

## INTELLECTUAL PROPERTY UPDATE

Squire, Sanders & Dempsey L.L.P.

Summer 2006

**Inside:**

China's Administrative Procedure for Patent Protection.....	2
Patent Subsidies in China.....	3
Patent Enforcement in China: Civil Remedies.....	5
New Chinese Regulation Strengthens Protection of Copyrighted Work on the Internet.....	8

*Conventional wisdom for some time has been that China does not provide sufficient safeguards against theft of intellectual property. China's commitment to changing people's perceptions is real. In this issue, as part of our continuing effort to meet the needs of our clients, we present a series of articles regarding protection of intellectual property rights in China. I hope you find these articles of value to your business.*

*James M. Smith, editor*

## China's Administrative Procedure for Patent Protection

A unique feature of China's civil system of patent protection is the two-track approach under which a patent holder may choose either the administrative track or the judicial track to protect patent rights. Under the administrative track, a patent holder pursues administrative action before a local Intellectual Property Office (IPO). Local IPO's are established in the provinces, autonomous regions and certain cities, and are supervised by the State Intellectual Property Office (SIPO). Under the judicial track, a patent holder seeks redress in civil court. This article focuses on the administrative protection of patent rights.

The procedure for a patent enforcement proceeding before a local IPO is governed by the Measures for Administrative Enforcement of Patent promulgated by the SIPO. To initiate such a proceeding, a patent holder must file a request identifying the alleged infringer and the matter in dispute and certifying that the patent holder has not instituted court proceedings. Upon receipt, the IPO must forward the request to the respondent within 14 days. The respondent then has only 15 days to submit a written defense. If the respondent does not answer, the action will proceed without the participation of the respondent. The IPO has the discretion to decide whether to conduct an oral hearing. If it decides to do so, the IPO must inform the parties of the time and place of the oral hearing at least three days in advance. The IPO may, of its own initiative, conduct investigations and collect evidence including making copies of documents, questioning the parties and witnesses, collecting samples and conducting on-site investigations. The IPO generally issues a decision within a few months.

If the respondent is found liable for patent infringement, the IPO may issue an order to cease infringing activities and to destroy infringing products. The IPO may also confiscate illegal earnings and impose fines. The IPO is not, however, authorized to award damages. If the respondent refuses to abide by the IPO's orders, the IPO may petition the court to enforce those orders.

If the respondent is not satisfied with the IPO's decision, he may, within 15 days from the date of receipt of the decision, institute legal proceedings in the court in accordance with the Administrative Procedure Law of China. However, the decision of the IPO will continue to be enforced during the court proceedings.

An administrative action can offer a quick, efficient and cost-effective remedy, especially when there is a clear case of infringement, damages are minimal and the infringer is unlikely to contest the allegations of infringement. While an administrative action is effective in clear-cut and simple infringement cases, court proceedings are desirable in complex cases and are necessary when the patent holder seeks damages. If the alleged infringer is likely to vigorously contest the case and challenge any administrative decision in court, it is

more efficient to avoid the administrative procedure and seek remedy in court. Another disadvantage of the administrative procedure is that the local IPO is sometimes influenced by local government officials who are eager to protect their local industries.

*Song Zhu, Senior Associate, Palo Alto*

### Patent Subsidies in China

There are many advantages to setting up a manufacturing plant or a research and development (R&D) center in China. Some of the better known advantages include low labor costs, low corporate tax rates and inexpensive land. However, a lesser known advantage is the patent subsidies that are available. These subsidies, including rebates and rewards, are available to Chinese entities, including Chinese subsidiaries of foreign companies, and are meant to encourage R&D so that China moves up the value chain from manufacturing to higher margin design.

