



MMLC Group – China Update

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Business News

China replaces US as Japan's biggest customer

China overtook the US as Japan's largest export market for the first time in July. Japan's exports to China rose 16.8% year-on-year - the highest level since Tokyo began tracking the statistic - while shipments to the US fell 11.5%. As the US economic slowdown intensifies, Japanese companies, including Honda and Komatsu, increasingly look to China for growth. However, Japanese exports to China might decelerate given the expected slowdown in Chinese growth and the country's increasing dependence on the EU as a source of goods.

Nissan to start exporting cars from China

Nissan Motor will start exporting passenger cars from China in the next few months. Nissan's first shipment will be to Egypt and will involve 400 Livina hatchbacks and Bluebird Sylphy sedans made at a joint venture plant in south China. This will be Nissan's first export of cars made in China.

KFC raises China prices again

Increasing commodities costs have led KFC to raise its prices in China for the second time this year. Prices will rise up to RMB2.5 (US\$0.36) for some items. The Kentucky-based restaurant chain posted a US\$378 million operating profit for the second quarter. Its China division contributed US\$90 million.

30% increase in software registration in the first half of 2008

In the first half of this year, a total of 14,540 software registrations were filed in China (including software copyright registrations and license registrations). This is 27.4% higher than for the same period last year. Of these registrations, the number of software copyright registrations hit 14,000, which represents a 29.12% increase over last year. The top five regions for the registrations are Beijing, Guangdong, Shanghai, Jiangsu and Zhejiang. Beijing still tops the list with 5,053 registrations.

Beijing plans value-added tax reform

Beijing is planning a new value-added tax regime that may save companies up to 150 billion yuan (HK\$171.14 billion) annually and encourage more investment in industries feeling the impact of slowing economic growth. Reforming the tax system is a prelude to a new round of economic sweeteners from Beijing as policymakers struggle to cushion the impact of weakening global and domestic economies. The adjustment in value-added tax will mainly ease the burden on manufacturers that have large investments in fixed assets such as factories and machinery. It is estimated that the change will reduce funds flowing into government coffers by between 100 billion yuan and 150 billion yuan a year.

China's outbound investment picks up

Outbound investment by Chinese businesses has entered a faster stage of development. In the first half of this year, China invested \$25.66 billion in other countries in the financial sector, up 229 percent on the same period last year. The commerce ministry is working on a series of reports on investing overseas. They cover investment opportunities, tax policies, investment risk and macroeconomic information.

Huijin increases stake in three top commercial lenders

Chinese three largest commercial banks announced that Central Huijin Investment Co Ltd, an investment arm of the Chinese government, had increased its shareholdings of the three banks. According to announcements released by the banks, Huijin has increased shareholdings of 2 million shares for each bank through shares purchases on the Shanghai Stock Exchange, and intends to continue to increase its shareholdings in the three banks on the secondary market within 12 months.

Dairy manufacturers to consolidate

Several Chinese dairy manufacturers are expected to go out of business or merge during the fight to win back public trust in the safety of their products. The fight will likely be a long one, predicting that the fallout from the melamine scare will be far more severe than the previous worst health crisis, in 2004, when 13 babies died after being fed infant formula that contained virtually no nutrition. The demand for foreign produced dairy products remains strong, leading to reports that the larger Chinese dairy companies may be looking at foreign acquisitions.

China cuts import taxes on large equipment spare parts

The Chinese government has cut back on import taxes on spare parts of large equipment and canceled the import tariff exemption on some complete sets. The adjustments were made to support the domestic manufacturing of large equipment, said the Ministry of Finance. The policy applied to imports after January 1, 2008, depending on the date of declaration of imports. In the meantime, the import of some complete sets of equipment by enterprises approved after September 1, 2008 would no longer enjoy the tax exemption. Both domestic and foreign-funded projects are subject to the new policy. Imports of such equipment by enterprises approved before September 1 would continue to enjoy the previous tax policies until March 1, 2009.

