



PRC Telecoms, Media & Technology Law Newsletter 23 January 2009

This TMT Newsletter contains the following articles:

- Baidu Embroiled in Search Ranking Scandal
- Regulations on News Gathering by Resident Foreign News Organizations and Foreign Journalists: Current Law and Recent Developments

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BAIDU EMBROILED IN SEARCH RANKING SCANDAL

Background

In mid-November 2008, a report shown on China Central Television (**CCTV**, the state television network) shook the Chinese Internet community, which is the largest in the world. The report claimed that Baidu.com, China's leading search engine, provided search results leading to fake clinics and illegal medicines. Specifically, when a CCTV reporter entered key words such as "treatment of sexually transmitted diseases" in Baidu's search engine, some of the search results on the first page led to fake clinics, and some of the medicines advertised on the top of the webpage had not undergone government inspection and approval.

Not surprisingly, the CCTV report generated a range of adverse reactions from the public. Baidu was accused by users of excessively intervening in its search results, thereby spreading inaccurate and misleading information. It was also alleged to intentionally be blocking certain websites. These problems were mainly attributed to Baidu's competitive search ranking system.

Issues

Under the competitive search ranking system, an advertiser pays a fee to a web site so that the company or its products receive better placement in the search results and advertisements that the site generates. In order to ensure optimal placement, advertisers enter into agreements to purchase key search terms related to their businesses.

As a result, Baidu's use of a competitive search ranking system in its search engine has greatly enhanced the sales volume of its advertisers' products and services. Advertising fees generated from this system thus account for nearly 80% of Baidu's profits. When viewed against the backdrop of these 2 direct consequences, it is not surprising that Baidu's system has been heavily criticized, as follows:

- In focusing on the amount of money it can generate from this system, Baidu is paying little attention to whether the products or services provided being advertised are genuine or legal, a viewpoint presented by the CCTV news report.
- Baidu does not segregate the search results generated by its competitive search ranking system from those generated based on the volume of ordinary web traffic. This confuses web users and affects the information delivered to them, as they are unable to tell which search results are derived from paid advertisements, and which are derived naturally, without intervention from Baidu.
- Some small and medium enterprises claim that Baidu intentionally blocks the websites of the competitors of its advertisers. They also allege that Baidu blocks the websites of former advertisers that have stopped paying fees to Baidu.
- Many web users have complained that the search results generated by Baidu's competitive search ranking system are skewed by artificial transactions, which in effect make the search results a form of active advertising published by the search engine. That is, the search results are ranked by Baidu according to which advertiser or cooperation partner has paid the most in fees.

Many interested parties have called for Baidu to be penalized as its practice is harming the interests of web users as well as of advertisers that are unwilling to pay for premier placement in its search results.

In response, Baidu has consistently denied any wrong-doing. It also continues to assert that no legal violation has taken place, because there is no law in China which regulates competitive search ranking systems.

TAL Commentary

From the perspective of advertising and anti-monopoly law, Baidu's search ranking system raises 2 important questions:

- Does Baidu's failure to review the qualifications of its advertisers and their products violate the PRC Advertising Law?
- Does Baidu's blocking of certain websites violate the PRC Anti-Monopoly Law?

Advertising Perspective

In recent years, lawsuits have frequently been instituted against search engine providers such as Baidu alleging violations of the Advertising Law. They generally relate to claims for damages arising from false information provided via search results. The key issues relate to:

- whether the search results from a competitive search ranking system constitute a form of advertisement; and
- whether the search engine operator should be responsible for reviewing advertisers' qualifications.

Search engine operators often argue that they are not advertising agents or publishers, and thus have neither the capacity nor the legal obligation to examine the qualifications of each advertiser. They also often submit that the search results are part of their services as a search engine provider, rather than an expression of the intent to provide advertisements. That is, merely providing links to websites in search results does not constitute an act of advertising, and therefore a search engine operator is not obligated to examine the authenticity of the content of such websites.

In 2007, Shanghai based Da Zhong Removals (大众搬场, **Dazhong**), found a link on the Baidu search engine to a forged website with the same information as its own site. This led to a marked decline in Dazhong's business, as potential clients were blocked or directed away from the legitimate company's site. Dazhong initiated an action against Baidu in the Shanghai Second Intermediate Court, claiming compensation of RMB 500,000. The court ruled in Dazhong's favor, but only required Baidu to publish a statement and to compensate Dazhong RMB 50,000 plus legal costs.

