

# TIME TO PAY THE DUES OR CAN INTELLECTUAL PROPERTY RIGHTS FEEL SAFE WITH THE WTO?

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## INTRODUCTION

*"The human mind has first to construct forms, in-  
dependently, before we can find them in things."*

*Albert Einstein.*

The power and extent of the human brain is inexplicable. The genius of imagination is manifold. It manifested the wheel, then the spaceship; it dressed the humanity in denim jeans, and accentuated it with a few drops of Chanel; it created vaccines and weapons of mass destruction. Much of what we see, smell, touch and hear was brought

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into life by somebody's mind. Possessed by desire to own numerous material objects and the power they represent, the man would fight, flatter and deceive. However, prior to a shaped form there is an immaterialized idea. Its value has undoubtedly been known since the dawn of humanity, but its high price has been only recently defined.<sup>2</sup> Its name is intellectual property.

"Over the last eight years, the Bush Administration has led a global fight against counterfeiting and piracy."<sup>3</sup> The price America pays for counterfeiting reaches hundreds of billions of dollars a year.<sup>4</sup> Consequently, harmful effects throughout the economy range from serious health and safety risks caused by fake products, to losses in tax revenues and usage of counterfeit sales to finance illegal groups and their operations.<sup>5</sup> Companies that become targets of counterfeiters frequently get an injurious slap on their reputation and a subsequent drop in consumers' demand.

Despite the recent change of administration in the White House, President-elect Barack Obama's hypnotizing slogans calling for change are not likely to be reflected in the intellectual property rights (IPR) situation. According to Clark T. Randt Jr., the United States Ambassador to China and founder of the 7th Annual Ambassador's IPR Roundtable, IPR protection is likely to remain "a top priority of the U.S. government at home and abroad."<sup>6</sup> Mr. Obama's selection for the Secretary of State position reinforces this prognosis. Mrs. Hillary Clinton has been an avid proponent of a new intellectual property enforcement network to strengthen IPR protections.<sup>7</sup>

Many of the United States IPR-related efforts have been focused on China, "the global epicenter of counterfeiting and piracy."<sup>8</sup> Despite China's impressive steps to prioritize IPR protection and enforcement, piracy and counterfeiting levels in China cost United States

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<sup>2</sup> See Mark A. Lemley, *Property, Intellectual Property, and Free Riding* 13 (Stanford Law and Econ. Olin Working Paper No. 291, 2004), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=582602](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=582602).

<sup>3</sup> Press Release, Office of the White House Press Secretary, Fact Sheet: Protecting American Innovation (Oct. 13, 2008) (on file with the White House Press Secretary), available at <http://www.whitehouse.gov/news/releases/2008/10/20081013-7.html> [hereinafter, Fact Sheet].

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

<sup>6</sup> Steven Schwankert, *US, China spar over copyright at conference*, NETWORKWORLD, Nov. 7, 2008, available at <http://www.networkworld.com/news/2008/110708-us-china-spar-over-copyright.html?page=1>.

<sup>7</sup> Press Release, Hilary Clinton for President, Hillary Clinton Calls For Stepped Up Enforcement of Trade Laws (Apr. 14, 2008) (on file with <http://wire52.com>), available at <http://www.hillaryclinton.com/news/release/view/?id=7089>.

<sup>8</sup> Fact Sheet, *supra* note 3.

firms and workers billions of dollars each year.<sup>9</sup> For example, only last year the F.B.I., jointly with the Chinese authorities, seized “more than \$500 million worth of counterfeit Microsoft and Symantec software that was being made in China and distributed worldwide.”<sup>10</sup> However, despite the magnitude of this operation, 82% of the software used in China today remains counterfeit.<sup>11</sup> Moreover, many counterfeit products, especially counterfeit medicines, pose a serious risk of harm to consumers in China, the United States and around the world.<sup>12</sup> For example, counterfeit Colgate toothpaste distributed in the United States and Canada contained poisonous chemicals and dangerous bacteria, respectively.<sup>13</sup>

“In April 2007, the U.S. requested the WTO to dispute settlement consultations with China over deficiencies in China’s legal regime for protecting and enforcing copyrights and trademarks on a wide range of products.”<sup>14</sup> Unfortunately, the consultations did not resolve the issues and on September 25th the WTO established a formal panel, requested by the United States, to investigate the matter.<sup>15</sup> The United States alleges that China has violated the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)<sup>16</sup> in several ways. Firstly, China’s criminal laws maintain safe harbors that allow commercial-scale counterfeiting and piracy undeterred by criminal prosecution or conviction for those acts.<sup>17</sup> Secondly, Chinese

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<sup>9</sup> *Id.*

<sup>10</sup> David Barboza & Steve Lohr, *F.B.I. and Chinese Seize \$500 Million of Counterfeit Software*, N.Y. TIMES, July 25, 2007, available at <http://www.nytimes.com/2007/07/25/business/worldbusiness/25soft.html>.

<sup>11</sup> *Huge Chinese piracy ring tackled*, BBC NEWS, July 26, 2007, <http://news.bbc.co.uk/2/hi/technology/6917127.stm>.

<sup>12</sup> Press Release, U.S. Trade Representative, United States Files WTO Cases Against China Over Deficiencies in China’s Intellectual Property Rights Laws and Market Access Barriers to Copyright-Based Industries (Apr. 09, 2007) (on file with the Office of the United States Trade Representative), available at [http://www.ustr.gov/Document\\_Library/Press\\_Releases/2007/April/United\\_States\\_Files\\_WTO\\_Cases\\_Against\\_China\\_Over\\_Deficiencies\\_in\\_Chinas\\_Intellectual\\_Property\\_Rights\\_Laws\\_Market\\_Access\\_Barr.html](http://www.ustr.gov/Document_Library/Press_Releases/2007/April/United_States_Files_WTO_Cases_Against_China_Over_Deficiencies_in_Chinas_Intellectual_Property_Rights_Laws_Market_Access_Barr.html).

<sup>13</sup> *Contaminated Counterfeit Toothpaste Now Found in 6 States, Canada*, FOXNEWS, July 1, 2007, <http://www.foxnews.com/story/0,2933,287544,00.html>

<sup>14</sup> OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE, 2008 SPECIAL 301 REPORT (2008), available at [http://www.ustr.gov/assets/Document\\_Library/Reports\\_Publications/2008/2008\\_Special\\_301\\_Report/asset\\_upload\\_file702\\_14868.pdf](http://www.ustr.gov/assets/Document_Library/Reports_Publications/2008/2008_Special_301_Report/asset_upload_file702_14868.pdf).

<sup>15</sup> *Id.*

<sup>16</sup> See Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, Annex 1C, 33 I.L.M. 1125 (1994) [hereinafter TRIPS].

<sup>17</sup> First Written Submission of the United States, *China – Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, ¶ 87, WT/DS362 (Jan.

customs officers lack the required authority to dispose of counterfeit and pirated imports.<sup>18</sup> Thirdly, China denies automatic and immediate copyright protection to certain works, including those that have not yet cleared China's content review process.<sup>19</sup>

The outcome of this landmark case is of great importance for a number of reasons. To begin with, it is going to provide substantive definition of the TRIPS provisions, the interpretation of which until now has not been invoked in a formal WTO dispute.<sup>20</sup> Furthermore, should the United States prevail, the prescribed remedies and China's reaction are likely to be genuine signs of how effective the WTO dispute settlement mechanism actually is. Although time is the only true judge, in this paper I will evaluate the United States claims against China, the potential outcome of the case, and provide certain contextually based predictions as to the implementation of the Dispute Settlement Body's (DSB) recommendations.

## I. RELEVANT LAW

In order to appreciate the existing WTO dispute resolution system and its application to the United States claims against China, it is important to evaluate its predecessor, the General Agreement of Tariffs and Trade ("GATT") dispute settlement procedure, and to understand the reasons why it failed its purpose.<sup>21</sup>

### A. *The GATT Dispute Settlement Procedure*

Article XXIII is the cornerstone of the GATT dispute settlement procedure.<sup>22</sup> It provides that a contracting party, whose benefits under the GATT are "being nullified or impaired", may make "written representations or proposals" to the other contracting party or parties concerned.<sup>23</sup> In response to such representations or proposals, their recipient shall "give sympathetic considerations" thereto.<sup>24</sup> If the par-

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30, 2008) available at <http://www.ifta-online.org/Uploads/Issues/58.pdf> [hereinafter First Submission].

