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## **1 ARTICLE 59**

### **1.1 Text of Article 59**

#### **Article 59**

##### *Remedies*

Without prejudice to other rights of action open to the right holder and subject to the right of the defendant to seek review by a judicial authority, 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. In regard to counterfeit trademark goods, the authorities shall not allow the re-exportation of the infringing goods in an unaltered state or subject them to a different customs procedure, other than in exceptional circumstances.

### **1.2 "infringing goods"**

1. In *China – Intellectual Property Rights*, the Panel clarified that, when read in context with Article 51, the infringing goods covered by the first sentence of Article 59 are those covered, as a minimum, under Article 51, i.e. imported "counterfeit trademark or pirated copyright goods":

"The first sentence of Article 59 applies to 'infringing goods'. The ordinary meaning of these words is not limited to goods that infringe any specific rights. However, read in context, there are certain limitations. The first sentence of Article 51 provides for the relevant procedures to apply, as a minimum, to 'the importation' of 'counterfeit trademark or pirated copyright goods'. This applies to Article 59 for the reasons set out ... above."<sup>1</sup>

2. In *China – Intellectual Property Rights*, the Panel also clarified that Article 59, when understood in context with Article 51, expressly allows Members, as an option, to provide for procedures at the border for *other* infringing goods:

"The second sentence provides for an optional extension to 'other infringements of intellectual property rights'. This is a reference both to goods that infringe trademarks and copyright without constituting counterfeit trademark goods or pirated copyright goods, as well as to goods that infringe other categories of intellectual property rights, such as patents. The second sentence includes an express condition that applies where Members provide border measures for other infringements of intellectual property rights, namely 'provided that the requirements of this Section are met'.<sup>2</sup> The

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<sup>1</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.221.

<sup>2</sup> (*footnote original*) There are some express differences between the procedures applicable to different goods: Article 53.2 of the TRIPS Agreement only applies to goods involving industrial designs, patents, layout-designs or undisclosed information; the second sentence of Article 59 only applies to counterfeit trademark goods.

requirements of that 'Section' include those found in Article 59. Therefore, to the extent that a Member provides for such an application to be made in respect of goods involving other infringements of intellectual property rights, such as patents, the obligation in Article 59 applies."<sup>3</sup>

3. The Panel in *China – Intellectual Property Rights* further clarified that Article 59, when understood in context with Article 51, contains an option, but not an obligation, to provide for its application to goods destined for exportation:

"The third sentence of Article 51 provides for an optional extension to 'infringing goods destined for exportation' from a Member's territory. The terms of the third sentence do not attach any express condition to this option. An option with respect to 'corresponding procedures' is not, on its face, an obligation that procedures shall correspond. The omission of any express condition in the third sentence stands in contrast to the proviso in the second sentence, which also serves the purpose of providing for an optional extension of the border measures. Whilst it would not have been appropriate to include an identical condition to that found in the second sentence, as the requirements of Section 4 refer to importation, the third sentence could nevertheless have included an express condition that the procedures with respect to infringing goods destined for exportation shall correspond to those set out in the Section, or shall comply with the principles thereof.<sup>4</sup> However, it does not. Read in context, this omission is not ambiguous. Therefore, the Panel finds that there is no obligation to apply the requirements of Article 59 to goods destined for exportation."<sup>5</sup><sup>6</sup>

### 1.3 "shall have the authority"

4. In *China – Intellectual Property Rights*, the Panel considered that, under Article 59, the obligation that the authorities "shall have the authority" to make certain orders applies from the time that competent authorities find that goods subject to suspension at the border are infringing, right until the time a remedy is ordered:

"The obligation in the first sentence of Article 59 is that competent authorities 'shall have the authority' to order certain types of remedies with respect to infringing goods. It is clear from the context within Section 4 that the obligations in Article 59 apply where customs authorities have suspended the release into free circulation of goods suspected of infringing intellectual property rights. The fact that Article 59 applies to 'infringing goods' indicates that the obligations in this Article are triggered when competent authorities find that the goods subject to the suspension are infringing. The fact that Article 59 addresses the authority to order remedies implies that the obligations continue until the time that a remedy has been ordered. The text of the Article does not indicate any other limitation on the temporal scope of the obligations. Therefore, the obligation that competent authorities 'shall have the authority' to make certain orders applies from the time that competent authorities find that goods subject to suspension at the border are infringing, right up until the time that a remedy is ordered."<sup>7</sup>

5. In *China – Intellectual Property Rights*, the Panel also considered that the phrase "shall have the authority" does not mean, unless otherwise specified, any obligation that a competent authority shall *exercise* its authority in a particular way:

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<sup>3</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.223.