Beijing boosts financing for SMEs

Beijing has increased the amount the government can loan to small and medium-sized enterprises (SMEs). The Ministry of Finance posted a notice on its website announcing it had raised the ceiling on direct government aid to qualified SMEs to US\$440,463 (RMB3 million) from US\$293,642. The treasury also doubled the amount of interest loans allowed for each qualified borrower, to US\$440,463.

Ministry to hold hearing on Coke offer for Huiyuan

China's Ministry of Commerce will hold a hearing on Coca Cola's \$2.4 billion offer to buy China's largest juice maker Huiyuan. Domestic juice producers will jointly submit to the ministry three new acquisition plans for Huiyuan to replace the Coke deal. Huiyuan can be split and sold to Chinese enterprises separately, or be purchased by a yuan-denominated fund jointly set up by domestic companies, according to the plans. Another proposal was to okay the Coke-Huiyuan merger but retain the brand of Huiyuan and sell it to Chinese companies. Coke is obviously planning to "outbid" these offers even if they receive government support.

China cuts rates to ward off slowdown

China, following other economies, cut the benchmark deposit and lending rates by 0.27 of a percentage point to anchor its economy amid a worsening global financial crisis. The move will help prevent economic growth from declining as the global financial market turmoil is believed to further cut into world growth, which in turn will reduce demand for Chinese exports.

Buffett unit buys stake in battery firm BYD

MidAmerican Energy Holdings Co, a unit of US billionaire investor Warren Buffett's Berkshire Hathaway Inc, said it would pay \$230 million for a 10 percent stake in Chinese rechargeable battery firm BYD Co Ltd to support its 'green' technologies. The deal gives MidAmerican a foothold in the Hong Kong-listed company which is developing electric-hybrid cars it expects to start selling in China later this year and Europe by 2010.

Zoomlion buys Italian machinery maker

China's top construction machinery maker, Zoomlion, signed a purchase agreement with Italy's Compagnia Italiana Forme Acciaio Spa (CIFA). Zoomlion, along with Goldman Sachs

and two other investors, plans to buy CIFA for 271 million euros (\$395.7 million). Changsha Zoomlion Industry Science and Technology Development Co Ltd will pay 163 million euros for a 60 percent stake in the Italian construction machinery maker. After the acquisition, Zoomlion is expected to be the largest concrete machinery maker in the global market.

Legal News

B&Q wins trade mark litigation

B&Q, the British retailer of DIY and home improvement tools and supplies, won an action in the Zhejiang High People's Court against a Chinese competitor. The Court upheld an earlier judgment of trade mark infringement in favour of B&Q. The Defendant, Zhoushan Bai An Ju Trading Co. Ltd (Bai An Ju), offers services similar to those offered by B&Q. It uses 'Bai An Ju' as the distinctive part of its company name. The Zhejiang High People's Court held that the Chinese transliteration of 'B&Q' (Bai An Ju) was recognised as a well-known trade mark. The Defendant was ordered to immediately cease using its current company name, publish a rectification statement and pay damages of RMB 80,000 (approximately US\$11,765).

Chinese environmental firm notches up patent victory

In a high-profile patent dispute regarding environmental protection technology, the co-Defendants Japan Fujikasui Engineering and Huayang Engineering, a wholly owned subsidiary of Formosa Plastics Corporation USA, were found to have infringed the patent rights of CEPT (Wuhan Environmental Project

Technology Company). The Fujian High People's Court found that FKK had infringed CEPT's patent right on the method and the apparatus for natural seawater flue gas desulphurization. Damages were set at RMB 50 million (approximately US\$7.44 million). Huayang Engineering will also have to pay royalties of RMB 240,000 (approximately US\$35,294) for each unit and year of using the equipment in question. CEPT has appealed the damages and royalties awards.

Firm sued over 'copied' whisky

Diageo, the maker of Johnnie Walker Scotch Whisky, is seeking RMB 2 million (US\$294,118) in compensation from a local wine company for unfair competition and packaging violations. Diageo accuses Blueblood (Shanghai) Wine Co. Ltd of adopting similar packaging to Johnnie Walker Black Label on its Polonius whisky. Blueblood had argued that it used its own designers on the packaging and that it was using the packaging before Johnnie Walker entered the Chinese market. The Shanghai No. 2 Intermediate People's Court has heard the case, but has not yet reached a verdict.