<sup>18</sup> *Id.* ¶ 56.

<sup>19</sup> *Id.* ¶¶ 195–96.

<sup>20</sup> See generally Wayne M. Morrison, CONGRESSIONAL RESEARCH SERVICE, CHINA-U.S. TRADE ISSUES (July 11, 2007), available at <http://www.fas.org/sgp/crs/row/RL33536.pdf> (contending that: "The U.S. WTO cases on China's IPR regime represent the most comprehensive and complex cases the United States has filed against any WTO to date").

<sup>21</sup> General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194 [hereinafter GATT].

<sup>22</sup> *Id.* art. XXIII.1.

<sup>23</sup> *Id.*

<sup>24</sup> *Id.*

ties fail to resolve the dispute among themselves, the petitioner is entitled to bring the complaint before other contracting parties that shall "promptly investigate, make recommendations or give a ruling on the matter, as appropriate."<sup>25</sup> Originally, all of the contracting parties had to be present at the meeting.<sup>26</sup> Later, several alternatives became available to such a time-consuming and inefficient arrangement. One of them was a working party, composed of representatives of the disputing countries and of several neutral countries that would conduct the investigation and make a recommendation.<sup>27</sup> Another more popular variant was a panel that consisted of three to five trade experts.<sup>28</sup> The panel was required to act independently of any government and to be fair and impartial in exercising its judgment.<sup>29</sup> After considering all the arguments, including those of the interested third parties, the panel would issue a report containing a summary and recommendations.<sup>30</sup> However, recommendations could be implemented only if all member states, including the losing member, adopted the panel's report.<sup>31</sup> If the report did get unanimously adopted and "circumstances were serious enough to justify such action" the winning party could retaliate by depriving the offender of concessions or other circumstantially appropriate obligations under the GATT.<sup>32</sup>

At the onset of the GATT, when its few members were homogeneous and supportive of the GATT rules, contracting parties usually complied with the system in good faith.<sup>33</sup> However, as more nations became contracting parties, less conformity was observed.<sup>34</sup> The unanimous consent requirement of all member states was an obvious leeway for avoiding any penalty for non-compliance. Under Article XXIII, a losing party's objection to the panel's decision could not only veto the adoption of its recommendations, but also indefinitely delay the creation of the panel itself.<sup>35</sup> Obviously, unless all contracting parties voted in good faith, which is not required by Article XXIII, the

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<sup>25</sup> *Id.* art. XXIII.2.

<sup>26</sup> JOHN H. JACKSON, *THE WORLD TRADING SYSTEM: LAW AND POLICY OF INTERNATIONAL ECONOMIC RELATIONS* 95 (The MIT Press, 1989).

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> *Id.*

<sup>30</sup> Philip M. Nichols, *GATT Doctrine*, 36 VA. J. INT'L L. 379, 396 (1996).

<sup>31</sup> *Id.*

<sup>32</sup> GATT, *supra* note 21, art. XXIII.2.

<sup>33</sup> Miquel Montaña i Mora, *A GATT with Teeth: Law Wins over Politics in the Resolution of International Trade Disputes*, 31 COLUM. J. TRANSNAT'L L. 103, 108 (1993).

<sup>34</sup> *Id.* at 119-20.

<sup>35</sup> See William J. Davey, *Dispute Settlement in GATT*, 11 FORDHAM INT'L L.J. 51, 85 (1987).

petitioner's remedy would be contingent upon turbulent political interests and the economic might of other member states.<sup>36</sup> For example, in 1955 the United States political influence allowed it to circumvent certain agricultural obligations.<sup>37</sup> Furthermore, those member states that had been previously injured by the petitioner's veto on the panel's report could be motivated to cast their veto in retaliation.<sup>38</sup>

Unable to rely on the GATT dispute resolution system to redress their claims any longer, member states began to act unilaterally through threats and trade sanctions.<sup>39</sup> Naturally, such methods mostly benefited politically and economically strong states, while the weaker members did not have any effective means of redress. By the time the Uruguay Round of trade negotiations was commenced in 1986, the necessity for an effective and accessible dispute resolution mechanism had become a dire priority.<sup>40</sup>

### B. *The WTO Dispute Settlement Mechanism*

After almost a decade of trade negotiations, the Uruguay Round culminated in the WTO, which officially came into existence on January 1, 1995. The WTO became the first international organization to oversee the world trading system, including intellectual property and services, neither of which was covered by the GATT.<sup>41</sup> With it emerged a new centralized procedure for resolving trade-related disputes: the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU").<sup>42</sup> The preamble to the WTO Charter calls on the signatories "to develop an integrated, more viable and durable multilateral trading system", contrary to instability and unpredictability of Article XXIII of the GATT.<sup>43</sup>

The DSU, unlike Article XXIII of the GATT, lays out a structured procedure for dispute resolution arising under the WTO. As

<sup>36</sup> See Glen T. Schleyer, *Power to the People: Allowing Private Parties to Raise Claims Before the WTO Dispute Resolution System*, 65 *FORDHAM L. REV.* 2275, 2284 (1997).

<sup>37</sup> JACKSON, *supra* note 26, at 96.

<sup>38</sup> Michael K. Young, *Dispute Resolution in the Uruguay Round: Lawyers Triumph over Diplomats*, 29 *VA. J. INT'L LAW* 389, 399 (1995).

<sup>39</sup> Nichols, *supra* note 30, at 398-99.

<sup>40</sup> See G. Richard Shell, *Trade Legalism and International Relations Theory: An Analysis of the World Trade Organization*, 44 *DUKE L.J.* 829, 845-48 (1995).

<sup>41</sup> Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, Apr. 15, 1994, 33 *I.L.M.* 1125, 1144 (1994) [hereinafter Final Act].

<sup>42</sup> Understanding on Rules and Procedures Governing the Settlement of Disputes, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, Legal Instruments—Results of the Uruguay Round, 33 *I.L.M.* 1125, 1226 (1994) [hereinafter DSU].

<sup>43</sup> Final Act, *supra* note 41, pmbl.



well, it describes the remedies available to successful petitioners and methods of their enforcement.<sup>44</sup> Unlike the GATT, which enabled parties to choose a way of forming a dispute resolution panel based on their objectives, the WTO contains a single unified nucleus, the Dispute Settlement Body (DSB), which administers all disputes.<sup>45</sup> Furthermore, the DSU allows parties to appeal the panel's decision to the Appellate Body, a permanent entity consisting of seven judges.<sup>46</sup>

In addition, the DSU makes the adoption of the panel's and the Appellate Body's reports almost automatic.<sup>47</sup> In order to prevent a report from being implemented, the objection must be unanimous, meaning the victorious petitioner must also object.<sup>48</sup> Comparatively, under the GATT, any single party, including the losing respondent, had veto power, while under the WTO, the victorious petitioner's vote is sufficient to require report implementation.<sup>49</sup> At the same time, the DSU requires unanimous consent of all parties in order to delay the establishment of the panel, while under the GATT a single objection was enough to cause an indefinite delay.<sup>50</sup> Essentially, the DSU seeks to ensure that the petitioner shall have an opportunity to be heard, regardless of other members' personal interests and influences.

Remarkably, while the GATT imposed virtually no time limitations and panels could deliberate on numerous sessions for months,<sup>51</sup> the DSU effectively imposes strict procedural time frames for disputing parties,<sup>52</sup> the panel,<sup>53</sup> the Appellate body<sup>54</sup> and the DSB.<sup>55</sup>

The DSU's enforcement mechanism has been another impressive step forward. Under Article XXIII of the GATT, the panel's power was limited to authorizing the injured party to impose sanctions against the violator.<sup>56</sup> Unfortunately, if the victorious party was economically and/or politically weaker than the transgressor, the latter could evade the sanctions and proceed with its offensive practices.<sup>57</sup>

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<sup>44</sup> See Schleyer, *supra* note 36, at 2286.

