

***CHINA – MEASURES AFFECTING THE PROTECTION AND
ENFORCEMENT OF INTELLECTUAL PROPERTY RIGHTS***

(WT/DS362)

**EXECUTIVE SUMMARY OF THE SECOND SUBMISSION OF
THE UNITED STATES OF AMERICA**

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I. INTRODUCTION

1. This submission will show how China's arguments in its First Written Submission, Oral Statement at the First Panel Meeting, and Responses to the Panel's Questions fail to rebut the demonstration in the U.S. first submission that China's measures in certain areas are inconsistent with its obligations under the TRIPS Agreement.

II. CHINA'S THRESHOLDS FOR CRIMINAL PROCEDURES AND PENALTIES FOR TRADEMARK COUNTERFEITING AND COPYRIGHT PIRACY ARE INCONSISTENT WITH CHINA'S OBLIGATIONS UNDER ARTICLES 61 AND ARTICLE 41.1 OF THE TRIPS AGREEMENT

2. The United States has met the burden of proof by successfully demonstrating that China's measures are inconsistent with China's obligations under the first and second sentences of Article 61 and Article 41.1 of the TRIPS Agreement. The United States, and a number of third parties, have provided numerous concrete illustrations of how China's thresholds permit wilful trademark counterfeiting and copyright piracy on a commercial scale to exist. China has not disputed that acts of "wilful trademark counterfeiting and copyright piracy" occur in many cases without triggering these criminal thresholds, and as the U.S. has demonstrated, China does not provide criminal penalties and procedures for many of these acts that are "on a commercial scale."

A. Article 61, first sentence, of the TRIPS Agreement

3. The obligation in the first sentence of Article 61 is comprised of a number of elements. China "shall provide for" criminal procedures and penalties "to be applied" "at least" in cases of "wilful trademark counterfeiting and copyright piracy" "on a commercial scale." China observes that the core aspect of this claim is the meaning of the term "on a commercial scale." The United States agrees and has provided an interpretation for "commercial scale" that accords with the customary rules of interpretation reflected in the *Vienna Convention*.

4. The U.S. explanation of the term "commercial scale" is set out in detail in the U.S. first submission. In particular, two features emerge from the ordinary meaning of the term. First, by using the term "commercial *scale*," the TRIPS Agreement makes clear that WTO Members must criminalize acts of infringement that reach a certain extent or magnitude. Second, in using the term "*commercial scale*," the TRIPS Agreement draws a link to the commercial marketplace – where business-minded IPR infringers take the fruits of their counterfeiting or piracy. Thus, it is clear that the ordinary meaning of "commercial scale" extends to those who engage in commercial activities, including manufacturing, distribution, and retail sales.

5. China claims that the U.S. position is that commercial scale only means commercial purpose. That is demonstrably not the U.S. view. That said, an infringer seriously engaged in pursuing financial gain in the marketplace is *necessarily* acting on a "scale" that is "commercial," and therefore falls within the ordinary meaning of the term. However, the meaning of the term "commercial scale" does not depend on the intent of the infringer. An infringer with a different intent may or may not be acting on a "scale" that is "commercial."

6. China also alleges that the United States wrongly interprets the ordinary meaning of the term "commercial scale" by looking at the meaning of the individual words "commercial" and "scale."

However, that is a completely acceptable method for interpreting a term and is similar to that followed by past panels and the Appellate Body.

7. China invites the Panel to ignore the ordinary meaning of “commercial scale,” as explicated by the United States, and instead substitute a concept that China has labeled “significant magnitude of activity” which is not consistent with the *Vienna Convention* customary rules. *First*, China’s proposed interpretation is at odds with the ordinary meaning of “commercial scale.” Its reads “commercial” out of Article 61, by essentially replacing “commercial” with “significant” and further, the word “scale” means a “*certain* extent or magnitude,” not a “*significant* extent or magnitude.” While China claims that its proposed meaning derives from “common usage” and from “statements of the TRIPS negotiating parties,” China provides no evidence that the Uruguay Round negotiations distilled any sort of prevailing understanding of “commercial scale” from the unrelated sources cited by China. These isolated references are clearly insufficient to constitute any sort of “common usage.” In these other sources, where “commercial scale” is used in the context of “production” or “manufacturing” there is no suggestion that “commercial scale” would not apply to other acts – for example, retail sale. Further, Article 61 does not contain references to “manufacturing” or “production” – it refers instead simply to “counterfeiting” and “piracy.”

8. China’s reliance on a 1988 WIPO Committee of Experts on Counterfeiting and Piracy document and accompanying discussions does not provide support for its proposed interpretation of Article 61 on numerous grounds. First, it is unclear what status this document has under the *Vienna Convention* – as China has not argued that it should be taken into account pursuant to Article 31 or Article 32 of the *Vienna Convention*. In fact, this WIPO document does not constitute an appropriate “supplementary means of interpretation” within the scope of Article 32 of the *Vienna Convention* for many reasons. The WIPO Committee proceedings were independent of the TRIPS negotiations, there was no consensus on the document, and the WIPO Committee of Experts (much less the country members of WIPO) did not adopt the document China has cited.

