

Reflections on the practices in investigating and handling infringement of trade secret cases

Qingdao Municipal Industrial and Commercial Administration

Trade secret is the life line of businesses. In recent years, the Qingdao Municipal Administration of Industry and Commerce (the Administration) has taken protecting businesses' trade secrets as the top priority in its endeavor of assisting enterprises and maintaining good order in market competition. It has dealt with a host of infringement of trade secret (ICS) cases, with fines and forfeits amounting to half a million RMB Yuan and recovered about 30 million RMB Yuan of losses for the victims, achieving excellent legal, economic and social effect. Now I will brief you on the cases handled by the Administration and share with you our experiences in dealing with them.

I. Basic characteristics of the ICS cases handled by the Administration

The ICS cases handled by the Administration in the past two years mainly take on the following features:

First, the majority of victims of those cases are high and new technology enterprises. Nearly all of the four cases handled by the Administration involved such enterprises. For example, one of the victims is a Qingdao based new materials company specializing in the export of ceramics materials. One of the products concerned is a kind of frit which is mainly exported to Southeast Asian markets. Another victim, a limited liability company in Qingdao specializing in measuring

technologies, is a leading coordinate measuring machine manufacturer. It boasts the most advanced technologies in this field in China with three types of machines, ALPHA、GLOBAL and TORO as its core products. A third victim is a Qingdao based company (ltd) specializing in ecological technologies. It's main line of business is the forestation of barren hills and it enjoys cutting edge technologies in this industry. All three companies have been officially accredited the status of high and new technology company of Qingdao by the Qingdao Municipal Science Commission.

Secondly, most of the infringing acts are committed by employees or former employees of the victims. Of the four above mentioned cases, two involve former employee abusing trade secrets of the companies after a job hop; the other two involve current employees stealing and selling the trade secrets of their employer. For instance, in the case involving the import and export company, one of the violator's employee used to as the vice CEO and then vice director general of the bidding & procurement department of the victim company; in the case involving the new material company, the manager of the violator used to be a share holder and vice general manager of the victim company and another employee of the violator used to be in charge of related business when working in the victim company. And the violators in the cases involving the measuring technology company and the ecological technology company are all current employees of their respective victims.

Third, the trade secrets involved are invariably of great practical utility. In all four cases, the trade secrets involved are of high practical utility, which can bring about considerable economic benefits and a strong competitive edge to their owners. On the other hand, violation of them will cause the obligees huge losses and even precipitate them into

serious difficulties due to the loss of advantages. For instance, the victim in the case involving the Qingdao import and export company suffered sharp decline of business volume and a total loss of about 2.5 million RMB Yuan. In the case involving the Qingdao new material company, the violator took advantage of the client information obtained through the former employee(s) of the victim company to conclude a deal of 110 tons of goods that worth 33 thousand US dollars.

Fourth, investigation and evidence taking of the cases involve great technical difficulties. It is hard to get a lead to these cases where the infringing acts involve high technologies, are well hidden and the violators know how to counter investigation. What's more, the legal definition to trade secrets is a little vague. For these reasons, it is usually very difficult to investigate and take evidence of these cases. For instance, on the question of whether client information should be termed as trade secret, confusion exists due to the fact that those clients are out there and some of them even make use of various media to publicize their products and services and thus are widely known to the public. What's more, as information technologies develop in leaps and bounds, ways of obtaining, storing and communicating information are increasing, their speed ever increasing and functions strengthening, all these will cause difficulties in the investigation of the cases.

II. Standards adopted by the Administration for authenticating evidences in ICS cases

In handling ICS cases, the Administration have focused on resolving two core questions: whether the secret (s) involved constitute trade secret (s) and whether the activities involved constitute infringement on trade

secrets. With the cooperation and support of the obligee and public securities departments, we have done much work in investigation and evidence taking, which is vital to affirming a case. The following is a case in which a Qingdao import and export company takes advantage of the client information obtained through the former employee of an investment group company to make illegal profits. The case will be used as an example to demonstrate the standards adopted by the Administration to confirm a case.

First, the objective existence of the trade information in question.

Information is the major component of trade secret and a major right asserted by the obligees as well. Trade information takes the forms of products promotion tactics, financial assessments of the company, list of clients, the bottom price in an offer and other information relevant to the company's market operation. In this regard, the Administration will have the obligee present their operation information to be protected and name the protection scope, so as to ascertain the areas where secrets lie.

