

China Trade Secret Ruling Shows U.S. Cos. Path To Protection

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In February, China's Supreme People's Court upheld a ¥159 million, or roughly \$25 million, trade secret infringement award in *Jiaying Zhonghua Chemical Co. Ltd. and Shanghai Xinchun New Technology Co. Ltd. v. Wanglang Group Co. Ltd.*

The judgment amount is on par with recent verdicts in the U.S. under the Defend Trade Secrets Act and Section 337 actions before the U.S. International Trade Commission, and it represents China's increased interest in protecting trade secrets.

Historically, companies were hesitant to seek to enforce their trade secrets in a Chinese court and often chose other forums. For example, companies are increasingly filing Section 337 actions before the ITC or U.S. federal court actions under the DTSA.

ITC proceedings have a number of benefits, including potentially blocking the import of infringing products into the U.S. and providing protective orders to limit disclosure. The rulings may have preclusive effect in other matters, which can be effective when a company elects to simultaneously file a claim before the ITC and initiate federal court litigation under the DTSA, because ITC procedures move at a faster pace.

In addition, utilizing these options requires jurisdiction in the U.S., and companies continue to push the boundaries of this jurisdiction, in hopes of litigating their cases in a forum that is historically more advantageous to a plaintiff's trade secret claims.

However, a major concern for companies litigating in the U.S. against Chinese defendants must be the enforcement of foreign judgments in China. If the defendant is utilizing the trade secrets in China, injunctive relief issued by a U.S. court would not be enforceable in China, and enforcement of foreign judgments in China is rare and time-consuming.

Thus, if the defendants' businesses are located in China and their use of infringing trade secrets occurs within China, it would be difficult for companies to ultimately obtain the benefit of their U.S. litigation time and cost. In this situation, companies should consider initiating actions in China.

China has developed an increasing interest in the protection of trade secrets as illustrated by legal developments and the judgment in Jiaxing. In 2019, China modified its Anti-Unfair Competition Law to add increased protection of trade secrets. In 2014, China instituted specialized intellectual property courts and divisions with particular expertise in IP cases.

Furthermore, Chinese procedural law has a number of preservation measures that operate in the same manner as injunctive relief in common law jurisdictions but are standard practice and relatively simple to obtain against a defendant. Thus, with the increased emphasis on protection of trade secrets, companies should consider utilizing Chinese courts when the defendant and its assets are inside of China.

The Jiaxing case provides an excellent illustration of the efficacy of bringing trade secret cases against Chinese defendants in China. The case arose when the plaintiffs, Jiaxing Zhonghua Chemical Co. and Shanghai Xinchun New Technology Co., developed and used a method for vanillin production.

Although the plaintiffs had instituted protections for their trade secrets, an employee of both plaintiffs in charge of equipment maintenance provided trade secret information to the defendants and then joined the defendants as an employee. The defendants then utilized the stolen trade secret to manufacture and sell vanillin.

The Jiaxing case moved quickly, taking less than three years to make it from the court of first instance to judgment in the Supreme People's Court. In May 2018, the plaintiffs sued the defendants in the Zhejiang Higher People's Court, and the court ultimately issued a judgment in favor of the plaintiffs.

This judgment was appealed to the specialized IP division of the Supreme People's Court, which affirmed the ruling and increased the damages the defendants jointly and severally owed the plaintiffs.

Because this case was filed in 2018, the court did not apply the current Anti-Unfair Competition Law that became effective in 2019, which made several changes that would have been favorable to the plaintiffs, including:

- Adding protection for previously unprotected confidential business information;
- Including violations for aiding trade secret infringement;
- Increasing the punitive damages for malicious violations by setting the possible multiplier to five times the damages; and
- Increasing the possible compensation amount to ¥5 million (\$767,650).

Even without the additional protections of the 2019 amendments to the Anti-Unfair Competition Law, the judgment in Jiaxing demonstrates a growing trend in China of plaintiffs' ability to bring trade secret cases successfully.

As noted above, the defendants appealed the original ruling through the IP division of the Supreme People's Court—specialized courts that were created in 2014. There are now three specialized IP courts—in Shanghai, Beijing and Guangzhou—approximately 20 specialized IP divisions, and the newly established Supreme People's Court IP division that has national jurisdiction over appeals.

The usage of these IP courts has increased by over 100% from 2019 to 2020, with that trend expected to continue. Recently, the average time to complete an appeal through the IP courts has been less than six months, as was true in this case.

It cannot be determined from the judgment whether preservation measures were applied for and granted in the case. However, based on our experience litigating complex cases in China, it would be expected that some of the defendants' bank accounts, assets and equipment would have been frozen throughout the pendency of the case.

Under the Civil Procedure Law of China, there are two types of preservation: asset preservation and evidence preservation. In practice, asset preservation measures are adopted in nearly every case, and the procedure is direct.

Typically, a party would submit an application to the court at the same time it submits its case, though prelitigation preservation is possible in urgent circumstances.

The preservation application is forwarded to an enforcement judge who would conduct the relevant preservation measures. The timing of the preservation depends on the details in the application and the ability of the law firm to coordinate with the enforcement judge.

China's increased interest in protecting trade secrets, the speed of its IP docket, as well as its clear jurisdiction over China-based parties, should make China courts a consideration and part of the strategy for foreign companies to protect their trade secrets, including in conjunction with litigation in other jurisdictions.

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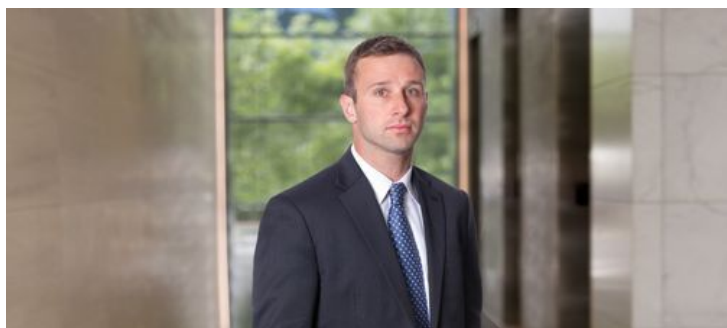
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