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

(WT/DS362)

ORAL STATEMENT OF THE UNITED STATES OF AMERICA AT THE SECOND SUBSTANTIVE MEETING OF THE PANEL

JUNE 18, 2008

1. Good morning, Mr. Chairman and members of the Panel. On behalf of the United States, we would like to begin by again thanking the Panel and the Secretariat staff for their time and hard work in evaluating the claims that we have raised in this dispute. Our delegation looks forward to continuing our work with you, and with the delegation of China, as you complete your efforts.

I. Introduction

2. At this point in the proceeding, it is appropriate to take stock of where we are. We have now reviewed China's arguments in its submissions, statements, and responses to the Panel's Questions. This has been helpful in that China has retreated from some of the positions it originally took. At the same time, it is evident that China has failed to rebut our showing that China's measures are inconsistent with China's obligations under the TRIPS Agreement.

3. Our written submissions have already addressed many of the arguments that China has made in this dispute. In this statement, therefore, we will concentrate on those points that China made for the first time – or chose to re-emphasize – in its second written submission. At the conclusion of our statement, we will of course be pleased to elaborate on any of these topics, or to address others that may be of interest to the Panel.

II. China's Criminal IPR Thresholds for Criminal Procedures and Penalties

4. Turning to our first claim, the TRIPS Agreement states that "Members 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." Yet China's laws establish safe harbors from criminal liability for commercial-scale counterfeiting and piracy by prohibiting prosecution or conviction unless a case meets specific quantitative or value thresholds. These thresholds provide infringers a legally certain roadmap that allows them to enter and thrive in the market while escaping criminal sanctions for their commercial-scale IPR infringement.

5. 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. As we have demonstrated, "wilful trademark counterfeiting and

copyright piracy" occur "on a commercial scale" in many cases without triggering these thresholds, and therefore China does not provide criminal penalties and procedures for them.

6. China takes issue with the U.S. approach to the meaning of the term "on a commercial scale," but in fact China continues to misconstrue the U.S. position. In contrast to China, however, the United States has faithfully used the customary rules of interpretation reflected in the *Vienna Convention* to explain the meaning of "commercial scale."

7. The U.S. explanation of the term "commercial scale" is set out in detail in the U.S. first submission but bears repeating in light of China's continued misreading of the U.S. position and its rhetorical questions this morning. Two features of "commercial scale" emerge from the ordinary meaning of the term. First, by using the word "*scale*" in 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 word "*commercial*" in 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.

8. Accordingly, in light of the foregoing two features, 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. A wilful infringer with a different intent may or may not be acting on a "scale" that is "commercial."

9. Could a single sale of an infringing product qualify as "commercial scale" under this interpretation? That is a question that China repeatedly raises. The answer is that it is possible, but – as the United States has consistently emphasized – it would depend on the circumstances, including a consideration of a number of relevant factors that the United States and Third Parties have referred to in our submissions.

10. In providing the panel with the interpretation of "commercial scale," the United States has employed a well-established method for interpreting a two-word term – a method consistent with that followed by past panels and the Appellate Body. By contrast, China invites the Panel to ignore the ordinary meaning of "commercial scale," as explained by the United States, and instead substitute a concept that China has labeled "significant magnitude of activity."

11. As the United States has demonstrated, China's concept does not accord with the customary rules of interpretation. While some of China's arguments helpfully bring into relief the inconsistencies in its arguments, they all ultimately fail to withstand scrutiny. This morning I would like to touch on a few of these arguments.

12. *First*, throughout this proceeding it has not been clear how China arrived at its proposed interpretation of "significant magnitude of activity" – but in its second submission, China reveals that it believes "commercial scale" is a measure of "significant business activity."[1] Of course, neither "scale" nor "commercial" leads to "significant." Further, use of the term "commercial scale" sets up a contrast between "commercial" and "non-commercial" magnitudes of activity. And so the question is what is "non-commercial" scale, not what qualifies as "significant commercial-scale activity."

13. 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 negotiatiors distilled any sort of prevailing understanding of "commercial scale" from the unrelated sources cited by China. These isolated references do not constitute any sort of "common usage"; furthermore, as China now confirms, they do not constitute any sort of "special meaning" under the *Vienna Convention*.[2] In other words, to the extent China claims that "common usage" means "ordinary meaning," China is mistaken. As the United States has shown, the ordinary meaning of "commercial scale" is not what China has proposed. Furthermore, to the extent that

[1] Written Rebuttal of the People's Republic of China, para. 142.
[2] Written Rebuttal of the People's Republic of China, para. 82.

China instead means "common usage" to mean a meaning other than the ordinary meaning, then again China is mistaken – there is nothing in the TRIPS Agreement that establishes a special meaning for the term "commercial scale."