<sup>45</sup> DSU, *supra* note 42, art. 2.

<sup>46</sup> *Id.* art. 17.

<sup>47</sup> Schleyer, *supra* note 36, at 2286.

<sup>48</sup> DSU, *supra* note 42, arts. 16.4, 17.14.

<sup>49</sup> See Shell, *supra* note 40, at 850.

<sup>50</sup> See Davey, *supra* note 35, at 81–89 (describing the problems of the GATT dispute settlement system).

<sup>51</sup> Nichols, *supra* note 30, at 395–96.

<sup>52</sup> See DSU, *supra* note 42, arts. 12.5, 12.6, 15.1, 15.3.

<sup>53</sup> *Id.* arts. 12.3, 12.8, 12.9, 21.5.

<sup>54</sup> *Id.* art. 17.5.

<sup>55</sup> *Id.* arts. 20, 21.4.

<sup>56</sup> GATT, *supra* note 21, at art. XXIII.2.

<sup>57</sup> See JACKSON, *supra* note 26, at 96.

Contrarily, the DSU ensures continuous observance of the violator's steps taken in order to comply with the recommendations.<sup>58</sup> Finally, Article twenty-three of the DSU grants the WTO unilateral power to impose sanctions on other members.<sup>59</sup>

### 1. *Report Implementation under the DSU*

According to Article 19 of the DSU, where the panel or Appellate Body finds the measure inconsistent with a covered agreement, it shall recommend the violating member "bring the measure in conformity with that agreement" and may also recommend ways to implement the suggested changes.<sup>60</sup> Article 21 emphasizes the importance of "prompt compliance with recommendation or rulings of the DSB" for effective dispute resolution.<sup>61</sup> However, the DSU allows, where immediate compliance is impractical, to act within a reasonable period of time, which can be any period of time proposed by the violator and approved by the DSB.<sup>62</sup> Absent such approval, the time should be mutually agreed upon by the parties within forty-five days after the adoption of the report, or determined by arbitration within ninety days after the adoption of the report provided.<sup>63</sup> With some variations depending on circumstances, such implementation shall not exceed fifteen months from the day of the adoption of the report.<sup>64</sup> Absent exceptional circumstances, the time from the establishment of the panel by the DSB until the determination of a reasonable implementation time shall not exceed eighteen months.<sup>65</sup> In addition, "the DSB shall keep under surveillance the implementation of adopted recommendations or rulings."<sup>66</sup> If there is a dispute regarding whether the suggested measures are being implemented, it can be brought to the attention of the DSB at any time and shall be decided through the dispute settlement procedures provided in the DSU.<sup>67</sup> Also, the original panel shall be resorted to whenever possible.<sup>68</sup>

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<sup>58</sup> See DSU, *supra* note 42, art. 21.6.

<sup>59</sup> See Young, *supra* note 38, at 400-01.

<sup>60</sup> DSU, *supra* note 42, art. 19.

<sup>61</sup> *Id.* art. 21.1.

<sup>62</sup> *Id.* art. 21.3.

<sup>63</sup> *Id.*

<sup>64</sup> *Id.*

<sup>65</sup> *Id.* art. 21.4.

<sup>66</sup> *Id.* art. 21.6.

<sup>67</sup> *Id.*

<sup>68</sup> *Id.* art. 21.5.



## 2. *Temporary Measures When Implementation is Delayed or Fails*

When "the recommendations and rulings are not implemented within a reasonable period of time," Article 22 of the DSU provides for temporary measures such as compensation, which must be voluntary and consistent with other agreements, and suspension of concessions.<sup>69</sup> Both are only temporary measures and shall be terminated upon implementation of the measures in conformity with the agreement.<sup>70</sup> Thus, if a respondent fails to comply with recommendations and rulings within reasonable time, it shall enter into negotiations with the petitioner in order to develop a mutually acceptable compensation.<sup>71</sup> However, if twenty days after the expiration of the reasonable time no consensus regarding the compensation has been reached, the petitioner is allowed to request authorization from the DSB to suspend the application to the respondent concerning concessions or other obligations under the covered agreements.<sup>72</sup> Furthermore, Article 22 lists principles and procedures, which must be considered in deciding which concessions to suspend.<sup>73</sup> Depending on whether it is practical and effective, the petitioner should seek to suspend the concessions with respect to the same sectors where violations have occurred and then other sectors of agreement.<sup>74</sup> Other concessions or obligations under another covered agreement shall be suspended only if the circumstances are serious enough.<sup>75</sup> The petitioner should also take into account the importance of trade to the petitioner state in the sector where the violation has occurred, as well as the broader economic elements related to the violation and the broader economic consequences of the suspension of concessions.<sup>76</sup> Moreover, the level of concessions suspended must be equivalent to the level of impairment or nullification.<sup>77</sup> Concessions cannot be suspended if prohibited by a covered agreement.<sup>78</sup> If the respondent objects to the substance or procedure of the suspension of concessions, preferably the original board or an arbitrator appointed by the Director-General shall carry out the arbitration.<sup>79</sup> The results of such arbitration are final.<sup>80</sup>

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<sup>69</sup> *Id.* art. 22.1.

<sup>70</sup> *Id.*

<sup>71</sup> *Id.* art. 22.2.

<sup>72</sup> *Id.*

<sup>73</sup> *Id.* art. 22.3.

<sup>74</sup> *Id.* art. 22.3(a).

<sup>75</sup> *Id.* art. 22.3(c).

<sup>76</sup> *Id.* art. 22.3(d)(i)–(ii).

<sup>77</sup> *Id.* art. 22.4.

<sup>78</sup> *Id.* art. 22.5.

<sup>79</sup> *Id.* art. 22.6.

<sup>80</sup> *Id.* art. 22.7.

Essentially, the WTO has comprehensively reformed the dispute resolution mechanism, obviating the need for individual countries to act unilaterally, and granting every member, regardless of its development status, equal access to justice.

### C. *The TRIPS Agreement*

Undoubtedly, the TRIPS agreement is one of the WTO's most remarkable innovations. It is the first international trade agreement that unifies into a single multilateral framework of principles diverse IPR that were previously protected by subject-specific agreements, such as the Berne, Paris and Rome Conventions.<sup>81</sup> Since the TRIPS agreement is one of the WTO treaties, the DSU principles apply to IPR-related disputes.<sup>82</sup> Thus, a victorious petitioner may not only obtain the judgment in its favor, but also adequate remedy and its implementation.

Essentially, the TRIPS agreement is a 'minimum standards' agreement.<sup>83</sup> It requires neither the creation of a separate and distinct legal body for IPR enforcement, nor uniformity of IPR enforcement in all member states.<sup>84</sup> Rather, the TRIPS agreement attempts to reconcile various ways of IPR protection in different member states by establishing mandatory minimum levels of protection that each government must provide to the intellectual property of other WTO members.<sup>85</sup>

Overall, the TRIPS agreement addresses the application of the basic principles of the GATT and other international intellectual property agreements such as the Berne and Paris conventions; availability of adequate protections of IPR; enforcement of IPR by countries on their own territories; settlement of IPR disputes between the WTO members; and special arrangements during the transitional period.<sup>86</sup>

While Part I of the TRIPS agreement lays out general principles of the agreement, it also emphasizes a national-treatment com-

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<sup>81</sup> Laurence R. Helfer, *Adjudicating Copyright Claims Under the TRIPS Agreement: The Case For a European Human Rights Analogy*, 39 HARV. INT'L L.J. 357, 358 (1998).

<sup>82</sup> See *id.* at 358.

<sup>83</sup> *Id.*

<sup>84</sup> See TRIPS, *supra* note 16, art. 1.1.

