

NEWSLETTER
EFFECTIVE PROTECTION OF TRADE SECRETS
BY CRIMINAL AND CIVIL ACTIONS



Effective Protection
of Trade Secrets
by Criminal and Civil Actions

The protection of intellectual property rights (IPR) has always been a concern to foreign investors investing in China. Among the various types of intellectual property rights, trade secrets that investors are reluctant to disclose or that cannot be publicly registered due to lack of the patent novelty are very often involved in foreign investment projects.

Based on the recent development of legislation and judicial practices in China, this article provides investors with some practical suggestions for protecting trade secrets.



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Trade secrets are primarily protected in China through the relevant provisions of the Anti-Unfair Competition Law. China amended this law in 2019 to strengthen the protection of trade secrets. Recently, on September 10, 2020, the Supreme People's Court officially issued the Provisions of the Supreme People's Court on Several Issues Concerning the Application of Law in the Trial of Civil Cases Involving Infringement of Trade Secrets (the "Judicial Interpretation on Trade Secrets"), which further provides a clear and explicit basis for the protection of trade secrets with many details. At the same time, the "Interpretation (III) of the Supreme People's Court and the Supreme People's Procuratorate on Several Issues Concerning the Concrete Application of Laws in Handling Criminal Cases of Infringement of Intellectual Property Rights" ("Judicial Interpretation (III) of the Two Highs"), issued on September 12, 2020, expands the incrimination of infringing on trade secrets.

Based on the aforementioned laws and regulations and in form of questions and answers, this article provides investors with some practical suggestions for protecting trade secrets.

1. What kind of information of my company could be considered as trade secrets?

Article 9 of the Anti-Unfair Competition Law stipulates that trade secrets refer to technical information, operating information and other commercial information that is not known to the public, has commercial value and is subject to appropriate secrecy measures taken by the right holder.

According to the Judicial Interpretation of Trade Secrets, **technical information** means information related to technology such as structure, raw materials, components, formulas, materials, samples, patterns, plant new breeding materials, processes, methods or their procedures, algorithms, data, computer programs and their related documents. **Operating information** means information such as ideas, management, sales, finances, plans, samples, bidding materials, customer information, data, etc., related to business activities.

It is worth noting that the **customer information** here includes the customer's name, address, contact information, as well as trading habits, intentions, content, and other information. In the judicial precedents, simple and publicly available customer

name, address, contact information, etc. can often not be directly recognized by the court as trade secrets. Customer information that constitutes a trade secret shall be special customer information that differs from related public information, or customer lists of many customers that have been collected and compiled over a long period of time.

2. What requirements should be met for such information to be protected as trade secrets?

Traditionally, information that is a trade secret under Chinese law is required to meet three basic conditions: (1) it is not known to the public; (2) it has commercial value; and (3) the owner has taken measures to keep it confidential. The Judicial Interpretation of Trade Secrets lowers the threshold for information to be considered as a trade secret by further refining the aforementioned three basic requirements.

Not known to the public usually means not freely available from a public resource, public forum etc.. For example, information that is common knowledge or practice in the industry, or that is presented or displayed in reports, seminars or publications, is usually considered to be available to the public. However, information may be considered "not available to the public" if the information is compiled, improved, or processed based on public information.

In terms of **commercial value**, the Judicial Interpretation of Trade Secrets only requires that the information has actual or potential commercial value. Unfinished working results formed in the course of production and business activities can also be recognized as trade secrets. For example, an enterprise's research and development of a product, even if it does not result in a finished product that can be put into production, the information in the research and development process can still be protected by trade secret stipulations.

3. What confidentiality measures should we take as the owner of the information?

In judicial practice, the question of whether the owner of the information has taken "confidentiality measures" has been the focus of court scrutiny. Failure to take the necessary protective measures is difficult to obtain the protection of trade secrets.



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According to the nature of the trade secret and its vehicle, the commercial value of trade secrets, secrecy measures' identifiable degree and its correspondence to the value of the trade secret, the right holder's willingness to keep secrets and other factors, the court determines whether the right holder has taken corresponding and sufficient confidentiality measures. Accordingly, it is recommended that the information owner adopt at least the following confidentiality measures in his business activities.

- 1) Signing confidentiality agreements or agreeing on confidentiality obligations in commercial contracts;
- 2) Imposing confidentiality requirements on employees, former employees, suppliers, customers, and visitors who have access to trade secrets through company bylaws, training, internal rules and regulations, and written communication;
- 3) Restricting visitors to, or distinguishing and managing, confidential production and business premises such as factories and workshops;
- 4) Distinguishing and managing trade secrets and their carriers by means of marking, classifying, isolating, encrypting, sealing, restricting access to them or limiting the range of persons who can access them;
- 5) Taking measures to prohibit or restrict the use, access, storage and copying of computers, electronic devices, network infrastructure, storage devices, software, etc. that can access and obtain trade secrets;
- 6) Requiring departing employees to register and return, remove or destroy trade secrets and their carriers which they have access to or have acquired, and prolonging their obligation of confidentiality after departing.

