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Adam Bobrow
Jin Ma
Adria Warren

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China

ADAM BOBROW, JIN MA, AND ADRIA WARREN*

I. Introduction

In 2009, China's law making system paused to take a breath after several years during which major legal changes dominated the scene. While by no means quiet, the period covered by this article has no mentions of developments matching the introduction of a property law in a country that did not recognize private property thirty years ago or an anti-monopoly law where the state maintained a monopoly on the means of production within the same time frame. Adjusting to the sea change that occurred over the last three decades will require many years of adaptive legal changes, such as those discussed in this article.

This article covers developments in Chinese legislative, regulatory, advisory, and financial laws between December 1, 2008 and November 30, 2009. This article summarizes the third amendment to China's Patent Law, which was passed and became effective within this period. It is a major amendment to the intellectual property regime. Developments in the anti-monopoly realm remain critical to lawyers interested in the development of China's legal regime. This article examines developments related to the merger review at China's Ministry of Commerce Anti-Monopoly Bureau, and focuses on the one case where the Ministry denied Coca-Cola's proposed acquisition. The financial scene in China saw the creation of a new Growth Emergence Market at the Shenzhen Stock Exchange. Finally, the Supreme People's Court's efforts to bolster court-connected mediation are also examined.

II. The Third Amendment to the Patent Law

The Patent Law of the People's Republic of China (Patent Law) was promulgated on March 12, 1984, and became effective April 1, 1985. The National People's Congress

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* Adam Bobrow is the Co-Chair of the China Committee and Committee Editor, drafted the article's introduction, the Patent Law, and merger developments sections and edited the article. Jin Ma is an attorney practicing in Beijing, China and drafted the growth emergence market section. Adria Warren is Senior Counsel in the Boston Office of Foley & Lardner LLP and drafted the court mediation section.


The NPCSC considered wide-ranging amendments to the Patent Law over a three-year drafting process. In the end, however, the Post-Amendment Patent Law differs from the 2000 version in only a few substantive ways. The NPCSC did not make structural changes to the existing Patent Law, leaving the basic system for administering the patenting system in place. Rather than write a new law, the text of the law was modified. The NPCSC also declined to unify the review of invalidation cases by administrative and infringement cases by civil tribunals, leaving in place existing systems of separate review. Patent Re-examination and Adjudication Board invalidation decisions accordingly will continue to face long and multi-layered judicial review procedures. Domestic industries had previously sought new proscriptions on the “abusive use of patents,” but the NPCSC took a milder approach, permitting compulsory licensing to cure monopolization. The language on abusive use of intellectual property rights (IPR) already exists in the Anti-monopoly Law.

A. Changes Patenting Requirements

The Post-Amendment Patent Law adopts the absolute novelty standard for patentability. The previous version of the law recognized prior art in the form of publication outside of China, but required the inventor to demonstrate novelty of use only within


5. See id. The decision by the NPCSC listed thirty-six specific changes (although it omitted from the list articles that were only renumbered because of the introduction of new articles), which is not a tremendous number of changes in an area of law that is constantly changing. Quan guo ren min dai biao da hui chang wu wei yuan hui guan yu xiu gai "zhong hua ren min gong he guo zhuan li fa" de jue ding [Decision of the Standing Comm. Nat'l People's Cong. on Amending the Patent Law] (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 27, 2008, effective Oct. 1, 2009) (P.R.C.), available at http://www.npc.gov.cn/huiyi/fzzx/zxzcw/2009-02/05/content_1517164.htm [hereinafter Decision].

6. E.g., Amended Patent Law, art. 76. The text remains unchanged from the original version of the law, adopted in 1984: "This Law shall enter into force on April 1, 1985." Id.

7. Id. art. 48. This will require a finding of monopolization by the relevant anti-monopoly authorities first.

China. This change will likely be welcomed as a step forward and, in fact, exceeds any requirement of international intellectual property rights treaty to which China is a party.

B. NEW CONDITIONS ON COMPULSORY LICENSES

The ability of the State Intellectual Property Office (SIPO), China's patent office, to issue compulsory licenses for patents was sharply curtailed in this amendment. The conditions under which SIPO will be permitted to issue a compulsory license were specified and limited to two: (1) where no exploitation has occurred for some time after application or issuance of the patent, or (2) where such licensing can combat monopolization by a patentee. An additional provision permits compulsory licensing in public health emergencies, allowing such licensing for export of medicines where authorized by international agreement. In other cases, the amendment also makes explicit that compulsory licensing for lack of exploitation shall supply only the domestic market.

