

# STATE SECRETS AND TRADE SECRETS IN CHINA

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**STATE SECRETS  
AND  
TRADE SECRETS  
IN CHINA**

# PREFACE

This publication has been written with the aim of providing practical guidance to foreign enterprises doing business in mainland China. It has also been written to assist the many legal counsel and other business advisors (both in the region and internationally) whose role is to assist these enterprises navigate their way through the different and special business, legal and regulatory environment that is found in mainland China.

Before readers move onto the main sections, it is important to understand the context of this publication and a little of its broader aims and issues as well.

## **Understanding the rationale for the laws**

In order to conduct business with any counterparty anywhere in the world there needs to be an exchange of commercial information; Sino-foreign commercial relationships are no different. However, in mainland China, this exchange often involves an additional, somewhat novel, risk to foreign counterparties in that they need to be aware of and comply with broader PRC laws on State and trade secrets which protect their Chinese counterparty's information. This publication is about the implication of these laws on the exchange of China-related commercial information.

On a practical level this publication therefore aims to provide ways to identify where State and trade information risk arises in mainland China. In doing so, it is hoped that readers will be able to understand where these risks exist and then take appropriate steps to mitigate them in their business. This publication also sets out, in outline, some of the main practical methods of mitigating this particular risk.

While the publication will assist readers in understanding the relevant laws and how they work, we hope it will also assist readers in understanding the legislative purpose behind the State secrets and trade secrets laws. To properly understand the legislative intent, readers need to appreciate some of the historical, political and economic reasons why China treats certain types of information as State secrets (particularly State secrets relating to China's economic development).

In short, if readers can understand why these laws exist, they will be better prepared to ascertain the scope of the risks involved in any particular dealing. The whole area will also become clearer and a little less difficult to navigate through.

### Broader topics

There are broader discussions to be had on State secrets. These include the problem of definitional uncertainty (which most commentators agree is the core concern with State secrets) and the way in which the law is applied in mainland China. In this respect, we have set aside a whole chapter to discuss the *Rio Tinto* decision, which, although decided on the law of trade secrets, represents one of the more problematic decisions on the way in which commercial information is treated in China.

There is also of course the broader question of whether a State-Owned entity's ability to rely on State secrecy laws somehow gives them an advantage over foreign entities.<sup>1</sup> We do not intend to focus too much on this aspect, but consider that at a basic level SOEs do in fact have a distinct advantage over their foreign counterparts in this regard.

One advantage is the available remedies for infringing the same classes of business information (say for example research and development data for a new product). If the SOE has classified the information as a "State secret", it may be able to refer the matter to the State Security Bureau for investigation and eventual prosecution. If the information is a trade secret, then of course it has the option of commencing a civil action and if the damage is "significant", a criminal prosecution. In both cases, the SOE has the home court advantage of the Chinese courts. Although a foreign entity is, according to Chinese law, also able to seek the assistance of the authorities in bringing a criminal prosecution for breach of trade secrets law, we have not been able to locate any report of this in fact happening. It is certainly not a regular occurrence.<sup>2</sup> The foreign entity with a claim for a similar infringement will usually be left with the option of a civil claim in the Chinese courts.<sup>3</sup> Irrespective of the potential differences in compensation, the level of deterrence provided by the prospect of a criminal prosecution under State secrecy laws will, in itself, provide the SOE with a much greater level of protection of its information than any foreign entity is able to obtain in mainland China.

Finally, while a comprehensive legal analysis on all of the issues is somewhat beyond the scope of this work, we hope that some of the issues raised in this publication

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<sup>1</sup> We use "foreign entities" to refer to foreign companies (registered outside mainland China) and Wholly Owned Foreign Enterprises (WOFE) and Foreign Invested Enterprises (FIE).

<sup>2</sup> See the further discussion of this issue in Chapters 2 and 3.

<sup>3</sup> While breaches of agreements with an appropriately drafted arbitration clause will of course allow the foreign investor to arbitrate their claims for breach of trade secrets, the claims for the unlawful obtaining/infringement of trade secrets in extra contractual scenarios will require a civil claim to be brought in the Chinese courts.

may encourage further study and research in this area by academics in the PRC and abroad.

It is intended that the Law as stated in this publication is as at February 2011.

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Herbert Smith LLP  
Beijing, February 2011

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