14. The flaws in China's approach are highlighted by China's treatment of the draft model provisions prepared by the International Bureau of WIPO to assist the work of the WIPO Committee of Experts on Counterfeiting and Piracy. China now appears to have reconsidered its position and no longer asks this Panel to incorporate the document's definitions into Article 61.[3] It appears that China had not previously focused on the fact that the drafters of the WIPO document considered many factors in their discussion of the term "commercial scale." In our view, China should not be permitted to selectively refer to one aspect of the WIPO document – the mention of manufacturing – and then ignore the rest of the concept; i.e that "commercial scale" cannot be reduced to a simple value or volume metric. (In that context, we would also note that China now recognizes that "commercial scale" can be met by retail sales – as opposed to just industrial or manufacturing activities.[4])

15. By contrast, the United States has taken a consistent line throughout this proceeding: the document can *at most* be considered as a supplemental means of interpretation under the customary rules of interpretation (as reflected in Article 32 of the Vienna Convention); and when so considered, the document confirms the interpretation provided by the United States.

16. *Second,* China also persists in its efforts to persuade the Panel that "commercial scale" is a "broad and flexible" standard with the implication being that a "broad" and "flexible" obligation is one that cannot easily be breached. That proposed approach, however, is fundamentally unsound.

[3] Written Rebuttal of the People's Republic of China, para. 144.
[4] Written Rebuttal of the People's Republic of China, paras. 84-85.

Article 61 must be interpreted in accordance with the customary rules of treaty interpretation; those rules do not divide treaty provisions into categories such as "broad" and "narrow."[5]

17. Moreover, nothing about the ordinary meaning of the term "commercial scale" leads to ambiguous interpretations, as China would have the Panel believe. Indeed, while China attempts to use the views of the Third Parties[6] as support for this notion, this argument fails. First, any variation in views would not mean that "commercial scale" is susceptible to interpretations other than the one proposed by the United States. Indeed, the term has a clear meaning. Second, many Third Parties in fact have expressed views consistent with the United States – and noting that it may be necessary to consider multiple factors to decide whether a particular infringement is "on a commercial scale" in no way creates ambiguity or conflicts with the U.S. views.

18. *Third*, the United States was also pleased to learn in China's second submission that it now agrees with the United States and a number of Third Parties that Article 1.1 and Article 41.5 do not allow WTO Members to ignore explicit TRIPS obligations.[7] As made clear by the first sentence of Article 1.1, China must in fact implement Article 61 in a manner that fully reflects its terms.

19. However, China also raises the second sentence of Article 61 as a contextual argument in another failed attempt to escape the obligations of Article 61.[8] The second sentence of Article 61 reads: "[r]emedies available shall include imprisonment and/or monetary fines sufficient to provide a deterrent, consistently with the level of penalties applied for crimes of a corresponding gravity." China mistakenly uses the second sentence as support for its contention that

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[5] *Cf.* Appellate Body Report, *EC Measures Concerning Meat and Meat Products (Hormones)*, WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, para. 104 ("... merely characterizing a treaty provision as an 'exception' does not by itself justify a 'stricter' or 'narrower' interpretation of that provision than would be warranted by examination of the ordinary meaning of the actual treaty words, viewed in context and in the light of the treaty's object and purpose, or, in other words, by applying the normal rules of treaty interpretation").

[6] Written Rebuttal of the People's Republic of China, para. 74.

[7] Written Rebuttal of the People's Republic of China, paras. 100-101.

[8] Written Rebuttal of the People's Republic of China, para. 110.

"comparable" crimes should be taken into account when determining the meaning of "commercial scale." However, the second sentence does not change how the first sentence of Article 61 should be interpreted. The second sentence only addresses the relative severity of the criminal remedies that must be available, whereas the first sentence addresses the floor ("on a commercial scale") of what must be criminalized in the first place.

20. *Fourth*, China also appears to advance a new theory of the scope of application of Article 61. It claims that criminal penalties must be actually applied to fulfill the first sentence of Article 61.[9] It bases this, in part, on its assertion that the United States in practice prosecutes large-scale infringement. Of course, U.S. practice is not at issue in this dispute, nor does it constitute "subsequent practice" in the application of the TRIPS Agreement by WTO Members in the sense of the *Vienna Convention*.

21. Similarly, whether or not 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. As we have noted, a legal regime that denies the availability of criminal procedures and penalties for such activity is not compatible with Article 61. Indeed, it is puzzling why China refers the Panel to U.S. prosecutions in this regard. For example, if criminal prosecution of the U.S. vendor found in Exhibit CHN-179 were attempted in China, it would have been impossible, as based on the case description, the vendor's activity does not appear to meet China's Article 217 copy and illegal business volume thresholds.

22. China also repeatedly mis-states the basis for *in dubio mitius* in its second submission, utilizing a host of different formulations. China says that this principle applies when the meaning is not "clear and specific" (para. 51) or the meaning is not "clearly and precisely" stated (para. 55) or is not "expressly and unequivocally" stated (para. 56). In fact, the Appellate Body has found that *in dubio mitius* applies when the meaning is "ambiguous," and in this case there is no need to

[9] Written Rebuttal of the People's Republic of China, para. 123.

rely on this concept. The meaning of "commercial scale" is reached through the general rules of interpretation reflected in Article 31 of the *Vienna Convention*.

