Get your evidence right

Yang Li and **Richeza Herrmann** explain how a series of civil cases over trade secrets show the importance of obtaining the right evidence

The infringement of IP is not unique to China, but comes up frequently in discussions about Chinese business. Trade secrets are a particularly sensitive right. In contrast to other kinds of IP, which relate more closely to statutory law, trade secrets are more a creature of jurisprudence. An in-depth knowledge of past court decisions is crucial for the accurate assessment of new cases concerning on this issue. A series of cases examined by Chinese courts in the last 10 years shows what strategies need to be adopted.

One-minute read

Any company investing in China needs to have a strategy to protect its trade secrets. Employee turnover is high and when these workers leave they can take a lot of know-how with them. Trade secret protection is also important in the context of joint ventures between foreign and Chinese companies. Both Japan's Kawasaki Heavy Industries and Germany's Siemens have complained in the last year of theft of their trade secrets in joint ventures with Chinese companies to build high-speed rail systems in China. But enforcing trade secrets in China's courts is not easy. A series of cases decided in various Chinese courts shows that carefully drafted employee agreements and painstakingly assembled evidence are the key ingredients for success.

Definitions

China's framework for protection of trade secrets consists of different laws and regulations such as the Unfair Competition Law, the Contract Law, the Labour Law and the Criminal Law. Of these, the most relevant is the Unfair Competition Law, which was promulgated in 1993. Article 10 of the Unfair Competition Law stipulates three preconditions for trade secrets. First, trade secrets are technical information and business information that are unknown to the public. Second, they must create business interest or profits for their legal owner. And third, secrecy must be maintained by their legal owner. Theft of a trade secret requires that the infringer uses methods of stealing, coercing or other unfair methods to circumvent the owner's business secrecy, and that the infringer must disclose, use or permit others to use the business secrets.

The necessity of protection measures

The owner must take reasonable measures to ensure that the third party is aware of the secrecy. To give an example: In the case *Funing Factory vs Nanxin Co Ltd*, Funing sold a patented dust removal plant to Nanxin. Because the dust removal plant did not reach the agreed standard written in the contract, Nanxin refused payment. Then, both factories came to an agreement that Funing would dismantle the equipment itself. When Funing sent workers to dismantle the plant they found out the equipment was already dismantled and destroyed. Funing therefore claimed Nanxin has stolen the trade secret of the dust removal plant by removing the equipment.

At first instance, the Provincial Superior Court of Zhejiang Province determined that the asserted trade secret of the plant could not be proved. There was also no confidentiality agreement between the two parties, which meant that the claim of trade secret infringement was not supported. The appeal to the Supreme Court was dismissed. This means a patented product may include trade secrets, but a trade secret must also be protected through reasonable measures.

Technological trade secrets

Trade secrets incorporate two types of protection: technological and operational. Regarding technology, the plaintiff must prove that the alleged infringing technology is exactly the same as the protected technology. The claim must be supported by a complete chain of evidence.

Using the same technology

To give an example for these conditions: several former employees of Hua Li, a manufacturer of glass insulation tapes, joined a new factory named Gao Jie, which also produced glass insulation tapes. The ex-staff had confidentiality agreements with Hua Li. Hua Li claimed that Gao Jie used the same technology to produce glass insulation tapes, which the company claimed to be its trade secret. Hua Li proved that the ex-staff did know about the secret technology and that they had signed confi-

dentiality agreements and filed a lawsuit against Gao Jie for trade secret infringement. The defendant was able to provide evidence that its technology had been transferred to its company by a third party, Cuixiang Chen.

The Beijing Second Intermediate Court as court of first instance determined that the technology of the plaintiff was a trade secret. The ex-staff had access to the secret technology. But, the technology used by the two parties could not be proved as the same technology, as the moulds used in the production had different parts. Gao Jie could also provide the transfer contract with the third party Cuixiang Chen. Whether Cuixiang Chen got the technology legally was not the question of this case. So the claim was not upheld. An appeal to the Beijing High Court was dismissed.

To prove that operating information incorporates trade secrets is usually much more difficult than technological information

Improving imported technology

The improvement of foreign technology is also often relevant. Any improvement of imported advanced technology can create trade secrets as long as investment in the improvement took place, the secrecy of the improvement is maintained and the improvement has economic benefit for its holder.

For example, since 1988 the Chinese Academy of Agricultural Mechanisation Sciences (CAAMS) has invested in a programme for developing new technologies for puffed fodder machines. In March 1996, Fenyan Jiang was one of the major research fellows of the puffed fodder machine programme. The puffed fodder machine at issue was certified as an improved machine on the basis of overseas advanced technology. The changes that were made to the machine led to an extension of the operating life of the machine and reduced the costs. In December 1996, Linqing Jia began his work in CAAMS. Both employees left the Academy shortly afterwards. In May 1997 Fenyan Jiang and Linqing Jia established a new company named Daze to produce a puffed fodder machine together with other investors. They produced their machine with the same technology as CAAMS. Until January 1999 Daze sold 13 machines. Therefore CAAMS filed a suit against Fenyan Jiang, Linqing Jia and Daze for trade secret infringement.

The defendants asserted the technology of the puffed fodder machine was publicly known. Fenyan Jiang asserted he had no knowledge of the infringement and CAAMS did not make reasonable efforts to maintain its secrecy.

The Beijing Second Intermediate Court pointed out that the technology of the puffed fodder machine at issue can be confirmed as a trade secret. Daze has used the same technology in its new product. The defendants were not able to prove that the used design was developed by them. The court determined that the defendant infringed the trade secret of the plaintiff and that Fenyan Jiang was responsible for the infringement. The defendants were sentenced to stop the infringement of trade secrets, to apologise in written form and to pay compensation to CAAMS. The appeal to the Beijing High Court was dismissed.