The subsidy schemes vary by municipality and most cover not only Chinese filings, but also foreign patent filings. Some schemes are actually rewards for patent grants. Chengdu, for example, provides 5,000 RMB (US\$625<sup>1</sup>) upon grant for a Chinese patent and 30,000 RMB (US\$3,750) upon grant of a foreign patent, with a maximum of two foreign patents per invention. In Beijing, the subsidy consists of a rebate for a maximum of 950 RMB (US\$118.75) for the Chinese application fee and a maximum of 1,200 RMB (US\$150) for requesting substantial examination for a Chinese patent application. For foreign applications, a reward of 2,000 RMB (US\$250) per application grant is available. While the amount of the subsidy in Beijing is substantially less than in Chengdu, a request can be made for the rebate after filing the grant application rather than waiting until the patent is granted, which can be several years later.

In Chongqing, the subsidy consists of a rebate covering the application fee, a substantial examination fee, maintenance fee and the annual fee of the first year paid with respect to an invention (currently totaling 4,600 RMB or US\$575). However, the rebate of the

Aaron Wininger was quoted in the August 2006 issue of the Shanghai Business Review on the importance of filing patent applications promptly in China because of China's adherence to a first-to-file policy for patent priority.

<sup>1</sup> At the rate of 8 RMB per US\$1.

examination fee, maintenance fee and annual fee can only be applied for after the patent is granted. Further, the applicant or assignee must be registered with a Patent Service Plan in Chongqing in order to qualify for the rebates. In addition, there is no rebate for foreign patent filings.

In Guangzhou, the subsidy consists of a reward of 1,200 RMB (US\$150) for a Chinese filing, 2,800 RMB (US\$350) for substantial examination of a Chinese patent application and a 5,000 RMB (US\$625) reward for grant of a Chinese patent. For filing a Patent Cooperation Treaty (PCT) application the reward is 10,000 RMB (US\$1,250) and for filing a foreign application the reward is 20,000 RMB (US\$2,500) per country. If a foreign patent application is granted, there is an additional reward of 10,000 RMB (US\$1,250) per country. Further, if the application will make “great” contributions to the economy or technology base of Guangzhou, additional rewards are available. However, it is not clear what would qualify as such.

Shenzhen has an extremely generous program for foreign filings. If an application is granted by the European Patent Office, Japan or the United States the reward is 50,000 RMB (US\$6,250) per jurisdiction for up to two jurisdictions. For other countries the reward is 30,000 RMB (US\$3,750). For filing in China, Hong Kong or Taiwan a reward is provided in the amount of 2,200 RMB (US\$275) for requesting substantial examination. Upon grant, a reward of 2,000 RMB (US\$250) is provided.

In Shanghai, rebates are available for the Chinese patent application fee, examination fee, grant fee, maintenance fee and first three annuity fees (currently totaling 6,655 RMB or US\$831.88). For grant of a foreign patent, rewards of 30,000 RMB (US\$3,750) are available per country for up to three countries per invention. For Hong Kong and Macao, rewards of 10,000 RMB (US\$1,250) each are available.

When choosing a municipality in China in which to open up an R&D center, therefore, one may want to consider factors other than the availability of a low cost, highly educated workforce and a robust infrastructure. The availability of patent subsidies, particularly if one plans to file a large number of foreign applications, should also be considered. For example, a company could receive a subsidy of US\$13,025 per invention when filing in China, the US and Japan. When filing patents for 100 inventions annually, the subsidy could add up to \$1,302,500 per year.

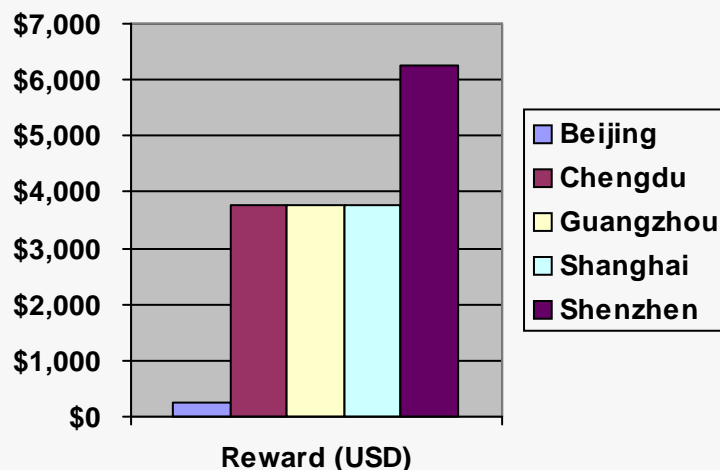


Chart: Rewards for Foreign Patent Filings and Grant  
(Per Country/Per Invention)