23. *Fifth*, China also continues to seek special deference because of its non-common law legal system, but this tack should not be countenanced. China is free to provide an IPR enforcement regime consistent with, for example, systems in effect in countries with a civil law tradition. Indeed, some of the Third Party members that have taken issue with China's measures also come from the civil law tradition.

24. In summary, China's proposed interpretation of Article 61 is flawed and cannot justify its TRIPS-inconsistent regime. Furthermore, it is worth noting that even under China's mistaken interpretation of "commercial scale," China's regime would still have to be considered inconsistent with its obligations under the TRIPS Agreement.

25. While China claims that the commercial-scale standard means a "significant magnitude of business activity," it seems clear that its own thresholds fail even under its own erroneous standard. For example, China claims that the RMB 50,000 "illegal business volume" threshold is less than 25% of the average annual revenue of a household or 30% of the annual revenue of households engaged in retail trade.[10] But that implies that such a household could engage in retail sales of pirated or counterfeit goods for approximately four months out of the year and still not commit a crime under China's "illegal business volume" threshold. It is difficult to imagine four months of retail activity not being "significant" infringement activity.

26. Now that we have described how China's newest arguments regarding the interpretation of Article 61 fail to withstand scrutiny, I would like to briefly reiterate how China's measures are inconsistent with the standard in Article 61.

[10] First Written Submission of the People's Republic of China, para. 135.

27. China's thresholds are set at such a level, and structured in such a way, that they do not permit prosecution or conviction of infringing activity involving values or volumes that are below the thresholds but are still "on a commercial scale." For example, the thresholds require Chinese authorities to rely on a limited set of one-size-fits-all tests to find commercial scale counterfeiting and piracy that can be subject to criminal prosecution or conviction. A range of factors are probative of "commercial scale," but China's rigid criminal thresholds preclude their consideration. China's metric is ill-adapted to the diversity of commercial activity in China and provides many ways for commercial scale counterfeiting and piracy to escape prosecution.[11]

28. While China protests that so-called "hypotheticals" should not be relied upon,[12] what the United States has provided are numerous, concrete illustrations of commercial-scale piracy and counterfeiting that takes place underneath China's thresholds. For example, the findings of the CCA Report are plain to see: the vast majority of traditional retail outlets selling recorded music and/or home video products – which China agrees is an example of commercial-scale activity[13] – faced no possibility of criminal prosecution or conviction under China's criminal thresholds. The CCA Report is a real-world demonstration of the safe harbor from criminal prosecution and conviction provided by China's thresholds.

29. But, as we have seen, instead of denying this core safe harbor problem, China attempts to disagree with the *degree* but not the *reality* of the inconsistency. At no point does China claim that criminal prosecution or conviction under Articles 213, 214, 215, 217, and 218 is possible for <u>any</u> trademark counterfeiting or copyright piracy below the thresholds themselves. Indeed, China does not rebut the core issue raised by the United States with respect to the Article 61 claim: that is, if a case fails to meet at least one of the thresholds, that fact will preclude criminal prosecution and conviction.

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[11] *See* First Written Submission of the United States, paras. 137, 140, and 156.
[12] *See* Written Rebuttal of the People's Republic of China, paras. 148-151.
[13] Written Rebuttal of the People's Republic of China, para. 84.

30. China has decided to take a different tack: it essentially concedes the existence of a safe harbor from criminal prosecution and conviction for some commercial-scale counterfeiting and piracy, and instead only attempts to chip away at the size of the safe harbor. Even so, we have described in our submissions how China's arguments about the size of the safe harbor fail to withstand scrutiny. However, in its second submission, China presents some new arguments. We would briefly like to show how these arguments are similarly without merit.

31. *First*, even China cannot say that it reaches all of the examples of counterfeiting and piracy cited by the United States and others – the best that China can assert is that it reaches "most" of it.[14] However, as the United States has demonstrated, the application of *any* or *all* of the alternative Chinese thresholds still leaves much commercial-scale piracy and counterfeiting immune from criminal prosecution or conviction.

32. *Second*, China mistakenly claims that we have conceded that the valuation methodology is irrelevant to this dispute.[15] The existence of China's valuation methodology as a component of its rigid and high thresholds is fully relevant; it creates a safe harbor, whether it is based on the value of the infringing goods or the legitimate goods. However, by relying on the prices of infringing products, China contributes greatly to the capacity of the safe harbor to shelter commercial scale counterfeiting and piracy. Indeed, China's valuation methodology is directly related to the size of the safe harbor created by China's thresholds.

33. *Third*, China continues to assert that its laws are in compliance because thresholds can cover an extended time-frame of infringement. It appears that by making this argument, China is re-defining "commercial scale" to require that the activity be sustained over a period of time. To the extent that China's IPR regime requires not just commercial-scale activity, but *sustained* commercial scale activity, that additional requirement does not comport with Article 61. Further,

[14] Written Rebuttal of the People's Republic of China, para. 17.
[15] Written Rebuttal of the People's Republic of China, paras. 94-95.