<sup>4</sup> (*footnote original*) For example, Articles 49 and 50.8 of the TRIPS Agreement provide for optional procedures, subject to a contingent obligation that they "shall conform to principles equivalent in substance to those set forth" in the relevant Sections. In contrast, footnote 13 to the TRIPS Agreement sets out an option but contains no contingent obligation. However, footnote 13 limits the scope of the obligation in the first sentence of Article 51 rather than providing for an optional extension.

<sup>5</sup> (*footnote original*) The text of Article 59 itself provides a confirmation of this point. The second sentence refers to the "re-exportation" of the infringing goods not "exportation", which implies that the counterfeit trademark goods are only presented for importation.

<sup>6</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.224.

<sup>7</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.234.

"The Panel notes that the word 'authority' can be defined as 'power or right to enforce obedience; moral or legal supremacy; right to command or give a final decision.'<sup>8</sup> The obligation is to 'have' authority not an obligation to 'exercise' authority.<sup>9</sup> The phrase 'shall have the authority' is used throughout the enforcement obligations in Sections 2, 3 and 4 of Part III of the TRIPS Agreement, specifically, in Articles 43.1, 44.1, 45.1, 45.2, 46, 48.1, 50.1, 50.2, 50.3, 50.7, 53.1, 56 and 57.<sup>10</sup> It can be contrasted with terminology used in the minimum standards of protection in Part II of the TRIPS Agreement, such as 'Members shall provide' protection, or that certain material 'shall be' protected. The obligation in Article 46 that certain authorities 'shall have the authority' to make certain orders reflects *inter alia* that orders with respect to specific infringements are left to enforcement authorities' discretion.<sup>11</sup>

...

Therefore, the obligation that competent authorities 'shall have the authority' to make certain orders is not an obligation that competent authorities shall exercise that authority in a particular way, unless otherwise specified."<sup>12</sup>

6. In *China – Intellectual Property Rights*, the Panel further considered that the obligation to have authority to order certain remedies under Article 59 does not mean that these are the only remedies a Member can allow its competent authorities to order. Interpreting Article 59 in context with Article 41, the Panel stated:

"Moreover, the obligation to have the authority to order certain types of remedies is not an obligation to have the authority to order those remedies *only*. Both parties to the dispute, and certain third parties, expressly recognize that the obligation that competent authorities 'shall have the authority' to order certain types of remedies leaves Members free to provide that competent authorities may have authority to order *other* remedies not required to be within their authority by Article 59 of the TRIPS Agreement.

The Panel agrees. The terms of Article 59 do not indicate that the authority to order the specified types of remedies must be exclusive. This interpretation is confirmed by Article 46, which forms part of the context of Article 59, as Article 59 incorporates the principles of Article 46, and both Articles are phrased as obligations that authorities 'shall have the authority' to order certain types of remedies. The first sentence of Article 46 provides, basically, that authorities shall have the authority to order that goods be disposed of *outside* the channels of commerce *or* destroyed. At the same time, the fourth sentence of Article 46 relates to release *into* the channels of commerce which does not correspond to either of the remedies required by the first sentence. This is an express recognition that the remedies set out in the first sentence of Article 46 are not exhaustive. The same position applies under Article 59."<sup>13</sup>

7. The Panel in *China – Intellectual Property Rights* cautioned however that the fact that Members can provide other remedies besides those provided under Article 59 can sometimes be WTO-inconsistent:

"Whilst authority to order a disposition method *not* required by Article 59 does not, in itself, lead to WTO-inconsistent action, to the extent that such authority mandates a disposition method in any given circumstance it may preclude authority that *is* required by Article 59. The preclusion of such authority may be WTO-inconsistent.

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<sup>8</sup> (footnote original) *New Shorter Oxford English Dictionary* (1993).

<sup>9</sup> (footnote original) This is without prejudice to other obligations regarding enforcement.

<sup>10</sup> (footnote original) The phrasing in Article 57 is slightly different. The phrase "shall have the authority" is also used in Articles 31(g), (k) and 34.1 in Part II of the TRIPS Agreement.

