Several Legal Issues Concerning Disputes over Service Invention Remuneration

Xu Zhuobin

In recent years, with the promotion of Chinese market environment, technology progress and talent quality, more and more transnational companies set up their R&D institutes in China, thereby bringing China into the process of global technological innovation. Transnational companies usually conduct global "centralized" management over intellectual property rights acquired through R&D, while there are provisions concerning reward and remuneration based on service invention in Chinese laws. Therefore there may be some conflicts that will cause litigations. Recently, the Shanghai Court concluded a final judgment on a dispute over service invention remuneration between a transnational company and its employee, involving such legal issues as how to determine the locality where an invention was completed, how to deal with the "centralized" intellectual property management mode, whether the contracted remuneration was legally effective, etc. This article will conduct analysis on those aforesaid issues based on the said case.

Case brief

In April 2003, Zhang was employed by 3M China. Subsequently, Zhang took part in the transnational R&D work with regard to LCD-TV related issues carried out by 3M Company in China. The relevant invention-creation was applied for patent by 3M Innovation Company in June 2006 and was patented in March 2010 with Zhang and three other foreign employees of 3M Company as inventors. In January 2006, 3M Company, 3M China and 3M Innovation Company entered into a "Contract Research Agreement", the main contents of which include: 1. 3M Innovation Company acquires new intellectual property rights from 3M Company and other members of Global 3M Company Family, and then licenses 3M Company, other members of the Global 3M Company Family and third parties to use the rights for license fees. 2. 3M Company may allow other members of Global 3M Company Family to take part in the process development. 3M China is willing to render the intellectual property rights acquired from R&D projects to 3M Company and 3M Innovation Company for proper consideration. 3M China has begun to draft relevant policies concerning rewards and remuneration based on service invention since January 2010, for the purpose of which 3M China has provided communication channels between employees and management team, in which

Zhang was also involved. The "3M China Service Invention Reward Plan" was formally implemented on 1 September 2010, which stated that the policy was involved with invention-creations made by employees of affiliated companies of 3M China within their employment period. The commission calculation formula is that annual sales × 0.01% × product coefficient × patent distribution coefficient × inventor distribution coefficient. In November 2011, 3M China paid 20,384.16 RMB to Zhang as service invention remuneration. In 2012, Zhang filed a lawsuit against 3M China, requesting 3M China and 3M Innovation Company to pay him the service invention remuneration of 4.4 million RMB in total. The defendant 3M China argued that it was not the patentee of the patent involved in the said case, and thereby it was not the subject of obligation to pay the service invention remuneration. The majority of the patent involved was completed abroad so that the Chinese laws should not be applied. The amount of remuneration shall be calculated in accordance with the "3M China Service Invention Remuneration Plan". The defendant, 3M Innovation Company argued that it had no employment relationship with Zhang, and thereby there was no ground for Zhang's claim that it should pay him the service invention remuneration. The Court of first instance held that the mainland China was one of the places the invention-creation was implemented and the said invention-creation was patented in China, and hence, Chinese laws should be applied. 3M China transferred the patent application rights with regard to the invention-creation to 3M Innovation Company, which finally was granted patent for invention in China, so Zhang was entitled to the service invention remuneration. As 3M China did not provide the relevant data based on which the remuneration was calculated, including annual sales, the amount it provided could not be accepted by the Court. Meanwhile, the calculation method claimed by Zhang was also groundless. Therefore, the court decided at its own discretion that the amount of the service invention remuneration was 200,000 RMB. After the first trial, both Zhang and 3M China were dissatisfied with the judgment and lodged the appeal proceedings. The Court of the second instance sustained the trial judgment. [1]

Determination of the locality where the invention is completed

In the said Case, 3M China thought that the substantial portion and the inventive point of the invention in suit were not contributed to by Zhang; instead, they were completed by other inventors in the United States. Hence, the place where the invention in suit was completed was the United States, which should therefore exclude the application of the Chinese Patent Law. However, Zhang believed that the service inventor's right to remuneration was based on the granting of patent right for the service invention rather than the completion of the invention-creation. The law of the jurisdiction where the invention was granted should be applied, i.e. the Chinese law in this case. Moreover, part of the invention in suit was completed within the territory of China, making China one of the places where the invention in suit was completed. Therefore, Chinese laws should be applied in the said case and Chinese courts had the jurisdiction. It was recorded in the patent certificate that Zhang was one of the inventors. When the invention was applied for patent in the United States, Zhang, as one of the inventors, signed the declaration of "Assignment of Application", and 3M China paid him the service invention remuneration for the year of 2010. All the facts mentioned above indicated that both 3M China and 3M Company recognized Zhang as one of the inventors of the invention in suit. Whether the Chinese laws shall be applied is one of the issues in dispute in the said case.