China's argument is belied by its continued emphasis on administrative enforcement, because administrative penalties will preclude criminal punishment and would therefore not permit criminal prosecution or conviction in many of these cases. And, as we have explained before, China's obligations under TRIPS Article 61 are not met by its administrative enforcement system.

34. *Fourth*, China claims that certain "general provisions" of its Criminal Law – namely inchoate crimes and joint liability – can establish criminal procedures and penalties.[16] China's assertion that these general provisions for inchoate crimes can be used to address evidence of *potential* infringement is beside the point. The inconsistency with Article 61 arises because China's thresholds rule out criminal liability based on evidence of *actual* infringement that does not meet the metrics; *i.e.*, some *actual* infringement that has already occurred is exempted from criminal prosecution or conviction.

35. Additionally, China for the first time states that the crime of "joint" liability should also be considered. In the first place, this argument is of no consequence with respect to infringers who work alone. Second, China's reference to the *Zhao Chaoying* case found in Exhibit CHN-12 in any event does not demonstrate that below-the-thresholds activity can be captured; it shows only that such activity can be captured if it exists as part of the above-the-thresholds activity. Simply put, this argument is at best another attempt by China to chip away at the *size* of the safe harbor; it does not change the *reality* that the safe harbor exists.

36. In summary, we have addressed and refuted China's attempts to use its flawed interpretation of Article 61 to justify its TRIPS-inconsistent regime. Indeed, even under China's mistaken interpretation of "commercial scale," China's regime would still have to be considered inconsistent with its obligations under the TRIPS Agreement.

[16] Written Rebuttal of the People's Republic of China, paras. 33-35.

37. To conclude: China fails to provide for criminal procedures and penalties to be applied in all cases of commercial-scale trademark counterfeiting and copyright piracy. We therefore respectfully request the Panel to find China's IPR thresholds inconsistent with China's obligations under the first and second sentences of Article 61, and Article 41.1, of the TRIPS Agreement.

III. China's Border Measures for Disposal of Confiscated Goods

38. Now we would like to turn to our second claim. This claim concerns China's measures for disposal of infringing goods confiscated by border authorities. Under these measures, Customs authorities are only permitted to destroy the goods as a last resort, and they do not have the power to dispose of goods outside the channels of commerce in a manner that avoids any harm to the rightholder. Customs' rules require them to attempt to dispose of the goods in accordance with a strict hierarchy – first, by either transferring them to public welfare organizations or selling them to the right holder; if this is not feasible, they must take the second step and auction off the seized goods following removal of the infringing features, if this is possible. And, if Customs can take any of these actions, Customs does not ever acquire the power to destroy the goods. These measures are inconsistent with China's obligations under Articles 59 and 46 of the TRIPS Agreement.

Article 59 of the TRIPS Agreement

39. The first sentence of 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, this requires focus on two of the sentences in Article 46. *First*, a Member's competent authorities for border enforcement "shall have the authority to order that goods that they have found to be infringing be, without compensation of any sort, 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."

40. China's Customs authorities do not have the authority to order the destruction or disposal of infringing goods in accordance with these Article 46 principles. This is because Article 30 of the Customs IPR Implementing Measures, which implements Article 27 of the State Council Customs IPR Regulation, 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.

41. The United States has already demonstrated the deficiencies in China's broad claims of compliance with Article 59 and Article 46. For example, China brandishes China Customs statistics on the actual disposition of confiscated goods found to be infringing, arguing mistakenly from them that it has implemented its TRIPS obligations. Those figures, however, provide no response to the U.S. claim. They can not and do not demonstrate that Chinese officials were able to exercise full Article 46 authority in dealing with such goods.

42. China also fails in arguing that the authority to take action in accordance with Article 46 can be "reasonably conditioned" and that China simply includes certain "factors for discretion" in its Customs disposal regime.[17] Article 46 describes the required scope of authority both to dispose of goods and to destroy goods – and nowhere includes the many obstacles and conditions present in the Chinese legal regime. To the contrary, the TRIPS Agreement obligates China to provide China Customs with the full authority 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.

[17] *See, e.g.*, Written Rebuttal of the People's Republic of China, paras. 181-186.

43. In China's second submission, China agrees with the United States that China Customs must have the authority to dispose of seized goods outside the channels of commerce in such a manner that avoids any harm to the right holder. However, in China's view, acting with a high "probability" that harm to the right holder will be avoided is enough.[18] Unfortunately, this view does not accord with the text of Article 46. Authority to dispose of goods "in such a manner as to avoid any harm caused to the right holder" requires a structure and process that – as the text plainly states, actually "avoids any harm caused" – not that has *good prospects* for avoiding this harm. China's arguments therefore should be rejected.