9. Even assuming that the document could be considered as a “supplementary means of interpretation,” the normal application of the *Vienna Convention* principles to the term “commercial scale” does not leave its meaning “ambiguous or obscure” or leads to “manifestly absurd or unreasonable results.” Therefore, it could only be properly used to confirm an interpretation reached by means of the rules in Article 31 of the *Vienna Convention*.

10. In this context, the WIPO document serves to confirm the U.S. interpretation, as it underscores the U.S. view that the scope of commercial scale cannot be reduced merely to a value or volume metric. Instead, a variety of open-ended factors would need to be taken into account: including the “circumstances” surrounding the manufacture, as well as “the will to make a profit” and the way that the goods “are intended to be used,” in addition to the “quantity of goods.” China’s rigid and high numerical thresholds is far from these open-ended set of factors. The United States, supported by a number of third parties, believes that a range of quantitative and qualitative factors should be taken into account to ensure that all “commercial scale” activities are subject to this discipline.

11. Furthermore, the WIPO Committee’s “definition” of “commercial scale” did not form the basis of the negotiations on TRIPS Article 61. There was no “definition” adopted by the WIPO Committee; and even though China is correct that the WIPO Committee’s Model Provisions were brought to the attention of the TRIPS negotiation participants, the particular concept of “on a commercial scale” in Article 61 emerged in the TRIPS negotiations. The focus of the initial discussions cited by China differs sharply from the context in which the term “commercial scale” ultimately was used by the TRIPS negotiators, i.e., to define which acts of trademark counterfeiting and copyright piracy must be subject to criminal procedures and penalties.

12. China also fails in its attempt to use the WIPO document as support for its efforts to limit the scope of Article 61 to only “larger-scale” activities such as the manufacture of infringing goods. Nothing in the ordinary meaning of “commercial” implies that it is limited to the industrial context. Had the TRIPS negotiators intended the obligations to apply only to industrial-level production, they presumably would have used the term “industrial scale” and not commercial scale. In any event, the reference to “manufacturing on a commercial scale” was not included in the final text of Article 61. The omission of “manufacture”– where it was present in the WIPO document – tends to confirm that other commercial activity, such as retailing and wholesaling, is included in the meaning of “on a commercial scale” in Article 61. Furthermore, the document also provides that retail sale can also be an act of counterfeiting or piracy, referring back to the principles in the manufacturing section to incorporate the concept of “commercial scale” into the retail context.

13. The WIPO Committee discussions also do not provide support for China’s proposed interpretation of “commercial scale” as “broad and flexible standard.” China’s arguments is misplaced to the extent that China is claiming that this discussion demonstrates a consensus for variable meaning to this term as used in Article 61, or provides a basis for China not to comply with the obligation in that Article. The meaning of this term in Article 61 is clear and its application is uniform across all WTO Members.

14. *Second*, China’s purported context for interpreting Article 61 is also unavailing. China’s argument that Articles 1.1 and 41.5 allow China to define for itself the obligations of Article 61 is contrary to plain text of these provisions. First, as made clear by the text of the final sentence, Article 1.1 deals with the *method* by which a Member implements TRIPS Agreement obligations, not *whether or to what extent* a Member should implement them in the first place. While during the TRIPS negotiations, WTO Members expressed diverse views on various draft provisions of the TRIPS Agreement, the negotiators coalesced around the final text of the TRIPS Agreement. The first sentence of Article 1.1 states that Members shall “give effect to these provisions” and therefore because Article 1.1 does not alter the obligations in Article 61, China must implement Article 61 in a manner that reflects its terms.

15. Likewise, Article 41.5 deals with the implementation of a Member’s Part III enforcement obligations, not the substance of the obligations themselves. The thrust of the second sentence of Article 41.5 concerns the distribution of enforcement resources between the enforcement of the law in general and the enforcement of intellectual property rights. Article 41.5 does not provide an exception or affect the scope of the substantive obligations of Article 61. The United States is not

arguing that China should alter how China enforces its laws in general; rather, the United States argues that China's criminal thresholds fall short of the minimum standards in Article 61.

16. Whether China chooses to actually prosecute relatively smaller cases of wilful trademark counterfeiting or copyright piracy “on a commercial scale” is not at issue in this dispute. Consequently, the level of resources China chooses to dedicate to such prosecution is, from the perspective of the legal claims in this dispute, beside the point.

17. China's other contextual arguments for “commercial scale” are similarly unavailing. China's arguments that the TRIPS Agreement and Berne Convention “do not set forth a definition of infringement” are simply beside the point because the United States does not claim in this dispute that, leaving aside the thresholds, there are substantive types or categories of acts constituting “wilful trademark counterfeiting or copyright piracy” (as those terms are used in Article 61) for which China has failed to make criminal procedures and penalties available under Articles 213, 214, 215, 217, and 218. Rather, it is that China does not make them available for all acts of “wilful trademark counterfeiting or copyright piracy” that are “on a commercial scale.”

18. Furthermore, China's accusation that the U.S. is “impos[ing] a fixed, concrete international standard” of “commercial scale” is also misplaced. Establishing an obligation concerning the minimum enforcement provisions of WTO Members must have in place is precisely what the TRIPS Agreement does. Additionally, China's assertions that Article 61 lacks “specificity” gain China no ground. No amount of comparison to other provisions in the TRIPS Agreement and other WTO Agreements assist China in escaping the requirements of Article 61.

