

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

*Report of the Panel*



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<b>Short Title</b>	<b>Full Case Title and Citation</b>
<i>Australia – Automotive Leather II</i>	Panel Report, <i>Australia – Subsidies Provided to Producers and Exporters of Automotive Leather</i> , WT/DS126/R, adopted 16 June 1999, DSR 1999:III, 951
<i>Brazil – Retreaded Tyres</i>	Appellate Body Report, <i>Brazil – Measures Affecting Imports of Retreaded Tyres</i> , WT/DS332/AB/R, adopted 17 December 2007
<i>Brazil – Retreaded Tyres</i>	Panel Report, <i>Brazil – Measures Affecting Imports of Retreaded Tyres</i> , WT/DS332/R, adopted 17 December 2007, as modified by Appellate Body Report, WT/DS332/AB/R
<i>Canada – Pharmaceutical Patents</i>	Panel Report, <i>Canada – Patent Protection of Pharmaceutical Products</i> , WT/DS114/R, adopted 7 April 2000, DSR 2000:V, 2289
<i>EC – The ACP-EC Partnership Agreement II</i>	Award of the Arbitrator, <i>European Communities – The ACP-EC Partnership Agreement – Second Recourse to Arbitration Pursuant to the Decision of 14 November 2001</i> , WT/L/625, 27 October 2005, DSR 2005:XXIII, 11703
<i>EC – Bed Linen</i>	Appellate Body Report, <i>European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India</i> , WT/DS141/AB/R, adopted 12 March 2001, DSR 2001:V, 2049
<i>EC – Chicken Cuts</i>	Appellate Body Report, <i>European Communities – Customs Classification of Frozen Boneless Chicken Cuts</i> , WT/DS269/AB/R, WT/DS286/AB/R, adopted 27 September 2005, DSR 2005:XIX, 9157
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<i>EC – Trademarks and Geographical Indications (Australia)</i>	Panel Report, <i>European Communities – Protection of Trademarks and Geographical Indications for Agricultural Products and Foodstuffs, Complaint by Australia</i> , WT/DS290/R, adopted 20 April 2005, DSR 2005:X, 4603
<i>EC – Trademarks and Geographical Indications (US)</i>	Panel Report, <i>European Communities – Protection of Trademarks and Geographical Indications for Agricultural Products and Foodstuffs, Complaint by the United States</i> , WT/DS174/R, adopted 20 April 2005, DSR 2005:VIII, 3499
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<i>US – Gambling</i>	Appellate Body Report, <i>United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services</i> , WT/DS285/AB/R, adopted 20 April 2005, DSR 2005:XII, 5663
<i>US – Gasoline</i>	Panel Report, <i>United States – Standards for Reformulated and Conventional Gasoline</i> , WT/DS2/R, adopted 20 May 1996, as modified by Appellate Body Report, WT/DS2/AB/R, DSR 1996:I, 29
<i>US – Gasoline</i>	Appellate Body Report, <i>United States – Standards for Reformulated and Conventional Gasoline</i> , WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:I, 3

<b>Short Title</b>	<b>Full Case Title and Citation</b>
<i>US – Oil Country Tubular Goods Sunset Reviews</i>	Appellate Body Report, <i>United States – Sunset Reviews of Anti-Dumping Measures on Oil Country Tubular Goods from Argentina</i> , WT/DS268/AB/R, adopted 17 December 2004, DSR 2004:VII, 3257
<i>US – Section 110(5) Copyright Act</i>	Panel Report, <i>United States – Section 110(5) of the US Copyright Act</i> , WT/DS160/R, adopted 27 July 2000, DSR 2000:VIII, 3769
<i>US – Section 211 Appropriations Act</i>	Panel Report, <i>United States – Section 211 Omnibus Appropriations Act of 1998</i> , WT/DS176/R, adopted 1 February 2002, as modified by Appellate Body Report, WT/DS176/AB/R, DSR 2002:II, 683
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<i>US – Superfund</i>	GATT Panel Report, <i>United States – Taxes on Petroleum and Certain Imported Substances</i> , L/6175, adopted 17 June 1987, BISD 34S/136
<i>US – Section 301 Trade Act</i>	Panel Report, <i>United States – Sections 301-310 of the Trade Act of 1974</i> , WT/DS152/R, adopted 27 January 2000, DSR 2000:II, 815
<i>US – Tobacco</i>	GATT Panel Report, <i>United States Measures Affecting the Importation, Internal Sale and Use of Tobacco</i> , DS44/R, adopted 4 October 1994, BISD 41S/131
<i>US – Wool Shirts and Blouses</i>	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB/R, adopted 23 May 1997, DSR 1997:I, 323
<i>US – Zeroing (Japan)</i>	Appellate Body Report, <i>United States – Measures Relating to Zeroing and Sunset Reviews</i> , WT/DS322/AB/R, adopted 23 January 2007

TABLE OF ABBREVIATIONS USED IN THIS REPORT

DSB	Dispute Settlement Body
DSU	Dispute Settlement Understanding
EC	European Communities
MAT	Mutually Agreed Translation
TRIPS	Agreement on Trade-Related Aspects of Intellectual Property Rights
WIPO	World Intellectual Property Organization
WTO	World Trade Organization



## I. INTRODUCTION

1.1 On 10 April 2007, the United States requested consultations with the Government of the People's Republic of China pursuant to Articles 1 and 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU") and Article 64 of the Agreement on Trade-Related Aspects of Intellectual Property Rights ("TRIPS Agreement") (to the extent that Article 64 corresponds to Article XXII of the General Agreement on Tariffs and Trade 1994) with respect to certain measures pertaining to the protection and enforcement of intellectual property rights in China.<sup>1</sup> Consultations were held on 7-8 June 2007 but did not lead to a resolution of the dispute.

1.2 On 13 August 2007, the United States requested the Dispute Settlement Body ("DSB") to establish a panel pursuant to Article 6 of the DSU, with standard terms of reference.<sup>2</sup> At its meeting on 25 September 2007, the DSB established a Panel, pursuant to the request of the United States in document WT/DS362/7, in accordance with Article 6 of the DSU (WT/DSB/M/239).

1.3 The Panel's terms of reference are the following:

"To examine, in the light of the relevant provisions of the covered agreements cited by the United States in document WT/DS362/7, the matter referred to the DSB by the United States in that document, and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements."

1.4 On 3 December 2007, the United States requested the Director-General to determine the composition of the Panel pursuant to paragraph 7 of Article 8 of the DSU.

1.5 On 13 December 2007, the Director-General accordingly composed the Panel as follows:

Chairperson: Mr. Adrian Macey

Members: Mr. Marino Porzio  
Mr. Sivakant Tiwari

1.6 Argentina, Australia, Brazil, Canada, the European Communities, India, Japan, Korea, Mexico, Chinese Taipei, Thailand and Turkey reserved their rights to participate in the Panel proceedings as third parties.

1.7 The Panel met with the parties on 14-16 April 2008 and on 18-19 June 2008. It met with the third parties on 15 April 2008.

1.8 The Panel submitted its interim report to the parties on 9 October 2008. The Panel submitted its final report to the parties on 13 November 2008.

## II. FACTUAL ASPECTS

### A. MEASURES AT ISSUE

2.1 The measures at issue in this dispute are identified in the United States' request for establishment of a panel as follows:

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<sup>1</sup> WT/DS362/1.

<sup>2</sup> WT/DS362/7, attached as Annex D-1 to this report.

## **1. Thresholds for criminal procedures and penalties**

2.2 The United States claims that China has not provided for criminal procedures and penalties to be applied in cases of wilful trademark counterfeiting or copyright piracy on a commercial scale that fail to meet certain thresholds. China has established these thresholds through the following measures:

- (a) the Criminal Law of the People's Republic of China (adopted at the Second Session of the Fifth National People's Congress on 1 July 1979 and revised at the Fifth Session of the Eighth National People's Congress on 14 March 1997), in particular Articles 213, 214, 215, 217, 218, and 220;
- (b) the Interpretation by the Supreme People's Court and the Supreme People's Procuratorate on Several Issues of Concrete Application of Law in Handling Criminal Cases of Infringing Intellectual Property (adopted at the 1331<sup>st</sup> Session of the Judicial Committee of the Supreme People's Court on 2 November 2004 and the 28<sup>th</sup> Session of the Tenth Procuratorial Committee of the Supreme People's Procuratorate on 11 November 2004 and to be effective as of 22 December 2004); and
- (c) the Interpretation by the Supreme People's Court and the Supreme People's Procuratorate on Several Issues of Concrete Application of Law in Handling Criminal Cases of Infringing Intellectual Property (II) (adopted on 4 April 2007, at the 1422<sup>nd</sup> Session of the Judicial Committee of the Supreme People's Court and the 75<sup>th</sup> Session of the Tenth Procuratorial Committee of the Supreme People's Procuratorate, and to be effective on 5 April 2007);

as well as any amendments, related measures, or implementing measures.

## **2. Disposal of goods confiscated by customs authorities that infringe intellectual property rights**

2.3 The United States claims that China's measures for disposing of confiscated goods that infringe intellectual property rights are inconsistent with China's obligations under the TRIPS Agreement. In this regard, the measures at issue are:

- (a) the Regulations of the People's Republic of China for Customs Protection of Intellectual Property Rights (adopted at the 30th Ordinary Meeting of the State Council on 26 November 2003, published by the State Council on 2 December 2003, and effective from 1 March 2004), in particular Chapter 4 thereof;
- (b) the Implementing Measures of Customs of the People's Republic of China for the Regulations of the People's Republic of China on Customs Protection of Intellectual Property Rights (adopted at an Administration Affairs Meeting of the General Administration of Customs on 22 April 2004, issued by the General Administration of Customs with Order No. 114 on 25 May 2004, and effective from 1 July 2004), in particular Chapter 5 thereof; and
- (c) General Administration of Customs Announcement No. 16 (2 April 2007);

as well as any amendments, related measures, or implementing measures.

**3. Denial of copyright and related rights protection and enforcement to works that have not been authorized for publication or distribution within China**

2.4 The United States claims that China is acting inconsistently with its obligations under the TRIPS Agreement by denying the protection of its Copyright Law to creative works of authorship (and, to the extent Article 4 of the Copyright Law applies to them, sound recordings and performances) that have not been authorized for, or are otherwise prohibited from, publication or distribution within China. In this regard, the measures at issue are:

- (a) the Copyright Law of the People's Republic of China (adopted at the 15th Session of the Standing Committee of the Seventh National People's Congress on 7 September 1990, and amended according to the Decision on the Revision of the Copyright Law of the People's Republic of China, adopted at the 24th Session of the Standing Committee of the Ninth National People's Congress on 27 October 2001), in particular Article 4;<sup>3</sup>

as well as any amendments, related measures, or implementing measures.

**B. PROCEDURAL HISTORY**

**1. Translations**

2.5 Paragraph 10 of the Working Procedures adopted by the Panel on 10 January 2008 provided that where the original language of exhibits or text quoted in a submission was not an official WTO language, the submitting party shall submit the original language version of that at the same time.

2.6 In view of certain differences between the parties' respective translations of certain measures the Panel, at its first substantive meeting, suggested that the parties submit mutually agreed translations of these measures. In communications dated 11 and 14 June 2008, the parties submitted mutually agreed translations ("MATs") of the following measures:

- (MAT-1) Criminal Law (Articles 213, 214, 215, 217, 218 and 220)
- (MAT-2) 2007 Judicial Interpretation (Articles 1 through 7)
- (MAT-3) 2004 Judicial Interpretation (Articles 1 through 17)
- (MAT-4) 1998 Judicial Interpretation (Article 17 paragraph 2)
- (MAT-5) Prosecution Standards on Economic Crimes (Articles 8, 16, 23, 38, 39 and 70)
- (MAT-6) Regulations on Customs Protection of Intellectual Property Rights (Article 27)
- (MAT-7) Customs IPR Implementing Measures (Article 30)
- (MAT-8) Customs Announcement No. 16/2007
- (MAT-9) Measures on the Administration of Property Confiscated by Customs (Articles 1, 2, 3, 17 and 18)

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<sup>3</sup> The United States does not request relief in respect of certain other measures specified in its request for establishment of a panel in conjunction with Article 4 of the Copyright Law.

- (MAT-10) Law on Donations for Public Welfare
- (MAT-11) Copyright Law (Articles 2 and 4)
- (MAT-12) Regulations on the Administration of Films (Articles 2, 24, 25, 27, 28, 29, 31, 42 and 55)
- (MAT-13) Regulations on the Administration of Audiovisual Products (Articles 2, 4, 28 and 36)
- (MAT-14) Regulations on the Administration of Publication (Articles 6, 26, 27, 40, 44, 45 and 56)

## **2. Request for factual information from the International Bureau of WIPO**

2.7 On 21 April 2008, the Panel sent a letter to the International Bureau of WIPO requesting its assistance in the form of any factual information available to it relevant to the interpretation of certain provisions of the Berne Convention for the Protection of Literary and Artistic Works (1971).<sup>4</sup> The parties had been given the opportunity to comment on the draft letter at the Panel's first substantive meeting.

2.8 The International Bureau's reply was received by the Panel and the WTO Secretariat on 7 June 2008. The Panel gave the parties an opportunity to submit comments on the reply by 7 July 2008. The United States submitted its comments on 7 July 2008. China informed the Panel that it would not submit comments on the WIPO reply. China submitted comments on the United States' comments on 21 July 2008.

2.9 The factual information provided by the International Bureau consists of a note that it prepared and 16 annexes containing excerpts from the Official Records of the various Diplomatic Conferences which adopted, amended or revised the provisions currently contained in Articles 5(1), 5(2) and 17 of the Berne Convention (Paris Act of 1971).<sup>5</sup>

## **III. PARTIES' REQUESTS FOR FINDINGS AND RECOMMENDATIONS**

### **A. UNITED STATES**

3.1 The United States requests that the Panel find that:

- (a) China's IPR thresholds are inconsistent with China's obligations under Article 61, 1<sup>st</sup> and 2<sup>nd</sup> sentence, and Article 41.1 of the TRIPS Agreement;
- (b) the compulsory sequences of steps set out in the Chinese measures 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 that the measures at issue are therefore inconsistent with China's obligations under Article 59 of the TRIPS Agreement;
- (c) the first sentence of Article 4 of China's Copyright Law is inconsistent with Article 9.1 of the TRIPS Agreement, incorporating Articles 5(1) and 5(2) of the

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<sup>4</sup> The Panel's letter is attached as Annex D-2 to this report.

<sup>5</sup> The International Bureau's Note, but not its annexes, is attached as Annex D-3 to this report.

Berne Convention (1971), as well as Article 14; Article 61, 1<sup>st</sup> and 2<sup>nd</sup> sentence; and Article 41.1 of the TRIPS Agreement.

3.2 The United States requests that the Panel recommend, pursuant to Article 19.1 of the DSU, that China bring its measures into conformity with the TRIPS Agreement.

B. CHINA

3.3 China requests that the Panel find China's measures to be consistent with China's obligations under the TRIPS Agreement.

#### **IV. ARGUMENTS OF THE PARTIES**

4.1 The arguments of the parties as set forth in their executive summaries of their written submissions submitted to the Panel, are attached to this Report as Annexes A and B (see List of Annexes, page v).

#### **V. ARGUMENTS OF THE THIRD PARTIES**

5.1 The arguments of the third parties as set forth in their executive summaries of their written submissions and oral statements submitted to the Panel, are attached to this Report as Annex C (see List of Annexes, page vi).<sup>6</sup>

#### **VI. INTERIM REVIEW**

6.1 On 9 October 2008, the Panel submitted its interim report to the parties. On 23 October 2008, the United States and China submitted written requests for review of precise aspects of the interim report. On 30 October 2008, the United States and China submitted written comments on each other's request for interim review.

6.2 The Panel has modified specific aspects of its report, where it considered appropriate, in light of the parties' comments as explained below, and made other modifications for the purposes of accuracy and clarity. References to paragraph numbers and footnotes in this Section VI refer to those in the interim report.

##### **1. Copyright Law**

###### *Works that fail content review*

6.3 China requests that the Panel consider amending paragraphs 7.87 and 7.103 to avoid confusion regarding the parties' respective descriptions of works that have failed content review.

6.4 The United States opposes this request, as it believes that the Panel has accurately characterized the positions that the parties expressed to the Panel.

6.5 The Panel has not made the requested modification but modified paragraphs 7.87 and 7.88 and made consequential changes to paragraphs 7.103 and 7.118 to clarify its characterization of works that have failed content review and works for which an edited version has been approved for distribution in China, and to explain why it does not accept some of China's description of such works.

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<sup>6</sup> India, Thailand and Turkey did not make written submissions. Argentina, India and Turkey did not make oral statements.

*Rights specially granted by the Berne Convention*

6.6 The United States requests that paragraph 7.107 be modified so as to add a reference to Article 14*bis*, and to delete the reference to Article 14*ter*, in the list of rights specially granted by the Berne Convention (1971).

6.7 China responds that the request to add a reference to Article 14*bis* is not warranted. That Article does not articulate any independent rights, and the request is unnecessary in view of the Panel's footnote providing that the enumeration of minimum rights is without prejudice.

6.8 The Panel has modified the list to add a reference to Article 14*bis* which provides for the grant of a right to a particular category of works. The Panel has not deleted the reference to Article 14*ter*, as it provides for a distinct right, but this is without prejudice to the provisions of Article 14*ter*(2) and (3). The Panel has also deleted the reference to Article 13 and reiterates its statement in footnote 111 that this list is without prejudice to other such rights.

*Effectiveness of prohibitions on content*

6.9 China requests that paragraph 7.138 be modified to refer to Article 364 of the Criminal Law and Article 56 of the Film Regulations.

6.10 The United States responds that, in the context discussed in paragraph 7.138, China only referred to Article 56 of the Film Regulations and that that Article does not change the substance of the Panel's finding in that paragraph.

6.11 The Panel has not made the requested modification because the paragraph in question concerns the actual effectiveness of enforcement actions whilst China's comment refers to standards set out in legislation. The Panel has also merged this paragraph with the previous one, for clarity.

*Other modifications*

6.12 China requests a clarification in paragraph 7.101 regarding the jurisdiction of its copyright authorities. The Panel has made the clarification.

6.13 The United States requests that paragraph 7.136 be modified to track the text of the response quoted. The Panel has made the requested modification.

**2. Customs measures**

*Donation to social welfare bodies*

6.14 The United States requests that paragraph 7.310 be modified because there are circumstances in which donation is possible to other social welfare bodies besides the Red Cross.

6.15 China responds that the United States appears to misinterpret the second sentence of paragraph 7.310 because that sentence simply observes that Customs has the power to donate to the Red Cross in all instances where it can donate to other social welfare organizations.

6.16 The Panel has not made the requested modification. The point of the paragraph in question is that China Customs has authority to donate infringing goods to the Red Cross Society of China, with whom it has a donation agreement, and that authority to donate infringing goods to other social welfare bodies does not preclude that authority. The Panel has modified the paragraph, for clarity.

*Auction and authority to order the destruction of infringing goods*

6.17 The United States requests that paragraph 7.341 be modified due to a systemic concern because the Panel appears to take the position that the word "shall", when used in Chinese legal measures, does not impose a mandatory legal obligation. The meaning of the Chinese term translated as "shall" in the formal legal context differs from its meaning in other contexts. It was because of this difference that the parties agreed that the correct translation was "shall" for the purposes of translation into English. China confirmed that the use of the verb "shall" in the context of the measures at issue meant that once Customs makes particular findings it has a legal obligation to carry out the relevant disposal option.

6.18 China responds as follows: (1) in reaching the mutually agreed translation, there was no discussion between the parties on whether the meaning of the word translated as "shall" in formal legal contexts was different from its meaning in other contexts; (2) the Panel's assessment of the measure is a factual finding particular to this dispute and does not affect future assessments by other panels in other disputes involving China's domestic law; (3) the dictionary definition of the word translated as "shall" forms part of the Panel's assessment of the meaning of the measure and the Panel is within its authority in using such a source.

6.19 The Panel notes that the English word "shall" is only used in a non-authentic translation. Even then, the word is used specifically in the description of the auction method in only one of the three Customs measures, and that measure is a lower norm. The United States' case seems to place great weight on the choice of the word "shall" in the translation of that lower norm. This may not be the case in other disputes. However, in this dispute, the Panel is not satisfied that the translation, on an objective assessment, can support the conclusion that the United States apparently seeks to draw from it as regards the conformity of the measures at issue with China's WTO obligations. The Panel has modified the paragraph, in part as requested.

*Auction and "simple removal of the trademark unlawfully affixed"*

6.20 China requests a revision of the conclusion in paragraph 7.397(c) for the following reasons: (1) Article 46 does not apply to goods from which all infringing features have been removed as they are no longer infringing; (2) reaffixing a counterfeit trademark constitutes a separate act of infringement; and (3) US authorities may publicly auction merchandise after obliteration of the trademark.

6.21 The United States opposes this request, and responds to China's three reasons as follows: (1) this is just a variant of an argument that the interim report already disposes of in paragraphs 7.381-7.382; (2) this is irrelevant as the obligation in the fourth sentence of Article 46 refers to a procedure not the substantive legal effect of affixing a counterfeit trademark; (3) the United States has previously demonstrated that China's arguments regarding this aspect of US law are irrelevant and without merit.

6.22 The Panel has not made the requested modification for the reasons already given in paragraph 7.235 regarding the temporal scope of the obligations in Article 46, paragraph 7.264 noting that the "counterfeit trademark goods" referred to in the fourth sentence of Article 46 are a category of the infringing goods covered by that Article, and paragraphs 7.375 and 7.382 regarding the insufficiency of ceasing infringement. The Panel has modified paragraph 7.382 to emphasize that the fourth sentence of Article 46 imposes an additional requirement and clarified paragraph 7.388. The third point raised by China in its interim review comments concerns US measures which are not part of the matter before the Panel.

*Exceptional cases*

6.23 The United States requests a clarification before paragraph 7.396 that the Customs measures provide that simple removal of the trademark unlawfully affixed is sufficient to permit release of the goods into the channels of commerce in *more* than just exceptional cases.

6.24 China responds that the text of TRIPS uses the formulation "other than in exceptional cases" so that the request that the Panel alter the text of its finding is unwarranted by the record evidence and the text of TRIPS.

6.25 The Panel has added the requested clarification. The Panel has used the phrase "more than just exceptional cases" as requested because it indicates that the Customs measures do not comply with the formulation in the fourth sentence of Article 46 of the TRIPS Agreement as regards exceptional cases.

**3. Criminal thresholds**

*Construction of the measures at issue*

6.26 The United States requests that the subheading above paragraph 7.471 be modified.

6.27 China considers that the subheading is neither inaccurate nor misleading.

6.28 The Panel has made the requested modification, for clarity.

*"on a commercial scale"*

6.29 The United States requests adjustments of the text or the insertion of cross-references for clarity to indicate that certain paragraphs refer to the concept in paragraphs 7.579 and 7.580.

6.30 The Panel has not made the requested adjustments. Paragraph 7.600 states that the interpretation of "on a commercial scale" is set out in paragraph 7.579 and that the Panel will apply that interpretation in the following sub-section. Paragraphs 7.605 and 7.607 relate that interpretation to China's marketplace. The Panel has modified one aspect of paragraph 7.580 and added a new paragraph introducing the remainder of the Panel's assessment.

*Article 63.3 of the TRIPS Agreement*

6.31 The United States requests that paragraph 7.631 be modified to delete a reference to Article 63.3 of the TRIPS Agreement as it could be misunderstood.

6.32 China objects to this request because it understands that the Panel included this statement as part of the explanation of its treatment of the evidence on the record. The US concern is misplaced because Article 63.3 of the TRIPS Agreement is not part of the matter before the Panel and the Panel's use of the word "notwithstanding" indicated that the conclusions in this section are made setting aside any issues relating to Article 63.3.

6.33 The Panel has made the requested modification to avoid any possible misunderstanding as to the meaning of Article 63.3 of the TRIPS Agreement.

*Physical evidence*

6.34 The United States requests that paragraph 7.642 be modified as regards the anti-counterfeiting efforts of Nintendo of America.

6.35 China responds that paragraph 7.642 requires no change. Only three criminal cases were analysed in the Nintendo report and the record of this dispute does not disclose the status of two of them.

6.36 The Panel has made the requested modification, in part, but drawn no conclusion as to the status of two of the cases analysed in the Nintendo report.

## **VII. FINDINGS**

### **A. COPYRIGHT LAW**

#### **1. Description of the measure at issue**

7.1 This Section of the Panel's findings concerns China's **Copyright Law**. The Copyright Law was adopted by the Standing Committee of the National People's Congress and promulgated in 1990 then amended by a Decision of the Standing Committee of the National People's Congress in 2001. The claims concerning the Copyright Law address, in particular, the first sentence of Article 4. The parties agreed to translate that sentence as follows:

"Works the publication and/or dissemination of which are prohibited by law shall not be protected by this Law."<sup>7</sup>

7.2 This Report refers to the first sentence of Article 4 as "Article 4(1)" for ease of reference, although the original version does not use paragraph numbers within that Article.

#### **2. Claim under Article 2(6) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement**

7.3 The United States informed the Panel in its comments on the draft descriptive part of this Report that it makes a claim under Article 2(6) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement. In this regard, it refers the Panel to arguments in its written submissions. It also notes that its request for establishment of a panel referred to "Articles 1 through 21 of the Berne Convention".<sup>8</sup>

7.4 The Panel recalls that its terms of reference are limited to the matter set out in the United States' request for establishment of a panel.<sup>9</sup> The Panel also recalls that Article 6.2 of the DSU provides that a request for establishment of a panel shall, *inter alia* "provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly".

7.5 In the present dispute, the request for establishment of a panel refers to Article 5(1) and 5(2) of the Berne Convention (1971), followed by the incorporation provision in Article 9.1 of the TRIPS Agreement. The request sets out three sentences on the measure at issue, then one sentence reciting terms used in Article 5(1) of the Berne Convention (1971), followed by a conclusion under Article 9.1 of the TRIPS Agreement, then another sentence reciting terms used in Article 5(2) of the Berne

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<sup>7</sup> Mutually agreed translation no. 11.

<sup>8</sup> United States' comments on the draft descriptive part of the report dated 4 September 2008.

<sup>9</sup> See the Notice of Constitution of the Panel in document WT/DS362/8.

Convention (1971), followed by a conclusion under Article 9.1 of the TRIPS Agreement. The request makes no specific reference to Article 2 of the Berne Convention (1971) at all.

7.6 It was in this context that the request for establishment of a panel recited part of the terms of Article 9.1 of the TRIPS Agreement, insofar as it requires all WTO Members to comply with "Articles 1 through 21" of the Berne Convention. There is no indication that the reference to the terms of the Berne Convention (1971) incorporated by Article 9.1 of the TRIPS Agreement was intended to refer to any particular provision of that Convention besides Article 5(1) and 5(2).

7.7 The Panel notes that Articles 2 and 5 of the Berne Convention (1971) are incorporated in the TRIPS Agreement by the same provision, i.e. Article 9.1 of the Agreement. However, a reference to Article 9.1 of the TRIPS Agreement and a broad reference to 28 incorporated provisions of the Berne Convention (1971) are not sufficient to "provide a brief summary of the legal basis of a complaint sufficient to present a problem clearly". In such circumstances, the respondent, third parties and the Panel cannot know which particular obligations under the Berne Convention (1971) are at issue.

7.8 The Panel notes that its approach to the proper way to summarize the legal basis of a claim under the provisions of an intellectual property convention incorporated in the TRIPS Agreement is consistent with the approach followed in the Panel Report in *EC – Trademarks and Geographical Indications (Australia)* which ruled that a claim regarding a provision of the Paris Convention (1967) that had not been specifically mentioned in the request for establishment of a panel was outside its terms of reference.<sup>10</sup>

7.9 For the above reasons, the Panel finds that the request for establishment of a panel discloses no claim under Article 2(6) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement.

7.10 Even if the Panel were to accept *arguendo* that the request for establishment of a panel had been unclear in its broad reference to the incorporated provisions of the Berne Convention (1971) and its specific reference to the "protection" of "works" (terms used in Article 2(6), as in many other provisions of the Berne Convention (1971)), the United States' first written submission did not explicitly make any claim regarding Article 2(6) of the Berne Convention (1971) either. The United States argued in its first written submission that several of the Berne Convention Articles with which China must comply pursuant to TRIPS Article 9.1 "are relevant" in this dispute. It quoted Article 5(1) of the Berne Convention (1971), then mentioned ten other provisions of that Convention in order to elaborate on the meaning of certain phrases used in Article 5(1), regarding "works" and "the rights specially granted".<sup>11</sup> Article 2(6) was one of those ten other provisions. None of those references hinted at a claim under any provision besides Article 5(1). The United States also argued that Article 4 of the Copyright Law excludes from copyright protection an entire category of works, but that exclusion from protection is not permitted or even contemplated by the Berne Convention. It mentioned six provisions of Articles 2 and 2*bis* of the Berne Convention (1971) in support of that argument.<sup>12</sup> Article 2(6) was one of those six provisions. However, there was no explicit statement that a separate claim was being made under Article 2(6).

7.11 China understood that the United States' claims under the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement, were made under Article 5(1) and 5(2).<sup>13</sup>

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<sup>10</sup> Panel Report in *EC – Trademarks and Geographical Indications (Australia)*, paras 7.37-7.43.

<sup>11</sup> United States' first written submission, paras 210-214.

<sup>12</sup> United States' first written submission, paras 215-216.

<sup>13</sup> China's first written submission, para. 232; rebuttal submission, para. 220.

7.12 None of the third parties referred to a claim under Article 2(6) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement.

7.13 Even in its rebuttal submission, the United States did not clarify explicitly that it wished to make a claim under Article 2(6) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement. Rather, it presented only two claims regarding the provisions of the Berne Convention. In the first, it argued that Article 4 of the Copyright Law denies copyright to works contrary to China's obligations under Article 9.1 of the TRIPS Agreement and "the provisions of the Berne Convention" referenced in Article 9.1. Its arguments regarding "works" and "rights" supported a single claim which, in light of the request for establishment of a panel, appeared to be the original claim under Article 5(1), as incorporated by Article 9.1 of the TRIPS Agreement. It referred to two provisions of Article 2, one of which was Article 2(6), without expressly articulating a claim under Article 2(6). A subheading asserted an inconsistency with "Articles 2 and 5(1) of the Berne Convention" but, given that the definition of works in Article 2 is relevant to the claim under Article 5(1) (as shown in the Panel's consideration of the claim under Article 5(1) at paragraphs 7.115 and 7.116 below), it was still not clear that the United States wished to assert a separate claim under Article 2 of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement.

7.14 For the above reasons, even if the Panel were to accept *arguendo* that the request for establishment of a panel had been unclear, the Panel finds that the United States' submissions to the substantive meetings with the Panel did not clarify that a claim was being made under Article 2(6) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement, in accordance with Article 6.2 of the DSU.

7.15 Therefore, in light of the above, the Panel finds that a claim under Article 2(6) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement, lies outside the Panel's terms of reference.

### **3. Claim under Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement**

#### **(a) Main arguments of the parties**

7.16 The United States claims that Article 4(1) of China's Copyright Law denies the protection of the Copyright Law to certain categories of works, and refers to the text of that sentence. The United States recalls that China, during a review of its legislation in the Council for TRIPS in 2002, explained that this sentence referred to works of which the publication or distribution was prohibited by such laws and regulations as the Criminal Law, the Regulation on the Administration of Publishing Industry, the Regulation on the Administration of Broadcasting, the Regulation on the Administration of Audiovisual Products, the Regulation on the Administration of Films and the Regulations on the Administration of Telecommunication. The United States gives examples of four regulations that prohibit the publication or distribution of works under various circumstances.<sup>14</sup> The United States claims that Article 4(1) of China's Copyright Law denies to the authors of works "the publication or distribution<sup>15</sup> of which is prohibited by law" the broad set of rights enumerated in Article 10 of the Copyright Law, which largely encompasses the rights contemplated by the provisions of the Berne Convention (1971). Nor do authors of works denied protection of the Copyright Law benefit from the remedies specified in Articles 46 and 47 of the Copyright Law. Consequently, the authors of such works do not enjoy the minimum rights that are "specially granted" by the Berne Convention,

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<sup>14</sup> United States' first written submission, paras 68-69, referring to Review of Legislation (China) in document IP/Q/CHN/1, p. 26; and paras 70-85.

<sup>15</sup> This translation was taken from China's notification to the Council for TRIPS in IP/N/1/CHN/C/1. The parties later agreed that it should be translated as "publication and/or dissemination".

inconsistently with Article 5(1) of that Convention.<sup>16</sup> The United States submitted more detailed arguments with respect to content review in relation to Article 5(2) of the Berne Convention (1971) (see paragraph 7.145 below).

7.17 China responds that copyright vests upon creation and is independent of publication. Article 2 of the Copyright Law grants full copyright protection by expressly incorporating into Chinese law the rights conferred under international agreements, including the Berne Convention and the TRIPS Agreement. In contrast, Article 4(1) of the Copyright Law is extremely limited in scope. China, like many other countries in the world, bans from publication and dissemination such works as those that consist entirely of unconstitutional or immoral content. Article 4(1) simply provides that such a work shall not be protected by the Copyright Law. China argued in its first written submission that the application of Article 4(1) was not dependent on content review or any other regulatory regime related to publication and that the only result of a finding of prohibited content in that process was a denial of authority to publish, not a denial of copyright. Specifically, China argued that works that fail content review were not denied copyright protection.<sup>17</sup> Article 17 of the Berne Convention (1971) subjects to the sovereign power of governments all of the rights otherwise granted by that Convention.<sup>18</sup>

7.18 At the first substantive meeting with the Panel, the United States stated that China's written submission appeared simply to concede that Article 4 of its Copyright Law was inconsistent with its obligations under the TRIPS Agreement because it admitted that Article 4(1) denies protection to works whose contents are prohibited.<sup>19</sup>

7.19 At the same meeting, China confirmed parts of its first written submission but clarified that, with respect to a work edited to pass content review, it would protect copyright in the edited version of the work, including against copies of the unedited version that infringed copyright in the edited, approved version. With respect to works that *failed* content review, China informed the Panel that it intended to provide additional written comments and clarification of its position later.<sup>20</sup>

7.20 China provided its additional comments together with its responses to the Panel's questions after the first substantive meeting and asked the Panel to rely on these additional comments to the extent that they were inconsistent with its first written submission. China confirmed that it would protect copyright where a work was edited to pass content review. Where no authorized edited version had been created, it would enforce copyright in the legal portion of the original work against copies of an unauthorized edited version. However, it would not enforce copyright against unedited, prohibited copies of an unedited, prohibited work that failed content review.<sup>21</sup>

7.21 At the same time, in response to the Panel's questions, China submitted that Article 4(1) of the Copyright Law did not affect the vesting of copyright under Article 2 of that Law. China asked the Panel to note that under the Chinese system of copyright, "copyright" and "copyright protection" are distinguishable. To the extent that Article 4(1) of the Copyright Law would come into play with respect to a work, it would operate not to remove copyright, but to deny the particularized rights of private copyright enforcement.<sup>22</sup>

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<sup>16</sup> United States' first written submission, paras 217-219.

<sup>17</sup> China's first written submission, paras 228-230 and 234-254. Paras 243-252 were later revised by China's response to Question No. 52.

<sup>18</sup> China's first written submission, paras 255-263.

<sup>19</sup> United States' first oral statement, para. 79.

<sup>20</sup> China's first oral statement, paras 81-86.

<sup>21</sup> China's response to Question No. 52. See also responses to Question No. 51 and US Question No. 2.

<sup>22</sup> China's response to Question No. 44; reiterated in its rebuttal submission, para. 281.

7.22 The United States notes that China admits that it denies copyright protection to certain works whose contents Chinese authorities determine are prohibited by law and submits that, therefore, China has confirmed that it is acting inconsistently with its obligations under Article 9.1 of the TRIPS Agreement. The United States rebuts China's arguments as follows: first, even if Article 2(2) of the Copyright Law grants protection to foreigners' works, Article 4(1) denies protection to those for which publication or distribution is prohibited by law. Article 2 cannot, by the terms of Article 4, apply to such works. Second, as Article 4 denies the exclusive rights enumerated in Article 10 of the Copyright Law, the minimum set of exclusive rights guaranteed by Article 5(1) of the Berne Convention (1971) is denied to such works. The distinction between "copyright" and "copyright protection" is not found in the text of the Berne Convention and is irrelevant. Third, Article 4(1) creates significant commercial uncertainty and, where it is clear that a work has been denied copyright protection, allows pirates to profit at the expense of the legitimate right holder, including by exporting.<sup>23</sup> Article 17 of the Berne Convention (1971) does not permit Members to deny copyright protection to authors in their respective works.<sup>24</sup>

7.23 China responds that the United States has failed to make a prima facie case with respect to its view that copyright protection is contingent upon content review (see paragraph 7.145 below). The whole claim with respect to Article 4(1) of the Copyright Law must therefore fail. With respect to the claim of a facial violation, there is a strong presumption that a Member's law is WTO-compliant and the United States has offered no evidence in support but the text of Article 4(1) of the Copyright Law itself. Article 2 of the Copyright Law directly implements an author's rights under the Berne Convention into Chinese law. The scope and operation of Article 4(1) of the Copyright Law are extremely limited.<sup>25</sup> The sovereign power to prohibit works, recognized in Article 17 of the Berne Convention (1971), permits Members to maintain a provision of law such as Article 4(1) of the Copyright Law.<sup>26</sup>

(b) Main arguments of third parties

7.24 Argentina considers that Article 4(1) of the Copyright Law appears to deny to works that are prohibited or not permitted the protection established in Article 10 of the Copyright Law, which contains the rights enumerated in the Berne Convention (1971). This does not imply that China has no right to prohibit the publication or distribution of certain kinds of works. In fact, Article 17 of the Berne Convention (1971) contemplates such a possibility.<sup>27</sup>

7.25 Canada notes that China has admitted that Article 4(1) of its Copyright Law refers to works, including those of the Berne Union, that the Chinese authorities find unconstitutional or immoral, and that these works are not protected in China. Canada does not see how this conclusion is affected by the second sentence of Article 2 of the Copyright Law as Article 4 seems to take precedence. Canada agrees that Members can prohibit the publication and distribution of work but considers that Members do not have a right to deny copyright protection to them.<sup>28</sup>

7.26 The European Communities notes that China acknowledges that Article 4(1) of its Copyright Law denies copyright protection for works "the publication or distribution of which is prohibited" because of "unconstitutional or immoral" or "reactionary, pornographic or superstitious" content. Such denial of protection is not covered by the exemptions or limited exceptions permitted under the

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<sup>23</sup> United States' rebuttal submission, paras 184-194.

<sup>24</sup> United States' rebuttal submission, para. 221.

<sup>25</sup> China's rebuttal submission, paras 225-226, 266-269, 276-277 and 281.

<sup>26</sup> China's rebuttal submission, paras 286-306.

<sup>27</sup> Argentina's third party written submission, paras 89-91.

<sup>28</sup> Canada's third party written submission, paras 22-23; third party oral statement, para. 15.

Berne Convention (1971) and the TRIPS Agreement. Article 17 of the Berne Convention (1971) does not allow limiting exclusive rights or even exempting works from protection.<sup>29</sup>

7.27 Chinese Taipei considers that, without a content review, it can never be determined whether a work is unconstitutional or immoral. Works that have not passed, or that fail to pass, content review are prohibited from distribution by law, which means that they fall within the scope of Article 4(1) of the Copyright Law. Clarification is required as to whether China protects works that have not been submitted for a content review or that are pending authorization. Even if Article 4(1) of the Copyright Law were limited to works that fail to pass a content review, this withdrawal of protection would be inconsistent with the obligation under Article 9.1 of the TRIPS Agreement and Article 5(1) of the Berne Convention (1971). Chinese Taipei shared the view of both parties that China has the right to conduct content review based on Article 17 of the Berne Convention (1971).<sup>30</sup>

(c) Consideration by the Panel

(i) *Construction of the measure at issue*

7.28 The Panel notes that this claim challenges China's Copyright Law, in particular Article 4(1), not as it has been applied in any particular instance but "as such". The parties have disagreed on the proper interpretation of that measure since shortly after the first substantive meeting. Therefore, the Panel is obliged, in accordance with its mandate, to make an objective assessment of the meaning of the relevant provisions of that measure. In this context, the Panel is mindful that, objectively, a Member is normally well-placed to explain the meaning of its own law.<sup>31</sup> However, in the context of a dispute, to the extent that either party advances a particular interpretation of a provision of the measure at issue, it bears the burden of proof that its interpretation is correct.<sup>32</sup> The Panel emphasizes that it examines the measure solely for the purpose of determining its conformity with China's obligations under the TRIPS Agreement.<sup>33</sup>

7.29 The United States claims that Article 4(1) of the Copyright Law on its face denies immediate, automatic protection to certain works of creative authorship.<sup>34</sup>

7.30 China responds that this claim is based on the "mistaken view" that copyright protection in China is contingent upon successful completion of content review.<sup>35</sup> In the course of addressing the issue of when copyright vests under Chinese law, China acknowledged that Article 4(1) of the Copyright Law denies protection to certain works due to their content.<sup>36</sup>

7.31 The United States stated at the first substantive meeting that, in view of that acknowledgement, China appeared simply to concede that Article 4 of the Copyright Law was inconsistent with China's obligations under the TRIPS Agreement.<sup>37</sup> Canada and the European

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<sup>29</sup> European Communities' third party written submission, paras 22-27; oral statement, para. 21.

<sup>30</sup> Chinese Taipei's third party written submission, paras 33-40.

<sup>31</sup> China stresses that part of this claim involves "an arcane area of Chinese law, with little practical application, and with respect to which there is little or no practical experience on which to base legal judgments": see China's response to Question No. 52.

<sup>32</sup> See the Panel Reports in *EC – Trademarks and Geographical Indications (US)*, at para. 7.55, and *EC – Trademarks and Geographical Indications (Australia)*, at para. 7.106.

<sup>33</sup> See Appellate Body Report in *India – Patents (US)*, paras 65-68.

<sup>34</sup> United States' first written submission, para. 196.

<sup>35</sup> China's first written submission, para. 8.

<sup>36</sup> China's first written submission, paras 229 and 243.

<sup>37</sup> United States' first oral statement, para. 79.

Communities, as third parties, took the same view.<sup>38</sup> Argentina considered that the text of Article 4 was straightforward.<sup>39</sup>

7.32 After that meeting, China clarified the terms of its earlier acknowledgement. It clarified that Article 4(1) denies "copyright protection" in the sense of enforcement but does not disturb "copyright".<sup>40</sup>

7.33 The United States dismissed China's clarification as an "artificial distinction".<sup>41</sup>

7.34 The Panel begins its assessment by observing that Chapter I of the Copyright Law comprises eight articles. Article 1 sets out the purpose of the law, which includes the purpose of protecting the copyright of authors in their literary, artistic and scientific works and the rights and interests related to copyright.

7.35 Article 2 sets out criteria of eligibility for protection. The first paragraph (to which the Panel will refer as "Article 2(1)") may be translated as follows:

"Chinese citizens, legal entities or other organizations shall enjoy copyright in their works in accordance with this Law, whether published or not."<sup>42</sup>

7.36 The second (to which the Panel will refer as "Article 2(2)") may be translated as follows:

"The copyright enjoyed by foreigners or stateless persons in any of their works under an agreement concluded between China and the country to which the author belongs or in which the author has his habitual residence, or under an international treaty to which both countries are parties, shall be protected by this Law."<sup>43</sup>

The Berne Convention (1971) is defined as an "international copyright treaty" for the purposes of the Provisions on the Implementation of International Copyright Treaties.<sup>44</sup>

7.37 Article 3 sets out a non-exhaustive list of "works" for the purposes of this Law, including works of literature, art, natural sciences, social sciences, engineering and technology which are created in the form of any of a series of enumerated works.

7.38 Article 4 provides *inter alia* that certain "works" shall not be protected by this Law.

7.39 Article 5 sets out subject matter to which this Law does not apply (that appears to concern subject matter that falls into the public domain or is considered to lack originality).

7.40 Article 6 provides that certain works will be dealt with in other measures.<sup>45</sup>

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<sup>38</sup> Canada's third party written submission, para. 22; European Communities' third party written submission, para. 22, third party oral statement, para. 21.

<sup>39</sup> Argentina's third party written submission, para. 82.

<sup>40</sup> China's response to Question No. 44; rebuttal submission, paras 280-281.

<sup>41</sup> United States' second oral statement (closing statement), para. 25.

<sup>42</sup> Mutually agreed translation no. 11.

<sup>43</sup> Mutually agreed translation no. 11.

<sup>44</sup> Provisions on the Implementation of International Copyright Treaties, promulgated by decree of the State Council in 1992 and effective from 1992, Article 3, reproduced in Exhibit CHN-117. These Provisions, which predate the TRIPS Agreement, do not refer to the TRIPS Agreement in the definition of "international copyright treaties", although other legal provisions might. The United States has not challenged this aspect of the measure.

7.41 A link can be observed between Article 2(2) and 4(1). Article 2(2) provides that the copyright enjoyed by certain foreigners in any of their works "shall be protected by this Law" (受本法保护) whilst Article 4(1) uses identical language with the addition of a negative (不) to provide that certain works "shall not be protected by this Law" (不受本法保护). This suggests that Article 4(1) denies what Article 2(2) grants.

7.42 Turning to Article 4(1), the text of this provision is quoted at paragraph 7.1 above.

7.43 The term "works" (作品) is defined in the previous article, Article 3.

7.44 The term "publication and/or dissemination" (出版、传播) was agreed between the parties as an appropriate translation. The parties had earlier used the phrases "publication or distribution" and "publication and dissemination". China alleges that the word translated as "dissemination" (传播) has a distinct, and wider, meaning than a word commonly used in its content review regulations, which may be translated as "distribution" (发行).<sup>46</sup>

7.45 The term "prohibited by law" (依法禁止), on its face, is not limited to any particular piece of legislation but could apply to any law that prohibits the publication and/or dissemination of a work. The United States alleges that it refers to "other laws and regulations".<sup>47</sup> In any event, it is clear from its wording that the provision applies to a class of "works", the class being defined as those the publication and/or dissemination of which are, in some way, prohibited by law. (This phrase is examined in greater detail at paragraphs 7.72 to 7.82 below.)

7.46 The phrase translated as "shall not be protected by this Law" (不受本法保护) does not include the word "shall" in the original, as it uses no modal verb. However, it is not disputed that Article 4(1) of the Copyright Law is mandatory. The reference to "this Law" (本法) is evidently a reference to the Copyright Law. On its face, it refers to the protection of the Copyright Law and not to any subset of its protection.

7.47 The United States explained that this phrase provided for the denial of the rights enumerated in Article 10 of the Copyright Law and the remedies in Articles 46 and 47 of the Copyright Law.<sup>48</sup> China agreed that it included all the rights listed in Article 10.<sup>49</sup>

7.48 The Panel observes that the protection provided by the Copyright Law is addressed *inter alia* in Chapter II, Section 1 titled "Copyright Owners and Their Rights". That Section includes Article 10, which provides that "copyright" includes a list of four moral rights and 13 economic rights set out in the first paragraph of that Article. The economic rights include, for example, (5) the right of reproduction; (11) the right of broadcasting; (14) the right of adaptation; and (15) the right of translation. Every specific right in that list relates to "a work" (作品). The second paragraph of Article 10 provides that copyright owners may "authorize" others' exercise of the economic rights set out in subparagraphs (5) through (17). Chapter II, Section 3, titled "Term of Protection for the Rights" provides in Article 21 for the term of "protection" for the economic rights set out in subparagraphs (5) through (17) of the first paragraph of Article 10.

7.49 The economic rights appear to be exclusive rights in light of, *inter alia*, Article 11, which provides that the copyright in a work shall belong to its author, and Article 24, which provides that

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<sup>45</sup> The remaining provisions of Chapter I concern the departments responsible for administration (Article 7); and collective copyright administration (Article 8).

<sup>46</sup> China's first written submission, fn. 261.

<sup>47</sup> United States' rebuttal submission, para. 201.

<sup>48</sup> United States' first written submission, paras 217-218.

