

May 2008
Volume 4, Issue 2

China Committee
Leadership

Co-Chairs

Elizabeth Cole
ecole@orrick.com

Michael E. Burke
mburke@williamsmullen.com

Vice Chairs

Qiang Bjornbak
qbjornba@gmail.com

Adam F. Bobrow
Afb3@georgetown.edu

Beth Farmer
bfarmer@psu.edu

James F. Grandolfo
James.Grandolfo@
hongkong.allenoverly.com

Jeffrey Paul Layman
jlayman@fullbright.com

Adam Li
liqi@junhe.com

Susan Ning
Susan.ning@kingandwood.com

Adria E. Warren
AWarren@foley.com

Jun Wei
jwei@hhlaw.com

Newsletter Editors
Qiang Bjornbak
qbjornba@yahoo.com

Paul B. Edelberg
pedelberg@murthalaw.com

Cameron J. Smith
cjsmith82@gmail.com

Russell K.L. Leu
leu@taftlaw.com

CHINA LAW REPORTER

中国法律报道

*REPORTING ON DEVELOPMENTS IN THE FOUR LEGAL SYSTEMS OF
GREATER CHINA*

Message from the Co-Chairs of the China Committee

Welcome to the May edition of the China Law Reporter! It has been a very busy few months for the China Committee. At the 2008 Spring Meeting, we hosted “Hot Topics in Doing Business in China: What You Need to Know Now,” a program that featured Co-Chair Elizabeth Cole and former Committee Co-Chair Amy Sommers as speakers and discussed recent developments in China’s employment contract law and real estate markets. That program was a joint effort between the Committee and the Inter-Pacific Bar Association (IPBA), and we owe a “thank you” to José Rosell, the IPBA’s Programs Officer, and Jingzhou Tao of Jones Day in Beijing for helping put together the program.

The China Committee co-sponsored the program, “The Struggle for Legal and Judicial Independence in Asia, Africa, and the Middle East,” that featured Committee Vice Chair Adam Bobrow as a speaker. We were honored also to co-sponsor the program “China’s First Comprehensive Antitrust Statute,” put together by Yee Wah Chin, a Division Chair in the Section. The Antitrust program successfully recruited two speakers from China: a senior member of the Ministry of Commerce and a speaker from the Chinese Academy of Social Sciences.

We also held a Committee breakfast and Committee dinner where we saw old friends and made new friends. We want to reiterate that participation in the China Committee’s activities is open to any interested party—and we welcome your help! For example, any Committee member may join the Steering Group—all we ask is that you (a) let us know of your interest; and (b) invest some time and effort into a project (either ongoing or something you propose). To volunteer for the China Committee Steering Group, please send an email to either of the Committee’s Co-Chairs, Elizabeth Cole (ecole@orrick.com) or Mike Burke (mburke@williamsmullen.com).

Co-Chairs Message, continued

The Committee has several activities planned in the next few months. We're in the process of working with the Section's International Tax Committee on a CLE teleconference discussing China's revised corporate tax code. We are also developing a CLE programs on supply chain security on imports from China and on cross-cultural issues in doing business in China. The Committee also has plans for CLE events in Shanghai and Beijing in the near future.

The largest event the Committee will co-host this year is the International Legal Exchange (ILEX) Program that will stop in Seoul, Tokyo, Beijing, Shanghai, and Hong Kong in July to examine the relationship between rule of law reforms and economic development. If you are interested in learning more about this ILEX program, please send an email to either of the Committee's Co-Chairs, Elizabeth Cole (ecole@orrick.com) or Mike Burke (mburke@williamsmullen.com).

The ABA year will conclude with the Section's leadership retreat in Atlantic City, NJ, and the ABA Annual Meeting in New York. The leadership retreat is open to current and future leaders, and those who wish to get more involved in the Section. Information on the leadership retreat may be found at http://www.abanet.org/intlaw/annual08/retreat_home.html. At the Annual Meeting, the Section will be headquartered at the Waldorf-Astoria Hotel. The China Committee will host a brown-bag lunch on Friday, August 8 at 12:00 in the Grand Ballroom at the Waldorf-Astoria, and the Section will host a gala celebration of the its 130 years of existence and 75th anniversary as an ABA section.

