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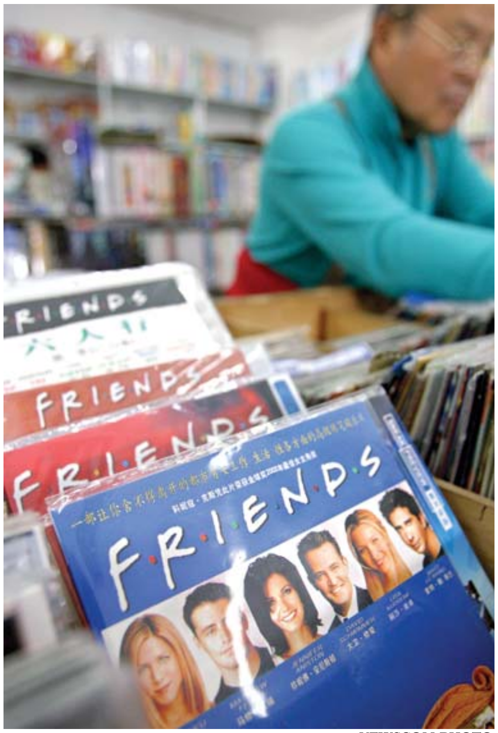
NOVEMBER 13, 2006



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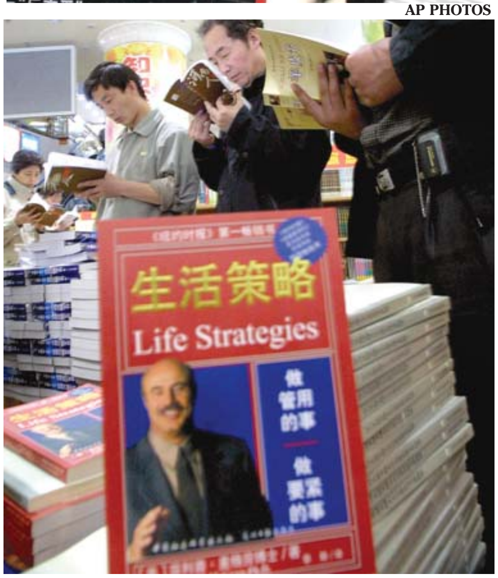

Navigating Media Rules in CHINA

Despite greater openness, companies still face restrictions.

BY ROBERT D. BALIN AND J.H. JERRY ZHU

ON SEPT. 10, China pro-mulgated new regulations that restrict the manner in which foreign news agencies may distribute their news and information in China. These regulations have been blasted by Western critics as yet another effort by the Chinese government to tighten its control over the dissemination of information to the Chinese people. At the very same time, China is being touted by Western media analysts as one of the top spots set to drive global media growth in the near future. With a population of 1.3 billion, a print and TV advertising market of $23.3 billion, the upcoming 2008 Olympics in Beijing and the 2010 World's Fair in Shanghai, China's media market has been described as "explosive." Media giants from the West cannot afford to ignore China. Yet the Chinese regulatory system is a minefield.

What exactly is going on in China? How does a Western media company, tempted by a market with 700 million radio listeners, more than a billion TV viewers and over 100 million receivers of cable TV, do business in China? What are the rules of the road? Perhaps, a little historical perspective may be helpful here.

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From Mao to Mickey

China has changed dramatically since the death of the Great Helmsman, Mao Zedong. There was a time some 30 years ago when the only books one could find in China's bookstores were the four volumes written by Mao himself and works by one or two Chinese authors he approved. Western literature, music and visual arts were viewed as tools of cultural infiltration, and clandestine Chinese consumers of decadent Western culture might well find themselves in trouble if caught.

Now, in places like Beijing and Shanghai, book lovers frequent what they call "Book Cities"—multi-floor emporiums that are two or three times larger than the biggest Barnes and Noble stores in the United States and that offer the latest bestsellers from around the world. Newsstands in the streets of China's cities are bulging with glitzy magazines boasting the trendiest fashions and the hottest movie stars. The Simpsons, SpongeBob SquarePants and Pokemon have all found a home on Chinese TV. Clearly, this isn't your grandfather's China, not even your father's China.

Yet, while China has become a vibrant society with a thriving capitalistic culture, and offers vast opportunities for savvy foreign media companies, there still remain many restrictions—on both domestic and foreign media—through which the government seeks to control the flow and content of information. The Cultural Revolution may be long gone. But the Party's belief that it can promote its goals through regulation of information survives. While ham-handed, direct censorship of Western content (particularly entertainment) may be on the wane, China's current regulatory system still typically requires that foreign content be funneled through domestic Chinese-owned entities—entities that are subject to self-censorship and answerable to the government for disseminating information that does not comply with China's content restrictions.

It is not realistic to expect that China will adopt our hands-off media law model any time in the near future. To successfully do business in China, foreign media companies must, thus, do the best they can in an imperfect and not always predictable legal regime: understand the applicable rules, know the limitations and restrictions and, above all, keep expectations at a reasonable level.