<sup>11</sup> (footnote original) Certain obligations guide the exercise of that discretion, for example, the principle of proportionality and the need to take into account the interests of third parties under the third sentence of Article 46.

<sup>12</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.236-7.238.

<sup>13</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.239-7.240. See also paras. 7.285, 7.309 and 7.327.

For that reason, the Panel will examine whether certain aspects of the Customs measures are mandatory."<sup>14</sup>

8. In *China – Intellectual Property Rights* the parties disagreed as to the circumstances in which competent authorities may be considered to have "authority" in accordance with Article 59, in particular, the extent to which the availability of authority may be subject to conditions. In this respect, the Panel first observed that the obligation under the first sentence of Article 59 would be satisfied even if a competent authority has authority to order only one of the two remedies under that Article:

"The Panel observes that the reference to alternatives in Article 59 of the TRIPS Agreement implies a particular type of condition. Article 59 requires authority to order 'destruction or disposal' (emphasis added). It is not disputed that where competent authorities have authority in any given situation within the scope of Article 59 to order *either* destruction or disposal (in accordance with applicable principles), this is sufficient to implement the obligation in the first sentence of Article 59. Therefore, a condition that precludes the authority to order one remedy (e.g. destruction) could be consistent with Article 59 as long as competent authorities still had the authority to order the other remedy (in this example, disposal)."<sup>15</sup>

9. The Panel in *China – Intellectual Property Rights* then observed that the phrase "shall have the authority" does not require Members to take any action in the absence of an application or request:

"The Panel also observes that a common feature of Sections 2, 3 and 4 of Part III of the TRIPS Agreement is that the initiation of procedures under these Sections is generally the responsibility of private right holders. This is reflected in the first sentence of Article 42 and the first sentence of Article 51, the reference to an 'applicant' in Article 50.3 and 50.5, the reference to 'request[s]' in Articles 46 and 48.1, and the option (not obligation) to make *ex officio* action available under Article 58. Viewed in context, the phrase 'shall have the authority' does not require Members to take any action in the absence of an application or request. Therefore, a condition that authority shall only be available upon application or request seems to be assumed in much of Sections 2, 3 and 4 of Part III. This is consistent with the nature of intellectual property rights as private rights, as recognized in the fourth recital of the preamble of the TRIPS Agreement. Acquisition procedures for substantive rights and civil enforcement procedures generally have to be initiated by the right holder and not *ex officio*."<sup>16</sup>

#### 1.4 "disposal"

10. The Panel in *China – Intellectual Property Rights* observed that the 'authority' required by Article 59 concerns two types of remedies, namely "destruction or disposal". The Panel considered that the meaning of "destruction" was not a controversial one. As for "disposal", the Panel considered that it meant disposal "outside the channels of commerce":

"[T]he Panel notes that the English text of Article 59 does not qualify this word so that it could, in accordance with its ordinary meaning, refer both to disposal outside the channels of commerce as well as to release into the channels of commerce. However, read in context, the word 'disposal' could be a reference to an order that goods be 'disposed of' outside the channels of commerce as set out in Article 46. This ambiguity is resolved by reference to the French and Spanish texts, which are equally authentic. The French text of Article 59 refers to authority to order 'la mise hors circuit' which is a reference to the authority to order that infringing goods be 'écartées des circuits commerciaux' in Article 46. The Spanish text of Article 59 refers to authority to order 'eliminación' which, read in its context as an alternative to 'destrucción', is evidently a reference to the authority to order that infringing goods be 'apartadas de los circuitos comerciales' in Article 46. Accordingly, the correct

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<sup>14</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.252.

<sup>15</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.246. See also *ibid.* para. 7.251.

<sup>16</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.247.

interpretation of the term 'disposal' in the first sentence of Article 59 is disposal 'outside the channels of commerce'.<sup>17</sup>

## 1.5 "the principles set out in Article 46"

### 1.5.1 General

11. In *China – Intellectual Property Rights*, the Panel first noted that the principles set out in Article 46 attach to the obligation in Article 59 to provide for the "authority to order the destruction or disposal of infringing goods" and that Article 59 does not include the authority to the disposition of materials and implements:

"The first sentence of Article 59 provides that competent authorities shall have the authority to order the destruction or disposal of infringing goods 'in accordance with the principles set out in Article 46'. The phrase referencing the principles set out in Article 46 attaches to 'the authority to order the destruction or disposal of infringing goods'. This directs the treaty interpreter to those principles in Article 46 that attach to such authority.<sup>18</sup>