44. Further, China continues to pursue a number of arguments that misread the text of the last sentence of Article 46. *First*, China claims that procedural actions taken in setting up its auctions of these goods, such as reserve prices and comments from the right holder, qualify as more than the "simple removal" of the trademark, thus justifying its auctions under Article 46.[19]

45. However, the word "simple" in the phrase "simple removal" means what it says: Customs may not just remove the offending trademark from the goods and release such goods into the channels of commerce, *other than in exceptional cases*. (China is not arguing that it transforms the goods into recyclable raw materials before auction, or takes any other similar action. Rather, it concedes that, under its measures, in the case of counterfeit trademark goods, it only removes the infringing trademark.[20])

46. *Second*, China claims that the term "release" in the last sentence of Article 46 refers to returning the goods to the infringer, and that China's auction procedures guard against this. In point of fact, the infringers appear to be fully eligible to bid for their goods at China's auctions, but that is beside the point. China's reading is flatly contrary to the text of Article 46, which says

[18] Written Rebuttal of the People's Republic of China, para. 158.
[19] Written Rebuttal of the People's Republic of China, paras. 207, 218.
[20] Responses of the People's Republic of China to the Questions of Panel, para. 125.

release into "channels of commerce"– not "return of the goods to the infringer." Accordingly, this textual interpretation and accompanying argumentation must fail.

47. We would like to now turn to China's arguments that attempt to justify the hierarchy provided by the measures at issue. As we have demonstrated, 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.

48. While China claims its Customs authorities have the "discretion" to make factual findings that eliminate the need to take action under any one of the prescribed steps in the hierarchy, China concedes that when Customs finds certain facts are present, it is compelled to follow the particular step set forth in its measures.[21] This is the core of the U.S. concern.

49. We would like to turn the Panel's attention to the flowchart (Exhibit US-68) illustrating the Chinese Customs hierarchy, which we have attached to our statement this morning. As you will note, China's hierarchy mandates a series of steps that must be taken by Customs. In each of the circumstances denoted with the word "yes," Customs lacks the authority that the TRIPS Agreement requires to opt for destruction or disposal in accordance with Article 46 principles.

50. Beginning with the first step of China's mandatory hierarchy, the United States has provided a full description of how neither alternative in this initial step – donation or sale to the right holder – meets the principles of Article 46. China argues that the United States needs to provide factual evidence of harm in the case of the donation option to demonstrate an inconsistency with the principles of Article 46. But our claim is based on the *legal structure* that

[21] Written Rebuttal of the People's Republic of China, para. 184.

governs Customs's decision-making in these circumstances. This legal structure does not ensure that in all cases the Article 46 principles will be respected.

51. The fact that China donates infringing goods to public welfare organizations is not what is at issue here. Our concern centers on the lack of Customs' *authority* to make these donations in accordance with Article 46 principles. Two key points illustrate the problem: First, the lack of proper authority is evidenced by the national Law on Public Donations, which expressly authorizes the sale into commerce of donated goods, when certain conditions are present. Second, the same lack of authority is evidenced by the necessity for Customs to have to persuade a charitable organization to enter into a donation agreement to try to avoid the sale of these goods – a telling sign of the deficiency in its authority.

52. The United States' concerns do not end here. Even when a donation agreement has been reached, the Law on Public Donations appears to allow sale into commerce. China has not provided any legal basis for asserting that the terms of the donation agreement override this law. Indeed, China's Contract Law indicates that when a contract contains a provision inconsistent with a Chinese law, the law prevails over that contract provision.[22] Further, contrary to China's claims, charitable organizations' rights under this law to sell donated goods when circumstances change after donation would not be affected by regulations China Customs itself follows in choosing who will receive the goods in the first instance.

53. China's latest defense regarding its "sale to the right holder" option also fails. China argues there is only a small chance that such goods will enter the channels of commerce by public auction, so right holders need not worry if they do not purchase the goods.[23] Accordingly, China claims these purchases are totally unforced. However, this dispute concerns the consistency of

[22] *See* Contract Law of the People's Republic of China (1999) (Exhibit US-73); Explanations by the Supreme People's Court on Several Issues Regarding the Application of the Contract Law (1999) (Exhibit US-74).

[23] Written Rebuttal of the People's Republic of China, para. 170.

China's measures with required norms; it is futile to argue about likely or unlikely outcomes, when China's measures do not avoid any harm to the right holder.

54. As the flowchart shows, China's measures require Customs to move to the public auction step if the right holder does not pay for these goods (and donation is not appropriate). Since auction is the next legal step to be taken under this measure, it will in fact have an impact on right holders' decisions about buying the infringing goods. As the United States has noted, if right holders pay for infringing goods, wishing to ensure that they are destroyed to prevent their release into the channels of commerce (such as, for example, by public auction), this payment causes financial harm.

55. Turning to the next step in the hierarchy, the public auction of the confiscated goods, the United States has demonstrated that China's public auction process for these goods does not comport with the Article 46 principles incorporated into Article 59.