<sup>85</sup> World Trade Organization, Understanding the WTO: The Agreements, Intellectual Property: Protection and Enforcement, [http://www.wto.int/English/thewto\\_e/whatis\\_e/tif\\_e/agrm7\\_e.htm](http://www.wto.int/English/thewto_e/whatis_e/tif_e/agrm7_e.htm) (last visited Jan. 30, 2009) [hereinafter Understanding the WTO].

<sup>86</sup> GATT Focus Newsletter (1993), available in John H. Jackson et al., *LEGAL PROBLEMS OF INTERNATIONAL ECONOMIC RELATIONS* 1003 (5th ed. 2008) [hereinafter GATT Focus].

mitment.<sup>87</sup> This principle of non-discrimination obliges each WTO member to treat other WTO members no less favorably than it treats its own nationals with regard to IPR protection.<sup>88</sup> Also, a unique feature of the TRIPS agreement, compared to prior international conventions, is a most-favored-nation clause under which any advantage a member state gives to nationals of one foreign state must be automatically extended to nationals of all member states.<sup>89</sup> Thus, authors of computer programs and producers of sound recordings can authorize or prohibit the commercial rental of their works.<sup>90</sup> In addition, the Berne Convention calls for protection of performers from unauthorized recording and broadcasting of live performances.<sup>91</sup>

For the purposes of this paper, Part III of the TRIPS, designated "Enforcement of Intellectual Property Rights", is of particular interest. Article 41 requires that "members shall ensure enforcement procedures as specified in this Part are available under their law so as to permit effective action against any act of infringement of intellectual property rights covered by this Agreement."<sup>92</sup> Specifically, member governments must provide procedures and remedies under their domestic law to ensure "fair and equitable" IPR enforcement, which is not "unnecessarily complicated or costly, or entails unreasonable time-limits or unwarranted delays."<sup>93</sup> Article 41.4 requires that judicial review of final administrative decisions shall be available, except for review of acquittals in criminal cases.<sup>94</sup> Importantly, Article 41.5 explicitly provides that member states shall not be required to create a separate judicial system for IPR enforcement distinct from an existing general law enforcement system.<sup>95</sup> IPR enforcement should not "affect the capacity of Members to enforce their law in general" and does not need to be prioritized in the distribution of resources.<sup>96</sup>

Although the TRIPS does not mandate prioritizing the subsidization of IPR,<sup>97</sup> considerable investment is still inherently required to meet the minimum standards. Thus, developing countries may argue that an imposition of costly minimum standards deprives them of finances necessary for medicine, education and the development of infrastructure. However, since counterfeit goods manufactured in

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<sup>87</sup> *Id.*

<sup>88</sup> *Id.*

<sup>89</sup> *Id.*

<sup>90</sup> *Id.*

<sup>91</sup> *Id.*

<sup>92</sup> TRIPS, *supra* note 16, art. 41.1.

<sup>93</sup> *Id.* art. 41.2.

<sup>94</sup> *Id.* art. 41.4.

<sup>95</sup> *Id.* art. 41.5.

<sup>96</sup> *Id.*

<sup>97</sup> *See id.* art. 41.

developing countries often injure the economy and consumers of developed states, such minimum standards mandatory to all WTO members are reasonable and necessary to deter global IPR violations. Another criticism of Article 41 has been that the "minimum standards" versus "the best" standard of compliant behavior, make it difficult to estimate the bottom of the minimum, especially since intellectual property is intangible.<sup>98</sup> However, "the best" standard may be higher and more difficult to comply with. Potentially, outraged developing countries could refuse to comply en masse, which may cause the repetition of the tragic fate of Article XXIII of the GATT.

The civil and administrative procedures and remedies section of TRIPS includes provisions on evidence, proof, injunctions and damages. The TRIPS also specifies the right of judicial authorities to order the disposal or destruction of counterfeit imports outside the channels of commerce.<sup>99</sup> Judicial authorities shall also order prompt and effective provisional measures, especially when delay is likely to cause irreparable harm to the right holder, or when evidence is likely to be destroyed.<sup>100</sup> Further provisions encompass measures that customs officers are authorized to take after suspending counterfeit and pirated goods at the border. For example, Article 59 requires that customs officers shall be authorized to destroy or dispose of infringing goods outside of the channels of commerce.<sup>101</sup>

Finally, Article 61 sets minimum standards that trigger criminal prosecution. It requires that parties shall provide for criminal procedures and penalties at least in cases of willful trademark counterfeiting or copyright piracy on a commercial scale.<sup>102</sup> Available remedies shall include imprisonment and/or monetary fines sufficient to effectively deter crimes of similar magnitude.<sup>103</sup>

In addition, the Council for the TRIPS shall monitor the operation of the agreement and member states' compliance.<sup>104</sup> According to Article 64, the dispute settlement shall be governed by "Articles XXII and XXIII of GATT 1994 as elaborated and applied by the [DSU]."<sup>105</sup>

The drafters of the TRIPS appear to recognize inherent difficulties certain WTO members might face when implementing the TRIPS requirements due to their lack of economic development. This is ap-

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<sup>98</sup> See Rochelle Cooper Dreyfuss & Andreas F. Lowenfeld, *Two Achievements in the Uruguay Round: Putting TRIPS and Dispute Settlement Together*, 37 VA. J. INT'L L. 275, 281-83, 331-33 (1997).

<sup>99</sup> TRIPS, *supra* note 16, art. 61.

<sup>100</sup> *Id.* art. 50.

<sup>101</sup> *Id.* art. 59.

<sup>102</sup> *Id.* art. 61.

<sup>103</sup> *Id.*

<sup>104</sup> *Id.* art. 63.

<sup>105</sup> *Id.* art. 64.

parent as the TRIPS provides developing countries with a 5-year transition period and countries in the process of transformation from a centrally-planned into a market economy, with an 11-year transition period to bring their legislation and practices into conformity with the TRIPS.<sup>106</sup> In comparison, the developed countries were permitted one year to comply.<sup>107</sup>

## II. CASE STUDY: UNITED STATES V. CHINA

China and the United States have been working together to advance IPR observance and effective ways of IPR enforcement. The U.S.-China Joint Commission on Commerce and Trade (JCCT), in conjunction with the high-level U.S.-China Strategic Economic Dialogue established in September 2006, are the main vehicles through which the Office of the U.S. Trade Representative (USTR) together with the Department of Commerce, cooperate with China on IPR issues.<sup>108</sup> The USTR and the U.S. Patent and Trademark Office co-chair the JCCT's IPR Working Group (IPRWG) with China's Ministry of Commerce.<sup>109</sup> As noted by the United States Trade Representative, "American and Chinese agencies responsible for IPR protection and enforcement meet regularly in the IPRWG to discuss IPR issues."<sup>110</sup> Furthermore, an open strategic framework for related issues was created by the initiation of the Strategic Economic Dialogue (SED).<sup>111</sup>

However, despite this complex framework of bilateral negotiations, the U.S. has chosen to address its concerns through the WTO dispute resolution system. Moreover, the EC, Japan, Canada, and Mexico joined the U.S.'s request for consultations.<sup>112</sup> This may indicate that, despite optimistic press releases emphasizing the two countries' cooperation in the IPR sphere, the United States and China have so far failed to secure practical solutions.

The importance of intellectual property for twenty first century society gives the United States suit against China phenomenal significance.<sup>113</sup> It represents a chance for the DSU to reveal to the world

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<sup>106</sup> *Id.* art. 65.

<sup>107</sup> *Id.*

<sup>108</sup> Press Release, U.S. Trade Representative, *supra* note 12.

<sup>109</sup> *Id.*

<sup>110</sup> *Id.*

<sup>111</sup> *Id.*

<sup>112</sup> Panel Report, Dispute Settlement, China — Measures Affecting the Protection and Enforcement of Intellectual Property Rights, WT/DS362 (May 30, 2007) [hereinafter Measures Affecting Protection Panel Report].

<sup>113</sup> EU, Mexico Seek to Join China WTO Talks, INT'L HERALD TRIBUNE, May 1, 2007, [www.ihf.com/articles/ap/2007/05/01/business/EU-FIN-ECO-WTO-China-Piracy.php](http://www.ihf.com/articles/ap/2007/05/01/business/EU-FIN-ECO-WTO-China-Piracy.php).

through its decision and its effective enforcement the supremacy of the WTO dispute settlement system and the true benefits of WTO membership.