For more information about the rebates or if you are considering municipalities other than those listed above, please contact us. We would be happy to assist you in setting up R&D centers in China and applying for rebates.

*Aaron Winger, National Partner, Shanghai*

*Xiao Luo, Law Clerk, Shanghai*

## Patent Enforcement in China: Civil Remedies

### A Brief Overview

China's intellectual property enforcement system is comprised of four different avenues: the State Intellectual Property Office (SIPO), administrative approaches, civil approach and criminal approach. The SIPO has sole jurisdiction over patent validity and invalidity disputes through its reviewing body, the Patent Reexamination Board (PRB). Intellectual property administrative offices throughout the provinces and municipalities of China can also exercise their authority over some aspects of patent disputes. Criminal remedies are available to false patent marking cases. This article will briefly address patent litigation in court.

In China, the court system is called the People's Court. The People's Court system has four levels: county, intermediate, higher and supreme courts. Because intellectual property rights are of a special or complicated character, civil disputes arising from infringement in China are under the first-instance jurisdiction of intermediate courts situated in the capital cities of the provinces, autonomous regions and municipalities directly under the central government, and a few specially authorized intermediate courts and county courts. These disputes are under the second-instance, or appeal, jurisdiction of the court at a higher level. There are approximately 50 intermediate courts and over 30 higher courts and the Supreme People's Court that have jurisdiction over intellectual property-related civil disputes. The People's Court also has jurisdiction over patent litigation law suits. The court has the power to issue preliminary and permanent injunctions and to determine the amount of damages.

The civil procedure of the court is initiated entirely at the request of the plaintiff. There is no evidentiary discovery system in China and parties must produce evidence to support their assertions and claims. A party may petition the court to provide for evidence preservation or collection under certain circumstances. In the course of fact finding, the court generally takes, as legal facts for deciding a case, the facts proved with the filed evidence after cross-examination.

The quality of the courts varies from province to province. It is advisable to choose a court located in an economically developed region which is likely to be more experienced, a court outside the region where the first defendant has its domicile or a higher court as the first instance court when the case is of special importance. The Supreme People's Court will then be in a position to directly intervene in the second-instance trial.

### **Evidence and Evidence Collection**

Whichever approach is chosen to impose legal liabilities on an infringer, the plaintiff should present evidence to the authority handling the case that attests to the ownership and validity of the intellectual property right as well as evidence showing the infringement of that right.

#### *Evidence Showing Ownership and Validity*

The evidence the plaintiff furnishes should support the assertion that (1) the plaintiff is the owner or party interested in the right involved, i.e., a legitimate plaintiff or complainant; and (2) the intellectual property right is lawfully in existence, valid and enforceable according to the law in China. In patent litigation, this evidence can result in a stay of litigation.<sup>2</sup>

According to established practices in patent litigation in China, when the subject patent is an invention patent, which has been examined by the SIPO to be patentable, courts generally will not grant a stay of the litigation if the validity of the patent is challenged. China patent law provides for invention patents and utility model, or petty, patents. Invention patents are regular patents similar to utility patents in the US. Utility model patents are different in that they receive no examination and have a term of ten years from the filing date. Utility model patents cannot claim a process or method, but must be an article or device. When the subject patent is a utility model patent, which has not received substantive examination by the SIPO, courts will generally grant a stay of the litigation if the validity of the patent is challenged.<sup>3</sup>

<sup>2</sup> In patent litigation in China, when the validity of the patent in dispute is challenged, the court may grant a stay of the litigation to wait for resolution of the validity issue by the Patent Reexamination Board (PRB) of SIPO. The general rule of staying a litigation proceeding is as follows: When the patent in dispute is a utility model patent, the court will generally grant a stay unless the PRB had previously examined this patent as valid; when the patent in dispute is an invention patent, the court will generally not grant a stay.

