

Liability Issues Are Consideration In China Licensing

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Product quality liability and product liability are issues to consider when licensing with entities in China.

The quality of products is an issue receiving increasing attention in many nations. Quite a few countries, especially those of the industrialized and some of the industrializing, have enacted special laws or regulations governing the legal issues in that respect. In the world today, the governing laws in relation to the quality of products may generally be divided into two major categories.

One is called Product Quality Law, and the like. The other is termed Product Liability Law, and the similar. The former is generally known in the attachable Eastern Bloc, such as Romania and Poland, etc., while the latter usually seen in the so-called western countries, e.g., the United States, Japan and western European states. In terms of the governing of legal relations with regard to the quality of products, China may be regarded as belonging to the first category.

Historically, China may be regarded as the pioneer in the field of legal control of product quality. The earliest institution relating to the liability of the producers to their products could be retrospicued to some 2,000 years ago, which carried regulations banning the selling of shrewish and scoundrel carts not in conformity with required specifications. In the dynasties following Qin, which unified China by conquering other warring states, similar regulations governing product quality control were promulgated and enforced.

Since the founding of the People's Republic in 1949, the Chinese government has been attaching in-

creasing importance to the upgrading of product quality. However, not until February 21, 1993, did China have its first Product Quality Law. It became enforceable on September 1, 1995.

WITH PRODUCT QUALITY LAW

To have a special law governing product quality control was first moved in March 1986 at the First Plenary Session of the Seventh National People's Congress. After the motion was primarily accepted by the Legislative Body, there ensued a great debate with respect to what kind of law to be made to govern legal relations involved in quality control and product liability.

One school held that a Product Liability Law based on the experiences of western practice was sufficient. The other major opinion was that since market mechanisms was underdeveloped in this country and product quality was voluntarily guaranteed in an unfledged market economy, it was imperative that a Product Quality Law covering not only product liability but also the legal relations in terms of product quality control and liabilities therein be promulgated and enforced. Useful studies were carried on, and the latter opinion was adopted upon three major considerations:

1. It is essential that a unified market economy be established in China. As the initial stage of this economic mechanism, product quality is a vital factor to the interests of manufacturers that are regarded as basic elements of a market economy. To guarantee the upgrading of product quality in general and give a push to the competition by the Chinese producers with their foreign counterparts in world market, a strong law governing product quality control and

product liability is unavoidable.

2. To keep the market in order and give harsh sanctions to the producers spoiling the market with poor quality and fake products, a product quality law must be made and enforced.

3. With a Product Quality Law, consumers' interests and benefits can be well-protected, not only in case of product liability but also in terms of the violation by the producers of their quality obligations.

PRODUCT QUALITY OBLIGATIONS AND LIABILITIES

Under the PRC Product Quality Law, manufacturers and sellers are obliged to do or not to do something such as composing the product quality obligations of the manufacturers and sellers. If one of these obligations is violated, the violator is liable to administrative, civil, or even criminal sanctions. Producer's product quality obligations are concentrated on the following aspects:

1. Producers shall make their products up to such quality standards not being unreasonably hazardous to human life and properties, or being in conformity with state or industry standards, or with the explicitly indicated quality standards set forth by the producers, etc.

2. Producers shall label their products, unless sold unpacked, indicating quality properties, name of the product to be sold, the name and address of the producer, specifications, contents, expiry date, warning signs and statement, etc.

3. The package shall be up to the requirements, especially for poisons, hazardous or fragile products, and proper warning signs shall be given accordingly.

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4. Producers shall not display such prohibitive marks as not to make supervised products as banned by the government, not to put on the product false origin, certificate logs, etc., or to pass off the name and address of other producers, not to make false products or low-quality products, not to trade labels of poor quality products or brand name or quality products, etc.

Seller's product quality obligations include:

1. **Obligations in buying goods.** Sellers are obliged to inspect the quality of the goods to be bought in, including the logs, warning signs, required statements and indications, etc., and shall declare to take the goods not up to the legally required standards or conditions.

2. **Obligations after buying and before selling.** Sellers shall have the responsibility to take measures to keep good the quality of the goods to be sold, and shall be liable to product defects that are revealed after being bought by the sellers.

3. **Obligations in indications on goods.** The marks, signs or symbols on the products to be sold shall be in accordance with the stipulations in PRC Product Quality Law.

4. **Prohibitive marks for sellers.** Sellers shall not market deteriorated or expired goods, not to put on the goods false origin, certificate mark, logo, quality product symbol, etc., or name and address of other's, not to sell low quality or fake products as quality or genuine products.