To better understand the contextual significance of this case, I would like to provide a brief overview of China's legal system and its current position in the world economy.

#### A. China's Economy

Since 1978 when Deng Xiaoping came to power, China has enjoyed a spectacular economic growth rate averaging 9.8% per year.<sup>114</sup> Meanwhile, after joining the WTO in 2001, China has become increasingly dependent on foreign markets, with a staggering 38% of its growth attributable to exports.<sup>115</sup> Today, in the face of worldwide recession, China's booming economy is at its slowest rate, with economy expansion of just 9% in the third quarter, compared to the 10.6% growth in the first quarter and 10.1% in the second quarter of 2008.<sup>116</sup> Such a slowdown is explained mainly by a decline in exports.<sup>117</sup> In southern China, factories that have relied on exporting to the U.S. and other wealthy nations have begun closing down and laying off thousands of workers.<sup>118</sup> Chinese President Hu Jintao stated that despite the challenges and difficulties China is facing due to the global financial crisis, "*the fundamentals of China's economy have not changed.*"<sup>119</sup> He emphasized the necessity of expanding consumer demand and maintaining economic financial stability while continuing to promote rapid economic development.<sup>120</sup> Thus, China's primary focus has shifted from controlling inflation to boosting growth with fiscal and monetary measures, assuming that with a small number of adjustments and a large amount of spending, the country can buy its way out of crisis.<sup>121</sup> However, some experts believe that despite such measures as a new value-added tax rebate and new incentives for the real estate sector, the program will fail because it relies on a flawed assumption.<sup>122</sup> Experts suggest that the true reason lies with consum-

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<sup>114</sup> Gordon G. Chang, *Beijing Bust?*, FORBES, Oct. 23, 2008, available at [http://www.forbes.com/opinions/2008/10/23/china-economy-bust-oped-cx\\_gc\\_1024chang.html](http://www.forbes.com/opinions/2008/10/23/china-economy-bust-oped-cx_gc_1024chang.html).

<sup>115</sup> *Id.*

<sup>116</sup> *Id.*

<sup>117</sup> *See id.*

<sup>118</sup> *Id.*

<sup>119</sup> Hu says fundamentals of China's economy have not changed despite crisis, ASIAN PAC. NEWS, Oct. 24, 2008, available at [http://www.channelnewsasia.com/stories/afp\\_asiapacific/view/385150/1.html](http://www.channelnewsasia.com/stories/afp_asiapacific/view/385150/1.html).

<sup>120</sup> *Id.*

<sup>121</sup> *See* Chang, *supra* note 114.

<sup>122</sup> *See id.*



ers' unwillingness to consume and not with their inability to afford Chinese goods.<sup>123</sup>

The impact of the international financial crisis on China is at least two-fold. On the one hand, it may reveal such issues as bad loans, corruption, environmental problems, unfunded social welfare obligations that were caused by China's heavy reliance on exports; issues once disguised by China's economic success.<sup>124</sup> The economic slowdown may motivate China to be more sensitive to the concerns of major export markets, including the United States' complaints regarding China's flawed IPR protection and enforcement.

### *B. Relevant Features of the Chinese Legal System*

With written records dating back 4,000 years, China is one of the four great ancient civilizations of the world.<sup>125</sup> China introduced gunpowder, papermaking, printing and the compass to the world.<sup>126</sup> As noted by Assistant Commerce Minister Chong Quan, China established a high level IPR protection system in line with international practices in twenty years; by comparison Europe and the United States took hundreds of years to set up a similar system.<sup>127</sup>

However, for a long time and with few interruptions, China's clan-based society was governed by the emperor, who was not only the ruler of the country but also the ultimate source of law.<sup>128</sup> Only in 2004 did China amend its 1982 constitution to mandate the rule of the country by law.<sup>129</sup> In 2007, the 17th Communist Party of China's National Congress expressly called for a comprehensive implementation and strengthening of the fundamental principle of rule of law in the country.<sup>130</sup> However, the independence of the Chinese judiciary, a necessary element of the rule of law, remains uncertain.<sup>131</sup> Under the current regime, unilaterally dominated by the Communist party, it is

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<sup>123</sup> *Id.*

<sup>124</sup> *Id.*

<sup>125</sup> Formation of the Chinese Civilization, CHINA INTERNET INFORMATION CENTER, <http://www.china.org.cn/e-gudai/index.htm> (last visited Feb. 8, 2009).

<sup>126</sup> Formation of the Chinese Civilization: The Four Great Inventions, CHINA INTERNET INFORMATION CENTER, <http://www.china.org.cn/e-gudai/8.htm> (last visited Feb. 8, 2009).

<sup>127</sup> *China defends efforts to protect intellectual property rights*, AFP, Nov. 6, 2008, <http://afp.google.com/article/ALEqM5gvZkF6DVnobjsVshdKfOnDQJTp1A>.

<sup>128</sup> Mo Zhang, *Rule of Law and Judicial Independence in China, Dedication to Dean Robert J. Reinstein*, 80 TEMP L. REV. 627, 645 (2007).

<sup>129</sup> *Id.*

<sup>130</sup> The State Council Information Office, China, *China's Efforts and Achievements in Promoting the Rule of Law*, 7 CHINESE J. INT'L L. 513, 516 (2008).

<sup>131</sup> Zhang, *supra* note 128, at 646.

unlikely that China's judiciary will exercise its judgment independent of the government which secures the positions of sitting judges.<sup>132</sup>

Many laws have been enacted to create a complete legal system for the protection of the IPR. These laws include:

Patent Law, Trademark Law, Copyright Law and Law on Countering Unfair Competition, and the promulgation of a series of administrative regulations, including the Regulations on the Protection of Computer Software, Regulations on the Protection of Layout-design of Integrated Circuits, Regulations on the Collective Management of Copyrights, Regulations on the Protection of Dissemination of Information Through Internet, Regulations on Customs Protection of Intellectual Property Rights and Regulations on the Protection of New Varieties of Plants.<sup>133</sup>

Today, according to the Constitution and the Law on Legislation of the People's Republic of China, the National People's Congress (NPC) is the highest organ of power.<sup>134</sup> Together with the Standing Committee as its permanent body the NPC exercises the legislative power of the State, including the power to formulate China's laws.<sup>135</sup> China's highest judicial body is the Supreme People's Court ("SPC"). Its primary functions include hearing appeals, supervising the work of local courts, and giving judicial interpretations of the specific utilization of laws.<sup>136</sup> Meanwhile, the Supreme People's Procuratorate ("SPP") and other lower procuratorates administer an independent legal supervisory system that makes decisions on arrest and prosecution.<sup>137</sup> Importantly, the NPC and Standing Committee have delegated some of its legislative powers to the SPC and the SPP allowing them to make legally enforceable binding interpretations of questions involving the specific applications of laws and decrees in court trials and procuratorial work respectively.<sup>138</sup>

### *1. China's Thresholds for Criminal Penalties and Procedures for Trademark Counterfeiting and Copyright Piracy.*

The Chinese law requires that certain acts of IPR infringement shall be criminally prosecuted only when specific monetary or volume-

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<sup>132</sup> *Id.*

<sup>133</sup> State Council, *supra* note 130, at 528.

<sup>134</sup> *Id.* at 518.

<sup>135</sup> *See id.*

<sup>136</sup> *Id.* at 534.

<sup>137</sup> *See id.* at 537.

