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Win, Lose, or Draw? An Update on the World Trade Organization's Recent Ruling in U.S./China Intellectual Property Rights Dispute*

by Heidi L. Belongia**

On January 26, 2009, a panel (Panel) of the World Trade Organization (WTO) ruled that several aspects of China's legal system for protecting and enforcing intellectual property rights (IPR) were inconsistent with China's obligations under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). (A full report is available at http://www.wto.org/english/news_e/news09_e/362r_e.htm.) The dispute began in April 2007 after bilateral discussions between the United States and China broke down. The U.S. complaint focused on three key issues, namely (1) whether China denies copyright protection for categories of works based on content in violation of the Berne Convention (Berne) (as incorporated by TRIPS); (2) whether Chinese customs has full authority to destroy or dispose of infringing goods consistent with TRIPS; and (3) whether China's minimum thresholds for criminal prosecution violate TRIPS. The Panel reached a split decision, finding for the United States on the first issue, splitting the second issue, and finding that the United States failed to provide enough evidence to prevail on the third issue.

The Panel's findings are discussed below.

Copyright Law

The United States claimed that Article 4 of China's Copyright Law violates TRIPS and Berne because it denies copyright protection to certain categories of works that fail China's content review.

Article 4(1) of China's Copyright Law provides as follows: "Works the publication and/or dissemination of which are prohibited by law shall not be protected by this Law."

In finding for the United States, the Panel found that Article 4(1) denies copyright protection to works that fail China's content review in violation of China's obligations under TRIPS. Specifically, Article 4(1) denies copyright protection to works that (1) failed content review and (2) deleted portions of works edited to satisfy content review. Although the Panel recognized that "government has the right to control or prohibit the circulation, presentation, or exhibition of a work for public order," it is inconsistent with TRIPS to use censorship to deny copyright protection to an entire class of works. Accordingly, the Panel found that Article 4(1) of China's Copyright Law violates TRIPS and Berne.

Customs Measures

With respect to the second issue, the United States objected to three of China's customs measures governing disposal or destruction of counterfeit and/or infringing goods as inconsistent with TRIPS. The relevant TRIPS provision requires the following: "... competent authorities shall have the authority to order the destruction or disposal of infringing goods ..."

The Panel found that the United States failed to establish that China's customs measures are inconsistent with TRIPS.

ISSUE NO. 152
August 2009

IN THIS ISSUE:

Second Circuit Decision Reviving Lanham Act Trademark Infringement Suit Against Google's "Adwords" Program Leaves Important Issues Open1

Identity Theft: When The Only Fear Is Fear Itself5

PRO-IP Act Provides IP Rights Owners Enhanced Weapons for Combating Piracy and Counterfeiting.....9

Win, Lose, Or Draw? An Update On The World Trade Organization's Recent Ruling In U.S./China Intellectual Property Rights Dispute11

Supreme Court Grants Certiorari in *Bilski v. Doll*13

A General "Reservation of Rights" Clause Does Not Reserve "Have Made" Rights Under a Patent License15

UPDATES16

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The Panel noted that the phrase “shall have authority” does not mean that customs officials must exercise that authority or that destruction of infringing/counterfeit goods must be the exclusive remedy. China’s limits on customs authority were not inconsistent with TRIPS because disposal or destruction of the goods is an option under all scenarios—it was therefore acceptable for China to require customs to consider donation, sale, and auction prior to destruction.

However, the Panel agreed with the United States that “simple removal of the trademark” from infringing or counterfeit goods is not sufficient to permit auction and release of the goods back into the stream of commerce. This is especially true in the case of counterfeit goods where the goods are often altered to resemble closely the branded goods. Accordingly, the Panel found that China’s measures were inconsistent with TRIPS to the extent they allow release of infringing or counterfeit goods in commerce based on “simple removal” of the offending trademark or indicia.

Criminal Thresholds

In its third claim, the United States objected to certain thresholds required to trigger criminal prosecution of “willful trademark counterfeiting” and “copyright piracy.” Under TRIPS, China is obligated to provide criminal penalties for “willful trademark counterfeiting or copyright piracy on a commercial scale.”

The parties and the Panel focused on the meaning of the term “commercial scale.” The Panel found that “commercial scale” requires the counterfeiting or piracy to be carried on at the magnitude or extent of typical or usual commercial activity with respect to a given product in a particular market. This market-based approach to defining “commercial scale” will necessarily require a factual determination in each case. Accordingly, the Panel scrutinized the evidence offered by the United States to prove that China’s thresholds prohibited criminal prosecution for counterfeiting or piracy on a commercial scale.

The Panel found that the United States failed to establish a *prima facie* case because its evidence was “too little and too random to demonstrate a level that constitutes a commercial sale for any product in China.” Moreover, the United States’ evidence failed to demonstrate that the

thresholds were too high, that a safe harbor was created, or that China should consider “other indicia of infringement.” Accordingly, the Panel found that the United States failed to prove that China’s thresholds are inconsistent with China’s obligations in TRIPS 61.

As a result of the above findings, the Panel recommended that China bring its Copyright Law and Customs Measures into conformity with its obligations under TRIPS.

Reactions and Potential Implications

Given that the Panel’s decision was split, it is not surprising that both the United States and China claimed victory. According to U.S. Trade Representative Ron Kirk, “[T]he membership of the WTO agreed that China must bring its intellectual property rights enforcement regime into conformity with its WTO obligations.” Similarly, China “welcomed” the Panel’s decision that the United States “has not established that criminal thresholds are inconsistent with China’s obligations under the first sentence of Article 61 of TRIPS.”

The Panel’s decision is highly specific to the facts presented and may not readily allow extrapolation to other scenarios. However, the market-based analytical approach used by the Panel to evaluate counterfeiting and piracy on a commercial scale is a positive development. This approach will support future arguments that industry/product specific factors, technological advances (including the Internet), and other indicia of infringement should be considered when analyzing China’s criminal thresholds. It also sends the signal that the WTO and the Panel are interested in enforcing IPR not only in theory, but in practice—it is not enough for member nations to merely pay lip service to IPR and their obligations under TRIPS. That result should be viewed as a positive sign for IPR holders worldwide.

ENDNOTES

- * This article was originally published in the *Foley Legal News: China Quarterly Newsletter*, “Eye on China” on June 11, 2009. Copyright Foley & Lardner LLP. All rights reserved. Reprinted with permission.
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