<sup>49</sup> China's response to Question No. 89.

anyone who exploits another person's work shall conclude a copyright licensing contract with the copyright owner, subject to exceptions.

7.50 The Panel finds that the Copyright Law is sufficiently clear, on its face, to show that Article 4(1) denies the protection of Article 10 to certain works, including those of WTO Member nationals, as the United States claims.

7.51 This interpretation is consistent with, and clarified by, the view expressed by the Supreme People's Court of China in the course of domestic litigation in 1998, to which the Panel will refer as "the *Inside Story* case".<sup>50</sup> The United States submitted a letter sent from the Supreme People's Court to a provincial Higher People's Court during that case, which the Supreme People's Court reissued in 2000.<sup>51</sup> This letter, from China's highest judicial body, is instructive in the interpretation of Article 4(1) of the Copyright Law.<sup>52</sup> That case concerned a book, the publication of which violated administrative regulations but the content of which did not violate any laws. In the letter, the Court ruled that it was correct for the courts of the first and second instances to provide protection under the Copyright Law to the book at issue for the following reason:

"The *Inside Story* was originally published in the magazine 'Yanhuang Chunqiu' (1994, No. 2). In May of the same year, the United Front Department of the Sichuan Provincial Communist Party Committee reviewed the book and approved its publication. Nothing was found in the text of the *Inside Story* to violate any laws. Therefore, it is correct for the courts of the first and second instances to provide it protection under the Copyright Law."<sup>53</sup>

7.52 The Panel finds that the Supreme People's Court letter confirms that Article 4(1) of the Copyright Law denies copyright protection and clarifies that Article 4(1) applies where the publication and/or dissemination of a work is prohibited due to its content.

7.53 The Panel notes that China's own submissions support this view. In the course of its submission that the application of Article 4(1) of the Copyright Law does not depend on content review or any other regulatory regime related to publication (in defence of the claim that content review constituted a "formality" under Article 5(2) of the Berne Convention (1971)), China made the following statements:

"China, like many countries in the world, bans from publication and dissemination such works as those that consist entirely of unconstitutional or immoral content. Art. 4.1 simply provides that such a work also shall not be protected by the Copyright Law. ..."<sup>54</sup>

"As a matter of law, Article 4.1 of the Copyright Law only denies protection to works whose contents are completely unconstitutional or immoral."<sup>55</sup>

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<sup>50</sup> The title of the book that was the subject of the dispute begins with the words "Inside Story".

<sup>51</sup> Letter from the Supreme People's Court to the Hunan Province Higher People's Court in *Zheng Haijin v Xu Zheng Xiong and Tianjin People's Publishing House* (知监字 [1998] Letter no. 33). The letter was redistributed by the Supreme People's Court on 9 March 2000 in an intellectual property document series. It is now listed on the website of the State Intellectual Property Office under the heading "judicial interpretation" (司法解释). The original version is reproduced in Exhibit US-60.

<sup>52</sup> The Panel notes that judicial decisions in China do not have a binding effect for other courts but serve as a reference only.

<sup>53</sup> Exhibit US-60.

<sup>54</sup> China's first written submission, para. 229.

<sup>55</sup> China's first written submission, para. 243.

"China also notes that to the extent that Art. 4.1 independently of the content review process might act to deny copyright protection to a work independently found by a court to be prohibited by law, this act of prohibition is protected by Berne Convention Art. 17 ..."<sup>56</sup>

7.54 China submitted a written reply from the National Copyright Administration of China ("NCAC") to the Supreme People's Court in the *Inside Story* case, in response to a request from the Supreme People's Court prior to sending the letter quoted at paragraph 7.51 above. China quoted the NCAC reply in its first written submission which stated, in part, as follows:

"Under the Copyright Law, the copyright is created upon the composition of the work. In general, the author is entitled to the copyright, and is protected by the Copyright Law. Only works the publication or dissemination of which are prohibited by law are not protected by the Copyright Law. Yet the '[w]orks the publication and dissemination of which are prohibited by law' in Article 4 of the Copyright Law refer only to works whose contents are illegal (reactionary, pornographic, or superstitious contents). If the contents of *Inside* are illegal, it will not be protected by Copyright Law, and all the presses shall neither publish nor disseminate it. ..."<sup>57</sup>

7.55 From the above, China concluded in its first written submission as follows:

"Thus, the NCAC had clarified that only when the contents of the work are found to be illegal will Article 4.1 come into play; violation of publishing rules does not deprive the right-holder the right to have its copyright protected and enforced by law."<sup>58</sup>

7.56 In its first oral statement, China stated as follows:

"China also notes that while Article 4.1, on its face, could operate to deny protection to works whose contents are illegal or immoral, the content review process operates independently of Article 4."<sup>59</sup>

7.57 The above evidence confirms the Panel's finding at paragraph 7.50 above, as confirmed and clarified at paragraph 7.52. Later, China continued to confirm the same point (subject to a clarification, discussed at paragraph 7.61 below) but explained that denial of protection under Article 4(1) of the Copyright Law was subject to a determination by a court or the NCAC. In response to questions after the first substantive meeting, China stated that:

"Article 4.1 of China's Copyright Law empowered China's courts and the National Copyright Administration of China to deny copyright protection to works that are prohibited by law."<sup>60</sup>

7.58 In its rebuttal submission, China reiterated the point as follows:

"Nor does Art. 4.1 function in any other way as a condition precedent to copyright. ... Art. 4.1 is envisaged by China's authorities to operate as a condition subsequent in

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<sup>56</sup> China's first written submission, para. 280.

<sup>57</sup> China's first written submission, para. 243, quoting a reply from the Copyright Administration Department of the NCAC (权司 [1998] No. 39) to the Intellectual Property Rights Tribunal of the Supreme People's Court, reproduced in Exhibit CHN-118.

<sup>58</sup> China's first written submission, para. 243.

<sup>59</sup> China's first oral statement, para. 83.

<sup>60</sup> China's response to Question No. 44.

one narrow judicial context, and to the extent that it so operates, it is entirely consistent with the requirements of the Berne Convention."<sup>61</sup> (footnote omitted)

7.59 China specifically acknowledged that it would not protect the copyright in the unedited, prohibited version of a work that failed content review where enforcement action was requested against unedited, prohibited infringing versions.<sup>62</sup>

7.60 All of the above statements confirm the Panel's view, based on the evidence submitted by the United States including, in particular, the wording of the Copyright Law on its face, that Article 4(1) of that Law provides for the denial of copyright protection to certain works based on their content.

7.61 However, after the first substantive meeting, China provided a clarification of its earlier statements. China submits that Article 4(1) of the Copyright Law does not lead to a denial of "copyright" but only of "copyright protection". China argues that Article 4(1) of the Copyright Law does not affect the vesting of copyright afforded by Article 2. The core principle is that Chinese law will not enforce the protection of the Copyright Law for works the contents of which are already illegal. China explained as follows:

"To the extent that Art. 4.1 would come into play with respect to a work, it would operate not to remove copyright, but to deny the particularized rights of private copyright enforcement. Art. 4.1 thus does not operate in any manner that would violate Berne Art. 5(1): it does not destroy the residual Art. 2 copyright. If applied, its effect would be to deny to the right-holder the power of private censorship that would generally be available to non-prohibited works."<sup>63</sup>

7.62 In response to questions after the second substantive meeting, China argued that, after "protection" is denied under Article 4(1), the underlying recognition – the "enjoyment" of, or "entitlement" to, copyright – would continue.<sup>64</sup> As noted earlier, the United States submits that this distinction is artificial.<sup>65</sup>

7.63 The Panel notes that China equates the "protection" of the Copyright Law referred to in Article 4(1) with enforcement rights. However, China does not show any suitable basis in the text of Article 4(1) that would limit its effect to a subset of the protection under the Copyright Law. China contrasts the "protection" of the Copyright Law referred to in Article 4(1) with the "enjoyment" of copyright in accordance with Article 2 of the Copyright Law. However, the concepts referred to in Articles 2(2) and 4(1), on their face, are identical. China points out that Article 4(1) does not state that certain works "shall not enjoy copyright".<sup>66</sup> That is true, but the protection of the Law *is* copyright.

7.64 China's argument distinguishing "copyright" from "copyright protection" also contrasts the vesting of copyright under Article 2 of the Copyright Law, which allegedly occurs upon creation of a work automatically without formality, on the one hand, with the procedure for denial of copyright under Article 4(1) of the same Law, which allegedly occurs only after a determination by a court or the NCAC during an enforcement proceeding, on the other hand.

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<sup>61</sup> China's rebuttal submission, para. 261.

<sup>62</sup> China's response to Question No. 52.

<sup>63</sup> China's response to Question No. 44; see also its response to Question No. 45; rebuttal submission, paras 280-281.

<sup>64</sup> China's response to Question No. 92.

<sup>65</sup> United States' second oral statement (closing statement), para. 25.

<sup>66</sup> China's response to Question No. 88.

7.65 The United States submits that the fact that an author may not be on official notice of the operation of Article 4 until the denial of protection is stated by an authoritative content review agency or court does not appear to alter the way in which the law operates.<sup>67</sup>

7.66 The Panel considers that the distinction drawn by China is inapposite. It appears to be a consequence of the rule that the enjoyment and exercise of copyright shall *not* be subject to any formality whilst the denial of protection, in China's view, *is* subject to a formal determination. Even accepting the distinction at face value, it does not properly address the situation *after* a court or the NCAC has denied protection to a work under Article 4(1) of the Copyright Law. It is difficult to conceive that copyright would continue to exist, undisturbed, after the competent authorities had denied copyright protection to a work on the basis of the nature of the work and the prohibition in the Copyright Law itself.

7.67 After a denial of copyright protection under Article 4(1) of the Copyright Law, China has not explained in what sense authors would enjoy copyright, or copyright would exist, in their works. For example, it has not explained how authors would be able to assert ownership of, license, or transfer copyright in their works. To the extent that any copyright exists under Article 2 in this situation, it would seem to be no more than a phantom right, the existence of which could not be demonstrated. Therefore, on the basis of the evidence submitted, the Panel is unable to conclude that, after a work is denied protection under Article 4(1) of the Copyright Law, the author could enjoy "copyright" in that work.

7.68 In any event, the scheme of the TRIPS Agreement is one which provides for certain subject matter to enjoy protection under Part II, and Members must ensure that procedures to enforce that protection are available as specified in Part III. Where a Member's law provides that eligible subject matter shall not be protected by an intellectual property law, this is not simply a provision that the enforcement procedures shall not be available, inconsistent with Part III. Rather, it is inconsistent with Part II as well. Whilst China's judicial authorities may decide that they will not provide particular remedies in particular circumstances in the exercise of their own discretion, Article 4(1) of China's Copyright Law goes further by denying protection of eligible subject matter altogether.

7.69 China refers to the letter of the Supreme People's Court and to the written reply of the NCAC in the *Inside Story* case, both quoted above, in support of a distinction between "copyright" and "copyright protection".<sup>68</sup> The Panel observes that those distinguished authorities used the language of Article 4(1) of the Copyright Law and that the NCAC related Article 4(1) both to copyright protection and to the enjoyment of copyright.<sup>69</sup> Therefore, the Panel sees no reason why this evidence would lead to a different conclusion from that reached based on the wording of the Copyright Law on its face.

7.70 China asserts that Article 2 of the Copyright Law directly implements an author's rights under the Berne Convention (1971) into Chinese law and that, so long as copyright is granted under the Berne Convention, that right is protected by Chinese law.<sup>70</sup> China does not argue that any international treaty prevails over the terms of the Copyright Law with respect to foreign works in case

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<sup>67</sup> United States' rebuttal submission, para. 188.

<sup>68</sup> China's responses to Questions Nos. 88 and 92.

<sup>69</sup> The NCAC reply referred to in note 57 above explained as follows:

"However if the contents do not violate the law ... the work does not fall within the scope of the '[w]orks the publication and dissemination of which are prohibited by law' in Article 4 of the Copyright Law. ... [T]he contents of the book were not illegal, thus it is proper to affirm that Zheng Haijin *enjoys the copyright* in Inside." (emphasis added)

<sup>70</sup> China's first written submission, para. 240; rebuttal submission, paras 276-277. China does not argue that it directly implements the TRIPS Agreement.

of any deviation from the obligations in an international treaty.<sup>71</sup> Rather, China specifically confirms that Article 4(1) is envisaged as a limited exception to this general principle in Article 2.<sup>72</sup> Therefore, the Panel sees no reason to consider the possible direct effect of the rights specially granted by the Berne Convention (1971), as incorporated by the TRIPS Agreement.

7.71 For the above reasons, the Panel does not consider that China has provided any evidence that would disturb its finding at paragraph 7.50 above.

(ii) *Criteria for prohibited works*

7.72 The Panel will now consider the range of works that are subject to Article 4(1) of the Copyright Law. This depends in large part on the meaning of the phrase "the publication and/or dissemination of which are prohibited by law" as used in Article 4(1). The Panel recalls its finding at paragraph 7.45 above that that term, on its face, is not limited to any particular law.

7.73 The United States submits an illustrative list of laws and regulations prohibiting publication or distribution that, in its view, lead to the denial of copyright protection under Article 4(1) of the Copyright Law. The list was provided by China during the Council for TRIPS review of its legislation in 2002 in a response to a question regarding the laws and regulations to which Article 4(1) of the Copyright Law refers. The laws and regulations mentioned are the Criminal Law, the Regulations on the Administration of Publishing Industry, the Regulations on the Administration of Broadcasting, the Regulations on the Administration of Audiovisual Products, the Regulations on the Administration of Films, and the Regulations on the Administration of Telecommunication.<sup>73</sup>

7.74 China confirms that the listed laws reference a legal standard defining what kind of works, or contents, are prohibited.<sup>74</sup> In response to a question from the Panel, China confirmed that the term "prohibited by law" has a broad meaning, and may refer to the criteria set forth in various provisions of some of the laws and regulations in this list, so that a work that contains contents prohibited by such laws is a prohibited work within the meaning of Article 4(1) of the Copyright Law.<sup>75</sup>

7.75 The Panel notes the parties' eventual agreement regarding criteria for prohibited works but, in view of the evolution of this issue during this proceeding, the Panel will review the evidence.

7.76 The letter from the Supreme People's Court of China in the *Inside Story* case shows that Article 4(1) of the Copyright Law was considered inapplicable in that case because nothing was found in the text of the work at issue to violate "any laws".<sup>76</sup> The terms of the letter were not limited to any particular laws but appear to include any law that determines the legality of content.

7.77 The written reply of the NCAC to the Supreme People's Court of China in the same case was translated as follows:

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<sup>71</sup> For example, under a specific provision such as Article 19 of the Provisions on the Implementation of International Copyright Treaties, set out in Exhibit CHN-117, or general principles of law.

<sup>72</sup> China's response to Questions Nos. 45 and 89; rebuttal submission, para. 280.

<sup>73</sup> United States' first written submission, para. 69, referring to document IP/Q/CHN/1, p. 26. This list was also reproduced in the request for establishment of a panel but the United States, in its submissions to the Panel, does not request relief in respect of these measures in conjunction with Article 4 of the Copyright Law: see paragraph 2.4, note 3 above. China confirmed that the referenced "Regulations on the Administration of Telecommunication" are the Regulations on Telecommunications cited in note 82 below: see China's first written submission, fn. 261.

<sup>74</sup> China's first written submission, fn. 261.

<sup>75</sup> China's response to Question No. 90.

<sup>76</sup> See paragraph 7.51 above, referring to letter from the Supreme People's Court reproduced in Exhibit US-60.

"Yet the '[w]orks the publication and dissemination of which are prohibited by law' in Article 4 of the Copyright Law refer only to works whose contents are illegal (reactionary, pornographic, or superstitious contents)."<sup>77</sup>

7.78 China, in its first written submission to the Panel, interpreted this as follows:

"As a matter of law, Article 4.1 of the Copyright Law only denies protection to works whose contents are completely unconstitutional or immoral."<sup>78</sup>

7.79 The broad criteria quoted in China's submission appeared to the Panel to be subsets of the criteria applied under the content review regulations. For example, Article 25 of the Regulations on the Administration of Films, Article 3 of the Regulations on the Administration of Audiovisual Products and Article 26 of the Regulations on the Administration of Publications contain identical lists of ten categories of prohibited content in films, audiovisual products and publications, including those that:

- (1) are against the fundamental principles established in the Constitution;
- (2) jeopardize the unification, sovereignty and territorial integrity of the State;
- (3) divulge State secrets, jeopardize security of the State, or impair the prestige and interests of the State;
- (4) incite hatred and discrimination among ethnic groups, harm their unity, or violate their customs and habits;
- (5) propagate cults and superstition;
- (6) disrupt public order and undermine social stability;
- (7) propagate obscenity, gambling, or violence, or abet to commit crimes;
- (8) insult or slander others, or infringe upon legitimate rights and interests of others;
- (9) jeopardize social ethics or fine national cultural traditions;
- (10) other contents banned by laws, administrative regulations and provisions of the State."<sup>79</sup>

7.80 China confirmed that content falling within categories (1), (2) and (7) were "clearly unconstitutional".<sup>80</sup> Categories (5) and (7) on their face refer to "superstitious" and "pornographic" content, or "immoral" content, which is mentioned in paragraphs 7.77 and 7.78 above. In response to a question from the Panel, China submitted that the phrase "prohibited by law" may refer to the above

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<sup>77</sup> See paragraph 7.54 above. The NCAC is a competent administrative agency under the Copyright Law in accordance with Article 7 of the Law.

<sup>78</sup> China's first written submission, para. 243.

<sup>79</sup> Mutually agreed translation no. 12.

<sup>80</sup> China's first written submission, fn. 255, referring to the 1982 Constitution, Articles 52-54, reproduced in Exhibit CHN-122.

substantive criteria<sup>81</sup> and to provisions such as Article 57 of the Regulations on Telecommunications<sup>82</sup> and Article 364 of the Criminal Law.<sup>83</sup>

7.81 The Panel notes that the list of prohibited content in the three content review Regulations set out at paragraph 7.79 includes six other categories of content that were not mentioned by the NCAC. However, the Panel does not infer that the NCAC meant that the criteria to determine whether the publication and/or dissemination of a work are prohibited by law for the purposes of Article 4(1) of the Copyright Law are narrower than the complete list of criteria in the content review regulations. The written reply of the NCAC listed three broad criteria, followed in the original version by 等, meaning "etcetera", indicating that they were not exhaustive, and the written reply was provided in the context of a case where the issue was whether a prohibition of publication for administrative reasons *unrelated* to content fell foul of Article 4(1) of the Copyright Law. China's submissions referred to at paragraph 7.74 above appear to confirm this view.

7.82 For the above reasons, the Panel accepts that prohibited works for the purposes of Article 4(1) of the Copyright Law include works that contain content considered illegal under the criteria set out in the law and regulations listed at paragraph 7.73 above, including the content review regulations.

(iii) *Procedure for determination that a work is prohibited for the purposes of Article 4(1)*

7.83 The Panel notes that the range of works "prohibited by law" may depend not only on the criteria by which content is considered illegal but also on the procedure for determination that a work contains illegal content for the purposes of Article 4(1) of the Copyright Law.

7.84 The United States claims that Article 4(1) of the Copyright Law applies to (a) works never submitted for content review in China; (b) works awaiting the results of content review in China; (c) the unauthorized versions of works edited for distribution in China; and (d) works that have failed content review.<sup>84</sup>

7.85 China, in its first written submission, submitted that the content review process operates independently of Article 4(1) of the Copyright Law and that the only result of a finding of prohibited content is a denial of authority to publish. Nothing in that finding leads to a denial of copyright.<sup>85</sup> However, after the first substantive meeting, China revised lengthy sections of its first written submission with respect to the relationship between copyright and content review.<sup>86</sup>

7.86 China maintains that "[t]he process of content review remains, as an administrative matter, separate from copyright."<sup>87</sup> The only authorities competent to make a decision under Article 4(1) of the Copyright Law are the courts and the NCAC. However, a court or the NCAC, when making a decision on copyright protection under Article 4(1) of the Copyright Law, would be "deferential" to a content review finding. When a content review authority makes a determination that a work contains prohibited content, that finding will "guide" a determination by the NCAC or the courts that the work

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<sup>81</sup> China's response to Question No. 90, listing in fn. 3 the ten criteria set forth in Article 25 of the Regulation on the Administration of Films.

<sup>82</sup> Article 57 of the Regulations on Telecommunications adopted by the Standing Committee of the State Council on 20 September 2000, and promulgated by Decree No. 291 of the State Council on 25 September 2000, contains many of the same criteria as Article 25 of the Regulation on the Administration of Films. The Regulations on Telecommunications are reproduced in Exhibit CHN-124.

<sup>83</sup> Article 364 of the Criminal Law prohibits *inter alia* the dissemination of pornographic materials. Article 364 is reproduced in Exhibit CHN-1.

<sup>84</sup> United States' first written submission, para. 198.

<sup>85</sup> China's first written submission, paras 246.

<sup>86</sup> See China's response to Question No. 52.

<sup>87</sup> China's rebuttal submission, para. 242.

would be considered "prohibited by law". China specifically acknowledges that when a work has failed content review it will not protect the copyright in the unedited, prohibited version of a work against infringing versions that also are unedited and prohibited. Nor will it protect copyright in the deleted portion of a work edited in order to pass content review.<sup>88</sup>

7.87 The Panel will first consider works that have failed content review as a whole.<sup>89</sup> The parties agree that such works are prohibited works under Article 4(1) of the Copyright Law. The Panel recalls that Article 4(1) denies prohibited works the protection of the Copyright Law, not just a subset of the protection of that Law. China asserts that works that have failed content review can receive protection under the Copyright Law in a situation where the illegal content has been deleted. The Panel observes that this situation does not apply where the work that failed content review is considered illegal in its entirety. If a prohibited work includes some legal content, and an edited version has been produced without approval, China asserts that it "will enforce the copyright in the legal portion of the original work, even though that work itself – as a whole – is prohibited by law."<sup>90</sup> However, China did not explain how this was possible under its law. Therefore, the Panel finds that the class of prohibited works under Article 4(1) of the Copyright Law includes works that have failed content review.

7.88 The Panel now considers works that have passed content review subject to a requirement to delete specific illegal content.<sup>91</sup> China protects the approved version but acknowledges that it will not protect the deleted illegal content.<sup>92</sup> It is not clear on the face of the Copyright Law if or how Article 4(1) applies where enforcement is sought against infringing copies of the unedited version. The Panel notes China's position in this proceeding that:

"China notes that it also will enforce the right-holder's copyright in [a situation] where there is an authorized edited version. In that case, the copyright will be protected irrespective of whether the infringing copy is of the edited or the unedited version."<sup>93</sup>

7.89 The Panel now turns to works never submitted for content review in China and works awaiting the results of content review in China. The United States provides no specific examples where such works have been denied copyright protection.<sup>94</sup> The claim, with respect to these categories of works, is based on the response given by China in the Council for TRIPS' review of its legislation referred to at paragraph 7.73 above, and the United States' own construction of the relationship between these other measures and the Copyright Law.

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<sup>88</sup> China's responses to Questions Nos. 45 and 52 posed by the Panel and to Question No. 2 posed by the United States; rebuttal submission, para. 249.

<sup>89</sup> For example, the evidence shows that when approval was declined for certain audiovisual products, the content review notices stated that the films as a whole violated relevant criteria, without listing the illegal content: see Exhibits CHN-142, CHN-143, CHN-144, CHN-145 and CHN-146.

<sup>90</sup> China's response to Question No. 52.

<sup>91</sup> For example, the evidence shows that when approval was granted for certain audiovisual products, the licence was accompanied by a list of specific scenes to be deleted from some of them: see Exhibit CHN-147.

<sup>92</sup> China's response to Question No. 2 posed by the United States.

<sup>93</sup> China's response to Question No. 52.

<sup>94</sup> China submits that this is because no such examples exist: see China's response to Question No. 52; rebuttal submission, para. 234. However, China also submitted that the Supreme People's Court is not aware of a single instance in which a defendant in a copyright infringement action successfully asserted a defence that the work did not enjoy copyright because it failed a content review process (first written submission, para. 277) but later acknowledged that it would not protect copyright in such a work under certain conditions (response to Question No. 52).

7.90 The Panel will first consider the content review regulations. The Regulations on the Administration of Films, in Article 24, provide as follows:

"Article 24. Films which have not been reviewed and approved by the film review institutions under the administrative department of radio, film and television under the State Council ... shall not be distributed, projected, imported or exported."<sup>95</sup>

7.91 The Regulations on the Administration of Audiovisual Products, in Article 36, provide for mandatory content review prior to wholesaling, retailing or rental of audiovisual products.<sup>96</sup>

7.92 It is not disputed that films and audiovisual products that have not yet been approved under the Regulations on the Administration of Films or the Regulations on the Administration of Audiovisual Products, as the case may be, may not be published and/or distributed. Although none of the content review regulations submitted in evidence makes any express provision for the denial of copyright protection, they do provide for the prohibition of publication of films and audiovisual products. Whilst it seems plausible that films and audiovisual products in this situation might be considered *ipso facto* works the publication of which is prohibited for the purposes of Article 4(1) of the Copyright Law, it is not clear if another determination is required that their *content* violates these Regulations before the works are considered prohibited works within the scope of Article 4(1).

7.93 The Regulations on the Administration of Publications do not provide for mandatory government content review prior to publication. However, in Articles 40 and 44, they do prohibit the distribution by a "distribution entity", or the importation by a "publication importation entity", of publications containing prohibited content.<sup>97</sup> A determination would appear to be required that their content violates these Regulations before such works are considered prohibited works within the scope of Article 4(1) of the Copyright Law.

7.94 Two of the measures listed by the United States prohibit certain content without providing a procedure for content review.<sup>98</sup> These are the Regulations on Telecommunications<sup>99</sup> and the Criminal Law.<sup>100</sup> Accordingly, with respect to these two measures, a determination is required that works violate these measures for the purposes of Article 4(1) of the Copyright Law.

7.95 Where no content review has taken place, it is not clear on the face of any of these measures how a determination is made that a work is prohibited within the meaning of Article 4(1) of the Copyright Law. China submits that if no prior review has taken place, a court or the NCAC must determine legality or illegality *de novo* and that this would normally be the case for most books, periodicals and newspapers, foreign works not released in China, works pending review and other unpublished books and works that may have illegally bypassed the reviewing process and are in unlicensed circulation.<sup>101</sup> China also submits that the court or the NCAC could be expected to solicit opinions from the content reviewing authorities.<sup>102</sup>

7.96 The question arises as to the status of copyright in such works in the absence of a determination for the purposes of Article 4(1) of the Copyright Law. The Panel notes that Article 2 of the Copyright Law, on its face, provides that copyright in certain works shall be protected by the

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<sup>95</sup> Mutually agreed translation no. 12. Article 31 also provides that films to be imported for public show shall be submitted to the film review institution for review before importation.

<sup>96</sup> Mutually agreed translation no. 13.

<sup>97</sup> Mutually agreed translation no. 14, where the word "distribute" translates the word "发行".

<sup>98</sup> China's first written submission, fn. 261.

<sup>99</sup> See note 82 above.

<sup>100</sup> See note 83 above.

<sup>101</sup> China's rebuttal submission, para. 249.

<sup>102</sup> China's response to Question No. 45.

Copyright Law. Article 6 of the Regulations for the Implementation of the Copyright Law of 2002 (the "Copyright Implementing Regulations") provides that "[a] copyright shall subsist on the date when a work is created."<sup>103</sup>

7.97 Whilst it is clear on the face of the measure that Article 4(1) of the Copyright Law denies copyright protection to certain works, it does not necessarily follow that this pre-empts the subsistence of copyright protection under Article 2, as implemented by Article 6 of the Copyright Implementing Regulations, from the time of creation of the work up until the time that a competent authority makes a decision under Article 4(1) of the Copyright Law. Consequently, it is not clear to the Panel whether works not submitted for mandatory content review and works awaiting the results of content review would fall within the scope of Article 4(1) of the Copyright Law.<sup>104</sup>

7.98 The Panel has also reviewed evidence of specific instances of administrative enforcement submitted by China. With respect to works never submitted for content review, the evidence includes examples of pirated versions of foreign textbooks. The Panel notes that Decision notices for administrative penalties were issued by the NCAC and two subsidiary copyright bureaux in June and October 2006 under Article 47 of the Copyright Law to three universities for unauthorized reproduction and distribution of textbooks.<sup>105</sup> However, the Panel does not find these instances instructive as (1) there is no mandatory pre-publication content review procedure for university textbooks; and (2) the textbooks concerned subjects such as bridge design, social welfare, physics and economics that do not have any obvious relationship to the content prohibited under the relevant Regulations.

7.99 With respect to works awaiting the results of content review, the evidence includes an example of a "special" administrative enforcement action with respect to pirated audio-visual products of one foreign animated film, *Shrek 2*, before the genuine version was approved for marketing.<sup>106</sup> The Panel notes that administrative penalty documents citing Article 47 of the Copyright Law and Article 36 of the Copyright Implementing Regulations were issued in September 2004 to one audio-visual shop in Xiamen relating to the distribution of unauthorized DVD copies of *Shrek 2*.<sup>107</sup>

7.100 The evidence also includes a Circular of the NCAC issued in November 2001 to subsidiary copyright bureaux in order to enhance enforcement actions against a list of 788 foreign cinematographic works in response to a request from the Motion Picture Association of America. The introductory paragraph of the Circular indicates that this was also a special action. The Circular included works without enquiry as to whether they had all been edited to pass content review and, in accordance with paragraph 2, it applied *inter alia* to pirated DVDs coded for zones outside China, which may include unedited versions not approved during content review.<sup>108</sup>

7.101 The United States responds that the NCAC and local copyright bureaux are administrative agencies with no authority to interpret the Copyright Law in cases that are before the courts.<sup>109</sup> China replies that Articles 46 and 47 of the Copyright Law and Articles 217 and 218 of the Criminal Law provide three means of enforcement of copyright: civil procedures, administrative procedures and

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<sup>103</sup> Exhibit CHN-19.

<sup>104</sup> China's response to Question No. 52.

<sup>105</sup> Exhibits CHN-136, CHN-137, CHN-138 and CHN-139. An investigation report by a provincial copyright bureau against university textbooks in Exhibit CHN-140 did not cite the Copyright Act.

<sup>106</sup> United States' first written submission, paras 239-241, citing a statement of China in the minutes of a meeting of Council for TRIPS in IP/C/M/46 at para. 203 in Exhibit US-57; cf. China's first written submission, paras 268-270.

<sup>107</sup> China's first written submission, para. 270, referring to Exhibits CHN-132; CHN-133; CHN-134; response to Question No. 95.

<sup>108</sup> Circular No. 55 of the National Copyright Administration 权司 [2001] No. 55 in Exhibit CHN-141.

<sup>109</sup> United States' first oral statement, paras 85-86.

criminal procedures, and that the courts have jurisdiction over civil and criminal matters while the NCAC has jurisdiction over administrative matters.<sup>110</sup>

7.102 The Panel notes that the NCAC is a competent administrative agency under the Copyright Law<sup>111</sup> and that the Supreme People's Court of China sought its view in the *Inside Story* case on the issue under examination in this claim. Therefore, the Panel considers that it may take this evidence into account. However, the Panel notes that both instances discussed in paragraphs 7.99 and 7.100 above occurred in special circumstances and there is no indication in the second instance that any enforcement procedures actually took place. Therefore, the Panel gives this evidence little weight in its assessment of the Copyright Law as such. Accordingly, the Panel reiterates its comments at paragraph 7.88 and 7.97 above.

7.103 For the reasons set out above, the Panel finds that the class of works denied protection under Article 4(1) of the Copyright Law includes works that have failed content review and, to the extent that they constitute copyright works, the deleted portions of works edited to satisfy content review. The Panel considers that the United States has not made a prima facie case with respect to works never submitted for content review in China, works awaiting the results of content review in China and the unedited versions of works for which an edited version has been approved for distribution in China.

(iv) *Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement*

7.104 This claim is made under Article 9.1 of the TRIPS Agreement, insofar as it incorporates Article 5(1) of the Berne Convention (1971). Article 9.1 of the TRIPS Agreement provides as follows:

"Members shall comply with Articles 1 through 21 of the Berne Convention (1971) and the Appendix thereto. However, Members shall not have rights or obligations under this Agreement in respect of the rights conferred under Article 6bis of that Convention or of the rights derived therefrom."

7.105 The United States and China are both WTO Members and, accordingly, both are bound by the TRIPS Agreement, including the incorporated provisions of the Berne Convention (1971). The provisions of the Berne Convention (1971) incorporated by Article 9.1 of the TRIPS Agreement include Article 5(1) of that Convention, which provides as follows:

"(1) Authors shall enjoy, in respect of works for which they are protected under this Convention, in countries of the Union other than the country of origin, the rights which their respective laws do now or may hereafter grant to their nationals, as well as the rights specially granted by this Convention."

7.106 Article 5(1) of the Berne Convention (1971) provides for the enjoyment of two overlapping sets of rights that have been described as "the twin pillars on which protection under the Convention rests".<sup>112</sup> First, there are "the rights which their respective laws do now or may hereafter grant to their

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<sup>110</sup> China's response to Question No. 46.

<sup>111</sup> Article 7 of the Copyright Law.

<sup>112</sup> Ricketson, S., *The Berne Convention for the Protection of Literary and Artistic Works: 1886-1986* (Queen Mary College, 1987) ("Ricketson"), p. 543, para. 5.66; and also Ricketson, S. and Ginsburg, J.C., *International Copyright and Neighbouring Rights – The Berne Convention and Beyond* (Oxford University Press, 2006), p. 310, para. 6.90.

nationals".<sup>113</sup> This is a national treatment obligation. The request for establishment of a panel included a claim under this part of Article 5(1) with respect to the Copyright Law in conjunction with certain other measures listed at paragraph 7.186 below, but this claim was not pursued.

7.107 Second, there are "the rights specially granted by this Convention". This term is not defined. However, Article 5(1) refers to rights that authors shall enjoy in respect of works. Articles *6bis*, 8, 9, 11, *11bis*, *11ter*, 12, 14, *14bis* and *14ter* all provide for such rights.<sup>114</sup> Nevertheless, the incorporation of provisions of the Berne Convention (1971), including Article 5, is subject to the terms of Article 9.1 of the TRIPS Agreement (quoted at paragraph 7.104 above). Therefore, "the rights specially granted by this Convention" as used in Article 5(1) of that Convention, as incorporated by Article 9.1 of the TRIPS Agreement, do not include the rights referred to in Article *6bis* of the Berne Convention (1971). This Report refers to these rights in that sense.

7.108 The United States' claim relates to these rights, as a group. It makes a separate claim with respect to Article 5(2) of the Berne Convention (1971), which the Panel does not consider in this subsection of this Report.

7.109 China submits that it has implemented Article 5(1) of the Berne Convention (1971).<sup>115</sup> It offers no defence based on the terms of that Article but rather refers to Article 17 of the Berne Convention (1971), which the Panel addresses at paragraphs 7.120 to 7.137 below.

7.110 The Panel notes that the "rights specially granted" by the Berne Convention (1971), as incorporated by the TRIPS Agreement, include the exclusive right of making and of authorizing translation of works (in Article 8) and the exclusive right of authorizing reproduction of works (in Article 9), to name but the first two substantive rights.

7.111 As regards China's implementation of the "rights specially granted" by the Berne Convention (1971), the United States refers to the rights enumerated in Article 10 of the Copyright Law, as well as Articles 46 and 47 of the same Law. It does not challenge any of these particular Articles of the Copyright Law.<sup>116</sup>

7.112 China agrees that it grants to authors all the substantive protections of the Berne Convention, in addition to others, through Article 10 of the Copyright Law.<sup>117</sup> It submits that Article 10 of the Copyright Law fully complies with all Berne Convention requirements.<sup>118</sup>

7.113 The Panel notes that many of the rights listed in subparagraphs (5) to (17) of the first paragraph of Article 10 of the Copyright Law provide for rights specially granted by the Berne Convention (1971), that the second paragraph of Article 10 provides that copyright owners may authorize others' exercise of these economic rights, and that these rights appear to be exclusive (as reviewed at paragraphs 7.48 and 7.49 above). Therefore, the Panel finds that it is Article 10 of the Copyright Law that implements rights specially granted by the Berne Convention (1971).<sup>119</sup>

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<sup>113</sup> The Panel notes that this provision, as incorporated by Article 9.1 of the TRIPS Agreement, is distinct from Article 3.1 of that Agreement.

<sup>114</sup> This enumeration is without prejudice to other such rights.

<sup>115</sup> China submits that its obligations under Article 5 of the Berne Convention are implemented by Article 2(1) of the Copyright Law and Article 6 of the Copyright Implementing Regulations: see China's first written submission, paras 239-241.

<sup>116</sup> United States' first written submission, paras 64-66.

<sup>117</sup> China's rebuttal submission, para. 279.

<sup>118</sup> China's rebuttal submission, para. 303.

<sup>119</sup> This is without prejudice to the consistency of Article 10 of the Copyright Law with the Berne Convention (1971), as incorporated in the TRIPS Agreement.

7.114 The Panel recalls its finding at paragraph 7.50 above that Article 4(1) of the Copyright Law denies the protection of Article 10 to certain works, including those of WTO Member nationals, as the United States claims. The Panel observes that no party alleges that the denial of protection under Article 4(1) of the Copyright Law is permitted by any of the exceptions available with respect to certain specific rights under Articles 9(2), 10 or 10*bis* of the Berne Convention (1971). Nor does any party allege that the denial of protection under Article 4(1) of the Copyright Law is permitted by the exceptions provision in Article 13 of the TRIPS Agreement.

7.115 The Panel notes that both sets of rights under Article 5(1) of the Berne Convention (1971) relate to "works" for which authors are protected under that Convention. The categories of "works" in respect of which authors shall enjoy the rights specially granted by the Convention vary according to the terms of each Article granting the relevant right. For example, the rights of reproduction (Article 9) and of broadcasting (Article 11*bis*) are granted to authors of "literary and artistic works". That expression is defined, in a non-exhaustive manner, in Article 2(1) of the Berne Convention (1971).

7.116 The Panel recalls its finding at paragraph 7.103 above that the class of works denied protection under Article 4(1) of the Copyright Law includes works that have failed content review and, to the extent that they constitute copyright works, the deleted portions of works edited to satisfy content review. The Panel also recalls its findings at paragraphs 7.37 and 7.43 regarding the meaning of the word "works" as used in the Copyright Law, in particular in Article 4(1). No party has disputed that the "works" to which the Copyright Law, in particular Article 4(1), applies include at least some, if not all, the categories of works falling within the definition of "literary and artistic works" in Article 2(1) of the Berne Convention (1971). It is not disputed that the "works" to which Article 4(1) of China's Copyright Law applies are more extensive than those for which protection may be refused or limited under other provisions of Article 2, and under Article 2*bis*, of the Berne Convention (1971).

7.117 For the above reasons, the Panel finds that the Copyright Law is sufficiently clear on its face for the United States to have established that the Copyright Law, specifically Article 4(1), is inconsistent with Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement. This finding is subject to the Panel's consideration of Article 17 of the Berne Convention (1971), set out below.

7.118 The Panel recalls its finding at paragraph 7.103 above and confirms that this conclusion does not apply to works never submitted for content review in China, works awaiting the results of content review in China and the unedited versions of works for which an edited version has been approved for distribution in China. However, the Panel recognizes that the potential denial of copyright protection, in the absence of a determination by the content review authorities, implies uncertainty with respect to works that do not satisfy the content criteria prior to a determination under Article 4(1) of the Copyright Law, with the consequent impact on enjoyment of rights described above. Therefore, the Panel reiterates for the record the firm position of China taken in these proceedings that:

"Copyright vests at the time that a work is created, and is not contingent on publication. Unpublished works are protected, foreign works not yet released in the Chinese market are protected, and works never released in the Chinese market are protected."<sup>120</sup>; and

"Works that are unreviewed are decidedly not 'prohibited by law'."<sup>121</sup>

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<sup>120</sup> China's rebuttal submission, para. 239.

<sup>121</sup> China's rebuttal submission, para. 255.

7.119 China has an international obligation to protect copyright in such works in accordance with Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement.

(v) *Article 17 of the Berne Convention (1971) as incorporated by Article 9.1 of the TRIPS Agreement*

7.120 China raises a defence under Article 17 of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement. China submits that all rights granted to authors under the Berne Convention (1971) are limited by Article 17 of that Convention, that Article 17 is not an exhaustive codification of the sovereign right to censor<sup>122</sup> and that Article 17 is drafted using very expansive language "that effectively denies WTO jurisdiction in this area".<sup>123</sup>

7.121 The United States responds that Article 17 of the Berne Convention (1971) does not authorize a content review system that denies all enforceable copyright protection to all works that have not been approved for publication or distribution.<sup>124</sup>

7.122 The Panel recalls that Article 9.1 of the TRIPS Agreement, quoted at paragraph 7.104 above, incorporates Article 17 of the Berne Convention (1971). Article 17 of the Berne Convention (1971) provides as follows:

"The provisions of this Convention cannot in any way affect the right of the Government of each country of the Union to permit, to control, or to prohibit, by legislation or regulation, the circulation, presentation, or exhibition of any work or production in regard to which the competent authority may find it necessary to exercise that right."

7.123 "The provisions of this Convention" as referred to in Article 17 include Article 5(1) of the Berne Convention (1971).<sup>125</sup>

7.124 The parties agree that Article 17 confirms that governments have certain rights to control the exploitation of works. They do not agree as to whether those rights include a denial of all copyright protection with respect to particular works.

7.125 The Panel observes that the terms of Article 17 include certain broad phrases, notably "cannot in any way affect" and "any work or production". The use of the words "any work" (although it is slightly different in the French text) confirms that the subject-matter dealt with by Article 17 is the same as that addressed by the other substantive provisions of the Convention. However, these phrases are not used in isolation but refer to the right of a government to "permit, to control, or to prohibit ... the circulation, presentation, or exhibition" of any work or production.

7.126 The right of a government "to control, or to prohibit" the "circulation, presentation, or exhibition" of any work or production clearly includes censorship for reasons of public order.<sup>126</sup> Both

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<sup>122</sup> China's first written submission, paras 258-259.

<sup>123</sup> China's rebuttal submission, paras 286-287.

<sup>124</sup> United States' rebuttal submission, para. 221; see also first written submission, fn. 129.

<sup>125</sup> It is not contested that China's laws prohibiting the publication and/or dissemination of works, including determinations made with respect to particular works, constitute "legislation or regulation" within the meaning of Article 17.

<sup>126</sup> Even the right of a government "to permit" the circulation, presentation, or exhibition of a work could be exercised for reasons of public order, such as the publication or broadcast by the police of a photograph of a wanted criminal: see Masouyé, C., *Guide to the Berne Convention*, (World Intellectual Property Organization, 1978) ("WIPO Guide to the Berne Convention"), para. 17.3. The Panel notes that, as stated in its

China and the United States referred to the records of the diplomatic conferences of the Berne Convention<sup>127</sup>, opinions in the academic literature<sup>128</sup> and (in the case of China) to the WIPO Guide to the Berne Convention<sup>129</sup>, that explained that Article 17 relates mainly to censorship and public order.

7.127 The Panel accepts that the three terms "circulation, presentation, or exhibition" are not necessarily an exhaustive list of the forms of exploitation of works covered by Article 17. However, a noticeable feature of these three terms is that they do not correspond to the terms used to define the substantive rights granted by the Berne Convention (1971), although they may be included within some of those rights<sup>130</sup> or they may refer to acts incidental to the exercise of some of those rights.<sup>131</sup> The word "exhibition" is not even used in the provisions setting out the substantive rights granted by the Convention.<sup>132</sup> Therefore, it cannot be inferred that Article 17 authorizes the denial of all copyright protection in any work.

7.128 The Panel appreciates that the position may be somewhat different under Article 10 of China's Copyright Law. Article 10 of the Copyright Law grants in subparagraph (6) "the right of distribution", in subparagraph (8) "the right of exhibition", and in subparagraph (10) "the right of presentation", which may correspond to the "circulation, presentation, or exhibition" of any work in Article 17 of the Berne Convention (1971). Article 10 of the Copyright Law also grants in subparagraph (1) "the right of publication", as well as the "right of distribution", both of which appear to be directly contrary to a prohibition of the publication and/or dissemination of a work due to illegal content, as referenced in Article 4(1) of the Copyright Law. To the extent that Article 10 of the Copyright Law might provide rights additional to, or broader than, those specially granted by the Berne Convention (1971), as incorporated in the TRIPS Agreement and, hence, that Article 4(1) of that Law might deny such rights, the Panel makes no finding.

7.129 The Panel does note that the *second* sentence of Article 4 of the Copyright Law (that is not the subject of the claim in this dispute) may already address China's public policy concerns with respect to some of these rights. The second sentence of Article 4 provides as follows:

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preface, this Guide is not intended to be an authentic interpretation of the provisions of the Berne Convention since such an interpretation is not within the competence of the International Bureau of WIPO.

<sup>127</sup> Main Committee I Report, p.1174 in *Records of the Stockholm Conference 1967*, quoted in Ricketson, see note 112 above, reproduced in Exhibit CHN-128; referred to in the United States' comments dated 7 July 2008 on the material provided to the Panel by the International Bureau of WIPO; referred to in China's first written submission, para. 262; and China's responses dated 21 July 2008 to the United States' comments on the material provided to the Panel by the International Bureau of WIPO.

<sup>128</sup> Ricketson, see note 112 above, *loc. cit.*; Patry, W.F., *Patry on Copyright* (Thomas West, 2007), §23:39 (see Exhibit CHN-129); Goldstein, P., *International Copyright: Principles, Law & Practice* (Oxford University Press, 2001), p. 27, reproduced in Exhibit CHN-126; referred to by China in its first written submission, fns. 264, 266-268 and in its rebuttal submission, paras 296-297.

<sup>129</sup> WIPO Guide to the Berne Convention, see note 126 above, at para. 17.2 in Exhibit CHN-125. Cited in China's first written submission, para. 260; rebuttal submission, para. 293; see also rebuttal submission para. 290 and response to Question No. 93.

<sup>130</sup> For example, the term "la représentation" is expressly included in the French text in Article 17 as well as in Articles 11(1)(i) (ii), 14(1)(ii) and 14*bis*(2)(b) in the phrase "la représentation et l'exécution", rendered as "performance" in the English text.

<sup>131</sup> For example, the word "la circulation" used in Article 17 of the French text is also used in provisions on possible limitations on the rights of translation and reproduction in Articles I(4), II(6), II(8), III(2)(b), III(4)(d), III(6) and IV(5) of the Appendix, rendered as "circulation" in the English text in Articles II(8) and III(4)(d) of the Appendix and "distributed" or "distribution" elsewhere.

<sup>132</sup> The word "exhibition" in Article 17 is also used in the definition of "published works" in Article 3(3) which provides *inter alia* that "the exhibition of a work of art ... shall not constitute publication". Article 3(3) of the French text also uses the word "la représentation" of certain categories of works for the same purpose.

"Copyright owners, in exercising their copyright, shall not violate the Constitution or laws or prejudice the public interests."

7.130 This provision does not deny copyright protection but, as China acknowledges, obliges copyright owners and authorized parties to respect the law in the exercise of their rights.<sup>133</sup> In contrast, the first sentence of Article 4 of the Copyright Law denies all copyright protection with respect to particular works.

7.131 China draws the Panel's attention to the WIPO Guide to the Berne Convention, which states as follows regarding Article 17 of the Berne Convention (1971):

"It covers the right of governments to take the necessary steps to maintain public order. On this point, the sovereignty of member countries is not affected by the rights given by the Convention. Authors may exercise their rights only if that exercise does not conflict with public order. The former must give way to the latter. The Article therefore gives Union countries certain powers to control."<sup>134</sup>

7.132 The Panel agrees with this interpretation. A government's right to permit, to control, or to prohibit the circulation, presentation, or exhibition of a work may interfere with the exercise of certain rights with respect to a protected work by the copyright owner or a third party authorized by the copyright owner. However, there is no reason to suppose that censorship will eliminate those rights entirely with respect to a particular work.