56. First, because China's mandatory procedures strip Customs of the authority to prevent auction when this option becomes operative in the Customs hierarchy, the auction procedures are inconsistent with the first sentence of Article 46. A public auction obviously is not destruction, and China does not dispute that it leads to release of such goods into the channels of commerce. In addition, we have shown that China's auction procedures do not allow goods to be disposed of "in such a manner as to avoid any harm to the right holder."

57. China vainly attempts to argue that the trademarked goods it auctions are exempt from Article 46's protection, because "right holders have a legal right to protection from goods that infringe their intellectual property, but not to unmarked goods."[24] China's argument misses the point. Members agreed under the TRIPS Agreement that their customs' authorities would have the authority to order the destruction or disposal of infringing goods in accordance with Article 46.

[24] Written Rebuttal of the People's Republic of China, paras. 194.

And in the last sentence of Article 46, Members agreed that simple removal is not sufficient, other than in exceptional cases, to allow the good to be released into the channels of commerce. In other words, Members have already settled the issue raised by China – there is no requirement for a further showing of harm to the right-holder before the last sentence of Article 46 applies.

58. Second, we have also shown that China's public auction step is inconsistent with the principle in the last sentence of Article 46, because China releases these goods into the channels of commerce as a matter of course, rather than only in exceptional cases.

59. And now we would like to move to the final step of the mandatory hierarchy. As the flowchart indicates, this step becomes operational only if no earlier options prove feasible. Then and only then, China Customs gains the power to destroy the infringing goods. The highly limited circumstances under which China's legal regime permits destruction do not comport with Article 46, which requires this authority, or proper disposal authority, to be available to China Customs authorities at all times.

60. To summarize: China's border measures do not provide Chinese border officials with the authority required under TRIPS Article 46 principles, and thus are inconsistent with China's obligations under Article 59. The United States respectfully requests that the Panel find that (1) the compulsory sequences of steps set out in the Chinese measures at issue mean that Chinese customs authorities lack the authority to order destruction or disposal of infringing goods in accordance with the principles set out in Article 46 of the TRIPS Agreement, and (2) the measures at issue are therefore inconsistent with China's obligations under Article 59 of the TRIPS Agreement.

IV. Article 4 of China's Copyright Law

61. This brings us to our third and final claim. This claim is centered on the first sentence of Article 4 of China's Copyright Law. Article 4, first sentence, provides that "[w]orks the publication or distribution of which is prohibited by law shall not be protected by this Law."

62. At the outset, we must emphasize that China has admitted that it denies copyright protection to certain works whose contents Chinese authorities determine are prohibited by law.[25] Moreover, the National Copyright Administration of China (NCAC) has confirmed that Article 4 denies copyright protection to "works whose contents are illegal." Thus, Article 4.1 on its face denies copyright protection to works that are required to be afforded protection. The United States has demonstrated how this is contrary to China's obligations under the Berne Convention and is thus inconsistent with China's obligations under the TRIPS Agreement.

63. China now focuses on arguments regarding the burden of proof in this case, but those arguments are unavailing. As the Appellate Body has confirmed, an "as such" challenge is based on the "text of the relevant legislation."[26] Indeed, the text of Article 4.1 itself demonstrates that China's measure is inconsistent with its obligations under the TRIPS Agreement. And while China complains that the main evidence behind our claim is Article 4.1 itself,[27] that is precisely the provision that serves as the principal "fact" demonstrating our claim. Furthermore, the United States has also provided additional other evidence in our submissions that support our contentions, including a discussion of statements by China's Supreme People's Court;[28] an explanation of the legal force of Chinese judicial interpretations and the relationship between Chinese judicial statements and Chinese administrative agency statements;[29] China's own formal statements to the WTO about the operation of the Copyright Law;[30] and analysis by recognized scholars and legal experts.[31] We have carefully explained how the denial of copyright protection under Chinese Copyright Law is inconsistent with China's WTO obligations.

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[25] *See* First Written Submission of the People's Republic of China, para. 243.

[26] Appellate Body Report, *United States – Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany*, WT/DS213/AB/R, adopted 19 December 2002, para. 157.

[27] Written Rebuttal of the People's Republic of China, para. 266.

[28] *E.g.*, U.S. Oral Statement at the First Panel Meeting, para. 88, and Second Submission of the United States, paras. 206-210.

[29] *E.g.*, First Submission of the United States, para. 23, and Second Submission of the United States, para. 203.

[30] *E.g.*, First Written Submission of the United States, paras. 68-69, and Second Submission of the United States, para. 201.

[31] *E.g.*, Second Submission of the United States, para. 202.

64. While we have set out in detail the U.S. claim in our submissions to the panel and responded to China's mistaken arguments in our second submission, I would like to touch briefly on a few arguments that China makes in its latest submission.