The terms under which SIPO might authorize compulsory licensing and the terms of such a license were also limited and clarified. The law places a new evidentiary burden on an applicant for a compulsory license, requiring that the failed negotiations involved both reasonable terms and a reasonable timeframe. When SIPO grants a compulsory license, it shall also award a royalty to the patentee that is consistent with a subsequent agreement between the patentee and the licensee or on terms that fulfill the requirements of any international agreements on the subject to which China has acceded. The Post-Amendment Patent Law also retained a provision that permits compulsory licensing of patents owned by state-owned enterprises or public institutions.

This approach to compulsory licensing represents a step toward greater clarity but does not go as far as some international commentators sought. In their comments to SIPO on an earlier draft of the amendments, the ABA Sections on Intellectual Property Law, International Law, and Science & Technology Law suggested that provisions that authorize a process for issuing compulsory licenses be removed, and warned against domestic market sales of pharmaceuticals manufactured under a compulsory license for an international emergency.

C. PROTECTION FOR GENETIC RESOURCES

The amendments addressed the patentability of genetic resources. Applications for a patent that incorporates genetic resources must specifically disclose where the genetic re-

9. Publication anywhere was sufficient to defeat novelty, but only public use in China. See Amended Patent Law, art. 22, ¶ 2; see also Post-Amendment Patent Law, art. 22, ¶ 1.
11. Id. art. 50.
12. Id. art. 53.
13. Id. art. 54.
14. Id. art. 57.
15. Id. art. 14.
sources came from and to whom they belong. If such a disclosure is not possible, the application must state the reasons why disclosure is impossible. This limitation on patentability of an invention based on genetic resources does not provide any particular guidance to a potential patentee. It only provides that a patent shall not be granted where the utilization of such genetic resources violates a law or regulation. Unfortunately, this gives no insight into what applications SIPO might have to deny as a limitation on patentability, such as inventions that violate the law, social mores, or are detrimental to the public interest. With the eventual adoption of implementing regulations, SIPO may provide additional guidance to potential applicants regarding the types of genetic resources on which they should not rely.

D. ADAPTING A RESEARCH EXCEPTION

The amendment introduced a research exception for pharmaceutical companies to conduct research and trials to generate data for regulatory approval of medicines and medical devices protected by patents close to expiration. This change introduces an exception that has become the norm in most of the developed world as a means of encouraging the safe production of generic medications as soon as possible after the expiration of the patent underlying the brand-name product. Under the Post-Amendment Patent Law, manufacturing, use, and importation of drugs and medical appliances used solely to apply for regulatory approval are deemed not an act of infringement.

E. EQUALIZING TREATMENT BETWEEN CHINESE AND FOREIGN APPLICANTS AND PATENTEES

The Post-Amendment Patent Law has also narrowed some of the remaining gaps between the treatment of foreign and domestic applicants and patentees. The requirement that a Chinese patentee seek government review when assigning the patent to a foreigner has been eliminated. The 2000 Patent Law also required foreign patent applicants with-
out a fixed address or business operations in China to use a patent agent selected by SIPO to make the application on behalf of the foreign applicant. This requirement was relaxed so that a foreign applicant can now use any SIPO-authorized patent agent. A foreign applicant is still prohibited from selecting any individual to act as its patent agent or choosing to act pro se.

A potential Chinese applicant is no longer proscribed from seeking a patent in another jurisdiction before seeking a Chinese patent, although secrecy concerns are still addressed through a SIPO review. Under the previous law, a Chinese applicant would lose the right to apply for a Chinese patent if the same invention was the subject of a patent application outside China first. The current version relaxes that requirement but still requires the Chinese applicant to submit a report on the invention to SIPO for secrecy review. The law also makes it explicit that if such a report is not filed, the Chinese applicant cannot receive a Chinese patent. The Draft Implementing Regulations require either a report providing a detailed explanation of the art or a copy of the patent application itself before submission to a foreign patent office. Those regulations clarify that the reason for such review is to determine whether there is secret material in the application that should not be permitted outside China and commits such secrecy review to be completed in five months at most.

