agree with the laborer on the inclusion of non-competition provisions . . . and stipulate that the Unit shall pay economic compensation . . . during the term of non-competition . . .”).

obligation indefinitely so long as the trade secret is not publically disclosed.¹⁸⁰

An MNC should be careful to ensure that its employee signs the labor contract and the confidentiality agreement with the FIE and not directly with the MNC. Under Chinese law, the MNC cannot directly employ a Chinese national within China; only a Chinese legal entity, like an FIE, can employ a Chinese national.¹⁸¹ If the employee signs a confidentiality agreement directly with the MNC, a Chinese court might find that, since the confidentiality agreement is derived from an employment relationship, the lack of a lawful employment relationship will void the confidentiality agreement. The lack of an ability to directly employ Chinese nationals in China is one reason why all MNCs that do business in China form FIEs, such as a joint venture or a WFOE. The confidentiality agreement should be carefully drafted so that it covers in detail the scope and nature of the trade secrets owned by the MNC and licensed to its Chinese business entity.

Not only should the MNC have the employee sign a confidentiality agreement with its FIE, but the employee should also be required to sign documents acknowledging receipt of business secrets on a regular basis during the course of his employment.¹⁸² The document acknowledging receipt of business information should be kept in permanent records by the FIE and can be offered as evidence that the employee has possession of the MNC's trade secrets. Note that with these two documents, the MNC might be able to satisfy the first two steps in the burden of proof in a trade secrets case:¹⁸³ the signed confidentiality agreement provides documentary evidence of the existence and ownership of a trade secret by the MNC,

180. See *Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa* (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat'l People's Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 10 (China) (providing prohibited means of infringing upon trade secrets and defining trade secrets as "any technology information or business operation information which is unknown to the public"); see also Bai & Da, *supra* note 12, at 368 (suggesting that along with specifying a time limit in a confidentiality agreement, "[a]nother option is to specify that the post-termination obligation continues so long as the trade secrets remain secret").

181. See *Zhong Hua Ren Min Gong He Guo Lao Dong Fa* (中华人民共和国劳动法) [Labor Law of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., July 5, 1994, effective Jan. 1, 1995), art. 2 (China) (stating that the PRC labor laws apply to "enterprises, individually-owned economic organizations, and labourers who form a labour relationship with them . . ."); Labor Contract Law of the PRC, art. 2 (stating that the PRC labor contract laws apply to "enterprises, individual economic entities and private non-enterprise organizations").

182. See Bai & Da, *supra* note 12, at 366 (stating that companies should "require all employees to sign a written acknowledgement prior to receiving any company information").

183. See 2007 SPC Interpretation, *supra* note 90, art. 14 (setting forth the burden of proof in a trade secrets case).

and the signed acknowledgement by the employee is documentary evidence that the employee has obtained possession of the MNC's trade secrets.

B. Non-Competition Agreements

The MNC should have the employee sign a non-competition agreement in addition to a confidentiality agreement.¹⁸⁴ The 2008 Labor Contract Law makes clear that a non-competition agreement is separate and distinct from a confidentiality agreement.¹⁸⁵ While the confidentiality agreement imposes a duty on the employee to prevent disclosure of trade secrets, the non-competition agreement prohibits the former employee from accepting employment from a competitor after the termination of employment.¹⁸⁶ One common rationale for preventing a former employee from working for a competitor is that the former employee will inevitably reveal trade secrets even if the former employee has signed a confidentiality agreement.¹⁸⁷

Under Article 23 of the Labor Contract Law, senior management, senior technical personnel, and other personnel under a confidentiality obligation can be asked to sign a non-competition agreement with the employer.¹⁸⁸ The employer must be careful to draft the non-competition clause so that it is not too broad. Article 24 of the Labor Contract Law requires that the scope, territory, and term of the non-competition clause be agreed upon by the employer and employee.¹⁸⁹ Non-competition clauses are inherently anticompetitive,¹⁹⁰ so a clause that prohibits the employee from

184. See Bai & Da, *supra* note 12, at 369 (recommending non-competition agreements as preventative measures for the protection of trade secrets in China and discussing such agreements in terms of Articles 23 and 24 of the Labor Contract Law).

185. See Labor Contract Law of the PRC, art. 23 ("If a laborer has an obligation to maintain the confidentiality of his Unit's trade secrets, the Unit may agree with the laborer on the inclusion of non-competition provisions in the labor contract or a separate confidentiality agreement . . .").