The Panel makes the following observations. First, Article 59 refers to 'authority'. Second, Article 59 incorporates principles that attach to authority to order 'destruction or disposal' (outside the channels of commerce ...). Third, Article 59 relates to the authority to order destruction or disposal of 'infringing goods' but not principles applicable to the disposition of materials and implements.<sup>19</sup>

12. In *China – Intellectual Property Rights*, the Panel then considered that the principles set out in Article 46 incorporated in the first sentence of Article 59 were those contained in the third and fourth sentences of Article 46. The Panel first made the following general considerations with respect to these principles:

"Article 59 refers to the 'principles' set out in Article 46. Therefore, it is necessary to determine what precisely that refers to in the first, third and fourth sentences of Article 46. The word 'principles' can be defined as 'a general law or rule adopted or professed as a guide to action.' Each of these sentences of Article 46 contains language that is a guide to action by authorities and none dictate the precise terms of orders in specific cases.

The Panel does not consider that the choice of the word 'principles' was intended to reflect a hierarchy of provisions within Article 46 that would include only the most general concepts and exclude the less general. There is a strong similarity in the language and purpose of the two provisions that both provide for authority to order destruction or disposal with respect to goods that have been found to infringe intellectual property rights at the conclusion of an enforcement procedure. However, there are also differences in the government agencies to which they relate ('competent authorities' to order remedies in border measures under Article 59 but 'judicial authorities' under Article 46) and also in the scope of property to which the remedies apply ('infringing goods' under Article 59 and 'infringing goods as well as materials and implements the predominant use of which has been in the creation of the infringing goods' under Article 46). These differences made it inappropriate simply to provide that the obligation in Article 59 applied 'in accordance with Article 46' or otherwise incorporate the whole of Article 46. Instead, the cross-reference to 'principles' avoided the duplication of a relatively large amount of text. Therefore, in the Panel's view, the reference to 'principles' is a reference to language that is a guide to action by authorities with respect to orders for the destruction or disposal of infringing goods.<sup>20</sup>

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<sup>17</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.279.

<sup>18</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.255.

<sup>19</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.256. See also para. 7.259.

<sup>20</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.264-7.265.

13. The Panel in *China – Intellectual Property Rights* then listed the following principles contained in the first, third and fourth sentences of Article 46 that serve as guide to action by authorities with respect to orders for the destruction or disposal of infringing goods:

"Accordingly, for the purposes of Article 59, the Panel considers that the first sentence of Article 46 sets out the following 'principles':

- (a) authorities shall have the authority to order disposal or destruction in accordance with the first sentence 'without compensation of any sort'; and
- (b) authorities shall have the authority to order disposal 'outside the channels of commerce in such a manner as to avoid any harm caused to the right holder'; or
- (c) authorities shall have the authority to order destruction 'unless this would be contrary to existing constitutional requirements'.

The third sentence sets out the following principle that applies *inter alia* to the authority to order disposal or destruction of infringing goods under the first sentence:

- (d) in considering such requests 'the need for proportionality between the seriousness of the infringement and the remedies ordered as well as the interests of third parties shall be taken into account'.

The fourth sentence sets out the following principle that attaches to the authority to order destruction or disposal of infringing goods under the first sentence:

- (e) in 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.

The interpretation of all these principles is informed by the common objective set out at the beginning of Article 46, i.e. 'to create an effective deterrent to infringement' which is, in itself, also a guide to action with respect to orders for the destruction or disposal of infringing goods and, hence, a principle set out in Article 46."<sup>21</sup>

14. The Panel in *China – Intellectual Property Rights* rejected the argument that, in effect, the second sentence of Article 59 constitutes a *lex specialis* that would exclude the incorporation of the fourth sentence of Article 46 into Article 59. In rejecting this argument, the Panel made the following observations with respect to the language of the fourth sentence of Article 46 and the second sentence of Article 59:

"Like the fourth sentence of Article 46, this sentence begins with the words '[i]n regard to counterfeit trademark goods' and includes the words 'other than in exceptional' circumstances (as opposed to cases). There is also a similarity in that the second sentence of Article 59 applies to goods 'in an unaltered state' whilst the fourth sentence of Article 46 applies to 'the simple removal of the trademark unlawfully affixed' which is a means of altering the state of counterfeit trademark goods. Both sentences are found in Articles that provide for remedies after particular enforcement procedures.