First is how to apply the laws with regard to disputes concerning service invention remuneration. The issue of application of law only exists in foreign-related civil disputes; otherwise, Chinese laws shall be applied. By making reference to the Law on Choice of Law for Foreign-related Civil Relationships[2], the laws of the locality where protection is claimed shall be applyed to issues concerning the ownership and contents of the intellectual property, and the infringement liability for intellectual property. However, the dispute concerning service invention remuneration does not fall into such category. Such a dispute, in essence, is a contract dispute, to which laws of the habitual residence of one party whose duty of performance can best embody the characteristics of the contract or other laws which are most closely related to the contract shall be applied. In view of the fact that both the employer and the employee are within the territory of China, the Chinese laws are certainly the most closely related laws to the relevant contract. The laws of the working locality shall be applied to the labor contract. As to the agreement on the service invention remuneration, it, in fact, is part of the labor contract, and thereby the laws of the working locality of the labors are applicable. As can be seen, the

following laws might be applicable in disputes over service invention remuneration: the laws of the habitual residence of the contracting parties, the laws of the locality most closely related to the contract, or the laws of the working locality of the labors.

Theoretically, "sitz of legal relationship theory" and "the most significant relationship theory" are accurate methods to determine lex causae in the international private law field.[3] In accordance with "sitz of legal relationship theory", every legal relationship is logically and rationally in necessary link with some particular legal system.[4] The locality of the act should be deemed as the sitz of the act.[5] The locality of the occurrence of the invention act is the sitz for a dispute over service invention remuneration. Hence, it is fairly rational to determine the application of law based on the working locality of the inventor or the locality where the invention is completed. "The most significant relationship theory" is the most popular theory for application of law in the contemporary international private law field since it realizes the coordination between the certainty and the flexibility of the application of law[6]. In accordance with "the most significant relationship theory", the relevant connection factors of the legal relationships should be fully weighed, so as to find out the laws which have the most direct, the most essential and the most authentic connection with the legal relationship or the interested parties through qualitative and quantitative analysis for application.[7] The invention-creation *per se* is completed under legal circumstances of the completion locality of an invention which is meanwhile the working locality of the inventors, so the laws of the completion locality of the invention-creation are in closest association with the invention-creation, which is more convenient for the local court to make and implement a judgment. It is also more reasonable and operable. Using the laws of the locality where the invention-creation is completed is the fairest and the most reasonable way as the interests of all parties have been taken into account.

According to the Chinese Patent Law, an invention-creation, made by a person in execution of the tasks of the entity to which he belongs, or made by him mainly using the material and technology of the entity is a service invention-creation. The so-called "service invention-creation" exists due to the labor relationship between the inventor and the employer, irrespective of whether it is a formal labor relationship or a temporary one. The reason why a company gives remuneration to a service inventor is that the inventor has made technological contribution and therefore is entitled to appropriate labor remuneration. Based on their job duties, inventors have received their labor remuneration. The service invention remuneration is derived from the company's recognition over the relevant invention achievements, which have no necessary relationship with the efforts and input made in the process of its creation. The service invention remuneration plays a role in inspiring inventors' initiatives to further engage in inventions-creations.[8] Therefore, the service invention remuneration may be taken as some kind of incentive supplementary remuneration paid for the completion of the service invention. If the service invention-creation is not completed, the inventors certainly will not get the service invention remuneration. Whether an inventor is capable of attaining to the service invention remuneration crucially depends on whether the relevant service invention-creation has been completed. Therefore, as to the cases concerning service invention remuneration, the laws of the locality where the invention is completed should be applied. The relevant provisions concerning service invention reward and remuneration stipulated in the Chinese Patent Law and its Implementing Regulations shall be applied to those invention-creations completed within the territory of mainland China.

Second is how to determine the locality where an invention is completed. The subject matter of a patent is an entire technical solution, which is, however, composed of a number of inventive concepts. Cross-territory cooperation in an invention-creation is very common in the R&D of a transnational company. Hence, it is neither objective nor fair to take the place where the entire technical solution is completed as the sole locality where an invention is completed. The locality where the invention is completed does not mean that the entire technical solution and its various parts thereof should be completed in one place, and the place where part of the technical contribution is completed should also be deemed as one of the localities where an invention is completed.