7.133 With respect to those rights that are granted by the Berne Convention (1971), China is unable to explain why Article 4(1) of its Copyright Law provides for the complete denial of their protection with respect to particular works. Without prejudice to the range of rights that are granted by the Berne Convention (1971), it suffices to note that they are mostly exclusive rights of authorizing certain acts with respect to protected works. An exclusive right of authorizing necessarily entails the right to prevent others from carrying out the relevant acts with respect to protected works. China is unable to explain why censorship interferes with copyright owners' rights to prevent third parties from exploiting prohibited works.

7.134 China argues that such copyright protection is a "legal and material nullity", as economic rights are pre-empted by public prohibition. It also argues that copyright enforcement is meaningless in this context.<sup>135</sup> China asks the Panel to note that Article 4(1) of the Copyright Law is an exceedingly narrow provision of law with negligible implications in the marketplace and in terms of any nullification or impairment of benefits to Members.<sup>136</sup>

7.135 The Panel notes that copyright and government censorship address different rights and interests. Copyright protects private rights, as reflected in the fourth recital of the preamble to the TRIPS Agreement, whilst government censorship addresses public interests.

7.136 In response to a question from the Panel, China indicated that it "will always enforce copyrights against infringing edited versions, even when there is no edited version authorized by the author".<sup>137</sup> It did not explain how this was possible under its law. In response to another question from the Panel, China indicated that if an unprotected, prohibited work later becomes legal, it will protect copyright in the work going forward.<sup>138</sup> This might require a new court or NCAC

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<sup>133</sup> China's response to Question No. 93.

<sup>134</sup> WIPO Guide to the Berne Convention, see note 126 above, at para. 17.2.

<sup>135</sup> China's first written submission, para. 280; rebuttal submission, para. 319.

<sup>136</sup> China's rebuttal submission, para. 273; and response to Question No. 44.

<sup>137</sup> China's response to Question No. 51.

<sup>138</sup> China's response to Question No. 53; rebuttal submission, paras 285 and 324.

determination but, in China's view, such a requirement does not constitute a formality under Article 5(2) of the Berne Convention (1971). In any event, the Panel recalls that Article 4(1) of the Copyright Law produces commercial uncertainty prior to a determination that a work is prohibited.<sup>139</sup>

7.137 China maintains that public censorship renders private enforcement unnecessary, that it enforces prohibitions on content seriously, and that this removes banned content from the public domain more securely than would be possible through copyright enforcement.<sup>140</sup> The Panel notes that these assertions, even if they were relevant, are not substantiated.

7.138 The Panel also recalls that if a measure infringes China's obligations under a covered agreement, in accordance with Article 3.8 of the DSU, this is considered *prima facie* to constitute a case of nullification or impairment. Even if the measure at issue has had no actual impact on foreign works to date, it has a *potential* impact on works of WTO Member nationals.

7.139 For the above reasons, the Panel confirms its finding at paragraph 7.117 above and concludes that, notwithstanding China's rights recognized in Article 17 of the Berne Convention (1971), the Copyright Law, specifically Article 4(1), is inconsistent with Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement.

(vi) *Procedural issue*

7.140 China emphasizes that the United States bears the burden of proof of this "as such" claim.<sup>141</sup> China alleges that the only evidence that the United States has offered is the text of Article 4(1) of the Copyright Law itself.<sup>142</sup>

7.141 The Panel notes that the United States provided more evidence than the text of the provision. In any case, the Panel recalls the following statement in the Appellate Body Report in *US – Corrosion-Resistant Steel Sunset Review*:

"When a measure is challenged '*as such*', the starting point for an analysis must be the measure on its face. If the meaning and content of the measure are clear on its face, then the consistency of the measure *as such* can be assessed on that basis alone. If, however, the meaning or content of the measure is not evident on its face, further examination is required. ..." <sup>143</sup>

7.142 In the present case, the Panel's review of the Copyright Law, in particular Article 4(1), on its face, shows that the measure is sufficiently clear to conclude that the United States has made a *prima facie* case of inconsistency. Article 5(1) of the Berne Convention (1971) provides that Members shall ensure that authors shall enjoy in respect of their works the rights specially granted by that Convention. Article 4(1) of the Copyright Law provides that certain works shall *not* receive the protection of that Law and that Law provides the rights specially granted by that Convention. Whilst the Panel has not accepted all the United States' allegations regarding the range of works that fall within Article 4(1), that does not undermine the basic finding of an inconsistency.

7.143 Therefore, the Panel confirms its conclusion at paragraph 7.139 above that the Copyright Law, specifically Article 4(1), is inconsistent with Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement.

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<sup>139</sup> As noted in the United States' rebuttal submission, paras 193-194.

<sup>140</sup> China's rebuttal submission, paras 273 and 318.

<sup>141</sup> China's rebuttal submission, paras 227-229.

<sup>142</sup> China's rebuttal submission, paras 266-268.

<sup>143</sup> Appellate Body Report in *US – Corrosion-Resistant Steel Sunset Review*, para. 168.

7.144 The Panel wishes to emphasize that the United States' claim did not challenge China's right to conduct content review.<sup>144</sup> The Panel's findings do not affect China's right to conduct content review.

**4. Claim under Article 5(2) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement**

(a) Main arguments of the parties

7.145 The United States claims that China subjects the enjoyment and exercise of copyright to the formality of successful conclusion of content review, inconsistently with Article 5(2) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement. Works that have not successfully completed content review under the Regulation on the Administration of Films, the Regulation on the Management of Publications, the Regulation on the Management of Audiovisual Products or the Regulations on the Management of Electronic Publications may not legally be published or distributed within China. The United States submits that, consequently, works in this unauthorized status fall within the scope of Article 4(1) of the Copyright Law, and thus they are not protected by that Law. The United States submits that the Copyright Law's protection attaches only after such a work has been submitted for content review and, if it passes that review unchanged, an authorization to publish and distribute the work has issued. As a formal matter, therefore, copyright protection is dependent, in part, on the issuance of the authorization to publish and distribute resulting from successful conclusion of the content review process.<sup>145</sup>

7.146 China responds that, under Article 2 of the Copyright Law and Article 6 of the Copyright Law Implementing Regulations, copyright protection vests upon creation of a work. While such works are pending review they enjoy the full panoply of copyright.<sup>146</sup> In response to the Panel's questions, China asked the Panel to note that under the Chinese system of copyright, "copyright" and "copyright protection" are distinguishable. To the extent that Article 4(1) of the Copyright Law would come into play with respect to a work, it would operate not to remove copyright, but to deny the particularized rights of private copyright enforcement. Article 4(1) of the Copyright Law thus does not operate in any manner that would violate Article 5(2) of the Berne Convention (1971) as it is not a condition precedent to copyright formation, nor does it destroy the residual copyright granted under Article 2 of the Copyright Law.<sup>147</sup>

7.147 The United States responds that China's distinction between copyright and copyright enforcement lacks any legal effect under Article 5(2) of the Berne Convention (1971). Article 5(2) applies both to the enjoyment and "exercise" of rights so that a content review that affects the exercise of rights would still impose a "formality" within the meaning of that provision.<sup>148</sup>

7.148 China further submits that the type of "formality" referred to in Article 5(2) of the Berne Convention (1971) is a condition precedent to the vesting of copyright. Given that Article 4(1) of the Copyright Law does not function as a condition precedent to copyright but rather as a condition subsequent, it is consistent with Article 5(2) of the Berne Convention (1971).<sup>149</sup>

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<sup>144</sup> United States' first written submission, para. 207; rebuttal submission, paras 221-222; acknowledged by China in its first written submission, para. 255.

<sup>145</sup> United States' first written submission, paras 220-221.

<sup>146</sup> China's first written submission, para. 235.

<sup>147</sup> China's response to Question No. 44.

<sup>148</sup> United States' rebuttal submission, paras 211-214.

<sup>149</sup> China's rebuttal submission, paras 261-264.

(b) Main arguments of third parties

7.149 Australia considers that Article 5(2) of the Berne Convention (1971) prohibits the enjoyment and exercise of rights in a protected work being subject to any prior legal or administrative procedure, such as registration of the work or approval of its content.<sup>150</sup>

7.150 Brazil does not consider that Article 5(2) of the Berne Convention (1971) requires that copyright arise "automatically" or "immediately" independently of what national legislation may dispose. The principle of automatic protection should be understood and limited to the fact that copyright protection is not conditional upon compliance with any formality, such as registration, deposit and the like.<sup>151</sup>

7.151 Canada considers that the term "formality" extends to national laws that make copyright protection for foreign works contingent on compliance with administrative obligations. China seems to have laid down in its national laws the administrative obligation for exporters or importers to obtain approval to publish and distribute the work in China such that, if not fulfilled, it will lead to the loss of copyright or copyright-related protection.<sup>152</sup>

7.152 The European Communities considers that if the enjoyment and exercise of copyright were contingent upon the dissemination approval by Chinese censorship authorities, this would be a "formality" inconsistent with Article 5(2) of the Berne Convention (1971). The European Communities does not comment upon the factual question of whether such a nexus exists under Chinese law but would be reticent to give specific instances of administrative enforcement too much weight in the assessment of an "as such" claim that appears to be based on the plain wording of the Chinese law.<sup>153</sup>

(c) Consideration by the Panel

7.153 The Panel notes that this claim concerns the denial of copyright protection under Article 4(1) of the Copyright Law. The Panel has already ruled on that issue in its consideration of the claim under Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement. Additional findings regarding this claim under Article 5(2) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement, would not contribute further to a positive solution to this dispute. Therefore, it is unnecessary for the Panel to rule on this claim.

## 5. Submission regarding Article 14 of the TRIPS Agreement

(a) Description of relevant provisions of the Copyright Law

7.154 Article 4 of the Copyright Law uses the term "works". Article 3 provides an inclusive definition of "works" for the purposes of the Copyright Law that does not expressly mention performances or phonograms (sound recordings). Meanwhile, Chapter IV of the Copyright Law sets out provisions regarding publication, performance, sound recording, video recording and broadcasting.

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<sup>150</sup> Australia's third party written submission, para. 34.

<sup>151</sup> Brazil's third party oral statement, paras 3-11.

<sup>152</sup> Canada's third party written submission, para. 24.

<sup>153</sup> European Communities' third party oral statement paras 22-24.

(b) Main arguments of the parties

7.155 The United States submitted to the Panel that "[d]epending on the construction given to Article 4, its first sentence *may* also be inconsistent with China's obligations under Article 14 of the TRIPS Agreement"; that "[i]t is unclear whether Article 4 of the Copyright Law operates to deny the protection of the Law to performances (or their fixations) and sound recordings whose publication or distribution is prohibited"; that "*it is not certain* that Article 4 is meant to be limited to "works" that are the subject matter of copyright, as opposed to encompassing as well the subject matter of related rights (such as performances and sound recordings)"; and that "*if* Article 4 of the Copyright Law does deny protection" of certain related rights *then* in those cases performers and producers will not have certain rights required by Article 14.1 and 14.2 of the TRIPS Agreement.<sup>154</sup> (emphasis added in each instance)

7.156 The United States concludes "[t]herefore, to the extent that Article 4 of the Copyright Law is interpreted as applying to performances (or their fixations) and to sound recordings, it is also inconsistent with China's obligations under Article 14 of the TRIPS Agreement."<sup>155</sup>

7.157 China responds that the United States has failed to properly state a justiciable claim on this issue. It argues that the US first written submission fails to allege that Article 4 of the Copyright Law actually violates Article 14 of the TRIPS Agreement, and that the United States fails to make a prima facie case that it does.<sup>156</sup>

(c) Main arguments of third parties

7.158 Canada submits that China's Copyright Law is inconsistent with Article 14.1 and 14.2 of TRIPS for the same reasons that it alleges the Law is inconsistent with Article 9.1 of the TRIPS Agreement.<sup>157</sup>

(d) Consideration by the Panel

7.159 The Panel has carefully reviewed the United States' request for establishment of a panel and its submissions. The Panel observes that at no point has the United States actually asserted that Article 4 of China's Copyright Law, in fact, applies to performances and phonograms or sound recordings and is, in fact, inconsistent with Article 14 of the TRIPS Agreement. Therefore, the Panel cannot discern a claim on which it may rule.

7.160 In any event, the Panel's findings with respect to Article 4(1) of the Copyright Law under the claim under Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement, would appear to dispose of the United States' underlying concern as regards Article 14 of the TRIPS Agreement.

## 6. Claim under Article 41.1 of the TRIPS Agreement

(a) Main arguments of the parties

7.161 The United States claims that the enforcement provisions of Chapter V of China's Copyright Law are unavailable with respect to works denied copyright protection under Article 4 of that Law.

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<sup>154</sup> United States' first written submission, paras 227, 228 and 230; see also rebuttal submission, fn. 201.

<sup>155</sup> United States' first written submission, para. 231.

<sup>156</sup> China's first written submission, paras 282 and 290.

<sup>157</sup> Canada's third party written submission, para. 25.

Therefore, China fails to ensure that enforcement procedures as specified in Part III of the TRIPS Agreement are available under its law, as required by Article 41.1 of the TRIPS Agreement.<sup>158</sup>

7.162 China responds that this claim fails in light of the fact that copyright is not in fact denied under the Copyright Law as alleged by the United States, for the reasons set out above in relation to Article 5(1) of the Berne Convention (1971).<sup>159</sup>

7.163 The United States notes China's defence – that Article 4(1) of the Copyright Law only denies "copyright protection" not "copyright" – and argues that, therefore, authors of the works for which copyright protection is denied do not benefit from the enforcement remedies specified in Chapter V of the Copyright Law.<sup>160</sup>

7.164 China submits that Article 41.1 of the TRIPS Agreement only requires enforcement procedures to be provided for rights covered by the TRIPS Agreement. If a right is not covered by the Agreement, then there is no obligation to enforce it. China also submits that the standard for enforcement procedures is that they permit "effective action". Given that China prohibits publication of the content at issue entirely, and rigorously enforces that prohibition, it has provided a procedure for "effective action" against any attempt to publish that content.<sup>161</sup> Lastly, China submits that its copyright enforcement procedures are "available", in the sense in which that term was interpreted in *US – Section 211 Appropriations Act*, because the author of any work may go to court and seek remedies, regardless of what judgement a court eventually reaches.<sup>162</sup>

(b) Main arguments of third parties

7.165 Canada submits that as a result of Article 4 of the Copyright Law, that Law does not apply to works that have been banned from publication or distribution in China and that, as a result, none of the required enforcement procedures is applicable. Therefore, Article 4 of the Copyright Law is also inconsistent with Article 41.1 of the TRIPS Agreement.<sup>163</sup>

(c) Consideration by the Panel

7.166 The Panel observes that Chapter V of the Copyright Law, titled "Legal Liabilities and Enforcement Measures", includes Articles 46 and 47. Article 46 provides for civil liability for 11 types of acts of infringement, many of which correspond to the rights set out in Article 10. Article 47 provides for civil and administrative liability and investigation of criminal liability for eight specific types of action, many of which correspond to rights set out in Article 10.

7.167 It is undisputed that Chapter V of the Copyright Law provides for enforcement procedures against acts of infringement of copyright, including orders to cease infringement, to pay compensation for damages and to confiscate the products of infringement, and provisional measures to order discontinuation of the infringement and to preserve property.

7.168 The Panel recalls its conclusion at paragraph 7.139 above that the Copyright Law, specifically the first sentence of Article 4, is inconsistent with China's obligations (with respect to the rights specially granted by the Berne Convention) under Article 5(1) of that Convention, as incorporated by Article 9.1 of the TRIPS Agreement. In the absence of protection of the rights specially granted by

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<sup>158</sup> United States' first written submission, paras 232-237.

<sup>159</sup> China's first written submission, para. 283.

<sup>160</sup> United States' rebuttal submission, paras 216-218.

<sup>161</sup> China's rebuttal submission, paras 309-311.

<sup>162</sup> China's response to Question No. 94.

<sup>163</sup> Canada's third party written submission, para. 26.

the Berne Convention, there can be no enforcement procedures against any act of infringement of such rights with respect to the relevant works.

7.169 The Panel recalls that, in reaching that conclusion, it dismissed China's argument that Article 4(1) of the Copyright Law does not remove copyright but only "the particularized rights of private copyright enforcement".<sup>164</sup> However, the Panel will accept that argument *arguendo* for the purposes of the claim under Article 41.1 of the TRIPS Agreement.

7.170 Article 41.1 of the TRIPS Agreement provides as follows:

"1. Members shall ensure that enforcement procedures as specified in this Part are available under their law so as to permit effective action against any act of infringement of intellectual property rights covered by this Agreement, including expeditious remedies to prevent infringements and remedies which constitute a deterrent to further infringements. These procedures shall be applied in such a manner as to avoid the creation of barriers to legitimate trade and to provide for safeguards against their abuse."

7.171 This claim is made under the first sentence of Article 41.1. This raises certain interpretative issues. The first concerns the scope of application of this sentence, as expressed by the phrase "any act of infringement of intellectual property rights covered by this Agreement".

7.172 The term "intellectual property" is defined in Article 1.2 of the TRIPS Agreement as follows:

"For the purposes of this Agreement, the term 'intellectual property' refers to all categories of intellectual property that are the subject of Sections 1 through 7 of Part II."

7.173 The subject of Section 1 of Part II is "Copyright and Related Rights". Within Section 1, Article 9.1 incorporates Articles 1 through 21 of the Berne Convention (1971) and the Appendix thereto, with the exception of rights conferred under, or derived from, Article *6bis*. Those provisions provide for the grant of various rights to authors in respect of their literary and artistic works. Any act falling within the scope of those rights carried out with respect to protected works without the authorization of the right holder or outside the scope of an applicable exception is *a priori* an act of infringement. Accordingly, an act of infringement of copyright in a literary or artistic work, as provided for in those provisions of the Berne Convention (1971) that are incorporated by Article 9.1 of the TRIPS Agreement, is an "act of infringement of intellectual property rights covered by this Agreement" within the meaning of the first sentence of Article 41.1 of the TRIPS Agreement.<sup>165</sup>

7.174 China acknowledges that a right holder of a work denied copyright protection under Article 4(1) of the Copyright Law is denied "the particularized rights of private copyright enforcement".<sup>166</sup> China has explained Article 4(1) in the following terms:

"Its core principle is that the Copyright Law shall not enforce the protections of the copyright law for works the contents of which are illegal."<sup>167</sup>

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<sup>164</sup> China's response to Question No. 44, discussed at paras 7.61 to 7.71 above.

<sup>165</sup> The Panel's approach does not imply any view as to whether the phrase "any act of infringement of intellectual property rights covered by this Agreement" refers only to acts of infringement of the exclusive rights provided for in the TRIPS Agreement.

<sup>166</sup> See note 164 above.

<sup>167</sup> China's response to Question No. 45.

7.175 In the Panel's view, this is an acknowledgement that, despite the alleged existence of "copyright" under Article 2 of the Copyright Law, there are no enforcement procedures against any act of infringement of copyright in the relevant works, as required by Article 41.1 of the TRIPS Agreement.

7.176 China contested that the rights denied by Article 4(1) of the Copyright Law were "covered by [the TRIPS] Agreement". This defence stems from China's view that it is entitled, under Article 17 of the Berne Convention (1971), to deny the rights provided for in Article 5(1) of that Convention. The Panel recalls its findings at paragraphs 7.122 to 7.139 above in which it rejected that view. Accordingly, that view provides no defence to the claim that the rights denied by Article 4(1) of the Copyright Law include protection against "act[s] of infringement of intellectual property rights covered by [the TRIPS] Agreement", within the meaning of the first sentence of Article 41.1 of the TRIPS Agreement either.

7.177 The second issue concerns the nature of the obligation to ensure that "enforcement procedures as specified in this Part are available under their law so as to permit effective action". Article 41 is found in Part III of the TRIPS Agreement. Therefore, the reference to the enforcement procedures as specified in "this Part" is a reference to the enforcement procedures as specified in Part III of the TRIPS Agreement.

7.178 China asserts that the enforcement procedures in Chapter V of the Copyright Law are "available" in the sense that the authors of all works have "access" to enforcement process irrespective of whether they have adequate evidence or a valid right to enforce.<sup>168</sup> The Panel observes that this argument, in effect, asserts that a Member may make available the enforcement procedures as specified in Part III of the TRIPS Agreement simply by not preventing right holders from filing and pursuing claims in vain.

7.179 The Panel notes that, whilst right holders whose works are denied protection under Article 4(1) of the Copyright Law may or may not have access to process, the enforcement procedures "as specified in [Part III]" of the TRIPS Agreement are far more extensive. This is clear, among other things, from the text of Article 41.1 of the TRIPS Agreement which specifies that these procedures include "remedies". For example, Articles 44, 45, 46 and 50 of the TRIPS Agreement specify that the judicial authorities shall have the authority to make certain orders, such as injunctions, orders to pay damages, orders for the disposal or destruction of infringing goods, and provisional measures. Where copyright protection is denied to a work under Article 4(1) of the Copyright Law, the judicial authorities have no such authority under Chapter V of the Copyright Law. It is not asserted that they are available in China under any other law.<sup>169</sup> Therefore, this set of enforcement procedures, including remedies, is not available to the right holders as required by Article 41.1 of the TRIPS Agreement.

7.180 China asserts that an entire ban on publication of a work is a form of "effective action" and that "it is in a sense an alternative form of enforcement against infringement".<sup>170</sup> The Panel notes that the range of exclusive rights recognized under the Berne Convention (1971) that may be infringed is broader than simply a right to authorize publication. In any event, the effectiveness of a government ban on publication is beside the point. Part III of the TRIPS Agreement includes a multilaterally-agreed minimum set of enforcement procedures that Members must make available to right holders against any infringement of intellectual property rights covered by the TRIPS Agreement. Where a Member chooses to make available other procedures – for enforcement of intellectual property rights

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<sup>168</sup> China's response to Question No. 94.

<sup>169</sup> China's response to Question No. 46 refers only to Articles 46 and 47 of the Copyright Law and Articles 217 and 218 of the Criminal Law.

<sup>170</sup> China's rebuttal submission, para. 311; responses to Questions Nos. 52 and 94.

or for enforcement of other policies with respect to certain subject matter – that policy choice does not diminish the Member's obligation under Article 41.1 of the TRIPS Agreement to ensure that enforcement procedures as specified in Part III are available.<sup>171</sup>

7.181 For the above reasons, the Panel concludes that the Copyright Law, specifically the first sentence of Article 4, is inconsistent with China's obligations under Article 41.1 of the TRIPS Agreement.

## **7. Claims under Article 61 of the TRIPS Agreement**

### **(a) Main arguments of the parties**

7.182 The United States claims that the criminal procedures referred to in Article 47 of China's Copyright Law are unavailable with respect to works denied copyright protection under Article 4 of that Law. Therefore, China does not provide for, or make available, criminal procedures and penalties to be applied in certain cases of wilful copyright piracy on a commercial scale, as required by the first and second sentences of Article 61 of the TRIPS Agreement.<sup>172</sup>

7.183 China responds that this claim fails in light of the fact that copyright is not in fact denied under the Copyright Law as alleged by the United States.<sup>173</sup>

### **(b) Main arguments of third parties**

7.184 Canada submits that Article 47 of China's Copyright Law provides for criminal procedures and penalties to be applied in certain case of copyright piracy. However, by operation of Article 4 of that Law, such criminal procedures and penalties do not apply to banned foreign works.<sup>174</sup>

### **(c) Consideration by the Panel**

7.185 The Panel notes that these claims concern the denial of copyright protection under Article 4(1) of the Copyright Law and its impact on enforcement. The Panel has already ruled on those issues in its consideration of the claims under Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement, and under Article 41.1 of the TRIPS Agreement, respectively. Additional findings regarding these claims under Article 61 of the TRIPS Agreement would not contribute further to a positive solution to this dispute. Therefore, it is unnecessary for the Panel to rule on these claims.

## **8. National treatment claims**

### **(a) List of relevant measures at issue**

7.186 Section III of the request for establishment of a panel lists the following other measures: the Criminal Law; the Regulations on the Administration of Publishing Industry; the Regulations on the Administration of Broadcasting; the Regulations on the Administration of Audiovisual Products; the Regulations on the Administration of Films; and the Regulations on the Administration of Telecommunication; the Regulations on Administration of the Films Industry; the Administrative Regulations on Audiovisual Products; the Administrative Regulation on Publishing; the Administrative Regulations on Electronic Publications; the Measures for the Administration of Import of Audio and Video Products; the Procedures for Examination and Approval for Publishing

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<sup>171</sup> China makes no reference to Article 41.5 of the TRIPS Agreement in relation to this claim.

<sup>172</sup> United States' first written submission, paras 232-233 and 238.

<sup>173</sup> China's first written submission, para. 283.

<sup>174</sup> Canada's third party written submission, para. 27.

Finished Electronic Publication Items Licensed by a Foreign Copyright Owner; the Procedures for Examination and Approval of Importation of Finished Electronic Publication Items by Electronic Publication Importation Entities; the Procedures for Recording of Imported Publications; the Interim Regulations on Internet Culture Administration; and the Several Opinions on the Development and Regulation of Network Music; as well as any amendments, related measures, or implementing measures.<sup>175</sup>

(b) Arguments of the parties

7.187 The United States claimed in its request for establishment of a panel that these measures appear to establish different pre-distribution and pre-authorization review processes for Chinese nationals' works, performances (or their fixations) and sound recordings than for foreign nationals' works, performances (or their fixations) and sound recordings. It claimed that these measures, taken together with Article 4 of the Copyright Law, appeared to result in earlier and otherwise more favourable protection and enforcement of copyright rights for Chinese authors' works than for foreign authors' works, inconsistently with China's obligations under Article 3.1 of the TRIPS Agreement and under Article 9.1 of the TRIPS Agreement with respect "at least" to Articles 5(1) and 5(2) of the Berne Convention (1971).<sup>176</sup> However, the United States has made no submission to the Panel with respect to these claims. The United States referred to four of the Regulations listed above in connection with its claim under Article 5(2) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement.

7.188 China submits that the United States has neglected to assert any claim whatsoever and thus has seemingly abandoned the national treatment arguments.<sup>177</sup>

7.189 The United States confirms that it is not pursuing a claim under Article 3.1 of the TRIPS Agreement before this Panel.<sup>178</sup>

(c) Consideration by the Panel

7.190 The Panel takes note that the United States has not pursued any national treatment claims in this dispute.

## 9. Conclusions with respect to the Copyright Law

7.191 The Panel recalls its conclusions at paragraphs 7.139 and 7.181 above that the Copyright Law, specifically the first sentence of Article 4, is inconsistent with China's obligations under:

- (a) Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement; and
- (b) Article 41.1 of the TRIPS Agreement.

7.192 The Panel exercises judicial economy with respect to the claim under Article 5(2) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement, and the claims under Article 61 of the TRIPS Agreement (with respect to the Copyright Law).

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<sup>175</sup> WT/DS362/7, attached as Annex D-1 to this report.

<sup>176</sup> *Ibid.*

<sup>177</sup> China's first written submission, para. 291.

<sup>178</sup> United States' rebuttal submission, fn. 201.

B. CUSTOMS MEASURES

1. Description of the measures at issue

7.193 This Section of the Panel's findings concerns three of China's Customs measures. The Regulations on Customs Protection of Intellectual Property Rights ("**Customs IPR Regulations**") were enacted by the Standing Committee of the State Council in November 2003 and entered into force in March 2004. The Regulations were formulated in accordance with the Customs Law and provide a procedure for Customs to take protective measures against goods suspected of infringing trademark, copyright and related rights and patent rights upon importation or exportation. Article 27 provides for the confiscation of goods determined to have infringed an intellectual property right and, in the third paragraph, sets out different options for the disposal or destruction of such goods. The parties agreed to translate the relevant text as follows:

"Where the confiscated goods which infringe on intellectual property rights can be used for the social public welfare undertakings, Customs shall hand such goods over to relevant public welfare bodies for the use in social public welfare undertakings. Where the holder of the intellectual property rights intends to buy them, Customs can assign them to the holder of the intellectual property rights with compensation. Where the confiscated goods infringing on intellectual property rights cannot be used for social public welfare undertakings and the holder of the intellectual property rights has no intention to buy them, Customs can, after eradicating the infringing features, auction them off according to law. Where the infringing features are impossible to eradicate, Customs shall destroy the goods."<sup>179</sup>

7.194 The Measures for the Implementation of the Customs IPR Regulations ("**Implementing Measures**") were adopted by the Standing Committee of the General Administration of Customs in April 2004 and entered into force in July 2004. The Implementing Measures were formulated in accordance with the Customs Law and other laws and administrative regulations for the purpose of effectively implementing the Customs IPR Regulations.<sup>180</sup> The parties agreed to translate Article 30 of the Implementing Measures as follows:

"Article 30 Customs shall dispose of infringing goods it has confiscated according to the following provisions:

(1). Where the goods concerned may be used directly for the social public welfare or the holder of the intellectual property rights wishes to purchase the goods, Customs shall<sup>181</sup> hand the goods over to the relevant social welfare bodies<sup>182</sup> for the use in social public welfare<sup>183</sup> or assign them to the holder of the intellectual property rights with compensation;

(2). Where the goods concerned cannot be disposed of in accordance with Item (1) but the infringing features can be eradicated, they shall<sup>184</sup> be auctioned off according to law after eradicating the infringing features. The proceeds arising from the auction shall be turned into the state treasury; and

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<sup>179</sup> Mutually agreed translation no. 6.

<sup>180</sup> Implementing Measures, Article 1.

<sup>181</sup> The original version does not say "shall" in item (1). See paragraph 7.339 below.

<sup>182</sup> In the original versions, the identical word has been translated as "social welfare bodies" in the Implementing Measures and as "public welfare bodies" in the Customs IPR Regulations.

<sup>183</sup> In the original versions, the identical word has been translated as "social public welfare" in the Implementing Measures and as "social public welfare undertakings" in the Customs IPR Regulations.

<sup>184</sup> The original version does not say "shall" in item (2). See paragraph 7.339 below.

(3). Where the goods concerned cannot be disposed of in accordance with Items (1) and (2), they shall be destroyed.

When Customs destroys the infringing goods, the holder of the intellectual property rights shall provide necessary assistance. In cases where relevant social welfare bodies use the infringing goods confiscated by Customs for the social public welfare, or the holder of the intellectual property rights assists Customs in destroying the infringing goods, Customs shall carry out necessary supervision."<sup>185</sup>

7.195 **Public Notice No. 16/2007** was notified by the General Administration of Customs in April 2007. Public Notice No. 16/2007 was notified in order *inter alia* to regulate the auction of infringing goods by Customs in accordance with Article 27 of the Customs IPR Regulations. The parties agreed to translate the operative paragraphs as follows:

"1. Where the confiscated infringing goods are auctioned by Customs, Customs shall completely eradicate all infringing features on the goods and the packaging thereof strictly pursuant to Article 27 of the Regulations, including eradicating the features infringing trademarks, copyright, patent and other intellectual property rights. Any goods the infringing features of which cannot be completely eradicated shall be destroyed and shall not be auctioned.

"2. Customs shall solicit comments from the holder of the intellectual property rights before the infringing goods are auctioned."<sup>186</sup>

7.196 It is not disputed that these three measures are all binding upon the General Administration of Customs.<sup>187</sup> These three measures are referred to collectively in this Report as "the Customs measures".

## 2. Claim under Article 59 of the TRIPS Agreement

### (a) Main arguments of the parties

7.197 The United States claims that the competent Chinese authorities lack the scope of authority to order the destruction or disposal of infringing goods required by Article 59 of the TRIPS Agreement. The measures at issue create a "compulsory scheme" so that the Chinese customs authorities cannot exercise their discretion to destroy the goods and must give priority to disposal options that allow infringing goods to enter the channels of commerce or otherwise cause harm to the right holder.<sup>188</sup> *Donation to social welfare bodies* can be harmful to a right holder and nothing appears to prevent such bodies from selling the infringing goods; *sale to the right holder* harms the right holder in the amount that the right holder pays for the infringing goods; and *auction* does not constitute disposal outside the channels of commerce and, absent his consent, may harm the right holder. Where any of these three options is available, the authorities are not authorized to order *destruction* of the infringing goods.<sup>189</sup>

7.198 China responds that its Customs authorities possess the authority to order both disposal and destruction of infringing goods in accordance with Article 59 of the TRIPS Agreement. *Donation to social welfare bodies* and *sale to the right holder* constitute disposal outside the channels of

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<sup>185</sup> Mutually agreed translation no. 7.

<sup>186</sup> Mutually agreed translation no. 8.

<sup>187</sup> United States' first written submission, paras 59-61 and responses to Questions Nos. 26 and 75; China's response to Question No. 26.

<sup>188</sup> United States' first written submission, paras 56-57 and 172.

<sup>189</sup> United States' first written submission, paras 179-192.

commerce in such a way as to avoid harm to the right holder.<sup>190</sup> Article 59 must be read in conjunction with Article 1.1 of the TRIPS Agreement.<sup>191</sup> Chinese law sets forth criteria that reflect an official preference for the use of disposition methods besides destruction but Customs has the discretion to determine whether the criteria are met and therefore which disposition method is appropriate. China Customs chose to destroy 58 per cent of the total value of infringing goods between 2005 and 2007 which proves that the putative hierarchy of disposition options does not hinder Customs' ability to order *destruction* of infringing goods.<sup>192</sup> The obligation in Article 59 to grant "authority" to order destruction does not mean that Members must make a grant of unfettered and unguided discretion and that domestic agencies must have the absolute power to order destruction of infringing goods in any circumstance whatsoever.<sup>193</sup>

7.199 The United States responds that Article 59 requires full authority to be granted to dispose of or destroy confiscated infringing goods in accordance with the principles of Article 46. The authorities should have the *power* to choose among any legitimate options for dealing with these goods from the outset when the goods are found to be infringing, and thereafter until the goods are finally dealt with.<sup>194</sup> Article 1.1 of the TRIPS Agreement only offers flexibility in how a Member implements TRIPS obligations and does not exempt a Member from full compliance with TRIPS obligations.<sup>195</sup> Statistics provide no response to this claim because the United States is not arguing that the TRIPS Agreement obligations *require* China to destroy or dispose of all infringing goods in accordance with the principles in the first sentence of Article 46. The pertinent issue is what decisions China Customs is permitted by law to make in particular circumstances.<sup>196</sup>

7.200 China responds that it does not have an obligation under the TRIPS Agreement to ensure that every infringing good disposed of outside the channels of commerce avoids harm to the right-holder. Rather, Customs must have the *authority* to dispose of seized goods outside the channels of commerce in such a way as to avoid harm to the right-holder.<sup>197</sup> The determination of what constitutes an appropriate grant of authority under the TRIPS Agreement is highly circumstantial. China Customs' authority is appropriate in light of the level of discretion that it enjoys in making decisions, its autonomy, that the rules constraining it serve legitimate government interests and the deterrence of infringement and the avoidance of harm to the right-holder.<sup>198</sup>

7.201 The United States claims that the measures at issue are inconsistent with the principle in the fourth sentence of Article 46 because nothing suggests that the auctioning of goods after removal of the infringing mark is permitted only in "exceptional cases".<sup>199</sup>

7.202 China responds that, even if the fourth sentence of Article 46 set forth an independent obligation on Customs authorities, which it does not admit, China Customs would fulfil the obligation because they remove "all" infringing features, not just the trademarks, and solicit comments from the right holders.<sup>200</sup> China argues that the use of the word "release" envisions a return to the infringer. Customs uses a reserve price at auction to ensure that infringers do not have the opportunity to purchase the seized goods at an unreasonably low cost and reattach counterfeit marks. In China's view, this complies with the purpose of the fourth sentence of Article 46, which is to ensure that in the

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<sup>190</sup> China's first written submission, para. 182.

<sup>191</sup> China's first written submission, para. 185.

<sup>192</sup> China's first written submission, para. 194.

<sup>193</sup> China's first written submission, para. 196.

<sup>194</sup> United States' rebuttal submission, para. 128; response to Question No. 38.

<sup>195</sup> United States' rebuttal submission, para. 129.

<sup>196</sup> United States' rebuttal submission, para. 131.

<sup>197</sup> China's rebuttal submission, para. 160.

<sup>198</sup> China's rebuttal submission, paras 181-188.

<sup>199</sup> United States' first written submission, para. 190; rebuttal submission, para. 169.

<sup>200</sup> China's first written submission, paras 222-225.

course of dealing with seized goods authorities deprive infringers of economic benefits from the goods.<sup>201</sup> China also argues that the word "sufficient" indicates that release of goods into the channels of commerce is permitted by the fourth sentence of Article 46, and not only in exceptional cases. It also raises the possibility that China's use of auction is "exceptional" as it constitutes a mere 2 per cent of disposition outcomes.<sup>202</sup>

(b) Main arguments of third parties

7.203 Argentina considers that customs authorities can freely select from a number of alternatives the most viable method for the situation at issue. Officials could discretionally choose either to destroy confiscated merchandise or to dispose of it outside the channels of commerce in a manner harmless to the right holder's interests. Donation to social welfare organizations is a viable alternative but avoidance of harm to the right holder would need to be determined by customs authorities on a case-by-case basis.<sup>203</sup>

7.204 Australia considers that "the channels of commerce" comprise any activity relating to the supply or transfer of goods in pursuit of financial reward within a Member's territory. Article 59 requires, in effect, that competent authorities be able to order that infringing goods be destroyed or be disposed of in such a manner that the goods do not enter the channels of commerce within that Member's territory. Such disposal methods could include recycling or donation to a charity within a Member's territory, provided the infringing goods are not likely to enter the channels of commerce as a result.<sup>204</sup>

7.205 Brazil considers that the fourth sentence of Article 46 suggests that the release of infringing goods into the channels of commerce is admitted by the TRIPS Agreement. The obligation is to grant the power to dispose of infringing goods outside the channels of commerce or order their destruction. The authority to employ one disposal option or another does not need to be unconditional but it should not be simply theoretical. Article 46 does not require Members to ensure that absolutely no harm ever happens to the right holder following disposal of infringing goods, rather, the obligation is to *avoid*, which is not an obligation of result but one of means.<sup>205</sup>

7.206 Brazil considers that the limitation set forth in the fourth sentence of Article 46 applies to disposal of infringing goods into the channels of commerce. An *a contrario* reading indicates that goods other than counterfeit trademark goods may be released into the channels of commerce, and counterfeit trademark goods may be released into the channels of commerce when additional measures are adopted besides the simple removal of the trademark.<sup>206</sup>

7.207 Canada submits that Article 59 of the TRIPS Agreement requires Members to give their competent authorities the powers set out in Article 46 *ab initio*, that is, as soon as it is has been established that the goods infringe intellectual property rights. China's competent authority acquires the requisite powers only after other disposal options have been explored or, in some cases, not at all. Obvious ways to dispose of goods outside the channels of commerce without harming the right holder are to give them to the right holder or to recycle them. Donation to social welfare bodies precludes destruction and the social welfare bodies may sell the infringing goods. The right holder has a choice of purchasing the infringing goods, thereby suffering financial harm, or running the risk that the goods

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<sup>201</sup> China's first oral statement, paras 72-77; rebuttal submission, paras 210-215.

<sup>202</sup> China's rebuttal submission, paras 206-209 and fn. 161.

<sup>203</sup> Argentina's third party written submission, paras 50 and 70.

<sup>204</sup> Australia's third party written submission, paras 26-32.

<sup>205</sup> Brazil's third party written submission, paras 43-52.

<sup>206</sup> Brazil's third party written submission, paras 45 and 52.

will be auctioned. The competent authorities only then acquire the power to destroy the goods when the infringing feature can not easily be removed or nobody has purchased them at auction.<sup>207</sup>

7.208 Canada submits that China's measures are inconsistent with Article 59 for an additional reason. The obligation to dispose of infringing goods in accordance with the principles of Article 46 includes complying with the prohibition on releasing counterfeit goods after simply removing the infringing features. China's customs authority does not auction counterfeit trademark goods from which it has removed infringing features "in exceptional cases" only.<sup>208</sup>

7.209 The European Communities agrees with China that Articles 59 and 46 of the TRIPS Agreement do not impose an obligation to dispose of infringing goods only through the two options set out in Article 46, first sentence. The terms of both Article 59 and Article 46 require that "authorities shall have *the authority* to order" remedies, not that they *must use* these remedies under specified circumstances. However, if customs authorities choose a different way of disposing of infringing goods, for example by auction, the principle of Article 46, fourth sentence applies. With respect to disposal outside the channels of commerce, this must be in such a manner as to avoid *any* harm caused to the right holder.<sup>209</sup> This means that even a slight degree of harm is too much. A core interpretation question is the extent to which the obligation in Article 59 permits Members to subject the "authority" to order disposal or destruction to conditions.<sup>210</sup>

7.210 The European Communities disagrees with China that the fourth sentence of Article 46 is not incorporated into Article 59. Article 59 refers to "the principles set out in Article 46" in their entirety. The second sentence of Article 59 is not a *lex specialis* derogating from the general provision in the fourth sentence of Article 46 as the two provisions address different ways of dealing with counterfeit trademark goods that are all relevant for customs authorities.<sup>211</sup>

7.211 Chinese Taipei submits that a Member should be considered to have met the minimum standard of Article 46 of the TRIPS Agreement if its judicial authority is provided with power and authority that includes both destruction and disposal according to the conditions set out in that Article. A Member is free to determine for itself the circumstances under which infringing goods are to be disposed of or destroyed and the sequence or priority between the two options.<sup>212</sup>

(c) Consideration by the Panel

(i) *Introduction*

7.212 The Panel notes that this claim challenges the Customs measures "as such". The parties disagree on the proper interpretation of the measures at issue. The Panel is therefore obliged, in accordance with its mandate, to make an objective assessment of the meaning of the relevant provisions of those measures. The Panel recalls its observations at paragraph 7.28 above and confirms that it examines the Customs measures solely for the purpose of determining their conformity with China's obligations under the TRIPS Agreement.

(ii) *Border measures*

7.213 This claim is made under Article 59 of the TRIPS Agreement, which provides as follows:

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<sup>207</sup> Canada's third party written submission, paras 14-19; third party oral statement, paras 10-14.

<sup>208</sup> Canada's third party written submission, paras 20-21.

<sup>209</sup> European Communities' third party written submission, paras 16-20.

<sup>210</sup> European Communities' third party oral statement, paras 15-20.

<sup>211</sup> European Communities' third party written submission, paras 17 and 19.

<sup>212</sup> Chinese Taipei's third party written submission, paras 22-29; oral statement, paras 13-17.

*"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."

7.214 This Article contains a number of key terms, such as "the right holder", "the defendant", "competent authorities" and "infringing goods" which are not defined in the Article itself but can only be understood by reading the whole Article in context.

7.215 Article 59 is found in Section 4 of Part III of the TRIPS Agreement on Special Requirements Related to Border Measures. Section 4 sets out procedures for the suspension at the border by the customs authorities of the release into free circulation of goods. Article 59 sets out the step in these procedures that applies after goods have been found to be infringing. As such, Article 59 forms part of a set of procedures and its key terms must be understood in that context.

7.216 This reading is confirmed by the opening provision of Section 4. The first sentence of Article 51 provides as follows:

"Members shall, in conformity with the provisions set out below, adopt procedures to enable a right holder, who has valid grounds for suspecting that the importation of counterfeit trademark or pirated copyright goods may take place, to lodge an application in writing with competent authorities, administrative or judicial, for the suspension by the customs authorities of the release into free circulation of such goods." (footnotes omitted)

7.217 This sentence refers to "procedures to enable a right holder ... to lodge an application ... for the suspension by the customs authorities of the release into free circulation" of certain goods. These procedures must conform with "the provisions set out below". The "provisions set out below" are the provisions of Section 4, which include Article 59.

7.218 The description of the procedure as one for an "application" for "suspension" does not appear to exclude related aspects of the procedure in the provisions set out below, such as the provisions on *ex officio* action in Article 58 or the remedies as a result of application and/or suspension set out in Article 59. Rather, the procedures in Section 4 form a set that must be read together. This is reflected in the second sentence of Article 51 (with respect to other goods, set out below) that refers to "such an application" (i.e. an application such as that referred to in the first sentence) being subject to "the requirements of this Section". This tends to confirm that the "provisions set out below" Article 51 include the whole of Section 4.

7.219 The need to read provisions in the context of the relevant Section is a feature of Sections 2, 3 and 4 of Part III of the TRIPS Agreement. Whilst some provisions refer expressly to prior provisions, such as Articles 52, 54 and 56, many others do not, such as Articles 53.1, 55, 57 and 59, but rather rely on context for clarity. This confirms that the provisions of Section 4 must be read as a coherent set of procedures and not in isolation.

7.220 Therefore, the Panel will refer to other provisions of Section 4, in particular to Article 51, in its interpretation of certain terms used in Article 59.

(iii) *"infringing goods"*

7.221 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 at paragraphs 7.213 to 7.220 above.

7.222 Article 51 expressly allows Members to provide for procedures at the border for other infringing goods as well. The second and third sentences of Article 51 provide as follows:

"Members may enable such an application to be made in respect of goods which involve other infringements of intellectual property rights, provided that the requirements of this Section are met. Members may also provide for corresponding procedures concerning the suspension by the customs authorities of the release of infringing goods destined for exportation from their territories."

7.223 Both these sentences use the word "may", indicating that they are optional provisions. 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>213</sup> The 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.

7.224 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>214</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>215</sup>

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<sup>213</sup> 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.

<sup>214</sup> 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>215</sup> 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.

7.225 Turning to the measures at issue, the Panel notes that the Customs IPR Regulations, in Article 2, provide that "Customs protection of intellectual property rights in these Regulations means the protection provided by the Customs for the exclusive rights to use a *trademark, copyrights and their related rights, and patent rights* (hereinafter referred to as intellectual property rights) ..." (emphasis added). The same is true of the Implementing Measures and Public Notice No. 16/2007, that both implement the Customs IPR Regulations.<sup>216</sup>

7.226 It is apparent that the intellectual property right infringements covered by the Customs measures include not only counterfeit trademark goods and pirated copyright goods, but certain other infringements of intellectual property rights, namely other trademark-infringing goods, other copyright-infringing goods, and patent-infringing goods. For the reasons set out in paragraph 7.223 above, the Panel finds that Article 59 applies to the Customs measures as those measures apply to all these infringements of intellectual property rights.<sup>217</sup>

7.227 The Panel notes that the Customs IPR Regulations, in Article 2, also provide that "Customs protection of intellectual property rights in these Regulations means the protection provided by the Customs ... related to *imports or exports* ..." (emphasis added). The same is true of the Implementing Measures and Public Notice No. 16/2007, that both implement the Customs IPR Regulations.<sup>218</sup>

7.228 In this respect, China's border measures provide a level of protection *higher* than the minimum standard required by Section 4 of Part III of the TRIPS Agreement. The practical effect of this is that, according to uncontested statistics prepared by China Customs, 99.85 per cent by value of infringing goods disposed of or destroyed under the measures at issue in the years 2005 to 2007 were destined for exportation.<sup>219</sup>

7.229 The United States' claim refers to "infringing goods"<sup>220</sup> and specifically notes that the measures at issue apply to imports and exports.<sup>221</sup> However, in response to a question from the Panel concerning its claim and the relevance of Article 51, the United States advised that it "takes no position" with regard to whether the first sentence of Article 59 also governs border authorities' actions with respect to goods destined for exportation.<sup>222</sup>

7.230 In light of the United States' response, and given the complainant's responsibility to assert and prove its claim, China submits that its measures are not subject to this claim with respect to goods destined for exportation.<sup>223</sup>

7.231 The Panel notes that the United States has not withdrawn its claim with respect to any aspect of the Customs measures. For the reasons set out in paragraph 7.224 above, the Panel concludes that

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<sup>216</sup> See paragraphs 7.194 and 7.195 above.

<sup>217</sup> This finding only applies with regard to imports, in accordance with paragraph 7.231 below.

<sup>218</sup> These measures implement the Customs IPR Regulations. Further, in the Implementing Measures, Article 4 refers to the intellectual property rights of imports and exports, Chapter III on "Detention upon application" begins with Article 14 that refers to goods to be imported or exported imminently, Chapter IV on "Investigation by authority" begins with Article 20 that refers to discovery of any imports or exports by Customs and is followed by Chapter V on disposal of goods and expenses which begins with Article 30 that refers to infringing goods that Customs has confiscated. Public Notice No. 16/2007 was notified to regulate the auction of goods in accordance with Article 27 of the Customs IPR Regulations that applies to both imports and exports.