The International Law Section also co-sponsored the successful IPBA meeting that took place in Los Angeles in April, 2008. Our Committee's Vice Chair Qiang Bjornbak participated in the IPBA event and received a delegation of attorneys from Beijing, China.

This edition of the China Law Reporter has two great articles:

- "Does China's New Labor Contract Law Better Protect Intellectual Property Owners?" by Edward Lehman of Lehman, Lee and Xu, that explores the impact the new Labor Contract Law has on trade secrets, intellectual property and confidentiality related issues; and
- "Resolution of Disputes Involving China Investments: Practical Considerations" by Cedric C. Chao and Maria Chedid of Morrison & Foerster, that provides practical insights to effective resolution, and enforcement, of disputes involving investments in China.

In addition, Kara Phillips, Associate Director / Collection Development Librarian at the Seattle University School of Law, provides an update on selected China law books and articles.

We thank Edward Lehman, Cedric C. Chao, Maria Chedid and Kara Phillips for their valuable contributions to the China Law Reporter. We also thank Qiang Bjornbak, Paul Edelberg, Russell Leu and Cameron Smith for their hard work in putting together this edition of the China Law Reporter.

We look forward to an exciting few months for the Committee!

Elizabeth Cole is a partner in the Shanghai office of Orrick, Herrington & Sutcliffe.

Michael Burke is a partner in the Washington D.C. office of Williams Mullen.

RECENT DEVELOPMENTS

Does China's New Labor Contract Law Better Protect Intellectual Property Owners?

By Edward Lehman

The Labor Contract Law was adopted and announced on June 29, 2007 during the 28th session of the Standing Committee of the National People's Congress (NPC) and is certainly a "hot" topic of discussion and debate around the hot water dispensers amongst lawyers, IP portfolio managers, academics, government officials, workers & management, and foreign businessmen throughout the middle kingdom. Why all the fuss? This is, after all, a Communist country which has been striving to create a worker-peasant paradise since October 1, 1949. The answer is that this new law contains provisions to regulate both employers and employees on trade secrets, intellectual property and confidentiality related issues.

Now let us take a look at what that means. Chapter Two, clause 23 of the Labor Contract Law stipulates that employers and employees may elect to enter into an agreement regarding trade secret (read sales and distribution lists, customer lists, and even the actual sales and distribution employee list at the organization) as well as intellectual property and confidentiality related issues in the labor contract (so setting out in the employment contract an in-the-alternative set of clauses all within one document).

Also, employers can include non-competition restriction clauses in the labor contract with employees who are involved in trade secrets, and the parties may agree to a monthly compensation within the non-competition restriction period (for Europeans it is what is known as a "Garden Leave") upon termination of the contract. These non-competition clauses, in practice of course and according to my experience of creating what we call a legally binding "human resources package for employers", should always be included in all labor contracts. The employer may then elect to enforce the non-competition portion of the Labor agreement or not. As many employers in China know, in certain cases, employers are happy to be rid of certain lackluster employees and such employees may wish to go directly to their competitor. If this were to happen the employer can elect not to enforce the non-competition clause of the employment contract.

Another aspect to the new labor law is that employees who violate the non-competition restriction covenant may be held liable for damages. The Chinese NPC, in their wisdom, drafted this new Labor Contract Law to encourage innovation in the workplace and fair competition for all by stipulating the aforementioned non-competition restriction rule. However, keep in mind that this provision was only meant to apply to an employer's high-ranking management personnel, high-level technology personnel, and to those other employees who may be obliged to "keep trade secrets." So the warning here is to be very

specific in a non-competition clause, even to the point of naming your key competitors in the provision clause. The more specific you are, the more likely courts will enforce these non-competition agreements. Do not forget to set a specific formula for compensation to the employee (for example 40 percent of last annual income plus insurance, and welfare benefits). This too makes it easier for lawyers, courts and/or employers to enforce these clauses. The scope, region, and duration of the non-competition restriction must be agreed between employers and employees, and such covenant may not, of course, violate national laws, policies and regulations (again depends upon the industry sector, scope of the business license, and the nature of the employer's organization, so use professional help when drafting the agreements on a case-by-case basis to assure employer-clients are best protected). In any event, the duration the concerned personnel may be restrained from working with competitors, or set up their own businesses in the same trade, may not be longer than two years after the termination of the current labor contract. This is a change from the former laws, regulations and policies, which allowed for up to three years for the enforcement of an employee non-compete period. Score one for the employees.