However, Article 59 applies to procedures at the border with respect to goods destined for importation whilst Article 46 applies to civil judicial procedures within Members' territories. The second sentence of Article 59 refers to re-export or release into a different customs procedure (for example, into transit) which is specific to the enforcement procedure in Section 4. Article 46 refers to release into the channels of commerce which can be applicable to importation and domestic sale in both Sections 2

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<sup>21</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.266-7.269.

and 4. The second sentence of Article 59 and the fourth sentence of Article 46 apply in different circumstances and neither is in fact more specific than the other."<sup>22</sup>

**1.5.2 Principle in the first sentence of Article 46: "outside the channels of commerce in such a manner as to avoid any harm caused to the right holder"**

15. In *China – Intellectual Property Rights* the parties disagreed as to the meaning of the principle set out in the first sentence of Article 46 that refers to disposal "outside the channels of commerce in such a manner as to avoid any harm caused to the right holder". The Panel addressed the meaning of this principle and a concern raised by one of the parties concerning the harm that donations may cause to right holders and the possibility that the donated goods may later be sold by the social welfare bodies:

"The Panel notes that this principle, by its terms, relates to disposal of goods 'outside' the channels of commerce, and not into the channels of commerce. It is not disputed that this principle is applicable to donations (i.e. gifts) to social welfare bodies for their own use or for charitable distribution. However, if the social welfare bodies later *sell* goods donated to them by Customs for charitable distribution, even to raise money for charitable aims, the goods are not in fact disposed of outside the channels of commerce but *into* the channels of commerce. If the social welfare bodies charitably distribute goods donated to them by Customs but the goods later find their way back into the channels of commerce, this does not alter the fact that the goods were disposed of outside the channels of commerce, in the ordinary sense of 'disposal'. Instead, the later sale of the distributed goods is relevant to the assessment of whether the disposal outside the channels of commerce was 'in such a manner so as to avoid any harm caused to the right holder'. Therefore, the Panel will consider the interpretation of that part of the principle in further detail.

This principle, by its terms, provides that authorities shall have the authority to order that the goods 'be disposed of', in the passive voice. There is no obligation that the relevant authorities carry out the disposal themselves but rather they may entrust the actual disposal to another body. The carrying out of disposal 'outside the channels of commerce' recognizes the opportunity for involvement of other bodies, such as charities, or non-commercial use by government. The principle attaches to the 'manner' in which infringing goods are disposed of, not to the actual disposal. Authorities are not held responsible for acts of the bodies carrying out the disposal that is beyond the authorized manner. Further, the principle is that the manner shall be 'so as to' avoid harm. This is phrased in terms of purpose, not result. The responsibility of the authorities is to ensure that the manner in which the goods are disposed of outside the channels of commerce is designed in such a way that it will comply with the principle."<sup>23</sup>

16. The Panel in *China – Intellectual Property Rights* addressed the specific requirement within this principle that the manner of disposal shall "avoid" harm:

"The principle is that the manner of disposal shall 'avoid' harm. China argues that this is an obligation to 'pay due regard to'. However, the Panel notes that the ordinary meaning of 'avoid' can be defined as 'keep off, prevent; obviate'. Further, the principle is that the manner shall avoid 'any' harm caused to the right holder, not just 'harm' or 'some' harm. Therefore, the manner of disposal must be designed in such a way as to prevent any harm occurring to the right holder.

It must be recalled that disposal of infringing goods outside the channels of commerce, in context, is an alternative to destruction of the goods. In the Panel's view, this implies that any inherent risk of harm due simply to the fact that the goods have not been completely destroyed is insufficient to disqualify a disposal method, as it would nullify the choice between disposal and destruction. However, more specific concerns linked to harm caused to the right holder by a particular manner of disposal are relevant in assessing conformity with the principle that disposal outside the

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<sup>22</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.273-7.274.

<sup>23</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.279-7.280.

channels of commerce be 'in such a manner as to avoid any harm caused to the right holder'.

The Panel finds confirmation of this interpretation within Article 46. The fourth sentence of Article 46 expressly provides that simple removal of the trademark unlawfully affixed is not sufficient to permit release of counterfeit trademark goods *into* the channels of commerce other than in exceptional cases. In contrast, the first sentence of Article 46 contains a more general requirement that the requisite authority to order disposal of goods outside the channels of commerce shall be 'in such a manner as to avoid any harm caused to the right holder'. Whilst this reflects, in part, the fact that the first sentence does not only apply to counterfeit trademark goods, it also demonstrates that when goods are disposed of *outside* the channels of commerce it is not assumed that the removal of the trademark is required (or insufficient).

