

# LICENSING IN CHINA: THE GOOD, THE BAD AND THE UGLY

技术合同在中国：  
善的， 恶的， 丑的

Paul Jones

Jones & Co. 钟保禄律师事务所 Джоунс и Ко.

Licensing Executives Society

April 27, 2006

# Introduction:

## Why China?

- World Bank ranks the Chinese economy as second only to the U.S. on the basis of purchasing power parity
- China has maintained an inflation adjusted average annual growth rate of 8% for the past 25 years
- GDP Growth for the first Quarter of 2006 – 10.2%

# Introduction:

## Problems:

- Weakly developed rule of law- 依法治国
- “Our [China’s] technology is a re-innovation on the basis of assimilating advanced foreign technologies of foreign countries” *Economist*, March 25, 2006  
p.69
- Role of Government

# Legal Structure

- Do more than a technical legal analysis; include political and sociological analysis
- Example –analysis of 1999 依法治国 ( yi fa zhi guo) amendment
- Constitution – not justiciable

# Legal Structure

- China is considered a unitary state
- Reality is that the 31 provinces have considerable power
- Constitution has no division of powers
- March 15 2000 – 立法法 (LiFaFa)  
Legislation Law – reserved some powers
- Luoyang Seed Case – 河南省洛阳市中级人民法院 June 2003 – first ruling where national law overruled provincial law

# Legal Structure

- China is a civil law jurisdiction
- But civil code is mostly in draft form
- Slow process – drafting relies heavily on consensus
- Draft Property Rights Law (物权法) not presented to the National People's Congress as expected in March
- IP and technology contract decisions now available online in Chinese at: <http://ipr.chinacourt.org>

# Contract Law

- 合同法 (He Tong Fa) – in force October 1, 1999
- Contains both general and specific provisions
- Art. 6 - 当事人行使权利、履行义务应当遵循诚实信用原则 – The parties shall observe the principle of good faith in exercising their rights and fulfilling their obligations.

# Contract Law

- Art. 42 In the making of a contract, the party that falls under any of the following circumstances, causing loss to the other party, shall hold the liability for the loss.
  - (1) engaging in consultation with malicious intention in name of making a contract;
  - (2) concealing intentionally key facts related to the making of the contract or providing false information;
  - (3) taking any other contrary to the principle of good faith



# Contract Law

- Art. 60 – the parties shall observe the principle and fulfill the obligations of notification, assistance and confidentiality in accordance with the nature and aims of the contract and trade practices.
- Art. 126 – parties to a foreign-related contract can choose laws

# Contract Law

## Arts. 322 - 364 技术合同 (Technology Contracts)

- Common Provisions
  - Technological Development Contracts
  - Technological Transfer Contracts
  - Technical Consultation Contracts and Technical Service Contracts
- 
- Art. 329 Any technology contract that illegally monopolizes technologies, impedes technological progress or infringes upon technological results of others is null and void

# Contract Law

- 2002 Technology Contract Regulations
  - Administration of Technology Import and Export
  - Administrative Measures on Prohibited and Restricted Technology Exports
  - Administrative Measures on Prohibited and Restricted Technology Imports
  - Catalogue of Technologies Prohibited and Restricted for Import
  - Circular (MOFTEC & SAFE) Administration of Foreign Exchange Sale and Payment Related to Technology Import Contracts – Feb 20, 2002

# Contract Law

- Supreme People's Court (最高人民法院)  
Interpretations and Minutes
  - Interpretation of the Supreme People's Court concerning some issues on the Application of Law for the Trial of Cases on Disputes over Technology Contracts – Dec. 16, 2004
  - Second National Foreign-related Commercial and Maritime Trial Work Meeting Minutes – Dec. 26, 2005 – on conflict of laws and when Chinese courts should take jurisdiction (not yet available in English)

# Competition Law

- Draft Anti-Monopoly Law (反垄斷法) still under discussion
- Concerns regarding intellectual property abuse expressed in regulations and Supreme People's Court Interpretation of 2004

# Competition Law

- Examples in SPC Interpretation:
  - Restricting one party from doing new research
  - Restricting one party from obtaining competitive technology
  - Unreasonable restrictions on exploitation
  - Unreasonably restricting sources for materials
  - Prohibiting challenges to the effectiveness of the subject technology

# Licensing Strategies

- Early Choices:
  - Select what will be made in China carefully – perhaps withhold the most innovative or high-margin products, or separate functions so that no one manufacturer makes the whole product
  - Make sure that your project is economically feasible
  - Be careful not to base your business plan on WTO-noncompliant rules

# Licensing Strategies

- **Early Choices** cont'd:
  - Know the authority of the government that you are dealing with (understand the true division of powers)
  - Know your limit on losses from the project in advance, do a thorough risk analysis
  - Know in advance what you will do if the contract is breached (plan for trouble)
  - If you plan to take legal action, in what country are the relevant assets or people located



# Licensing Strategies

- Due Diligence:
  - Insist upon the right to make background checks on key people and the company
  - Conduct checks on the reputation of the local area.
  - Hire outside investigators, and use them
  - Carefully evaluate any property contributions by your Chinese partner, disputes over property valuation have plagued joint ventures as well as the proposed Property Law
  - Some prefer partners with foreign trained key personnel

# Licensing Strategies

- Register your Intellectual Property:
  - Trade-marks – China is a first to file jurisdiction, Chinese character versions of all relevant trade-marks should be professionally developed and registered
  - Patents – three forms- Invention, Design and Utility Models
  - Copyright – Registration is needed for enforcement, but requires disclosure. Disclosure may be limited if registration exceeds 60 pages

# Licensing Strategies

- Prepare A Strong Contract:
  - Specify exact terms of payment and performance
  - Ensure that the terms conform to the law, do not rely on your Chinese partner
  - Make provision for inspections and audits, possibly including for the components or inputs, and use them
  - Carefully describe the scope of the grant

# Licensing Strategies

- Prepare A Strong Contract cont'd:
  - Ensure that that each page is signed and that the contract is properly signed and sealed. Are two signatures required?
  - Specify a choice of law that matches your exit strategy
  - If you are based outside of China, definitely use arbitration, China is a party to the New York convention on arbitral awards
  - Be careful in choice of arbitrator and arbitration rules, CIETAC has had serious problems recently
  - Consider negotiating for the right of discovery

# Licensing Strategies

- Prepare A Strong Contract cont'd:
  - Specify a choice of venue, the Chinese party is unlikely to agree to come to North America, in part because of cost considerations, consider Singapore law and venue, or Hong Kong SAR
  - If possible chose a Chinese venue in which you have other investments
  - Use non-competition covenants for the partner and for key personnel, and provide for specific and adequate compensation for the covenants (if there is appropriate compensation these provisions are enforced in China, even against employees)
  - Obtain government approvals as required

# Licensing Strategies

- Monitor Security Implementation:
  - Use surveillance equipment or firewalls
  - Negotiate to have a representative on site?
  - Ensure that proper security protocols are in place for trade secrets
  - Conduct regular training on security measures

# LICENSING IN CHINA: THE GOOD, THE BAD AND THE UGLY

## 技术合同在中国： 善的， 恶的， 丑的

Paul Jones

Jones & Co. 钟保禄律师事务所 Джоунс и Ко.

Licensing Executives Society

April 27, 2006

[pjones@jonesco-law.ca](mailto:pjones@jonesco-law.ca)

416-703-5716