<sup>138</sup> *Id.*

based thresholds are met.<sup>139</sup> The Criminal Law of the People's Republic of China ("Criminal Law") lists the legal requirements, while the SPC and SPP further define them in their joint binding interpretations: (1) the Interpretation by the Supreme People's Court and the Supreme People's Procuratorate of Several Issues Concerning the Specific Application of Law in Handling Criminal Cases Involving Infringement of Intellectual Property Rights ("December 2004 JI"), and (2) the Interpretation by the Supreme People's Court and the Supreme People's Procuratorate of Several Issues Concerning the Specific Application of Law in Handling Criminal Cases of Infringement of Intellectual Property Rights (II) ("April 2007 JI"). When December 2004 JI and April 2007 JI conflict, the latter controls.<sup>140</sup>

Illegal IPR infringement, which will result in criminal penalties in China, is defined in Part Two, Chapter III, Section 7 of China's Criminal Law.<sup>141</sup> Various trademark counterfeiting and piracy acts are specifically criminalized under Articles 213, 214 and 215, and Articles 217 and 218, respectively.<sup>142</sup> However, under the Criminal Law only piracy and counterfeiting that involve either "illegal gains" that are "relatively large" or "enormous" "circumstances" that are "serious" or "especially serious" can trigger criminal prosecution.<sup>143</sup> The December 2004 JI and the April 2007 JI further specify monetary and quantitative minimums to fit the legal standards set out in the Criminal Law.<sup>144</sup> Thus, to be subjected to criminal prosecution, the infringer must realize a minimum "illegal business volume" (USD \$ 6,925), obtain minimum amounts of "illegal gains" (USD \$4,155), or produce a minimum number of "illegal copies" (500 copies).<sup>145</sup> Importantly, the controlling April 2007 JI lowered the threshold for the minimum number to 500 copies from 1000, as previously required by the December 2004 JI.<sup>146</sup>

## 2. *China's Measures Regarding the Disposal of Infringing Goods Confiscated by the Customs Authorities.*

The Regulations of the People's Republic of China for Customs Protection of Intellectual Property Rights ("Customs IPR Regulations"), the Implementing Measures of Customs of the People's Republic of China for the Regulations of the People's Republic of China on

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<sup>139</sup> First Submission, *supra* note 17, ¶ 25.

<sup>140</sup> *Id.* ¶ 34 (citations omitted).

<sup>141</sup> *Id.* ¶ 31.

<sup>142</sup> *Id.*

<sup>143</sup> *Id.* ¶ 33.

<sup>144</sup> *Id.* ¶ 34.

<sup>145</sup> First Submission, *supra* note 17, ¶ 41.

<sup>146</sup> *Id.* ¶ 50.

Customs Protection of Intellectual Property Rights ("Customs IPR Implementing Measures"), and Announcement No. 16 of the General Administration of Customs ("Customs Announcement No. 16") lay out a hierarchical set of rules that the Chinese customs authorities shall follow when dealing with counterfeit goods seized at the border.<sup>147</sup> Essentially, customs authorities are first required to attempt to sell the seized goods to the right holder or, alternatively, transfer them to public welfare organizations. If this cannot be done, they may then auction them off after removing the infringing features. Only as a means of last resort are the customs officers authorized to destroy the seized counterfeit goods.<sup>148</sup>

### 3. *Article 4 of China's Copyright Law*

"The Copyright Law of the People's Republic of China ('Copyright Law') provides the legal basis for protecting and enforcing the copyrights of authors in their literary, artistic and scientific works as well as 'related rights' in China."<sup>149</sup> Importantly, Article 4 provides that "[w]orks[,] the publication or distribution of which is prohibited by law[,] shall not be protected by this Law."<sup>150</sup> The Chinese law might prohibit the publication or distribution of a certain work for various reasons, one of which is the work's content.<sup>151</sup> In addition, IPR protection can be compromised up until the moment the work receives censorship approval, thus falling into the secure zone of Article 4. For example, the Regulation on the Administration of Films governs the "production, import, export, distribution and screening of films within the territory of the People's Republic of China."<sup>152</sup> It also provides that "for some time after a film's creation, and until that film has been submitted for and has completed the content review, the film cannot be imported, distributed or projected."<sup>153</sup> Similarly, publications, audio and video products and electronic publications all possess prohibitions on publication and distribution until such time that a content review process has been successfully completed.<sup>154</sup>

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<sup>147</sup> *Id.* ¶¶ 56-57.

<sup>148</sup> *Id.* ¶¶ 58-61.

<sup>149</sup> *Id.* ¶ 62.

<sup>150</sup> *Id.* ¶ 67.

<sup>151</sup> *See id.* ¶ 71.

<sup>152</sup> *Id.* ¶ 72 (citing State Council Order No. 342, ST. COUNCIL GAZ., art. 2 (Dec. 25, 2001)).

<sup>153</sup> *Id.* ¶ 77.

<sup>154</sup> *Id.* ¶ 78.

### C. *The United States' Claims before the WTO*

In its complaint against China, the United States alleges three TRIPS violations. First, China's threshold system prevents certain commercial scale counterfeiting and piracy acts from criminal prosecution, violating Article 61 of the TRIPS.<sup>155</sup> Second, China's failure to entrust its customs officers with authority to destroy counterfeit and pirated imports violates Article 59 of the TRIPS.<sup>156</sup> Third, China's requirement of censorship approval as a necessary pre-requisite of copyright protection contradicts the automatic and immediate copyright protection duty under Articles 5(1) and 5(2) of the Berne Convention and Article 14 of the TRIPS.<sup>157</sup>

The United States advances several reasons why China's efforts in these three areas have been insufficient. First, Article 61 of the TRIPS requires that, "[m]embers shall provide for criminal procedures and penalties to be applied at least in cases of wilful trademark counterfeiting or copyright piracy on a commercial scale."<sup>158</sup> In this case "at least" indicates the mandatory minimum applicable to the rest of the sentence, i.e., "willful trademark counterfeiting or copyright piracy on commercial scale."<sup>159</sup> Here, the essence of the controversy lies in the interpretation of what constitutes "commercial scale."<sup>160</sup>

Following the customary rules of interpretation of the Vienna Convention as required by Article 3.2 of the DSU, the United States interprets "scale" as "of certain extent or magnitude", and "commercial" as linked "to the commercial market place."<sup>161</sup> Thus, according to the United States, "commercial scale" in its ordinary meaning extends to those who engage in commercial activities, including manufacturing, distribution and retail sales.<sup>162</sup> On the other hand, China contends that such interpretation is unreasonable since it could require criminal prosecution even for one pirated copy.<sup>163</sup> Instead, China suggests that "commercial scale" should be understood as "significant

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<sup>155</sup> See *id.* ¶ 87.

<sup>156</sup> *Id.* ¶ 170.

<sup>157</sup> *Id.* ¶¶ 210, 213.

<sup>158</sup> TRIPS, *supra* note 16, art. 61.

<sup>159</sup> First Submission, *supra* note 17, ¶ 93.

<sup>160</sup> *Id.* ¶ 95.

<sup>161</sup> *Id.* ¶ 109.

<sup>162</sup> *Id.*

<sup>163</sup> See Executive Summary of the Oral Statement of the United States of America at the Second Substantive Meeting of the Panel, *China – Measures Affecting the Protection and Enforcement of IPR*, WT/DS362 (June 30, 2008), available at [http://www.ustr.gov/assets/Trade\\_Agreements/Monitoring\\_Enforcement/Dispute\\_Settlement/WTO/Dispute\\_Settlement\\_Listings/asset\\_upload\\_file781\\_14436.pdf](http://www.ustr.gov/assets/Trade_Agreements/Monitoring_Enforcement/Dispute_Settlement/WTO/Dispute_Settlement_Listings/asset_upload_file781_14436.pdf) [hereinafter Oral Statement].

magnitude" and bases such interpretation on "common usage."<sup>164</sup> However, China has presented no evidence that the Uruguay Round of negotiations relied on the sources cited by China.<sup>165</sup> Also, China's argument does not take into account that the approach suggested by the United States is not simply numerical, but instead, it involves a fact-specific, case-by-case determination based on consideration of such relevant factors as:

"the market for the infringed goods, the object of the infringement, the magnitude or extent of the infringement, the value of the infringed goods, whether the infringer is seeking financial gain, the means of producing the infringing goods, the means of distributing the infringing goods, the marketing and solicitation of business, the intended use of the infringing goods, the impact of the infringement on the right holder, and the involvement of organized crime."<sup>166</sup>