It remains possible that the trademark unlawfully affixed may cause confusion, depending on the circumstances in which goods are disposed of outside the channels of commerce. Practical requirements, such as removal of the trademark, affixation of a charitable endorsement or controls over the use of goods or distribution methods, may avoid confusion. The cooperation of the right holder would be valuable in this regard but the terms of the Article do not indicate that that is a requirement. However, the issue of harm to the right holder, whether to its reputation or through lost sales, through disposal of goods outside the channels of commerce without removal of the trademark unlawfully affixed depends on the circumstances. Otherwise, any disposal outside the channels of commerce where persons could simply observe a counterfeit trademark would be presumed to cause harm to the right holder. This result is not contemplated by the terms of Article 46, as the possibility of observing the counterfeit trademark is incidental to the requisite authority not to destroy the goods."<sup>24</sup>

17. The Panel in *China – Intellectual Property Rights* examined a claim with respect to customs measures from China that contained certain optional disposition methods of infringing goods besides destruction (i.e., donation to social welfare bodies, sale to the right holder and auction). The claim was that, under such measures, competent authorities lacked authority to order disposal of such infringing goods in accordance with the principles of the first sentence of Article 46 as incorporated in Article 59. With respect to these three optional disposition methods, the Panel concluded, respectively, that the complainant had not established that Chinese Customs lacked such authority in accordance with the principles of Article 46.<sup>25</sup>

18. With respect to auction, the Panel in *China – Intellectual Property Rights* was confronted with the complainant's claim that, under the measures at issue, this disposition method was mandatory, in effect precluding the authority to order destruction of the infringing goods in violation of the principles set out in the first sentence of Article 46. The Panel began with the following considerations:

"The Panel will now consider Customs' authority to order that infringing goods be auctioned. Auction is the third disposal method set out in the measures at issue. Auction is not a form of destruction, and it is undisputed that auction is *not* a form of disposal outside the channels of commerce. Accordingly, this disposal method is clearly *not* required by Article 59. However, the Panel recalls its finding ... that the remedies specified in Article 59 are not exhaustive. Therefore, the fact that authority to order auction of infringing goods is not required is not in itself inconsistent with Article 59.

The United States claims that, because the auction method is allegedly mandatory, it deprives Customs of the authority to order destruction of infringing goods at a certain point within the purview of Article 59. It does not allege that Customs has authority

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<sup>24</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.281-7.284.

<sup>25</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.286-7.324 (with respect donation to social welfare bodies); paras. 7.325-7.326 (with respect sale to the right holder); and paras. 7.327-7.355 (with respect to auction).



to order donation to social welfare bodies (or sale to the right holder) in circumstances where Customs is considering auction. In these circumstances, it is assumed that Customs has already decided against those other methods. The issue is only whether the authority to order auction precludes authority to order *destruction* of infringing goods."<sup>26</sup>

19. Then, after reviewing the language of the measures before it, the Panel first found that the complainant had not "established that the Customs measures on their face oblige Customs to order the auction of infringing goods."<sup>27</sup> The Panel then turned to the evidence before it in order to confirm such finding:

"It is apparent that the number of shipments destroyed far exceeds the number of shipments auctioned, and that in three years Customs has only decided to auction goods twelve times. In fact, no infringing goods destined for importation have ever been auctioned under the measures at issue during the period for which statistics are available. Customs evidently has little, if any, difficulty in choosing to destroy goods, which is consistent with the view that it has wide authority to do so.

The Panel notes that there is a small number of cases where Customs has ordered the auction of goods. However, the small number of cases of auction does not indicate whether this was pursuant to a choice not to destroy the goods, or whether Customs considered that it lacked the authority to destroy the goods. The Panel reiterates that the pertinent issue is whether Customs was *permitted* by law to order destruction in those cases. The United States agrees that a Member may *choose* between destruction and auction in its discretion provided that it has unconditional power to order destruction in all circumstances.