4. What steps should we take if there is a risk of a leak or a breach of confidentiality?

In case of risk of disclosure, that is, the imminent illegal disclosure of trade secrets, if it can be proved that not immediately taking preservation measures could result in damages of the right holder's interests, the enterprise as owner of trade secrets can apply to the court for an injunction to prohibit the infringer from disclosing, using or allowing others to use the relevant information, documents, etc. protected by trade secrets. At the same time, the enterprise shall collect and preserve relevant evidence as soon as possible and initiate legal proceedings.

If the leak has already occurred, an application may also be made to the court for an injunction or for measures of preservation of property during or prior to civil proceedings.

5. What should we do if a former employee with knowledge of a trade secret brings the trade secret to his or her new employer for use?

1) Civil Action

Filing a civil lawsuit is the most common and effective way to resolve the matter, and the trade secret owner may consider suing both the former employee and his or her new employer at court. The court will generally examine:

- Whether the former employee and his new employer **had access to** the trade secrets in question. For example, the former employee's former job title, job description, and whether he or she dealt with trade secrets on the job.
- Whether the former employee and his new employer used information that was **substantially the same as** the trade secret in question. For example, whether the new employer and the trade secret owner used substantially identical tender documents, entered into substantially identical contracts with business partners, etc..
- Whether the new employer **knew or should have known of** the employee's tortious conduct so as to constitute contributory infringement. A new employer may be found to have knowledge or should have known when the new employer receives significant business growth as a result of the employee's onboarding and the new employer knows what the employee's job with the previous employer was and the employee had access to trade secrets.

2) Criminal Action

Filing with the public security office to initiate criminal proceedings is another means to be considered. The latest Judicial Interpretation (III) of the Two Highs has lowered the threshold for criminalization, and criminal liability can be triggered if the amount of damage caused to the right holder of a trade secret or the amount of illegal gains from infringement of trade



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secrets is more than **300,000 Yuan** (previously 500,000 Yuan).

For the calculation of the aforementioned amount of 300,000 Yuan, in different situations different calculation methods can be used, such as: 1) reasonable royalties for the trade secret; 2) the loss of sales profits suffered by the right holder due to the infringement i.e., the total amount of reduced sales multiplied by the right holder's reasonable profit per product or the infringing product sales multiplied by the right holder's reasonable profit per product; 3) the trade secret's commercial value, i.e., its research and development cost, the combined revenue from the implementation of the trade secret, etc.

It is worth noting that remediation costs incurred by the right holder of a trade secret to mitigate damage to business operations, business plans, or to re-establish the security of computer information systems, or other systems, should be included in the damage caused to the right holder of the trade secret. In this case, the 300,000 Yuan threshold will be reached easily.

3) Criminal and Civil Action in Parallel

In practice, many enterprises that have been infringed are willing to try to use both criminal and civil measures to protect their own interests to the maximum extent. As public power is involved in criminal proceedings, criminal investigation can be used to collect and fix evidence, take criminal coercive measures against infringers/suspects, and seize and freeze property involved in cases, so as to stop infringement in time and prevent the expansion of infringement damages, which can undoubtedly promote the smooth progress of subsequent civil proceedings.

It is important to note that under procedural law, how civil and criminal proceedings interface and how torts and damages are proved under different procedures require the assistance of a seasoned team of lawyers for thorough deployment and implementation.

6. To what extent the losses we have suffered are compensable

When calculating the damages available to the infringed right holder in civil proceedings, the court may, in accordance with the law, calculate the damages in way of the loss of the right holder or the tortfeasor's profit, or, in many cases based on the court's comprehensive discretion. In contrast, there is considerable uncertainty as to whether compensation will be achieved through recovery or refund in criminal proceedings. In many cases, the court considers the infringement of trade secrets does not fall into the "unlawful appropriation and disposal of the victim's property", hence the recovery or refund is not applicable. Therefore, the infringed right holder may still need to seek financial compensation through civil proceedings.

7. What should we look for when hiring new employees at our company

In view of the new legislation to strengthen the protection of trade secrets, the company hiring new employees, must be proactive about the new employee's past position, job content, whether subject to confidentiality obligations, etc., and document the findings in writing. In the employment contract, the employer should require new employees to warrant that he is not subject to the confidentiality obligations of the former employer, or if such obligations exist, he will not breach in his new job. The employer should especially closely supervise and assess the performance of such new employees in order not to be involved in potential infringement of other's trade secrets.



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