Currently, China's laws do not provide for criminal prosecution or conviction of piracy and counterfeiting acts unless they meet specific quantitative or value thresholds, regardless of whether they fall within "commercial scale" as interpreted by the United States.<sup>167</sup> While Article 61 of the TRIPS requires a legal regime that criminalizes all willful counterfeiting and piracy on a commercial scale, China's purely numerical thresholds potentially ignore whole classes of "commercial scale" piracy and counterfeiting.<sup>168</sup> Not surprisingly, statistical information has revealed that the lowest relevant threshold is met by less than twenty percent of establishments deemed to be selling copyright-infringing music CD's or DVD's.<sup>169</sup> Moreover, the very essence of the Chinese marketplace, composed of small manufacturers, middlemen, and distributors, indicates the ease with which counterfeiters adjust to the existing standards and avoid criminal sanctions.<sup>170</sup> For example, each page of the seizure data provided by the "The Report on Copyright Complaints, Raids and Resulting Criminal

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<sup>164</sup> *Id.*

<sup>165</sup> *Id.*

<sup>166</sup> *Id.*

<sup>167</sup> See generally First Submission, *supra* note 17, ¶¶ 111–63 (discussing the absence of any form of commercial scale threshold to the Chinese statutory provisions and the implications of this absence upon international IPR, specifically those involving the United States).

<sup>168</sup> *Id.*

<sup>169</sup> *Id.* ¶ 6.

<sup>170</sup> Executive Summary of the Closing Statement of the United States of America at the Second Substantive Meeting of the Panel, *China – Measures Affecting the Protection and Enforcement of IPR*, ¶ 3, WT/DS362 (June 30, 2008) available at [http://www.ustr.gov/assets/Trade\\_Agreements/Monitoring\\_Enforcement/Dispute\\_](http://www.ustr.gov/assets/Trade_Agreements/Monitoring_Enforcement/Dispute_)



Actions in China in Exhibit US-41", listed a business operating on a "commercial scale", yet below China's thresholds and beyond the reach of criminal prosecution.<sup>171</sup>

In its second complaint, the United States alleges that Chinese customs officers' lack of authority to order the destruction or disposal of infringing goods according with the principles of Article 46 of the TRIPS, is inconsistent with Article 59 of the TRIPS.<sup>172</sup> Article 59 provides that "competent authorities shall have the authority to order the destruction or disposal of infringing goods in accordance with the principles set out in Article 46."<sup>173</sup> The principles referred to include the authority to destroy infringing goods or to dispose of them outside the channels of commerce so as to avoid harm to the right holder.<sup>174</sup> Moreover, removing an unlawfully affixed trademark will not suffice to allow the release of the good into the channels of commerce, other than in exceptional cases.<sup>175</sup> However, Article 27 of the Customs IPR Regulations and Article 30 of the Customs IPR Implementing Measures requires Chinese customs officers to follow a mandatory set of rules in deciding how to treat imported counterfeit goods.<sup>176</sup> Customs officers must first estimate whether the seized goods can be used for "public good", and if so, donate them to an appropriate "public welfare organization."<sup>177</sup> Alternatively, customs officers may offer the right holder to purchase the seized goods.<sup>178</sup> Such an option, however, fails to meet Article 46 of the TRIPS requirement to "avoid any harm . . . to the right holder", since the owner will still suffer the harm in the amount of the price she has to pay for the goods.<sup>179</sup> Arguably, it is unwise to destroy products that might, for example, be donated to the poor in developing countries and thus serve a socially beneficial purpose. However, the stubborn propensity of fake Louis Vuitton and Rolex products to turn up in Amsterdam or New York City clearly diffuses the likelihood that counterfeit goods are staying within developing countries' borders. If neither the donation, nor the sale to the right holder option is available, customs officers must auction the seized goods.<sup>180</sup> Such method not only precludes the destruction of the goods,

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Settlement/WTO/Dispute\_Settlement\_Listings/asset\_upload\_file708\_14436.pdf [hereinafter, Closing Statement].

<sup>171</sup> *Id.*

<sup>172</sup> First Submission, *supra* note 17, ¶ 172.

<sup>173</sup> TRIPS, *supra* note 16, art. 59.

<sup>174</sup> First Submission, *supra* note 17, ¶ 175.

<sup>175</sup> *Id.* ¶ 178.

<sup>176</sup> *Id.* ¶ 179.

<sup>177</sup> *Id.* ¶ 180.

<sup>178</sup> *Id.*

<sup>179</sup> *Id.* ¶ 183.

<sup>180</sup> *Id.* ¶ 188.

but also introduces them back into the stream of commerce.<sup>181</sup> In addition, the harm inflicted on the rightful owner is not much different than the one resulting from the actual sale of counterfeit goods.<sup>182</sup> Article 46 of the TRIPS prohibits the seized goods from re-entering the channels of commerce even after the unlawfully affixed trademark is removed unless there are "exceptional circumstances."<sup>183</sup> Paradoxically, the Chinese legal standard has instead pushed the option to destroy the seized goods into a rare "exceptional circumstances" category.<sup>184</sup>

The third United States claim addresses China's denial of copyright and related rights protection and enforcement to works that have not yet received censorship approval in China.<sup>185</sup> According to Article 4.1 of the Copyright Law, "[w]orks the publication or distribution of which is prohibited by law shall not be protected by this Law."<sup>186</sup> Under the TRIPS and the Berne Convention, to which China is a party, a work almost always acquires copyright protection immediately and automatically upon the work's creation and copyright is not conditional upon application and registration.<sup>187</sup> Among minimum rights provided in Article 5(1) of the Berne Convention is the right to authorize and, by implication, prohibit certain economic activities, such as reproduction, translation, adaptation and some others.<sup>188</sup> Furthermore, Article 5(2) of the Berne Convention provides that the exercise of the rights listed in Article 5(1) "shall not be subject to any formality."<sup>189</sup> Meanwhile, the standards for copyright review and for estimating what is "prohibited by law" for the purposes of Article 4.1 overlap.<sup>190</sup> This makes copyright protection in China subject to the formality of content review, which violates Article 5(2) of the Berne Convention.

Essentially, the main flaw in China's design of its copyright protection laws is China's failure to differentiate between censorship and creators' right to authorize or prohibit certain uses of their works by third persons.<sup>191</sup> Such failure has created a comical situation

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<sup>181</sup> *Id.* ¶ 189.

<sup>182</sup> *Id.*

<sup>183</sup> TRIPS, *supra* note 16, art. 46.

<sup>184</sup> First Submission, *supra* note 17, ¶ 190.

<sup>185</sup> *Id.* ¶ 196.

<sup>186</sup> *Id.* ¶¶ 21, 217.

<sup>187</sup> *Id.* ¶ 215.

<sup>188</sup> Berne Convention for the Protection of Literary and Artistic Works, Sept. 9, 1886, as amended, July 14, 1967, art. 5.1, 1971 WL 123138, 828 U.N.T.S. 221 [hereinafter Berne Convention].

<sup>189</sup> *Id.* art. 5.2.

<sup>190</sup> Oral Statement, *supra* note 163, ¶ 26.

<sup>191</sup> Oral Statement, *supra* note 163, ¶ 24.

where authentic works are officially prohibited by the Chinese authorities, while their pirated copies are widely available to the Chinese consumers.<sup>192</sup> Importantly, the TRIPS does not obligate China, or any other WTO member, to authorize publishing and distribution of all works. What it does require is to protect and enforce the copyright of the works it prohibits.<sup>193</sup>

Thus, since Article 4 of the Copyright Law denies copyright protection to works absent censorship approval, no criminal procedures or remedies are available, even when piracy occurs on a commercial scale, which violates Articles 41 and 61 of the TRIPS.<sup>194</sup>

### 1. *Current Status of the Case and Future Predictions.*

A United States trade official has recently announced that the panel ruled in favor of the United States on two counts and in favor of China on one count.<sup>195</sup> According to trade sources, China's measures barring copyright protection for movies, music and books that have not been approved by state censors for legitimate sale in the Chinese market violate the TRIPS.<sup>196</sup> The panel has also ruled that auctioning of seized counterfeit goods after the infringing trademark is removed is a clear violation of the TRIPS.<sup>197</sup> However, the panel cast its votes in support of China's threshold system for criminal prosecution.<sup>198</sup> China's status as a developing country and its recent adjustment of the thresholds necessary for criminal prosecution from 1000 to 500 copies<sup>199</sup> could be a possible explanation for this outcome. By ruling two matters in favor of the United States and one matter in favor of China, the panel has probably sent a signal that IPR violations and non-compliance with the TRIPS agreement will not go unpunished; yet it still wanted to praise and encourage China's efforts, as a developing country, to create an effective legal system for IPR protection within such a short period of time.