65. *First*, the United States has shown, Article 4.1 of the Copyright Law – by excluding an entire category of works from copyright protection – is inconsistent with Articles 2(1) and 2(6) of the Berne Convention. *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 Convention Article 5(1), which specifies certain guaranteed minimum copyright protection for works, including a minimum set of exclusive rights. We note in passing that – contrary to what China says in its rebuttal submission – these are not newly emerging arguments; they were in fact the very first two points that the U.S. first submission made about Article 4 of the Copyright Law.[32]

66. In its second submission, China makes two principal arguments regarding Article 4.1 as legitimate and this denial of copyright protection. First, China argues that it broadly provides all TRIPS-protected rights, and asks the Panel to recognize the denial of protection under Article 4.1 because it is allegedly a narrow provision with limited marketplace effect. Second, China argues that Article 17 of the Berne Convention justifies its exclusion from copyright protection. While we have dealt with these erroneous arguments in our submission, we would like to address them this morning in further detail.

67. China first returns to the Copyright Law and states that its law provides all rights under the TRIPS Agreement. China also describes in detail the provisions of the Copyright Law on the protection of copyright. Of course, this description only serves to highlight the array of protections

[32] First Written Submission of the United States, paras. 215-219.

denied to works that come under the ambit of Article 4.1, since they are not protected by the Copyright Law.

68. China also continues to claim that this Panel should somehow ignore this TRIPS-inconsistency because, China asserts, the scope is limited and there is allegedly only a small effect in the marketplace. First, it hardly seems that the scope of Article 4.1's exclusion is limited. China's dedicated apparatus for censorship – including the many content review bodies and content review regulations in addition to the courts and NCAC which review content – suggest that substantial categories of works are potentially subject to being declared "illegal" and thus excluded from protection. Article 4.1 might be a provision with a short sentence, but those words are hardly limited in scope.

69. Second, the impact of Article 4.1 on right holders is hardly small. To the extent that China means impact on *China's* marketplace, the ongoing rampant infringement, including of works that have been censored or prohibited in China, suggests that there are serious implications. And to the extent that China means *foreign* marketplaces, if right holders cannot enforce their copyright against pirated products manufactured in China, they lose a crucial tool for preventing the export of such products. The enforcement burden falls instead on those countries that are the recipients of infringing exports, including other WTO Members.

70. Moreover, the uncertainty created by Article 4.1 should not be discounted. Due to Article 4.1, foreign right holders unfamiliar with the Chinese Government's current content preferences cannot be sure whether or when copyright protection will be granted or denied. Indeed, China has already acknowledged this uncertainty. China notes that, in the *Zheng Haijin* case, the publishing house submitted a work for review by the authorities because it was "uncertain about the legality of [the] work."[33] Therefore, for this reason as well, it is clear that the real-world impact of Article 4 is far from negligible.

[33] Written Rebuttal of the People's Republic of China, para. 249, fn. 205.

71. China's argument that Article 17 of the Berne Convention allows it to deny copyright protection to censored works likewise fails to withstand scrutiny. Article 17 states that countries' obligations to protect covered expressive works do not inhibit their ability to control or prohibit "the circulation, presentation or exhibition" of those works. It does not authorize a system that denies all enforceable copyright protection (including denial of protection of the rights of reproduction, translation, adaptation, etc.) to an entire category of disfavored works.

72. If the drafters of the Berne Convention had sought to do so, they could have expressed this easily by using the phrase "the protection of this Convention shall not apply to" the works in respect of which a Government exercises its right referred to in Article 17. Indeed, this is the language that the Convention uses when it truly excludes certain categories of works from copyright protection, such as the category of works noted in Berne Article 2(8). But they did not. Alternatively, the drafters could have used the following language from Berne Article 2*bis*(1): "it shall be a matter for legislation in the countries of the Union to exclude, wholly or in part... ." But, again, they did not. Article 17 is clear: it does not permit Members to deny copyright protection to authors in their respective works.

73. When a Member exercises its power to censor, that does not mean that the right holder is stripped of its copyright and the ability to enforce its copyright against third parties who, in spite of the government's censorship prohibition, might produce infringing copies or might seek to sell infringing copies in the domestic or foreign markets. Leading copyright scholars agree.[34]

74. In this connection, China's attempt to equate copyright protection with what China calls "private censorship" is incorrect. Censorship is distinct from a rightholder's right to authorize or prohibit certain uses of his or her expression of a particular idea by a third person. Even one of the scholars that China has cited agrees: "The conclusion is that copyright law is not purely a matter

[34] *See, e.g.*, Silke von Lewinski, *International Copyright Law and Policy* (2008), pp. 170-171 (Exhibit US-75); Stephen P. Ladas, *The International Protection of Literary and Artistic Property* (1938), p. 613 (Exhibit US-76).

of private law, but is imbued with a public purpose that has changed from censorship to production and dissemination."[35] In the words of Article 1 of the Berne Convention: "The countries to which this Convention applies constitute a Union *for the protection of the rights of authors* in their literary and artistic works"[36] – a very different purpose than that served by censorship.

75. *Third*, the United States has also demonstrated in its submissions that Article 4.1 makes copyright protection subject to a formality that is inconsistent with Berne Article 5(2), and therefore is also inconsistent with TRIPS Article 9.1.