<sup>219</sup> See "Statistics on Disposition of Infringing Goods by China Customs In Years 2005 through 2007 prepared by China Customs" in Exhibits CHN-166 and CHN-167.

<sup>220</sup> United States' first written submission, para. 171, 2<sup>nd</sup> sentence, refers to imports "in particular".

<sup>221</sup> United States' first written submission, para. 58, fn. 45; para. 179, fn. 117.

<sup>222</sup> United States' response to Question No. 28.

<sup>223</sup> China's second oral statement, paras 46-47.

Article 59 of the TRIPS Agreement is not applicable to the Customs measures insofar as those measures apply to goods destined for exportation.

7.232 The Panel will continue to assess the claim insofar as it concerns goods destined for importation. Imports represented 0.15 per cent by value of the goods disposed of or destroyed under the measures at issue in the years 2005 to 2007. During that period, all confiscated infringing imports were either donated to the Red Cross Society of China (0.12%) or destroyed (0.02%).<sup>224</sup> The volume of infringing imports that was sold to the right holder, or auctioned, was zero.

7.233 Nevertheless, the Customs measures on their face apply in the same way to both exports and imports. China confirms that its evidence, including of specific shipments of exports, is indicative of how the Customs measures operate with respect to both exports and imports.<sup>225</sup> The statistics comprising both exports and imports are a much larger, and therefore more reliable, sample. Therefore, the Panel considers that it may refer to evidence as it relates to both exports and imports in its assessment of this claim as it relates only to imports.

(iv) *"shall have the authority"*

7.234 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.

7.235 The United States confirms that it does not claim that the obligation that competent authorities "shall have the authority" to order certain remedies requires Members to make those orders. Rather, the United States claims that "[t]he pertinent issue is what decisions China Customs is permitted by law to make in particular circumstances".<sup>226</sup>

7.236 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>227</sup> The obligation is to "have" authority not an obligation to "exercise" authority.<sup>228</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>229</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

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<sup>224</sup> These figures do not total 0.15% due to rounding. See Customs Statistics in note 219 above.

<sup>225</sup> See provisions of the Customs IPR Regulations and Implementing Measures cited at para. 7.227 above, and China's confirmation of this point in its response to Question No. 30.

<sup>226</sup> United States' first oral statement, para. 55; rebuttal submission, para. 131.

<sup>227</sup> *New Shorter Oxford English Dictionary* (1993).

<sup>228</sup> This is without prejudice to other obligations regarding enforcement.

<sup>229</sup> 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.

make certain orders reflects *inter alia* that orders with respect to specific infringements are left to enforcement authorities' discretion.<sup>230</sup>

7.237 This is confirmed by the context. Article 41.1 of the TRIPS Agreement, quoted at paragraph 7.170 above, obliges Members to ensure that enforcement procedures as specified in Part III are "available" under their law so as to "permit" effective action against infringement, which addresses the potential for action.

7.238 Given the potential importance of this interpretation to the operation of much of Part III of the TRIPS Agreement, the Panel notes that it is further confirmed by the records of the negotiation of the Agreement.<sup>231</sup> Previous drafts of the TRIPS Agreement had provided that the authorities shall "provide for" certain remedies, but this phrasing was changed to read shall "have the authority", as were a number of other draft provisions.<sup>232</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.

7.239 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.<sup>233</sup>

7.240 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.

7.241 Given the potential importance of this interpretation to the operation of Part III of the TRIPS Agreement, the Panel notes that it is confirmed by the circumstances of conclusion of the Agreement.<sup>234</sup> One of the most important such circumstances was the fact that the pre-existing

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<sup>230</sup> 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>231</sup> The Panel has recourse to this supplementary means of interpretation in accordance with Article 32 of the Vienna Convention on the Law of Treaties ("Vienna Convention") in order to confirm the meaning resulting from the application of the general rule of interpretation in Article 31.

<sup>232</sup> See, for example, the Composite Draft Text of 12 July 1990, MTN.GNG/NG11/W/76.

<sup>233</sup> United States' rebuttal submission, para. 163; response to Question No. 37; China's first written submission, para. 213; response to Question No. 37; Brazil third party written submission, para. 51; European Communities' third party written submission, para. 18.

<sup>234</sup> The Panel has recourse to this supplementary means of interpretation in accordance with Article 32 of the Vienna Convention in order to confirm the interpretation resulting from application of the general rule of interpretation in Article 31. The Panel recalls the view of the Appellate Body in its report on *EC – Computer Equipment* (at para. 86), quoted in its report on *EC – Chicken Cuts* (at para. 284), referring to Sinclair, I., *The Vienna Convention on the Law of Treaties*, 2nd ed., (Manchester University Press, 1984) (at p. 141), that recourse to the circumstances of conclusion of a treaty "permits, in appropriate cases, the examination of the historical background against which the treaty was negotiated".

international intellectual property agreements contained comparatively few minimum standards on enforcement procedures beyond national treatment and certain optional provisions.<sup>235</sup> One of the major reasons for the conclusion of the TRIPS Agreement was the desire to set out a minimum set of procedures and remedies that judicial, border and other competent authorities must have available to them. This represented a major advance in intellectual property protection, as reflected in the second recital of the preamble to the Agreement as follows:

"*Recognizing*, to this end, the need for new rules and disciplines concerning:

(c) the provision of effective and appropriate means for the enforcement of trade-related intellectual property rights, taking into account differences in national legal systems"<sup>236</sup>

7.242 At the same time, the negotiators appear to have considered it unnecessary to state in either Article 46 or Article 59 that the authorities could not release goods that had been found infringing into the channels of commerce. This may have been due *inter alia* to the fact that such an action itself could constitute infringement or otherwise expose the authorities to liability. Such an action would not constitute infringement if the circumstances of disposal were non-commercial or if the state of the goods was altered so that the goods no longer infringed. The negotiators addressed both these issues: in the first sentence of Article 46, by providing for disposal outside the channels of commerce (and destruction) and, in the fourth sentence, in regard to counterfeit trademark goods, by setting a minimum degree of alteration of the state of goods before release into the channels of commerce.

7.243 The European Communities submitted that all authority to order remedies, including those not required by Article 59, is subject to an overarching requirement that it be "in such a manner as to avoid any harm caused to the right holder".<sup>237</sup> China addressed the degree to which auction, even though it does not satisfy the requirement that disposal be outside the channels of commerce, might still avoid any harm caused to the right holder.<sup>238</sup> The United States also addressed this issue.<sup>239</sup>

7.244 In the Panel's view, an interpretation that applies the phrase "in such a manner as to avoid any harm caused to the right holder" to all authority to order remedies is based on a selective reading of Article 46. The requirement that authority to order a remedy be "in such a manner as to avoid any harm caused to the right holder" is linked in the text of Article 46 to one remedy only, namely disposal outside the channels of commerce.<sup>240</sup> This does not exclude the possibility that other actions, notably release into the channels of commerce, may be subject to requirements, provided that those requirements are set out in the terms of Article 46 or Article 59.

7.245 The parties disagree 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

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<sup>235</sup> The Panel Report in *US – Section 211 Appropriations Act* noted that:

"The inclusion of this Part on enforcement in the TRIPS Agreement was one of the major accomplishments of the Uruguay Round negotiations as it expanded the scope of enforcement (...) of intellectual property rights. Prior to the TRIPS Agreement, provisions related to enforcement were limited to general obligations to provide legal remedies and seizure of infringing goods." (at para. 8.97)

<sup>236</sup> This language was agreed at the Uruguay Round Mid-Term Review meeting in April 1989 before the drafting of the TRIPS Agreement began: see document MTN.TNC/11, p. 14.

<sup>237</sup> European Communities' response to Third Party Question No. 16.

<sup>238</sup> China's first written submission, para. 214.

<sup>239</sup> United States' first written submission, para. 189; rebuttal submission, para. 161; response to Question No. 83.

<sup>240</sup> The European Communities appeared to acknowledge this initially in its third party written submission at para. 17.

availability of authority may be subject to conditions. China submits examples of other Members' legislation that, in its view, subject customs' authority to conditions.<sup>241</sup>

7.246 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.<sup>242</sup> 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).

7.247 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*.

7.248 The above observations do not imply that other types of conditions that do *not* find such a reflection in the text may not be attached to the required authority. However, the Panel does not consider it necessary, for the purposes of its examination of this claim, to consider what other conditions, if any, may be attached to "authority" consistently with Article 59. Therefore, other than the two conditions mentioned above, the Panel will accept *arguendo* that the availability of the "authority" required by Article 59 may not be subject to conditions in any given situation within the temporal scope of that Article, as described in paragraph 7.234 above.

7.249 The "authority" required by Article 59 concerns two types of remedies, namely "destruction or disposal". The meaning of "destruction" is not controversial. As for "disposal", the 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.<sup>243</sup> 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.<sup>244</sup> 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

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<sup>241</sup> China's first written submission, paras 198-200, referring to Exhibits CHN-102, CHN-106 to CHN-112.

<sup>242</sup> United States' response to Question No. 41; China in fact submits that the minimum standard permits reasonable conditions and sequencing or structuring authority "in a conditional and circumstantial manner": see its first written submission, paras 196 and 202.

<sup>243</sup> The ordinary meaning of "disposal" can be defined as "the action of disposing of or getting rid of; the action of settling or dealing with". "Dispose" in turn can be defined as "get rid of; deal conclusively with, settle": see the *New Shorter Oxford English Dictionary* (1993). This would include release to an importer or third parties, whether or not in exchange for payment.

<sup>244</sup> See the final clause of the WTO Agreement. According to Article 33(3) of the Vienna Convention, the terms of the Agreement are presumed to have the same meaning in each authentic text.

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 interpretation of the term "disposal" in the first sentence of Article 59 is disposal "outside the channels of commerce".

7.250 The Panel will refer to "destruction" and "disposal" collectively as "disposition methods" for ease of reference. It is not disputed that China's Customs measures provide the authority to order *destruction* of infringing goods in accordance with the principles set out in Article 46. However, the United States takes issue with what it considers the "highly limited circumstances" in which the Customs measures permit destruction.<sup>245</sup> China does not deny that its authority to order destruction is, in principle, subject to certain limitations but argues that China Customs has considerable discretion to decide whether such limitations apply. The statistics show that, in practice, over half of infringing goods seized by Customs in terms of value are in fact destroyed.<sup>246</sup>

7.251 The Panel recalls its finding at paragraph 7.246 above that China is permitted to limit the authority to order destruction of infringing goods provided that its competent authorities have the authority in such situations to order disposal of infringing goods in accordance with the principles set out in Article 46. The limitations on Customs' authority to order destruction of infringing goods are relevant to the claim only to the extent that they show that Customs has authority to order *neither* destruction of infringing goods *nor* disposal in accordance with those principles.

7.252 It is in this context that the United States claims that the measures establish a *mandatory* sequence of steps, as the authorities will not have either of the required forms of authority in a given situation if the measures at issue compel them to order another disposition method that is *not* required by Article 59.<sup>247</sup> This raises the so-called "mandatory/discretionary distinction" that has been discussed in a number of GATT and WTO Panel Reports relating to trade in goods.<sup>248</sup> 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. For that reason, the Panel will examine whether certain aspects of the Customs measures are mandatory.

7.253 The Panel also notes that authority to order a disposition method within the scope of Article 59 will often be discretionary, as the obligation that Members' competent authorities "shall have the authority" to make particular orders applies to what those authorities are *permitted* to order by domestic law. Accordingly, the obligation in Article 59 is applicable to both mandatory and discretionary measures and, in principle, both mandatory and discretionary measures "as such" can be examined for conformity with that obligation.<sup>249</sup>

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<sup>245</sup> United States' second oral statement, para. 59; response to Question No. 81.

<sup>246</sup> China's rebuttal submission, para. 154. See the statistics at paragraph 7.349 below.

<sup>247</sup> United States' rebuttal submission, para. 161; responses to Questions Nos. 39, 41, 80 and 83.

<sup>248</sup> See further paragraph 7.358 below.

<sup>249</sup> The Panel notes that its approach is consistent with the view of the Appellate Body in *US – Corrosion-Resistant Steel Sunset Review* (at para. 93) that "as with any such analytical tool, the import of the 'mandatory/discretionary distinction' may vary from case to case". The Panel also notes that the possibility of obligations which would render illegal even discretionary legislation was specifically envisaged in the Panel Report in *US – Section 301 Trade Act* (at para. 7.53) as follows:

"The question is then whether, on the correct interpretation of the specific WTO obligation at issue, only mandatory or also discretionary national laws are prohibited. We do not accept the legal logic that there has to be one fast and hard rule covering all domestic legislation. After all, is it so implausible that the framers of the WTO Agreement, in their wisdom, would have

7.254 The Customs measures at issue provide for three disposal options besides destruction. These are donation to social welfare bodies; sale to the right holder; and auction. The United States claims that *none* of these disposal options is in accordance with the principles set out in Article 46 and that all preclude authority to order destruction.<sup>250</sup> China responds that the first two of these disposal options constitute authority to order disposal in accordance with the principles set out in Article 46, and that the United States has not established that China Customs lacks authority to order destruction.<sup>251</sup> Therefore, the Panel will proceed as follows:

- (a) First, the Panel will determine what are "the principles set out in Article 46";
- (b) Second, the Panel will assess China Customs' authority to order donation to social welfare bodies and, if necessary, sale to the right holder, in order to determine whether they constitute authority to order disposal in accordance with the principles set out in the first sentence of Article 46; and
- (c) Third, the Panel will assess China Customs' authority to order auction of infringing goods (plus either of the first two disposal options that is found to be disposal not in accordance with the principles set out in the first sentence of Article 46) to determine whether such authority mandates a particular disposition method and thereby precludes authority to order destruction.

(v) *"the principles set out in Article 46"*

7.255 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.

7.256 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 for the reasons given at paragraph 7.249 above). 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.

7.257 Article 46 of the TRIPS Agreement provides as follows:

*"Other Remedies*

In order to create an effective deterrent to infringement, the judicial authorities 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. The judicial authorities shall also have the authority to order that materials and implements the predominant use of which has been in the creation of the infringing goods be, without compensation of any sort, disposed of outside the channels of commerce in such a manner as to minimize the risks of further infringements. In considering such

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crafted some obligations which would render illegal even discretionary legislation and crafted other obligations prohibiting only mandatory legislation?"

<sup>250</sup> United States' first written submission, paras 184, 189 and 191.

<sup>251</sup> China's rebuttal submission, paras 155, 156 and 171.

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. 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."

7.258 The first sentence of Article 46 refers to "authority" to order that "infringing goods" be "disposed of ... or ... destroyed". Therefore, it seems pertinent to Article 59.

7.259 The second sentence of Article 46 refers to disposal of materials and implements and is therefore inapposite. Indeed, materials and implements used to create infringing goods would not normally be suspended at the border with the infringing goods, unlike during enforcement actions within a Member's territory.

7.260 The third sentence of Article 46 refers to "such requests" although the previous sentences do not refer expressly to any requests. The content of the third sentence clearly relates to materials and implements as addressed in the second sentence but it could equally relate to infringing goods as addressed in the first sentence. The text is ambiguous on this point. This ambiguity can be resolved by reference to the records of the negotiation of the TRIPS Agreement.<sup>252</sup>

7.261 The TRIPS Agreement was negotiated during the Uruguay Round in the Negotiating Group on Trade-Related Aspects of Intellectual Property Rights, including Trade in Counterfeit Goods (referred to below as the "TRIPS negotiating group"). The Chairman's draft text of the Agreement of 23 July 1990 included a draft article corresponding to what is Article 46 in the text as finally agreed.<sup>253</sup> In that draft article, the principle of proportionality and the interests of third parties were related to a request of the right holder under the previous sentence. That request could be for remedies with respect to infringing goods as well as materials and implements. In a later draft<sup>254</sup>, the first sentence of the provision on remedies was divided into two separate sentences, one with respect to infringing goods and the other with respect to materials and implements. Both sentences included the phrase "upon request from the right holder". In the same draft, the phrase "[i]n considering such a request" was revised to read "[i]n considering such requests" (in the plural). This is the version of the third sentence that was retained in the so-called "Brussels Draft"<sup>255</sup> and the final text of Article 46 of the TRIPS Agreement.

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<sup>252</sup> The Panel has recourse to a supplementary means of interpretation in accordance with Article 32 of the Vienna Convention in order to determine the meaning when the interpretation according to the general rule of interpretation in Article 31 leaves the meaning ambiguous.

<sup>253</sup> That draft article read as follows:

"10. Other Remedies

10A Where an intellectual property right has been found to be infringed, the court shall have the authority to order, *upon request* of the right holder, that *the infringing goods, as well as materials and implements* the predominant use of which has been in the creation of the infringing goods, be, without compensation of any sort, destroyed or disposed of outside the channels of commerce in such a manner as to minimise any harm caused to the right holder. In considering *such a request*, 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. [In regard to counterfeit goods] [Other than in exceptional cases], the simple removal of the trade mark [or geographical indication] unlawfully affixed shall not be ordered." (emphasis added) See Part IV of document MTN.GNG/NG11/W/76.

<sup>254</sup> Chairman's revised draft text of 13 November 1990, document no. 2814.

<sup>255</sup> See draft Article 49 in document MTN.TNC/W/35/Rev.1 dated 3 December 1990 entitled "Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations – Revision".

7.262 Accordingly, the records of the negotiation of the TRIPS Agreement clarify that the terms of Article 46 in the third sentence refer *inter alia* to the consideration of requests for orders that infringing goods be disposed of outside the channels of commerce or destroyed. Therefore, the third sentence seems pertinent to Article 59 as well.

7.263 The fourth sentence refers to a category of infringing goods, i.e. counterfeit trademark goods. It does not refer expressly to authority to order destruction or disposal outside the channels of commerce. However, the context shows that the principle of proportionality in the previous sentence guides the competent authorities' choice between the remedies specified in the first sentence and any alternative remedies. Similarly, the fourth sentence of Article 46 sets out a consideration that the authorities must take into account when choosing between the required remedies, namely those specified in the first sentence, and release into the channels of commerce, if such an order is available. The fourth sentence attaches to the scope of authority to choose between destruction or disposal outside the channels of commerce and release into the channels of commerce, if that remedy is available. Therefore, the fourth sentence of Article 46 seems pertinent to Article 59.

7.264 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."<sup>256</sup> 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.

7.265 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.<sup>257</sup> 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.

7.266 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

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<sup>256</sup> *New Shorter Oxford English Dictionary* (1993).

<sup>257</sup> The Panel notes that the cross-reference from a draft article on remedies in Section 4 to the "principles" of a draft article on remedies in Section 2 was included in the earliest complete draft of the TRIPS Agreement, i.e. the Composite Draft Text of 12 June 1990 and can be traced to *inter alia* the EC draft text of May 1989 (MTN.GNG/NG11/W/68). The amount of duplication between the two provisions that the cross-reference avoided can be observed in the prior EC proposal (MTN.GNG/NG11/W/31): see note 261 below.

- (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",<sup>258</sup> or
- (c) authorities shall have the authority to order destruction "unless this would be contrary to existing constitutional requirements".

7.267 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".

7.268 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.<sup>259</sup>

7.269 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.

7.270 In the Panel's view, the above are the "principles set out in Article 46" incorporated by the first sentence of Article 59.

7.271 China disagrees, arguing, in effect, that 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.<sup>260</sup>

7.272 The Panel observes certain similarities in the respective texts of the fourth sentence of Article 46 and the second sentence of Article 59. The second sentence of Article 59 provides as follows:

"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."

7.273 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.

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<sup>258</sup> This principle is interpreted at paragraphs 7.278 to 7.285 below.

<sup>259</sup> This principle is interpreted at paragraphs 7.369 to 7.379 below.

<sup>260</sup> China first written submission, para. 222.

7.274 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 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.

7.275 There is no reason to infer that the risk of further infringement presented by counterfeit trademark goods was only intended to be addressed when the goods were re-exported or subject to another customs procedure and not when they were released at the border into the channels of commerce.<sup>261</sup> Counterfeit trademark goods suspended at the border and then released present a risk of further infringement whether the goods are released into the channels of commerce *within* a Member's territory, or transit through the Member's territory or are re-exported to another Member's territory, as under the second sentence of Article 59.

7.276 Indeed, read in context, the relevance of "release" of goods into the channels of commerce is even clearer in Article 59 than it is in Article 46. Section 4 concerns the suspension of "release" of goods to importers, and uses that word in Articles 51, 53.2, 54, 55, 56 and 58. In contrast, Article 46 is part of Section 2, on civil and administrative procedures and remedies, so the limited sense of "release" to an importer cannot apply. Read in context, a broader meaning, equivalent to release to any party in the channels of commerce, must apply when this word is used in relation to remedies.

7.277 For the above reasons, the Panel confirms its finding at paragraph 7.270 above as to the interpretation of "the principles set out in Article 46", as incorporated in Article 59.

(vi) *"outside the channels of commerce in such a manner as to avoid any harm caused to the right holder"*

7.278 The parties disagree 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 United States has raised concerns regarding 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.

7.279 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

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<sup>261</sup> The records of the TRIPS negotiations shows that similar language to the fourth sentence of Article 46 and the second sentence of Article 59 together with the cross-reference to the principles of another article were included in the earliest complete draft of the TRIPS Agreement, i.e. the Composite Draft Text of 12 June 1990. That Draft Text took this language from the EC, US and Swiss draft texts (MTN.GNG/NG11/W/68, W/70 and W/73). For the record, it can be observed that the prior EC proposal had duplicated language between the two provisions without a cross-reference. In that proposal, what is now the fourth sentence of Article 46 appeared in what is now Article 59, without the cross-reference or the second sentence (MTN.GNG/NG11/W/31). Without acknowledging its relevance to the interpretation of Article 59, the Panel notes that the negotiating record to which China itself referred shows that another participant in the negotiations envisaged application of "exceptional cases" in the border measures remedies provision to importation as well as reshipment, quoted in China's rebuttal submission, para. 211.

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".<sup>262</sup> 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.

7.280 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.

7.281 The principle is that the manner of disposal shall "avoid" harm. China argues that this is an obligation to "pay due regard to".<sup>263</sup> However, the Panel notes that the ordinary meaning of "avoid" can be defined as "keep off, prevent; obviate".<sup>264</sup> Further, the principle is that the manner shall avoid "any" harm caused to the right holder, not just "harm" or "some" harm.<sup>265</sup> Therefore, the manner of disposal must be designed in such a way as to prevent any harm occurring to the right holder.

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

7.283 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).

7.284 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

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<sup>262</sup> See note 243 above.

<sup>263</sup> China's first written submission, para. 186.

<sup>264</sup> *New Shorter Oxford English Dictionary* (1993).

<sup>265</sup> United States' rebuttal submission, para. 133.

requirement.<sup>266</sup> 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.

7.285 These observations are subject to the Panel's findings at paragraphs 7.239 to 7.240 above 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 by Article 59. The remedies specified in Article 59 are not exhaustive.

(vii) *Donation to social welfare bodies*

7.286 The Panel will now assess Customs' authority to order donation to social welfare bodies in order to determine whether it constitutes authority to order disposal of infringing goods in accordance with the principles set out in the first sentence of Article 46 of the TRIPS Agreement, specifically, whether it constitutes disposal "outside the channels of commerce in such a manner as to avoid any harm caused to the right holder".

7.287 The United States does not object to donation of goods to charity *per se*.<sup>267</sup> It accepts that donation with the right holder's consent may observe the principles of Article 46. The United States alleges that the measures do not provide any discretion to the Customs authorities to determine that transfer to a social welfare body is not appropriate in circumstances where the right holder would be harmed.<sup>268</sup>

– Defective goods

7.288 The United States argues that the donation of "shoddy counterfeit goods", if they fail to perform properly and especially if defective or dangerous, will damage the right holder's reputation or even expose it to claims for compensation.<sup>269</sup>

7.289 The Panel notes that the United States' argument is based on the legal structure of the measures, that allegedly allows defective goods to be donated.<sup>270</sup> The United States does not allege that any sub-standard, defective or dangerous goods have actually been donated by China Customs to social welfare bodies. In fact, apart from the text of the measures at issue, the United States submits only a US newspaper article titled "*China's New Concern: Exploding Phones*" reporting on an unrelated case of mobile phone batteries that had failed safety tests in China and were reportedly prone to explode under certain conditions.<sup>271</sup> The article reports statements by right holders that the batteries were counterfeit. There is no link in the story to Customs and no link to social welfare bodies. This alarming story is therefore irrelevant to the assessment of the claim as it adds nothing to the general point that goods can be dangerous.

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<sup>266</sup> United States' first written submission, para. 185 and response to Question No. 72, submitting that donation to charities with the right holder's consent was a manner of disposal that avoids any harm to the right holder.

<sup>267</sup> United States' response to Question No. 72.

<sup>268</sup> United States' first written submission, para. 187.

<sup>269</sup> United States' first written submission, para. 186.

<sup>270</sup> United States' first oral statement, para. 50.

<sup>271</sup> Exhibit US-45.

7.290 China responds that its Customs would never donate defective or dangerous goods.<sup>272</sup> Article 27 of the Customs IPR Regulations sets out a condition for donation, in that it provides for donation "[w]here the confiscated goods which infringe on intellectual property rights can be used for the social public welfare undertakings". Article 30 of the Implementing Measures restates the condition, providing for donation "[w]here the goods concerned may be used directly for the social public welfare".

7.291 The Panel sees no reason why defective or dangerous goods would satisfy this condition. Nothing else in the evidence suggests that Customs would donate defective or dangerous goods to charity. Therefore, the Panel finds that it has not been demonstrated that Customs lacks authority to donate goods to social welfare bodies in such a manner as to avoid any harm to the right holder caused by defective or dangerous goods.

7.292 China also referred to Article 6 of the Law on Donations for Public Welfare which provides as follows:

"Donation shall be made in compliance with laws and Regulations, and not in violation of social morality, nor to the detriment of public interests and the lawful rights and interests of other citizens."<sup>273</sup>

7.293 The Panel notes that this provision, on its face, refers to the "detriment of public interests" which could include the safety of persons who could potentially receive defective and dangerous goods from social welfare bodies where those goods were eligible for donation by Customs to those social welfare bodies. However, the Panel does not need to take a definitive view on this point as it has already found at paragraph 7.291 above that China has sufficiently substantiated its assertion on the basis of the provisions of the measures at issue.

– Harm to reputation

7.294 The United States submits that the above considerations do not address the situation of counterfeit and pirated goods that are usable but likely of lower quality. In its view, such goods could easily harm the right holder's reputation. Indeed, Article 6 of the Customs – Red Cross Memorandum (discussed at paragraphs 7.300 to 7.304 below) expressly foresees the possibility of handing over goods that have "quality problems".<sup>274</sup>

7.295 The Panel recalls its findings at paragraph 7.282 above 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, and that evidence of actual harm caused to the right holder by the manner of disposal could be relevant in assessing whether the manner of disposal conforms to this principle.

7.296 Under ordinary circumstances, consumers may be misled as to the origin of counterfeit and pirated goods, and counterfeit goods with quality problems may harm right holders' reputations. The Panel has taken due note that nothing in the measures at issue obliges Customs or the social welfare bodies to remove counterfeit trademarks. Whilst the evidence shows that, in one case, the Red Cross imprinted its seal on a batch of donated infringing clothes, apparently to prevent the goods being sold

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<sup>272</sup> China's first written submission, paras 162-163; response to Question No. 32.

<sup>273</sup> Mutually agreed translation no. 10. The Law on Donations for Public Welfare is, on its face, of general application (see Article 2) and therefore applicable to donations by Customs of infringing goods to social welfare bodies under the measures at issue.

<sup>274</sup> United States' rebuttal submission, para. 150.

after distribution<sup>275</sup>, it is not suggested that this was pursuant to an obligation or is in any other way relevant to the "authority" that Customs has to order disposal of goods.

7.297 However, goods donated by Customs to the Red Cross are not distributed in ordinary circumstances. The Red Cross distributes donated goods itself, outside the channels of commerce, including in disaster relief projects, where it cannot simply be assumed that the recipients are misled as to the origin of the goods.<sup>276</sup> The recipients do not choose the goods in the way that ordinary consumers do, nor can it be assumed that the recipients are potential consumers of the genuine goods. The purposes of the Red Cross and the circumstances in which it may use goods donated by Customs form part of the legal structure bearing on the "manner" of disposal of infringing goods by Customs. Nothing in the evidence suggests that any harm has ever been caused, or is likely to be caused, to right holders' reputations due to donation of infringing goods under the measures at issue. In fact, the evidence shows that two internationally famous right holders have actually participated in the distribution by the Red Cross of goods that infringed their rights<sup>277</sup>, suggesting that they do not presume donation of infringing goods harms their reputation. Therefore, the Panel finds that it has not been demonstrated that Customs lacks authority to donate goods to social welfare bodies in such a manner as to avoid any harm to the right holder caused by lower quality goods.

– Later sales of donated goods

7.298 The United States also alleges that "nothing appears to prevent [social welfare bodies] from selling the infringing goods they receive under the first "item" thus moving these goods back into commerce".<sup>278</sup>

7.299 China responds by reference to Article 30 of the Implementing Measures, which specifically provides in a final paragraph as follows:

"In cases where relevant social welfare bodies use the infringing goods confiscated by Customs for the social public welfare, or the holder of the intellectual property rights assists Customs in destroying the infringing goods, *Customs shall carry out necessary supervision.*"<sup>279</sup> (emphasis added)

7.300 China submits that this provision imposes on Customs a legal responsibility to ensure that donated goods are used exclusively for social welfare purposes.<sup>280</sup> By way of an example of Customs' implementation of its responsibility of supervision, China submits a Memorandum of Cooperation dated 13 May 2004 that the General Administration of Customs entered into with the Red Cross Society of China entitled "Memorandum of Cooperation on using confiscated infringing goods for social welfare" (the "Customs – Red Cross Memorandum").<sup>281</sup> This Memorandum was executed and entered into force shortly after the Implementing Measures were adopted but before they entered into force.<sup>282</sup>

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<sup>275</sup> Exhibit CHN-91.

<sup>276</sup> For example, the evidence shows goods being delivered in Red Cross packaging: Exhibit CHN-93.

<sup>277</sup> Exhibit CHN-91.

<sup>278</sup> United States' first written submission, para. 186.

<sup>279</sup> Mutually agreed translation no. 7. China also refers to Article 6 of the Law on Donations for Public Welfare, quoted at paragraph 7.292 above.

<sup>280</sup> China first written submission, para. 165.

<sup>281</sup> Exhibit CHN-92.

<sup>282</sup> The Standing Committee of the General Administration of Customs adopted the Implementing Measures on 22 April 2004. The Memorandum of Cooperation was executed by the General Administration of Customs and the Red Cross Society of China on 13 May 2004 and it came into force immediately: see Article 11. The Implementing Measures entered into force on 1 July 2004.

7.301 The Customs – Red Cross Memorandum recites the Customs IPR Regulations and other relevant laws and administrative regulations and sets up procedures regarding the use of confiscated infringing goods for social welfare.<sup>283</sup> It is, on its face, a legally binding agreement. Article 4 sets out the rights and obligations of Customs. Item (iv) provides that Customs must hand over the goods "free of charge". Hence, they are donations and not sales. Item (ii) obliges and entitles Customs to do the following:

"(ii) monitoring the whereabouts and the usages of Goods. Requiring [Red Cross] to correct any of its actions that are found in violation of the provisions of this Memorandum;"

7.302 Article 5 sets out the rights and obligations of the Red Cross and includes the following item:

"(iv) promptly notifying [Customs] of the distribution and the usage of the Goods upon the request of [Customs]."

7.303 Article 7 stipulates the use of goods donated to the Red Cross as follows:

"The Goods handed over to [the Red Cross] by [Customs] shall be restricted for use only for the living purposes of the person who receives relief. [The Red Cross] shall take effective measures to prevent goods from being used for other purposes or entering into the channels of commerce by any means."

7.304 The Panel observes that these terms, on their face, (a) require the Red Cross to restrict the use of infringing goods and take measures to prevent their sale; and (b) obliges Customs to monitor use and entitles Customs to require the Red Cross to correct any violation of the restriction on use or its duty to take measures to prevent their sale. These measures, on their face, show that Customs has a responsibility for the manner in which the goods are disposed of, and that it has provided that that manner avoids their return to the channels of commerce.

7.305 The United States argues that the preventive measures that the Red Cross must take under the Memorandum "do not in fact demonstrate that, under Chinese law, the goods *cannot* return to the channels of commerce"<sup>284</sup> (emphasis added). However, the Panel recalls that, in accordance with the relevant principles set out in Article 46, Customs must have the *authority* to order that the goods be disposed of outside the channels of commerce, and that 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 avoid any harm caused to the right holder.

7.306 China has provided evidence of cases of donation of infringing goods by Customs to the Red Cross Society. In one case, Customs donated infringing goods to the Red Cross that were allocated to people in areas struck by natural disasters such as typhoons, rainstorms and floods. The goods all infringed trademark rights and consisted of sport shoes, bags of rice noodles, washing powder, air-cooled chillers and kerosene heaters.<sup>285</sup> There is no evidence on the record that Customs has failed to discharge its responsibility to ensure that the use of such infringing goods is not circumvented and that goods do not find their way back into the channels of commerce.

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<sup>283</sup> The text of the Memorandum refers to "Party A" and "Party B", which are the General Administration of Customs and the Red Cross Society of China, respectively. The quotations from the Memorandum in this report refer to the parties by name for ease of reference.

<sup>284</sup> United States' rebuttal submission, para. 153.

<sup>285</sup> Exhibit CHN-93.

7.307 The Panel considers the Customs – Red Cross Memorandum particularly relevant to its assessment of Customs' authority to dispose of infringing goods by donation because the Red Cross Society of China is the recipient of the overwhelming majority of goods donated under the measures at issue. The statistics show that the Red Cross Society of China was the recipient of 91 per cent by value of the infringing goods donated by Customs in the years 2005 to 2007.<sup>286</sup> In fact, no infringing goods destined for importation have ever been donated to any social welfare body besides the Red Cross Society of China under the measures at issue during the period for which statistics are available.

7.308 The United States notes that other social welfare bodies are not *required* to enter into an agreement like the Customs – Red Cross Memorandum.<sup>287</sup> Donation of infringing goods to other social welfare bodies might not be in accordance with the principles set out in Article 46.

7.309 The Panel recalls its finding at paragraph 7.240 above that the remedies specified in Article 59 are not exhaustive. It has not been asserted that there are circumstances in which Customs can donate infringing goods to another social welfare body only and not to the Red Cross Society of China. In other words, authority to donate to another social welfare body does not preclude authority to donate to the Red Cross. Therefore, to the extent that Customs' authority to donate to the Red Cross Society of China conforms to the principles set out in Article 46, Customs has the authority to order disposal specified by Article 59. In any event, the possibility that other social welfare bodies might not have entered into a donation agreement, or that they might refuse to do so, is an issue to be demonstrated.

7.310 The United States argues that the Customs – Red Cross Memorandum does not demonstrate that Customs has the "authority" to order that goods be disposed of in such a manner because Customs must persuade a charitable organization both to enter into a donation agreement and to agree that it will not try to resell the goods.<sup>288</sup>

7.311 The Panel notes that Customs has already entered into the Memorandum with the Red Cross, and that Customs did so in the interval between the adoption and entry into force of the Implementing Measures. Customs does not need to persuade the Red Cross to agree any further to enter into such an agreement. Therefore, this does not disturb the Panel's finding at paragraph 7.309 above. In any event, the measures at issue show that if social welfare bodies refuse to accept donations, Customs can then consider other options which include, ultimately, destruction of the goods.

7.312 The Panel recalls that the United States' claim is that the three Customs measures at issue "provide no discretion" to Customs to determine that transfer to a social welfare body is not appropriate in circumstances where the right holder would be harmed and, hence, that Customs lacks authority to order disposal of infringing goods in accordance with the principles of Article 46.<sup>289</sup> On the evidence examined so far, the Panel's view is that the United States has not established that part of its claim, as the measures on their face show that: (a) Customs makes a determination as to whether infringing goods may be used for social public welfare; and (b) Customs has a duty to carry out necessary supervision of such use, which it executes by means of the Customs – Red Cross Memorandum.

7.313 The burden now shifts to the United States to show why, in light of this legal structure, the three Customs measures at issue "provide no discretion" to Customs to determine that transfer to a social welfare body is not appropriate in circumstances where the right holder would be harmed.

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<sup>286</sup> See Customs Statistics in note 219 above.

<sup>287</sup> United States' rebuttal submission, para. 152; see also second oral statement, para. 52.

<sup>288</sup> United States' comment on China's response to Question No. 74.

<sup>289</sup> See paragraph 7.287 above.

7.314 The United States referred, at the first substantive meeting and subsequently, to the Law on Donations for Public Welfare<sup>290</sup>, in particular, Article 17 of that Law which authorizes public welfare organizations to sell donated goods on the market if certain circumstances are present.<sup>291</sup> China replied that the terms of a donation agreement concluded under Article 12 of the Law – such as the Customs – Red Cross Memorandum – prevailed over Article 17 by virtue of Article 18.<sup>292</sup> The United States responded that selling goods under Article 17 of the Law and ensuring the resulting funds continue to be put to the "use" prescribed in the donation agreement appears, on its face, to be an action consistent with the mandates of Article 18.<sup>293</sup>

7.315 The Panel has several concerns with this line of argument. First, the Law on Donations for Public Welfare does not fall within the Panel's terms of reference.<sup>294</sup> The United States stated that this Law confirmed its concerns that delivery of infringing goods to social welfare bodies "under Chinese law" does not ensure that the goods will remain outside the channels of commerce.<sup>295</sup> However, the claim only specified the three Customs measures and no other parts of Chinese law. Whilst this Law is relevant to China's defence regarding the Customs – Red Cross Memorandum, it appears that the United States, in substance, purports to make a new claim that the manner in which Customs disposes of goods to social welfare bodies is inconsistent with Article 59 of the TRIPS Agreement based on the three Customs measures *in conjunction with this Law*.<sup>296</sup> The Panel is not entitled to rule on such a claim in this dispute.

7.316 Second, the United States seems unsure of the proper interpretation of the Law on Donations for Public Welfare. It was unaware of the existence of this Law at the time of its first written submission, stating that "nothing appears to prevent public welfare organizations from selling the infringing goods they receive".<sup>297</sup> In response to a question from the Panel, the United States stated that "[i]t is not evident whether or how other provisions in this Law affect the operation of Article 17 ...".<sup>298</sup> In response to a question from China, the United States stated that no legal authority to date demonstrated that Article 17 did *not* apply to all donations covered by the Law but that it "look[ed] forward to hearing more from China on this issue, including how the various provisions in the Law on Donations for Public Welfare relate to each other."<sup>299</sup> In its rebuttal submission, the United States asserted that selling donated goods under Article 17(iv) "appears, on its face, to be an action consistent with the mandates of Article 18."<sup>300</sup> In its comments on responses to questions after the second substantive meeting, the United States stated that the Law on Donations for Public Welfare

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<sup>290</sup> Adopted by the Standing Committee of the National People's Congress in 1999 and promulgated by Order of the President of the People's Republic of China, effective as of 1 September 1999.

<sup>291</sup> United States' first oral statement, para. 62; repeated in rebuttal submission, para. 151. An English translation of Article 17 of the Law, and a complete copy of the original version, were provided in Exhibit US-59.

<sup>292</sup> An English translation of Articles 12 and 18 of the Law was provided by China during the first substantive meeting.

<sup>293</sup> United States' rebuttal submission, para. 154.

<sup>294</sup> WT/DS362/7, attached as Annex D-1 to this report.

<sup>295</sup> United States' first oral statement, para. 62.

<sup>296</sup> The United States did make such a distinction in its copyright claims where the claims under Article 9.1 of the TRIPS Agreement identified "Article 4 of the Copyright Law" but the claim under Article 3.1 of the TRIPS Agreement identified "Article 4 of the Copyright Law, *in conjunction with* the nationality-dependent pre-authorization and pre-distribution review processes established by the other measures at issue". (emphasis added) The copyright claims under Articles 41.1 and 61 of the TRIPS Agreement identified "Article 4 of China's Copyright Law, *both independently and in conjunction with* the other measures at issue" (emphasis added).

<sup>297</sup> United States' first written submission, para. 186.

<sup>298</sup> United States' response to Question No. 31.

<sup>299</sup> United States' response to Question No. 2 posed by China.

<sup>300</sup> United States' rebuttal submission, paras 151-154.

appears to allow sale into the channels of commerce when certain exigencies are present.<sup>301</sup> However, the United States has provided no evidence to support its assertion besides the text of the Law (which is unclear) and three provisions of the Contract Law (considered at paragraphs 7.320 to 7.322 below). The United States asserts that China has not provided any legal basis for asserting that the terms of the donation agreement override this Law. However, as the party asserting that, due to this Law, the measures at issue and a donation agreement do not fulfil China's obligations under Article 59, the United States bears the burden of proof.

7.317 Third, this issue involves a detailed point of Chinese domestic law as to the proper construction of the Law on Donations for Public Welfare. Article 17(iv), to which the United States refers, provides as follows:

"Where the property donated is not preservable or transportable or exceeds the actual need, the donee may sell it, but all the income therefrom shall be used towards the aim of the donation."<sup>302</sup>

7.318 Meanwhile, Article 18 of the same Law, to which China refers, provides as follows:

"Where the donee has concluded a donation agreement with the donor, he shall use the donated property according to the purpose of use prescribed in that agreement and may not alter the said purpose of use without authorization. Where such alteration is actually needed, he shall seek consent from the donor."<sup>303</sup>

7.319 The Panel observes that Article 12 of the Law recognizes the right of donors and donees to enter into donation agreements. Article 17 contains four paragraphs of which at least three provide for use of donated property by certain types of social welfare organizations. Article 17 limits use by such organizations in various general ways. Article 18 refers to use of donated property in accordance with the specific purpose set out in a donation agreement. It is not clear how the two provisions are reconciled. Article 18 might supplement Article 17 or, equally, set out an alternative that allows donors and donees to contract out of Article 17. Without further evidence, the Panel cannot reach any conclusion concerning either party's assertions regarding these provisions of this Law.<sup>304</sup>

7.320 The United States also makes reference to the Contract Law in support of assertions that even when a donation agreement has been reached, the Law on Donations for Public Welfare appears to allow sale into commerce<sup>305</sup> and that China's Contract Law indicates that when a contract contains a provision inconsistent with a Chinese law, the law prevails over that contract provision.<sup>306</sup> As the party making these assertions, the United States bears the burden of proving that they are true.<sup>307</sup> However, the United States does not link the latter assertion to the specific evidence of the dispute. Instead, it submits three provisions of the Contract Law.<sup>308</sup> The first provision provides for the

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<sup>301</sup> United States' comment on China's response to Question No. 74.

<sup>302</sup> Mutually agreed translation no. 10.

<sup>303</sup> *Ibid.* Article 28 of the Law provides for legal responsibility where a donee, without permission of the donor, alternates the nature or purpose of use of the property donated.

<sup>304</sup> See also China's response to Question No. 74.

<sup>305</sup> United States' second oral statement, para. 52; comment on China's response to Question No. 74.

<sup>306</sup> United States' second oral statement, para. 52, annexing Exhibit US-73, setting out three provisions of the Contract Law, and Exhibit US-74, setting out one article of a Judicial Interpretation of certain issues concerning the application of the Contract Law.

<sup>307</sup> Appellate Body Report in *US – Wool Shirts and Blouses*, at p. 14.

<sup>308</sup> Adopted and promulgated by the National People's Congress in 1999.

invalidity of an entire contract.<sup>309</sup> It provides no substantiation of the improbable suggestion that the narrow provision in Article 17(iv) of the Law on Donations for Public Welfare renders the entire Customs – Red Cross Memorandum invalid. The third provision provides for monitoring and dealing with certain illegal acts and its relevance is not clear.<sup>310</sup> The second provision, Article 123, reads as follows:

"Where another law (法律) provides otherwise in respect of a certain contract, such provisions prevail."<sup>311</sup>

7.321 It is not clear what "otherwise" means, as the context of Article 123 has not been submitted in evidence. It seems that the suggestion is that, assuming Article 17(iv) of the Law on Donations for Public Welfare creates an "implied term", this could invalidate Article 7 of the Customs – Red Cross Memorandum by virtue of Article 123 of the Contract Law. However, the United States' assertions with respect to the collective construction of these two laws and a specific contract constitute mere speculation and the evidence on the record is wholly inadequate to form any view of it.<sup>312</sup>

7.322 Therefore, the terms of Article 17 of the Law on Donations for Public Welfare, read in context and in conjunction with the Contract Law, do not rebut China's defence nor, hence, disturb the Panel's finding at paragraph 7.312 above with respect to the terms of the Customs measures and the Customs – Red Cross Memorandum.

7.323 Lastly, the Panel recalls that the obligation in Article 59 is placed upon China, as the Member, and not upon the three Customs measures that the United States specified in its request for establishment of a panel. There is no reason why all conditions relevant to disposal outside the channels of commerce must appear in these three specific measures, as China is free to determine the method of implementation of its obligations under Article 59 in accordance with Article 1.1 of the TRIPS Agreement.<sup>313</sup> The Law on Donations for Public Welfare emerged in piecemeal fashion throughout these proceedings due to selective quotation by both parties to the dispute.<sup>314</sup> Yet the Law on Donations for Public Welfare is a public measure, adopted by the National People's Congress of China and promulgated by the President of China in 1999.<sup>315</sup> Had this Law, in particular Article 17, been the subject of consultations between the parties and specified in the request for establishment of the Panel in accordance with Article 6.2 of the DSU, it is likely that these issues would have been properly briefed and that the Panel could have reached a view on some of them.

7.324 For the reasons set out above, the Panel confirms its finding at paragraph 7.312 above and finds that the United States has not established that, with respect to the donation of infringing goods to

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<sup>309</sup> Article 52(v) of the Contract Law provides that "A contract is invalid in any of the following circumstances: (v) the contract violates a compulsory provision of any law (法律) or administrative regulation (行政法规)".

<sup>310</sup> Article 127 of the Contract Law provides that certain authorities shall monitor and deal with certain illegal acts.

<sup>311</sup> Exhibit US-73.

<sup>312</sup> See also China's response to Question No. 74.

<sup>313</sup> This was also the approach followed in the Panel Report in *EC – Trademarks and Geographical Indications (US)*, at paras 7.746-7.751.

<sup>314</sup> Article 6 of the Law on Donations for Public Welfare was provided with China's first written submission (Exhibit CHN-90); Article 17 with the United States' during first oral statement (Exhibit US-59); Articles 12 and 18 were provided by China later during the first substantive meeting and finally a complete translated copy was submitted after that meeting (Exhibit CHN-154). A mutually agreed translation was provided shortly before the second substantive meeting (MAT-10).

<sup>315</sup> See note 290 above. The United States accessed a copy of the Law from the Ministry of Commerce website prior to the first substantive meeting with the Panel: see United States' first oral statement, para. 61 and Exhibit US-59.

social welfare bodies under the measures at issue, Customs lacks authority to order disposal of infringing goods in accordance with the principles set out in the first sentence of Article 46.

(viii) *Sale to the right holder*

7.325 The second disposal method set out in the measures at issue is sale to the right holder. Sale to the right holder is voluntary in that it requires the consent of the right holder. If the right holder consents, it pays for the infringing goods at a price to be agreed.

7.326 Article 27 of the Customs IPR Regulations sets out sale to the right holder after donation to social welfare bodies. It uses the modal verb translated as "can" (or "may") (可以). Article 30 of the Implementing Measures sets out donation to social welfare bodies and sale to the right holder as alternatives with no apparent order between them.<sup>316</sup> Therefore, there appear to be no circumstances in which sale to the right holder is the only option available and could preclude any authority required by Article 59. In view of the Panel's finding at paragraph 7.324 above, it is therefore unnecessary to assess this option to determine whether the Customs measures are consistent with Article 59 of the TRIPS Agreement.

(ix) *Auction and authority to order the destruction of infringing goods*

7.327 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.<sup>317</sup> However, the Panel recalls its finding at paragraph 7.240 above 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.

7.328 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.<sup>318</sup> It does not allege that Customs has authority 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.