19. *Third*, China's claims regarding the object and purpose of the TRIPS Agreement are unavailing. A fair reading of the Preamble does not support China's position. Moreover, giving meaning to Part III of the TRIPS Agreement, including Article 61, is not “harmonizing” legal systems. China is free to provide an enforcement regime consistent with, for example, systems in effect in countries of the “civil law” traditions.

20. *Fourth*, China's resort to the subsequent actions of Members provisions do not provide any evidence of “subsequent practice in the application of the treaty” under Article 31(3) of the *Vienna Convention* establishing any agreement by WTO Members regarding the interpretation of Article 61. The provisions of U.S. free trade agreements are not relevant to this Panel's interpretation of the covered agreement, i.e., the TRIPS Agreement. Similarly, China fails in its attempts to claim that practices by certain third parties to the dispute are some type of “subsequent practice” within the meaning of the *Vienna Convention*. These claims are refuted by those third parties.

21. *Fifth*, China also hints at the argument that “commercial scale” might have a special meaning provided for under Article 31(4) of the *Vienna Convention*. However, there is no evidence, either in the Chinese submissions or elsewhere, of a “special meaning” for “commercial scale.”

22. *Sixth*, China's reliance on the negotiating history of the TRIPS Agreement is also unavailing. For the reasons stated above, China's claims that the negotiating record of the TRIPS

Agreement provides confirmation for its view of the “commercial scale” standard (“counterfeiting and piracy of a significant scale”) is incorrect and supports the U.S. position.

23. Finally, China’s arguments that deference to its criminal law should also be disregarded. China’s arguments amount to an invitation to the Panel to abandon the treaty interpretation principles that WTO Members have agreed shall govern this Panel’s work. These arguments regarding the special nature of criminal law have no bearing on the core question: whether China has fulfilled its obligations under Article 61. When China became a WTO Member, it also agreed to ensure that its criminal laws against piracy and counterfeiting meet the standards in the TRIPS Agreement. Furthermore, while China urges the Panel to take into account “*in dubio mitius*,” in this case, there is no need to rely on this concept, as the meaning of “commercial scale” is reached through the general rules of interpretation reflected in Article 31 of the *Vienna Convention*.

B. Contrary to Article 61, China’s Measures Fail to Provide Criminal Procedures and Penalties for Wilful Trademark Counterfeiting and Copyright Piracy on a Commercial Scale

24. China’s criminal thresholds create a safe harbor, preventing criminal procedures and penalties from being available for all instances of commercial scale counterfeiting and piracy. Instead of denying this core safe harbor problem, China attempts to disagree with the *degree* but not the *reality* of the inconsistency. The first fundamental problem with China’s thresholds is that they do not permit prosecution or conviction of infringing activity involving values or volumes below the thresholds but that are still “on a commercial scale.” At no point does China claim that criminal prosecution or conviction under Articles 213, 214, 215, 217, and 218 is possible for any trademark counterfeiting or copyright piracy below the thresholds themselves. Indeed, China does not rebut the core issue raised by the U.S. with respect to the Article 61 claim: that if a case fails to meet at least one of the thresholds, that fact will preclude criminal prosecution and conviction.

25. China takes a different tack: it attempts to whittle away at the size of the safe harbor. First, China seizes on certain U.S. explanations regarding the nature of the thresholds and attempts to show that “commercial scale” activity can be captured in some circumstances. However, the application of *any or all* of the alternative thresholds still leaves much commercial-scale piracy and counterfeiting immune from criminal prosecution or conviction. Furthermore, China concedes that in calculating certain thresholds the price of the legitimate good is used by courts only as a last option. This valuation methodology exacerbates the safe harbor problem by creating a larger safe harbor than would exist if China used a methodology based on the prices of legitimate goods.

26. Second, China takes issue with the U.S. characterization of the operation of the thresholds and mistakenly appears to argue that the provisions concerning the calculation of the thresholds under the measures at issue should not be subject to scrutiny under Article 61. What China calls “evidentiary” standards are, in fact, relevant to whether China meets the Article 61 obligation: they cause “criminal procedures” and “criminal penalties” not to be “applied” in some cases of wilful trademark counterfeiting and copyright piracy. Indeed, China’s thresholds provide a substantial safe harbor *capable* of sheltering commercial operations, thus inviting counterfeiters and pirates to structure their commercial operations in a way take advantage from the thresholds.

27. China's arguments about the operation of the thresholds, including that the thresholds can be calculated over a prolonged period of time and can count goods in other warehouses, likewise do not overcome the U.S. case. First, Article 12 of the December 2004 JI makes clear that the values of "illegal business volume," "illegal gains" and "amount of sales" can only be cumulated if engaging in such acts has not resulted in the imposition of an administrative penalty or criminal punishment. China admits that the imposition of administrative penalties is often its preferred remedy. Second, the "illegal business operation" threshold is structured so as to exclude many cases of "commercial scale" piracy and counterfeiting – regardless of whether goods at other warehouses or in transportation can be counted.