We are forever reminding our clients to "hope for the best, but prepare for the worst", especially when it comes to intellectual property protection. If clients wish to protect IP, they should be the "first to file" (in Chinese & English along with all devices) for their trademark rights (it takes twelve to twenty-four months to get the trademark granted after examination and an opposition period). In the case of patents, designate China in a Patent Cooperation Treaty (PCT) application (thereafter you have 30 months to enter the national phase), or in the alternative, should you fail to file the PCT, try and bring the filing under the Paris Treaty within twelve months from the country of origin initial patent application. If you have developed software, make sure that employees execute a separate work-for-hire agreement and meticulously seek software recordal at the earliest time possible. However, we advise our clients to file a copyright recordal only after you discover a violation; otherwise it is too costly to file everything first. Once you have the granted copyright recordal right, the rights holder has prima facie evidence that they are indeed the copyright owner in a Chinese court. Yet another aspect that many overlook is the filing of a "Customs Recordal" once you have a granted IP right. This will allow you a "sword" to prohibit an infringer from importing or exporting a product to or from China and to work with the Customs. Your law firm can track the infringing product so that it may be seized at the port. This remedial action certainly gets the attention of an infringer as it hits them right in their pocketbook.

So in a nutshell that is the new labor contract law as it may impact IP rights. As I have written, it is not a panacea but rather a clarification that the protection of IP is important even under employment situations. We would further recommend that any employer creates a set of contracts in addition to the labor contract to more practically serve their interests and further their company's protection goals.

Additionally, we still recommend that the following be created to complement a well-drafted labor contract, namely: an employee handbook, an anti-corruption contract (which complies with the USA FCPA, the EU corruption act and China's anti-corruption

act), a separate non-competition contract (which could possibly survive should the employment contract have been terminated and then an employer discovers a breach at a later date), a separate non-disclosure agreement, and a work-for-hire agreement (for the same reason in both instances, so that this contract may survive the termination of the labor contract in the event the employer later discovers a breach, as well as the fact that sometimes it is better to bring a breach of these contracts straight to the attention of the intellectual property courts rather than before a less experienced judge which handles primarily labor issues only). We also recommend an expense report procedure contract in order to establish a reason for dismissal for cause and thereby avoid paying out severance salary for one month for each year the employee worked for the employer.

Edward Lehman is the Managing Director of Lehman, Lee, and Xu. He can be reached by telephone 86-10-8532-1919 or by email at elehman@lehmanlaw.com.

Resolution of Disputes Involving China Investments: Practical Considerations

By Cedric C. Chao and Maria Chedid

One fundamental way in which foreign parties can seek to manage risk and safeguard their China investments is by educating themselves about, and planning for, effective dispute resolution.

A Conciliatory Approach Is Best

Dispute resolution in China can take the form of negotiation, mediation, arbitration, or litigation. As a general rule, parties first should attempt to resolve matters through negotiation or nonbinding mediation. While this may be advisable with respect to disputes arising in any region, it is more so in China because the culture places high value on conciliation and views it as essential to preserving commercial relationships. More compulsive and legalistic methods of resolving disputes are seen, on the other hand, as a last resort for parties who have experienced a complete breakdown in their relationships.

Advantages Of Arbitration

When negotiation or mediation proves unavailing, foreign parties most often choose arbitration. The advantages of arbitration over litigation are generally well known—*i.e.*, avoidance of local courts that might favor their own nationals, relatively widespread acceptance of enforceability of foreign awards, and the opportunity to secure confidentiality of the proceedings. In addition, there is concern that courts and judges in certain regions of China may not be adequately equipped to resolve complex cross-border disputes. By choosing arbitration, parties avail themselves of a wide selection of expert panelists who can be appointed to decide their disputes. Also, arbitration pursuant to a familiar arbitral institution may offer foreign parties more transparency in rules and procedure than is often the case in the more remote Chinese courts.

Choice Of Arbitral Institution

For cross-border or “foreign-related” disputes, the most commonly proposed arbitral institutions are the China International Economic and Trade Arbitration Commission (“CIETAC”), the Hong Kong International Arbitration Centre (“HKIAC”), and the Singapore International Arbitration Centre (“SIAC”). United States and European parties sometimes propose the International Chamber of Commerce (“ICC”) or the American Arbitration Association (“AAA”), but Chinese parties often are reluctant to agree to these more “foreign” institutions. Western parties, on the other hand, are often hesitant to agree to arbitrations conducted within China proper. Given the concerns on both sides, HKIAC and SIAC are increasingly the institutions chosen, as both Chinese and Western parties have confidence in their professionalism and transparency.