In the said case, 3M Company and 3M China were affiliated companies. The invention-creation in suit was jointly completed by Zhang and the other three inventors of 3M Company. Zhang's qualification as inventor was recognized by 3M Company and 3M Innovation Company, which indicated that Zhang had made substantial technical contribution to the invention-creation in suit. During the process of invention-creation activity, Zhang has been working within the territory of China all the time. Meanwhile, the invention-creation in suit was applied for patent and finally patented in China. In view of those facts, China could certainly be deemed as one of

the localities where the invention-creation was completed. Thus, Chinese laws shall be applied to the lawsuit lodged by Zhang concerning the service invention remuneration of the invention in suit. In fact, Chinese laws shall also be applied in the said case judging from the habitual residence of the contracting parties or the working locality of the service inventors.

How to deal with the "centralized" intellectual property management mode

The centralized management of intellectual property rights is a commonly seen mode in transnational companies, which will be beneficial for the promotion of the level of intellectual property implementation, management and protection. However, the "centralized" management mode is established based on agreement among affiliates of a transnational company, which cannot negate relevant rights the inventors are entitled to in light of laws. The service inventors are entitled to the service invention remuneration, which is exactly the right he is entitled to according to laws. Such a right shall not be impaired by agreements concluded with others. In the said case, there were some conflicts between the "centralized" management mode and the rights of the service inventors to remuneration. According to the Patent Law, the entity to which a patent is granted shall pay the inventor or designer a reasonable remuneration on the basis of the scope of popularization and application as well as the economic benefits yielded. Although the invention-creation in suit was completed by Zhang during his employment in 3M China, it was finally applied for patent by 3M Innovation Company and obtained the patent right thereafter. Judging from the literal interpretation of the relevant provisions of the Patent Law, the inventor shall not be entitled to the service invention remuneration since the company he served for did not attain the patent whereas the entity attaining the patent was not the one he served for. That led the service inventor to the embarrassment of "falling between two stools".

It is obvious that such literal and rigid interpretation and comprehension of the relevant provisions is unfair to the service inventors, which exactly demonstrates loopholes in the Patent Law. Meanwhile, the act of transferring an invention to a specialized intellectual property management company before applying for patent should be treated in an objective way. Viewing from the final results of patent application and grant, the previous act of transference in essence is an act of transference of right to apply for a patent; otherwise, there is no rational interpretation for such an internal transference and the grant of patent right. The finally granted patent right is virtually based on the previously right to apply for a patent. The invention in suit had been widely used in 3M Company's products, which brought about significant economic benefits. As long as there are loopholes in the laws, the court has the jurisdiction to rebuild the laws.[9] Under such circumstances, the court shall fill in the loopholes when applying laws, and by analogy, when applying the provisions in the Patent Law stipulating that the entity to which a patent is granted shall pay the inventor or designer a reasonable remuneration. In the said case, 3M Innovation Company applied for a patent on the invention in suit and finally obtained the patent right, based on the agreement concluded between 3M Company and its affiliated companies. Yet the service inventor's legitimate rights to remuneration should not be impaired by the internal agreement of a transnational company. Therefore, even if 3M China was not the patent owner of the invention in suit, it, as the employer of Zhang, was still obliged to pay him the service invention remuneration.

The legal effect of the agreement

The next issue is how to determine whether the agreement is valid or not. In the said case, the plaintiff and the defendant 3M China concluded the "Individual Employment Contract" on 21 April 2003, which stipulated that 3M China was allowed to establish incentive programs at its own discretion and the rewards would be issued on a regular basis according to the specific incentive program; the employees had been informed of the program and guaranteed that they would obey the relevant rules and regulations of 3M Company, etc. Seeing from the ascertained facts that Zhang was involved in drafting of the invention reward policies of 3M China, that 3M China set up "Dialogue with LOC" conference, and that Zhang had once sent emails to the management team of 3M China saying that he had taken part in the discussion of the inventor compensation rules, etc., 3M China consulted its employees during the process of drafting "3M China Service Invention Reward Plan", which belonged to the entity's rules for service invention remuneration as was stipulated in the Implementing Regulations of the Patent Law. It was expressly provided in the said "3M China Service Invention Reward Plan" that the scope of application of the

plan was "the service inventions made by employees of the affiliated companies of 3M China during their period of employment". The court held that 3M China Service Invention Reward Plan was, in essence, an agreement between 3M China and its employees on the calculation method for service invention remuneration. It was not illegal to reach an agreement on the method for calculating service invention remuneration prior to the release of the said Plan.