186. See *id.* (stating that the laborer may be prevented from "working for a competing Unit that either produces the same type of products or is engaged in the same type of business as his current Unit" for a period of up to two years).

187. This reasoning is the basis for the inevitable disclosure doctrine under U.S. law. Under this doctrine, an employer can enjoin a former employee from working for a competitor on the ground that the employee will inevitably disclose trade secrets obtained from his former place of employment. See, e.g., *PepsiCo, Inc. v. Redmond*, 54 F.3d 1262, 1268–69 (7th Cir. 1995) (applying Illinois trade secrets law). The doctrine is well accepted under U.S. law. See *Applicability of Inevitable Disclosure Doctrine Barring Employment of Competitor's Former Employee*, 36 A.L.R. 6th 537 (2008) (collecting cases).

188. See Labor Contract Law of the PRC, arts. 23–24.

189. See *id.* art. 24 ("The scope, territory and term of the non-competition provisions shall be agreed upon by the Unit and the laborer, and such agreement shall not violate laws and regulations.").

190. See Pagnattaro, *Protecting Know-How*, *supra* note 9, at 333 (quoting Beijing Hekang Scientific and Technical Development Company Ltd. and Li Zimin (2005),

working anywhere in China, for example, would probably be rejected as too broad.¹⁹¹ The non-competition agreement can prevent the former employee from working for an employer who manufactures products or engages in business that competes with the former employer, and can also prevent the former employee from forming his or her own business that competes with that of the former employer.¹⁹² The maximum term of the non-competition clause is two years.¹⁹³ The employer must pay compensation to the employee on a monthly basis in order for the non-competition clause to be enforceable.¹⁹⁴

Until 2013, the issue of the amount of required compensation under a non-competition agreement was a source of widespread confusion in China because different local jurisdictions had different requirements.¹⁹⁵ In 2013, the Supreme People's Court issued the "Interpretation on Certain Issues Concerning the Application of Law in the Trial of Labor Dispute Cases"¹⁹⁶ (2013 SPC Interpretation), which now sets uniform national guidelines. The 2013 SPC Interpretation states that, where the employer and employee have

Haidian District People's Court of Beijing, Hai Min Chu No. 5598 (China)) (arguing that a non-compete agreement "objectively restricts a 'person's right to work and freedom to participate in the market competition,'" so these agreements must be limited in scope and the company must demonstrate a justified business interest for the agreement).

191. *See id.* ("[N]on-compete agreements must be limited in their scope to a reasonable time period, limited to those with knowledge of trade secrets, and applied only to information that is legally a trade secret.").

192. *See id.* (further defining the contours of the scope of permissible non-compete agreements).

193. *See* Labor Contract Law of the PRC, art. 24 ("The term . . . shall not exceed two years."). Why limit the term of the non-competition agreement to two years? Non-competition agreements are inherently anticompetitive since they limit the freedom of employees to earn a living and thus should be supported by a strong rationale. *See* Pagnattaro, *Protecting Know-How*, *supra* note 9, at 333. Protection of trade secrets is an accepted justification. *See id.* But since all trade secrets lose commercial value with the passage of time, the thought is that after two years the harm to the employer caused by any disclosure of a trade secret is outweighed by the employee's right to be free from any restrictions on where he can work. *See id.*

194. *See* Labor Contract Law of the PRC, art. 23 ("[T]he Unit may agree with the laborer on the inclusion of non-competition provisions . . . and stipulate that the Unit shall pay economic compensation to the laborer on a monthly basis during the term of non-competition after the termination of the labor contract.").

195. *See* ORRICK, HERRINGTON & SUTCLIFFE LLP, *supra* note 28, at 862–64 (stating that "[t]he amount of non-compete compensation is largely governed by regional regulations" and detailing the "confusing" variation in mandatory minimum non-compete compensation amounts in different regions).