In violation of these obligations, the producers or sellers shall be liable to the following three major punishments:

1. **Administrative.** — The government agency in-charge shall supervise market operation of producers and sellers. In case of failing to perform product quality obligations, the producer or seller shall be subject to such sanctions as:

- Be ordered to stop producing or selling.
- Confiscation of illegal products and gains.
- A fine of one to five times of illegal gains.
- Cancellation of business license.
- Be ordered to alterate business firms, etc.

2. **Civil.** — Where product quality obligations are breached, it shall be regarded as a tort. A tortfeasor may be sued for damages and other liabilities:

• Damages resulted from product liability.

• Replacing or getting back the goods not up to the stipulated standards.

• Obligor to repair the goods in defect.

3. **Criminal.** — Where the violation constitutes a crime, the violator shall be liable to criminal sanctions:

- Being kept in supervision under Public Security Office into term is from three months to two years.
- Servitude of 3 days to six months.
- Term imprisonment of six months up to several years.
- Severe punishment, fine, deprivation of political rights, and confiscation of private property.

What principle is to be taken for judging the violation of product quality obligations by the producer or seller? Under current Chinese law, the principle contains three fundamental aspects:

1. **Implied warranty.** — The statutory obligations in respect to the quality requirements. For instance, products must be up to certain safety or health standards, must possess certain basic property, etc. Any relevant party shall be obliged to make its products meet those compulsory requirements and standards.

2. **Express warranty.** — The quality indicators expressed in the form of stipulated product standards, contractual specifications, product descriptions, or samples, etc. by the producer or seller to guarantee the quality of the products or to be made or sold. In case the products fail to satisfy these expressed conditions, the maker or seller shall be liable for the failure.

3. **Inherent defects.** — The products are intrinsically hazardous to the safety of human life or property of their customers, and caused damage to any consuming party.

In terms of the former two aspects, the fact of damage is not necessary for proving liability, while in the third case, the fact of damage is a prerequisite of the

liability.

PRODUCT LIABILITY

Product liability is also known as defective product liability, meaning that when a product, with inherent defects causes personal injury or property damage, the producer or seller is liable for monetary compensation to the victim. There has been an argument with regard to the nature of product liability. Some people are of the opinion that product liability is a special sort of liability for tort. Some hold that product liability is not only a liability for tort, but also a contractual liability. There are others who think that product liability is neither tort liability nor contractual but a new form of legal liability. Going through the history of the development of product liability in most countries in the world, the general idea is on the side of the first view.

Product liability differs with general liability for tort in that:

1. The principle of negligence is adopted in traditional theory, its relation to the liability for tort, while strict liability principle, i.e. liability without fault, is taken for judging product liability.

2. With regard to general liability for tort, the injuring party can only be individual citizen or entity. However, either single citizen or entity, or plural individuals or entities, may be the injuring party or parties who are jointly and severally liable to the injured.

3. To get compensation under general liability for tort, the injured must prove the fact of injury, the illegality of the injuring act, the causality of the injury and the act, and the fault of the injuring party. For product liability, the injured only needs to prove that he or she has suffered life or property damage caused by the defective product manufactured or sold by the defendant.

There are four basic elements for product liability:

1. The product at issue contains an inherent quality defect or is intrinsically hazardous to its consumers. There are generally three types of defects, i.e. defect due to improper design, defect caused in

manufacturing, and defect in indication on product.

2. The quality defect existed at the time of the product's being sold.

3. The defective product caused injury or damage to a consumer or a third party.

4. The quality defect is the direct cause of the injury or damage.

Under Chinese law, product quality liability is different from product liability in the following aspects:

1. Different natures. Product liability is a unique kind of liability for tort while product quality liability is a kind of comprehensive legal liability, including not only civil liability but also administrative and criminal liability.

2. Different scopes of liability. In product liability, only civil sanctions are involved, whereas in product quality liability, contractual, administrative and even criminal liabilities may be undertaken by the violator.

3. Different subjects of liabilities. The subjects in product liability may only be the entities in the stream of product manufacturing and marketing. However, not only producing or selling entities but also such individuals as the employees of the producer or sellers may be liable for product quality violations.

4. Different starting points for liability. Product liability can only be borne upon the fact of damage caused by the defective product after being put into the commercial stream, while product quality liability may exist in any ring in the whole chain of production, transportation, warehousing, marketing, and even consumption.