F. RIGHTS OF JOINT PATENTEES CLARIFIED

Filling in a blank that existed in the previous versions of the law, the Post-Amendment Patent Law prescribes the rights of all patentees where more than one person or entity files the application. The default position in the absence of an agreement among the patentees is that all patentees will have rights to exploit and license the patent. Royalties from any such licensing will be split evenly among the patentees. If the joint patentees have made an agreement, however, that agreement will control the division of rights and benefits from the patent.

G. MINOR CHANGES IN SYSTEMS FOR RESOLVING PATENT DISPUTES

In disputes, the Post-Amendment Patent Law maintains the existing rule that the Board of Patent Appeals and Interferences has the sole power to invalidate a patent on petition.
As a result, the alleged infringer cannot seek to invalidate the patent in the People's Court as part of infringement litigation. The Post-Amendment Law adds a provision that permits the alleged infringer to assert an affirmative defense on the basis that its exploitation of the art is part of prior art. This remaining split between determinations concerning validity and those related to infringement presumably is tied to concerns about the capacity of the People's Courts to sufficiently handle an analysis of a patent's validity. The expansion of a prior art defense, however, requires the People's Courts to address the underlying validity issues in the same venue with the assertions of infringement. This undermines the argument for maintaining the division between infringement and validity adjudication.

A variety of additional changes to the administration of patent-related disputes are contained in the Post-Amendment Patent Law. The provision for temporary, compulsory measures (similar to a petition for a preliminary injunction) has been expanded to include specific procedural requirements and force the patentee seeking such measures to post a bond. A perennial problem with litigation in Chinese courts is the lack of clear rules for discovery and the preservation of evidence. The Post-Amendment Patent Law grants the People's Court specific powers to preserve evidence on application of the patentee.

The measure of damages for infringement has also been clarified in the amendments. People's Courts will continue to use the actual damages suffered by the patentee as a primary measure, the gains from infringement as a secondary measure, and, in the absence of the first or second calculation, a multiple, between one and three times of a reasonable royalty, based on the royalty rate found in a licensing contract. Where none of those measures can be calculated, the Post-Amendment Patent Law for the first time codifies a statutory damage amount between 10,000 and 1 million RMB. The patentee...
may also recover the costs of stopping the infringement, including attorneys' fees. Commentators consider these statutory damages to be quite low, given that it is merely double what the SPC adopted in 2001 and is significantly lower than what a patent infringement judgment might be in many other jurisdictions.

H. CHANGES CONSIDERED BUT NOT ENACTED

The Post-Amendment Patent Law is also noteworthy for what it lacks. The drafters made no particular effort to match the substantive commitments of the World Intellectual Property Organization's Patent Law Treaty that seeks to offer uniform standards for substantive areas of patent law throughout the world. Not only was the bifurcated system of review for validity and infringement maintained, but the NPCSC ultimately offered no comprehensive modification of the judicial system aimed at patent or intellectual property infringement, such as the creation of a national intellectual property appellate court. Liability for indirect infringement (inducement, contribution, and sale or service of patented machines) is another important concept that the Post-Amendment Patent Law does not address. One final area that had concerned commentators was the possibility that the law would limit patentability or mandate compulsory licensing when a patented technology formed the basis of a Chinese mandatory national standard. The law is silent on this matter.

I. IMPLEMENTING MEASURES

On September 27 and 29, 2009, SIPO and the SPC, issued three limited measures to implement the revisions of the Patent Law that would come into force on October 1, 2009. The SPC issued a regulation clarifying that the revised law would apply to conduct that resulted in litigation that took place after October 1, 2009, when the new law was implemented. For cases where the conduct complained of took place completely after that date, the Post-Amendment version applies. And for cases where the conduct occurred before October 1, 2009, but is discovered only after that date, responsibility for infringement will be apportioned based on when it occurred, however the court will calculate compensation according to the Post-Amendment Patent Law.

Zhipei explains on his personal website that the figures in that Regulation came out of discussions in 1998 at a judicial conference on dealing with copyright disputes and were adopted by the SPC in 2001 for situations in which no adequate measure of damages could be found. The NPCSC seems to have simply doubled the potential damage amount here and adopted it in the text of the law.

