

December, 2011

**Draft amendment to the Measures for the Compulsory Licensing for Patent Implementation** (Draft for Comments) (Draft Amendment) (专利实施强制许可办法修订草案(征求意见稿)), issued by the Legislative Affairs Office of the State Council

Article 5 of the Draft Amendment introduces the possibility for any individual or organization to claim to the patent authorities the right of a compulsory patent license when the patentee's exercise of its patent rights constitutes monopolistic conduct. This amendment to the current *Measures for the compulsory licensing for patent Implementation* promulgated on June 13, 2003 is consistent with the revised PRC Patent Law that came into force on October 1, 2009. Under its article 48.2, where a patentee's exercise of its patent right is monopolistic under the Law and its negative impact on competition needs to be eliminated or minimized, the patent authorities may, if requested by an organization or individual that qualifies to exploit an invention patent or utility model patent, grant a compulsory license to exploit the patent. The amendment is also in line with article 55 of the Anti-Monopoly Law that came into force on August 1, 2008, which applies when business operators abuse their intellectual property rights to eliminate or restrict competition.

Under article 11 of the Draft Amendment, when applying for compulsory licensing, petitioners must submit an effective court judgment or decision from the anti-monopoly authorities finding that the patentee's exercise of the patent right is monopolistic conduct. However, as neither the PRC Patent Law or its implementing regulations, nor the Draft Amendment, clearly define "monopolistic conduct" or refer to the Anti-Monopoly Law, the ground for granting compulsory licensing remains unclear. In practice, the anti-monopoly authorities, the National Development and Reform Commission (NDRC), and the State Administration for Industry and Commerce (SAIC), have not issued guidelines on how to decide whether an act constitutes abuse of intellectual property rights and whether this abuse justifies compulsory licensing. Lack of clear guidance may give the responsible authority too much discretion in examining the compulsory licensing application.

This ambiguity may burden the patentee with having to fight against third parties' intentions to seek ways to obtain patents by pursuing compulsory licensing without paying.

Under the Draft Amendment, the State Administration of Intellectual Property is the only authority that has the power to accept and examine the application for patent compulsory licensing and to decide whether to grant it. The courts or the anti-monopoly authorities do not have the power to grant compulsory licensing when the abuse of intellectual property rights constitutes monopolistic conduct.

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#### Shanghai Office

27F Shanghai Central Plaza,  
381 Huai Hai Middle Road  
Shanghai 200020, P.R.C.  
+86 21 2327 7000  
+86 21 2327 7007  
shanghai@cuatrecasas.com

Contact partner:  
Omar Puertas

**Regulations on special labor protection of female employees** (Draft for Comments) (女职工特殊劳动保护条例 (征求意见稿)) (Draft Regulations), issued by the Legislative Affairs Office of the State Council

The Draft Regulations will replace the *Provisions on Labor Protection of Female Employees* currently in force. Compared to the *Provisions on Labor Protection of Female Employees*, the Draft Regulations have introduced various changes, including a significant change regarding maternity leave.

- Under the Draft Regulations, maternity leave for female employees will increase from 90 days to 14 weeks. In cases of difficult births, two more weeks are granted. In cases of multiple births, two more weeks are granted per additional baby.
- The Draft Regulations clearly state the maternity leave granted to female employees who have miscarriages or abortions. If this happens during the first four months, the female employee is entitled to at least two weeks' maternity leave. If it happens after the first four months, the female employee is entitled to at least six weeks' maternity leave.
- To be consistent with the recently issued *PRC Social Insurance Law*, the Draft Regulations provide guidelines on maternity allowance. If employers pay maternity insurance for female employees, then their maternity allowance will be calculated based on the average monthly salaries for all the employees of that employer during the previous year. This is good news for low-paid female employees, but bad news for high-paid female employees. However, if employers do not pay maternity insurance for female employees, their maternity allowance will be the same as their salary before delivery or miscarriage.

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**Administrative measures for registering debt-for-equity swaps** (公司债权转股权登记管理办法), issued by the State Administration for Industry and Commerce (SAIC)

These administrative measures are based on the draft measures issued on August 18, 2011 (see our August 2011 newsletter).

No significant changes are incorporated into these measures, except for deletion of paragraph 2 of article 5 of the draft measures, providing that when a creditor asks to register equity in foreign invested enterprises (FIEs) converted from indebtedness owed by such FIEs, or when a foreign creditor swaps loans that are already registered with the State Administration of Foreign Exchange (SAFE) as foreign debts for equity, these swaps must be approved by relevant authorities under the FIE laws, regulations and rules before their registration. It is not clear why SAIC deleted this in the final version of these measures. We will watch how the authorities deal with debt-for-equity swaps concerning FIEs and foreign loans registered with SAFE, and keep you updated.