7.329 The claim is that the measures, on their face, treat auction (and the other disposal methods) as "compulsory prerequisites" to destruction and create a "compulsory sequence of steps" that renders auction mandatory in certain circumstances.<sup>319</sup> China responds that the Regulations express a "preference" for certain disposition methods and that the Implementing Measures confirm this prioritization. China argues that the measures vest Customs with "considerable discretion" to determine what method is appropriate and that Customs has the legal authority to order any of the four disposition methods.<sup>320</sup>

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<sup>316</sup> The United States agrees that, as a legal matter, they are parallel options: see its response to Question No. 78.

<sup>317</sup> See paragraph 7.244 above.

<sup>318</sup> United States' rebuttal submission, para. 161; responses to Questions Nos. 39, 41 and 83.

<sup>319</sup> United States' first written submission, paras 191 and 194.

<sup>320</sup> China's first written submission, paras 158-159.

7.330 The Panel begins by examining the measures on their face. The Customs IPR Regulations set out four disposition methods in Article 27, of which auction is the third. With respect to auction, Article 27 provides as follows:

"Where the confiscated goods infringing on intellectual property rights cannot be used for social public welfare undertakings and the holder of the intellectual property rights has no intention to buy them, Customs *can*, after eradicating the infringing features, auction them off according to law."<sup>321</sup> (emphasis added)

7.331 This phrase provides for the auction of infringing goods. It is conditional on the non-application of the first two methods, i.e. donation to social welfare bodies and sale to the right holder. This phrase uses a modal verb translated as "can" (or "may") (可以). This indicates that the Customs IPR Regulations impose no obligation to auction infringing goods even where the first two disposition methods are not applied.

7.332 The context confirms that the choice of this modal verb is significant as the same paragraph also uses the modal verb translated as "shall" (应当) for other disposition methods; specifically, it uses "can" or "may" for sale to the right holder and auction, but "shall" for donation to social welfare bodies and destruction.

7.333 The succeeding phrase on destruction provides that "[w]here the infringing features are impossible to eradicate, Customs shall destroy the goods." This indicates that the provision that Customs shall destroy the goods is conditional upon whether "the infringing features are impossible to eradicate". That condition, on its face, does not imply that there is any lack of authority to destroy the goods where the infringing features are *not* impossible to eradicate.

7.334 It seems clear from the text that the eradication of infringing features is a condition attached to the auction method. This is in fact expressly confirmed by the first operative paragraph of Public Notice No. 16/2007 quoted at paragraph 7.195 above. In other words, the *inability* to eradicate infringing features precludes the auction method. However, that does not imply that the *ability* to eradicate infringing features precludes the destruction method because the auction method is optional, not mandatory, under Article 27 of the Customs IPR Regulations.

7.335 The United States submits that if none of the first three options is viable, "Customs *may, then and only*, proceed to the third item: destruction of the goods" (emphasis added).<sup>322</sup> However, in the Panel's view, this misreads the text which provides that if none of the first three options is viable, Customs shall destroy the goods. It does not state that Customs *shall not* destroy the goods in other situations.

7.336 In summary, Article 27 of the Customs IPR Regulations provides for four options of which the second, as well as the third, i.e. auction, are optional. The Panel will examine whether this position is altered by the Implementing Measures.

7.337 The Implementing Measures provide for the same four disposition methods in Article 30 in the same order. Article 30 sets out the first two options as alternatives in a single item numbered (1), then sets out auction in item (2) and destruction in item (3). Article 30 establishes a clear order among these options by providing that item (2) (auction) applies:

"[w]here the goods concerned cannot be disposed of in accordance with Item (1) but the infringing features can be eradicated";

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<sup>321</sup> Mutually agreed translation no. 6.

<sup>322</sup> United States' first written submission, para. 182.

and providing that item (3) (destruction) applies:

"where the goods concerned cannot be disposed of in accordance with Items (1) and (2)".

7.338 Like Article 27 of the Customs IPR Regulations, item (3) on destruction provides that the goods "shall" (应当) be destroyed when the above condition is met. However, this does not, of itself, imply that destruction is not permitted where the other disposition methods are available. That would depend on whether the measure obliged Customs to order any of the other disposition methods in any circumstances.

7.339 The parties agreed to include the modal verb "shall" in all three items of Article 30 of the Implementing Measures for the purposes of translation into English but China maintains that the measure gives Customs considerable discretion.<sup>323</sup> The Panel does not assume that the use of the word "shall" in a non-authentic translation of the Implementing Measures necessarily denotes an obligation in the same way as the word "shall" when used in the English version of the WTO covered agreements. The Panel notes that the original, authentic version of Article 30 of the Implementing Measures does not include a modal verb in either item (1) or item (2) with respect to any of the first three disposition methods but only in item (3) with respect to destruction. The original version uses the modal verb translated as "shall" (应当) in the introductory sentence that reads "Customs 'shall' dispose of infringing goods it has confiscated according to the following provisions".<sup>324</sup> The first three disposition methods are then set out as a series of steps that, in different circumstances, Customs "hands over", "assigns" or "auctions off"<sup>325</sup>, in contrast to item (3) which uses the modal verb translated as "shall" (应当) (as does the concluding paragraph, twice). This may indicate that Customs has a degree of discretion under the Implementing Measures, as China maintains. Therefore, the Panel does not consider that the text of Article 30 of the Implementing Measures is sufficiently clear on its own to conclude that it obliges Customs to auction goods at any point.

7.340 The Implementing Measures were adopted by the Standing Committee of the General Administration of Customs to implement the Customs IPR Regulations, which were enacted by the Standing Committee of the State Council. The State Council is the highest organ of administrative power in China. Therefore, any ambiguity in the Implementing Measures should be resolved by reference to the higher norm, i.e. the Customs IPR Regulations.<sup>326</sup> Article 27 of the Customs IPR Regulations provides that auction is optional.

7.341 Public Notice No. 16/2007 is another measure of the General Administration of Customs of general application with respect to the auction of infringing goods. It contains a single recital that reads as follows:

"In accordance with Article 27 of the Regulations of the People's Republic of China on Customs Protection of Intellectual Property Rights (hereinafter referred as the 'Regulations'), where the confiscated goods infringing intellectual property rights cannot be used in social public welfare and the holder of intellectual property rights does not wish to buy them, the Customs *may* auction them off according to law after eradicating the infringing features. In order to regulate the auction of infringing

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<sup>323</sup> See paragraph 7.328 above.

<sup>324</sup> Only the original version of the measures is authentic.

<sup>325</sup> Item (2) also includes the adverb 依法 which has been translated as "according to law". The United States acknowledges that this means auction should comply with the relevant rules governing these activities: see response to Question No. 77.

<sup>326</sup> The United States agrees that the higher source of law will likely carry more weight: see its response to Question No. 27.

goods by Customs, improve the transparency of enforcement by Customs, and safeguard the right to know of the holders of intellectual property rights, it is hereby publicly notified as follows in respect of relevant matters:" (emphasis added)

7.342 The recital indicates that the General Administration of Customs issued this Public Notice for the express purposes of regulating the auction of infringing goods by Customs and improving transparency of enforcement by Customs, as well as granting a right to comment to right holders. The Panel observes that although Public Notice No. 16/2007 post-dates both the Customs IPR Regulations and the Implementing Measures, it recites only the permissive language of Article 27 of the Customs IPR Regulations in describing its authority to auction infringing goods.<sup>327</sup> This tends to confirm that any ambiguity in the Implementing Measures should be resolved by reference to the higher norm, i.e. the Customs IPR Regulations.<sup>328</sup>

7.343 Accordingly, the Panel finds that the United States has not established that the Customs measures on their face oblige Customs to order the auction of infringing goods.

7.344 The evidence on the record also includes documents from Customs' case files and statistics that indicate how Customs has in fact discharged its authority under Article 30 of the Implementing Measures to destroy, rather than auction, goods. The Panel considers it appropriate to review this evidence, bearing in mind that the claim concerns whether Customs "[has] the authority" to order destruction, not whether it actually uses that authority.

7.345 The Panel observes that the documents from Customs' case files show that destruction has occurred in a circumstance that is not mentioned on the face of the Implementing Measures. Given that auction is the third disposition method in the order established in the measures at issue and that destruction is the fourth and last, auction must necessarily have been decided against with respect to any goods destroyed. The Implementing Measures on their face set out only one condition that, if not satisfied, would dictate a decision to destroy goods, rather than auction them. That condition, set out in item (2) of the Implementing Measures, is that "the infringing features can be eradicated".

7.346 However, in one case concerning counterfeit automobile parts, Customs expressly stated a different reason for not auctioning the goods. It stated that the infringing goods could not be used for public welfare and the right holders had no intention to purchase the goods (a condition on the face of the Implementing Measures) *plus* "[t]he safety of these goods can not be guaranteed, and thus it is not

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<sup>327</sup> The United States agrees that Public Notice No. 16/2007 "merely confirms the current hierarchy of disposal options for confiscated goods that exist under China's measures": see United States' first written submission, fn. 118.

<sup>328</sup> The Panel also observes that the documents from Customs' case files cite the Customs IPR Regulations but do not cite the Implementing Measures: for example, a Report on the destruction of certain infringing goods cites the Customs Law, the Trademark Law and the Customs IPR Regulations and reports that the goods were destroyed in accordance with the provisions of the Customs IPR Regulations (Exhibit CHN-96). In another case, a Decision Notice cited the Trademark Law, the Customs IPR Regulations and Regulations on the Implementation of Customs Administrative Punishments (Exhibit CHN-98). In another case, an Application form for destruction of infringing goods cites Article 27.3 of the Customs IPR Regulations in an opinion that goods should be destroyed (Exhibit CHN-99).

appropriate to auction them."<sup>329</sup> That condition does not appear on the face of the Implementing Measures. No reference was made to the eradication of infringing features.<sup>330</sup>

7.347 The issue of safety is not mentioned on the face of the Implementing Measures and the United States does not allege that it is somehow implied, for example, by the requirement that goods be auctioned "according to law".<sup>331</sup> China submits that Customs may not auction goods with quality and safety defects in accordance with the Law on Product Quality<sup>332</sup> and asserts that there are other applicable norms, that it does not substantiate.<sup>333</sup> The United States does not dispute that there may be other applicable laws but argues that, even if they do apply, the Customs hierarchy still remains mandatory.<sup>334</sup> The United States acknowledges that it "does not know" whether goods may have been destroyed for reasons other than those "mandated" in the Customs measures.<sup>335</sup>

7.348 In the Panel's view, if the United States argues that the measures are mandatory "on their face", the argument is that the measures are mandatory as stated. The fact that there appear to be circumstances in which Customs departs from the terms of the measures indicates that, at the very least, the measures are not "as mandatory" as they appear on their face which calls into question whether the particular disposal method at issue is, indeed, mandatory at all. This is consistent with the view that, in accordance with the terms of Implementing Measures, as interpreted in light of the

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<sup>329</sup> An Application form for destruction of infringing goods apparently prepared by Fuzhou Customs in 2006 refers to the destruction of certain counterfeit automobile parts. The application form sets out the opinion of the case handlers (in this case "suggesting destruction") and the opinions of the section chief, division chief and director (in each case "agreed" or a signature) in Exhibit CHN-99.

<sup>330</sup> China submitted evidence of three other cases in which Customs destroyed goods, allegedly for reasons other than that the infringing features could not be eradicated. However, the Panel does not find these case files probative. In a case concerning counterfeit game consoles, Customs states the reasons for destruction. These were that the goods infringed trademarks and "design patent rights". This does not expressly mention eradication of the infringing features (a condition on the face of the Implementing Measures for auction), but it might have implied that, as features of shape or ornamentation, the infringing features could not be eradicated: see "Report on the Destruction of the Counterfeit PS Game Console by Huangpu Customs" 埔关法 [2008] No. 78 in Exhibit CHN-96. Elsewhere, China suggests that "design patent rights" imply that the infringing features cannot all be eliminated: see China's first written submission, para. 224.

In a case concerning counterfeit electric irons, China submits a summary of the case and that asserts that the infringing features could be eliminated and the goods could be auctioned according to law but the goods were destroyed because they presented quality problems and safety risks. The Panel notes that the infringing goods were confiscated and the exporter was fined: see Decision Notice of Administrative Punishment 拱关知字 [2006] No. 9. Customs notified the exporter that it would sell the goods (as well as the vehicles) in case of non-payment of the fine but destroyed them instead. The Opinion Form does not state the reason why Customs chose to destroy, rather than auction, the goods. See Exhibit CHN-98.

In a case concerning counterfeit motorcycle seats, China asserts that the goods were destroyed because Customs determined that even the slight risk of defect warranted their destruction. However, this is not clear from the supporting documents: see a report prepared by Huangpu Customs in the case shows only that the infringing goods were destroyed without giving the reason in Exhibit CHN-173.

<sup>331</sup> United States' response to Question No. 77.

<sup>332</sup> Law on Product Quality, adopted by the Standing Committee of the National People's Congress and promulgated by Order No. 71 of the President of the People's Republic of China on 22 February 1993, amended in accordance with a Decision of the Standing Committee of the National People's Congress on 8 July 2000. Articles 12 and 13 of this Law are reproduced in Exhibit CHN-97: see China's first written submission, para. 170; response to Question No. 82. The Panel also notes that a document prepared by the General Office of Fujian Provincial People's Government dated 8 March 2006 in the case of the counterfeit automobile parts also refers to requirements of the National Office for Combating Smuggling that "all smuggled dismantled automobiles and fittings confiscated shall not be auctioned or released to the market, and shall be disposed by the local Customs after being crushed": in Exhibit CHN-99.

<sup>333</sup> China's response to Question No. 82.

<sup>334</sup> United States' second oral statement (closing statement), para. 22; response to Question No. 78.

<sup>335</sup> United States' response to Question No. 79.

Customs IPR Regulations, the auction method is not in fact mandatory, in the sense that it does not preclude the destruction option.

7.349 Uncontested statistics provided by China<sup>336</sup> show that Customs orders the disposition of infringing goods in the following proportions in terms of shipments: (1) donation to social welfare bodies (53.5%); (2) destruction (44.9%); (3) auction (0.87%); and (4) sale to the right holder (0.65%). The proportions in terms of value are as follows: (1) destruction (57.5%); (2) donation to social welfare bodies (39.5%); (3) auction (2.2%); and (4) sale to the right holder (1%).<sup>337</sup> The statistics are consistent with the Panel's reading of Article 27 of the Customs IPR Regulations, as set out at paragraph 7.336 above, as they show that the two disposition methods that are clearly optional under the Regulations are used far less than the two that are not.

7.350 Further, if one excludes all goods disposed of under item (1) of the Implementing Measures (i.e. by donation to social welfare bodies or sale to the right holder), one is left with the subset of goods where Customs chose between auction and destruction. The Implementing Measures on their face provide for the destruction of such goods only where the infringing features cannot be eradicated. The statistics show that, among goods dealt with under items (2) and (3) of the Implementing Measures, the following decisions were in fact made in terms of the number of shipments and the relative value of the infringing goods:

		2005	2006	2007	Total
<b>By shipment<sup>338</sup></b>					
<b>Exports + imports</b>	Auctioned	4	7	1	12
	Destroyed	143	227	248	618
<b>By value</b>					
<b>Exports + imports</b>	Auctioned	7.10%	3.54%	0.59%	3.70%
	Destroyed	92.90%	96.46%	99.41%	96.30%
<b>Imports only</b>	Auctioned	0%	0%	0%	0%
	Destroyed	100.00%	100.00%	100.00%	100.00%

7.351 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.

7.352 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

<sup>336</sup> See Customs Statistics in note 219 above.

<sup>337</sup> See Customs Statistics at note 219 above.

<sup>338</sup> The number of shipments of imports auctioned was zero. Separate figures for the number of shipments of imports destroyed were not provided.

law to order destruction in those cases.<sup>339</sup> 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.<sup>340</sup>

7.353 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.

7.354 For the above reasons, the Panel finds that the United States has 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.

7.355 The Panel recalls its findings at paragraphs 7.324 and 7.354 and concludes that the United States has not established that the Customs measures are inconsistent with Article 59 of the TRIPS Agreement, as it incorporates the principles set out in the *first* sentence of Article 46 of the TRIPS Agreement.

(x) *Auction and "simple removal of the trademark unlawfully affixed"*

– Procedural issue

7.356 The Panel recalls its finding at paragraph 7.270 above that "the principles set out in Article 46" as incorporated by Article 59 of the TRIPS Agreement include the *fourth* sentence of Article 46. That sentence provides as follows:

"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."

7.357 The Panel has *not* found that the Customs measures are mandatory with respect to the auction of infringing goods. However, the Panel does not consider that this is fatal to the United States' claim with respect to the fourth sentence of Article 46.<sup>341</sup>

7.358 The Panel recalls its finding at paragraph 7.253 above that the obligation in Article 59 applies both to mandatory and discretionary measures as the obligation that Members' competent 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.<sup>342</sup> 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>343</sup> Therefore,

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<sup>339</sup> The issue here can be contrasted with that addressed in paragraph 7.138 above. It is not disputed that Article 4(1) of the Copyright Law is mandatory, and the obligation at issue in that claim is not phrased in terms that authorities "shall have the authority".

<sup>340</sup> United States' response to Question No. 41.

<sup>341</sup> China acknowledged that this claim was also made with respect to the fourth sentence of Article 46: see China's first written submission, para. 6; first oral statement, para. 68; rebuttal submission, para. 8.

<sup>342</sup> This is without prejudice to the Panel's comments at paragraph 7.244 above.

<sup>343</sup> The position is the same under the second sentence of Article 59.

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.

7.359 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.<sup>344</sup> China does not assert that Customs might auction goods destined for importation in future<sup>345</sup> 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>346</sup>

7.360 Therefore, the Panel will continue with its assessment of this claim with respect to the other principle set out in Article 46 that the United States has raised.

– Simple removal of the trademark unlawfully affixed

7.361 The Panel recalls that the parties have differing views as to the applicability of this principle. The United States submits that the fourth sentence of Article 46 is applicable under the first sentence of Article 59.<sup>347</sup> China considers that Customs is not subject to the principles articulated by the fourth sentence of Article 46.<sup>348</sup> The Panel has found that the fourth sentence of Article 46 is so applicable and will now interpret the principle that it sets out.

7.362 The fourth sentence of Article 46 reads as follows:

"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."

7.363 The term "counterfeit trademark goods" is defined by footnote 14(a) to the TRIPS Agreement as follows:

"For the purposes of this Agreement:

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<sup>344</sup> See paragraphs 7.232 and 7.233 above.

<sup>345</sup> This can be contrasted with the position of the respondent in the GATT Panel Report in *US - Superfund* (at para 5.2.9 and noted at para. 5.2.10); the GATT Panel Report in *US - Tobacco* (at para. 122); and the WTO Panel Report in *US - Section 301 Trade Act* (at para. 7.112).

<sup>346</sup> See Appellate Body Report in *US - Oil Country Tubular Goods Sunset Reviews*, para. 172.

<sup>347</sup> United States' first written submission, paras 175-178.

<sup>348</sup> China's first written submission, paras 218-222.

(a) 'counterfeit trademark goods' shall mean any goods, including packaging, bearing without authorization a trademark which is identical to the trademark validly registered in respect of such goods, or which cannot be distinguished in its essential aspects from such a trademark, and which thereby infringes the rights of the owner of the trademark in question under the law of the country of importation;"

7.364 Turning to the measures at issue, the Panel recalls its findings at paragraph 7.225 above that the measures at issue apply *inter alia* to counterfeit trademark goods and at paragraphs 7.331 and following that the measures permit auction of such goods. In this regard, Article 27 of the Customs IPR Regulations provides as follows:

"Where the confiscated goods infringing on intellectual property rights cannot be used for social public welfare undertakings and the holder of the intellectual property rights has no intention to buy them, Customs can, *after eradicating the infringing features*, auction them off according to law."<sup>349</sup> (emphasis added)

7.365 It seems clear from this provision that the eradication of infringing features is a condition attached to auction of goods confiscated by Customs. Article 27 of the Customs IPR Regulations is implemented and confirmed by Article 30(2) of the Implementing Measures<sup>350</sup> and is expressly confirmed by the first operative paragraph of Public Notice No. 16/2007 which provides, relevantly, as follows:

"Where the confiscated infringing goods are auctioned by Customs, Customs shall completely eradicate all infringing features on the goods and the packaging thereof strictly pursuant to Article 27 of the Regulations, including eradicating the features infringing trademarks, copyright, patent and other intellectual property rights."<sup>351</sup>

7.366 It is undisputed that in all cases in which Customs auctions goods that it has confiscated under the measures at issue, Customs first removes the infringing features.<sup>352</sup> It is clear from the measure on its face that the phrase "infringing features" refers to features that infringe any intellectual property rights covered by the measures, including not only trademarks, but also copyright and patents. With respect to counterfeit trademark goods, it seems obvious that the infringing features will comprise the counterfeit trademarks. Therefore, the fact that the measures refer to infringing "features" does not suggest that anything besides the counterfeit trademark is eradicated in these cases. China has confirmed that "with regard to trademark-infringing goods, elimination of infringing features refers to removal of the infringing trademark from the goods".<sup>353</sup>

7.367 Therefore, insofar as the state of the counterfeit trademark goods is concerned, the only action taken prior to auction is the removal of the trademark. The question arises whether this constitutes "simple" removal of a trademark within the meaning of the fourth sentence of Article 46 of the TRIPS Agreement.

7.368 China argues that its measures do not provide for "simple" removal of the trademark because they also provide an opportunity for the trademark right holder to comment prior to auction.<sup>354</sup> This

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<sup>349</sup> Mutually agreed translation no. 6.

<sup>350</sup> See paragraph 7.194 above.

<sup>351</sup> Mutually agreed translation no. 8.

<sup>352</sup> United States' first written submission, para. 56; rebuttal submission, para. 169; China's first written submission, para. 224; rebuttal submission, para. 194.

<sup>353</sup> China's response to Question No. 34.

<sup>354</sup> China's first written submission, para. 224.

procedure is set out in the second operative paragraph of Public Notice No. 16/2007.<sup>355</sup> China does not allege that Customs has an obligation to take any right holder's comments into account.<sup>356</sup>

7.369 The Panel notes that the word "simple" can be defined as "with nothing added; unqualified; neither more nor less than; mere, pure".<sup>357</sup> 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.

7.370 It is inevitable that a Member's authorities exercising authority under Article 59 will take certain actions of a procedural nature in releasing the good into the channels of commerce, such as physically transferring them to the custody of another party. The question is which other actions render removal of the trademark unlawfully affixed not "simple".

7.371 The context within the fourth sentence of Article 46 shows that simple removal of the trademark unlawfully affixed "shall not be sufficient" to permit release of the goods into the channels of commerce. The text does not prohibit the release of the goods into the channels of commerce *per se*. Rather, by specifically addressing the case of counterfeit trademark goods, and stating what is "not ... sufficient" to permit release, the provision impliedly permits release of counterfeit trademark goods into the channels of commerce where more than simple removal of the trademark is carried out.

7.372 Removal of a counterfeit trademark would ensure that the goods do not infringe the exclusive rights set out in Article 16 of the TRIPS Agreement. However, the fourth sentence of Article 46 provides that that shall *not* be sufficient, other than in exceptional cases. The fact that the negotiators included an additional requirement shows that this principle is intended to achieve more than simply the cessation of an infringement.

7.373 The context within Article 46 shows that the fourth sentence is one of a series of expressions of an objective set out at the beginning of that Article, namely, "to create an effective deterrent to infringement". Where counterfeit trademark goods are released into the channels of commerce after the simple removal of the trademark unlawfully affixed, an identical trademark can be produced or imported separately and unlawfully reaffixed, often with relative ease, so that the goods will infringe once again.

7.374 This problem applies to counterfeit trademark goods in particular because, as provided in the definition of "counterfeit trademark goods" in footnote 14(a) to the TRIPS Agreement, the counterfeit trademark is *identical* to the valid trademark or cannot be distinguished in its essential aspects from the valid trademark. Counterfeit trademark goods are more likely to imitate the appearance of genuine goods in their overall appearance and not simply in the affixation of the counterfeit trademark, as the likelihood that a counterfeit trademark good will confuse a consumer is related to the degree to which all its features, infringing and non-infringing, resemble the genuine good. Where the counterfeit trademark is removed, the resulting state of the goods may still so closely resemble the genuine good that there is a heightened risk of further infringement by means of re-affixation of a counterfeit trademark. Whilst this may be true of other, non-infringing goods as well, the goods confiscated by Customs are already counterfeit and are being released into the channels of commerce. The negotiators evidently considered that the heightened risk of further infringement warranted additional measures to create an effective deterrent to further infringement.

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<sup>355</sup> See paragraph 7.195 above.

<sup>356</sup> For example, in a case concerning counterfeit padlocks, the right holder objected to auction and offered to buy the goods. However, Jinhua (金华) Customs destroyed the goods instead: see Exhibit CHN-94.

<sup>357</sup> *New Shorter Oxford English Dictionary* (1993).

7.375 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.

7.376 The Panel finds confirmation for this interpretation in the second sentence of Article 59, which addresses the same issue but in a different context, and provides as follows:

"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." (emphasis added)

7.377 This sentence addresses the same basic problem as the fourth sentence of Article 46. It confirms that the state of the counterfeit trademark goods is the relevant consideration, although the obligation in the second sentence of Article 59 is less specific with respect to removal of the trademark, suggesting that "simple removal of the trademark" is an example of a means of altering the state of infringing goods. However, in the present dispute, the applicable obligation is found in the fourth sentence of Article 46, as incorporated by Article 59.

7.378 China argues that right-holders have a legal right to protection from goods that infringe their intellectual property, but not from unmarked goods that do not.<sup>358</sup>

7.379 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.

7.380 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".

7.381 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 reaffix counterfeit marks.<sup>359</sup>

7.382 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".<sup>360</sup> 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 reaffixed. In other words, it remains economically viable for the importer or a third party to purchase the goods at auction and reaffix the trademarks in order to infringe again, with the heightened risk of this occurring discussed at paragraph 7.374 above. In any case, there is no evidence that the prices established by

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<sup>358</sup> China's rebuttal submission, para. 195.

<sup>359</sup> China's first oral statement, para. 77; first written submission, paras 170-171.

<sup>360</sup> China's rebuttal submission, para. 196.

the method used by China Customs are so high that it is no longer economically viable to purchase the goods and reaffix the trademarks.<sup>361</sup>

7.383 China argues that the measures at issue prevent the cheap return of the seized good to the infringer and, by ensuring that the infringers reap no economic benefits, effectively deter infringement.<sup>362</sup>

7.384 The Panel sees no reference to the original infringer in the relevant obligation or in the objective set out in Article 46. There is no reason to suppose that the text is aimed at deterring infringement by the importer only and not by other parties, such as purchasers at auction. The use of the word "release" into the channels of commerce does not imply such a limitation as the sentence reads "release into the channels of commerce" not "release to the importer".<sup>363</sup>

7.385 Therefore, the Panel considers that, in regard to counterfeit trademark goods, China's Customs measures provide that the simple removal of the trademark unlawfully affixed is sufficient to permit release of the goods into the channels of commerce.

7.386 The Panel does not conclude on this basis alone that the measures at issue are inconsistent with the requirement of the fourth sentence of Article 46, as incorporated by Article 59, because that sentence contains the phrase "other than in exceptional cases". This phrase, read in context, implies that "in exceptional cases" the simple removal of the trademark unlawfully affixed *may* be sufficient to permit release of the goods into the channels of commerce.

7.387 The United States, in response to a question, submits that the ordinary meaning of "exceptional" suggests that there is something about the circumstances that is unusual or special, not that there is some *de minimis* number of cases where it is permissible to release the goods into normal channels of commerce after simply removing the infringing mark. If the negotiators had intended it to be the number of cases, they might have been expected to phrase the provision more in terms of "other than in a very limited number of cases" or "other than in a *de minimis*/insignificant number of cases".<sup>364</sup>

7.388 China, in response to the same question, submits that the ordinary meaning of "exceptional" includes "special", which suggests a qualitative test, and "unusual", which refers to frequency and suggests a quantitative test. An interpretation in terms of the set of circumstances, and an

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<sup>361</sup> The specific measures for the establishment of reserve prices in auctions of goods confiscated by Customs are set out in the Measures on Administration of Property Confiscated by Customs. These are internal measures of the General Administration of Customs formulated in accordance with the Customs Law, the Law on Administrative Penalty and the Auction Law in 2003: see Exhibit CHN-100. Article 18 of these Measures provides as follows:

"A reserve price shall be set for the confiscated property authorized to be auctioned off. Should appraisal be required in accordance with relevant provisions of laws and regulations, a price assessment entity lawfully established shall be authorized to complete such appraisal. In the case that several auction enterprises bid for the right to auction, the bid prices shall be compared with the appraisal price and the highest one taken as the reserve price. In the case that there were no multiple bids for the right to auction, the reserve price shall be reasonably determined based on the appraisal price given by the price assessment entity." (footnote omitted) See mutually agreed translation no. 9.

<sup>362</sup> China's rebuttal submission, para. 218.

<sup>363</sup> As noted at paragraph 7.276 above, the use of the word "release" in Article 46 and, hence, as incorporated in Article 59, has a broader meaning than simply release to the importer.

<sup>364</sup> United States' response to Question No. 86.

interpretation in terms of the number of cases, are both consistent with the plain meaning of "exceptional cases".<sup>365</sup>

7.389 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. The question is how to determine when any such case may be considered "exceptional".

7.390 The word "exceptional" may be defined as "of the nature of or forming an exception; unusual, out of the ordinary; special;"<sup>366</sup> This definition does not explain *in what way* a case must be different from other cases in order to be considered "exceptional" within the meaning of the fourth sentence of Article 46. Further, the question of *how* different a case must be from others is also a question of degree.

7.391 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 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.<sup>367</sup> 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.

7.392 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.

7.393 Therefore, the Panel considers that, in regard to counterfeit trademark goods, China's Customs measures provide that the simple removal of the trademark unlawfully affixed is sufficient to permit release of the goods into the channels of commerce in more than just "exceptional cases".

7.394 For the above reasons, the Panel concludes that the Customs measures are inconsistent with Article 59 of the TRIPS Agreement, as it incorporates the principle set out in the *fourth* sentence of Article 46.

### **3. Conclusions with respect to the Customs measures**

7.395 The Panel recalls its conclusions at paragraphs 7.231, 7.355 and 7.394 above that:

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<sup>365</sup> China's response to Question No. 86.

<sup>366</sup> *New Shorter Oxford English Dictionary* (1993).

<sup>367</sup> Without prejudice to the relevance of statements by individual participants in the negotiations, the Panel notes that China referred to this example in the records of the negotiation of the TRIPS Agreement: see its rebuttal submission at paras 211-213.

- (a) Article 59 of the TRIPS Agreement is not applicable to the Customs measures insofar as those measures apply to goods destined for exportation;
- (b) the United States has not established that the Customs measures are inconsistent with Article 59 of the TRIPS Agreement, as it incorporates the principles set out in the *first* sentence of Article 46 of the TRIPS Agreement; and
- (c) the Customs measures are inconsistent with Article 59 of the TRIPS Agreement, as it incorporates the principle set out in the *fourth* sentence of Article 46 of the TRIPS Agreement.

C. CRIMINAL THRESHOLDS

1. Description of the measures at issue

(a) Introduction

7.396 This Section of the Panel's findings concerns criminal thresholds established by the following measures. China's **Criminal Law** was adopted by the National People's Congress in 1979, revised by the National People's Congress in 1997 and promulgated by Order of the President of the People's Republic of China in 1997. The Criminal Law is divided into two Parts: Part One, setting out "General Provisions", and Part Two, setting out "Specific Provisions". Part Two, Chapter III, provides for "Crimes of disrupting the order of the socialist market economy". Chapter III, Section 7, provides for "Crimes of infringing intellectual property rights" and comprises Articles 213 to 220, considered below.

7.397 The Interpretation of the Supreme People's Court and the Supreme People's Procuratorate Concerning Some Issues on the Specific Application of Law for Handling Criminal Cases of Infringement of Intellectual Property Rights (Interpretation No. 19 [2004] of the Supreme People's Court) ("**Judicial Interpretation No. 19 [2004]**") was adopted in November 2004 and entered into force in December 2004. It interprets certain terms used in Articles 213 to 219 of the Criminal Law and also deals with certain other matters.

7.398 The Interpretation of the Supreme People's Court and the Supreme People's Procuratorate Concerning Some Issues on the Specific Application of Law for Handling Criminal Cases of Infringement of Intellectual Property Rights – II (Interpretation No. 6 [2007] of the Supreme People's Court) ("**Judicial Interpretation No. 6 [2007]**") was adopted and entered into force in April 2007. It interprets certain terms used in Article 217 of the Criminal Law and also deals with certain other matters.

(b) Trademark provisions

(i) *Use of a counterfeit trademark*

7.399 Article 213 of the Criminal Law may be translated as follows:

"Whoever, without permission from the owner of a registered trademark, uses a trademark which is identical with the registered trademark on the same kind of commodities shall, if *the circumstances are serious*, be sentenced to fixed-term imprisonment of not more than three years or criminal detention and shall also, or shall only, be fined; if the circumstances are especially serious, the offender shall be

sentenced to fixed-term imprisonment of not less than three years but not more than seven years and shall also be fined."<sup>368</sup> (emphasis added)

7.400 Article 1 of Judicial Interpretation No. 19 [2004] interprets the phrase "the circumstances are serious" in Article 213 of the Criminal Law and may be translated as follows:

"Whoever, without permission from the owner of a registered trademark, uses a trademark which is identical with the registered trademark on the same kind of commodities, in any of the following circumstances which shall be deemed as 'the circumstances are serious' under Article 213 of the Criminal Law, shall be sentenced to fixed-term imprisonment of not more than three years or criminal detention for the crime of counterfeiting registered trademark, and shall also, or shall only, be fined:

- (1) the *illegal business operation volume* of not less than 50,000 Yuan<sup>369</sup> or the *amount of illegal gains* of not less than 30,000 Yuan;
- (2) in the case of counterfeiting two or more registered trademarks, the *illegal business operation volume* of not less than 30,000 Yuan or the *amount of illegal gains* of not less than 20,000 Yuan;
- (3) other serious circumstances."<sup>370</sup> (emphasis added)

7.401 Article 12(1) of Judicial Interpretation No. 19 [2004] defines the term "illegal business operation volume" and may be translated as follows:

"The 'illegal business operation volume' herein means the value of the infringing products manufactured, stored, transported or sold during the course of commission of the act of infringing intellectual property rights. The value of the sold infringing products shall be calculated at the actual sale price. The value of the infringing products manufactured, stored, transported and unsold shall be calculated at the labelled price or at the average actual sales price of the infringing products as verified. If there is no labelled price on the infringing products or the actual sales price is unable to be verified, the price of the infringing products shall be calculated at the middle market price of the infringed products."<sup>371</sup>

7.402 Article 17 of Judicial Interpretation No. 30 [1998]<sup>372</sup> defines the term "amount of illegal gains" and may be translated as follows:

"The 'amount of illegal gains' in this Interpretation refers to the amount of profit obtained."<sup>373</sup>

(ii) *Selling counterfeit trademark commodities*

7.403 Article 214 of the Criminal Law may be translated as follows:

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<sup>368</sup> Mutually agreed translation no. 1.

<sup>369</sup> This corresponds to US\$6,250 at average market exchange rates (¥8.013/US\$ for 2004-2007).

<sup>370</sup> Mutually agreed translation no. 3.

<sup>371</sup> Mutually agreed translation no. 3.

<sup>372</sup> The Interpretation by the Supreme People's Court of Certain Questions Concerning the Specific Application of Law in Adjudicating Criminal Cases Involving Illegal Publications (Interpretation No. 30 [1998] of the Supreme People's Court) in Exhibits US-4 and CHN-3.

<sup>373</sup> Mutually agreed translation no. 4. The parties agree that this definition is applicable under Judicial Interpretation No. 19 [2004]: see United States' and China's respective responses to Question No. 3(a).

"Whoever sells commodities, knowing<sup>374</sup> that such commodities bear counterfeit registered trademarks shall, if *the amount of sales is relatively large*, be sentenced to fixed-term imprisonment of not more than three years or criminal detention and shall also, or shall only, be fined; if the amount of sales is huge, the offender shall be sentenced to fixed-term imprisonment of not less than three years but not more than seven years and shall also be fined."<sup>375</sup> (emphasis added)

7.404 Article 2 of Judicial Interpretation No. 19 [2004] interpreted the phrase "the amount is relatively large" under Article 214 of the Criminal Law and may be translated as follows:

"Whoever sells commodities, knowing that such commodities bear counterfeit registered trademarks, with the amount of sales of not less than 50,000 Yuan, this shall be deemed as 'the amount is relatively large' under Article 214 of the Criminal Law, and the offender shall be sentenced to fixed-term imprisonment of not more than three years or criminal detention for the crime of selling commodities bearing a counterfeit registered trademark, and shall also, or shall only, be fined."<sup>376</sup>

(iii) *Forgery of trademarks and sale of forged trademarks*

7.405 Article 215 of the Criminal Law may be translated as follows:

"Whoever forges or, without the authorization of another person, makes representations of that person's registered trademarks, or sells representations of another person's registered trademark that are forged or made without authorization, shall, if *the circumstances are serious*, be sentenced to fixed-term imprisonment of not more than three years, criminal detention or public surveillance and shall also, or shall only, be fined; if the circumstances are especially serious, the offender shall be sentenced to fixed-term imprisonment of not less than three years but not more than seven years and shall also be fined."<sup>377</sup> (emphasis added)

7.406 Article 3 of Judicial Interpretation No. 19 [2004] interpreted the phrase "the circumstances are serious" under Article 215 of the Criminal Law and may be translated as follows:

"Whoever forges or, without the authorization of another person, makes representations of that person's registered trademarks or sells such representations, in any of the following circumstances which shall be deemed as 'the circumstances are serious' under Article 215 of the Criminal Law, shall be sentenced to fixed-term imprisonment of not more than three years, criminal detention or public surveillance for the crime of illegally producing or selling illegally made representations of the registered trademark, and shall also, or shall only, be fined:

(1) forging or, without the authorization, making representations of the registered trademarks or selling such representations of not less than 20,000 pieces, or with the *illegal business operation volume* of not less than 50,000 Yuan, or the *amount of illegal gains* of not less than 30,000 Yuan;

(2) forging or, without the authorization, making two or more kinds of representations of the registered trademarks or selling such representations of not less

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<sup>374</sup> Note in mutually agreed translation: Please refer to Article 9 of the 2004 Judicial Interpretation.

<sup>375</sup> Mutually agreed translation no. 1.

<sup>376</sup> Mutually agreed translation no. 3.

<sup>377</sup> Mutually agreed translation no. 1.

than 10,000 *pieces*, or with the *illegal business operation volume* of not less than 30,000 Yuan, or the *amount of illegal gains* of not less than 20,000 Yuan;

(3) other serious circumstances."<sup>378</sup> (emphasis added)

7.407 Article 12(1) of Judicial Interpretation No. 19 [2004] defines the term "illegal business operation volume" as set out at paragraph 7.401 above. Article 17 of Judicial Interpretation No. 30 [1998] defines the term "amount of illegal gains" as set out at paragraph 7.402 above. Article 12(3) of Judicial Interpretation No. 19 [2004] defines the term "piece" and may be translated as follows:

"'Piece' (件)<sup>379</sup> under Article 3 herein means one representation with the entire trademark pattern."<sup>380</sup>

(c) Copyright provisions

(i) *Criminal copyright infringement*

7.408 Article 217 of the Criminal Law may be translated as follows:

"Whoever, for the purpose of making profits, commits any of the following acts of infringement of copyright shall, if *the amount of illegal gains is relatively large*, or if *there are other serious circumstances*, be sentenced to fixed-term imprisonment of not more than three years or criminal detention and shall also, or shall only, be fined; if the amount of illegal gains is huge or if there are other especially serious circumstances, the offender shall be sentenced to fixed-term imprisonment of not less than three years but not more than seven years and shall also be fined:

(1) reproducing [/] <sup>381</sup> distributing written works, musical works, cinematographic works, television or video works, computer software or other works without permission of the copyright owner;

(2) publishing a book of which the exclusive right of publication is enjoyed by another person;

(3) reproducing [/] distributing audio recording [/] video recording made by another person without permission of the maker;

(4) making, selling <sup>382</sup> a work of fine art with the forged signature of another person."<sup>383</sup> (emphasis added)

7.409 Article 5 of Judicial Interpretation No. 19 [2004] interpreted the phrases "the amount of illegal gains is relatively large" and "there are other serious circumstances" under Article 217 of the Criminal Law and may be translated as follows:

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<sup>378</sup> Mutually agreed translation no. 3.

<sup>379</sup> Note in mutually agreed translation: in this context, piece (件) is a "measure word" for a trademark representation.

<sup>380</sup> Mutually agreed translation no. 3.

<sup>381</sup> The parties advised the Panel orally at the second substantive meeting that the use of "[/]" in mutually agreed translations nos. 1, 2 and 3 did not indicate disagreement but rather reflected the fact that the original version did not use the word "and".

<sup>382</sup> Note in mutually agreed translation: There is neither "and" or "or" between "making" and "selling", only a Chinese repetitive comma (、) or 顿号 which has no precise English equivalent.

<sup>383</sup> Mutually agreed translation no. 1.

"Whoever, for the purpose of making profits, commits any of the acts of infringement of copyright under Article 217 of the Criminal Law, with the *amount of illegal gains* of not less than 30,000 Yuan which shall be deemed as 'the amount of illegal gains is relatively large'; in any of the following circumstances which shall be deemed as 'there are other serious circumstances', shall be sentenced to fixed-term imprisonment of not more than three years or criminal detention for the crime of infringement of copyright, and shall also, or shall only, be fined:

- (1) the *illegal business operation volume* of not less than 50,000 Yuan;
- (2) reproducing [/] distributing, without permission of the copyright owner, a written work, musical work, cinematographic work, television or other video works, computer software and other works of not less than 1,000<sup>384</sup> 张 (份)<sup>385</sup> in total;
- (3) other serious circumstances."<sup>386</sup> (emphasis added)

7.410 Article 12(1) of Judicial Interpretation No. 19 [2004] defines the term "illegal business operation volume" as set out at paragraph 7.401 above. Article 17 of Judicial Interpretation No. 30 [1998] defines the term "amount of illegal gains" as set out at paragraph 7.402 above.

7.411 Article 1 of Judicial Interpretation No. 6 [2007] re-interpreted the phrase "there are other serious circumstances" under Article 217 of the Criminal Law and may be translated as follows:

"Whoever, for the purpose of making profits, reproduces [/] distributes, without permission of the copyright owner, a written work, musical work, cinematographic work, television or video works, computer software and other works of not less than 500 张 (份)<sup>387</sup> in total, [the offence] shall be deemed as 'there are other serious circumstances' under Article 217 of the Criminal Law ..."<sup>388</sup>

7.412 The number "500" in this provision conflicts with the number "1000" in the earlier Judicial Interpretation. The number "500" therefore prevails by virtue of Article 7 of Judicial Interpretation No. 6 [2007], which may be translated as follows:

"Where any previously promulgated judicial interpretation is in conflict with this Interpretation, this Interpretation shall prevail."<sup>389</sup>

(ii) *Selling copyright-infringing reproductions*

7.413 Article 218 of the Criminal Law may be translated as follows:

"Whoever, for the purpose of making profits, sells infringing reproductions, knowing that such infringing reproductions are those stipulated in Article 217 of this Law shall, if *the amount of illegal gains is huge*, be sentenced to fixed-term imprisonment

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<sup>384</sup> The number "1000" has been superseded by "500": see paragraphs 7.411 and 7.412 below.

<sup>385</sup> Note in mutually agreed translation: 张 is a Chinese "measure word" broadly used to count flat things (like optical disks, pages, etc.) and 份 is a "measure word" used to count copies in general.

<sup>386</sup> Mutually agreed translation no. 3.

<sup>387</sup> Note in mutually agreed translation: 张 is a Chinese "measure word" broadly used to count flat things (like optical disks, pages, etc.) and 份 is a "measure word" used to count copies in general.

<sup>388</sup> Mutually agreed translation no. 2.

<sup>389</sup> Mutually agreed translation no. 2 and the parties' respective responses to Question No. 3(a).

of not more than three years or criminal detention and shall also, or shall only, be fined."<sup>390</sup> (emphasis added)

7.414 Article 6 of Judicial Interpretation No. 19 [2004] interpreted the phrase "the amount of illegal gains is huge" under Article 218 of the Criminal Law and may be translated as follows:

"Whoever, for the purpose of making profits, commits any of the acts as stipulated in Article 218 of the Criminal Law, where the amount of illegal gains is not less than 100,000 Yuan, this shall be deemed as 'the amount of illegal gains is huge', and the offender shall be sentenced to fixed-term imprisonment of not more than three years or criminal detention for the crime of selling infringing reproductions, and shall also, or shall only, be fined."<sup>391</sup>

(d) Crimes of infringing intellectual property rights committed by a unit

7.415 The Panel's terms of reference also refer to Article 220 of the Criminal Law on crimes under Articles 213 to 219 where committed by a unit. The United States has not requested relief in respect of that Article. Therefore, the Panel does not consider this aspect of the measure.

## **2. Construction of the measures at issue**

(a) Introduction

7.416 The Panel notes that this claim challenges China's criminal measures "as such". The parties disagree on certain aspects of the measures at issue. The Panel is therefore obliged, in accordance with its mandate, to make an objective assessment of the meaning of the relevant provisions of those measures. The Panel recalls its observations at paragraph 7.28 above and confirms that it examines these measures solely for the purpose of determining their conformity with China's obligations under the TRIPS Agreement.

(b) Normative effect of the Judicial Interpretations

7.417 Under the 1982 Constitution of the People's Republic of China, the National People's Congress is the highest organ of State power and its permanent body is its Standing Committee. The National People's Congress and its Standing Committee exercise the legislative power of the State. The National People's Congress enacts and amends basic laws, such as the Criminal Law, whilst its Standing Committee enacts and amends other statutes.<sup>392</sup>

7.418 In 1981, the Standing Committee of the National People's Congress adopted a Resolution on Improving the Work of Interpreting the Law, in which it decided as follows:

"Questions involving the specific application of laws and decrees in court trials shall be interpreted by the Supreme People's Court. Questions involving the specific application of laws and decrees in procuratorial work shall be interpreted by the Supreme People's Procuratorate."<sup>393</sup>

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<sup>390</sup> Mutually agreed translation no. 1.

<sup>391</sup> Mutually agreed translation no. 3.

<sup>392</sup> 1982 Constitution of the People's Republic of China, Articles 62 and 67, explained in China's WTO Trade Policy Review, Report by the Secretariat, WT/TPR/S/161, Chapter II(2), referenced in United States' first written submission, para. 22, set out in Exhibit US-16.

<sup>393</sup> 1981 Resolution of the Standing Committee of the National People's Congress on Improving the Work of Interpreting the Law, paragraph 2, in Exhibit US-13.

7.419 In 1997, the Supreme People's Court formulated Certain Provisions on Judicial Interpretation Work. In March 2007, it replaced these with new Provisions on Judicial Interpretation Work, which may be translated as follows:

"Judicial interpretations issued by the Supreme People's Court shall have legal effect."<sup>394</sup>

7.420 In 1996 the Supreme People's Procuratorate formulated Provisional Provisions on Judicial Interpretation Work. In May 2006, it replaced these with Provisions on Judicial Interpretation Work, which may be translated as follows:

"Judicial interpretations made by the Supreme People's Procuratorate have legal effect. People's procuratorates may use provisions of judicial interpretation in legal documents such as bills of indictment or protest."<sup>395</sup>

7.421 The Provisions of the Supreme People's Court on Judicial Interpretation Work and the Provisions of the Supreme People's Procuratorate on Judicial Interpretation Work both provide for the joint formulation of judicial interpretations by the Supreme People's Court and the Supreme People's Procuratorate when an issue involves both judicial and prosecutorial work.<sup>396</sup>

7.422 The United States submits that, in light of the above, the Judicial Interpretations at issue in this dispute are binding and have the force of law.<sup>397</sup>

7.423 China submits that the Judicial Interpretations are issued "in order to ensure a uniform understanding and application of the law".<sup>398</sup> China does not disagree with the United States' description of the legal basis and binding nature of the Judicial Interpretations at issue as set out in the United States' first written submission.<sup>399</sup> China confirms that if an illegal act does not meet one of the pertinent thresholds set out in the Judicial Interpretations at issue, prosecution of that act is legally impossible.<sup>400</sup>

7.424 In light of the above, the Panel finds that the Judicial Interpretations of the Articles of the Criminal Law at issue are binding and have the force of law.