The essential issue of the service invention system is how to reduce the imparity between the inventor, as employee, and the entity, that is, how to alleviate the status inequality of the interested parties to the maximum extent, and realize the fair and reasonable distribution of the interests embodied in the service invention achievement by means of autonomy of will and equality-based consultation,[10] among which the autonomy of will should play a key role. Generally, a company will not make an agreement with some employees as to how to calculate the service invention remuneration, but will set forth such provisions in rules formulated by the company. The company is not entitled to legislative power. The so-called rules are virtually supplements to the employment contract, the effect of which is equal to that of the clauses in the employment contract, namely, having a contractually binding effect on the company and its employees. The binding effect of the rules is not decided by the company unilaterally. According to the Employment Contract Law, where an employer formulates, amends or decides rules or important events concerning the remuneration, working time, break, vacation, work safety and sanitation, insurance and welfare, training of employees, labor discipline, or management of production quota, which are directly related to the interests of the employees, such rules or important events shall be discussed at the meeting of employees' representatives or the general meeting of all employees, and the employer shall also put forward proposals and opinions to the employees and negotiate with the labor union or the employees' representatives on a equal basis to reach agreements on these rules or events. The issue of service invention remuneration just falls within the scope of the aforesaid provisions, which usually requires a negotiation between a company and its employees. Without such negotiation, no consensus can be reached on the issue of service invention remuneration, and thereby the so-called rules have no binding effect.

According to the ascertained facts in the said case, on the one hand, 3M China has negotiated with its employees, and on the other hand, the employees agreed that the company had its own discretion on establishing incentive remuneration programs judging from the clauses of the "Individual Employment Contract". Such an agreement is impartial in terms of the interests of the company and its employees. Why is that? Firstly, it is the duty of the employees engaged in R&D to carry out technological R&D. The company has paid them for their work and therefore the consideration of their R&D work has been at least partially realized. Secondly, although the company decides the incentive remuneration program at its discretion, it does not necessarily mean unreasonable rules will be formulated, because a company in a fiercely competitive market must have a reasonable salary system, or otherwise it will encounter the brain drain. In the judgment of the first instance, the court of first instance held that although the calculation formula in the "3M China Service Invention Reward Plan" with respect to service invention remuneration was based on the annual sales instead of the operating profit, there was still a great gap between the coefficient of 0.01% provided in the said "Plan" and that provided in Rule 78 of the Implementing Regulations of the Patent Law, namely, a percentage of not less than 2% shall be drawn from the operating profits as a result of the exploitation of the patent for the invention or utility model each year, which demonstrated that the plan was indeed unreasonable in some aspects. The writer opines that since the relevant calculation bases are different, there is no comparability between those coefficients.[11] The company and its employees shall reach an agreement on calculation and payment of the service invention remuneration. Just like the salaries of the employees, the market is at a position in deciding whether it is rational or not.

The contract law can be largely deemed as a trade law, which is a way to protect transactions. During the course of property transference and service performance, people certainly rely heavily on promises and agreements.[12] Once a consensus is reached, the agreement remains valid unless there are invalid grounds. Before releasing the rules regarding the service invention remuneration, once the company has negotiated with the employees to reach a consensus, it can be deemed that an agreement on such an issue is concluded between both parties. Thus the relevant rules should be deemed valid. Since the Patent Law has introduced the "contractual" mode embodying "autonomy of will", it makes the calculation of service invention remuneration an affair that can be decided freely by the company and its employees regardless of interventions from outside. The de jure stan-

dards can only be applied in the absence of contracts.