<sup>3</sup> The PRB, which has sole jurisdiction over the validity of a patent, will examine and rule on the subject patent. The rulings of the PRB are subject to the judicial review of the Beijing intermediate court via a proceeding called "administrative action." The rulings of the Beijing intermediate court are subject to review by the Beijing High Court. The PRB process can generally take from over a year to several years.

### *Infringement Evidence*

The infringement evidence the plaintiff presents must prove that the defendant has executed or is executing an alleged infringing act. Evidence can include the defendant's product, promotional material, product samples and sales contracts. Information from the internet may be used as evidence, but it should first be notarized or certified. Witness testimony may also serve as evidence, but the witness must be cross-examined before the court to enhance the authenticity and acceptability of such evidence.

When it is difficult or impossible, for some objective reason, for the plaintiff to obtain evidence, a request may be made for the court to collect evidence. When evidence is likely to be lost or destroyed, a plaintiff may apply for evidence preservation. The plaintiff applying to the court for evidence collection and preservation must inform the court of the title and location of the evidence as well as the name and location of the evidence holder.

### *Burden of Proof and Reversal Thereof*

Generally, the plaintiff has the burden of proof in connection with the facts claimed. That is, the plaintiff is under the burden of proving the right claimed and the existence of the alleged infringement. If the plaintiff claims damages, evidence should be adduced to that effect.

There is an exception to the general burden of proof rule. When an infringement dispute involves a process for making a new product, the defendant needs to furnish evidence showing that the allegedly infringing process for making the product is different from a patented process. The patent law then requires the plaintiff to show that the product made by the patented process has at least a "unique feature" pertaining to the patented process. This requirement essentially turns the process patent into a "product by process" patent and sometimes obviates the purpose of the reversal of the burden of proof.

Another situation involves the burden of proof in connection with the amount of damages. The plaintiff may calculate damages on the basis of one of the following: the plaintiff's losses, the defendant's benefits, multiplication of the reasonable license fees or royalties or the statutory amount of damages, not exceeding 500,000 RMB (US\$62,500<sup>4</sup>). In practice, because the plaintiff sometimes finds it difficult to prove the amounts of the first three choices, statutory damages may be requested in the largest possible amount. The defendant can present evidence (of the volume of production and sales, for example) to repudiate the amount of damages claimed by the plaintiff.

<sup>4</sup> At the rate of 8 RMB per US\$1.

## Conclusion

China's intellectual property enforcement system is in its early stages of development. It will mature as China's technology economy matures. It is reported that China has overtaken the US as the country that receives the most patent applications, albeit most of the filings are utility model applications. It is foreseeable that many of these patents will enter the litigation stage.

*Zhaoyang (Paul) Li, Associate, San Francisco*

## New Chinese Regulation Strengthens Protection of Copyrighted Work on the Internet

### Key Points:

- ***Requires royalty payment to copyright holders***
- ***Provides penalties for infringement***

On May 18, 2006, the State Council promulgated a new regulation to strengthen the protection of copyrighted work disseminated over the Internet. China is preparing to sign the Internet Treaty under the World Intellectual Property Organization ("WIPO"), and this regulation is a part of a package of regulations required of countries joining the treaty.

While the PRC Copyright Law grants copyright owners the right to publish or disseminate works over wired and wireless networks, the new regulation focuses on publication or dissemination over the Internet and provides a range of protection for works published there, as well as penalties for copyright infringement.