44. Post-Amendment Patent Law, art. 65, ¶ 1.
45. Joint Patent Submission supra note 16, at 65 (asserting that an upper limit for statutory damages of 400 million RMB would provide more incentive for infringers to preserve evidence related to damages so as to avoid facing statutory damage awards in the higher range of possibility).
46. For a more complete discussion of the areas where the ABA advocated treatment of different subjects in the Post-Amendment Patent Law, see id. at 72-84.
48. Id. ¶¶ 2-3.
Intriguingly, the SPC also permits lower courts to determine when its own previous regulations on compulsory measures and governance of the Patent Law will still apply. Courts are given the general injunction not to apply two existing SPC measures when they are inconsistent with the Post-Amendment Patent Law. The SPC does not, however, invalidate those measures.49

In its measures, SIPO also recognizes the need for the more detailed implementing measures that it will release in the near future. In its Circular, SIPO merely provides some clarification to SIPO offices on how it should respond to inquiries and handle pro forma requirements (such as filling out forms) regarding applications in a variety of circumstances.50 In the Measures, SIPO acknowledges that the changes in the law on the calculation of registration date will require additional clarification but, in the interim, seeks to provide a framework for the new calculation.51

SIPO also released its draft implementing regulations for comment, but the likely date of promulgation of the final regulations remains uncertain.52

III. Developments in Merger Review Under China's Anti-Monopoly Law

Since the Anti-monopoly Law came into effect on August 1, 2008, China's Ministry of Commerce Anti-Monopoly Bureau (MOFCOM) reviewed a significant number of merger applications. Applications came in many of the possible varieties contemplated under the law, including several concentrations involving two Chinese entities, the contemplated take-over of a Chinese entity with mostly Chinese sales by a multinational company with global sales,53 and the merger of two large multinational companies, each with only a part of its operations in China.54 In most cases, the review has resulted in an approval of the merger but in a small number of cases, however, MOFCOM has only approved the concentration with conditions and, in one case, prohibited the transaction.55

49. Id. ¶¶ 4-5.


52. Draft Implementing Regulations, supra note 20.


55. On July 21, 2009, MOFCOM released statistics on its merger review work from August 2008 when the Anti-monopoly Law took effect through the end of June 2009. In that time, MOCFOM received fifty-eight merger filings and had adjudicated forty-six of them. Of those adjudicated, two were approved with conditions and one was rejected. Jing ying zhe ji zong fan long dun shen cha an jian zui xin tong qi qing quang [The Most Recent Statistics on Anti-Monopoly Review of Consolidation of Undertakings] (promulgated by the Ministry of Commerce Anti-Monopoly Bureau July 21, 2009) (P.R.C.), available at http://fldj.mofcom.gov.cn/aarticle/zcfb/200907/20090706409831.html. No comprehensive statistics has been re-
A. NEW MEASURES TO IMPLEMENT THE ANTI-MONOPOLY LAW

The State Council and MOFCOM have issued measures governing the substantive and procedural rules for merger review. Immediately after the Anti-monopoly Law came into effect, the State Council issued a regulation governing the thresholds for reporting a transaction that would result in concentration based on the turnover of the combining entities.66 These Threshold Regulations were augmented by a MOFCOM measure explaining how undertakings should calculate the turnover to determine whether the resulting undertaking would require review by MOFCOM,67 as well as a specific measure dealing with turnover calculations in the financial industry, issued in conjunction with several other Chinese government agencies.58 MOFCOM has also issued measures governing the review process, including details on submissions to MOFCOM by the parties (everything must be in writing) and the conduct of any hearing by MOFCOM, should one prove necessary.59 In one final confusing development, MOFCOM also revised the measure it used from 2005 to review mergers, mostly seeking to make it consistent with current practice under the Anti-monopoly Law.60

B. COCA-COLA’S FAILED ATTEMPT TO PURCHASE HUIYUAN

The denial of Coca-Cola’s (Coke) petition for approval to acquire Chinese juice producer Huiyuan has attracted the most attention of all the merger review cases MOFCOM has decided. It was the first, and so far only, case in which MOFCOM prohibited the merger. It is also a case involving a large multinational corporation that sought to acquire a domestic operation. As such, the decision has been scrutinized for signs that MOFCOM treated Coke differently than it might have treated the merger of two domestic drink companies, resulting in a chilling effect on foreign investment.61

In rejecting Coke's bid to take over Chinese juice maker Huiyuan, MOFCOM identified competitive problems that could be caused by the merger. First, MOFCOM found that under articles 28 and 29 of the Anti-monopoly Law, the merger would suppress and restrict competition. Second, it could have a negative impact on the Chinese juice beverage market and the healthy development of the Chinese fruit juice industry. Finally, Coke had not provided enough evidence to demonstrate that the negative effect on competition in that market was offset by a positive effect or benefit to society. Although the decision refers to the analysis conducted by MOFCOM on a number of occasions, that analysis is not clear from the announcement of the decision.