The very low rate of auctions is consistent with the view that auctions are not mandatory. It could be consistent with the view that the auction method is mandatory if there were some indication that the infringing features cannot be eradicated from an exceedingly large number and proportion of goods confiscated by Customs. However, in the absence of such evidence, and in light of the other evidence discussed above, the Panel does not accept that view."<sup>28</sup>

20. Finally, with the above considerations in mind, the Panel found that the complainant had not "established that the authority to order auction of infringing goods under the Customs measures precludes authority to order destruction of infringing goods in accordance with the principles set out in the first sentence of Article 46."<sup>29</sup>

### **1.5.3 Principle in the fourth sentence of Article 46: "simple removal of the trademark unlawfully affixed"**

21. In *China – Intellectual Property Rights*, the Panel examined a claim with respect to the authority given by the measures at issue to release infringing goods into the channels of commerce by auctioning them. The claim was that such authority did not comply with the principle in the fourth sentence of Article 46, as incorporated in Article 59, which states:

"In 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."

22. The Panel first considered that even if under the measures auction was not a mandatory disposition method, and even if auction has never been used in practice with respect to imports, it could still be scrutinized, "as such", under the principle in the fourth sentence of Article 46:

"The Panel recalls its finding ... that the obligation in Article 59 applies both to mandatory and discretionary measures as the obligation that Members' competent

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<sup>26</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.327-7.328.

<sup>27</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.343.

<sup>28</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.351-7.353.

<sup>29</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.354.

authorities 'shall have the authority' to make particular orders attaches to what the authorities are *permitted* by law to order, not only to what they *must* order. This finding applies *a fortiori* to the principle in the fourth sentence of Article 46 as only discretionary authority to order release of goods into the channels of commerce will not preclude the authority required by the first sentence of Article 46 at some point. The principle in the fourth sentence of Article 46 regarding authority to order the release of goods into the channels of commerce, as an alternative to destruction or disposal outside the channels of commerce, could be redundant if it did not apply to discretionary measures.<sup>30</sup> Therefore, the fact that authority to release goods into the channels of commerce is not mandatory does not shield such a disposition method from a Panel's assessment of its conformity 'as such' with Article 59 of the TRIPS Agreement, as it incorporates the principle in the fourth sentence of Article 46.

This particular case also presents a specific set of circumstances. The nature of the measures at issue is such that, even if they do not mandate auction (and do not preclude authority to order destruction) the elimination of the infringing features *is* mandatory in every case where Customs chooses to auction infringing goods (as discussed below). If the elimination of the infringing features constitutes simple removal of the trademark, it will be inconsistent with the principle in the fourth sentence of Article 46, as incorporated by Article 59, in all cases where Customs orders auction of infringing goods. Although Customs has never auctioned goods destined for importation, this may be due only to the smaller volume of infringing goods destined for importation rather than exportation. China does not assert that Customs might auction goods destined for importation in future but defends its auction method based on its own good faith interpretation of the requirements of Article 59 of the TRIPS Agreement and of the fourth sentence of Article 46. Indeed, China advises the Panel that auction, whether of exports or imports, is a 'preferred' disposition method in certain circumstances and it vigorously defends its right to use it, albeit sparingly. Therefore, the Panel's rulings on the applicability of the fourth sentence of Article 46, as incorporated in Article 59, of the TRIPS Agreement and the conformity of China's auction method with that provision will, to the extent that the obligation is applicable, prevent China *ex ante* from engaging in certain conduct inconsistent with its obligations under a covered agreement, which is precisely the purpose of an 'as such' claim."<sup>31</sup>

23. The Panel then observed that, under the measures, the only action taken before the auction was the removal of the trademark from infringing goods. The Panel found that because such action constituted a "simple removal of a trademark" it was not consistent with the principle of the first sentence of Article 46.

"The Panel notes that the word 'simple' can be defined as 'with nothing added; unqualified; neither more nor less than; mere, pure'. A situation in which a trademark is removed from a good and no other action is taken will constitute 'simple' removal of the trademark. Therefore, the Panel's preliminary view is that eradication of the infringing features under the measures at issue constitutes 'simple' removal of the trademark as contemplated by the fourth sentence of Article 46, as incorporated by Article 59."<sup>32</sup>

24. In the Panel's view the fact that the measures provide for the right holders to be consulted and that the confiscated goods are subject to "reserved prices" are irrelevant to its finding that the measures provide for a simple removal of the trademark:

"Turning to the measures at issue, the Panel observes that the procedure for seeking comment by right holders does not affect the state of the goods, nor is there any obligation to take right holder's comments into account. Therefore, it is irrelevant to the question whether the measures at issue provide for 'simple removal of the trademark unlawfully affixed'.