The regulation requires persons who disseminate a copyrighted work through the Internet to obtain authorization from the copyright owner and pay royalties to the owner. In certain circumstances such as educational uses, where authorization is not required, users such as universities must adopt proper technical measures to prevent the work from being accessed by the public.

The administrative government office has the authority to investigate possible copyright infringements. The government office may request the network administrator or owner to provide detailed information on the suspected infringer if it believes an infringement has occurred, such as name, contact information, IP address and other necessary information. If the network provider, administrator or owner refuses to cooperate with the government, the authority may confiscate that provider's equipment.

If the copyright owner discovers that his or her work has been offered, linked to or stored in any Internet space without permission, he or she may send a written notice to the network administrator or owner. The network administrator or owner must suspend all access to the work immediately and notify the client who added the link or stored the work on the network. If the network administrator or owner receives a written counterargument from the client, the administrator or owner must reactivate the link and access to the stored work to the public and forward the counterargument to the alleged copyright owner. The administrator or owner is then exempt from further obligation and liability in connection to the disputed copyright issue.

The regulation also specifies penalties for violations. Copyright holders will have the right to claim civil damages against parties for unauthorized dissemination of their work on the Internet or for offering techniques or means by which to bypass technical measures in place for protecting their work on a network. The infringer or violator may also be fined by the authority and its illegal income may be confiscated.

The authority may confiscate the equipment of, impose an RMB100,000 fine upon, and even pursue criminal prosecution of parties who develop, import or offer the means by which to bypass copyright protection techniques or equipment.

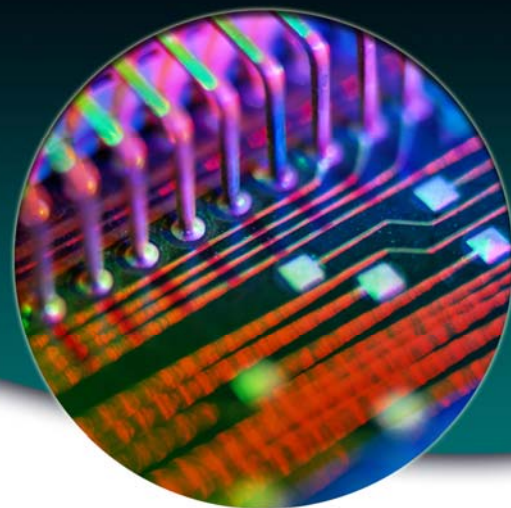
*Weiheng Jia*

## Editor's Corner

In the Winter 2006 edition of our newsletter, we noted that in an effort to address the financial burdens imposed by patent litigation a couple of companies were providing financing for plaintiffs. Recently, we learned that Fremont Bank, a bank situated in Northern California's Silicon Valley, is planning on providing a new financing product for local companies interested in purchasing insurance policies for intellectual property claims. Given the anecdotal evidence that such policies are usually quite expensive, the ability for small and start-up companies to amortize the insurance premiums over time may prove quite attractive to companies whose cash flow would otherwise make the premiums prohibitively expensive. You may contact Mike Nicholson (925.314.1425) at Fremont Bank for further information.

*The contents of this newsletter are not intended to serve as legal advice related to individual situations or as legal opinions concerning such situations. Counsel should be consulted for legal planning and advice.*

©Squire, Sanders & Dempsey L.L.P.  
All Rights Reserved  
September 2006



## Squire Sanders Intellectual Property Practice

### Nathan Lane III

Intellectual Property Practice Group Leader  
+1.415.954.0249, San Francisco  
+1.650.843.3322, Palo Alto  
nlane@ssd.com

### James M. Smith

Intellectual Property Update Editor  
Palo Alto  
+1.650.843.3230  
jmsmith@ssd.com