IV. Introduction of a Growth Emergence Market in China

In the capital market, China officially launched its Growth Enterprise Market (GEM) in late 2009. A group of twenty-eight private companies offered and listed their stock for public trading in the GEM on October 30, 2009. The GEM, a submarket inside the Shenzhen Stock Exchange, provides direct access to the capital market for companies that have demonstrated strong market performance and growth potential, even though they do not meet the rigorous criteria for the main board. For foreign funds investing in China, the market provides a new exit avenue, a welcome development at a time when the traditional exit avenue was somewhat narrowed by MOFCOM's foreign merger review regulation.

A. Qualified Issuer for the GEM

Similar to other second board markets, notably the Hong Kong GEM and the London Alternative Investment Market, companies seeking public listing in the Chinese GEM are subject to a less rigorous set of rules compared with main board listing. Nonetheless, the China Securities Regulatory Commission (CSRC) included in its regulations bright line rules regarding a potential issuer’s ability to operate as an ongoing interest, growth potential, and size.

62. Coke Announcement, supra note 53, ¶ 4 (citing Coke’s dominant position in the carbonated soft drink market, the acquisition of two well-known brand names in the juice market, and competitive impact on domestic small and medium-sized juice enterprises).

63. Id. ¶ 6.

64. MOFCOM did provide some discussion of the analysis conducted in a question and answer transcript from a few days before the decision was released, published on their website the same day as the decision. Shang wu bu Yao Jian jiu ke kou ke le shou gou hui yuan fan long duan shen cha [Ministry of Commerce spokesperson Yao Jian Asked about the Anti-Monopoly Review of Coke's Purchase of Huiyuan, Ministry of Commerce, Mar. 18, 2009, available at http://antifraud.mofcom.gov.cn/swzf/fld/223836.shtml.


Only companies with an operation history longer than three years may apply for listing in the GEM. The growth potential criterion requires an applicant to demonstrate either that it was profitable in the immediately previous two years with an aggregate income of at least RMB$10 million (US$1.47 million) or that the applicant was profitable in the most recent year with income of at least RMB$5 million (US$0.74 million), RMB$50 million (US$7.4 million) in operating revenue, and recorded a growth rate of at least thirty percent in that year. A potential issuer must also be large enough, with a net asset worth at least RMB$20 million (US$2.94 million) and post-IPO aggregate par value of at least RMB$30 million (US$4.41 million), to qualify.

B. GEM as Exit Avenue for Foreign Investors

The GEM provides a long awaited and new exit avenue for private equity (PE) funds and other institutional investors. Among the first twenty-eight companies listed in the GEM, twenty-three of them received investment from PE investors, two of which are foreign funds. For foreign PE funds, this exit avenue is much needed. Chinese companies with investments from foreign PE funds traditionally construct a “red chip” legal structure under which the mainland business operations are controlled by an offshore special purpose vehicle (SPV). Control of the mainland operation can then be maintained through an offshore arrangement outside the purview of the Chinese government. MOFCOM’s Order No. 10 and other subsequent directives narrowed this traditional exit avenue in 2006.

Although a new exit avenue has been opened, hurdles remain for foreign PE investors seeking an exit strategy through the GEM. One of these hurdles is the mandatory lock-up period requirement. The Shenzhen Stock Exchange GEM Public Listing Rules imposes a three-year lock-in period for controlling shareholders and a one-year period for other initial shareholders.