Evidences for the trade information can take various forms, such as paper material and computer data. In the example, the obligee Oumei Company presents two pieces of evidences, one is a cooperation agreement with a certain foreign company which appointed Oumei Company as its sole general agent of Hyogo pulp in Shandong, and stipulates that the supply price will be lower than that of like products in the market. The other is 15 lists of domestic clients' information. These evidences prove that the clients' list and price offer in the cooperation agreement are objective information and thus should be identified as trade secrets.

Second, the obligee has clear ownership over the information in question. Some of the information may be obtained by the obligees's

own research and development; others may be obtained by transfer. Generally speaking, the lawful owner of the operating information is the valid obligee of it, and those with exclusive right of use can also exert their due rights. In the case, the obligee came out with a series of pulp supply and sales standing books, tender offers, procurement accounts and personal information of the salespersons appeared in the pulp clients list. They indicated that the clients appeared in the lists and those made the price offers are the special client group of the victim, who has put into labor and fund to form them. The victim has exclusive right to the client group, which can bring advantage to it and can't be obtained without like efforts by others. On the other hand, when law enforcement officers required the violator to produce evidences, it wasn't able to present any evidence to prove the client information and price offers in its possession were attained by lawful means. It only maintained the clients' contact information, such as telephone number can be found online and belongs to public information. It can thus be concluded that the violator's reasons are invalid and the victim is the legal owner of the trade secret in question and is entitled to the due rights therein.

Third, there are verifiable evidences to prove that secret-keeping measures have been taken on the trade secrets in question. This is the statutory prerequisite for a piece of trade information to become legally protected trade secret, because no information can be termed as secret without secret-keeping measures to keep it so, nor can its holder gain profits by exploiting its monopoly of it. Evidences of secret-keeping measures take mainly the following forms: first, relevant regulations on strengthening control of the media of the information, such as regulations concerning security time limit, applying confidentiality seal to the media in question, encoding of computer data, the copying and destroying of materials and so on. Second, make secret keeping requirements in

employee's meeting or core staff meeting. Third, making a confidential agreement between the obligee and particular persons, this lays out their respective rights and duties. In this case, the obligee produced its company regulation on protecting trade secrets, which had been issued to the entire staff and its labor respective agreement with Mr. Ma and Mr. Han. These evidences proved that the clients list and price offer have been listed as trade secrets of the victim and Mr. Ma and Mr. Han, whose labor contracts with the victim were still in effect, were obliged to abide by the confidentiality clause. It can thus be concluded that the information in question has all the constitutive elements of trade secret and deserves legal protection.

Fourth, there are concrete evidences for the practical utility and economic value of the trade information in question. It is the obligee's economic interests that are supposed to be protected by law, if it can't be proved that the information in question can bring about economic return to its owner, it will be pointless to handle the case involving it. It is for this reason that the Law takes practical utility and economic value as important constitutive elements of trade secrets. In this case, it has been proved by the law enforcement officers that the information in question is of practical utility and economic value, drawing on evidences presented by both the violator and the victim.

Fifth, the activities in question carry strong signs indicating an infringement upon trade secrets. The State Administration of Industry and Commerce has laid out five instances of infringement on trade secrets in the "*Regulations on forbidding the infringement upon trade secrets*" (the Regulation). Evidence taking work should take different approaches in these five different instances. In this case, the acts of the violator fit into article 3, paragraph 2 of the Regulation, which provides that "Obtaining, using or disclosing another's trade secrets by a third party

who clearly knows or ought to know that the case falls under the unlawful acts listed in the preceding paragraph shall be deemed as infringement upon trade secrets”. In order to have a complete evidence chain, law enforcement officers conducted in-field investigation in the violator’s offices at the right time and collected key evidences of infringement at the earliest time possible, thus seized the initiative in the case. The evidence chain for the infringement is composed of the following items: First, two pieces of price offer signed by Ma, which can prove that Ma had worked in the pulp business in the victim company. Second, three pieces of correspondence about the wood pulp between the victim and its client, which can prove that the violator obtained the victim’s client information through Ma and Han. Third, five pieces of wood pulp clients list collected from the violator’s, which are largely the same with these of the victim’s. They can prove that the violator had obtained and exploited the victim’s trade secret. Fourth, two pieces of correspondence between Han and a certain foreign company, which can prove that Han had abused his relationship with the clients to provide favorable conditions for the violator in doing wood pulp business. Fifth, a sales contract of 315 tons of wood pulp between the violator and a certain paper making company in Rongcheng city, Shandong province, which can prove that the violator had completed a wood pulp deal using the victim’s trade secret. Investigation and inquiry on the registration record and current account of the violator were then carried out. It was confirmed that Ma and Han were those handling the violator’s business operation, and that they had, in violation of the confidential agreement with the victim, allowed the violator to use the trade secrets obtained during their long-term service at the victim company to gain illegal profits.