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<sup>192</sup> First Submission, *supra* note 17, ¶ 200.

<sup>193</sup> Executive Summary of the First Submission of the United States of America, *China — Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, ¶ 1, WT/DS362 (Feb. 8, 2008) available at [http://www.ustr.gov/assets/Trade\\_Agreements/Monitoring\\_Enforcement/Dispute\\_Settlement/WTO/Dispute\\_Settlement\\_Listings/asset\\_upload\\_file352\\_14436.pdf](http://www.ustr.gov/assets/Trade_Agreements/Monitoring_Enforcement/Dispute_Settlement/WTO/Dispute_Settlement_Listings/asset_upload_file352_14436.pdf) [hereinafter Submission Summary].

<sup>194</sup> See *id.* ¶ 13.

<sup>195</sup> See, e.g., Measures Affecting Protection Panel Report, *supra* note 112.

<sup>196</sup> Doug Palmer, *US claims win in WTO piracy case versus China*, REUTERS, Oct. 9, 2008, <http://www.reuters.com/article/domesticNews/idUSTRE49895G20081009>.

<sup>197</sup> *Id.*

<sup>198</sup> *Id.*

<sup>199</sup> *Id.*

The United States appeal of the panel's ruling against it is currently pending before the Appellate Body, which should make its determination within 60 to 90 days. Pursuant to Article 17 of the DSU, "an appeal shall be limited to issues of law covered in the panel report and legal interpretations developed by the panel."<sup>200</sup> Thus, the Appellate Body rarely reverses the panel's determinations since it is generally not authorized to reverse the panel's factual findings.<sup>201</sup>

After the issuance of the appellate report, China might be requested to implement the suggested recommendations regarding the issues that bore the violations of the TRIPS. The report might include a recommendation to prioritize China's customs officer's authority to destroy seized counterfeit goods, which is currently a mere formality and a means of last resort. In addition, China would probably be asked to amend its laws and to provide for copyright protection of all works, regardless of their stage in the censorship approval process. If the Appellate Body reverses the panel's finding and finds China's threshold system illegal, China would probably be requested to refrain from using the threshold mechanism. Instead, China would be required to focus on providing criminal prosecution for all willful trademark piracy and counterfeiting occurring on a commercial scale, which should be estimated not by numerical thresholds but by considering all relevant factors.

China would have to inform the DSU of the measures it intends to take in order to comply with the recommendations.<sup>202</sup> In addition, if the United States further questions China's compliance with the DSB's recommendations, the DSU panel, preferably the same one that resolved the initial dispute, should resolve the matter.<sup>203</sup>

Furthermore, if China fails to comply with the recommendations, or if China's attempts to comply are unsatisfactory, the United States shall, within a reasonable time established by the DSU, implement one of the temporary measures, i.e., compensation or withdrawal of concessions. Since the compensation must be agreed upon by both the parties and thus is more problematic to achieve, withdrawal of concessions is a preferred method of retaliation. Under Article 20 of the DSU, the United States must first consider the possibility of retaliation in the sphere of the articles of the TRIPS that were violated and then within the TRIPS overall. However, if the United States shows that the retaliation in the same sphere is not going to be effective, it

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<sup>200</sup> DSU, *supra* note 42, art. 17.

<sup>201</sup> *Id.*

<sup>202</sup> *Id.* art. 21.

<sup>203</sup> *Id.*

can retaliate in another sphere covered by the WTO and impact IPR enforcement in China vicariously.<sup>204</sup>

It is important that the United States should choose the target for retaliation with great caution in order to prevent a self-inflicted injury. For example, when the United States embargoed exports of grain into the USSR in response to the latter's war in Afghanistan, the USSR simply increased its own grain production and imported grain from Australia.<sup>205</sup> Consequently, the United States farmers lost a vast market for their grain and were injured by their own country's sanctions against a foreign state. Today, 11.9% of United States trade revenues result from its dealings with China.<sup>206</sup> Thus, the WTO sanctions on many of the Chinese products could injure the United States economy.<sup>207</sup>

Ideally, China would either implement the DSU's recommendations or the United States and China would reach a compromise. Although the compromise was not a viable option a year ago when the United States requested the establishment of the panel, such an optimistic outcome is not so far-fetched today, in the face of the current global financial crisis. While buyers' capacity around the world has been declining, China, unable to rely on large profits made from its aggressive exporting strategies, could be forced to become more humble and timid in terms of international cooperation. There is a reasonable probability that it will choose to implement the DSB's recommendations in order to maintain a stable relationship with other economies in these financially difficult times.

Therefore, even if the Appellate Body upholds the panel's decision in favor of China's threshold system, China potentially could lower its thresholds even more to avoid confrontation with the international community and worsening of its economic situation. For example, only recently China has severed its fines for IPR violations, which are expected to be an effective deterrent for intellectual property pirates and counterfeiters.<sup>208</sup>

In addition, valid concerns exist regarding global consequences of the DSU's decision. On the one hand, the ruling in favor of the United States may upset the interests of developing countries and di-

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<sup>204</sup> *Id.* art. 22.

<sup>205</sup> Donald H. Caldwell, Jr., *The Export Administration Amendments Act of 1895: a Reassessment and Proposals for Further Reform*, 19 VAND. J. TRANSNAT'L L. 811, 828 n.87 (1986).

<sup>206</sup> U.S. CENSUS BUREAU, FOREIGN TRADE DIVISION, FTD - STATISTICS - TRADE HIGHLIGHTS - TOP TRADING PARTNERS (2007), available at <http://www.census.gov/foreign-trade/statistics/highlights/top/top0612.html>.

<sup>207</sup> *Id.*

<sup>208</sup> China's Judiciary Improves IPR Protection, CHINA DAILY, Nov. 4, 2008, available at [http://www.chinadaily.com.cn/bizchina/2008-11/04/content\\_7172464.htm](http://www.chinadaily.com.cn/bizchina/2008-11/04/content_7172464.htm).

minish their motivation to comply with what they already view as high standards. At the same time, if the ruling is in favor of China, developed countries that often get injured by counterfeit goods coming from developing countries, might lose faith in the TRIPS and the WTO and deem it ineffective for the purposes of protecting and enforcing IPR. Although developing countries might be discouraged by the United States victory, the global nature of the world's economies has made it impossible for states to exist and develop in isolation. Therefore, developing states realize that in order to achieve prosperity they need to respect international standards. Such understanding will most likely foster compliance rather than total rejection of the WTO standards.

## CONCLUSION

The importance of the outcome of the current case becomes clear when we evaluate modern market development trends, with intellectual property being an expensive commodity, the value of which often surpasses one of tangible goods. Assuming that the Appellate Body is going to uphold the panel's decision, taken the interdependency of countries in the modern economy and seeing China's fast-paced evolution in its IPR laws, it would be rational for China to comply with the DSU's recommendations. Thus, China might want to make sure that its customs officers destroy the seized goods and that IPR protection extends to creative material regardless of censorship approval. Such attitudes could be motivated by the DSU's acknowledgment of China's efforts and recognition of its threshold system as valid under the TRIPS.

Essentially, the decision of the DSU and its consequences will reveal, to a certain extent, whether the WTO dispute resolution mechanism is effective enough to meet the needs of the twenty first century's highly interdependent and complex economies.