V. Recent Developments Regarding Court-Connected Mediation

The application of voluntary and enforceable mediation (or conciliation) through the courts was first officially recognized in China’s 1991 Civil Procedure Law. But judicial
mediation remains an evolving practice in China. With China's vast legal system often overwhelmed and underfunded, Chinese courts are now increasingly indicating their commitment to normalizing alternative dispute mechanisms, in particular by expanding access to, and institutionalization of, court-connected mediation as a form of alternative dispute resolution. Certain provincial courts, such as the Langfang City Intermediate Court and the basic courts within its jurisdiction, are beginning to introduce formal pre-trial mediation systems.

Nevertheless, judicial mediation in practice continues to pose many challenges, including uncertain enforcement procedures and lack of impartiality, as the judge assigned to a case is often the mediator.

A. UPDATES TO THE LEGAL REGIME FOR COURT-CONNECTED MEDIATION

Recent pronouncements by the SPC have recognized these challenges and indicate a greater willingness to address them. The Third Five-Year Reform Outline for the People's Courts (2009-2013) issued by the SPC in March 2009, includes among the court's mandates assisting the relevant departments in their efforts to develop alternative dispute resolution mechanisms, expanding the scope of parties to be mediated, improving mediation mechanisms, and improving conflict handling mechanisms which link litigation and alternative dispute resolution.

The SPC has recently expanded on the specific topic of judicial mediation. On August 4, 2009, the SPC issued a guidance document to try and incorporate judicial mediation into the litigation process. Although the opinions are not binding on the lower Chinese courts, they provide important legal guidance and indicate new trends in the Chinese judicial system.

The opinions confirm the enforceability of mediation agreements and provide that the judge who conducts mediation before trial should not adjudicate that dispute at trial (unless the parties agree). To implement the SPC's guidance in this area, the opinions encourage lower people's courts to establish mediation rosters, develop regulations covering management and fees, and adopt a mediator code of ethics. The regulations and professional ethics provisions developed by lower-level and intermediate People's Courts are to be reported to the higher People's Courts for the record and those developed by the higher People's Courts shall be reported to the SPC.

75. "Judicial mediation" as practiced in China differs from U.S. mediation models because of its court focus, and is best thought of as comparable to American settlement conferences.


78. See id. ¶¶ 11-13.

79. Id. ¶ 16.

80. Id. ¶ 30.

81. Id.

VOL. 44, NO. 1
B. Enforceability of Mediation Agreements

The opinions specifically give mediated agreements, if made in accordance with law and signed or stamped by both parties, the status of civil contracts for purposes of enforcement. This specifically applies to administrative settlements, civil settlements, settlements reached through business, trade, or labor organizations, and rural land contracts.\(^8\)

To give a mediated agreement enforceable effect through the courts, parties are encouraged to apply to the relevant court to confirm a mediated settlement. The court will review the application under simplified procedures. A mediated settlement will not be confirmed if by doing so it would (1) violate the laws and mandatory provisions of administrative regulations, (2) infringe national interests or social public interest, or (3) infringe outside parties' legitimate rights and interests. Further, a mediated settlement will not be confirmed if the agreement is unclear, if the mediator had a stake in the case that was not disclosed to the parties, if the mediation organization or mediator compelled mediation or a mediated settlement, if his or her impartiality was compromised, or if there occurred another serious violation of ethical norms of conduct.\(^9\)

C. Impartiality

The opinions state that in principle, a judge who mediates a dispute before trial shall not be personally involved in litigating the same case unless agreed to by the parties.\(^8\) In addition, unless the parties agree, the People's Court may not allow a mediator who has been involved in mediating a dispute to subsequently act as a party agent on a same or related dispute.\(^8\) This is notable as it is the first public formal position statement addressing the role of the judge in pre-trial judicial mediation proceedings.

Under the opinions, courts may order the parties to engage in mediation, but if the parties refuse or if they do not reach an agreement in mediation then the court must adjudicate the case.\(^8\) In addition, the opinions direct that staff or personnel engaged in mediation for the court shall not disclose relevant information about the mediation process, testify, or enter into evidence at trial the negotiations, discussions, or any transcripts from the mediation. The court can make an exception where admissibility of such evidence is (1) otherwise clearly allowed by law, (2) necessary to protect national interests, social public interests, and outside parties' legitimate rights and interests, or (3) if the parties otherwise agree.\(^8\)

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82. Id. ¶¶ 6-11.
83. Id. ¶¶ 21-25.
84. Id. ¶ 16.
85. Id. ¶ 27.
86. Id. ¶ 14.
87. Id. ¶ 19.