28. The second set of problems with respect to China's thresholds stems from the fact that Chinese authorities must rely on a very limited set of one-size-fits-all numerical tests. A range of considerations should be probative of "commercial scale," but China's rigid criminal thresholds preclude their use; the thresholds fail to reach some classes of commercial-scale piracy and counterfeiting not only because of their magnitude, but also because of what they do – and do not – measure. The thresholds do not measure reliable indicia of a commercial-scale piracy or counterfeiting operation, such as "worn molds" for pressing pirated products or counterfeit marks or other materials and implements of such an operation.

29. China argues around the issue of whether its thresholds can reach beyond the metrics of "illegal business volume," "illegal gains," "amount of sales," or "copies" to capture cases of commercial-scale piracy and counterfeiting that are probative of "commercial scale" but do not neatly fit under these categories. First, while China claims that criminal measures are available for the crimes of attempt and preparation, this does not address the concerns of the United States. Worn molds and similar reliable evidence would be evidence of a completed crime; that is, the worn mold supports the conclusion that commercial-scale infringement *already has* occurred. Attempt and preparation are "inchoate" or uncompleted crimes and despite the probative value of this evidence for proving a particular completed crime, evidence such as worn molds, which are implements used to commit the crime, unfinished products and non-infringing packaging is not cognizable under the metrics of China's thresholds.

30. But even if certain near-finished products can be counted against the thresholds in some cases, China's arguments still miss the point. Its thresholds will still exclude commercial-scale piracy and counterfeiting. For example, 499 unfinished copies of a video game not yet bearing an infringing trademark still qualify as evidence of a "commercial scale" operation, just as much as 499 finished video games bearing such a trademark. Further, contrary to China's assertion, the cases included in China's First Written Submission that involved conviction under the crime of "attempt" only involved convictions based on "unsold" but finished products and did not involve a situation where unfinished products or non-infringing packaging were used by the court for that conviction. Additionally, the cases that China claims counted "unfinished" goods do not assist China: the reasoning in the first case, involving washing powder, is quite confused, and the case appears to be an outlier and the second case involving game cartridges, is inapposite, and the case did not involve the Article 213 thresholds established by the December 2004 JI.

31. China also does not rebut the conclusions reached in the CCA Report on actual enforcement efforts. Rather, China argues that the “statistical trends” from the data are not meaningful and that “the U.S. has failed to present the correct conclusions from the data.” Contrary to China’s assertions, the United States does not advance any predictive theories from the CCA Report. The CCA Report is a compelling empirical study that pulls together raw data from actual conduct that occurred in the past. The conclusions are plain to see: the vast majority of traditional retail outlets selling recorded music and/or home video products – a classic example of commercial scale activity – faced no possibility of criminal prosecution or conviction under China’s criminal thresholds.

32. China’s attempts to cast doubt on the conclusions from the empirical study are unpersuasive. Rather than focus on the below-the-thresholds data at the heart of this dispute, China instead focuses on trying to construct a U.S. “hypothesis” based on activity happening above the thresholds – activity which is by definition criminalized and not the subject of this dispute. Moreover, China’s argument that there is no “dramatic shift” in infringing activity between the two time periods simply misses the point. Despite the lower 500 copy threshold that was in effect during the second time period, piracy and counterfeiting continued to flourish in the safe harbor below the thresholds.

33. China’s criticism of other U.S. exhibits, such as articles in newspapers and magazines that illustrate the safe harbor problem is puzzling, as when the United States attempted to obtain information from China pursuant to TRIPS Article 63.3, China declined to provide information but stated that relevant information was publicly available through official websites, newspapers, magazines, and other proper channels.

34. Based on its flawed interpretation of Article 61, China attempts to justify its TRIPS-inconsistent regime and asserts that it has “imposed criminal penalties for wilful infringement that involves a *significant magnitude of activity*” (its erroneous interpretation, emphasis added) that is (a) appropriate within the legal structures of China, and (b) appropriate within the commercial context of China. These arguments are without merit.

35. *First*, whether China’s criminal IPR thresholds are appropriate within the context of China’s domestic law is irrelevant. What China chooses to do with its domestic *non-IPR* criminal thresholds has no bearing on this Panel’s assessment of whether China meets its international obligations under the first sentence of *Article 61 of the TRIPS Agreement*. China appears to confuse its ability to determine what constitutes a “commercial crime” in its domestic law with its obligation to comply with the first sentence of TRIPS Article 61. In this dispute, the United States is seeking to ensure that a criminal law regime is in place where Article 61 requires China to have one (and where China, at the moment, does not).

36. *Second*, China’s arguments that its thresholds are reasonable “in terms of the scale of commerce in China” fail to withstand scrutiny. China neither explains nor justifies how the boundaries of criminal liability that China has chosen in fact capture all counterfeiting and piracy that is “on a commercial scale” under Article 61. China’s thresholds are not appropriate to the scale of commerce in China, as they miss many types of “commercial scale” activity and offer one

size for all cases; they do not accommodate the realities of the marketplace. Further China's statistics regarding the purported reasonableness of its "illegal business operation" threshold concedes that there is some "commerce" that falls below the thresholds and they do not shed any real light on the scope and scale of commerce in China.