PRINCIPLE OF LIABILITY ATTRIBUTION

In general practice, for judging civil liability, three principles are often adopted. They are the principle of liability for fault, the principle of liability without fault and the principle of fair liability attribution, which is, under Chinese law, a practice of liability sharing due to the fault of both parties in disparate product liability is a special

form of civil liability, only the former two principles are used for product liability attribution.

Different principles are applicable in different countries. Even in the same country, e.g. the United States, the two principles exist separately in states. And Ireland and the Netherlands are using the principle of liability for fault, whereas France, United Kingdom, Germany, Belgium, etc. are in favor of strict liability.

In accordance with the stipulation in PRC Product Quality Law, a combined principle of constructive liability and burden of proof shifting is taken to find whether the injuring party is in product liability, meaning, that if the injuring party can not prove he not being in fault with regard to the damage caused by the defective product, he is found in constructive liability. What the injured needs to do is no more than to prove the fact of damage resulting from product defect and the causality of the damage and the defect.

As stipulated in Article 29 of PRC Product Quality Law, the producer must state his non-fault by alleging he has never put the alleged injuring product into commercial stream, the alleged defect did not exist when the product was put into commercial stream, or scientific and technological means had not been developed to the extent that the inherent defect in the alleged injuring product could be detected when being put into the commercial stream.

In case of a seller, if he can not identify the producer or the supplier of the alleged defective product, he himself shall bear the responsibility of compensation.

LIABILITY-BEARING PARTIES

As stated in the PRC Product Quality Law, producers and sellers shall undertake product quality obligations. However, others may also be liable to quality undertakings. According to Article 32 of the General Principles of Civil Code in PRC, if a product defect is created in the course of transportation or storage, the party responsible for transportation or storage shall be

liable to the damage caused by the defective product.

Can a technology licensor be sued directly for the damage caused by a defective product made by utilizing the transferred technology? This is not a simple question of yes or no. It depends on the extent the licensor gets involved in the activities of production or marketing. If the dealing is a pure licensing without licensor's direct involvement in production or marketing, the licensor can hardly be sued for direct responsibility. Nevertheless, he may be liable in the breach of his contractual obligations in the guarantee of the performance of the licensed technology. When the licensor not only provides technology but also gets involved in the production and sale of products, e.g. setting up a joint venture with the licensee, the licensor may be held as part of the producer to bear product quality liability or product liability.

PRESCRIPTION

According to Article 33 of PRC Product Quality Law, the prescription in the claiming damages due to a defective product is two years from the time the injured party knows or should have known his legitimate rights and interests are harmed. However, the right to lodge a claim against product defect shall be lost 10 years after the relevant product was delivered to the initial user or consumer, i.e. the injured has no right to claim damages for the injury caused by a defective product if the damage happens 10 years after its first delivery, or if the damage appears within the said 10 years but the injured did not know of the infringement of his interests until the said 10 years lapse. That is to say, there are two fundamental conditions for claiming damages against product quality liability or product liability, i.e. (a) the damage caused by direct product results within 10 years after the said product was delivered to the first user or consumer; (b) the injured must lodge the claim within two years of the injury.

Dispute Resolution

In China, a product quality dispute may be resolved by different means, subject to the parties' choice, including:

1. Consultation. The disputing parties may negotiate a settlement between themselves with regard to the resolution of the dispute.

2. Mediation. *Ad hoc* mediation or institutional mediation may be chosen by the parties. Some associations for the protection of consumer's interests may be used as mediation institution. However, settlement made either by *ad hoc* or by institutional mediation is not enforceable.

3. Arbitration. If the quality dispute relates to a contract, the

disputing parties may submit the dispute to an economic or technical contract arbitration commission. In case of product quality liability, the dispute may be judged with a product quality arbitration commission approved by the state. The arbitral award is enforceable.

4. Litigation. Most of the product liability disputes can hardly be solved in the above three ways. Litigation may be resorted to solve the disputes.

CONCLUSION

In the framework of legal practice in China, there are two liabilities in relation to the quality of products, i.e. product quality liability and

product liability, which have some points in common, but they also differ in other ways. To invest in manufacturing in the country or to trade with Chinese entities, one must pay special attention to the production and sale of both capital goods and consumer goods. Although, according to the law, only producers or sellers may be liable to damage due to product defects, an investor, technology licensor may be interpreted as producer or seller to bear the liability. A producer or seller may not be liable to product liability upon damage by defective product, but may be liable to product quality liability due to its violations in product quality obligations.