196. Interpretation of the Supreme People's Court of Several Issues on the Application of Law in the Trial of Labor Dispute Cases (promulgated by the Supreme People's Court, Dec. 31, 2012, effective Feb. 1, 2013) (China) [hereinafter 2013 SPC Interpretation], available at <http://www.chinaemployment.com.cn/shownews.asp?id=108> [<http://perma.cc/TA4VZN95>] (archived Sept. 2, 2014); *see also* Bai & Da, *supra* note 12, at 369 (discussing the 2013 SPC Interpretation and its implications on non-compete agreements).

agreed upon a non-competition clause but not on the amount of compensation, the employee shall be entitled to monthly compensation of 30 percent of his or her average salary for the twelve-month period prior to termination, so long as the employee has fulfilled the non-competition obligation.¹⁹⁷ If the employer has not paid compensation for three months after the termination of the employment, the employee is entitled to have the non-competition clause cancelled by a court.¹⁹⁸ If the employer pays compensation on a monthly basis, the employer is entitled to have a court issue an order that the employee must comply with the non-competition clause for the two-year period.¹⁹⁹

C. Use of Preventative Measures to Protect Trade Secrets

As the previous discussion indicates, MNCs face a high evidentiary problem in proving breach of trade secrets and, in addition, could become ensnared in a murky web of risky and dangerous problems when seeking to enforce rights once the theft of a trade secret has occurred. Given the risk involved in enforcing a trade secret after theft has occurred, the prevention of the theft or disclosure of a trade secret becomes a much more attractive option. This Part now details how the use of these preventative measures can avoid the enforcement pitfalls detailed in Part III.C of this Article.

If the employee has signed a confidentiality agreement with an MNC's Chinese business entity, the MNC may be able to prevent an existing employee from disclosing trade secrets through injunctive relief. In a significant development, a Shanghai court recently issued an injunction in favor of the plaintiffs, Eli Lilly and its China business entity Lilly (China) Research & Development Co., Ltd.

197. See 2013 SPC Interpretation, *supra* note 196, art. 6 (providing that “[w]here, in the labor contract or confidentiality agreement, the parties agree on non-competition but fail to agree on the payment of economic indemnity to the employee after the rescission or termination of the labor contract, if the employee performs the non-competition obligation and claims a monthly payment of economic indemnity from the employer as per 30% of the employee’s average monthly wage for the 12 months before the rescission or termination of his or her labor contract, the people’s court shall support such a claim.”).

198. See *id.* art. 8 (“Where the parties agree on non-competition and economic indemnity in the labor contract or confidentiality agreement, if the employee requests the removal of the non-competition clause on the ground of non-payment of economic indemnity for three months after the rescission or termination of the labor contract for reasons attributable to the employer, the people’s court shall support such a request.”).

199. See *id.* art. 10 (“Where the employer requests the employee’s continued performance of the non-competition obligation as agreed on after the employee pays a penalty for his or her breach of the non-competition clause to the employer, the people’s court shall support such a request.”).

(hereinafter both “Lilly”).²⁰⁰ The employee had signed a labor contract and a confidentiality agreement with the plaintiffs.²⁰¹ The employee downloaded twenty-one confidential documents from Lilly’s computer server without consent.²⁰² Lilly asked the employee to delete the documents and after the employee refused, Lilly terminated the employment.²⁰³ Lilly obtained a preliminary injunction prohibiting the employee from disclosing any of the data and requiring the employee to post a bond for RMB100,000 as security.²⁰⁴ The injunction was issued under the 2013 amended Article 100 of the Civil Procedure Law.²⁰⁵ Article 100 authorizes the court to issue an evidence preservation order prohibiting the party from destroying evidence and also authorizes the equivalent of a preliminary injunction.²⁰⁶ This case is the only known case in China in which a court issued a preliminary injunction preventing an ex-employee from disclosing trade secrets. Lilly was able to obtain this result because it was able to meet all of the elements in the burden of proof of a violation of trade secrets case.²⁰⁷ Lilly had a written confidentiality agreement, documentary evidence of ownership of a trade secret, documentary evidence of the defendant’s possession of the plaintiff’s trade secret (the downloaded files), and documentary evidence in the form of computer records that the defendant had obtained the trade secrets illegally. Although it is possible that Lilly might have been able to obtain relief without such strong documentary evidence, the existence of such a documentary record surely facilitated the ability of Lilly to obtain the first known preliminary injunction preventing disclosure of a trade secret in China.

Having a strong documentary record will also assist an MNC in dealing with ex-employees, an even more troublesome problem since the ex-employee may have been lured to work for a competitor. If the

200. See Zhan, *supra* note 7 (reporting that “[t]he first preliminary injunction issued for a trade secret case in Shanghai is based on the amended Civil Procedure Law”).