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Foreign Investment

Direct investment by foreign companies in China is strictly regulated. China's "Industry Guide for Foreign Direct Investment" divides specific industries into four categories: Prohibited, Restricted, Encouraged and Permitted.

"Prohibited" is self-explanatory, meaning that no direct foreign investment is allowed in Chinese industries listed in the Prohibited category, including, for example, mining, certain pharmaceutical products and operation of power networks.

Falling into the "Restricted" foreign investment category may encompass a number of different restrictions, such as that the foreign investment may only take the form of a Sino-foreign "joint venture"; that the foreign investor can only acquire a minority interest in the joint venture; that qualification criteria may be imposed on both the foreign and the local Chinese partners to the joint venture; that certain minimum investment amounts may be required of the foreign investor; and that the joint venture project may be subject to government approval at a higher-than-usual level. Examples of activities in which direct foreign investment is subject to Restricted category limitations include the development and operation of high-end hotels and office buildings, large-scale theme parks (think Mickey) and healthcare facilities.

On the other end of the scale, for industries that are listed in the "Encouraged" category, such as companies that manufacture auto engines, or electronic, telecommunications or other high-tech equipment, direct foreign investment is actively encouraged by the Chinese government, and foreign investors typically receive investment incentives such as tax breaks.

Last (and somewhat less helpfully for potential foreign investors seeking clarity), the Chinese regulations do not itemize those industries which fall within the "Permitted" foreign investment category, but instead merely state that the Permitted category covers those business sectors not listed in the Prohibited, Restricted or Encouraged categories. By default, many manufacturing industries end up in the Permitted category, meaning that direct foreign investment is typically allowed without foreign ownership restrictions (though government approval of the foreign investment is still required).

Media and Publishers

Under the Industry Guide, direct foreign investment in businesses that publish books, magazines or newspapers or that collect and disseminate news content falls into the Prohibited category. In other words, foreign publishers and news organizations are not allowed to directly publish their books, magazines or content in China through foreign ownership (no matter how small) in a Chinese company or a joint venture with local Chinese partners.

Falling into the Prohibited category does not mean, however, that the products of Western media companies cannot enter into the Chinese market through channels other than direct investment. Take books and magazines as an example. While foreign companies are not allowed to set up either a foreign-owned entity or a joint venture to directly publish their books and magazines in China, foreign publishers can still sell their wares in China through Chinese book and magazine importers who are authorized (and regulated) by appropriate Chinese government agencies. The function of these authorized importers is to review and approve the content of books and magazines to be imported—raising the obvious potential for censorship of controversial topics. Nonetheless, most of the non-Chinese language books displayed in bookstores all over China find their way onto the shelves through this channel.[1]

Similarly, through various arrangements with China's state-owned media companies, Western content providers are also exporting quite a number of movies and TV shows to the Chinese market. Viacom has brought Nickelodeon to China through China's official television network, CCTV. CNBC has introduced CNBC programs in Shanghai through yet another large Chinese media company, Shanghai Media Group.

Foreign publishers may also have Chinese-language editions of their journals and magazines published and distributed in China by entering into a "copyright cooperation arrangement" with an authorized local Chinese publisher. This arrangement requires that the foreign publisher enter into a written agreement under which (a) the foreign publisher licenses its trademark and the copyrighted content of its magazine to the Chinese publisher, and (b) the Chinese publisher publishes the licensed content in its own magazine using its own magazine name together with the foreign publisher's licensed trademark on the cover.

The relevant regulations and rules also impose a number of restrictions, which if overlooked by the foreign publisher can land them in trouble: The final product must be a magazine owned and published by the Chinese publisher, not the foreign licensor; the foreign publisher's licensed content must not exceed 50 percent of the whole content of the magazine; the foreign publisher's licensed trademark/logo must not be bigger than the Chinese name of the magazine; and, above all, the arrangement must receive approval from China's General Administration of Press and Publications before publication and distribution of the magazine.

To date, about 50 such licensing deals have been approved, mostly in connection with consumer, fashion and computer magazines. These arrangements have made Chinese-language editions of Western magazines widely available to, and popular with, readers in China. Hearst Corp., for example, has a licensing arrangement with Beijing-based Trends magazine under which Chinese-language editions of various U.S. consumer magazines, such as Cosmopolitan, Esquire, Good Housekeeping and Popular Mechanics, are sold in the Middle Kingdom.

Signs of increased receptivity to foreign media business may be seen in other areas as well. In November 2004, television, radio and film production was opened up to foreign direct investment, and now falls into the Restricted

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category. The restrictions imposed on such direct production investment include (a) that the investment can only take the form of a joint venture with local Chinese companies; (b) that a foreign media company is allowed to form only one joint venture for purposes of program production; (c) that the foreign equity interest in the joint venture cannot exceed 49 percent; (d) that the "Legal Representative" of the joint venture (i.e., the board chairman under Chinese law) must be a representative of the Chinese investors; and (e) that the joint venture is required to operate its business in compliance with stipulated guidelines.