Operational trade secrets

To prove that operating information incorporates trade secrets is usually much more difficult than proving technological information as a trade secret. Problems of evidence often occur. In one case, Ying Guang Hua produced special galvanised tubes for electrical wiring (JDG). The company asserted that JDG was invented by its legal representatives Rencai Liu. Ying Guang Hua had employed Xian Liu as sales manager until December 2002 and stipulated rules to protect asserted trade secrets and operating information. Xian Liu left the company in February 2002 and was employed by Zhong Hao Hua, which produced the same products and sold them to the same clients. Ying Guang Hua filed a law suit against Zhong Hao Hua for trade secret infringement.

The Beijing Second Intermediate Court pronounced that the asserted trade secret of the products is common knowledge. The asserted trade secret of operation was also qualified as well-known information to other competitors: the plaintiff was not able to provide sufficient evidence of the special relationship between the plaintiff and its clients. There was also no evidence that divulged the information of operation. The appeal to the Beijing High Court was dismissed.

This means that a list of clients may be a trade secret. However, the information must not be known to competitors and must also confer some economic benefit to its holder. The rights owner must make a reasonable effort to maintain the secrecy of a list of clients.

The burden of proof

Problems of evidence are the critical point of many trade secret cases. In a civil law procedure about theft of trade secrets, the plaintiff must provide evidence for the claim that a trade secret is given.

In an example of the evidential problems that can occur, Yizhi produced centrifugal pumps and owned special technology covering production and design. It provided blueprints and moulds to different foundries in order to place orders with them. Shuang Jun Foundry was one of those foundries. Yizhi signed a confidentiality agreement with its employees and the foundries to protect its design of moulds. In July 2004 the company noticed that Shuang Jun Foundry gave back two sets of moulds. Yizhi claimed that it provided only one set of moulds of each sort to Shuang Jun Foundry and assumed Shuang Jun Foundry had copied its moulds without permission. The accused company asserted the mould was not a trade secret and that it got two sets of moulds from Yizhi. Yizhi then filed a law suit against Shuang Jun Foundry for trade secret infringement.

The Intermediate Court of Wuxi/Zhejiang Province confirmed that the moulds of the Yizhi were trade secrets. The technical evaluation of the moulds proved that Yizhi's moulds are not generally known to the public and that they could be confirmed as a trade secret. But the claim for trade secret infringement was not supported because Yizhi was not able to provide evidence that Shuang Jun Foundry copied the moulds. The court indicated that Yizhi was not able to provide evidence that it has given Shuang Jun Foundry only one set of moulds. The appeal to the High Court of Zhejiang Province was dismissed.

The theft of trade secrets must be supported by evidence. In practice, it is often difficult for the plaintiff to prove the illegitimate means used by the defendant. For this reason there is a principle of reverse burden of proof, which means the bur-

den of proof is reversed if two conditions are met: the trade secret is identical to the alleged business or technological information; and the defendant was able to copy the trade secret. Then it is the task of the defendant to prove the legal source of the alleged business or technological information.

Non-compete clauses

In addition to confidentiality agreements, non-compete clauses are a common way to ensure protection of trade secrets. The intention of a non-compete clause is to prevent methods of unfair competition after a former employee has left the employer's company. But if a non-compete clause is signed in a work contract, it is crucial to pay attention to the precise wording of the clause. Otherwise you risk the validity of the clause. For example, a non-compete clause is only enforceable if the employer offers the employee adequate compensation.

The rights owner must make a reasonable effort to maintain the secrecy of a list of clients

For example, several employees left the Beijing Software Institute (BSI) and sold software that had the same function as BSI's software to the same customers. BSI claimed to own the trade secret of the software in question and of the information about customers. The Institute filed against the ex-staff for infringement of trade secrets.

The Beijing First Intermediate Court pointed out that BSI was not able to provide evidence that could prove the protection of it trade secret and that it could not provide the list of clients. So the claim that BSI owned these trade secrets could not be supported. The Beijing High Court as appellate court pointed out that although one of the ex-employees had a non-compete clause with BSI, BSI did not offer adequate compensation; so the employee was not obliged to observe the agreement. The appeal was dismissed.

Criminal law

Chinese law also recognises the criminal relevance of theft of trade secrets. Article 219 of the Criminal Law of China stipulates criminal detention of up to seven years and/or fines in cases of proven theft of commercial secrets with intent, such as technical information and operation information, which caused "significant losses" or "particularly serious consequences".

Relevant criminal scenarios include not only the acquisition of commercial secrets through theft, lure by promise of gain, threat, or other improper means, but also the disclosure, usage or the allowance of others to use commercial secrets in violation of an agreement with the rightful owner or the owner's request of keeping commercial secrets.

Building a strategy

A variety of preparations are necessary for a successful defence strategy concerning theft of trade secrets in China. Every competitor should be aware of the dangers of theft of trade secrets in China. The great barrier for lawsuits about trade secrets is the problem of evidence. The plaintiff must demonstrate that he protected the trade secret through reasonable measures. This means, before any lawsuit, evidence must be carefully collected at every stage. In addition, means of competitive intelligence can be used to collect evidence. Investigative research methods as recorded notarised negotiations are often suitable to collect further evidence to prove an action of theft of trade secrets. Furthermore, the contractual possibilities should be fully taken into account. Confidentiality agreements and non-compete clauses in work contracts not only show the sensitivity of know-how accumulated in a company, but also deliver a juridical criterion in a potential lawsuit. Last but not least, the choice of lawyer is fundamental. Because local protectionism is still an important keyword in China, the lawyer should have broad experience in legal procedures in the Chinese core regions and should be familiar with the local authorities.

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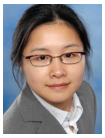
Yang Li


Richeza Herrmann