China – Law Firms

Protection Of IP In China: A Work In Process

The Editor interviews ***Dr. Xiang Wang****, Of Counsel, Jones Day.*

Editor: Dr. Wang, please tell our readers something about your background.

Wang: I am trained in both China and the United States. I have a bachelors degree, a masters degree and a Ph.D. in electrical engineering, and I have a J.D. as well. I was born in China and came to the U.S. 22 years ago. My practice at Jones Day involves patent litigation and prosecution as well as cross-border medical technology regulatory issues. Last month I was honored by *Asian Legal Business*, which selected me as one of the Hottest Thirty Lawyers in 2005 and the only patent attorney among this group.

Editor: Please describe Jones Day's IP practice in China.

Wang: The practice, which I co-head, is the largest among all of the foreign law firms in China. We have litigated many cross-border IP disputes and prosecuted over 1,500 patent applications. When it comes to the Greater China Area, namely, China, Taiwan and Hong Kong, our IP group consists of close to 30 IP lawyers, and they reside in the firm's offices in Beijing, Shanghai, Hong Kong and Taiwan. In the past several years we have litigated cross-border IP cases with an accumulated claimed amount of more than $8 billion U.S.

Editor: Much has been said and written about IP issues in China. What are the major ones?

Wang: Undoubtedly, China has made major improvements to its IPR protection, especially since joining the WTO. However, enforcement and practical issues remain daunting tasks.

One in particular concerns the increasing technological sophistication of some of the Chinese companies engaging in infringing activities. Some alleged infringers have become more advanced technologically and are moving away from the simple counterfeiting of the past and into a new level. They either make non-substantial modifications of others or copy patents of others directly, making the alleged infringing products functionally the same as the genuine products and often with similar quality. Only several years ago, when I first began to address the problem, the counterfeit product, at least on the surface, appeared identical to that produced by the owner of the patent. Closer inspection invariably indicated that it was of very poor quality. As Chinese companies have accumulated expertise and wealth, however, they are moving to carefully analyze the products of Western companies and the patents that purportedly protect them. From time to time they have the ability to design around those patents, which is entirely legal, but they are also often able to copy the product directly, at a level of sophistication that was not part of this process in the past. This means that a high-quality close copy of the product is available to the consumer at a much lower price. This puts considerable competitive pressure on the Western company that owns the patent. If it has failed to file for its patent rights in China, it finds itself on the defensive.

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China has three types of patent. The invention patent is substantially similar to a U.S. utility patent. It is the only one that is substantively examined by the Chinese Patent Office ("CPO") and it can take three to five years or longer to grant. The utility model and design patent, however, are *not* substantively examined by the CPO, and they are granted usually within 10 months. A literal copy of a Western patent can be filed in China as either a utility model (excluding process claims) or design patent (where applicable) and will be granted as a certainty as a Chinese patent. It remains valid until challenged, and challenging such a patent is often difficult. We continue to handle cases with the same general factual pattern: a foreign company enters into a joint venture with a Chinese company, and one of the principal assets of the foreign company is patents. The joint venture does not prosper, and at a certain point it is dissolved. The local employees of the venture then join a local enterprise – often one funded by the state – or they set up their own company, and in either case the intention is to compete with the foreign company. The local employees are quick to file for Chinese utility or design patents, very often utilizing without any amendment or revision whatsoever the drawings or specification of the owner of the original patent. The Western company, when it discovers the new competitor, then files or threatens to file a law suit and is immediately met with a counterclaim for infringement of the Chinese utility or design patent. On the other hand, the Western company's invention patent, if filed at all, is still pending before the CPO.

China has a two-track patent dispute resolution process. The first track is the Chinese Patent Re-examination Board ("Board"), which only handles patent validity issues. That is, the Board will examine a patent to determine whether it is valid, but it is the Chinese IPR courts which have the power to rule on infringement, not validity. *Neither* the Board nor the courts will consider the issue of bad faith. That means that a foreign company may be faced with a counterfeiter who has filed a utility patent which is a virtual copy of the company's product, and the infringer can sue the otherwise rightful owner in court. Because the court can *only* rule on the issue of infringement, and since the two products are virtually identical, it is likely that the court will find for the counterfeiter unless the foreign company can successfully stay the suit. While the court case is underway, the foreign company will be attempting to invalidate the counterfeiter's patent before the Board. Normally that takes longer than the concurrent court infringement case, so unless the foreign company can persuade the court to issue a stay pending resolution of the validity issue (the stay is not guaranteed), the odds of losing the case are good. Even if the Board ultimately rules that the counterfeiter's patent is invalid (which may be appealed twice), two years or more may have passed and there is a good chance that the market opportunity has been lost.