How to calculate the specific amount? A calculation method does not necessarily guarantee an accurate amount of remuneration calculated accordingly. In the said case, the "3M China Service Invention Reward Plan" could be applied to the invention in suit. Since there arose disputes over the calculation method of service invention remuneration between both parties, 3M China, as the payer of the remuneration, should have provided specific basis and process for the calculation thereof during the trial; however, it failed to provide the calculation process of the service invention remuneration of 20, 384.16 RMB paid to Zhang for the year of 2010. Nor were the data as the basis for the calculation, such as annual sales, product coefficient, patent distribution coefficient and inventor distribution coefficient, crystal clear. Therefore, it was difficult to verify the authenticity and legitimacy of the amount of the service invention remuneration provided by 3M China as well as whether such amount was fair and reasonable to Zhang. Zhang did not accept that figure, claiming that the profit rate of products made by implementing the invention in suit should be deemed as 50%, but he did not present any evidence with regard to the said profit rate. Therefore, Zhang's calculation method could not be accepted by the Court, either. In the said case, it is hard to identify the consideration 3M China attained by transferring the right to the invention in suit to 3M Innovation Company, the profits made by implementing the patent for the invention in suit and the license fees attained by the patentee, etc. In view that the claims made by both parties concerning the calculation of the service invention remuneration could not be supported, the court had to determine a specific amount concerning the service invention remuneration at its own discretion in consideration of the overall circumstances of the said case. The specific amount determined by the court was within the scope of judicial discretion. There are two noteworthy inspirations. Firstly, the company should justify the rationality of its amount of payment by fully demonstrating its calculation basis and process thereof, or otherwise, it is difficult for the court to verify its legitimacy since the court is not capable of determining whether or not such amount is in line with the provisions of the relevant rules related to service invention remuneration. Secondly, the calculation method proposed by the employee, or stipulated in de jure standards should also be supported by the calculation basis and process thereof, or otherwise it cannot be supported by the court either. For example, in the said case, if Zhang managed to provide corresponding legitimate evidence with regard to the profit rate to convince the court, such as the company's financial information, the average profit rate published by the trade association or recognized by the industry, it is likely that his claim is supported by the court.

Epilogue

The said case involves determination of the service invention remuneration, which provides some guiding significance to the China-based R&D institutes of transnational companies. Therefore, the case has gained some social concern. The transformation and upgrading of China's economy need to be driven by technological innovation. In order to attract numerous transnational companies to set up technological R&D institutes in China, to input R&D funds and to gain innovation achievements, it should be guaranteed in the first place that the innovation achievements shall be put under adequate and reasonable legal protection. Meanwhile the legitimate rights and interests and rational claims of innovative talents shall also be protected. Only in that way can a win-win situation with appearance of a large number of innovation talents and the burst of innovation achievements be created. When dealing with such case, the court should be prudent and follow the laws, demonstrating the judicial attitude towards the technological innovation activities carried out by entities: first is to respect the autonomy of will. Both service inventors and companies are free subjects in the market economy while the service invention conducts and the invention achievements are objects of commercial transaction. Hence, the contract enjoys a preferential effect. Second is to protect the legitimate rights. All the legitimate rights of the employees cannot be impaired by the agreements concluded among entities, that is, legitimate rights are prior to agreements. And third is to balance the interests between entities and service inventors. It is improper to simply invalidate the rules of an entity or to confirm that the amount of remuneration calculated by the entity is legitimate and valid. The service invention remuneration system is expected to encourage innovations. ■

The author: Judge of IP tribunal of the Shanghai Higher People's Court, Doctor Candidate of Department of Law of Graduate School of Chinese Academy of Social Sciences

[1] See the Shanghai Higher People's Court's Civil Judgment No.

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[2] Although the law was taken into effect on 1 April 2011, the legal relationships prior to its effective date can be determined in the spirit of this law in absence of explicit laws and regulations.

[3] See [Germany] Hans Dölle (2009, December). *Juristische Entdeckungen* (translated by Wang Zejian) in "Research on Civil Law Theory and Judicial Precedent" (Volume Four) (p.14). Peking University Publishing House.

[4] Jiang Rujiao and Wang Jiaoying (2003). The Value Pursue of the Methods of Choice of Law in International Private Law—and the Boom and Amendment of the Most Significant Relationship Theory. *Journal of Comparative Law, 3.*

[5] Han Depei (Editor-in-chief) (2003, July). *New Theory on International Private Law* (p.46). Wuhan University Publishing House.

[6] Ma Zhiqiang (2013). Analysis on Cause of Formation of Most Significant Relationship Theory. *Journal of Southwest Politics and Law University, 4.*

[7] See supra note 4.

[8] Xiao Bing (2012). Legislative Comparison and Reference of Japanese and German Service Invention Remuneration Systems. *Electronics Intellectual Property, 4.*

[9] [Germany] Karl Larenz (2003, July). *Methodenlehre der Rechtswissenschaft* (translated by Chen Ai'e) (p.46). The Commercial Press.

[10] See supra note 8.

[11] It is possible that the calculation method based on sales is more rational, because many factors will have influence on the profits. Even if the invention-creation has in fact brought up significant benefits, the accounts book of a company may be still in red. Liu Xiangmei and Liu Qunying (2006). International Comparison and Suggestion concerning Service Invention Remuneration Systems. *Intellectual Property, 2.*

[12] [England] Patrick Selim Atiyah (2002, April). *Introduction to Law of Contract (Version No. 5)* (translated by Zhao Xudong, etc.) (pp.3–5). Law Press China.