Practical Insights To Effective Enforcement

Parties can take certain practical steps to enhance their chances of enforcement of arbitral awards in China. Parties should ensure that the terms of their arbitration agreements are in conformity with Chinese law. For example, the arbitration agreement should unambiguously designate the parties' chosen arbitral institution. *Ad hoc* arbitration should be avoided, because it is not favored and sometimes not recognized under Chinese law. To facilitate enforcement proceedings and avoid unnecessary delays, parties would be well served to have executed and annexed to their contract a Chinese translation of the arbitration clause. Parties should follow arbitration notice and other procedural requirements to the letter, and keep careful records evidencing that they have done so; seek enforcement in an appropriate venue, *i.e.*, either where the respondent is domiciled or where the respondent's property is located; and retain highly regarded local counsel with enforcement experience in the local court in which they are proceeding. Finally, parties should be prepared to provide courts with all available information about the respondent's attachable assets, and apply early for an asset freeze order.

Cedric C. Chao is a partner in the San Francisco office of Morrison & Foerster LLP and can be reached by telephone at 415.268.7061 or by email at cchao@mof.com.

Maria Chedid is a partner in the San Francisco office of Morrison & Foerster LLP and can be reached by telephone at 415.268.6292 or by email at mchedid@mof.com.

ITEMS OF INTEREST

Selected Recent English Language Books on Chinese Law

Banking Laws in China, by Zhongfei Zhou, Kluwer Law International, 2007, 255 p.
ISBN13: 9789041125194

<http://www.kluwerlaw.com/KLI/Catalogue/titleinfo.htm?ProdID=9041125191>

From the publisher: “In this authoritative book, a leading Chinese expert on financial and economic law thoroughly explains the functions, activities and procedures that characterize the behavior of financial institutions under current Chinese law. The book features: control of monetary policy formulation and implementation by the People’s Bank of China (PBOC); modern central banking functions of the PBOC; independence and accountability of the PBOC; requirements and procedures for banking entry; specific risk-based regulatory and supervisory requirements of the China Banking Regulatory Commission (CBRC); problem bank resolutions of the CBRC; foreign banking law developments before and post WTO transitional period; impact of new foreign banking regulations and rules on foreign bank activities in China.”

Modern Chinese Rules of Order: Paradox of Law and Economics, by Ulric Killion, Nova Science Publishers, 2007, 272 p. ISBN: 1600218377

https://www.novapublishers.com/catalog/product_info.php?products_id=5869

From the publisher: “The book addresses the issues of China's modern social order, as influenced by an evolving economic order and especially legal order. Ongoing Chinese modernization is prompted by both domestic needs and WTO commitments, which includes both economic and legal reforms. Emphasis is placed on legal reforms, one of the most important areas of much needed reforms. The directional development of China's legal order has national, interregional and international implications, which affect the growth and prosperity of both China and the world's economy. A problem is an evolving inter-relationship between social order, economic order, and legal order, which can be described as either complementary or paradoxical. However, a paradoxical inter-relationship between these sources of order is problematic, because it effectively renders much-needed legal reforms increasingly more difficult to implement. This book explores both the complementary and paradoxical inter-relationship between these sources of order, the author proposes a "novel" and "viable" alternative for transplanting a more Western constitutional design in China.”

Ownership in China's Transitional Economy: the Limitations of Conventional Property Rights Theory, by Chen Yang, Edwin Mellen Press, 2007, 356 p. ISBN13: 9780773452657

<http://www.mellenpress.com/mellenpress.cfm?bookid=7202&pc=9>

From the publisher: "This study seeks to develop a thorough understanding of the change of ownership and property rights in the context of China in transition, with all the political and social implications that the process entails. To do so, the work aims both to understand and challenge the conventional property rights theory which fails to consider the organizational context of the societies in which economic institutions operate. The research identifies the strong presence of the state associated with the evolution of high-tech spin-offs in transitional China, the process of which has also been characterized by fuzzy property rights and public entrepreneurship as two key stepping stones of development."