Sixth, there are clear facts regarding the infringement scope.

Evidences in this respect are mainly used to identify the extent of infringement, such as the market scale of the product in question and the dissemination scope of the trade secret. Only after identifying the extent of infringement can the losses and impact of the infringement be confirmed, and they will then serve as the basis for imposing administrative penalty. In this case, evidences show that the violator only concluded one Hyogo wood pulp sale deal of 315 tons with the Rongcheng-based paper making company since its registration in March 2006 till the date of the case's reporting.

III. Some Observations

The Administration has built up the following observations through its practices in dealing with cases of trade secret infringement:

1, High and new technology (HNT) companies should be the focus in our efforts to strengthen protection of trade secrets. Firstly, these companies have the most trade secrets. Scientific discoveries and technical innovations made in the past 40 years by mankind exceeds all those made in the past 2000 years combined. Unlike traditional businesses, the survival of HNT companies rely totally on high and new technologies and human capital, and high technical and information content is the general characteristic of HNT business. The core part of the technology and information is unknown to the public, this is its secrecy; it can bring about economic benefits to its obligee, namely it has economic value; it can definitely be put into practice use, namely it has practical utility; and the obligee has taken secret-keeping measures on it. These four aspects are the innate and necessary constitutive elements of a trade secret. Secondly, trade secret is the lifeblood of HNT companies. There is intense competition in the market place, and as an invisible asset, trade

secret is playing an ever more important role. Using their trade secrets, companies can gain an upper hand in technology and business operation, and garner extra profits over their rivals. A technical know-how, a product formula or a piece of business intelligence often can breathe new life into a company and make it thrive. It can be safely said that trade secrets is a matter of life and death to HNT companies, which, if deprived of trade secrets, will lose the foundation to survive and progress and be reduced to nothing more than empty factories. Third, HNT companies have become the major driving force for sustained economic growth. For example, in Qingdao, HNT companies have a vital strategic position in the development of the municipal economy. By the end of 2009, 205 companies in Qingdao have been accredited the status of HNT enterprises. Statistics show that HNT companies in the city achieved a total output value of 442.753 billion RMB Yuan, accounting for 46.51% of the total gross output of industrial enterprises above a certain size. As the major driver of the city's economic development, they deserve to have the protection of their trade secrets high on our agenda. Fourthly, HNT companies are the frequent victims of trade secret infringements. Market economy is characterized by fierce competition, and the competition among HNT companies is even crueler. Controlling independent-innovated technologies and relevant information is a key to win out in competition, and he who controls technologies and information will gain himself a favorable living environment. Thus certain companies or persons, driven by the thirst for high and excessive profits, often attempt to steal the trade secrets of HNT companies. For instance, of the four above mentioned cases handled by the Administration, 3 or 75% of them are about the infringement on trade secrets of HNT companies.

2. Cooperation and coordination with relevant sectors must be strengthened to provide a strong safeguard to the protection of trade secrets. To effectively protect trade secret, the strength of industry and commerce administrative departments is not enough; coordination among various parties must be enhanced. First, cooperation with the obligee must be intensified. As the victims of an infringement case, obligees usually have strong motivation to cooperate in solving the case. At the same time, they usually have more direct, in-depth and unique knowledge of the case in question and can play a special role in tackling thorny issues the case involves. In the cases handled by the Administration, the obligees have played a key part in the course of investigation, evidence taking, evidence authentication and other related work. Second, cooperation with the public security department, mainly in intelligence sharing and law enforcement coordination, must be strengthened. The vast intelligence databases of public security department can be used to find more leads. Their investigation instruments and methods can help obtain and preserve more evidences. In the above mentioned cases, through close cooperation with the public security department, we got hold of leads in a timely manner and obtained useful information such as the violator's phone record, text messages, and relevant information on the website and in their personal accounts by virtue of the public security department's investigative techniques, paving the way for the solution of the case. Third, cooperation and coordination with scientific and technology departments and secret-keeping departments must be enhanced. Due to the diverse forms trade secrets take, sometimes it's hard to precisely determine if a piece of information is trade secret only by such criteria as the four constitutive elements. At this point, the role of scientific and technology departments and confidentiality departments must be given full play. Fourth, coordination with other professional