(c) Thresholds under the Criminal Law in general

7.425 China informs the Panel that it employs thresholds across a range of commercial crimes, reflecting the significance of various illegal acts for overall public and economic order and China's prioritization of criminal enforcement, prosecution and judicial resources. China submits that the criminal thresholds for counterfeiting and piracy are reasonable and appropriate in the context of this legal structure and the other laws on commercial crimes.<sup>401</sup>

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<sup>394</sup> Provisions of the Supreme People's Court on Judicial Interpretation Work, Article 5, 法发 [2007] No. 12 in Exhibit US-14.

<sup>395</sup> Provisions of the Supreme People's Procuratorate on Judicial Interpretation Work, Article 5, 高检发研字 [2006] No. 4 in Exhibit US-15.

<sup>396</sup> Provisions of the Supreme People's Court on Judicial Interpretation Work (referred to in note 394 above), Article 7, and Provisions of the Supreme People's Procuratorate on Judicial Interpretation Work (referred to in note 395 above), Article 21.

<sup>397</sup> United States' first written submission, para. 24.

<sup>398</sup> China's first written submission, para. 22.

<sup>399</sup> China's response to Question No. 10, referencing paras 20-24 of that submission.

<sup>400</sup> China's response to Question No. 55.

<sup>401</sup> China's first written submission, paras 122-127.

7.426 The United States responds that what China chooses to do with its domestic non-IPR criminal thresholds has no bearing on the Panel's assessment of whether China meets its international obligations under the first sentence of Article 61 of the TRIPS Agreement.<sup>402</sup>

7.427 The Panel observes that Part One of the Criminal Law sets out general provisions. Within Part One, Chapter II, Section 1 provides for "Crimes and Criminal Responsibility". Article 13 defines a crime and may be translated *in fine* as follows:

"However, if the circumstances are obviously minor and the harm done is not serious, the act shall not be considered a crime."<sup>403</sup>

7.428 China submits that, throughout the Criminal Law, the definitions of various crimes are accompanied by rules for determining at what point the particular proscribed conduct becomes so serious as to constitute a crime.<sup>404</sup> These are collated and issued in Prosecution Standards. In response to a question from the Panel, China indicated that most substantive provisions in Chapter III on economic crimes, Chapter V on property violation and Chapter VI, Section 9 on producing, selling and disseminating pornographic materials<sup>405</sup> are also subject to specific thresholds, such as those applicable to Articles 213, 214, 215, 217 and 218 of the Criminal Law that are at issue in this dispute.<sup>406</sup>

7.429 The Panel notes China's acknowledgement that a total of 11 crimes out of 117 crimes set out in these relevant Parts and this relevant Section of the Criminal Law are not subject to any specific threshold.<sup>407</sup> Therefore, whilst China may for internal policy reasons frequently use thresholds to define the point at which many classes of illegal act are considered serious enough to be criminalized, China's legal structure is capable of criminalizing certain acts without recourse to thresholds.

(d) Thresholds for conviction or aggravation

7.430 The Panel notes that some thresholds in the Criminal Law set minimum requirements for conviction ("conviction thresholds") whilst others set minimum requirements for higher penalties ("aggravation thresholds"). Most of the Articles at issue in this dispute include both. The conviction thresholds comprise "serious circumstances" in Articles 213 and 215, "relatively large amount of sales" in Article 214, "relatively large amount of illegal gains" or "other serious circumstances" in Article 217 and "huge amount of sales" in Article 218. The aggravation thresholds comprise "especially serious circumstances" in Articles 213, 215 and 217 and "huge amount of sales" in Article 214.

7.431 The United States only challenges the conviction thresholds as these render prosecution impossible in the absence of certain criteria. Therefore, the Panel does not consider the aggravation thresholds further.

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<sup>402</sup> United States' rebuttal submission, paras 100-102.

<sup>403</sup> Exhibit CHN-1.

<sup>404</sup> China's first written submission, para. 121.

<sup>405</sup> Crimes under Part Two, Chapter VI, Section 9 of the Criminal Law were addressed together with copyright crimes under Articles 217 and 218 in Judicial Interpretation No. 30 [1998] (referred to in note 372 above).

<sup>406</sup> See China's response to Question No. 57.

<sup>407</sup> China's response to Question No. 57.

(e) General provisions on inchoate crimes

7.432 China refers to certain general provisions of the Criminal Law that it alleges apply to the crimes of infringing intellectual property rights. These include Article 22 on preparation for a crime, and Article 23 on attempted crime, which may trigger criminal prosecution and penalties.<sup>408</sup>

7.433 The United States replied that the extent to which these general provisions on inchoate crimes can address evidence of *potential* infringement is beside the point, as the thresholds rule out criminal liability based on evidence of *actual* infringement.<sup>409</sup> In response to a question, the United States notes that neither the Criminal Law, Judicial Interpretation No. 19 [2004] nor Judicial Interpretation No. 6 [2007] contains any specific provisions concerning the offences of preparation or attempt relating to the completed crimes of trademark counterfeiting and copyright piracy.<sup>410</sup>

7.434 The Panel observes that Part One, Chapter II, Section 2 of the Criminal Law sets out three inchoate crimes of preparation for a crime, criminal attempt and discontinuation of a crime.<sup>411</sup> Article 22 may be translated as follows:

"Preparation for a crime refers to the preparation of the instruments or the creation of the conditions for a crime.

An offender who prepares for a crime may, in comparison with one who completes the crime, be given a lighter or mitigated punishment or be exempted from punishment."<sup>412</sup>

7.435 Article 23 may be translated, relevantly, as follows:

"A criminal attempt refers to a case where an offender has already started to commit a crime but is prevented from completing it for reasons independent of his will.

An offender who attempts to commit a crime may, in comparison with one who completes the crime, be given a lighter or mitigated punishment."<sup>413</sup>

7.436 The Panel notes that each of these Articles contains provisions that appear to be of general application and that relate explicitly to "a crime" (犯罪). The Articles to which China refers contain no express limitation to certain specific provisions of the Criminal Law. They form part of Chapter II on "Crimes" found in Part One on "General Provisions", which also sets out the aim, basic principles and scope of application of the Criminal Law in Chapter I, provisions on punishments in Chapter III and the concrete application of punishments in Chapter IV. On their face, there is no reason to suppose that Articles 22 and 23 do not apply to the crimes of infringing intellectual property rights in Articles 213, 214, 215, 217 and 218 of the Criminal Law. This reading is confirmed by examples of judicial decisions submitted by China that show courts applying Articles 22 and 23 of the Criminal Law in cases of crimes of infringing intellectual property rights.<sup>414</sup>

7.437 The Panel also notes that China has referred to the offences of preparation for a crime and attempted crime to show that packaging and product components can be taken into account in

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<sup>408</sup> China's first written submission, paras 35-37; rebuttal submission, paras 36-41.

<sup>409</sup> United States' second oral statement, para. 34.

<sup>410</sup> United States' response to Question No. 8.

<sup>411</sup> The parties have not referred to Article 24 on discontinuation of a crime.

<sup>412</sup> Exhibit CHN-1.

<sup>413</sup> Exhibit CHN-1.

<sup>414</sup> The United States refers to these judicial decisions and appears to acknowledge that the Articles were applied in these cases: see United States' response to Question No. 8.

determining the availability of criminal procedures to enforce the substantive crimes of infringing intellectual property rights. However, the Panel notes that China has not alleged that the offences of preparation and attempt render activities falling below the thresholds in Articles 213 to 220 generally subject to criminal prosecution.

(f) General provisions on joint crimes

7.438 Japan, supported by the European Communities, argues that quantitative thresholds would not capture counterfeiting activities of limited value or smaller quantities which are on a "commercial scale" due to their professional organization or the systematic cooperation with other persons.<sup>415</sup> Mexico further submits that small scale activity is "clearly meaningful" as it contributes to the chain of infringement.<sup>416</sup>

7.439 In response to these third party submissions, China refers to Articles 25, 26 and 27 of the Criminal Law on joint liability, criminal groups and accomplices to show that the Criminal Law recognizes certain non-quantitative factors, such as evidence of collaboration between infringers.<sup>417</sup> China submits that they apply to the crimes of infringing intellectual property rights in Articles 213, 214, 215, 217 and 218 of the Criminal Law.<sup>418</sup>

7.440 The United States replies that this argument is of no consequence with respect to infringers that work alone. All the evidence demonstrates is that below-the-threshold activity could be captured if it existed as part of an above-the-threshold activity.<sup>419</sup>

7.441 The Panel observes that Part One, Chapter II, Section 3 of the Criminal Law provides for "Joint crimes". It sets out five provisions. Article 25 may be translated, relevantly, as follows:

"A joint crime refers to an intentional crime committed by two or more persons jointly. ..." <sup>420</sup>

7.442 Article 26 may be translated as follows:

"A principal criminal refers to any person who organizes and leads a criminal group in carrying out criminal activities or plays a principal role in a joint crime.

A criminal group refers to a relatively stable criminal organization formed by three or more persons for the purpose of committing crimes jointly.

Any ringleader who organizes or leads a criminal group shall be punished on the basis of all the crimes that the criminal group has committed.

Any principal criminal not included in paragraph 3 shall be punished on the basis of all the crimes that he participates in or that he organizes or directs." <sup>421</sup>

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<sup>415</sup> Japan's third party written submission, para. 17; European Communities' third party oral statement, para. 10.

<sup>416</sup> Mexico's third party oral statement, paras 6-7.

<sup>417</sup> China's rebuttal submission, paras 42-46.

<sup>418</sup> China's rebuttal submission, para. 33.

<sup>419</sup> United States' second oral statement, para. 35, referring to the application of the joint crime provision in one case (CHN-12), cited by China in its rebuttal submission, para. 44, and its response to Question No. 56.

<sup>420</sup> Exhibit CHN-1.

<sup>421</sup> Exhibit CHN-1.

7.443 Article 27 may be translated as follows:

"An accomplice refers to any person who plays a secondary or auxiliary role in a joint crime.

An accomplice shall be given a lighter or mitigated punishment or be exempted from punishment."<sup>422</sup>

7.444 The Panel observes that Articles 26 and 27 are limited to "joint crimes" which are defined by Article 25 as "intentional crimes". On their face, there is no reason to suppose that Articles 25, 26 and 27 do not apply to the crimes of infringing intellectual property rights in Articles 213, 214, 215, 217 and 218 of the Criminal Law. Several judicial decisions submitted by China show one or more of these Articles being cited in relation to Article 213.<sup>423</sup> The decisions show that the relevant factors were aggregated among several offenders in order to reach a criminal threshold.

7.445 China submitted that it may apply criminal procedures and penalties, on the basis of joint crimes and criminal group membership, to infringers that would not otherwise reach the criminal thresholds of the substantive criminal laws.<sup>424</sup> However, in response to a question, China confirmed that the numerical thresholds under Articles 213, 214, 215, 217 and 218 of the Criminal Law apply to joint crimes under Articles 25, 26 and 27 of the Criminal Law.<sup>425</sup>

7.446 Therefore, the Panel considers that the concept of joint crimes is relevant to the capacity of the Criminal Law to take into account an element of organization among different offenders. However, it does not alter the lack of criminal procedures and penalties for acts of infringement falling below the thresholds in Articles 213 to 220.

(g) Specific features of the thresholds for crimes of infringing intellectual property rights

(i) *Profit-making purpose*

7.447 The United States submits that the thresholds "all require proof of an intention to make a financial gain or profit".<sup>426</sup>

7.448 The Panel observes that, as regards the trademark offences, two of the thresholds under Article 213 of the Criminal Law, as interpreted by Article 1 of Judicial Interpretation No. 19 [2004], are set in terms of "illegal business operation volume" and "illegal gains" (i.e. amount of profits obtained<sup>427</sup>). Article 214 of the Criminal Law applies to the act of selling, and the corresponding threshold in Article 2 of Judicial Interpretation No. 19 [2004] is set in terms of "amount of sales". These all imply a purpose of obtaining financial gain or making profits. Article 215 of the Criminal Law does not expressly refer to a profit-making purpose.

7.449 As regards the copyright offences, both Articles 217 and 218 of the Criminal Law expressly refer to acts carried out for "the purpose of making profits". This language is reiterated in the corresponding interpretations in Articles 5 and 6 of Judicial Interpretation No. 19 [2004] and Article 1 of Judicial Interpretation No. 6 [2007].

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<sup>422</sup> Exhibit CHN-1.

<sup>423</sup> Exhibits CHN-4, CHN-6, CHN-9, CHN-12, CHN-13 and CHN-16.

<sup>424</sup> China's rebuttal submission, para. 46.

<sup>425</sup> China's response to Question No. 56.

<sup>426</sup> United States' response to Question No. 59.

<sup>427</sup> See paragraph 7.402 above.

7.450 Therefore, Articles 213, 214, 217 and 218 of the Criminal Law take account of at least one qualitative factor in conjunction with the numerical thresholds. In this dispute, the United States does not challenge this aspect of the measure.<sup>428</sup>

(ii) *Alternative thresholds*

7.451 The parties agree that the thresholds refer to a range of different factors, comprising illegal business operation volume, amount of illegal gains (or profits), amount of sales, number of "copies" and "other serious circumstances". The first three are, by their own terms, indicators of business activity and are either expressly, or impliedly, linked to selling, in other words, commercial activity. The first four are all expressed in numerical terms.

7.452 China emphasizes that the multiple standards set forth in each of Articles 213, 215 and 217 of the Criminal Law are all alternatives.<sup>429</sup> The United States agrees and claims that application of any or all of the alternative thresholds leaves many acts of commercial scale piracy and counterfeiting immune from criminal prosecution or conviction.<sup>430</sup>

7.453 The Panel observes that Articles 213 and 215 of the Criminal Law each contain a single threshold. However, these are interpreted by Articles 1 and 3 of Judicial Interpretation No. 19 [2004] in terms of a series of distinct circumstances. It is clear from the text of Articles 1 and 3 that each of these circumstances applies in the alternative as Articles 1 and 3 each provide that the conviction threshold under the relevant Article of the Criminal Law shall be deemed satisfied in "any of the following circumstances".

7.454 The Panel observes that Article 217 of the Criminal Law contains two conviction thresholds namely, "the amount of illegal gains" and "other serious circumstances". The text of Article 217 makes it clear that these are alternatives to each other by the use of the word "or". Both of these thresholds are interpreted by Article 5 of Judicial Interpretation No. 19 [2004]: the former in terms of a numerical amount and the latter in terms of a series of distinct circumstances. It is clear from the text of Article 5 that each of these circumstances applies in the alternative as Article 5 provides that the conviction threshold of "other serious circumstances" under Article 217 of the Criminal Law shall be deemed satisfied in "any of the following circumstances". Satisfaction of any one of those circumstances, or "the amount of illegal gains" threshold, shall be deemed to satisfy the relevant conviction threshold.

7.455 This means, for example, that the use of a counterfeit trademark where the illegal business operation volume is, say, ¥40,000 (i.e. below the threshold of ¥50,000 applicable under Article 213 of the Criminal Law) is not exempt from criminal prosecution unless the amount of illegal gains, the number of registered trademarks involved in the offence, and other circumstances all fail to fulfil the other applicable thresholds. However, where an act of infringement falls below all the applicable thresholds, criminal prosecution and penalties are not available.

7.456 It is not disputed that the crimes of selling under Articles 214 and 218 of the Criminal Law each contain only one conviction threshold. Therefore, those thresholds do not apply as alternatives.

(iii) *Cumulative calculation over time*

7.457 China submits that the thresholds are calculated over a prolonged period of time. This is reflected in the general limitation period for crimes of a continuous nature, and the specific provision

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<sup>428</sup> See paragraphs 7.659 and 7.660 below.

<sup>429</sup> China's first written submission, paras 33-34.

<sup>430</sup> United States' rebuttal submission, para. 77.

on cumulative calculation in Article 12(2) of Judicial Interpretation No. 19 [2004]. China asserts that this principle also applies to thresholds in terms of numbers of copies. Therefore, the thresholds for crimes infringing intellectual property rights can be calculated over the entire duration of the infringing activity.<sup>431</sup>

7.458 The United States notes that Article 12(2) of Judicial Interpretation No. 19 [2004] is subject to a condition, namely, that no administrative penalty or criminal punishment has been imposed.<sup>432</sup> China responds that administrative enforcement forestalls the commission of the crime.<sup>433</sup>

7.459 The Panel observes that Part One, Chapter IV, Section 8 of the Criminal Law sets out limitation periods for the prosecution of crimes. Article 87 provides for limitation periods calculated according to the maximum punishment for the relevant crime, of which the shortest period is five years. Article 89 of the Criminal Law provides that the limitation period for a criminal act of a continual or continuous nature shall be counted from the date the criminal act is *terminated*.<sup>434</sup>

7.460 The Panel also notes that Article 12(2) of Judicial Interpretation No. 19 [2004] may be translated as follows:

"In the case of infringement committed for [*sic*] more than once for which no administrative penalty or criminal punishment has been imposed, the illegal business operation volume, the amount of illegal gains, or the amount of sales shall be calculated accumulatively."<sup>435</sup>

7.461 These provisions show that the thresholds may take into account multiple acts of infringement, and not simply the income, profits, sales or number of copies in a single transaction or at a single point in time. This point is confirmed by examples of judicial decisions submitted by China showing that, when calculating whether thresholds had been met, courts have taken into account infringements during periods of up to five years.<sup>436</sup> An administrative penalty for a particular act of infringement excludes that act from the cumulative calculation of the "illegal business operation volume", "the amount of illegal gains", or "the amount of sales" thresholds and, hence, from criminal procedures and penalties.

(iv) *Calculation of illegal business operation volume – goods*

7.462 China submits that the calculation of "illegal business operation volume" thresholds is not limited to goods in a single location at the same point in time. Rather, the threshold covers all infringing goods associated with the infringer, even those no longer in the infringer's possession.<sup>437</sup>

7.463 The United States acknowledges that, in certain circumstances, the definition of "illegal business operation volume" appears to permit an infringer's goods on different premises to be taken into account in calculation of the threshold.<sup>438</sup>

7.464 The Panel observes that three conviction thresholds under Articles 213, 215 and 217 of the Criminal Law are set in terms of "illegal business operation volume". The definition of "illegal

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<sup>431</sup> China's first written submission, paras 30-32; rebuttal submission, paras 26-27.

<sup>432</sup> United States' response to Question No. 2(a).

<sup>433</sup> China's rebuttal submission, paras 28-29.

<sup>434</sup> Exhibit CHN-1.

<sup>435</sup> Mutually agreed translation no. 3.

<sup>436</sup> Exhibits CHN-4, CHN-13 and CHN-14.

<sup>437</sup> China's first written submission, paras 23-24.

<sup>438</sup> United States' response to Question No. 2(a).

business operation volume" in Article 12(1) of Judicial Interpretation No. 19 [2004]<sup>439</sup> refers to infringing products "manufactured, stored, transported or sold" during the course of commission of the act of infringing intellectual property rights. On its face, this does not restrict the calculation of these thresholds to the value of goods seized in a single place at the same point in time. This interpretation is confirmed by examples of judicial decisions submitted by China showing that courts have taken into account the value of goods already sold<sup>440</sup>, as well as of goods seized at different locations<sup>441</sup> when calculating the illegal business operation volume.

(v) *Calculation of illegal business operation volume – price*

7.465 The United States claimed that the calculation methodology required for "illegal business operation volume" was based on the prices of infringing goods, not the value of legitimate non-infringing goods.<sup>442</sup>

7.466 China responded that the calculation methodology is based on the actual, labelled or average sales price of the infringing goods but, where this cannot be determined, the price will be calculated based on the average market price of the infringed, i.e. genuine, goods.<sup>443</sup> In response to a question from the Panel, China agreed that the price of the genuine goods is used as a last resort.<sup>444</sup>

7.467 The Panel observes that three conviction thresholds under Articles 213, 215 and 217 of the Criminal Law are set in terms of "illegal business operation volume", which can be calculated by alternative methods. Ultimately, the parties agree that, in accordance with the definition of "illegal business operation volume" in Article 12(1) of Judicial Interpretation No. 19 [2004]<sup>445</sup>, the primary method of calculation of those thresholds is based on the actual price at which *infringing* goods were sold or labelled or, if unsold, the average actual sales price of the *infringing* products as verified. It is only where there is no labelled price or the actual sales price is unable to be verified that the illegal business operation volume is calculated according to the "middle" market price of the *infringed* products. In other words, the threshold primarily relates to the value of the counterfeit trademark or copyright infringing goods but may, as a last resort, relate to the value of the genuine products.

7.468 It is not disputed that the value of the counterfeit trademark goods or copyright infringing goods will be less than the value of the corresponding genuine goods. This has the effect of making the illegal business operation threshold harder to satisfy in those cases where the price of the genuine goods is not used. The number of cases that will fall below the thresholds is therefore greater than if the price of the infringing goods is used in all cases.

(vi) *Number of goods and prices*

7.469 China also submits that the illegal business operation threshold, in particular, is a flexible standard in its own right because it takes into account both the number and the value of infringing articles.<sup>446</sup> The United States does not comment.

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<sup>439</sup> Set out at paragraph 7.401 above.

<sup>440</sup> Exhibits CHN-4, CHN-5 and CHN-6.

<sup>441</sup> Exhibit CHN-7.

<sup>442</sup> United States' first written submission, para. 119, relying on a translation in Exhibit US-2 that referred *in fine* to "products produced by infringing on intellectual property rights" rather than "the infringed products".

<sup>443</sup> China's first written submission, para. 28.

<sup>444</sup> China's response to Question No. 2(c).

<sup>445</sup> Set out at paragraph 7.401 above.

<sup>446</sup> China's rebuttal submission, paras 23-24.

7.470 The Panel observes that, in accordance with the definition of "illegal business operation volume" in Article 12(1) of Judicial Interpretation No. 19 [2004]<sup>447</sup>, these thresholds are calculated in terms of the price of goods. Naturally, the number of goods required to meet the threshold is inversely proportional to the value of those goods. Therefore, the threshold is flexible enough to capture a small number of high-value goods or a large number of low-value goods. However, where the number of goods multiplied by the value of the goods is less than the threshold and not captured by any alternative applicable threshold, no criminal procedures and penalties will apply.

(vii) *Residual thresholds*

7.471 The parties initially did not address another threshold, that of "other serious circumstances" applicable under Articles 213, 215 and 217 of the Criminal Law.

7.472 In response to a question from the Panel for clarification of the meaning of these thresholds, the United States noted a case in which a prosecutor had invoked the similarly undefined aggravation threshold of "other especially serious circumstances" under Article 1 of Judicial Interpretation No. 19 [2004]. That prosecutor had unsuccessfully cited "serious effects in both domestic and international society".<sup>448</sup>

7.473 In response to the same question, China explained that the inclusion of "other serious circumstances" was a legislative device that preserves legal flexibility for courts and for the future development of laws. The provisions allows a court to determine that a particular act, while not meeting the other defined thresholds, is comparable and equivalent to those thresholds and therefore deserves to be subject to criminal penalties. China was unable in the time available to provide specific examples of cases in which this threshold had been used.<sup>449</sup>

7.474 The Panel observes that, on the face of the measures at issue, one of the thresholds applicable to three crimes infringing intellectual property rights is a residual category of "other serious circumstances". In the case of Articles 213 and 215 of the Criminal Law, this threshold only appears in the text of Judicial Interpretation No. 19 [2004]. In the case of Article 217 of the Criminal Law, this threshold actually appears in the text of the Article itself, but is later defined in terms of two specific thresholds plus an identically worded residual category of "other serious circumstances". This bears out China's explanation that this threshold is a legislative device that allows for the future development of laws. However, it is not alleged that any other thresholds have yet been devised beyond those set out in this Report.

7.475 Moreover, it is not alleged that the courts or prosecutors would treat all infringing acts that fall below the numerical thresholds as criminal acts by virtue of this residual threshold. China confirms that if an illegal act does not meet one of the pertinent thresholds set out in the Judicial Interpretations at issue, prosecution of that act is legally impossible.<sup>450</sup> China also confirms that these residual thresholds apply to other acts that are "comparable and equivalent" to the defined thresholds. Therefore, these residual thresholds do not significantly alter the legal position but rather help define the class of trademark- and copyright-infringing acts that are not treated as criminal.

(viii) *Administrative enforcement*

7.476 China draws the Panel's attention to its system of administrative enforcement of intellectual property infringement that operates separately from its criminal enforcement system. It informs the

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<sup>447</sup> Set out at paragraph 7.401 above.

<sup>448</sup> United States' response to Question No. 9, citing Exhibit US-61.

<sup>449</sup> China's response to Questions Nos. 9 and 55; rebuttal submission, para. 22.

<sup>450</sup> See paragraphs 7.423 and 7.455 above.

Panel that in China infringement on *any scale* is subject to administrative enforcement. Public security authorities tend to focus more on infringement above the criminal thresholds, and copyright and commerce administrative authorities are more likely to target low-scale infringement.<sup>451</sup>

7.477 The United States responds that only criminal procedures and penalties can fulfil the obligations in Article 61 of the TRIPS Agreement. Administrative enforcement is not a substitute for criminal enforcement.<sup>452</sup>

7.478 The Panel notes that administrative sanctions, including fines, are available for intellectual property infringement falling below the criminal thresholds in China. Therefore, the thresholds do not create a "safe harbour". However, neither party to the dispute<sup>453</sup> argues that administrative enforcement may fulfil the obligations on criminal procedures and remedies set out in Article 61 of the TRIPS Agreement. Therefore, the Panel does not consider this issue further.

(h) Conclusion regarding construction of the measures at issue

7.479 For the above reasons, the Panel concludes that, whilst the structure of the thresholds and the method of calculation of some of them can take account of various circumstances, acts of trademark and copyright infringement falling below *all* the applicable thresholds are not subject to criminal procedures and penalties. The Panel will now consider whether any of those acts of infringement constitute "wilful trademark counterfeiting or copyright piracy on a commercial scale" within the meaning of Article 61 of the TRIPS Agreement.

### **3. Claim under the first sentence of Article 61 of the TRIPS Agreement**

(a) Main arguments of the parties

7.480 The United States submits that the concept of "commercial scale" extends both to those who engage in commercial activities in order to make a "financial return" in the marketplace, and who are, by definition, therefore operating on a commercial scale, as well as to those whose actions, regardless of motive or purpose, are of a sufficient extent or magnitude to qualify as "commercial scale" in the relevant market.<sup>454</sup> Later, it clarified that the concept of "commercial scale" referred to counterfeiting or piracy that reach a certain extent or magnitude with a link to the marketplace. Whether a particular counterfeiting or piracy activity is "on a commercial scale" will depend on the facts and circumstances surrounding that activity. Relevant factors would include the market for the infringed goods, the object of the infringement, the value of the infringed goods, the means of producing the infringed goods, and the impact of the infringement on the right holder.<sup>455</sup> Some activity would be so trivial or of a *de minimis* character so as *not* to be "on a commercial scale" in some circumstances, such as occasional infringing acts of a purely personal nature carried out by consumers, or the sale of trivial volumes for trivial amounts (i.e., the sale of one copy for ¥1) unless there are circumstances indicating to the contrary.<sup>456</sup>

7.481 China responds that "commercial scale" refers to a significant magnitude of infringement activity. This is a broad standard, subject to national discretion and local conditions.<sup>457</sup> The United States fails to interpret "commercial scale" as a single term and its interpretation reads the word

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<sup>451</sup> China's first written submission, paras 39-43.

<sup>452</sup> United States' rebuttal submission, paras 116-119.

<sup>453</sup> Contrast Brazil's third party written submission, paras 39-42.

<sup>454</sup> United States' first written submission, para. 110.

<sup>455</sup> United States' response to Question No. 59.

<sup>456</sup> United States' response to Question No. 60.

<sup>457</sup> China's first written submission, paras 64 and 117; China's first oral statement, para. 30.

"scale" completely out of the definition.<sup>458</sup> The context of Articles 1.1 and 41.5 of the TRIPS Agreement shows that Members retain considerable discretion with respect to law enforcement, and that the ability to define the standards of Article 61 is reserved for Members.<sup>459</sup> Later, it clarified that while these Articles did not provide an absolute defence against the substantive obligation of Article 61, they did provide relevant context and counselled strongly against interpretations of Article 61 in ways that would be inconsistent with China's legal system and would require the diversion of enforcement resources.<sup>460</sup> The negotiating record of the TRIPS Agreement, as well as subsequent actions of Members show that they understood "commercial scale" to impose only a high and broad standard which only covered significant infringement activity.<sup>461</sup>

7.482 The United States claims that China's criminal thresholds require authorities to disregard other indicia of commercial scale counterfeiting and piracy from physical evidence to consideration of the impact the piracy or counterfeiting has on the commercial marketplace and by extension, right holders.<sup>462</sup> The United States argues that a range of quantitative and qualitative factors should be taken into account to ensure all "commercial scale" activities are subject to Article 61.<sup>463</sup>

7.483 China responds that Chinese courts do consider semi-finished or unfinished products, and that these are evidence of preparation and attempt, as well as of substantive crimes.<sup>464</sup> Evidentiary procedures and impact on the right holder are irrelevant to Article 61 of the TRIPS Agreement.<sup>465</sup> The Criminal Law also addresses organizational elements of crimes in provisions on vicarious liability.<sup>466</sup>

(b) Main arguments of third parties

7.484 Argentina argues that China's measures do not appear to be inconsistent with Article 61 of the TRIPS Agreement, as Article 1.1 provided China with the flexibility to implement enforcement provisions in a way compatible with its existing constitutional and regulatory framework.<sup>467</sup>

7.485 Australia argues that "commercial scale" encompasses any act or series of acts of trademark counterfeiting or copyright piracy that adversely affects the financial rewards available to a right holder within a Member territory and that the ordinary meaning of the word "scale" incorporates the notion of a comparative assessment. Whether an individual case is on a commercial scale can only be determined case-by-case, taking account of all relevant circumstances, including the potential impact of digitally-based technologies.<sup>468</sup> This can include infringement activities with no financial advantage for the infringer, which nevertheless have substantial prejudicial impact on the right holder because of the availability of infringing material on digital networks.<sup>469</sup>

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<sup>458</sup> China's first written submission, paras 67-71, China's first oral statement, paras 26-27.

<sup>459</sup> China's first written submission, paras 90, 92 and 98-101.

<sup>460</sup> China's second written submission, paras 102-107.

<sup>461</sup> China's first written submission, paras 104-108 and 109-116; China's second written submission, paras 116-134.

<sup>462</sup> United States' first written submission, paras 143-150.

<sup>463</sup> United States' rebuttal submission, para. 38.

<sup>464</sup> China's first written submission paras 35-37; rebuttal submission, para. 32.

<sup>465</sup> China's first written submission, paras 141 and 139.

<sup>466</sup> China's rebuttal submission, paras 42-46.

<sup>467</sup> Argentina's third party written submission, paras 20 and 23.

<sup>468</sup> Australia's third party written submission, paras 18-19, supporting the definition suggested in the United States' first written submission, para. 110.

<sup>469</sup> Australia's third party written submission, para. 16, Australia's response to Third Party Question No. 6.

7.486 Brazil argues that an interpretation of "commercial scale" must give meaning to both terms in this expression, which combine "order of magnitude" with the purpose of obtaining financial gains. Therefore, Brazil considers that Article 61 establishes a two-pronged minimum standard that requires Members to provide for criminal procedures and penalties at least for wilful trademark and copyright infringements that involve profit-seeking motivation and significant amounts of infringing goods.<sup>470</sup>

7.487 Canada argues that China's authorities are precluded from applying criminal sanctions in many cases of wilful trademark counterfeiting or copyright piracy on a commercial scale because China's thresholds are arbitrary, too high and inflexible. The concept of "commercial scale" includes different factors. It relates to more than just industrial production and includes cases of wilful trademark counterfeiting and copyright piracy undertaken on sufficient scale to constitute the pursuit of profit or the carrying out of a business. This is a qualitative test and requires discretion in order to consider the circumstances of a given case. While negligible volumes of counterfeit would probably not qualify, the wilful reproduction of hundreds of pirated copies for the equivalent value of thousands of dollars in sales revenue would, by any objective measure, be infringing on a commercial scale. This would be especially true in China where annual GDP per capita is just US\$2,500 and 57 million people earn less than US\$125 per year. While Article 61 does not require prosecution of each case of wilful trademark counterfeiting and copyright piracy on a commercial scale, it does require Members to be in a position to do so, when circumstances merit the exercise of prosecutorial discretion.<sup>471</sup>

7.488 The European Communities argues that Article 61 singles out two types of infringements because they have a particular potential of harming right holders. Therefore, "on a commercial scale" must comprise all activities with a particular potential for harm which results from them pertaining to a business or profit generation. Quantitative thresholds alone are not enough to capture aspects of professional organization or systematic cooperation. In order to capture all infringements on a commercial scale, criminal enforcement authorities must be able to take into account additional factors such as indications of business organization or profit orientation of an activity.<sup>472</sup> The European Communities further argues that, because it provides for criminal procedures and penalties "to be applied", the first sentence of Article 61 obliges Members not just to criminalize, but also to prosecute the activities mentioned therein.<sup>473</sup>

7.489 Japan argues that while quantitative thresholds could identify many instances of "commercial scale" counterfeiting they would not capture counterfeiting activities of limited value or smaller quantities which are on a "commercial scale" due to additional circumstances, such as their professional organization or easy repetition. Mere quantification of "commercial scale" does not capture all instances of commercial scale counterfeiting, and additional qualitative elements need to be taken into account in order to consider such organizational characteristics of an activity.<sup>474</sup>

7.490 Korea argues that China's thresholds arbitrarily carve out certain IPR crimes from the possibility of criminal sanction and are therefore inconsistent with the TRIPS Agreement. "Commercial scale" represents a level of magnitude that is realized by operating or maintaining a business activity, large or small, for the purpose of gaining financial return through IPR infringement in a somewhat systematic fashion. Therefore, anybody engaging in a business activity by infringing

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<sup>470</sup> Brazil's third party written submission, paras 35-38

<sup>471</sup> Canada's third party written submission, paras 4-8 and 11.

<sup>472</sup> European Communities' third party oral statement, paras 10 and 14.

<sup>473</sup> European Communities' third party written submission, para. 10-11; European Communities' response to Third Party Question No. 10,

<sup>474</sup> Japan's third party written submission, paras 17 and 30; Japan's third party oral statement, para. 13.

IPRs and realizing a financial return, regardless of the alleged amount at issue, should be regarded as violating IPRs on a "commercial scale".<sup>475</sup>

7.491 Mexico submits that the concept of "commercial scale" encompasses activities that go beyond casual or occasional infringements that are not made for the purpose of generating revenue. In that context, the word "scale" is not necessarily bound to conditions of magnitude, but alternatively to that of quality. Mexico further submits that small scale activity is "clearly meaningful" as it contributes to the chain of infringement.<sup>476</sup>

7.492 Chinese Taipei submits that "commercial scale" is an abstract legal concept that involves multiple factors of local circumstances, such as nature of the infringed rights, value and price in the market, motive and purpose of act, method and scale of infringement, damage caused, profit gained, cultural background, advancement of modern technology and living standards, that need to be considered on a case-by-case basis.<sup>477</sup>

7.493 Thailand argues that, as there is no definition of "commercial scale" in the TRIPS Agreement, this constitutes a built-in flexibility recognizing the different legal systems of Members. Every Member can adopt the interpretation it deems appropriate.<sup>478</sup>

(c) Consideration by the Panel

(i) *Nature of the claim*

7.494 The United States' claim relates to cases of wilful trademark counterfeiting and copyright piracy in respect of which China does not provide for criminal procedures and penalties to be applied but which the United States claims are "on a commercial scale".<sup>479</sup> The claim is based on two alleged "fundamental problems" referred to in this Report as the two limbs of this claim. The first limb concerns the level and method of calculation of the thresholds. By specifying certain levels, the thresholds allegedly eliminate whole classes of counterfeiting and piracy from risk of criminal prosecution and conviction.<sup>480</sup> The second limb concerns the limited set of numerical tests in the thresholds. By focussing solely on these tests, the thresholds allegedly require law enforcement officials to disregard other indicia of counterfeiting and piracy.<sup>481</sup>

7.495 The Panel notes that the first limb of the claim addresses the numbers specified in the numerical tests, and the way in which some of them are calculated, in order to show that the thresholds are too high. These are quantitative issues. The second limb addresses certain factors that the numerical tests do not take into account. These are qualitative issues. Neither limb is a broad claim that numerical thresholds cannot capture all cases "on a commercial scale". In response to the Panel's requests for clarification of the claim after both the first and the second substantive meetings, the United States clarified that it did not object to the use of numerical thresholds *per se*.<sup>482</sup>

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<sup>475</sup> Korea's third party written submission, paras 20 and 27; Korea's third party oral statement, para. 6.

<sup>476</sup> Mexico's third party written submission, paras 10; Mexico's third party oral statement, paras 6-7.

<sup>477</sup> Chinese Taipei's third party written submission, para. 21; Chinese Taipei's third party oral statement, para. 11.

<sup>478</sup> Thailand's third party oral statement, para. 3.

<sup>479</sup> United States' first written submission, paras 116 and 143.

<sup>480</sup> United States' first written submission, para. 112; rebuttal submission, para. 74.

<sup>481</sup> United States' first oral statement, para. 36; first oral statement (closing statement), para. 16.

<sup>482</sup> United States' responses to Questions Nos. 25 and 54. It seems pertinent to note that during the negotiations of the terms of China's accession to the WTO, some members of the Working Party took a similar position. In particular, they expressed concerns that the monetary thresholds were very high and seldom met. They considered that those thresholds should be lowered: see the Working Party Report, para. 304. China

Accordingly, the Panel is not asked to consider whether numerical thresholds, as a matter of principle, can implement an obligation in terms of cases "on a commercial scale".

7.496 Therefore, in its assessment of this claim, the Panel will proceed as follows:

- (a) with respect to the first limb of the claim, the Panel will assess whether the *levels* in China's thresholds are too high to capture all cases on a commercial scale; and
- (b) with respect to the second limb of the claim, the Panel will assess whether the *other factors* raised by the United States can be taken into account by China's thresholds to capture all cases on a commercial scale and, if not, whether this is a TRIPS requirement.

(ii) *Procedural issues*

7.497 China argues that the United States bears "a significantly higher burden [of proof] than it would normally encounter" because this claim concerns criminal law matters. China argues that the Panel should treat sovereign jurisdiction over police powers as a powerful default norm, departure from which can be authorized only in light of explicit and unequivocal consent of State parties.<sup>483</sup> China later clarified that it was not referring to a factual burden of proof but rather to the inability of the United States to provide the evidence to support its legal interpretation of Article 61 of the TRIPS Agreement.<sup>484</sup> China also argues for the application of the "interpretative canon" of *in dubio mitius* which, it submits, has a particular justification in the realm of criminal law.<sup>485</sup>

7.498 The United States responds that the fact that Article 61 of the TRIPS Agreement touches on criminal law does not change the provisions of Article 3.2 of the DSU or the customary rules of treaty interpretation reflected in the Vienna Convention on the Law of Treaties ("Vienna Convention").<sup>486</sup> In this dispute, the meaning of "commercial scale" is reached through the general rule of interpretation in Article 31 of the Vienna Convention. There is no "doubt" which is a precondition of reliance on the concept of *in dubio mitius*.<sup>487</sup>

7.499 The Panel notes that this claim is brought under Article 61 of the TRIPS Agreement, which concerns criminal procedures and penalties.<sup>488</sup> Article 64.1 of that Agreement provides that:

"The provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding shall apply to consultations and the settlement of disputes under this Agreement except as otherwise specifically provided herein."

7.500 The application of the rules and procedures of the DSU to the settlement of disputes under the TRIPS Agreement is confirmed by Article 1.1 of the DSU, in conjunction with Appendix 1 of the DSU which lists the TRIPS Agreement as a "covered agreement". In accordance with Article 3.2 of the DSU, the Panel applies "the customary rules of interpretation of public international law" to its task of interpreting the TRIPS Agreement in this dispute. The general rule of interpretation,

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subsequently reduced certain thresholds with the adoption of Judicial Interpretation No. 19 [2004]: see United States' first written submission, para. 27.

<sup>483</sup> China's first written submission, paras 49-59.

<sup>484</sup> China's first oral statement (closing statement), paras 4-7.

<sup>485</sup> China's rebuttal submission, paras 51-56.

<sup>486</sup> United States' rebuttal submission, paras 63-67.

<sup>487</sup> United States' rebuttal submission, para. 68.

<sup>488</sup> Despite use of the word "remedies" in the second and third sentences, it seems clear that criminal sanctions are "penalties".

expressed in Article 31 of the Vienna Convention, and the rules on supplementary means of interpretation in Article 32 of the Vienna Convention, have attained the status of rules of customary or general international law.<sup>489</sup> The Panel will apply the general rule of interpretation and, to the extent warranted, supplementary means of interpretation. The Panel is mindful that Article 3.2 of the DSU *also* provides that "recommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements".

7.501 The Panel acknowledges the sensitive nature of criminal matters and attendant concerns regarding sovereignty. These concerns may be expected to find reflection in the text and scope of treaty obligations regarding such matters as negotiated by States and other Members.<sup>490</sup> Section 5 of Part III of the TRIPS Agreement, dedicated to criminal procedures and remedies, is considerably briefer and less detailed than the other Sections on enforcement in Part III. Brief as it is, the text of Section 5 also contains significant limitations and flexibilities. The customary rules of treaty interpretation oblige the treaty interpreter to take these limitations and flexibilities into account in interpreting the relevant provision.

(iii) *Nature of the obligation*

7.502 This claim is brought under the first sentence of Article 61 of the TRIPS Agreement. Article 61 constitutes the whole of Section 5 of Part III of that Agreement and provides as follows:

"SECTION 5: CRIMINAL PROCEDURES

*Article 61*

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. Remedies 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. In appropriate cases, remedies available shall also include the seizure, forfeiture and destruction of the infringing goods and of any materials and implements the predominant use of which has been in the commission of the offence. Members may provide for criminal procedures and penalties to be applied in other cases of infringement of intellectual property rights, in particular where they are committed wilfully and on a commercial scale."

7.503 The *first* sentence of this Article uses the word "shall", indicating that it is mandatory. This stands in contrast to the *fourth* sentence, which addresses the same issue with respect to other cases of infringement of intellectual property rights but uses the word "may", indicating that it is permissive. Unlike the *third* sentence, the first sentence contains no language such as "in appropriate cases" which might expressly introduce some margin of discretion. The terms of the first sentence of Article 61, read in context, impose an obligation.

7.504 This interpretation is confirmed by Article 41 of the TRIPS Agreement on "General Obligations", which is the first provision of Part III of the TRIPS Agreement and forms part of the context of Article 61. Article 41.1 provides, relevantly, as follows:

"Members shall ensure that enforcement procedures as specified in this Part are available under their law so as to permit effective action against any act of

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<sup>489</sup> Appellate Body Reports in *US – Gasoline*, at p. 17; and *Japan – Alcoholic Beverages II*, at p. 10.

<sup>490</sup> Articles 3, 4 and 41, in particular paragraph 4, of the TRIPS Agreement *inter alia* also apply to criminal enforcement procedures.

infringement of intellectual property rights covered by this Agreement, including expeditious remedies to prevent infringements and remedies which constitute a deterrent to further infringements."

7.505 In the Panel's view, the general obligation in Article 41.1 confirms that Article 61 contains obligations, as one of the specific provisions on enforcement procedures in Part III.

7.506 China submits that the first sentence of Article 61 cannot set forth a specific obligation because it provides for enforcement against certain types of infringement but neither the TRIPS Agreement nor the Berne Convention (1971) define what constitutes substantive infringement. Rather, they defer to national discretion to define the rights being infringed.<sup>491</sup>

7.507 The Panel agrees with China that the first sentence of Article 61 contains a number of terms that are not defined by the Agreement and that this can affect the proper interpretation of the provision. However, even though the first sentence does not use the term "infringement", it is important to note that Part II of the TRIPS Agreement, including the provisions of the Paris Convention (1967) incorporated by Article 2.1, and the provisions of the Berne Convention (1971) incorporated by Article 9.1, provide for minimum standards concerning the availability, scope and use of intellectual property rights that apply irrespective of national treatment. These provisions define the rights conferred by intellectual property and the circumstances in which those rights are infringed. Part III of the TRIPS Agreement provides for the enforcement of those rights, to varying degrees. Therefore, the Agreement contains substantive obligations that are not simply matters of national discretion.

7.508 China submits that Article 61 of the TRIPS Agreement is less specific than the Anti-Dumping Agreement and the Agreement on Subsidies and Countervailing Measures and lacks the clarity required to demonstrate a specific, concrete obligation. China also argues that the TRIPS Agreement lacks a provision such as Article 18.4 of the Anti-Dumping Agreement requiring Members to take steps to ensure the conformity of their laws with its provisions.<sup>492</sup>

7.509 The Panel agrees that the TRIPS Agreement differs from trade remedy agreements. However, the Panel will apply the usual rules of treaty interpretation to the terms used in the TRIPS Agreement and make its assessment on that basis in accordance with Article 11 of the DSU. The Panel draws China's attention to Article XVI:4 of the WTO Agreement which provides as follows:

"Each Member shall ensure the conformity of its laws, regulations and administrative procedures with its obligations as provided in the annexed Agreements."

7.510 The "annexed Agreements" include the TRIPS Agreement. Therefore, Members are obliged to ensure conformity of their respective laws with their respective obligations as provided in the TRIPS Agreement.

7.511 China submits that the third sentence of Article 1.1 of the TRIPS Agreement sets forth the overall context for interpreting the specificity of the standards in the TRIPS Agreement. It describes Article 1.1 as a specific "caveat" that establishes boundaries on obligations, specifically in the realm of enforcement.<sup>493</sup>

7.512 The Panel observes that Article 1.1 of the TRIPS Agreement provides as follows:

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<sup>491</sup> China's first written submission, paras 80-82.

<sup>492</sup> China's first written submission, paras 83-87.

<sup>493</sup> China's first written submission, paras 89-97.

"Members shall give effect to the provisions of this Agreement. Members may, but shall not be obliged to, implement in their law more extensive protection than is required by this Agreement, provided that such protection does not contravene the provisions of this Agreement. Members shall be free to determine the appropriate method of implementing the provisions of this Agreement within their own legal system and practice."

7.513 The first sentence of Article 1.1 sets out the basic obligation that Members "shall give effect" to the provisions of this Agreement. This means that the provisions of the Agreement are obligations where stated, and the first sentence of Article 61 so states. The second sentence of Article 1.1 clarifies that the provisions of the Agreement are minimum standards only, in that it gives Members the freedom to implement a higher standard, subject to a condition. The third sentence of Article 1.1 does not grant Members freedom to implement a lower standard, but rather grants freedom to determine the appropriate method of implementation of the provisions to which they are required to give effect under the first sentence. The Panel agrees that differences among Members' respective legal systems and practices tend to be more important in the area of enforcement. However, a coherent reading of the three sentences of Article 1.1 does not permit differences in domestic legal systems and practices to justify any derogation from the basic obligation to give effect to the provisions on enforcement.

7.514 Therefore, the standard of compliance with Article 61 is the minimum internationally agreed standard set out in that Article. The minimum standard in Article 61 does not defer to China's domestic practice on the definition of criminal liability and sanctions for other wrongful acts in areas not subject to international obligations under the TRIPS Agreement, unless it so states. For example, the second sentence refers to "crimes of a corresponding gravity" which might refer to domestic practice in other areas. However, the *first* sentence of Article 61 does not make any such reference.

7.515 For the above reasons, the Panel confirms its view at paragraphs 7.503 to 7.505 above that the first sentence of Article 61 of the TRIPS Agreement imposes an obligation. The Panel will now turn to the terms used in that provision, read in context and in light of the object and purpose of the Agreement, to determine the scope and content of that obligation.