*Date of Issue: November 23, 2011. Effective Date: January 1, 2012.*

**Circular on further clarifying and regulating the foreign exchange administration of certain capital account items** (Huifa [2011] 45) (国家外汇管理局关于进一步明确和规范部分资本项目外汇业务管理有关问题的通知), issued by the State Administration of Foreign Exchange (SAFE)

The Circular unifies the practices of local SAFE branches by clarifying that when foreign shareholders of foreign invested enterprises (FIEs) have not yet paid up their proportion of capital contribution, the FIE's debt capacity (the FIE's approved total investment minus its registered capital) will be calculated on a *pro rata* basis

proportionate to the capital paid in by the foreign shareholders. Therefore, for wholly foreign-owned enterprises (WFOEs) the picture has become clear. However, for non-WOFE FIEs (i.e., FIEs that have Chinese shareholders), the question remains unclear when the foreign shareholders have paid in their proportion of capital contribution but the Chinese shareholders have not fully paid in their proportion. Literally, the Circular clarifies situations in which foreign investors have not made full capital contributions, but remains silent about when Chinese shareholders have not fully paid in their capital contributions.

*Date of Issue: November 9, 2011. Effective Date: November 9, 2011.*

**Announcement on the launching of the pilot program on converting from business tax ("BT") payer to value added tax ("VAT") payer for the transportation industry and certain modern service industries in Shanghai** ("Announcement") (Caishui [2011] No. 111)( 关于在上海市开展交通运输业和部分现代服务业营业税改征增值税试点的通知), issued by State Administration of Taxation ("SAT") and Ministry of Finance ("MOF")

SAT and MOF issued a notification on converting from business tax ("BT") to value added tax ("VAT") (Caishui [2011] 110) on November 16, and on the same day both regulatory bodies issued Caishui [2011] No.111, which provides more details on how taxpayers in Shanghai can change from BT to VAT.

#### Taxpayers

Companies and individuals providing transport services and parts of modern services ("Services") within the territory of China ("China") are VAT taxpayers.

For companies and individuals located outside China ("Overseas Companies") providing Services within China, their agents will withhold the VAT, and the service recipients will do so if there is no agent.

#### Taxable services

Taxable services include transport services by land (excluding railway transport), water, air and pipeline, research and development and technical services, information technology services, creative cultural services, logistics and ancillary services, leasing services of moveable and tangible assets, and attestation advisory services.

Appendix I of No. 111 provides more details on taxable services.

To provide Services within China, the service provider or the service recipient must be in China.

The following factors are not relevant when providing Services in China:

- Overseas companies providing services to Chinese companies or individuals outside China.
- Overseas companies leasing assets located outside China for the use of Chinese companies or individuals.
- Other conditions stipulated by SAT and MOF.

#### Tax rates

Taxpayers whose annual service income is at least RMB 5 million must apply for VAT general taxpayer status with the responsible tax office. Taxpayers whose annual service income is lower than RMB 5 million are small-scale taxpayers.

Four different tax rates apply to VAT general taxpayers:

- 17% for leasing of assets.
- 11% for transport services.
- 6% for other modern service industries other than leasing of assets.
- 0% for the taxable services established by SAT and MOF.

The tax rate for small-scale VAT payers is 3%.

#### Calculating tax

For VAT general taxpayers, the VAT payable is calculated by subtracting the input VAT from the output VAT on the Services. The input VAT includes the VAT paid when purchasing goods or accepting processing or repairing services or Services.

Input VAT that cannot be credited includes that for receiving passenger transport services, transport services for goods purchased, work-in-process, and finished goods that are in abnormal loss situation.

For small-scale taxpayers, the VAT payable is the income of Service \* tax collection rate with no VAT input can be credited.

#### Transitional rules

For current BT taxpayers that may change to VAT taxpayers and still enjoy some BT incentives, Appendix III of Circular 111 introduces a VAT exemption or VAT collection with an immediate refund mechanism to maintain these BT incentives.

Items exempt from VAT include copyright transfers made by individuals; services provided by people with disabilities; pesticide-sowing services provided by airplane companies; technology transfers, development and related technology consulting and technical services provided by taxpayers in the pilot area; services provided by qualified energy-saving companies in energy-management projects; qualified offshore outsourcing services provided by companies established in Shanghai between January 1, 2012, and December 31, 2013; and companies employing relatives of soldiers and the unemployed.

VAT collection with an immediate refund mechanism includes authorized finance leasing companies in the pilot area, domestic cargo transport services, warehousing services, and loading services.

*The Circular was issued on November 16, 2011, and will be effective on January 1, 2012.*

### **China signs letter of intent to join Convention on Mutual Administrative Assistance in Tax Matters**

On November 3, 2011, members of the Group of Twenty (G20) signed the letter of intent with the Organization for Economic Cooperation and Development (OECD) to join the Convention on Mutual Administrative Assistance in Tax Matters. China's Minister of Finance, Xie Xuren, signed the letter of intent on behalf of the Chinese government.

The Convention on Mutual Administrative Assistance in Tax Matters offers a wide range of tools for crossborder tax cooperation. It includes automatic exchange of information, multilateral simultaneous tax examinations, and international assistance when collecting tax due. It also imposes safeguards to protect the confidentiality of the information exchanged. The protocol will bring the existing treaty into conformity with current international standards on the exchange of information for tax purposes between national tax authorities.