76. China has offered different and often conflicting views about the meaning and application of Article 4.1. But, 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. Therefore, where pre-publication review is required and publication is prohibited until the completion of a successful review, Article 4 by its terms denies copyright protection to such works. This means that copyright protection is subject to the results of that review – i.e., a formality.

77. China also asserts that a court would make an inquiry under Article 4.1 only if a defendant raises it as a formal defense. However, the *Zheng Haijin* opinion already demonstrates that courts examine the contents of a work before deciding whether or not copyright is protected. Indeed, in China's second submission, it admits that regardless of whether a particular defendant raises a formal defense, courts and the NCAC must determine the legality of a work *de novo*.[37] China's statements demonstrate that when it comes time to enforce a copyright owner's rights in a work, they must prove that it passes content review in order to be awarded copyright protection.

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[35] Shubha Ghosh, *Deprivatizing Copyright*, 54 Case W. Res. L. Rev. 387, 438 (Exhibit CHN-194).
[36] Emphasis added.
[37] Written Rebuttal of the People's Republic of China, para. 249.

78. Accordingly, if a copyright owner chooses to ignore the content review process and then seeks to enforce the copyright – the very copyright China says is protected upon creation – the court will, as China admits it must do, first engage in content review before the copyright owner is permitted to enforce a copyright. This is a clear condition precedent to copyright protection (or formality) that if not followed and satisfied, prevents the exercise and enjoyment of rights. Further, China has acknowledged the close relationship between the standard for content review and what is "prohibited by law" for purposes of Article 4.1, rendering any distinction between the two meaningless.[38]

79. Moreover, while China claims the content review measures cited by the United States are not referenced in the text of Article 4.1,[39] there is nothing in Article 4.1 that states that the works for which publication or dissemination is prohibited must be prohibited solely by the Copyright Law. The fact is that, at least where pre-publication review is required, the content review measures "prohibit" the "publication or dissemination" of a work until the work passes content review. Therefore, these procedures are directly related to whether such works come within the ambit of Article 4.1.

80. *Fourth*, a consequence of 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. The United States has demonstrated that because authors do not benefit from certain civil and criminal remedies by virtue of Article 4.1, China is not meeting its obligations under Article 41.1 and Article 61 first and second sentence. As we have just explained, China's Berne Article 17 arguments with respect to denial of copyright protection fail to withstand scrutiny, and likewise, because Article 4.1 prevents copyright holders from enforcing their exclusive rights, Article 17 does not serve to justify China's exclusion.

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[38] Responses of the People's Republic of China to the Questions of the Panel, para. 166.

[39] Written Rebuttal of the People's Republic of China, para. 232.

81. Additionally, China's argument that it has provided a procedure for "effective action" against infringers by banning "content" is without merit.[40] The enforcement of a censorship prohibition simply cannot replace the enforcement of copyright in the works concerned. China cannot escape TRIPS-required enforcement obligations by taking away rights that must be made available to the right holder and replacing them with a government-controlled censorship prohibition. Indeed, a right holder's copyright enforcement rights include the application of certain remedies, such as civil remedies, which do not form part of the governmental enforcement of censorship.

82. In closing, China's citation to DSU Article 3.7 is puzzling.[41] The Appellate Body has confirmed that a WTO Member has broad discretion in deciding whether to bring a case under the DSU.[42] The United States has been concerned about Article 4 for quite some time. We repeatedly sought information about the operation of Article 4 from China bilaterally. Before China's first written submission in this dispute, we had unfortunately received only the most limited of replies to our inquiries. China's statements in the context of this dispute have confirmed that this claim is "fruitful," as they have reinforced our concerns that Article 4.1 is inconsistent with China's obligations under the TRIPS Agreement.

83. To summarize: In its submissions, China has conceded that the first sentence of Article 4 of its Copyright Law operates to deny copyright protection to works containing prohibited content. Therefore, we respectfully ask the Panel to conclude that China is acting inconsistently with its obligations under the TRIPS Agreement.

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[40] Written Rebuttal of the People's Republic of China, para. 311.

[41] Written Rebuttal of the People's Republic of China, para. 224.

[42] *See* Appellate Body Report, *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, adopted 25 September 1997, para. 135.

V. Conclusion

84. Mr. Chairman and members of the Panel, the United States began this dispute after our IPR cooperation efforts with China reached an impasse on the three specific sets of issues in this dispute. We recall that Part III of the TRIPS Agreement implements the consensus that the Uruguay Round negotiators reached concerning the importance of providing effective IPR enforcement tools. As international trade in counterfeit and pirated goods has increased, the importance of providing effective and appropriate means to enforce IPR has become even more self-evident.

85. While the United States recognizes that China has made progress to achieve a modern IPR system, we continue to believe that China's efforts have fallen short in the three specific areas at issue in this dispute. The United States and other WTO Members have been deeply concerned that the measures relevant to the three areas at issue in this dispute are not consistent with China's obligations under the TRIPS Agreement.

86. At this point, I would like to bring our opening statement to a close. We look forward to addressing your questions. Thank you for your time and attention.