Draft amendments to the Patent Law tabled

The Chinese Government has submitted draft amendments to the Patent Law to the Standing Committee of the National People's Congress, the top legislature in China. Several important changes would be made, such as the application process and enforcement of the law. An important change is the proposed removal of the statutory requirement for all Chinese individuals and entities to 'first file' invention applications in China. This revision would allow Chinese individuals and entities to file their patent applications first in countries other than China. The current provision requiring special government approval for a patent to be assigned by a Chinese entity to a foreign entity will most likely remain however.

China issues regulation to clear labor contract law

China's State Council, the country's Cabinet, issued the implementation regulations for the Labor Contract Law in Beijing last month, in an effort to clarify confusion surrounding the law. The regulation listed 14 conditions under which an employer can terminate a labor contract – these clarify some aspects of the law. These include an employee's incompetence to live up to the job requirements, serious violations of regulations and dereliction of duty. Another 13 circumstances were also included in the regulation, under which an employee could terminate his or her contract with an employer, including delayed pay and forced labor.

Macau 'preparing to enact security bill'

Macau is preparing a bill to enact the controversial national security law and may table it to legislators by the end of the year. Given the expected lack of opposition, there might not be any public consultation before the bill was submitted to the Legislative Assembly. Hong Kong and Macau have the same Article 23 in their Basic Laws. Under their mini-constitutions, both cities must legislate against treason and subversion, based on the article, though no specific timetable has been given. An analyst said the Macau government had kept quiet about Article 23 this year for fear of affecting the Legislative Council election in Hong Kong.

Working rules for New Anti-Monopoly Committee approved and Concentration Guidelines Issues

The State Council has approved working rules for the anti-monopoly committee under the Chinese Cabinet, and promoted anti-monopoly work. The Anti-Monopoly Committee's main functions are:

- Study and develop competition policy;
- Organize survey assessments of the overall market competitive conditions, release assessment reports;
- Develop, publish anti-monopoly guidelines;
- Coordinate anti-monopoly administration and law enforcement work;
- Other duties under the State Council as allocated.

The State Council released the official version of the Regulations on Notification Thresholds of a Concentration of Undertakings (Final Notification Regulations), on August 3, 2008.

Provision 3 of the Final Notification Regulations establishes two thresholds for mandatory advance notification of an impending concentration. An undertaking must notify the relevant authority under the State Council in either of the following circumstances:

- The total combined global turnover of all participants in the concentration exceeded RMB ten billion in the preceding fiscal year, and the Chinese domestic turnover of at least two participants each exceeded RMB 400 million in the previous fiscal year; or
- The total combined Chinese domestic turnover of all participants in the concentration exceeded RMB two billion in

the previous fiscal year, and the domestic turnover of at least two participants each exceeded RMB 400 million in the previous fiscal year.

The other substantive section of the Final Notification Regulations, Provision 4, authorizes the Ministry of Commerce to initiate mandatory notification even if the above thresholds are not satisfied, provided that the ministry collects facts and evidence, in accordance with law, proving that the concentration of undertakings will restrict or eliminate competition.

Trouble ahead for USB manufacturers

In the first-ever case of a Chinese IT company pursuing a patent complaint overseas, Netac, a Shenzhen-based manufacturer of USB flash memory devices, has reached an out-of-court settlement in the United States with the alleged patent violator, PNY Technologies, a New Jersey-based company. Netac filed suit in 2006 alleging that PNY was in violation of a 2004 patent that recognized Netac's USB flash memory technology. The suit, filed in an Eastern Texas district court and made under a section of the 1930 Tariff Act, was the first of its kind for a Chinese IT company, and the result could have far-reaching consequences for manufacturers of similar portable USB flash memory products. While the exact terms of the settlement remain confidential, it is widely believed that the settlement involves the payment of royalties by PNY to Netac and the signing of a patent licensing contract between the two parties.

This update is aimed at keeping our clients informed of developments in Greater China. Whilst every care has been taken to ensure the accuracy of this update, it should not be relied upon before individual advice is obtained. The MMLC Group is an international legal and corporate advisory group.