With virtually every family in China now owning a TV set, and with an ever-growing number of movie theaters (2,396 screens as of 2004) as well, this opening up of the market to foreign investment (albeit restricted) has been hailed as a huge opportunity for Western media companies. News Corp., Viacom, Sony Pictures and Warner Brothers have all reportedly jumped in to take advantage of the opportunity by forming joint ventures with their respective Chinese partners.

Not So Fast

China is opening its door wider to foreign media content and investment, notably in the area of entertainment. Yet, issues of control still remain, as exemplified by the new Sept. 10 regulations (entitled "Measures for the Administration of Release of News and Information in China by Foreign News Agencies").

These new regulations restrict the manner in which foreign news agencies may distribute their news within China. Critics of the new regulations primarily focus their objections on Article 11, which sets forth a laundry list of content that foreign news agencies are prohibited from disseminating in China, including news or information that violates the basic principles enshrined in China's Constitution, undermines China's national security, reputation and interests, violates China's religious policies or preaches "evil cults or superstition," incites hatred and discrimination among ethnic groups, spreads false information, disrupts China's economic and social order, or undermines China's social stability.

This list of prohibited content is surely vague, incredibly overbroad and subject to arbitrary enforcement, but nothing new. Existing Chinese laws and regulations relating to content release and publication, including Internet publication, already contain lists of prohibited content in similar, if not exactly the same, language. What is new, as compared with the old 1996 rule on foreign news agencies, is the requirement that all foreign news agencies must now engage an authorized Chinese agent designated by Xinhua News Agency (the official Chinese Government news service) to distribute their news reports in China. The regulations expressly prohibit foreign news agencies from directly soliciting Chinese subscribers and further ban any Chinese company or individual, other than an entity designated by Xinhua, from distributing the news and information of foreign news agencies.

The building that houses the Shanghai Book City where books are sold on the first five to six floors.

Many commentators interpret this new requirement in financial terms, attributing it to Xinhua's desire to share the profits generated from news distribution by foreign news agencies in China. That may well be true, but the new rule is not just a revenue-generating scheme. It also places a large part of the responsibility for the content of foreign news reports on the shoulders of the Chinese agents that foreign news agencies are now required to hire, similar to the situation that currently exists with respect to foreign books and magazines, which can only be published and distributed in China through an authorized Chinese publisher or importer.

These Chinese news agents and publishers are subject to self-censorship. If they fail in their obligation to ensure that their foreign principals or licensors comply with China's content restrictions, their authorization to do business may be taken away by the government. The "new" rule relating to foreign news agencies is, thus, reflective of the censorship trend in modern China. It is a shift away from direct government censorship of foreign content, which tends to cause controversy and generate negative publicity, to a more subtle and indirect censorship through mandated contractual relationships with domestic companies subject to government oversight. And that, at least for the time being, is the regulatory framework and reality that foreign media companies must grapple with when seeking to do business in China.

Conclusion

Earlier this year, the authors and other lawyers from the firm were invited by the Cheung Kong Graduate School of Business and the Shantou University School of Journalism to lead a three-day seminar on comparative U.S./China media law in Beijing. Participants in the program included Chinese media executives, news reporters, publishers, film makers, advertising managers and other media professionals from China's major media companies, including, among others, CCTV, Xinhua News Agency, The People's Daily (China's official newspaper), Stellar MegaMedia (which produces and distributes films), China's National Geographic Channel, Trends magazine and Beijing Buena Vista (which works with Disney). In a stimulating exchange, we discussed various U.S. media law concepts, from First Amendment press protections to libel, privacy and copyright law, and compared those concepts to the laws regulating the media in China.

Real-life topics ranged from the famous Chinese film director who had threatened to bring copyright infringement claims over an amusing—and wildly popular—Internet parody of his film, "Steamed Buns" (which led us into the realm of fair use), to questions on whether a Chinese documentary that reported on physical abuse of children by their teachers might raise privacy or libel concerns—precisely the type of frank give and take we would expect in newsroom seminars with our American media clients. And, most of all, this cross-section of Chinese media professionals—who are or may someday be in positions of authority—expressed a genuine interest in broadening business relationships and opportunities with their U.S. media counterparts.

China's media laws and regulations, while in some areas, are still a work in progress in others. Yet, we came away from our experience in Beijing convinced that, while China's regulatory scheme requires careful navigation, business opportunities for foreign media companies in China will continue to grow.

1. In an interesting wrinkle, while the Chinese regulations prohibit foreign companies from investing in enterprises that publish in China, they now permit direct foreign investment in companies that merely distribute books, magazines and newspapers. In other words, foreign companies are allowed to directly invest in businesses engaged in the wholesale or retail distribution of books, magazines and newspapers within China. To date, 38 such foreign-invested distribution companies have been approved by the Chinese authorities. However, any books, magazines or newspapers that come from abroad must still first pass through an authorized Chinese importer, which, as noted above, serves as an entrance gate for review of foreign content.

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