In this case, the Shanghai Second Intermediate Court found that, although the services provided by Baidu could not be considered as advertising per se, the site nonetheless had to assume responsibility for supervising the content of its search results. The court held that the key differentiating factor between competitive search ranking results and ordinary search results was that Baidu's results are influenced by advertising fees. As such, since Baidu charges its advertisers, the site should shoulder the corresponding responsibility to the public to ensure that their links are authentic and their advertisement contents accurate.

In contrast to the cautious attitude of the courts, many lawyers and legal commentators in China believe that search results generated from competitive search ranking systems should fall under the purview of the Advertising Law, since the results are in substance a form of "advertisement". Even if the search results do not fall under the Advertising Law, these commentators believe that they fall within the spirit of the legislation and should be regulated accordingly.

It will be interesting to see whether the Chinese courts will one day be willing to assume the task of regulating competitive search ranking systems as a form of advertisement, and hence impose a requirement on search engine operators to ensure that the advertisers' content is true and genuine. Certainly, the absence of any regulations on such search results is a cause of concern: it leads to the dissemination of false information and, by extension, causes harm to the public.

Anti-Monopoly Standpoint

In March 2008, a local site called Quan Min Pharmaceuticals (全民医药网, **Quanmin**) contracted with Baidu to purchase the 3rd-highest position for an advertisement within the search results generated from the key words "medicine investment". As a result, the daily click rate of Quanmin rose from less than 3,000 to approximately 8,000, and its business significantly increased. After it stopped paying fees under the agreement, however, Quanmin's website was blocked by Baidu, and the company's revenue declined steeply as a result.

In October 2008, Quanmin filed a complaint against Baidu with the State Administration for Industry and Commerce, alleging monopolistic practices. In the complaint, Quanmin claimed that Baidu is abusing its dominant position in the search engine market by (a)

charging high fees for advertisements in search engine results, and then (b) blocking the websites of its advertisers if they fail to renew their advertising contracts or to pay the fees to Baidu.

Pursuant to Article 19 of the Anti-Monopoly Law, one way a company can be deemed to occupy a dominant position in a particular market is if it holds 50% or more of the market share. Since Baidu controls nearly 67% of China's search engine market, it is clearly a dominant player.

This case is still pending. However, Baidu has stated in its response that, although it refused to accept advertising from certain websites, it did so only because they failed to provide a good experience for Baidu's web users. Baidu also emphasized that its search results have nothing to do with its business model: rather, it is user experience that determines the content of search results.

Followers of online advertising and the search engine business in the PRC await the outcome of this case with great interest. Baidu has also been the target of various other lawsuits: for example, it was sued in connection with its opaque click rate recording system, as well as with regard to the appropriateness of placing its competitive search ranking system at the centre of its business model. However, this is the first time that a search engine has been challenged under the Anti-Monopoly Law.

Conclusion

Specific laws and regulations regarding the operation of search engines and their competitive search ranking systems need to be urgently considered and issued in China, to pave the way for coherent government supervision of search engine activities. Strong, clear legal grounds will also make pursuing unethical and unlawful behavior by search engines much easier. In the meantime, however, users and advertisers remain undaunted, and are continuing to assert claims against Baidu and other search engines. Indeed, the latest anti-monopoly case illustrates how such plaintiffs are exploring all the legal means available to pursue those claims.

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REGULATIONS ON NEWS GATHERING BY RESIDENT FOREIGN NEWS ORGANIZATIONS AND FOREIGN JOURNALISTS: CURRENT LAW AND RECENT DEVELOPMENTS

Introduction

Between 1990 and shortly before last year's Olympics, the activities of foreign news organizations and journalists were governed by the *Regulations on the Administration of Foreign Journalists and Resident Foreign News Organizations (1990 Regulations)*. The Regulations set out the general conditions and procedures for the establishment and activities in China of foreign news bureaus, as well as for the activities of foreign journalists, but did so in a vague and rudimentary fashion.