(iv) *Scope of the obligation*

7.516 The terms of the obligation in the first sentence of Article 61 of the TRIPS Agreement are that Members shall "provide for criminal procedures and penalties to be applied". That obligation applies to "wilful trademark counterfeiting or copyright piracy on a commercial scale". Within that scope, there are no exceptions. The obligation applies to *all* acts of wilful trademark counterfeiting or copyright piracy on a commercial scale.

7.517 The Panel recalls its conclusion at paragraph 7.479 above that, in China, acts of trademark and copyright infringement falling below the applicable thresholds are not subject to criminal procedures and penalties. The issue that arises is whether any of those acts of infringement constitute "wilful trademark counterfeiting or copyright piracy on a commercial scale" within the meaning of the first sentence of Article 61. This requires the Panel to consider the interpretation of that phrase.

7.518 The Panel notes that the first sentence of Article 61 contains no fewer than four limitations on the obligation that it sets forth. These define the scope of the relevant obligation and are not exceptions. The first limitation is that the obligation applies to trademarks and copyright rather than to all intellectual property rights covered by the TRIPS Agreement. The fourth sentence of Article 61 gives Members the option to criminalize other infringements of intellectual property rights, in particular where they are committed wilfully and on a commercial scale. Despite the potential gravity of such infringements, Article 61 creates no obligation to criminalize them. This can be contrasted

with Sections 2 and 3 of Part III of the TRIPS Agreement, regarding civil and administrative procedures and remedies, which apply to any act of infringement of intellectual property rights covered by the Agreement. It can also be contrasted with Section 4 of Part III which attaches conditions to the option to apply its procedures to other infringements of intellectual property rights.<sup>494</sup>

7.519 The second limitation in the first sentence of Article 61, which is related to the first, is that it applies to counterfeiting and piracy rather than to all infringements of trademarks and copyright. This can also be contrasted with Sections 2 and 3 of Part III of the TRIPS Agreement. This limitation, like the first, indicates an intention to reduce the scope of the obligation. Indeed, the records of the negotiation of the TRIPS Agreement confirm that the term "infringements of trademarks and copyright" on a commercial scale was considered in the draft provision on criminal procedures but ultimately rejected.<sup>495</sup>

7.520 The terms "trademark counterfeiting" and "copyright piracy" are not defined in the TRIPS Agreement. They are distinct from the concepts of "trademark infringement" and "copyright infringement". They are similar to the terms "counterfeit trademark goods" and "pirated copyright goods" which are defined for the purposes of the TRIPS Agreement<sup>496</sup> in footnote 14 as follows:

"For the purposes of this Agreement:

(a) 'counterfeit trademark goods' shall mean any goods, including packaging, bearing without authorization a trademark which is identical to the trademark validly registered in respect of such goods, or which cannot be distinguished in its essential aspects from such a trademark, and which thereby infringes the rights of the owner of the trademark in question under the law of the country of importation;

(b) 'pirated copyright goods' shall mean any goods which are copies made without the consent of the right holder or person duly authorized by the right holder in the country of production and which are made directly or indirectly from an article where the making of that copy would have constituted an infringement of a copyright or a related right under the law of the country of importation."

7.521 The terms used in the first sentence of Article 61 denote classes of acts or activity whilst the terms used in footnote 14 denote classes of goods only. This reflects the fact that Article 61 provides for criminal enforcement against infringing acts whilst Section 4 of Part III (in which the terms defined in footnote 14 are used) provides for enforcement at the border against infringing goods. The definitions in footnote 14 also refer to the law of the country of "importation" whilst Article 61 relates to the law of the Member to which the obligation applies – generally speaking, the law of the Member where the infringing act occurs. Subject to these observations, the Panel considers that the definitions in footnote 14 are relevant in understanding the terms used in Article 61.

7.522 The United States does not claim that Articles 213, 214, 215, 217 and 218 of the Criminal Law fail to cover the full extent of the terms "trademark counterfeiting" and "copyright piracy" as

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<sup>494</sup> See paragraph 7.223 above.

<sup>495</sup> The Panel has recourse to this supplementary means of interpretation in accordance with Article 32 of the Vienna Convention in order to confirm the meaning resulting from the application of the general rule of interpretation in Article 31. See, for example, the Chairman's draft text of 23 July 1990 (document MTN.GNG/NG11/W/76).

<sup>496</sup> The terms "counterfeit trademark goods" and "pirated copyright goods" are used not only in Section 4 of Part III but also in Article 69 of the TRIPS Agreement. The identical term "counterfeit trademark goods" is also used in Article 46.

used in Article 61 of the TRIPS Agreement.<sup>497</sup> China does not contest that each of the thresholds established by the Criminal Law, in particular Articles 213, 214, 215, 217 and 218, applies to acts of "trademark counterfeiting" and "copyright piracy". Therefore, it is unnecessary for the Panel to interpret those terms in greater detail at this stage.

7.523 The third limitation in the first sentence of Article 61 is indicated by the word "wilful" that precedes the words "trademark counterfeiting or copyright piracy". This word functions as a qualifier indicating that trademark counterfeiting or copyright piracy is not subject to the obligation in the first sentence of Article 61 unless it is "wilful". This word, focussing on the infringer's intent, reflects the criminal nature of the enforcement procedures at issue. It is absent from Section 4 of Part III, even though that Section is similarly limited, as a minimum, to counterfeit trademark goods and pirated copyright goods. The penalties for criminal acts, such as imprisonment, fines and forfeiture of property, are relatively grave, as reflected in the second sentence of Article 61. There is no obligation to make such penalties available with respect to acts of infringement committed without the requisite intent.

7.524 The fourth limitation in the first sentence of Article 61 is indicated by the phrase "on a commercial scale" that follows the words "trademark counterfeiting or copyright piracy". This phrase, like the word "wilful", appears to qualify both "trademark counterfeiting" and "copyright piracy". The limitation to cases on a commercial scale, like the limitation to cases of wilfulness, stands in contrast to all other specific obligations on enforcement in Part III of the TRIPS Agreement.<sup>498</sup>

7.525 The principal interpretative point in dispute is the meaning of the phrase "on a commercial scale". This phrase functions in context as a qualifier, indicating that wilful trademark counterfeiting or copyright piracy is included in the scope of the obligation provided that it also satisfies the condition of being "on a commercial scale". Accordingly, certain acts of wilful trademark counterfeiting or copyright piracy are excluded from the scope of the first sentence of Article 61.

7.526 Despite the fact that trademark counterfeiting and copyright piracy infringe the rights of right holders, and despite the fact that they can be grave, the two qualifications of wilfulness and "on a commercial scale" indicate that Article 61 does not require Members to provide for criminal procedures and penalties to be applied to such counterfeiting and piracy *per se* unless they satisfy certain additional criteria. This is highlighted by the fourth sentence of Article 61, which allows Members to provide for criminal procedures and penalties to be applied in other cases of infringement, "in particular" where they are committed wilfully and on a commercial scale. This indicates that the negotiators considered cases of wilful infringement on a commercial scale to represent a subset of cases of infringement, comprising the graver cases. This is useful context for interpreting the first sentence of Article 61, even though it does not refer to "infringement" in general, because the first sentence refers to both "counterfeiting" and "piracy" and wilfulness and commercial scale, evidently to limit the cases of infringement in different ways. Therefore, the text of Article 61 indicates that it must not be assumed that the nature of counterfeiting and piracy *per se* is such that Members are obliged to provide for the application of *criminal* procedures and penalties.

7.527 This is consistent with the nature of the obligation, being a minimum standard, as expressly confirmed by the use of the words "at least" in the first sentence of Article 61 and, more generally, by the second sentence of Article 1.1, quoted at paragraph 7.512 above. Members may, and many do, criminalize other acts of trademark counterfeiting, other acts of copyright piracy, other acts of infringement of trademarks and copyright, and acts of infringement of other intellectual property rights such as patents, but there is no obligation to do so under the TRIPS Agreement.

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<sup>497</sup> United States' first written submission, paras 101 and 106.

<sup>498</sup> Section 4 contains a *de minimis* exception, discussed at paragraph 7.553 below.

7.528 Part III of the TRIPS Agreement distinguishes between the treatment of wilful trademark counterfeiting and copyright piracy on a commercial scale, on the one hand, and all other infringements of intellectual property rights, on the other hand, in that only the former are subject to an obligation regarding criminal procedures and penalties. This indicates the shared view of the negotiators that the former are the most blatant and egregious acts of infringement. This view must inform the interpretation of Article 61.

7.529 The Panel recalls its findings at paragraph 7.241 above as to the circumstances of conclusion of the TRIPS Agreement with respect to enforcement procedures. Whilst some of the pre-existing international intellectual property agreements or conventions contain provisions on the characteristics of enforcement mechanisms, it is striking that none of them create any specific minimum standard for criminal enforcement procedures.<sup>499</sup> Among the international intellectual property agreements with wide membership, Article 61 of the TRIPS Agreement is, in this sense, unique.

7.530 This reflects, in part, the fact that intellectual property rights are private rights, as recognized in the fourth recital of the Preamble to the TRIPS Agreement. In contrast, criminal procedures are designed to punish acts that transgress societal values. This is reflected in the use of the word "penalties" in Article 61.

7.531 Bearing in mind these aspects of the context of the first sentence of Article 61, and the object and purpose of the TRIPS Agreement, the Panel now turns to the ordinary meaning of the words "on a commercial scale".

(v) *"on a commercial scale"*

7.532 The parties adopt different approaches to the task of interpreting the phrase "on a commercial scale". The Panel will examine each of these approaches in turn, beginning with that of the complainant.

7.533 The ordinary meaning of the word "scale" is uncontroversial. It may be defined as "relative magnitude or extent; degree, proportion. Freq. in *on a grand, lavish, small, etc. scale*".<sup>500</sup> The ordinary meaning of the word includes both the concept of quantity, in terms of magnitude or extent, as well as the concept of relativity. Both concepts are combined in the notions of degree and proportion. Therefore, a particular "scale" compares certain things or actions in terms of their size. Some things or actions will be of the relevant size and others will not.

7.534 The relevant size is indicated by the word "commercial". The ordinary meaning of "commercial" may be defined in various ways. The following two definitions have been raised in the course of these proceedings:

- "1. Engaged in commerce; of, pertaining to, or bearing on commerce.
2. (...)
3. Interested in financial return rather than artistry; likely to make a profit; regarded as a mere matter of business."<sup>501</sup>

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<sup>499</sup> The Convention for the Protection of Producers of Phonograms against Unauthorized Duplication of their Phonograms, Article 3, expressly provides that each Contracting State may implement the Convention by means of penal sanctions.

<sup>500</sup> *New Shorter Oxford English Dictionary* (1993). Mexico notes a definition in Spanish that refers to degree, but that is not apposite in context: see Mexico's third party oral statement, fn. 8.

<sup>501</sup> *New Shorter Oxford English Dictionary* (1993).

7.535 The Panel considers the first definition to be apposite. It includes the term "commerce" which may, in turn, be defined as "buying and selling; the exchange of merchandise or services, esp. on a large scale".<sup>502</sup> Reading this definition into the definition of "commercial" indicates that "commercial" means, basically, engaged in buying and selling, or pertaining to, or bearing on, buying and selling.<sup>503</sup> A combination of that expanded definition of "commercial" and the definition of "scale" would render a meaning in terms of a relative magnitude or extent (of those) engaged in buying and selling, or a relative magnitude or extent pertaining to, or bearing on, buying and selling. This draws a link to the commercial marketplace.

7.536 The United States also submits that the word "commercial" scale draws a link to the commercial marketplace. However, it refers to elements of the first and third meanings in definition 3., but dismisses the relevance of the second meaning, "likely to make a profit", because it is different from the other two.<sup>504</sup>

7.537 The Panel notes that the third definition, which includes the qualifiers "rather than artistry" and "mere", refers to usages such as a "commercial artist", "commercial film" or "commercial writing" in the sense of those who are more interested in financial return than the artistic merit of a work, works that are of such a nature that they are likely to make a profit and works that are regarded as a mere matter of business rather than as expressions of other values. This definition is not apposite in the first sentence of Article 61.

7.538 Therefore, the Panel considers that the first definition set out at paragraph 7.534 above is appropriate. However, the combination of that definition of "commercial" with the definition of "scale" presents a problem in that scale is a quantitative concept whilst commercial is qualitative, in the sense that it refers to the nature of certain acts. Some acts are in fact commercial, whilst others are not. Any act of selling can be described as commercial in this primary sense, irrespective of its size or value. If "commercial" is simply read as a qualitative term, referring to all acts pertaining to, or bearing on commerce, this would read the word "scale" out of the text. Acts on a commercial scale would simply be commercial acts. The phrase "on a commercial scale" would simply mean "commercial". Such an interpretation fails to give meaning to all the terms used in the treaty and is inconsistent with the rule of effective treaty interpretation.<sup>505</sup>

7.539 There are no other uses of the word "scale" in the TRIPS Agreement, besides the first and fourth sentences of Article 61. However, the wider context shows that the TRIPS Agreement frequently uses the word "commercial" with many other nouns, although nowhere else with "scale". The other uses of the word "commercial" include "commercial rental"<sup>506</sup>, "commercial purposes"<sup>507</sup>, "commercial exploitation"<sup>508</sup>, "commercial terms"<sup>509</sup>, "public non-commercial use"<sup>510</sup>, "first commercial exploitation"<sup>511</sup>, "honest commercial practices"<sup>512</sup>, "commercial value"<sup>513</sup>, "unfair commercial use"<sup>514</sup>, "non-commercial nature"<sup>515</sup> and "legitimate commercial interests".<sup>516</sup>

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<sup>502</sup> *Ibid.*

<sup>503</sup> The Panel also observes that the definition of "commerce" itself expressly includes a notion of "scale", but this appears to refer to commerce in a general sense, such as "trade and commerce", which does not appear apposite within the word "commercial".

<sup>504</sup> See United States' first written submission, paras 109, 110 and 123.

<sup>505</sup> See, for example, Appellate Body Reports in *US – Gasoline*, at p. 23; *Japan – Alcoholic Beverages II*, at p. 12.

<sup>506</sup> Articles 11 and 14.4 of the TRIPS Agreement.

<sup>507</sup> Articles 26.1 and 36 of the TRIPS Agreement.

<sup>508</sup> Article 27.2 of the TRIPS Agreement.

<sup>509</sup> Article 31(b) of the TRIPS Agreement.

<sup>510</sup> Article 31(b) and (c) of the TRIPS Agreement.

<sup>511</sup> Article 38.1 and 38.2 of the TRIPS Agreement.

7.540 The provisions of the Paris Convention (1967) incorporated by Article 2.1 of the TRIPS Agreement include uses of the word "commercial" in the phrase "industrial or commercial establishment" (in the singular or plural)<sup>517</sup> and in the phrases "industrial or commercial matters" and "industrial or commercial activities".<sup>518</sup> The provisions of the Berne Convention (1971) incorporated by Article 9.1 of the TRIPS Agreement include the phrase "any commercial purpose".<sup>519</sup> The provisions of the IPIC Treaty incorporated by Article 35 of the TRIPS Agreement include the phrase "commercially exploited" and "exploits ordinarily commercially".<sup>520</sup>

7.541 The context shows that the negotiators chose to qualify certain activities, such as rental, exploitation and use, as "commercial". They also chose to qualify various nouns, such as "terms", "value", "nature" and "interests", as "commercial" or "non-commercial". In a similar way, they could have agreed that the obligation in the first sentence of Article 61 would apply to cases of wilful and "commercial" trademark counterfeiting or copyright piracy. This would have included all commercial activity. Indeed, the records of the negotiation of the TRIPS Agreement show that this formulation was in fact suggested (by the United States) at an early stage.<sup>521</sup>

7.542 The context shows that the negotiators used the term "commercial purposes" in two provisions on the scope of protection of certain categories of intellectual property rights, and that the Appendix to the Berne Convention (1971) already did use that term in the singular in provisions on possible limitations to particular rights. However, the negotiators did not agree that the obligation in the first sentence of Article 61 would apply to cases of wilful trademark counterfeiting or copyright piracy "for commercial purposes". This would have included all activity for financial gain or profit.

7.543 Instead, the negotiators agreed in Article 61 to use the distinct phrase "on a commercial scale". This indicates that the word "scale" was a deliberate choice and must be given due interpretative weight. "Scale" denotes a relative size, and reflects the intention of the negotiators that the limitation on the obligation in the first sentence of the Article depended on the *size* of acts of counterfeiting and piracy. Therefore, whilst "commercial" is a qualitative term, it would be an error to read it solely in those terms. In context it must indicate a quantity.<sup>522</sup>

7.544 A review of the uses of the word "commercial" throughout the TRIPS Agreement indicates that it links various activities, not simply selling, to the marketplace. It also shows that "commercial" activities cannot be presumed to be on a larger scale than others, such as "public non-commercial" activities, even though they would generally be larger than, say, "personal" or "domestic" use. The distinguishing characteristic of a commercial activity is that it is carried out for profit.<sup>523</sup> The review

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<sup>512</sup> Article 39.2 of the TRIPS Agreement.

<sup>513</sup> Article 39.2(b) of the TRIPS Agreement.

<sup>514</sup> Article 39.3 of the TRIPS Agreement.

<sup>515</sup> Article 60 of the TRIPS Agreement.

<sup>516</sup> Article 63.4 of the TRIPS Agreement.

<sup>517</sup> Articles 3, 5C(3), 6*quinquies*A(2) and 7*bis*(1) of the Paris Convention (1967). This phrase also appears in footnote 1 to the TRIPS Agreement.

<sup>518</sup> Article 10*bis* of the Paris Convention (1967).

<sup>519</sup> Articles II(9)(a)(iv) and IV(4)(c)(iii) of the Appendix to the Berne Convention (1971).

<sup>520</sup> Article 7(1) and (2), of the IPIC Treaty.

<sup>521</sup> The United States suggested in October 1988 a provision applying to trademark counterfeiting and copyright infringement that were "wilful and commercial" (see document MTN.GNG/NG11/W/14/Rev.1). This suggestion was not taken up. A later US proposal, like certain other proposals, used the phrase "on a commercial scale" (see document MTN.GNG/NG11/W/70).

<sup>522</sup> The Panel is not required, for the purposes of this claim, to express a view as to whether "commercial" also indicates certain qualitative factors, such as a profit-seeking purpose.

<sup>523</sup> At the same time, some activities – such as experimentation – may be conducted in the course of business or in connection with a business without a specific profit-making purpose.

of the uses of the word "commercial" also shows that, unlike all the others, Article 61 uses the word "commercial" to qualify a notion of size.

7.545 In the Panel's view, the combination of the primary definition of "commercial" and the definition of "scale" can be reconciled with the context of Article 61 if it is assessed not solely according to the nature of an activity but also in terms of relative size, as a market benchmark. As there is no other qualifier besides "commercial", that benchmark must be whatever "commercial" typically or usually connotes. In quantitative terms, the benchmark would be the magnitude or extent at which engagement in commerce, or activities pertaining to or bearing on commerce, are typically or usually carried on, in other words, the magnitude or extent of typical or usual commercial activity. Given that the phrase uses the indefinite article "a", it refers to more than one magnitude or extent of typical or usual commercial activity. The magnitude or extent will vary in the different "cases" of counterfeiting and piracy to which the obligation applies. In the Panel's view, this reflects the fact that what is typical or usual varies according to the type of commerce concerned.

7.546 Turning to the arguments of the parties and various third parties on this point, they have attempted to give due meaning to both the terms "commerce" and "scale" in different ways. Initially, the United States submitted as follows:

"those who engage in commercial activities in order to make a 'financial return' in the marketplace ... are, by definition, therefore operating on a commercial scale"<sup>524</sup>

7.547 Similarly, Canada submitted that "commercial scale" refers to activities undertaken with a view to profiting.<sup>525</sup> The European Communities submitted that the terms "commercial" and "scale" denote activities that pertain to a business or to the generation of profits".<sup>526</sup>

7.548 The Panel considers these interpretations unsatisfactory, as they seem to equate "commercial scale" with "commercial purpose" or merely "commercial", which are not the term used in Article 61.

7.549 The United States then clarified that it does not read the word "scale" out of the term "commercial scale" and added a qualifier or two to its initial position, submitting that:

"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." (emphasis added and removed)<sup>527</sup>; and

"'commercial scale' certainly extends to those who are *genuinely* engaged in commercial activities in order to make a financial return."<sup>528</sup> (emphasis added)

7.550 In response to a request for clarification from the Panel, the United States explained:

"The United States has employed the words 'seriously' or 'genuinely' to underscore that the IPR infringer must be actually engaged in pursuing financial gain through non-trivial commercial activities in the marketplace, as opposed to, for example, a one-off entry into the marketplace of a limited nature.

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<sup>524</sup> United States' first written submission, para. 110. This submission also interpreted "scale": see paragraph 7.659 below.

<sup>525</sup> Canada's third party written submission, para. 5.

<sup>526</sup> European Communities' third party oral statement, paras 4 and 14.

<sup>527</sup> United States' rebuttal submission, para. 17.

<sup>528</sup> United States' closing oral statement at the second substantive meeting, para. 15.

Whether an infringer is 'seriously' or 'genuinely' engaged in commercial activities would depend on the facts and circumstances of the activity. (...)"<sup>529</sup>

7.551 The Panel understands that this refined approach interprets "commercial scale" as basically everything that is "commercial" with the exception of some trivial or *de minimis* activities. It is not clear how "seriously" and "genuinely" indicate "non-trivial" activities – if anything, "seriously" indicates something more important. However, there is no need to consider its meaning further as the word "seriously" is not used in the terms of the treaty, nor is it implied by the terms that are used.

7.552 Whilst the United States' refined approach has the merit of ensuring that its interpretation of "commercial scale" does not capture an identical class of acts as the term "commercial purpose", the difference seems minimal. This refined approach does not read the word "scale" *out* of the text but nevertheless it reads the word *down* to such an extent that it lacks the significance that the negotiators evidently intended. The negotiators chose the word "scale", which refers to size, rather than other words that they actually used elsewhere in the Agreement that do not exclude activities on the basis of size. They also used the word "scale" in the fourth sentence of Article 61, together with the term "in particular", which would be virtually redundant if the sentence simply meant that Members could provide for criminal procedures and penalties to be applied "in particular" to more than trivial or *de minimis* cases. The context throughout Part III shows that the limitations in Section 5 reflect an effort to address only the more blatant and egregious infringements.

7.553 As to the view that "on a commercial scale" is basically a *de minimis* provision, the Panel need look no further than the preceding provision, Article 60, to see how the negotiators addressed that issue. Article 60 forms part of Section 4 on special requirements related to border measures and serves an analogous purpose to the phrase "on a commercial scale" in Article 61 in that both define the lower end of infringement at which a particular type of enforcement procedure must be available. However, the terms of each are quite different: Article 60 defines *de minimis* infringement in terms of volume ("small quantities"), nature ("of a non-commercial nature") and circumstances ("in travellers' personal luggage or sent in small consignments"). Had the negotiators wanted to exclude only *de minimis* infringement from the minimum standard of Article 61, they had a model in Article 60, or they could have used words such as "except for minor or personal use". However, they did not.<sup>530</sup> Instead, Article 61 refers to size ("scale") qualified only by the word "commercial". This indicates that the negotiators intended something different from *de minimis*. Article 60 also indicates that the negotiators did not equate small with non-commercial, confirming that a "commercial" scale is not necessarily small-scale nor large-scale.

7.554 Among the other third parties, Brazil referred to a "significant" or "large" enough level based on certain factors<sup>531</sup>, Mexico argued for a "meaningful" level<sup>532</sup>; Korea referred to operating a business "in a somewhat systematic fashion".<sup>533</sup> Canada acknowledged as follows:

"There is perhaps no easily quantifiable measure because none is provided for in TRIPS. This omission suggests that the test is qualitative: what a reasonable person would think in the circumstances."<sup>534</sup>

7.555 The Panel considers that these interpretations, whilst they may reflect sound domestic policy considerations, lack a clear basis in the rules of treaty interpretation which the Panel is obliged to

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<sup>529</sup> United States' response to Question No. 63.

<sup>530</sup> Indeed, the United States expressed a similar view in order to explain why a reference to "exceptional cases" in Article 46 of the TRIPS Agreement is not a *de minimis* test (see paragraph 7.387 above).

<sup>531</sup> Brazil's third party written submission, para. 36.

<sup>532</sup> Mexico's third party oral statement, para. 6.

<sup>533</sup> Korea's third party written submission, para. 27.

<sup>534</sup> Canada's third party written submission, para. 7.

apply. All of these interpretations are valid explanations as to why such infringement should be unlawful but they do not explain why it must be a crime. The answer to that question must be found in the terms of the treaty as finally agreed.

7.556 In this connection it seems pertinent to recall that the negotiators chose a term that was different from the commercial purpose or financial return standards used in the national legislation of a number of the participants.

7.557 Turning now to the respondent's approach to the interpretation of "on a commercial scale", China submits that these words should be interpreted as a single term.<sup>535</sup> The United States proposes that each of the terms in the two-word term be interpreted and does not submit that there are other ordinary uses of the phrase that would be relevant.<sup>536</sup>

7.558 The Panel observes that the general rule of treaty interpretation in Article 31 of the Vienna Convention refers in paragraph 1 to the ordinary meaning of the terms of the treaty, read in context. Where the terms are a single term, or ordinarily used together, then the treaty interpreter should refer to the ordinary meaning of that single term, or of each term in the particular context of each other. This is a distinct exercise from that in paragraph 4 of Article 31 of the Vienna Convention which requires a "special meaning" to be given to a term if it is established that the parties so intended. No party to this dispute considers that a "special meaning" should be given to the phrase "on a commercial scale", and nor does the Panel.

7.559 The Panel will follow the approach explained by the Appellate Body in *EC – Chicken Cuts*:

"The Appellate Body has observed that dictionaries are a 'useful starting point' for the analysis of 'ordinary meaning' of a treaty term, but they are not necessarily dispositive. The ordinary meaning of a treaty term must be ascertained according to the particular circumstances of each case. Importantly, the ordinary meaning of a treaty term must be seen in the light of the intention of the parties 'as expressed in the words used by them against the light of the surrounding circumstances'".<sup>537</sup>

7.560 The Panel recalls that the dictionary definition of "scale" (quoted at paragraph 7.533 above) includes the entry "Freq. in *on a grand, lavish, small, etc. scale*". These examples show that the phrase "on a ... scale" is frequently used. Therefore, the use of the words "on a commercial scale" as a phrase appears to be relevant to their ordinary meaning.

7.561 The circumstances surrounding the inclusion of the phrase "on a commercial scale" show that the phrase has been used and, in some cases, defined in the intellectual property legislation of various countries for periods stretching back almost a century. Specifically, the patent laws of these countries refer to the working of inventions, or failure to work inventions, "on a commercial scale".<sup>538</sup> The term is used in relation to the exploitation of protected subject matter, as in Article 61, but the purpose of these non-working provisions, and the considerations relevant to their operation, are distinct from

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<sup>535</sup> China's first written submission, paras 69-71.

<sup>536</sup> United States' response to Question No. 68.

<sup>537</sup> Appellate Body Report in *EC – Chicken Cuts*, para. 175, quoting Appellate Body Report in *US – Softwood Lumber IV*, para. 59, and referring to Appellate Body Reports in *US – Offset Act (Byrd Amendment)*, para. 248, and *US – Gambling*, para. 166, and quoting McNair, *The Law of Treaties* (Oxford, Clarendon Press, 1961), p. 365.

<sup>538</sup> See, for example, the Australian Patent Act 1990, s. 135(1) (mentioned in response to Third Party Question No. 9); Indian Patents Act 1970, ss. 83-84; South African Patent Act 1978, s. 56; United Kingdom Patent Act 1977-1988, s. 50; Zimbabwean Patents Act 1971, s. 31, in Exhibit CHN-198, and the patent laws of other Commonwealth countries. Earlier, the United Kingdom Patents and Design Act 1919, s. 27, had referred to working a patent "on a commercial scale".

those of criminal procedures and penalties as addressed in Article 61 of the TRIPS Agreement. There is insufficient indication that the meaning ascribed to the term "on a commercial scale" in such legislation was that intended by the negotiators of the TRIPS Agreement when they used the term in the first and fourth sentences of Article 61. However, this circumstance shows the phrase in use in an intellectual property context long before the negotiation of the TRIPS Agreement.

7.562 The term "on a commercial scale" was also used in the specific context of trademark counterfeiting and copyright piracy in the WIPO Committee of Experts on Measures Against Counterfeiting and Piracy in 1988 contemporaneously with the earlier part of the negotiations of the TRIPS Agreement. Draft Model Provisions for National Laws set out in a Memorandum by the International Bureau of WIPO for that Committee included, in Article A(1), (2) and (3), three draft Model Provisions on manufacturing as an act of counterfeiting, manufacturing as an act of piracy and additional acts of counterfeiting and piracy, respectively. Each of those draft Model Provisions contained a proviso that such goods were manufactured, or the act was committed, "on a commercial scale". An explanatory observation accompanied the term "commercial scale" as a phrase.<sup>539</sup>

7.563 The evidence on the record includes many other uses of the words "commercial scale" and "on a commercial scale" in a variety of contexts. Accordingly, the Panel considers that the words "commercial" and "scale" provide important context for the ordinary meaning of each other when used together in the phrase "on a commercial scale" as in the first sentence of Article 61 of the TRIPS Agreement.

7.564 China submits that the phrase "on a commercial scale" refers to "a significant magnitude of infringement activity".<sup>540</sup> China refers to four isolated uses of the phrase "commercial scale" spread out over a period of forty years: one at the 1947-1948 Havana Conference, one in a 1985 GATT Council meeting, and two in US national legislation on alternative energy development. From these uses, China posits an interpretation suggestive of industrial scale activity.<sup>541</sup>

7.565 The Panel considers that this interpretation is predetermined by the context of the uses that China has selected, which refer to commercial scale activities at an industrial level. This is inapposite in the context of Article 61 of the TRIPS Agreement which applies to acts of infringement of individual rights, including those subsisting in individual products. This interpretation simply replaces the term "commercial", that is used in the text, with "significant", that is not used in the text, effectively reading out the term "commercial".

7.566 China also argues that the explanatory observation that accompanied the draft Model Provisions is an example of ordinary usage of the term "commercial scale".<sup>542</sup>

7.567 The Panel notes that the explanatory observation did not purport to be a definition but was prepared by the International Bureau of WIPO for the specific purpose of accompanying a provision on manufacturing in the draft Model Provisions. The Report of the WIPO Committee of Experts on Measures against Counterfeiting and Piracy of April 1988 shows that the concept of "commercial

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<sup>539</sup> That explanatory observation read as follows:

"Commercial scale' is a notion which will have to be applied taking into consideration the circumstances accompanying the manufacture. The quantity of the goods manufactured, the way in which they were, are or are intended to be used and the will to make profit are among the factors that the courts will have to take into consideration."

See WIPO document C&P/CE/2 of 18, 19 February 1988, para. 17, set out in Exhibit CHN-43

<sup>540</sup> China's first written submission, para. 64.

<sup>541</sup> Exhibits CHN-44, CHN-45, CHN-46 and CHN-47.

<sup>542</sup> China's first written submission, para. 72; rebuttal submission, para. 76.

scale" proved controversial.<sup>543</sup> Accordingly, it is not an example of ordinary usage. In any event, the draft Model Provisions of the Committee of Experts themselves were never agreed.<sup>544</sup> Therefore, it would not be appropriate to select an explanatory observation that accompanied them and elevate it to the status of the proper interpretation of a treaty text that was negotiated in another forum and that *was* finally agreed.

7.568 Turning to other evidence on the record, two third parties contrasted "commercial scale" production with "pilot scale" production or "small scale test" production.<sup>545</sup> The Panel finds these contrasting terms relevant because they indicate a quantity, and because production can be an act of counterfeiting or piracy.

7.569 In response to questions from the Panel, China, but not the United States, provided other examples of ordinary uses of the phrase "commercial scale", including in company press releases, filings with the US Securities and Exchange Commission and patent applications. The United States argues that these examples are functions of individuals' "own lexicography" and are not used in the same fashion or manner.<sup>546</sup> The United States also notes that patent applications are unrelated to the *first* sentence of Article 61 of the TRIPS Agreement.

7.570 The Panel considers that each of the uses on the record, being in the English language, reflects the understanding of the authors as to the ordinary meaning of those words and phrases in that language. That is the reason why a language allows its speakers to render themselves mutually intelligible. These are the very meanings that dictionaries catalogue. Naturally, words and phrases in the same language may have more than one meaning, "common or rare, universal or specialized".<sup>547</sup> It is incumbent on the Panel to assess these usages in context to discern which is relevant to the question of interpretation at hand, just as the Panel has done when confronted with multiple definitions of the words "commercial" and "scale" in the same dictionary. The Panel also notes that Article 61 of the TRIPS Agreement specifically relates the concept of infringement "on a commercial scale" to other intellectual property rights, which include patents, in the *fourth* sentence of that Article.

7.571 Turning to the ordinary meaning of the term "on a commercial scale", the evidence includes examples of uses of that precise term and also the words "commercial scale" followed by a noun. It is not suggested that this changes the meaning. The nouns include "manufacturing", "production", "facility", "processes", "reactor", "composition" and "cultivation", and the term also follows "manufacture" and "employ".<sup>548</sup> This confirms that the phrase can be used in different contexts as a single term.

7.572 Some of these nouns, notably manufacturing and production, refer to acts that could constitute trademark counterfeiting and copyright piracy, and are therefore particularly apposite to the interpretation of the first sentence of Article 61 of the TRIPS Agreement. However, counterfeiting and piracy include other acts besides manufacturing and production. There are no uses on the record of the phrase with the word "sales" or "selling".

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<sup>543</sup> See Report adopted by the WIPO Committee of Experts on Measures Against Counterfeiting and Piracy, WIPO document C&P/CE/4 of 28 April 1988, reproduced in Exhibit CHN-72, at paras 71-81 and 94.

<sup>544</sup> The April 1988 session of the Committee of Experts could not complete its work and it was envisaged that a revised text would be prepared: see Report in note 543 above, at para. 177.

<sup>545</sup> Australia's and Mexico's respective responses to Third Party Question No. 4.

<sup>546</sup> United States' response to Question No. 69; comments on China's response to Question No. 68.

<sup>547</sup> Appellate Body Report in *US – Gambling*, para. 164.

<sup>548</sup> Press releases of Novovax and Dupont, and US Securities and Exchange Commission filings of Amylin Pharmaceuticals, Inc., Biocryst Pharmaceuticals, Inc., Cambridge Display Technology, Inc. and Verenum Corporation in Exhibit CHN-196; and China's original evidence in Exhibits CHN-44, CHN-45, CHN-46 and CHN-47.

7.573 Simple searches of online patent databases of the Patent Cooperation Treaty, the United States Patent and Trademark Office and the European Patent Office, reveal many patent applications that use the phrase "commercial scale". China has provided abstracts of some applications that define the phrase "commercial scale" in precise, quantitative terms of volume, weight or speed.<sup>549</sup> These definitions vary greatly and relate to different factors, according to the invention claimed in the application. From this evidence, China concludes that:

"In the context of patent applications, the phrase 'commercial scale' refers to a certain level of magnitude. This magnitude is not necessarily objectively high, but it is relatively high in the context of the operation involved."<sup>550</sup>

7.574 The United States finds this statement "telling" and recalls its view that:

"[B]ased on its ordinary meaning, what qualifies as 'commercial scale' piracy or counterfeiting will vary among product and market, and therefore, what is 'commercial scale' can be determined using factors relevant to a particular situation."<sup>551</sup>

7.575 The United States argues that the uses in the press releases and SEC filings must be understood in context, as in some cases:

"[W]hether a manufacturing activity is 'commercial scale' may well mean whether the activity is undertaken on a scale, or at a level of economic efficiency, that allows that public company to make a return on investment or profit for its shareholders."<sup>552</sup>

7.576 The Panel observes a certain degree of convergence between the parties' views, as compared to their initial positions, when addressing these ordinary uses of the phrase "commercial scale". The Panel considers that the contexts in which the term "on a commercial scale" or "commercial scale" is used, given their variety, indicate that each of the words "commercial" and "scale" provides important context for the interpretation of the other when used together. Their combined meaning varies greatly according to the context around them and the lack of precision in the term is apparent.<sup>553</sup> However, it is clear that none of these uses refer to activities that are simply commercial. Rather, they are evidently intended to distinguish certain activities (or premises) from others that pertain to or have a bearing on commerce but which do not meet a market benchmark in terms of what is typical. The precise benchmark in each case depends on the product and the market to which the phrase relates.

7.577 The Panel recalls its view at paragraph 7.545 above and, in light of the evidence considered above, finds that a "commercial scale" is the magnitude or extent of typical or usual commercial activity. Therefore, counterfeiting or piracy "on a commercial scale" refers to counterfeiting or piracy carried on at the magnitude or extent of typical or usual commercial activity with respect to a given product in a given market. The magnitude or extent of typical or usual commercial activity with respect to a given product in a given market forms a benchmark by which to assess the obligation in the first sentence of Article 61. It follows that what constitutes a commercial scale for counterfeiting or piracy of a particular product in a particular market will depend on the magnitude or extent that is typical or usual with respect to such a product in such a market, which may be small or large. The

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<sup>549</sup> International applications published under the PCT: WO 00/61722; WO 2004/054949 A1; WO 2006/110534 A2; WO2008/020357 A2; United States patent no. 6,525,205 B2; United States patent application no. 2007/0202578 A1; in Exhibit CHN-197.

<sup>550</sup> China's response to Question No. 69.

<sup>551</sup> United States' comment on China's response to Question No. 69, citing its response to Question No. 16 and second oral statement (closing statement), paras 10-11.

<sup>552</sup> United States' comment on China's response to Question No. 68.

<sup>553</sup> The lack of precision is highlighted by the addition of specific definitions in the patent applications.

magnitude or extent of typical or usual commercial activity relates, in the longer term, to profitability.<sup>554</sup>

7.578 The Panel observes that what is typical or usual in commerce is a flexible concept. The immediate context in the second sentence of Article 61, which is closely related to the first, refers to the similarly flexible concepts of "deterrent" and "corresponding gravity". Neither these terms nor "commercial scale" are precise but all depend on circumstances, which vary according to the differing forms of commerce and of counterfeiting and piracy to which these obligations apply.

7.579 The parties have presented certain other facts and arguments in relation to the interpretation of "a commercial scale", which the Panel will now assess.

(vi) *Subsequent practice*

7.580 China refers to certain material as "subsequent practice" in the application of the TRIPS Agreement within the meaning of Article 31(3) of the Vienna Convention. The material comprises the enforcement policies of two authorities of two Members, a draft Directive of another Member and various free trade agreements entered into by the United States.<sup>555</sup>

7.581 The Panel has reviewed the material and considers that it lacks the breadth to constitute a common, consistent, discernible pattern of acts or pronouncements. Further, the content of the material does not imply agreement on the interpretation of Article 61 of the TRIPS Agreement.<sup>556</sup> Therefore, the Panel does not consider that it constitutes subsequent practice for the purposes of this interpretation.

(vii) *Supplementary means of interpretation*

7.582 China initially submitted that the draft Model Provisions contained a definition which formed the basis for discussion of the term in the negotiation of the TRIPS Agreement.<sup>557</sup>

7.583 The United States responded that the status of this document under the Vienna Convention is unclear. If the document could be used as a supplementary means of interpretation, it would confirm that a variety of factors would need to be taken into account to determine whether an act is on a commercial scale.<sup>558</sup>

7.584 Canada and Japan refer to the explanatory observation on "commercial scale" that accompanied the draft Model Provisions, noting that it referred to quantitative as well as non-quantitative factors. The European Communities sees limited interest in recourse to supplementary means of interpretation but notes the same point.<sup>559</sup>

7.585 The Panel recalls its observations regarding the explanatory observation that accompanied the draft Model Provisions at paragraph 7.567 above. It appears that the explanatory observation did not represent the common intentions of the WIPO Committee of Experts on Measures Against

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<sup>554</sup> This finding is without prejudice to the qualitative aspect of "commercial scale" considered with respect to the second limb of this claim.

<sup>555</sup> China's first written submission, paras 104-108.

<sup>556</sup> See Appellate Body Reports in *Japan – Alcoholic Beverages II*, p. 13; *US – Gambling*, paras 192-193, and *EC – Chicken Cuts*, para. 259.

<sup>557</sup> China's first written submission, paras 72-75 and 110.

<sup>558</sup> United States' rebuttal submission, paras 26-37.

<sup>559</sup> Canada's third party written submission, para. 6; Japan's third party written submission, paras 22-23; European Communities' third party oral statement, paras 11-12.

Counterfeiting and Piracy, much less the common intentions of the participants in the negotiation of the TRIPS Agreement.

7.586 The draft Model Provisions were mentioned in the records of the TRIPS negotiations, in May 1988<sup>560</sup> and August 1988<sup>561</sup>, in the context of a discussion of the scope of a framework on trade in counterfeit goods (that was never concluded). Documents of the WIPO Committee of Experts, including the draft Model Provisions, were communicated to the TRIPS negotiating group and made available in the GATT Secretariat for consultation by interested delegations, but not circulated, in June 1988.<sup>562</sup> The Panel considers that this evidence indicates that the negotiators of the TRIPS Agreement were aware of the explanatory observation by the International Bureau of WIPO addressing "commercial scale", but it does not indicate that the content of that explanatory observation represented their common intentions.

7.587 There is a certain temporal correlation between the work of the WIPO Committee of Experts and the use of the term "commercial scale" in the drafting of Article 61 of the TRIPS Agreement. The European Communities' proposal for the negotiations on the enforcement of trade-related intellectual property rights in May 1989 ("EC proposal")<sup>563</sup> contained a draft provision on criminal procedures and sanctions that bears a strong similarity to the first, second and fourth sentences of Article 61 in the final text of the TRIPS Agreement. It was also the first proposal to use the words "on a commercial scale". In response to a question from the Panel, the European Communities informed the Panel that:

"In spite of intense research, the European Communities has not been able to find any trace that the phrase 'on a commercial scale' in the EC proposal of 30 May 1989 was sourced from another instrument."<sup>564</sup>

7.588 In any event, there are differences between the draft Model Provisions of the WIPO Committee of Experts, the EC proposal on criminal procedures and sanctions to the TRIPS negotiating group, and the terms of Article 61 of the TRIPS Agreement. In particular, the draft Model Provisions incorporated the phrase "on a commercial scale" *within* the concepts of "counterfeiting" and "piracy" whilst Article 61 uses the phrase "on a commercial scale" to qualify the concepts of "wilful trademark counterfeiting or copyright piracy". Further, the explanatory observation that accompanied the draft Model Provisions was limited to the act of manufacturing whilst Article 61 encompasses the range of acts of counterfeiting and piracy.

7.589 The records of the TRIPS negotiations do not disclose any discussion of the meaning of the phrase "on a commercial scale".

7.590 Therefore, the Panel does not consider that the explanatory observation that accompanied the draft Model Provisions sheds any further light beyond that noted at paragraph 7.562 above on the intentions of the TRIPS negotiators when they used the term "commercial scale".

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<sup>560</sup> It was suggested that, in that connection, the negotiating group should take into account definitions established in national legislation, those under preparation in the WIPO Committee of Experts on Measures Against Counterfeiting and Piracy and the existing obligations of relevance in intellectual property conventions: see the minutes of the meeting in document MTN.GNG/NG11/7, paras 23 and 33, in Exhibit CHN-71.

<sup>561</sup> A participant suggested that, in determining the types of infringement to be covered by a framework on trade in counterfeit goods, the criteria suggested in the WIPO draft model legislation should be employed: see the minutes of the meeting in document MTN.GNG/NG11/8, at para. 52, in Exhibit CHN-55.

<sup>562</sup> See GATT document MTN.GNG/NG11/W/5/Add.6.

<sup>563</sup> GATT document MTN.GNG/NG11/W/31.

<sup>564</sup> European Communities' response to Third Party Question No. 8.

(viii) *Article 41.5 of the TRIPS Agreement*

7.591 China submits that Article 41.5 of the TRIPS Agreement makes clear that none of the enforcement provisions can be read to require Members to set out low-scale – and therefore high resource – thresholds for the criminalization of intellectual property infringement.<sup>565</sup> It later clarified that low-scale thresholds implied high amounts of resources because the first sentence of Article 61 is only satisfied by criminal measures that are actually applied.<sup>566</sup>

7.592 The United States does not claim that China has an obligation to prosecute all counterfeiting and piracy falling within the scope of the first sentence of Article 61.<sup>567</sup>

7.593 Article 41.5 provides as follows:

"It is understood that this Part does not create any obligation to put in place a judicial system for the enforcement of intellectual property rights distinct from that for the enforcement of law in general, nor does it affect the capacity of Members to enforce their law in general. Nothing in this Part creates any obligation with respect to the distribution of resources as between enforcement of intellectual property rights and the enforcement of law in general."

7.594 The Panel considers that Article 41.5 is an important provision in the overall balance of rights and obligations in Part III of the TRIPS Agreement. Both sentences apply to "this Part", which includes Article 61.

7.595 The first sentence of Article 41.5 does not appear to be relevant to this dispute. China has administrative agencies dedicated to intellectual property enforcement that are separate from its law enforcement agencies in general. It is under no obligation to put in place a separate judicial system for IPR enforcement.

7.596 The second sentence of Article 41.5 relates to the deployment of resources for enforcement. In the Panel's view, that plays an important role in relation to Article 41, in particular, paragraph 1<sup>568</sup>, and the actual exercise of authority to enforce intellectual property rights throughout Part III. However, the Panel's findings in this dispute regarding the first sentence of Article 61 are confined to the issue of what acts of infringement must be criminalized and not those which must be prosecuted.

7.597 China refers to the second sentence of Article 61 on remedies and notes that it contains an element of flexibility in its reference to "the level of penalties applied for crimes of a corresponding gravity". China argues that if Members are not required to impose meaningful punishment for low-level crimes, they should not be required to enforce intellectual property crimes at a low level either.<sup>569</sup> The Panel simply recalls its comment in paragraph 7.596 and confirms that it has not made a finding on any duty to prosecute.

7.598 China asks the Panel to note that its criminal law allows for the possibility of private prosecution of certain crimes. It speculates that defining a crime with too low a threshold "could unleash a large volume of private enforcement actions and impose a significant burden on the judicial

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<sup>565</sup> China's first written submission, paras 98-101.

<sup>566</sup> China's rebuttal submission, paras 122-124: see also European Communities' response to Third Party Question No. 10. Australia makes a similar point in relation to the second sentence of Article 61: see its third party written submission, para. 25.

<sup>567</sup> United States' rebuttal submission, paras 47-48.

<sup>568</sup> Article 41.1 of the TRIPS Agreement is quoted at paragraph 7.170 above.

<sup>569</sup> China's rebuttal submission, paras 108-110.

system".<sup>570</sup> However, in response to questions, China was unable to substantiate its concern. In particular, it lacked any data relevant to its experience after it lowered thresholds for the crimes infringing intellectual property crimes in 2004.<sup>571</sup> Therefore, the Panel does not need to consider that issue further.

7.599 In light of the above, the Panel confirms its interpretation of "on a commercial scale" set out at paragraph 7.577 above. The Panel will now apply that interpretation to the measures at issue.

(ix) *Conformity of the measures at issue with respect to the level of the thresholds*

7.600 The Panel recalls its finding at paragraph 7.545 above regarding the interpretation of the phrase "wilful trademark counterfeiting or copyright piracy 'on a commercial scale'", as used in Article 61 of the TRIPS Agreement. The Panel recalls, in particular, that this is a relative standard, which will vary when applied to different fact situations.

7.601 The Panel notes that it is the standard in the treaty obligation that varies as applied to different fact situations, and not necessarily the means by which Members choose to implement that standard. The Panel recalls that the third sentence of Article 1.1 of the TRIPS Agreement, quoted and discussed at paragraphs 7.512 and 7.513 above, provides as follows:

"Members shall be free to determine the appropriate method of implementing the provisions of this Agreement within their own legal system and practice."