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<sup>30</sup> (*footnote original*) The position is the same under the second sentence of Article 59.

<sup>31</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.358-7.359.

<sup>32</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.369.

China alleges that auctions of goods confiscated by Customs are subject to a reserve price that ensures that infringers do not have the opportunity to purchase the seized goods at an unreasonably low cost and reattach counterfeit marks.

The Panel does not agree. As China itself stated in its rebuttal submission, 'the very principle of trademark protection is that a trademark distinguishes a good and allows for a significant market premium'. The Panel points out that a counterfeit trademark is designed to obtain some or all of that economic premium. When the counterfeit trademark is removed, the value of the good is diminished and is less than its market value if it is resold with a counterfeit trademark reattached. In other words, it remains economically viable for the importer or a third party to purchase the goods at auction and reattach the trademarks in order to infringe again, with the heightened risk of this occurring discussed ... above. In any case, there is no evidence that the prices established by the method used by China Customs are so high that it is no longer economically viable to purchase the goods and reattach the trademarks."<sup>33</sup>

25. In making the above findings, the Panel also made various observations on the meaning and objective of the term "simple removal of the trademark":

"Viewed in light of the objective, the 'simple' removal of the trademark is principally a reference to the fact that the state of the goods is not altered in any other way so that the absence of the trademark is not an effective deterrent to further infringement. Removal of the trademark is not 'simple' if the state of the goods is altered sufficiently to deter further infringement.

...

The Panel notes that the fourth sentence of Article 46, by its specific terms, is not limited to an action to render goods non-infringing, which the simple removal of the trademark would achieve. Rather, the fourth sentence of Article 46 imposes an additional requirement beyond rendering the goods non-infringing in order to deter further acts of infringement with those goods. Therefore, it is insufficient, other than in exceptional cases, to show that goods that have already been found to be counterfeit are later unmarked. The release into the channels of commerce of such goods, while they may no longer infringe upon the exclusive rights in Article 16 of the TRIPS Agreement, will not comply with the requirement in the fourth sentence of Article 46, as incorporated by Article 59."<sup>34</sup>

26. Finally, the Panel considered that the "simple" removal of trademark under the measures at issue did not fall under the category of "exceptional cases" of simple removals permitted under the fourth sentence of Article 46, as incorporated in Article 59. As to the scope of this exception, the Panel stated:

"The Panel notes that the phrase 'other than in exceptional cases', read in context, refers to a subset of the cases covered by the fourth sentence of Article 46, as incorporated by Article 59, namely, those cases in which a Member's competent border authorities permit the release of goods that have been found to be counterfeit trademark goods into the channels of commerce."<sup>35</sup>

27. The Panel then consider the question of *how* to determine when any such case may be considered "exceptional":

"The Panel considers that the phrase 'other than in exceptional cases', like the rest of the principle set out in the fourth sentence of Article 46, must be interpreted in light of the objective of that Article, namely, 'to create an effective deterrent to infringement'. There may well be cases in which the simple removal of the trademark prior to release of the goods into the channels of commerce would not lead to further infringement. For example, an innocent importer who has been deceived into buying

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<sup>33</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.380-7.382.

<sup>34</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.373 and 7.379.

<sup>35</sup> Panel Report, *China – Intellectual Property Rights*, para. 7.389.

a shipment of counterfeit goods, who has no means of recourse against the exporter and who has no means of reaffixing counterfeit trademarks to the goods, might constitute such a case. However, such cases must be narrowly circumscribed in order to satisfy the description of 'exceptional'. Even when narrowly circumscribed, application of the relevant provision must be rare, lest the so-called exception become the rule, or at least ordinary.

The Panel does not consider that 'exceptional cases' for the purposes of the fourth sentence of Article 46 may simply be demonstrated by a low rate of cases in which simple removal of the trademark is treated as sufficient to permit release of goods into the channels of commerce. Firstly, 'exceptional cases' within the meaning of the fourth sentence of Article 46, as incorporated in Article 59, is not assessed in terms of a proportion of all cases of infringing goods seized at the border. Secondly, such an approach to goods that have already been found to be counterfeit trademark goods would amount to a margin of tolerance of further infringement that is not consistent with the objective of Article 46 of creating an effective deterrent."<sup>36</sup>

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<sup>36</sup> Panel Report, *China – Intellectual Property Rights*, paras. 7.391-7.392.