Pirates in the Middle Kingdom: the Ensuing Trademark Battle, 2nd Edition, by Tan Loke Khoon, Thomson/Sweet and Maxwell Asia, 2007, 480 p. ISBN: 9789626613276

http://www.sweetandmaxwellasia.com/products/prod_spec.asp?ProdId=2015&cvalue=a25a54a124a48

From the publisher: "The second edition of *Pirates in the Middle Kingdom* provides a comprehensive analysis of China's developing trademark laws. Application of relevant rules in regulations are neatly illustrated by case studies and useful appendices include translations of the Chinese Intellectual Property and Trademark laws, related notices and regulations and cases decided by the Chinese Supreme People's Court."

Selected English Language Legal Articles

The Rule of Law in China: Chinese Law and Business Series, published by the Oxford Foundation for Law, Justice and Society China Programme has recently published its second volume entitled, Is China Trapped in Transition? Implications for Future Reforms. Contents include:

- *Is China Trapped in Transition? Introduction: Randall Peerenboom
- *Is China's Transition Trapped and What Should the West Do about it? Policy Brief 1: Minxin Pei
- *The Political Economy of China's Transition Policy Brief 2: Joseph Fewsmith
- *China's Transition: Predatory State or Developmental Autocracy? Policy Brief 3: Barry Naughton
- *China: Suffering from Growth Pains or Doomed to Stagnation? Policy Brief 4: Dali L. Yang
- *Are China's Legal Reforms Stalled? Policy Brief 5: Randall Peerenboom
- *Traps, Gaps, and Law: Prospects and Challenges for China's Reforms Policy Brief 6: Jacques deLisle

- *China's Transition and the Limits of the American Constitutional Perspective Policy Brief 7: Michael W. Dowdle
- *The Chinese Banking Sector Policy Brief 8: Victor Shih
- *The Role of Foreign Investment in China's Transition Policy Brief 9: Lester Ross
- *China's Trapped Transition Reconsidered Policy Brief 10: Minxin Pei

Foreign Affairs has published a feature issue (v. 87, issue 1, January/February 2008) entitled "Changing China." Articles include:

- *"Long Time Coming," by John Thornton, p. 2
- *"The Rise of China and the Future of the West," by G. John Ikenberry, p. 23
- *"China's New Dictatorship Diplomacy," by Stephanie Kleine-Ahlbrandt and Andrew Small, p. 38
- *"Reconsidering Revaluation," by David Hale and Lyric Hughes Hale, p. 57

Submitted by Kara Phillips, Collection Development Librarian/Associate Director, Seattle University Law Library. Ms. Phillips can be reached at: phillips@seattleu.edu.

Volume 4, Issue 2
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About the China Committee

This committee supports ABA members with interests in China-related legal matters. Committee work, both in the U.S. and in Greater China (the Chinese mainland, Hong Kong, Taiwan and Macau), includes review, analysis, comment and information-sharing on matters of law, legal practice and related policy. Within Greater China, the China Committee works to facilitate links and understanding between US and local legal practitioners and law students and to further the development of the rule of law, including implementation by China of its WTO commitments.

About the China Law Reporter

The *China Law Reporter* is a publication of the China Committee of the Section of International Law of the American Bar Association. Editors are Qiang Bjornbak, Esq., of the Law Offices of Qiang Bjornbak in Los Angeles, California and Vice Chair of the China Committee (qbjornba@yahoo.com), Paul B. Edelberg, Esq., Counsel to Murtha Cullina LLP in its Stamford, Connecticut office (pedelberg@murthalaw.com), Cameron J. Smith, a law student at Northern Illinois University (cjsmith82@gmail.com) and Russell K.L. Leu, Esq., Counsel to the law firm Taft, Stettinius & Hollister LLP (leu@taftlaw.com). Contributions of articles and other items for the *China Law Reporter* are welcome. Please submit to all of the editors simultaneously. All articles are subject to editing by the editors. Guidelines for authors of articles for this Reporter can be obtained by contacting any of the editors or found at <http://www.abanet.org/dch/committee.cfm?com=IC860000>.

The articles published in this issue reflect the views of their respective authors and are not necessarily the views of the China Committee, its leadership or the Section of International Law. Any questions regarding such articles should be directed to the author(s) in question. The articles in this issue should not be construed as legal advice in any particular transaction.