sectors must be deepened. With the sophisticated distribution of labor, people in one industry hardly know much of other trades. So experts and personnel of related professional institutes must be consulted to facilitate the investigation of cases.

3. Trade secrets protection demands a swift and heavy-handed approach towards infringement cases. Swift actions will ensure the cases be solved in a timely manner while heavy-handed measures are needed to achieve due effect of punishment. The ultimate goal is to recover the obligee's losses to the largest extent. First, with the rapid development of modern technologies, there are more convenient ways to copy and store information, which can be transmitted through a much wider range of channels and at a much higher speed. Therefore, trade secrets once lost, can trigger huge and rapid consequences in the split of a second. This reality calls for swift actions in protecting trade secrets. Second, nowadays the work force is increasingly composed of young people, who tend to change job frequently. They have diverse pursuits in life and have no regular bases; they are usually not restrained by family bound or economic burden, so there is a considerably high turn-over in the work force. For instance, the employee turn-over rate in IT industry is as high as 25%, and the figure reaches 50% in some companies. Given this reality, were an infringement done, it will become more and more difficult to investigate the case and take evidences with the passage of time. That's why the law enforcement department has to move fast. Third, the great practical utility of trade secret can bring about considerable economic interests to the obligee. However, once it's lost, the obligee will not only lose advantage, but also suffer incalculable losses, such as shut-down, closure or even bankruptcy. Therefore, infringing acts must be punished heavy-handedly so as to increase the cost of the infringing act, achieve due deterrence and reduce potential violators' desire and attempt

to commit infringing acts. In this connection, the legal responsibility provided for in Article 25 of the Law is too light as a punishment to achieve due deterrence. It is suggested the ceiling for the fine be raised and confiscation be added to the clause. For instance, it should be stipulated that the range of the fine can be set as from 10,000 RMB Yuan to 2 million RMB Yuan and the unlawful income be confiscated.

4, Stepping up prevention measures is the fundamental approach to the protection of trade secrets. Rather than trying to amend after losses have been made, it is better to do a good job in prevention. Over the years, the Administration has urged and directed companies under its jurisdiction to adopt and keep improving a host of secret-keeping measures on their trade secrets through administrative guidance. We helped them to address fundamental issues and actively put in place long term mechanisms of trade secrets protection, which have produced good results. First, companies must be urged to set up trade secret regulations and mechanisms and be provided guidance in the course. Companies, on their part, should classify their trade secrets and manage them in a standardized and unified manner. Trade secrets, including technical information and operation intelligence should be classified by their weight of importance and divided into different categories, such as top secret, secret, and classified. Related regulations and mechanisms should be put in place to strictly clarify the level of secrecy of different information, define the right of access by staff at various levels to the information and the procedure of decoding and the level of review; as well as reasonable storing and sign-in rules. Second, companies should be urged to enter into confidentiality agreement and prohibition of business strife contract with their employees. Companies should make the confidentiality agreement with the employees, incorporate confidentiality clause into the discipline handbook and hand them out to all those with