37. The inappropriateness of China's thresholds is borne out by other illustrations including Canada's citation to China's estimated per capita gross domestic product. It is clear that "commercial scale" counterfeiting and piracy is not limited to large-scale or industrial-scale enterprises – on the contrary, the growth of the Internet and digital technological advancements permit commercial-scale piracy and counterfeiting to occur with a computer in a small space. While China also argues that it does not have an obligation to consider the "commercial impact of the intellectual property infringement when setting its thresholds," advances in digital technology and the Internet, among other market conditions, enable piracy and counterfeiting to take place in situations that escape the reach of China's thresholds, even though they can have a large (and commercial) impact and are on a large (and commercial) scale.

38. China's other arguments regarding the implementation of Article 61 are unavailing. First, China's arguments regarding the ability of private parties to bring prosecution of certain criminal acts are of little relevance to the Panel's consideration of whether China's criminal thresholds are consistent with China's obligations under Article 61. China's assertion that lowering its thresholds "could unleash a large volume of private enforcement actions" is unsubstantiated. Second, China's administrative enforcement regime has no bearing on whether China meets the obligations of the first sentence of Article 61. Part III of the TRIPS Agreement deals with a number of enforcement procedures. Section 2 pertains to "Civil and Administrative" procedures and Section 5, where Article 61 can be found, pertains to "Criminal" procedures. It is notable that Article 61 is the only provision that focuses on criminal penalties and procedures. Conversely, that also means that only criminal penalties and procedures can fulfill the obligations in Article 61.

C. China's Criminal IPR Thresholds Are also Inconsistent with Article 61, Second Sentence and Article 41.1 of the TRIPS Agreement

39. The United States has also demonstrated why China's criminal IPR thresholds are also inconsistent with the second sentence of Article 61 and Article 41.1. China acknowledges that if the Panel finds that China's criminal IPR thresholds are inconsistent with the first sentence of Article 61, it must also find an inconsistency with the second sentence of Article 61 and with Article 41.1.

III. CHINA'S MEASURES FOR DISPOSING OF CONFISCATED GOODS THAT INFRINGE INTELLECTUAL PROPERTY RIGHTS ARE INCONSISTENT WITH CHINA'S OBLIGATIONS UNDER ARTICLE 59 OF THE TRIPS AGREEMENT

A. Article 59 of the TRIPS Agreement

40. Article 59 provides in pertinent part that the "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.” For the purposes of this dispute, the relevant authority needed under Article 59 is detailed in two sentences in Article 46. Read together, Article 46 and Article 59 require, first, that a Member’s competent authorities for border enforcement “shall have the authority to order that goods that they have found to be infringing be disposed of outside the channels of commerce in such a manner as to avoid any harm caused to the right holder, or, unless this would be contrary to existing constitutional requirements, destroyed.” Second, “[i]n regard to counterfeit trademark goods, the simple removal of the trademark unlawfully affixed shall not be sufficient, other than in exceptional cases, to permit release of the goods into the channels of commerce.”

41. China advances a number of arguments that would minimize China’s obligations under Articles 46 and 59. These arguments are without merit. *First*, China’s arguments that Article 59 does not require that Members provide a broad grant of authority to agencies and that China’s regime simply “stipulates conditions and sequencing for its exercise by domestic agencies” are unavailing. Article 59 plainly requires full authority to be granted to dispose of or destroy confiscated infringing goods in accordance with the principles of Article 46. The broad scope of Article 59 authority regarding infringing goods confiscated by border authorities is clear from the absence of any restrictions on this authority in Article 46. China Customs should have the *power* to choose among any legitimate options for dealing with these goods – in accordance with the principles of Article 46 – from the outset when the goods are found to be infringing, and thereafter until the goods are finally dealt with.

42. China’s attempts to use TRIPS Article 1.1 to argue for the acceptability of its rigidly constrained disposal regime are unavailing as Article 1.1 does not exempt China from complying with these provisions of the TRIPS Agreement. China’s references to other Members’ copyright and trademark laws are similarly misplaced as this dispute concerns China’s measures, not other Members’ laws, and further, substantively, these laws do not resemble in any respect the problematic disposal hierarchy used by China.

43. *Second*, China also points to China Customs statistics showing the disposition of confiscated goods found to be infringing. Those figures, however, provide no response to the U.S. claim; the United States is not arguing that the TRIPS Agreement obligations *require* China to destroy or dispose of all such goods in accordance with the relevant principles of Article 46.

44. *Third*, China’s argument that the Article 46 principle to “avoid any harm caused to the right holder” only obliges China to “pay due regard to potential harms to the right-holder and to refrain from disposition methods that consistently or significantly harm the right-holder’s interests” is contrary to the meaning of the provision. The obligation is not to “pay due regard” to the interests of a right holder and to tolerate intermittent or “non-significant” harm. The standard requires avoiding any harm to the right holder. Indeed, the definition China itself cites for the word “avoid” is “to keep away or refrain from; *prevent from doing or happening*.”

45. *Fourth*, China’s argument that the final sentence of Article 46 is not incorporated into Article 59 is at odds with the text of Article 59. There is no limiting language in Article 59 that would selectively incorporate only the obligations in the first sentence of Article 46. If the

negotiators of the TRIPS Agreement had intended to carve out specific obligations in Article 46 from being transposed to Article 59, they would have done so.