201. See *id.* (“Lilly and the Employee entered into a labor contract and a confidentiality agreement on 3 May 2011.”).

202. See *id.* (“The Employee . . . downloaded confidential documents from the server of Lilly without the consent of the plaintiffs on 19 January 2013.”).

203. See *id.* (“Lilly terminated the employment contract with the Employee on 27 January 2013 after failure to request the Employee to delete the confidential documents.”).

204. See *id.* (“[T]he plaintiffs applied with the court to issue the injunction to prevent the Employee from copying, disclosing, using or licensing any third party to use the twenty-one documents which included trade secrets of the plaintiffs, and provided the security in the amount of RMB100,000 to the court for the application of the injunction.”).

205. See Civil Procedure Law of the PRC, *supra* note 114, art. 100.

206. See *id.*

207. See 2007 SPC Interpretation, *supra* note 90, art. 14 (defining burden of proof for trade secrets claims); see also *supra* Part III.C (discussing high evidentiary burden and traps in the enforcement process).

MNC has the employee sign a confidentiality agreement and a non-competition clause, then the MNC and its Chinese FIE should conduct an exit interview in order to obtain information about the employee's new place of employment.²⁰⁸ If the employee is evasive or otherwise gives the MNC reason to doubt his intentions, the 2013 SPC Interpretation allows the employer to obtain a court order that enforces the non-competition agreement.²⁰⁹ If the MNC has reason to know that a departing employee intends to work for a competitor, the MNC might wish to engage a private investigation company in order to discover the identity of the employer, since the employee might not be forthcoming with this information.²¹⁰ The MNC must be careful to draft the non-competition agreement in accordance with the requirements of the Labor Contract Law,²¹¹ and, in particular, the FIE must pay the monthly compensation as required by law—otherwise the non-competition agreement becomes unenforceable.²¹² If the MNC has met all of these requirements, the MNC might be able to obtain a preliminary injunction enjoining the employee from working for a competitor.

Note carefully that the MNC is not trying to enforce a trade secret directly when dealing with a former employee who intends to work for a competitor. The MNC is seeking to enforce the non-competition agreement. This is a crucial distinction. The requirements for enforcing such an agreement are (1) a non-competition agreement that satisfies the permitted scope of such

208. See Bai & Da, *supra* note 12, at 366 (describing how exit interviews are a way of ensuring that employees are not taking any company information to their new jobs and reminding them that their obligation not disclose trade secrets extends beyond their employment with the company).

209. See 2013 SPC Interpretation, *supra* note 196, art. 10 (“Where the employer requests the employee’s continued performance of the non-competition obligation as agreed on after the employee pays a penalty for his or her breach of non-competition clause to the employer, the people’s court shall support such a request.”).

210. Private investigation companies are commonly used in China and are tolerated by PRC enforcement authorities. Private investigation companies are technically not permitted since they engage in investigatory work that is similar to police work, but, due to a shortage of resources, PRC authorities tolerate private investigation companies, which are able to obtain business licenses as media companies or market research companies. See Chow, *Anti-Counterfeiting*, *supra* note 32, at 764 (discussing the Chinese private investigation industry, including its dramatic growth and ongoing issues).

211. See Zhong Hua Ren Min Gong He Guo Lao Dong He Tong Fa (中华人民共和国劳动合同法) [Labor Contract Law of the PRC] (promulgated by the Standing Comm. Nat’l People’s Cong., June 29, 2007, effective Jan. 1, 2008), arts. 23–24 (China) (defining the scope and availability of non-competition agreements).

212. See *id.* art. 23 (“[T]he Unit shall pay economic compensation to the laborer on a monthly basis during the term of non-competition after the termination of the labor contract.”); see also 2013 SPC Interpretation, *supra* note 196, arts. 6, 10 (mandating compensation for the performance of non-competition agreements by employees).

agreements under the Labor Contract Law,²¹³ (2) a confidentiality agreement,²¹⁴ and (3) payment of compensation for the non-competition obligation.²¹⁵ In enforcing a non-competition agreement, the plaintiff is not required to prove the existence of a trade secret or its theft by the employee. Compared with the evidentiary burden for proving the breach of a trade secret, this evidentiary burden is far lower and easier to satisfy. Moreover, enforcing a non-competition agreement does not get the MNC entangled with the PSB or with a state-owned research institute. If the MNC has planned carefully, the MNC should have documentary evidence, of the three requirements set forth above,²¹⁶ for the enforcement of a non-competition agreement in its records.