confidentiality obligations and require them to sign on it. Confidentiality awareness raising programs should be carried out regularly among the employees. Prohibition of business strife contract with relevant personnel should be concluded in a timely manner to make clear that employees shall not hold posts in companies which operate in the same category of business and are in competition with the company, nor shall they operate themselves in such business when they are working for the company or within a certain period after quitting the company or. In practice, many disputes over trade secrets are caused by former employee job-hopping to their former employer's rival. Thus prohibition of business strife contract with core technical staff can help strengthen protection of companies' trade secrets. Third, companies should be urged to standardize the use of internet within the company and use tradition information media in certain particular cases. Measures should be taken to standardize access to internet or intranet in the company, such as installing relevant software or set access permission. It must be stressed that traditional paper-based media should be used in the management of important information, for they can easily be used as evidence when dispute arises. Fourth, companies should be urged to improve secret-keep hardware. While adopting legal measures enhance the protection of trade-secrets, companies should also improve related hardware, for example, carrying out in-out recording and management, install screen monitoring system and so on, which will facilitate investigation and evidence taking. Fifth, companies should be urged to add confidentiality clause into their contracts with other market players and exercise self-discipline. When concluding contracts of technology development, technology transfer, technological service and processing work, companies should ensure confidentiality clause is included in the contracts so that when a breach of confidence occurs, the obligee can demand the default party to cease the

infringing act, pay liquidated damage or indemnification for damage in accordance with the contract.

Attached: Brief introduction to the case of infringement on trade secret by a Qingdao-based import and export company

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On September 26 2006, an investment group company (hereinafter the obligee) reported to the Administration that a Qingdao-based import and export company (hereinafter the violator) has been making profit by the client information obtained through Ma and Han, the obligee's employees and is allegedly infringing the obligee's trade secret.

After investigation, it is found out that the obligee is the import agency of the Hyogo wood pulp of certain foreign country. Mr. Han serves as the vice chairman of the obligee while Mr. Ma serves as the vice director of the obligee's Tender and Purchasing Department and is mainly in charge of the purchasing and sale of wood pulp. Both Ma and Han have signed labor contract with the obligee. The labor contract and the company's regulation both have confidentiality clause which provides that the company's trade secrets must not be leaked. Field survey of the obligee's offices resulted in the following: two pieces of price offer made by the

obligee to its clients, which were signed by Ma. They prove Mr. Ma worked in the pulp business in the victim company; three pieces of correspondences about the Hyogo wood pulp between the victim and its client, which prove that the violator obtained the victim's client information; five pieces of wood pulp clients list, which are largely the same with these of the victim's. They prove that the violator has obtained and exploited the victim's trade secret; two pieces of correspondences between Mr. Han and the Hyogo Corporation, which said that Han has quitted the obligee and will conduct wood pulp business with the Hyogo corporation through the violator, which proved that Han has used his relationship with the clients to provide favorable condition to the violator in doing wood pulp business; a box of name cards of Mr. Ma as the vice general manager of the violator, which proved that Ma has engaged in business operation in the violator; a sales contract of 315 tons of wood pulp between the violator and a certain paper making company in Rongcheng city, Shandong province, which proves that the violator has completed a wood pulp deal using the victim's trade secrets. While the field survey is in process, we inquired the employees, which proved that Ma has been serving as the general manager of the violator and is the actual operator of its business. Later we inquired many times Ma, and the violator's representative, and take related evidences regarding the violator's bank account and the Rongcheng-based paper making company. It was proved that the violator indeed has concluded a wood pulp contract of 315 tons through Ma and Han and the contract has been fully executed. The Hyogo Corporation and the Rongcheng-based paper making company are both the obligee's ex clients. Ma and Han took away the clients using the obligee's client information in their possession, and this caused the obligee's business volume to decline sharply, resulting in a loss of over 2.5 million RMB Yuan. To control loss, at the appeal of the

obleege, the Administration issued a “Order to cease sale” to the violator in accordance with Article 25 of the Law, which stipulates that “In case a business operator violates the provisions of Article 10 of this Law and infringes upon trade secrets, the supervision and inspection department shall order the cease of the illegal acts”. The Administration is of the view that the violator's act has violated Article 10, paragraph 2 of the Law, which stipulates that Obtaining, using or disclosing another's trade secrets by a third party who clearly knows or ought to know that the case falls under the unlawful acts listed in the preceding paragraph shall be deemed as infringement upon trade secrets", and constitutes infringement on trade secret. Article 25 of the Law stipulates that “In case a business operator violates the provisions of Article 10 of this Law and infringes upon trade secrets, the supervision and inspection department shall order the cease of the illegal act and may impose a fine of not less than 10,000 Yuan but not more than 200,000 Yuan in light of the circumstances.” In light of the fact that the violator has only concluded one deal since starting business, in line with the principle of matching the punishment with the violation, the Administration decided to impose a fine of 20,000 RMB Yuan on the violator and order it to cease unlawful acts.