46. Additionally, China’s claim the principle in the last sentence of Article 46 only means that the “removal of the trademark is not sufficient” to permit this release is contrary to the language of Article 46, last sentence. China misreads the relationship between the phrases “removal of the trademark unlawfully affixed shall not be sufficient” and “exceptional cases.” The phrase “other than in exceptional cases” means that only in exceptional cases may the competent authorities “permit release of the goods into the channels of commerce.” Moreover, while China further claims that it complies with the purpose behind this principle, since China Customs removes all infringing features from the goods and takes other steps, the TRIPS Agreement does not provide for Members to only comply with what they identify to be a “purpose” behind a provision.

B. Contrary to Article 59, China’s Customs Authorities Do not Have the Authority to Order the Destruction or Disposal of Infringing Goods in Accordance with the Principles Set out in Article 46

47. Article 30 of the Customs IPR Implementing Measures, which implements Article 27 of the State Council Customs IPR Regulation and binds Customs officials across China, sets out a compulsory sequence of steps that Chinese Customs must follow in deciding how to treat goods seized at the border that it has determined infringe intellectual property rights. While China claims that its Customs authorities have the “discretion” not to follow the prescribed steps in the hierarchy, the essential point in the U.S. claim is that in circumstances where Customs makes a certain determination under its measures, it is compelled to follow the option set forth in the hierarchy. And in those circumstances, China Customs lacks the authority that the TRIPS Agreement requires to opt for destruction or disposal in accordance with Article 46 principles.

48. China also asserts that its rigid disposal regime somehow does not strictly constrain Customs officials’ scope of action, because other generally applicable Chinese laws regarding such matters as safety also govern Customs authorities’ decision making. However, in response to panel questions, China specifically concedes that Chinese Customs officials must make particular findings under its disposal regime, and once they have made them, they have no discretion as to their acts.

49. Neither alternative in the initial step of China’s mandatory hierarchy – donation or sale to the right holder – meets the principles of Article 46. China Customs’ donation of infringing goods to “public welfare organizations” under the measures at issue does not provide Customs with the authority to dispose of the confiscated goods “outside of the channels of commerce in such a manner as to avoid any harm caused to the right holder.” First, while China claims that its Customs authorities only donate goods suitable for public welfare purposes, these standards would not prevent donation of usable but likely lower-quality counterfeit or pirated products that would be used by potential consumers of the genuine article and also could harm the right holder’s reputation. Accordingly, the donation option in China’s measures is inconsistent with the Article 46 principle concerning harm to the right holder.

50. Second, while China states its legal obligation to supervise the use of the donated goods ensures that they will not return to commerce, Article 17 of the Law on Donations specifically authorizes public welfare organizations to sell donated goods on the market if certain circumstances are present. While the Red Cross Memorandum does contain a provision obligating the Red Cross to “take effective measures . . . entering into the channels of commerce,” at the same time, the Law on Donations makes clear that donee organizations are not required to enter into these kinds of agreements, and when no agreement is in place, Chinese authorities have offered no legal argument that they can override the provisions of Article 17. Accordingly, for that reason, China is not meeting its obligations under Articles 59 and 46.

51. While China points to Article 18 of the Law on Donations in an attempt to dismiss the relevance of Article 17, selling the goods under Article 17 and ensuring the resulting funds continue to be put to the “use” prescribed in the donation agreement appears, on its face, to be an action consistent with the mandates of Article 18. Likewise, a general contractual commitment such as in the Red Cross Memorandum would not override rights provided under a national law.

52. Furthermore, China’s claim that Article 30 of the Customs IPR Implementing Measures renders the resale option under Article 17 of the Law on Donations “null” is unavailing. Article 30 governs Customs’ donations to a public welfare organization and Article 17 governs the donees’ disposal of such goods after the donation, when the circumstances presented in Article 17 arise.

53. The second option at the initial step in China’s disposal hierarchy, which allows Customs to sell the infringing goods to the right holder, does not permit disposal “in such a manner as to avoid any harm caused to the right holder,” as Article 46 requires. In situations where donation is not appropriate, China’s measures require Chinese authorities to offer the infringing goods for sale to the right holder. If right holders pay for infringing goods to ensure that they are destroyed or removed from the channels of commerce (such as, for example, by public auction), financial harm will result in the form of the payment. While China argues that the required efforts to sell infringing product to the right holder advance right holder’s interests, this argument is without merit. It requires the untenable assumption that right holders are eager to buy extra product they have not ordered and whose production is outside the terms of their contract.

54. Where the transfer to a public welfare organization is unavailable, and the right holder does not elect to purchase the infringing goods, the Customs authorities must turn to the next compulsory step involving the public auction of the confiscated goods. China’s public auction process for these goods likewise does not comport with the Article 46 principles incorporated into Article 59.

55. Because China’s mandatory procedures strip Customs of the authority to prevent auction when this option becomes operative in the Customs hierarchy, the procedures are inconsistent with the first sentence of Article 46. A mandated auction under China’s measures also precludes Customs from having the authority to destroy these products. While China argues that Article 59 does not obligate China to limit its customs agencies to disposal outside the channels of commerce, the U.S. claim concerns the scope of authority under Article 59. Because China’s mandatory public

auction procedure does not permit China Customs to act in accordance with the Article 46 principles, it is inconsistent with China’s obligations under the TRIPS Agreement.