This situation could have been largely obviated however, *if* the foreign company had filed a Chinese patent simultaneous to its U.S. filing. In addition, if it had filed for a Chinese utility patent (where applicable) when filing for a Chinese invention patent, the rapid issuance of the former would have served to gain patent protection and close the loophole. Part of the problem is that foreign companies often do not realize that China is a first-to-file system, not a first-to-invent. Many U.S. companies do not realize that, when their U.S. filings are published at the 18th month, these applications will be carefully reviewed by potential infringers and may even be duplicated or slightly modified and then filed in China as utility patents for non-process claims, which are usually one step ahead in this game.

Editor: How serious are these issues as threats to economic growth and foreign direct investment?

Wang: A problem like this cuts both ways. It is a threat to foreign investment because foreign companies are becoming increasingly frustrated at being defendants in the fact pattern I have described. It is also a frustrating situation for Chinese companies because the counterfeiters do not discriminate between domestic and foreign owners of patents in deciding what to appropriate. If Western companies have suffered more than their Chinese counterparts, it is only because they have more innovations at the present time. This will change as the Chinese companies become more technologically advanced.

With respect to foreign investment, many Western companies are concerned about the types of investment to be made in China, especially with respect to pharmaceutical products, which normally take a long time to enter into the market. This is having a dampening effect on companies bringing their technology into the Chinese market.

While in the U.S. the holder of a patent for a new drug is protected from anyone copying it for a period of time, some Chinese drug manufacturers, however, may still believe that a copy is acceptable or economically justified so long as it does not bear the name or trademark of the patent holder. This is also causing considerable difficulty for the foreign pharmaceutical companies operating in China.

Editor: What common misconceptions about IP in China do foreign companies have?

Wang: One common misconception is that since counterfeiters do not respect IP rights, there is no reason to file patents in China. With the increasing volume of domestic company filings, if you do *not* file your patents in China, the likelihood of their being copied is greater, not less.

A second misconception is that only invention patents should be filed in China. In fact, the utility patent – which is not examined and is quickly granted – should also be filed when economically feasible. Once granted, it may serve as a weapon against the counterfeiters. It is important to be proactive here, and not merely reactive.

Editor: If a company has failed to take preventative action, are there still remedies available?

Wang: Yes. We recently had a case where a client in the power industry had a product that was making considerable money in China. One of their major European customers called to thank them for making the product cheaper in China. Since they did not have a manufacturing operation in China at that time, they called upon us to investigate. Of course, we found a counterfeit operation underway and we subsequently raided the counterfeiter only to find we were unable to obtain an administrative penalty letter that would have enabled us to bring a court action for an injunction and damages (we believe someone at the local government agency had been unduly influenced). We filed an administrative action against the local agency, which immediately resulted in the issuance of the requisite letter, backdated. I hasten to add, this was a very complicated process, and we also had to invoke the aid of both the U.S. Embassy and the U.S. Congress before achieving the desired result. Further, the fact that the infringer was a state-owned company also added difficulty to the process.

Editor: Is it realistic to believe that violators will pay damages and fees?

Wang: In China there are no consequential or punitive damages, and the maximum statutory award is very low compared with Western standards. Western companies which choose to litigate usually do not expect for big damages. The real victory here still lies in obtaining an injunction to stop future counterfeiting.

Editor: Is there anything that you would like to add?

Wang: During the past twenty years China has come a very long way. At the beginning of the process the state owned everything, and only in 2004 was an amendment to the Constitution adopted which serves to protect private property. I believe that most recently IPR protection has been driven by the fact that the government realizes its dominance in manufacturing cannot be based solely on the low cost of labor. As living standards have risen, so have labor costs. The government understands that the country's future lies in Chinese companies engaging in R&D work and becoming exporters of technology, something that requires effective protection of IPR and enforcement of the property rights of the owners of IP. In the interests of both domestic and foreign industries, the Chinese government has made significant strides to improve IPR protection especially during the past three years since China's accession to the WTO. Improvement is undeniable. China will be no different from any other major market, where your IP portfolio will largely decide where you stand.

Please email the interviewee at xiangwang@jonesday.com with questions about this interview.