### Majid AlBassam

Tyson's Corner  
malbassam@ssd.com

### Adam R. Fox

Los Angeles  
afox@ssd.com

### Caroline H. Mead

San Francisco  
cmead@ssd.com

### Charna E. Sherman

Cleveland  
cesherman@ssd.com

### Angela M. Augustus

San Francisco  
aaugustus@ssd.com

### Douglas H. Goldhush

Tyson's Corner  
dgoldhush@ssd.com

### Joseph A. Meckes

San Francisco  
jmeckes@ssd.com

### Bryan A. Sims

Tyson's Corner  
bsims@ssd.com

### Olga M. Bezrukova

Moscow  
obebrukova@ssd.com

### Philip J. Graves

Los Angeles  
pgraves@ssd.com

### A.J. Moss

Phoenix  
amoss@ssd.com

### James M. Smith

Palo Alto  
jmsmith@ssd.com

### Barry D. Brown

Palo Alto  
bbrown@ssd.com

### Anna A. Grozovskaya

Moscow  
agrozovskaya@ssd.com

### Hisako Muramatsu

Los Angeles  
hmuramatsu@ssd.com

### Michael E. Sobel

Palo Alto  
msobel@ssd.com

### David E. Brown

Tyson's Corner  
dbrown@ssd.com

### Chris Hubbard

London  
chubbard@ssd.com

### Arlene P. Neal

Tyson's Corner  
aneal@ssd.com

### Jeffrey C. Talkington

San Francisco  
jtalkington@ssd.com

### Kristin C. Castle

San Francisco  
kcastle@ssd.com

### Cameron K. Kerrigan

San Francisco  
ckerrigan@ssd.com

### Jacqueline M. Nicol

Phoenix  
jnicol@ssd.com

### Linda Teng

Beijing  
lteng@ssd.com

### Nicholas Chan

Hong Kong  
nchan@ssd.com

### Suzanne K. Ketler

Cleveland  
sketler@ssd.com

### Stephen T. Owens

Los Angeles  
sowens@ssd.com

### James D. Troxell

Cleveland  
jtroxell@ssd.com

### Alicia M. Choi

Tyson's Corner  
amchoi@ssd.com

### Nathan Lane III

San Francisco  
nlane@ssd.com

### Daniel B. Pollack

Palo Alto  
dpollack@ssd.com

### Aaron R. Winger

Shanghai  
awinger@ssd.com

### Francesca E. Crisera

San Francisco  
fcrisera@ssd.com

### Zhaoyang Li (Paul)

San Francisco  
zli@ssd.com

### David E. Rogers

Phoenix  
drogers@ssd.com

### Han Yu

Los Angeles  
hyu@ssd.com

### David S. Elkins

Palo Alto  
delkins@ssd.com

### Mark Lupkowski

San Francisco  
mlupkowski@ssd.com

### Bernard F. Rose

San Francisco  
brose@ssd.com

### Philip Zender

San Francisco  
pzender@ssd.com

### Matthew J. Evans

Phoenix  
mjevans@ssd.com

### Eric G. S. Marcks

San Francisco  
emarcks@ssd.com

### Angela Scott

Miami  
anscott@ssd.com

### Peter C. Flanagan

Tyson's Corner  
pflanagan@ssd.com

### Jose Luis Martin

Palo Alto  
jlmartin@ssd.com

### Song Zhu

Palo Alto  
szhu@ssd.com

### NORTH AMERICA

Cincinnati  
Cleveland  
Columbus  
Houston  
Los Angeles  
Miami  
New York  
Palo Alto  
Phoenix  
San Francisco  
Tallahassee  
Tampa  
Tyson's Corner  
Washington DC  
West Palm Beach

### LATIN AMERICA

Buenos Aires\*  
Caracas  
Rio de Janeiro  
Santiago\*  
Santo Domingo

### EUROPE

Bratislava  
Brussels  
Bucharest\*  
Budapest  
Dublin\*  
Frankfurt  
Kyiv\*  
London  
Milan\*  
Moscow  
Prague  
Warsaw

### ASIA

Beijing  
Hong Kong  
Shanghai  
Tokyo

Associated Office\*