56. China’s arguments regarding how its public auction procedure avoids harm to the right holder should be disregarded. A public auction can cause great harm to the right holder, since the infringer whose goods have been confiscated can simply purchase the seized goods at the auction, re-affix the infringing features, and proceed to distribute the goods. While China focuses on the impact on the infringer, the Article 46 principle at issue concerns avoiding any harm to the right holder, not assessing the status of the infringer. Moreover, a right holder’s ability to “comment” on China’s measures is not a right to *prevent* the goods from being auctioned, and is not a means to ensure that the authorities act in a manner that avoids any harm to a right holder. Additionally, even if some “safety” concerns will prevent a public auction, in the many cases where the infringing features can be eliminated and the goods do not pose safety concerns, the measures mandate public auction – and thus, entry into the channels of commerce.

57. Further, with respect to counterfeit trademark goods, China’s public auction step is also inconsistent with the principle in the last sentence of Article 46. Simply put, China does not confine its release of these goods into the channels of commerce to exceptional cases. China’s focus on actions such as reserve prices and comments from the right holder are misplaced: the problem is that China’s measures compel public auction if the infringing features of the products can be eliminated, assuming no safety defects.

58. In the final step of the mandatory hierarchy, if no earlier options prove feasible, then and only then, China Customs gains the power to destroy the infringing goods. In other words, this step will not be reached if any of the options higher in priority are available. In these situations, Chinese customs authorities are not, as a matter of Chinese law, authorized to destroy the infringing good (or otherwise dispose of the good in a way that is both outside of the channels of commerce and handled in a manner that avoids any harm to the right holder).

59. China does not deny that China Customs only possesses the authority to destroy the goods when the other options in its disposal hierarchy (i.e., donation, sale to the right holder, public auction) are not available. Indeed, the cases China cites where China Customs destroyed infringing goods do not contradict the mandatory nature of the Customs disposal hierarchy. The text of China’s Customs IPR Implementing Measures state that when certain facts are present, Customs officials have no discretion, i.e., they must dispose of the goods only in the manner stipulated. In each of those circumstances, Chinese customs authorities lack the authority, as a matter of Chinese law, to order the destruction of infringing goods.

IV. CHINA’S DENIAL OF COPYRIGHT PROTECTION AND ENFORCEMENT TO CERTAIN WORKS IS INCONSISTENT WITH THE TRIPS AGREEMENT

60. In its submissions, China admits that it denies copyright protection to certain works whose contents Chinese authorities determine are prohibited by law. Moreover, the National Copyright Administration of China (NCAC) has confirmed that Article 4 denies copyright protection to

“works whose contents are illegal.” Therefore, contrary to China’s obligations under TRIPS Article 9.1 (and the provisions of the Berne Convention referenced in Article 9.1), Article 4.1 on its face denies copyright protection to works that are required to be afforded protection.

61. *First*, Article 4 of the Copyright Law excludes from copyright protection an entire category of works – “works the publication or distribution of which is prohibited by law” – but that exclusion from protection is not permitted by the Berne Convention. Pursuant to Berne Convention Article 2(1) and Article 2(6), China’s Article 4.1 blanket exclusion for certain works is inconsistent with the Berne Convention as incorporated into the TRIPS Agreement.

62. While China asserts that under Article 2 of the Copyright Law, Chinese law “protects copyright from the time a work is created” as “copyright vests upon creation,” China concedes that Article 4.1 denies protection to certain works. Thus, China already admits that *some* subject matter does not receive protection at all since it is denied such protection as a matter of law. While courts and/or competent authorities may *confirm* what is illegal after the fact, such confirmation is not a prerequisite for concluding as a legal matter that content is not protected by copyright. Additionally, Article 2 of the Copyright Law cannot, by the terms of Article 4, apply to certain works. The Berne Convention (or the TRIPS Agreement) does not permit copyright to be extended initially, but then rescinded for the reasons stated in Article 4.

63. *Second*, because Article 4 denies copyright protection to certain works, the exclusive rights enumerated in Article 10 of China’s Copyright Law, and all the protections of the law, are also denied to such works. As a result, Article 4 of the Copyright Law does not comply with the requirements of Berne Article 5(1), which specifies certain guaranteed minimum copyright protection for works, including a minimum set of exclusive rights.

64. China’s attempts to distinguish “copyright” and “copyright protection” are unavailing. The relevant provisions of the Berne Convention provide that China has obligations with respect to “protection” of copyright, thus, the existence of what China calls “Article 2 copyright” – whatever that could mean in the absence of protection under China’s Copyright Law – is not relevant to the analysis of whether Berne Convention-mandated “protection” is afforded.

65. China’s arguments regarding the limited “marketplace effect” of Article 4.1 should be disregarded, as the denial of copyright protection in China has significant real-world impact, including commercial uncertainty for right holders and permitting copyright pirates to profit at the expense of the legitimate rightholder. Furthermore, if right holders cannot enforce their copyright against pirated products manufactured in China, then this deprives them of a critical mechanism for preventing the export of such products.

66. *Third*, the United States has also demonstrated in its first submission that first sentence of Article 4 makes copyright protection subject to a formality that is inconsistent with Berne Article 5(2), and therefore also inconsistent with TRIPS Article 9.1.