In recognition of the heavy reporting generally associated with the Olympics, and the fact that the 1990 Regulations were inadequate in both scope and application, the State Council issued the *Regulations on Reporting Activities in China by Foreign Journalists during the*

Beijing Olympic Games and the Preparatory Period (Olympic Regulations). These were implemented between 1 January 2007 and 17 October 2008. They relaxed various major restrictions on journalism in China, including the conduct of interviews and the types of equipment that could be imported for use by foreign reporters.

After the Olympics, the government introduced, on 17 October 2008, the *Regulations on News Gathering by Resident Foreign News Organizations and Foreign Journalists in the People's Republic of China (2008 Regulations)*. These came into effect immediately, superseding and revoking the 1990 Regulations and the Olympic Regulations but inheriting the basic principles of the latter. The 2008 Regulations aim to:

- provide a more detailed and user-friendly regulatory framework for the administration of foreign news organizations and foreign journalists in China; and
- clarify the related responsibilities of the Chinese supervisory and approval authorities.

Key Amendments to the 1990 Regulations

1. Approval Applications

Under the 1990 Regulations, foreign news entities had to submit applications to set up a resident foreign news organization in China directly to the Ministry of Foreign Affairs (**MOFA**)'s Information Department in Beijing. The 2008 Regulations make it possible for applications to be submitted indirectly from overseas, through Chinese embassies or consulates.

2. Administrative Authorities

Nevertheless, the MOFA remains the principal authority in charge of the administration of resident foreign news organizations and foreign journalists. However, under the 2008 Regulations, local governments' foreign affairs departments are mandated to "process" the affairs of resident foreign news organizations and foreign journalists and their information office counterparts are entrusted with handling the "administration" of those affairs. The distinction between "processing" and "administration" is unclear.

Accordingly, most day-to-day issues are now handled at the local level, with the MOFA only involved in matters such as the establishment and closure of resident foreign news organizations and the assignment of foreign journalists.

3. General Administration

The 2008 Regulations have helped to clarify some of the administrative aspects of resident foreign news organizations and foreign journalists, most notably:

- the MOFA's approval is no longer required for minor changes to an established resident foreign news organization, which may be handled at the local government level;

- foreign news organizations to which no resident foreign journalist has been assigned for more than 10 consecutive months will be deemed to have terminated their operations, and their operating permits will be revoked automatically;
- the permits of foreign journalists who reside in China cumulatively for less than 6 months a year will be revoked; and
- resident foreign journalists must now apply for the renewal or extension of their permits when they expire, rather than undergoing annual registration procedures.

4. Interview and Equipment Import Requirements Relaxed

Under the 2008 Regulations, foreign journalists may interview Chinese organizations or individuals with their consent and without being accompanied by a local host organization. Moreover, with the requisite approvals, resident foreign news organizations and journalists are allowed to temporarily import, set up and use wireless communications equipment.

Practical Implementation

To date, the MOFA has published detailed procedural instructions relating to matters such as the establishment and dissolution of resident foreign news organizations and the issuance and revocation of Resident Foreign News Organization Permits and Resident Foreign Journalist Permits. Thus, it is easier for news organizations and journalists to function, and for the government to supervise them. However, it is important to note that the 2008 Regulations only address the administrative side of journalism in China; they do not discuss censorship, policies on sensitive topics or other aspects of the actual content of the stories being produced.

Conclusion

The changes brought about by the 2008 Regulations are aimed at encouraging and facilitating the general activities of foreign news organizations and foreign journalists in China. Without question, the 2008 Regulations provide a more practical and feasible framework for such entities to operate in China. In this regard, they reflect the Chinese government's oft-repeated undertaking to open up the media. Certainly, foreign journalists will appreciate the convenience of being able to interview organizations or individuals without having to obtain the prior approval of the authorities or being accompanied by a Chinese host organization.

It does not appear that the global financial crisis, and the pessimistic stories associated with it, has yet caused the government to think twice about its approach. However, as is always the case in China and particularly in this sensitive area, this could well change as circumstances, and political expediency, dictate.

It must also be remembered that, while the 2008 Regulations relax the regime applying to resident foreign news organizations and journalists, restrictions on contact between Chinese citizens and the foreign media remain firmly in place. It is these restrictions,

rather than the administrative regime, that are likely to prevent the true opening-up of the media in China.

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