V. CONCLUSION

The law of trade secrets is still evolving in China, but it remains fragmented and is behind in its development compared to laws relating to other forms of intellectual property. The primary law applicable to trade secrets, the Anti-Unfair Competition Law, was enacted over two decades ago, and there is no sign that a unified law will be enacted in the place of all of the scattered provisions that currently exist.

A comparison with trademarks illustrates the significantly higher evidentiary burden that is required for the enforcement of trade secrets. The plaintiff is required to show documentary evidence of three elements: (1) the plaintiff owned a trade secret, (2) the defendant has in its possession identical or substantially similar information to the plaintiff's trade secret, and (3) the defendant illegally obtained the trade secret. This type of evidence is often unavailable or is in the possession of the defendant. The plaintiff is not aided in overcoming these evidentiary burdens in Chinese courts by any presumptions or the shifting of the burden of proof.

213. See Labor Contract Law of the PRC, art. 24 ("The personnel subject to non-competition provisions shall be limited to the Unit's senior management, senior technicians and other personnel who have knowledge of trade secrets of the Unit. The scope, territory and term of the non-competition provisions shall be agreed upon by the Unit and the laborer, and such agreement shall not violate laws and regulations.")

214. See *id.* art. 17 (providing for confidentiality agreements in employment contracts).

215. See *id.* art. 23 (providing for economic compensation for employees acting in accordance with non-competition agreements); see also 2013 SPC Interpretation, *supra* note 196, arts. 6, 10 (same).

216. See Zhong Hua Ren Min Gong He Guo Fan Bu Zheng Dang Jing Zheng Fa (中华人民共和国反不正当竞争法) [Anti-Unfair Competition Law of the PRC] (promulgated by the Standing Comm. of the Nat'l People's Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 10 (China); see also *supra* text accompanying note 86.

In order to obtain such documentary evidence that is in the possession of the defendant, the MNC might find it necessary to file a criminal case with the PSB because the PSB has wide investigatory powers and can compel the defendant to produce evidence. Such a mechanism does not exist in civil cases in China because China lacks a discovery system. The PSB might then engage the services of a state-owned technology consultancy organization to submit an expert's report on the existence of the trade secret and its theft. As many MNCs have discovered, dealing with the PSB and a state-owned research institute could result in an entanglement that could lead the MNC to make repeated cash payments, acts that could be illegal under both PRC²¹⁷ and U.S. law.²¹⁸

To avoid the high evidentiary burdens and the risky entanglements with PRC authorities, the MNC should invest significant resources in implementing preventative measures. The focus of these measures should be in developing a solid documentary record that would allow the MNC to enforce confidentiality obligations against existing employees and non-competition agreements against former employees. The evidentiary burdens involved with these preventative measures are far lower than those involved in enforcing trade secrets and do not require the MNC to become ensnared into dealing with Chinese authorities. As the discussion in this Article indicates, once the theft of the trade secret has occurred, the MNC is left with few effective options under the current legal system.²¹⁹ While China's recent self-proclaimed emphasis on improving its legal system relating to trade secrets is a promising development,²²⁰ MNCs would be ill-advised to rely on this pronouncement as a solution. The flaws with the current system are too complex and some of the problems (e.g., government corruption) are too fundamental to admit an easy solution. MNCs should develop a detailed and sophisticated program of preventative measures and a detailed documentary record. Documented preventative measures protecting trade secrets should be a high priority for all MNCs doing business in China in an age where proprietary know-how, knowledge, and information are more important than ever in doing business in the modern global economy.

217. See *supra* text accompanying note 144.

218. See Chow, *China Under the Foreign Corrupt Practices Act*, *supra* note 145 (recommending compliance with the FCPA to mitigate risks that might await MNCs doing business in China).

219. See *supra* Part III.C.

220. See U.S. DEP'T OF COMMERCE, *supra* note 11 ("China will accelerate its negotiation on accession to the WTO Agreement on Government Procurement (GPA) and submit a revised offer in 2014 that is on the whole commensurate with the coverage of GPA parties.").