67. China’s submissions do not address the U.S. concerns that the impact of content review on copyright protection constitutes a “formality” under Article 5(2). First, while China asserts that copyright protection and content review are separate and that the effect of a content review process does not deny copyright, this is contradicted by China’s own statements. China acknowledges that it maintains pre-publication review with respect to the publication and distribution of certain kinds of works including films and audiovisual products and admits that in certain cases, it does not permit publication until content has been approved. China’s own admissions related to the content review regulations confirm that works that have been found to contain such prohibited content would clearly come under the ambit of Article 4.1, as they are “unconstitutional.” Therefore, by analogy, where pre-publication review is required and publication is prohibited until the completion of a successful review, Article 4 denies copyright to such works. This means that copyright protection is subject to the results of that review – i.e., to a formality.

68. Second, China’s arguments regarding the alleged separation between the content review authorities and NCAC do not accord with the fact that Article 4 of the Copyright Law refers to other laws and regulations in China that prohibit the publication or distribution of works. First, China’s current position does not sit well with the position that China expressed to WTO Members *before* having to respond in this dispute: during the 2002 WTO Review of Legislation in the TRIPS Council, China explained that the copyright denial in Article 4 is the result of prohibitions in other laws, not a separate assessment by NCAC. Second, prominent Chinese copyright scholars writing at the time of the adoption of Article 4 have confirmed that the intended purpose of promulgating Article 4.1 was to deny copyright protection to works for which the publication or distribution of which are prohibited by other laws.

69. Third, the power to interpret Chinese law rests with the Standing Committee of the National People’s Congress. Because the NCAC does not have delegated authority by the Standing Committee, its actions do not represent a definitive interpretation of Article 4, at least with respect to China’s TRIPS obligations to afford civil and criminal remedies for copyright infringements heard by the courts and procuratorate.

70. Moreover, China’s discussion of a NCAC reply in the *Zheng Haijin* case fails to show that the content review process is separate from copyright in the work. The guidance issued by China’s Supreme People’s Court (SPC) in this case appears to demonstrate that the SPC considered that copyright protection was contingent on the work’s successful completion of content review. China’s answer to the Panel’s question regarding this SPC guidance document, however, is confusing. First, China’s response acknowledges that, in the *Zheng Haijin* case, the SPC “endorsed the finding that there was no basis to deny the protection of the copyright law to the work.” If China is stating that the SPC was endorsing a “finding” of the *content review* authority with respect to the *copyright law*, then that confirms the U.S. view.

71. However, if China is suggesting that the SPC was merely endorsing a lower court’s finding, then that suggestion sits very uneasily with what the SPC actually said. The SPC states that “*therefore*” (i.e., for those reasons stated in the document) the lower court’s protection of copyright

was correct. The United Front Department’s review and approval were indispensable to the court’s opinion. Additionally, China’s assertion in its answer that the “not yet been approved for publication” defense would fail is unsupported by the *Zheng Haijin* case, as the case demonstrates that, even where book numbers rather than content are at issue, courts examine the content of a publication before deciding whether or not copyright is protected.

72. China claims that Article 4 “would not remove the “residual copyright under Article 2,” but rather, would “deny the particularized rights of private copyright enforcement” to works that are determined to be prohibited by law. However, Berne Article 5(2) states that both “the enjoyment and exercise of rights shall not be subject to any formality.” Therefore, a content review that affects the exercise of an author’s rights still would impose a “formality” under the Berne Convention.

73. *Fourth*, a consequence of the China’s denial of copyright protection under Article 4 is that the provisions of Chapter V of China’s Copyright Law are unavailable with respect to such works. Therefore, authors of such works do not benefit from the remedies specified in Articles 46 and 47 of this law which provide civil liability (and in some cases, administrative and/or criminal liability) for copyright infringement. Moreover, authors cannot take advantage of other remedies provided by Articles 48 and 49 of this law that, respectively, provide for monetary damages and the ability to seek a court order to stop an infringement that is being committed.

74. China is therefore not in compliance with its obligations under TRIPS Article 41.1. to ensure that enforcement procedures as specified in Part III of the TRIPS Agreement (including those provided by Articles 42, 44.1, and 45.1) are available to copyrighted works in order to permit effective action and expeditious remedies against copyright infringements. Furthermore, because criminal procedures under Article 47 of the Copyright Law are not available at all with respect to works whose distribution or publication in China is prohibited, no criminal procedures or remedies are available when piracy of those works occurs on a commercial scale. China is thus not meeting its obligations under TRIPS Article 61, first and second sentence.

75. Finally, Berne Article 17 does not authorize a content review system that denies enforceable copyright protection (including denial of protection of the rights of reproduction, adaptation, etc.) to all works that have not been approved for publication or distribution. The United States challenges the TRIPS-inconsistent copyright consequences of Article 4.1. That is, the content review measures do not create the TRIPS-inconsistency; rather they provide one important basis for the Article 4.1 denial of copyright protection.

V. CONCLUSION

76. The United States respectfully requests the Panel to find that China’s measures, as set out in the U.S. panel request and discussed in the submissions of the United States, are inconsistent with China’s obligations under the TRIPS Agreement. The United States further requests, pursuant to Article 19.1 of the DSU, that the Panel recommend that China bring its measures into conformity with the TRIPS Agreement.