7.602 This provision confirms that the TRIPS Agreement does not mandate specific forms of legislation.<sup>572</sup> The Panel may not simply assume that a Member must give its authorities wide discretion to determine what is on a commercial scale in any given case, and may not simply assume that thresholds, including numerical tests, are inconsistent with the relative benchmark in the first sentence of Article 61 of the TRIPS Agreement. As long as a Member in fact provides for criminal procedures and penalties to be applied in cases of wilful trademark counterfeiting or copyright piracy on a commercial scale, it will comply with this obligation. If it is alleged that a Member's method of implementation does not so provide in such cases, that allegation must be proven with evidence. Therefore, the Panel will assess whether the evidence shows that China fails to provide for criminal procedures and penalties to be applied in any such cases.

7.603 The Panel begins with the first limb of the claim. In the first limb of the claim, the United States challenges the *levels* at which certain thresholds are set. Having chosen to challenge the level of a series of numerical thresholds as compared to a relative standard, it is necessary for the United States to demonstrate that the levels are higher than that standard as applied in certain factual situations. That calls for quantitative evidence. Later, the Panel will address the second limb of the claim, in which the United States challenges the *factors* taken into account by the criminal thresholds. That calls for qualitative evidence.

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<sup>570</sup> China's first written submission, para. 38, referring to Article 170 of the Criminal Procedure Law, as restated in Article 5 of Judicial Interpretation No. 6 [2007].

<sup>571</sup> China's response to Question No. 14.

<sup>572</sup> The United States accepts this: see its rebuttal submission, paras 42-44; response to Question No. 54.

7.604 The parties agree that the standard of "a commercial scale" will vary by product and market and that the conformity of China's criminal thresholds with that standard must be assessed by reference to China's marketplace.<sup>573</sup>

7.605 The Panel recalls that a previous Panel had occasion to apply certain relative standards in the TRIPS Agreement in quantitative terms. The Panel in *US – Section 110(5) Copyright Act* interpreted the phrase "certain special cases" *inter alia* in terms of a narrow scope or reach, and the phrase "a normal exploitation of the work" *inter alia* in an empirical or quantitative sense, as those phrases are used in Article 13 of the TRIPS Agreement.<sup>574</sup> As in the present case, the parties in that dispute agreed that conformity had to be assessed wholly or primarily in relation to the respondent's market. The Panel in that dispute adopted the following approach in assessing the conformity of a measure with Article 13:

"We note that while the WTO Members are free to choose the method of implementation, the minimum standards of protection are the same for all of them. In the present case it is enough for our purposes to take account of the specific conditions applying in the US market in assessing whether the measure in question conflicts with a normal exploitation in that market, or whether the measure meets the other conditions of Article 13."<sup>575</sup> (footnote deleted)

7.606 In the present dispute, the Panel considers this approach appropriate as well. The Panel needs to consider the specific conditions applying in China's marketplace in assessing whether the measures in question, which exclude certain acts of infringement from particular liability, conform to the relative standard in Article 61.<sup>576</sup> This applies *a fortiori* as the relative standard is set in terms of what is "on a commercial scale", which varies not only by market but also by product within the same market.

7.607 The nature of the measures at issue and the applicable treaty obligation under consideration in this Section of this Report can be contrasted with those considered in Section VII:A. It was not necessary for the United States to demonstrate the particular class of works to which the Copyright Law denies copyright protection because it was clear that the measure at issue denies *all* copyright protection to some works and the relevant obligation in the TRIPS Agreement does not permit denial of all copyright protection to any such works. In contrast, the measures that establish the criminal thresholds set forth levels that deny criminal procedures and penalties in some, but not all, cases of wilful trademark counterfeiting and copyright piracy, and the relevant obligation permits the denial of criminal procedures and penalties in some such cases.

7.608 The United States argues that the criminal thresholds exclude certain commercial activity. The United States relies, in particular, on the text of the measures establishing the criminal thresholds themselves.<sup>577</sup>

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<sup>573</sup> United States' first written submission, fn. 78 and para. 118; rebuttal submission, para. 17; responses to Questions Nos. 16 and 66; China's first written submission, paras 133-137; response to Question No. 16.

<sup>574</sup> See Panel Report in *US – Section 110(5) Copyright Act*, paras 6.113 and 6.178.

<sup>575</sup> *Ibid.*, para. 6.189.

<sup>576</sup> The Panel Report in *Canada – Pharmaceutical Patents* also considered the meaning of "normal" exploitation (in that case, of a patent) but in abstract terms. However, it did so in an assessment of an exception that was challenged on the basis of the nature of the acts that the measures excused from liability, not their magnitude or extent. Both parties also addressed the meaning of "normal" in that case in abstract terms: see paras 7.51-7.59.

<sup>577</sup> United States first written submission, para. 110; rebuttal submission, para. 10.

7.609 The Panel has reviewed the measures and agrees that, on their face, they do exclude certain commercial activity from criminal procedures and penalties. For example, some of the criminal thresholds are set in terms that refer expressly to commercial activity, such as "illegal business operation volume", which is defined in terms of "manufacture, storage, transportation, or sales" of infringing products, and "illegal gains" which is defined in terms of profit. However, based solely on the measures on their face, the Panel cannot distinguish between acts that, in China's marketplace, are on a commercial *scale*, and those that are not.

7.610 Certain thresholds are set in monetary terms, ranging from ¥20,000 profit to ¥50,000 turnover or sales. The measures, on their face, do not indicate what these amounts represent as compared to a relevant commercial benchmark in China.<sup>578</sup> Each of these amounts represents a range of volumes of goods, which vary according to price. Another factor to take into account is the period of time over which infringements can be cumulated to satisfy these thresholds. One threshold is set not in monetary terms but rather at 500 张 (份) ("copies" for the sake of simplicity). Whilst it is reasonably clear to the Panel how many goods that comprises with respect to certain traditional media, this is not, on its face, related to any relevant market benchmark in China either.

7.611 The Panel has noted the United States' repeated assertions that certain amounts constitute counterfeiting or piracy on a commercial scale. The most recurrent example concerns 499 copyright-infringing "copies", although it is not related to the same product in all examples or, sometimes, to any product.<sup>579</sup> The only facts in these examples are amounts equal to, or slightly less than, those in the measures themselves. Those amounts, in combination with the monetary thresholds and the factors used in the thresholds, demonstrate the class of acts for which China does not provide criminal procedures and penalties to be applied. Those numbers and factors do not, in themselves, demonstrate what constitutes a commercial scale for any product or in any market in China.

7.612 China asserted the relevance of the scale of commerce in China in its first written submission and referred to Economic Census statistics (considered below).<sup>580</sup>

7.613 The Panel asked both parties after the first substantive meeting whether "commercial scale" varies according to characteristics of markets, products and operators within a market, how "commercial scale" can be related to these considerations and what type of data could be relevant.<sup>581</sup>

7.614 In response to the Panel's question, the United States referred to the interpretation of "commercial scale" that it had proposed in its first written submission, which included all commercial activity by definition. The United States agreed that "commercial scale" must be viewed with reference to the marketplace, and acknowledged that the scale of what is commercial necessarily will vary by product and market. It acknowledged that what is "commercial scale" can vary from situation to situation according to a number of factors. It asserted that China's criminal thresholds fail to capture commercial scale in certain market situations.<sup>582</sup> Nevertheless, the United States did not provide data regarding products and markets or other factors that would demonstrate what constituted "a commercial scale" in the specific situation of China's marketplace.

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<sup>578</sup> The parties agree that the thresholds should be assessed in the form in which they appear in China's measures, namely *Renminbi* (¥), which is the local currency used in China's marketplace: see their respective responses to Question No. 5.

<sup>579</sup> United States' first written submission, para. 139; response to Question No. 25; rebuttal submission, para. 112; response to Question No. 64.

<sup>580</sup> China's first written submission, paras 133-137.

<sup>581</sup> Question No. 16.

<sup>582</sup> United States' response to Question No. 16.

7.615 In its rebuttal of China's assertion regarding the scale of commerce in China, the United States noted that the "commercial scale" standard was a relative one.<sup>583</sup> It commented on the Economic Census statistics submitted by China but at the same time dismissed their relevance as they are aggregate statistics related to undefined average economic units. It also recalled an earlier assertion that the Chinese market, including the market for many copyright and trademark-bearing goods, is fragmented and characterized by a profusion of small manufacturers, middlemen, distributors, and small outlets at the retail level.<sup>584</sup>

7.616 The Panel has reviewed the evidence in support of this assertion.<sup>585</sup> The evidence comprises a quote from a short article from a US newspaper, the *San Francisco Chronicle*, titled "*30,000-Store Wholesale Mall Keeps China Competitive*" regarding the number of stores in a particular mall in Yiwu and the physical dimensions of some stalls<sup>586</sup>; a statistic quoted from an extract from a management consultant report titled "*The 2005 Global Retail Development Index*" that the top ten retailers in China hold less than 2 per cent of the market, and another statistic that the top 100 retailers have less than 6.4 per cent<sup>587</sup>; and a quote from an article in *Time* magazine titled "*In China, There's Priceless, and for Everything Else, There's Cash*" that a shopping mall in Luohu spans six floors of small stores.<sup>588</sup>

7.617 The Panel finds that, even if these sources were suitable for the purpose of demonstration of contested facts in this proceeding, the information that was provided was too little and too random to demonstrate a level that constitutes a commercial scale for any product in China.

7.618 The United States referred to Canada's third party written submission, which had provided an estimate of China's gross domestic product per capita.<sup>589</sup> It did not explain specifically how this figure was comparable to China's numerical thresholds.

7.619 The Panel considers GDP per capita a reliable indicator of average national income but not a sufficient indicator of a commercial scale, as it is calculated with a denominator of total population.<sup>590</sup> The Panel also notes that GDP is a far more aggregated figure than those in the Economic Census statistics that the United States dismissed.

7.620 China submits that the United States must provide evidence that China's laws actually function to exclude a category of infringement that meets the "commercial scale" standard. Hypothetical examples do not qualify as sufficient evidence.<sup>591</sup>

7.621 In response, the United States asserts that it, and a number of third parties, have provided "numerous, concrete illustrations" of commercial-scale piracy and counterfeiting that take place underneath China's thresholds.<sup>592</sup> It refers to a "Report on Copyright Complaints, Raids and Resulting

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<sup>583</sup> United States' rebuttal submission, para. 104.

<sup>584</sup> United States' rebuttal submission, paras 106-107.

<sup>585</sup> The evidence was submitted with the United States' first written submission, para. 122.

<sup>586</sup> Exhibit US-28.

<sup>587</sup> A.T. Kearney: "Destination: China" in *The 2005 Global Retail Development Index* in Exhibit US-29.

<sup>588</sup> Exhibit US-30. An article from the London *Daily Telegraph* is also submitted in Exhibit US-31.

<sup>589</sup> United States' rebuttal submission, para. 108, referring to Exhibit CDA-1.

<sup>590</sup> As noted in China's rebuttal submission, para. 142.

<sup>591</sup> China's rebuttal submission, para. 149.

<sup>592</sup> United States' second oral statement, para. 28, elaborating on its rebuttal submission, paras 9-10.

Criminal Actions in China" prepared by a coalition of trade associations in 2008 (the "CCA Report").<sup>593</sup>

7.622 The Panel has reviewed the CCA Report to determine whether it bears out the United States' assertion. The CCA Report was originally submitted as a case example intended to show that the criminal thresholds create a "safe harbour" (an assertion not borne out by the data<sup>594</sup>) and also to show that significant quantities of retail sales of infringing product take place in China at levels below China's thresholds.<sup>595</sup>

7.623 The Panel notes that the question whether retail sales of infringing product take place below the thresholds is not dispositive of the claim, as the first sentence of Article 61 does not require Members to provide for criminal procedures and penalties to be applied to all such cases. Further, the CCA Report sets out for each raid "total units seized (DVD, CD, VCD)". For some raids, the total units seized were as few as five. Therefore, while the aggregate number of seizures below China's thresholds may or may not be "significant", the seizure data does not permit any deduction as to the scale of operations of the individual raided retail outlets. The total units seized in many cases may be only part of, or even incidental to, a commercial operation. The seizure data illustrates the scale of infringing stock on hand (as it is intended to do) but it does not show the scale of the individual retail businesses or what constitutes a commercial scale for those products in that market.<sup>596</sup>

7.624 China provided official statistics from its Economic Census.<sup>597</sup> The statistics include figures for average annual revenue for enterprises engaged in different industrial sectors in China. Annual revenue appears to be a concept capable of comparison with "illegal business operation volume" as defined in Judicial Interpretation No. 19 [2004] and set out at paragraph 7.401 above. The statistics show that the illegal business operation volume threshold of ¥50,000 for counterfeiting one registered trademark in violation of Article 213 of the Criminal Law is equivalent to 0.41 per cent of the average

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<sup>593</sup> The Report, contained in Exhibit US-41, was prepared by the "China Copyright Alliance", a coalition of six trade associations that represent several creative industry sectors.

<sup>594</sup> The CCA Report was submitted as a case example of how the thresholds allegedly create a "safe harbour" for commercial scale trademark counterfeiting and copyright piracy and provide "clear guideposts" as to how to avoid the risk of criminal prosecution. It was alleged that the CCA Report shows that when the numerical thresholds are shifted down, commercial operations are adjusted and restructured to ensure that they remain at levels that fall under the thresholds. The CCA Report covers the period January 2006 to November 2007 - the period during which a threshold under Article 217 of the Criminal Law was lowered from 1000 copies to 500 copies (see paragraphs 7.411 and 7.412 above). The CCA Report highlights a congruence in the percentage of seizures below the threshold before and after it was lowered. However, when further data was provided regarding the percentage of seizures below 500 copies before the threshold was lowered, when it was an *irrelevant* number, the Panel was able to observe a (somewhat lesser but still strong) congruence between that percentage and the percentage of seizures below the same level when it *was* the threshold. Therefore, the Panel does not find that the data in the CCA Report supports the conclusion that the commercial operations of infringers are related to the levels of the thresholds. See United States' first written submission, paras 151-161. The further data was provided by the United States in response to Question No. 1 posed by China.

<sup>595</sup> United States' first written submission, para. 157; rebuttal submission, paras 93-97.

<sup>596</sup> The United States alleged in response to an unrelated question that if a person engaged in legitimate commercial activities is also engaged in infringing activities, the existence of the legitimate commercial platform to support the infringing activities would be a pertinent consideration in assessing whether the infringing activities are "on a commercial scale": see United States' response to Question No. 62. However, the Panel notes that the phrase "on a commercial scale" qualifies the terms "trademark counterfeiting or copyright piracy" and a legitimate commercial platform does not fall within the scope of either of those terms.

<sup>597</sup> *China Economic Census Yearbook 2004*, edited by the Executive Office of the First National Economic Census Leading Group of the State Council, published in Chinese and English by the China Statistics Press. Extracts from the Volume of Secondary Industry (Section One) and the Volume of Synthesis, including interpretation of main indicators and rules on classification, are reproduced in Exhibit CHN-79.

annual revenue of enterprises engaged in light industry; 0.8 per cent of the average annual revenue of small-size enterprises; and 0.84 per cent of the average revenue of Chinese retail businesses.<sup>598</sup>

7.625 The Economic Census statistics also refer to a concept of the "Individual Operation Household" which is defined as the smallest unit of commerce in Chinese economic statistics. The statistics show that the illegal business operation volume threshold of ¥50,000 for counterfeiting one registered trademark is equivalent to 22.56 per cent of the average annual revenue of Individual Operation Households and 29.44 per cent of the average annual revenue of Individual Operation Households engaged in retail.<sup>599</sup>

7.626 The Panel notes that these calculations are percentages of an average and may be relevant to establishing what is a typical or usual level of commercial activity in a general sense. However, the statistics are highly aggregated and do not refer to any particular products, according to which the benchmark of "a commercial scale" necessarily varies. Moreover, the statistics regarding individual operation households engaged in retail do not address the basic question of whether retail sales by individual operation households are typical or usual in China. Therefore, the Panel does not consider that these statistics are sufficient for it to form a view as to whether the illegal business operation volume thresholds capture all trademark counterfeiting or copyright piracy on a commercial scale in China.

7.627 The United States also submitted other press articles to illustrate points in its first written submission, particularly regarding the calculation of certain thresholds. China objected at the outset arguing that "[t]he Panel can afford little or no weight to such anecdotal and potentially misinformed reports".<sup>600</sup> The United States was puzzled by China's concern at its recourse to newspapers or other media. It recalled its prior attempts to obtain information from China pursuant to Article 63.3 of the TRIPS Agreement. China had declined to provide information and stated instead that its competent domestic IPR authorities had also made relevant information publicly available through their official websites, newspapers, magazines and other proper channels. The United States added that the information in newspapers and magazines is "drawn from a variety of well-established and well-regarded sources".<sup>601</sup>

7.628 The Panel has reviewed the press articles and notes that none of them are corroborated, nor do they refer to events or statements that would not require corroboration. Whilst the publications are reputable, most of these particular articles are brief and are quoted either for general statements or random pieces of information. Most are anecdotal in tone, some repeating casual remarks about prices of fake goods, anonymous statements or speculation. They have titles including "*Fake Pens Write Their Own Ticket*", "*Chasing copycats in a tiger economy*", "*Hollywood takes on fake Chinese DVDs*", "*Film not out yet on DVD? You can find it in China*" and "*Inside China's teeming world of fake goods*".<sup>602</sup> Most of the press articles are printed in US or other foreign English-language media that are not claimed to be authoritative sources of information on prices and markets in China. There are four press articles from Chinese sources, one from Xinhua News Agency and three from the English-language *China Daily*. Two are quoted simply to demonstrate the existence of certain goods in China<sup>603</sup>; another quotes a vague statement from unnamed "market insiders" on how illegal publishers tend to work<sup>604</sup>; and the other quotes an "insider" for the maximum and minimum prices of

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<sup>598</sup> See China's response to Question No. 17.

<sup>599</sup> *Ibid.*

<sup>600</sup> China first written submission, para. 45.

<sup>601</sup> United States' rebuttal submission, para. 98 and fn. 102.

<sup>602</sup> Exhibits US-24, US-30, US-31, US-33, US-34, US-37.

<sup>603</sup> A Xinhua News Agency article refers to goods with high turnover and relatively low cost, in Exhibit US-26, and a *China Daily* article refers to the existence of HDVDs, in Exhibit US-39.

<sup>604</sup> Exhibit US-38.

a range of pirated and genuine goods.<sup>605</sup> One other alleged "recent news account" is not attributed to any source at all.<sup>606</sup>

7.629 The Panel emphasizes that, in the absence of more reliable and relevant data, it has reviewed the evidence in the press articles with respect to a central point in this claim that is highly contested. The credibility and weight of that evidence are therefore critical to the Panel's task. For the reasons set out above, the Panel does not ascribe any weight to the evidence in the press articles and finds that, even if it did, the information that these press articles contain is inadequate to demonstrate what is typical or usual in China for the purposes of the relevant treaty obligation.<sup>607</sup>

7.630 There is no indication that probative evidence on this point would be difficult to obtain. Indeed, it can be noted that more specific information on prices and markets in China is contained in various US exhibits, notably information on prices of products in a report on Cinema and Home Entertainment in China prepared by Screen Digest and Nielsen NRG<sup>608</sup> (submitted in support of the claim regarding the Copyright Law) and in annexes to a letter from Nintendo of America to the United States Trade Representative.<sup>609</sup> The United States did not refer to this evidence in its submissions. Further, in response to a question from the Panel, the United States had no apparent difficulty in providing a translation of a Chinese judicial decision that had been mentioned in one of the press articles.<sup>610</sup>

7.631 The information in the exhibits would not necessarily have been sufficient and, even if it were, it would not be appropriate for the Panel to trawl them for evidence to which the United States did not refer to make the United States' case for it. As the Appellate Body Report in *US – Gambling* states:

"A *prima facie* case must be based on 'evidence *and* legal argument' put forward by the complaining party in relation to *each* of the elements of the claim. A complaining party may not simply submit evidence and expect the panel to divine from it a claim of WTO-inconsistency. Nor may a complaining party simply allege facts without relating them to its legal arguments."<sup>611</sup>

7.632 For the above reasons, the Panel finds that the United States has not made a *prima facie* case with respect to the first limb of its claim under the first sentence of Article 61 of the TRIPS Agreement. The Panel will now turn to the second limb of the claim.

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<sup>605</sup> Exhibit US-32.

<sup>606</sup> United States' first written submission, para. 136, citing the price of a *Spider Man 3* DVD.

<sup>607</sup> The Panel's approach is consistent with the approach of other international tribunals, notably the International Court of Justice: see Rosenne, S., *The Law and Practice of the International Court 1920 – 2005*, (M. Nijhoff, 2006), Volume III at para. 257, and Highet, K., "Evidence and Proof of Facts", in Damrosch, L., *The International Court of Justice at a Crossroads*, (Transnational, 1987) cited in the Panel Report in *Australia – Automotive Leather II* at para. 9.65, fn. 210. The Panel's approach in the present dispute is also consistent with the approach in the Arbitrator's Award in *EC – The ACP-EC Partnership Agreement II*, at paras 57-58. Whilst the Appellate Body Report in *Brazil – Retreaded Tyres* referred to a newspaper article in a footnote, it did so after referencing two substantial reports on point, and the point was not central to the findings in that dispute: see Appellate Body Report, para. 207, fn. 393, citing the Panel Report, para. 7.201, fn. 1358.

<sup>608</sup> United States' first written submission, para. 200, citing Exhibit US-49.

<sup>609</sup> United States' first written submission, paras 146 and 153, citing Exhibit US-36.

<sup>610</sup> Exhibit US-61 referred to in the United States' first written submission, para. 120 and a newspaper article in Exhibit US-25.

<sup>611</sup> Appellate Body Report in *US – Gambling*, para. 140 (footnotes omitted).

(x) *Other indicia – physical evidence*

7.633 With respect to the second limb of this claim, the United States alleges that China's value and volume thresholds are tied to finished goods and therefore ignore other indicia of commercial scale operations, such as the presence of unfinished products and fake packaging.<sup>612</sup> The Panel will assess whether these other indicia *can* be taken into account by China's thresholds and, to the extent that they cannot, whether the term wilful trademark counterfeiting or copyright piracy "on a commercial scale" *requires* China to take these other indicia into account.<sup>613</sup>

7.634 This argument is premised on an assertion that China's criminal thresholds "focus[] solely on business volume, copy, and profit thresholds that can only be met by counting finished goods".<sup>614</sup> It is not clear why the United States considers that thresholds expressed in these terms are tied exclusively to finished goods. Its concern may relate to the definition of "illegal business operation volume" in Article 12(1) of Judicial Interpretation No. 19 [2004]<sup>615</sup> and to the use of the term 张 (份) in one threshold<sup>616</sup> but this is not explained. It is not clear how its concern relates to "illegal gains".<sup>617</sup> In sum, the United States does not sufficiently relate its assertion to the measures at issue.

7.635 Further, the United States has challenged China's criminal thresholds as established by the Criminal Law, "in particular" certain Articles establishing the substantive crimes of infringing intellectual property rights and relevant Judicial Interpretations.<sup>618</sup> However, the United States has not properly addressed any other provisions of the Criminal Law, such as the general provisions, that could have a bearing on questions of evidence. Having cast the entire Criminal Law as a relevant measure, it is incumbent on the United States to explain how the thresholds established by that Law operate. A complainant cannot avoid the burden of proof with respect to other apparently relevant provisions of the Law at issue, particularly when it identified that whole Law in its request for establishment of a panel, simply by neglecting to address those provisions, leaving it to the respondent to assert their relevance.

7.636 Instead, the United States provided a copy of Articles 1 to 12 of the Criminal Law, without comment, and responded only briefly to the arguments of the respondent on the offences of preparation for a crime and attempted crime established by Articles 22 and 23 of the Criminal Law. When asked whether Articles 22 and 23 of the Criminal Law permit courts to take into account other physical evidence, such as unfinished products and packaging (which the United States asserts that they cannot), the United States stated as follows:

"The United States is not aware of the extent to which the offenses of preparation and attempt permit courts to convict an offender based on physical evidence other than the infringing products themselves, such as unfinished products and packaging, for the purpose of meeting the thresholds."<sup>619</sup>

7.637 The Panel recalls its findings at paragraphs 7.434 to 7.437 above regarding the offences of preparation for a crime and attempted crime established by Articles 22 and 23 of the Criminal Law. The United States does not dispute that these general provisions apply to the substantive crimes of infringing intellectual property rights, and acknowledges that certain courts (whose decisions were

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<sup>612</sup> United States' first written submission, paras 113 and 143 to 147.

<sup>613</sup> See paragraph 7.496 above.

<sup>614</sup> United States' first written submission, para. 143. The same submission also referred to China's reliance on "value and volume" thresholds tied to finished goods: see para. 113.

<sup>615</sup> See paragraph 7.401 above.

<sup>616</sup> See paragraph 7.411 above.

<sup>617</sup> United States' first written submission, para. 143, cf. para. 144.

<sup>618</sup> See the request for establishment of a panel, attached as Annex D-1 to this report.

<sup>619</sup> United States' response to Question No. 8.

submitted by China) have applied them accordingly.<sup>620</sup> Therefore, the United States does not sufficiently explain the operation of the measures at issue to support its assertion.

7.638 To the extent that the crimes of preparation for a crime and attempted crime provide for criminal prosecution and sanctions, it is not dispositive of the issue whether they may be taken into account in relation to the crimes set out in Articles 213, 214, 215, 217 and 218 of the Criminal Law. China's obligation under the first sentence of Article 61 is to provide for criminal procedures and penalties to be applied. That obligation is indifferent as to the means by which China provides for such procedures and penalties to be applied, whether by means of substantive crimes only or by means of accessory liability in some cases.

7.639 The United States cited in support of its concerns regarding physical evidence data collected by Nintendo of America in an anti-counterfeiting campaign in China. The data shows that some seizures of infringing products included product components, packaging and materials and implements.<sup>621</sup>

7.640 The Panel notes that the Nintendo data does *not* show whether China provides for criminal procedures and penalties to be applied to cases where the authorities find only product components, packaging and materials and implements, nor does the United States sufficiently relate the seizure data to that issue.

7.641 The Panel notes that Nintendo emphasized its concerns regarding product components, packaging and materials and implements through a discussion of three criminal cases. China submitted the judgement of a court in one of these cases.<sup>622</sup> The judgement shows that the court did take into account both finished and semi-finished infringing products in its evaluation of the substantive crime under Article 213 of the Criminal Law. That case was decided before the entry into force of Judicial Interpretation No. 19 [2004], but it is not clear if the interpretation of the thresholds in that Judicial Interpretation was the reason why the authorities in the two later cases did not (allegedly) take unfinished products into account.

7.642 The United States argues that the court should have taken into account unfinished products that do not in fact infringe, and materials and implements.<sup>623</sup> However, given that the court did take account of all products that were trademark-infringing, and not simply finished products, it is not clear why or if the United States considers that the possession of non-infringing items should have been sufficient for conviction of an intellectual property crime.

7.643 China submits another judgement that, in its view, shows that a court took into account unfinished components in its evaluation of a substantive crime under Article 213. The court also considered machines and scales as evidence that the components were to be used to produce counterfeit products.<sup>624</sup>

7.644 The United States dismisses this judgement, arguing that the reasoning is confused and that the case is an "outlier".<sup>625</sup> However, the United States does not deny that the court took the unfinished components into account and, given that it has provided no information on judicial decisions on point, it is unable to substantiate its assertion that the case is in any way exceptional. The United States does

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<sup>620</sup> United States' rebuttal submission, para. 91.

<sup>621</sup> United States' first written submission, para. 146, citing Nintendo data in Exhibit US-36.

<sup>622</sup> Exhibit CHN-16.

<sup>623</sup> United States' rebuttal submission, para. 92.

<sup>624</sup> Exhibit CHN-15, to which China referred in its rebuttal submission, para. 32.

<sup>625</sup> United States' rebuttal submission, para. 92.

point out that one other judicial decision submitted by China shows that a court did not count semi-finished products, packaging and tools<sup>626</sup>, which the Panel has noted.

7.645 China submits that the inchoate crimes of preparation of a crime, and attempted crime, apply to all substantive crimes in Part Two of the Criminal Law, including the crimes of infringing intellectual property rights. China argues that these inchoate crimes allow courts to take into account unsold goods, with respect to crimes of selling, and unfinished products, with respect to crimes of production.<sup>627</sup>

7.646 The Panel recalls its findings at paragraphs 7.436 and 7.437 above regarding the construction of the measures at issue. These are confirmed by the judicial decisions submitted in evidence showing courts applying either or both of the general provisions in Articles 22 and 23 of the Criminal Law to various crimes of infringing intellectual property rights.<sup>628</sup> Specifically, one of the courts gave its reason for applying Article 23 and, hence, sentencing the infringer to a lesser penalty, which was that the infringer had not finished production at the time he was apprehended.<sup>629</sup>

7.647 The United States submits that Articles 22 and 23 of the Criminal Law do not apply to evidence of completed crimes, such as "worn moulds" for pressing pirated products or counterfeit marks or other materials and implements of such an operation.<sup>630</sup>

7.648 China replies that its authorities consider materials and implements and other reliable indicia in determining criminal infringement, and would consider as relevant evidence a "worn mould" that showed with reasonable certainty that it had produced sufficient number of items to cross the criminal threshold. China refers to a judicial decision in which the court considered the presence of materials and implements.<sup>631</sup>

7.649 The Panel notes that in the case referred to by China the court took into account packaging and tools as evidence of the intended use of product components seized on site, so that the value of the product components was included in the assessment of illegal business operation volume. The tools, though relevant, did not substitute for the thresholds.

7.650 In any event, the Panel considers that the United States' allegation regarding physical evidence relates to the evidence sufficient to initiate a criminal prosecution more than to the definition of the crime itself. Article 61 of the TRIPS Agreement does not address evidence. The first sentence of Article 61 addresses the infringing activity in respect of which the minimum standards must apply. Evidence, including in criminal procedures, is mentioned in Article 41.3, but that provision has no bearing on this claim.

7.651 Section 5 of Part III of the TRIPS Agreement, on criminal procedures, can be contrasted with Section 2, on civil and administrative procedures and remedies, which makes mention of evidence in Article 42 and contains a dedicated provision addressing certain specific issues regarding evidence in

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<sup>626</sup> Exhibit CHN-9, to which the United States referred in its rebuttal submission, para. 93. The case concerns the order, manufacture and sale of several thousand units of counterfeit alcoholic beverages over the course of six months. At the time of arrest, 1,480 units of manufactured counterfeit alcoholic beverage and more than 4,000 bottles of semi-finished beverage were seized, with a large amount of packaging materials and tools for manufacturing counterfeit products. The judicial decision makes no mention of the semi-finished products, packaging materials or tools in the calculation of the thresholds of illegal business operation volume for the purposes of conviction under Article 213 of the Criminal Law.

<sup>627</sup> China's rebuttal submission, paras 39-41, referring to Exhibits CHN-12, CHN-14, CHN-175.

<sup>628</sup> Exhibits CHN-12, CHN-14 and CHN-175.

<sup>629</sup> Exhibit CHN-175.

<sup>630</sup> United States' rebuttal submission, para. 85.

<sup>631</sup> China's rebuttal submission, para. 32, referring to Exhibit CHN-15.

Article 43. Even Article 43 does not address the detailed issue of sufficiency of evidence. Rather, Section 2 leaves such questions to the judicial authorities who weigh that issue in the exercise of their authority to order the remedies set out in Articles 44 to 46. Given the brevity of Section 5, which devotes two sentences to acts of infringement and two sentences to remedies (or penalties), it would be surprising if it was intended to create a broader obligation addressing issues of evidence and procedure. The terms used in Article 61 do not suggest that it was so intended. The different phrasing of the obligation to "provide ... to be applied" in the first sentence does not have a bearing on this issue.

7.652 For all of the above reasons, the Panel does not consider that the United States has made a prima facie case with respect to other indicia of infringement, such as physical evidence including product components, packaging and materials or implements.

(xi) *Other indicia – impact on the commercial marketplace*

7.653 With respect to the second limb of this claim, the United States also alleges that China's thresholds are tied to finished goods and therefore ignore other indicia of commercial scale operations, such as the impact that the piracy or counterfeiting has on the commercial marketplace and by extension, right holders.<sup>632</sup> The Panel will assess whether impact on the commercial marketplace can be taken into account by China's thresholds and then whether the term wilful trademark counterfeiting or copyright piracy "on a commercial scale" requires China to take into account impact on the commercial marketplace.<sup>633</sup>

7.654 The United States raises a concern in support of this argument related to the Internet and digital technological advancements that can permit commercial piracy and counterfeiting that creates major damage to a market.<sup>634</sup> The United States mentions the example of HDVDs (high-definition digital video discs) that can hold up to ten episodes of a TV series or several films.<sup>635</sup>

7.655 The Panel notes that the United States has not attempted to substantiate its assertion regarding HDVDs. This example appears to be based on the view that the term 张 (份) in the thresholds ("copies" for the sake of simplicity) refers only to physical discs and cannot be applied in any other way in a novel situation. There is no evidence on the record indicating that the thresholds have ever been applied to HDVDs, so this example is merely speculation based on the indirect reference to flat objects in the word 张 and to copies in the word 份.<sup>636</sup> This example can be compared to an assertion that a copyright law does not provide protection to computer programs simply on the basis that the legislation refers to the term "literary and artistic works" and computer programs are not obviously literary or artistic. Some evidence is required that the authorities could not or would not apply that measure in the appropriate manner to new technology.<sup>637</sup> The Panel notes China's assertion that, at such time as this issue arises for consideration, its authorities can apply the threshold in terms of the number of films or episodes on each disc.<sup>638</sup>

7.656 More generally, the argument with respect to new technology appears to be premised on the view that a determination of whether trademark counterfeiting or copyright piracy is "on a

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<sup>632</sup> United States' first written submission, paras 143 and 148 to 149; rebuttal submission, para. 112.

<sup>633</sup> See paragraph 7.496 above.

<sup>634</sup> United States' first written submission, para. 149; rebuttal submission, para. 112.

<sup>635</sup> The United States refers to a *China Daily* article reproduced in Exhibit US-39.

<sup>636</sup> See note 387 above.

<sup>637</sup> The Panel notes that, in this regard, the parties did not refer to subparagraph (17) of the first paragraph of Article 10 of the Copyright Law which provides for other rights for a copyright owner due to new technology. The United States' first written submission, para. 64, referred to this in relation to the Copyright Law.

<sup>638</sup> China's rebuttal submission, para. 25; response to Question No. 6.

commercial scale" must be able to take into account the impact of piracy or counterfeiting on right holders. However, the Panel recalls its findings at paragraph 7.577 above regarding the interpretation of the term "on a commercial scale". Read in context, that term refers to "wilful trademark counterfeiting or copyright piracy", which are acts of infringement. The benchmark of a typical or usual commercial activity is relevant to the assessment of whether counterfeiting or piracy is covered by Article 61. The impact is neither part of the act of infringement nor the benchmark of "on a commercial scale". Therefore, it does not appear to be a relevant consideration.

7.657 The Panel emphasizes that the terms used in the first sentence of Article 61, in particular "commercial", are technology-neutral. A "commercial scale" can apply to various forms of commerce and, hence, various means of infringement. The specific forms of commerce are not static but adapt to changing forms of competition due to technological development and the evolution of marketing practices.<sup>639</sup> The Panel sees no reason why those forms of commerce should be limited to the forms of commerce that existed at the time of negotiation of the TRIPS Agreement. Accordingly, the application of the term "commercial scale" can adjust to different situations, and refer to a different relative magnitude or extent, degree or proportion, depending on the facts.<sup>640</sup> However, subsequent technological developments do not alter the considerations relevant to the interpretation of the terms used in Article 61.

7.658 The United States also mentions an example of a "high-value niche market item" such as a specialized software application. This example refers to a *Seattle Times* newspaper article titled "*Inside China's teeming world of fake goods*".<sup>641</sup> The Panel accepts that the market for certain products may be small, but considers that a single, anecdotal newspaper article is insufficient evidence to demonstrate what is a commercial scale for such a product. To the extent that this article concerns the impact on the right holder, it has been addressed in the second limb of the claim.

7.659 The Panel observes a link between this argument and the issue of large-scale infringement with no commercial purpose. The United States originally submitted that the term "commercial scale" included the following:

"Thus, the concept of 'commercial scale' extends ... to those whose actions, regardless of motive or purpose, are of a sufficient extent or magnitude to qualify as 'commercial scale' in the relevant market."<sup>642</sup>

7.660 The United States indicated that this was not the focus of its submission, and confirmed that in this dispute it does not challenge the thresholds on the basis that they require a "profit-making purpose".<sup>643</sup> In response to a question from the Panel, the United States confirmed that its own Copyright Law was only amended in 1997 to deal with the problem of massive infringement, such as via the Internet, even if the infringing activity is not necessarily pursued for financial gain.<sup>644</sup>

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<sup>639</sup> See also the Panel Reports in *Canada – Pharmaceutical Patents* (at para. 7.55) and *US – Section 110(5) Copyright Act* (at para. 6.187) with respect to the phrase "normal exploitation" in Articles 30 and 13 of the TRIPS Agreement, respectively.

<sup>640</sup> The United States' concern regarding the volume of distribution by means of digital technology and the Internet is therefore relevant to the assessment of a "commercial scale": see United States' rebuttal submission, para. 112.

<sup>641</sup> United States' first written submission, para. 148, referring to Exhibit US-37.

<sup>642</sup> United States' first written submission, para. 110.

<sup>643</sup> United States' first written submission, paras 110 and 133, fn. 96; response to Question No. 59. See paragraphs 7.449 to 7.450 above, showing that Articles 213, 214, 217 and 218 of China's Criminal Law take account of a profit-making purpose.

<sup>644</sup> United States' response to Question No. 67.

7.661 For all the above reasons, the Panel does not consider that the United States has made a prima facie case with respect to impact on the commercial marketplace.

7.662 The Panel wishes to emphasize that its findings should not be taken to indicate any view as to whether the obligation in the first sentence of Article 61 of the TRIPS Agreement applies to acts of counterfeiting and piracy committed without any purpose of financial gain.

(xii) *Miscellaneous factors*

7.663 The United States asserted that the breadth of the term "on a commercial scale" presumes that a wide range of considerations should be probative of "commercial scale".<sup>645</sup> However, it did not submit argument in support of any other considerations besides those discussed above.

7.664 The Panel recalls its finding at paragraph 7.602 above that, if it is alleged that a Member's method of implementation does not provide for criminal procedures and penalties to be applied in cases in accordance with the first sentence of Article 61 of the TRIPS Agreement, that allegation must be proven with evidence.

7.665 The United States briefly mentioned various factors and examples, most raised by third parties, and apparently considers that these may be relevant to a determination of a "commercial scale".<sup>646</sup> It gave the example of "the manufacture of prototypes to test the infringer's production equipment"<sup>647</sup> but did not explain why this would not attract criminal liability under the Criminal Law, including its general provisions, or why it would constitute trademark counterfeiting or copyright piracy. It did not explain why "marketing and soliciting of business" would not attract criminal liability under the Criminal Law, including its general provisions, or why it would constitute trademark counterfeiting or copyright piracy. It did not explain why a "previous history of infringement" could not be covered by the threshold of "other serious circumstances".

7.666 Further, Japan, supported by the European Communities, and with whom the United States agreed, referred to a possible "organizational element" that can be taken into account in determining a commercial scale.<sup>648</sup> The Panel notes that Japan included this factor in its interpretation of "commercial scale" on the basis of a definition of "commerce" as a countable noun in French and Spanish that means, basically, a shop. However, the English language does not include the word "a commerce" in that sense. As the English version of the TRIPS Agreement is equally authentic<sup>649</sup>, the Panel does not consider this aspect of Japan's interpretation correct. Further, if a typical or usual commercial activity included an element of organization, in terms of cooperation with other parties, the United States has not explained why the general provisions of China's Criminal Law (discussed at paragraphs 7.439 to 7.446 above) that allow aggregation of infringing acts by different persons cooperating in a joint crime, are inadequate, beyond the issue of the level of the thresholds, or why the cumulation of infringements over time, or cumulation of infringing products on different premises within the definition of "illegal business operation volume" would be inadequate.

7.667 Therefore, the United States did not relate these factors sufficiently to the measures at issue or to its claim to discharge its burden of proof.

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<sup>645</sup> United States' first written submission, para. 113; see also rebuttal submission, para. 38.

<sup>646</sup> United States' response to Question No. 16; rebuttal submission, fn. 35 and fn. 36.

<sup>647</sup> United States' response to Question No. 62.

<sup>648</sup> See note 415 and United States' rebuttal submission, para. 38.

<sup>649</sup> See the final clause of the WTO Agreement.

7.668 The Panel recalls its findings at paragraphs 7.652, 7.661 and 7.667 above and finds that the United States has not made a prima facie case with respect to the second limb of its claim under the first sentence of Article 61 of the TRIPS Agreement.

(xiii) *Conclusion with respect to the claim under the first sentence of Article 61*

7.669 In light of the Panel's findings at paragraphs 7.632 and 7.668 above, the Panel concludes that the United States has not established that the criminal thresholds are inconsistent with China's obligations under the first sentence of Article 61 of the TRIPS Agreement.

#### **4. Claim under the second sentence of Article 61 of the TRIPS Agreement**

(a) Main arguments of the parties

7.670 The United States claims that, as China's criminal measures do not comply with the first sentence of Article 61 of the TRIPS Agreement, they are accordingly also inconsistent with China's obligations under the second sentence of that Article. In the United States' view, China can not make the necessary remedies "available" or sufficient to deter piracy and counterfeiting.<sup>650</sup>

7.671 China responds that the obligation in the second sentence of Article 61 is supplementary to, and contingent on, that of the first sentence of that Article. The obligation in the second sentence is only triggered in the event that a Member has an obligation under the first sentence to provide criminal procedures and penalties.<sup>651</sup>

(b) Main arguments of third parties

7.672 Australia argues that Article 61 creates an obligation of result, namely to put in place penalties that are sufficient to actively discourage others from engaging in such acts. A Member must actively prosecute and punish such acts. The question whether punishments are sufficient to provide such a deterrent is assessed in light of the circumstances in a Member's territory but it is open to another Member to challenge the adequacy of a Member's remedies to achieve the deterrent effect under the DSU.<sup>652</sup>

7.673 Brazil notes that the second sentence of Article 61 refers not only to imprisonment but also to monetary fines. In China, low-level infringement seems to be punishable at least with monetary fines following administrative proceedings. It seems to be overly formalistic to assume that because a domestic legal system qualifies monetary fines as administrative penalties, the core substantive issue of the deterrence capability of the remedy should be put aside.<sup>653</sup>

7.674 Canada submits that China's thresholds may make available administrative remedies, but they preclude the application of criminal penalties in cases that fall below the thresholds for criminal liability. The thresholds create "safe harbours" in which professional infringers are free to carry out wilful trademark counterfeiting and copyright piracy without risk of imprisonment or monetary fine. Rather than deterring infringement, the thresholds provide infringers clear parameters for committing wilful trademark counterfeiting or copyright piracy with immunity.<sup>654</sup>

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<sup>650</sup> United States' first written submission, paras 164-166.

<sup>651</sup> China's first written submission, paras 144-147.

<sup>652</sup> Australia's third party written submission, para. 25.

<sup>653</sup> Brazil's third party written submission, paras 39-42.

<sup>654</sup> Canada's third party written submission, para. 12.

(c) Consideration by the Panel

7.675 The Panel observes that the United States has made this claim contingent upon the outcome of its claims under the first sentence of Article 61 of the TRIPS Agreement. Additional findings regarding this claim under the second sentence of Article 61 would not contribute further to a positive solution to this dispute. Therefore, it is unnecessary for the Panel to rule on this claim.

**5. Claim under Article 41.1 of the TRIPS Agreement**

(a) Main arguments of the parties

7.676 The United States claims that China has failed to make the procedures and penalties required by the first and second sentences of Article 61 "available" as required by Article 41.1 of the TRIPS Agreement.<sup>655</sup>

7.677 China responds that the United States has failed to show that China breaches its obligations under Article 61 and therefore fails to show that China breaches its obligations under Article 41.1.<sup>656</sup>

(b) Main arguments of third parties

7.678 Argentina submits that China's measures do not appear to be inconsistent with Article 41.1 of the TRIPS Agreement. Article 41.1 should be read in light of Article 1.1, which provides flexibility in implementation; Article 41.2 which requires Members to ensure that enforcement procedures are fair and equitable; and Article 41.5 which renders the obligation in Article 41.1 relative, not absolute.<sup>657</sup>

7.679 Canada refers to its arguments regarding the claims under Article 61. Further, the fact that "a plethora of counterfeit and pirated goods continues to be produced, reproduced and distributed in China, and exported from China", makes it clear that China does not provide effective action against wilful acts of infringement on a commercial scale and does not provide remedies that deter further infringements, contrary to Article 41.1.<sup>658</sup>

(c) Consideration by the Panel

7.680 The Panel observes that this claim is consequent upon the outcome of the claims regarding the criminal measures under Article 61 of the TRIPS Agreement. Additional findings regarding this claim under Article 41.1 of the TRIPS Agreement would not contribute further to a positive solution to this dispute. Therefore, it is unnecessary for the Panel to rule on this claim.

**6. Conclusions with respect to the criminal thresholds**

7.681 The Panel recalls its conclusion at paragraph 7.669 above that the United States has not established that the criminal thresholds are inconsistent with China's obligations under the first sentence of Article 61 of the TRIPS Agreement.

7.682 The Panel exercises judicial economy with respect to the claims under Article 41.1 of the TRIPS Agreement and under the second sentence of Article 61 of the TRIPS Agreement (with respect to the criminal thresholds).

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<sup>655</sup> United States' first written submission, paras 167-169.

<sup>656</sup> China's first written submission, paras 148-150.

<sup>657</sup> Argentina's third party written submission, paras 30-37.

<sup>658</sup> Canada's third party written submission, para. 13.

## VIII. CONCLUSIONS AND RECOMMENDATION

8.1 For the reasons set out in this Report, the Panel concludes as follows:

- (a) the Copyright Law, specifically the first sentence of Article 4, is inconsistent with China's obligations under:
  - (i) Article 5(1) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement; and
  - (ii) Article 41.1 of the TRIPS Agreement;
- (b) with respect to the Customs measures:
  - (i) Article 59 of the TRIPS Agreement is not applicable to the Customs measures insofar as those measures apply to goods destined for exportation;
  - (ii) the United States has not established that the Customs measures are inconsistent with Article 59 of the TRIPS Agreement, as it incorporates the principles set out in the *first* sentence of Article 46 of the TRIPS Agreement; and
  - (iii) the Customs measures are inconsistent with Article 59 of the TRIPS Agreement, as it incorporates the principle set out in the *fourth* sentence of Article 46 of the TRIPS Agreement; and
- (c) the United States has not established that the criminal thresholds are inconsistent with China's obligations under the first sentence of Article 61 of the TRIPS Agreement.

8.2 The Panel exercises judicial economy with respect to:

- (a) the claim under Article 5(2) of the Berne Convention (1971), as incorporated by Article 9.1 of the TRIPS Agreement; and the claims under Article 61 of the TRIPS Agreement (with respect to the Copyright Law); and
- (b) the claims under Article 41.1 of the TRIPS Agreement and under the second sentence of Article 61 of the TRIPS Agreement (with respect to the criminal thresholds).

8.3 Under Article 3.8 of the DSU, in cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered *prima facie* to constitute a case of nullification or impairment. China did not succeed in rebutting that presumption. Accordingly, the Panel concludes that, to the extent that the Copyright Law and the Customs measures as such are inconsistent with the TRIPS Agreement, they nullify or impair benefits accruing to the United States under that Agreement.

8.4 In light of these conclusions, the Panel recommends pursuant to Article 19.1 of the DSU that China bring the Copyright Law and the Customs measures into conformity with its obligations under the TRIPS Agreement.

### *Concluding remark*

8.5 In this dispute, the Panel's task was not to ascertain the existence or the level of trademark counterfeiting and copyright piracy in China in general nor to review the desirability of strict IPR

enforcement. The United States challenged three specific alleged deficiencies in China's IPR legal system in relation to certain specific provisions of the TRIPS Agreement. The Panel's mandate was limited to a review of whether those alleged deficiencies, based upon an objective assessment of the facts presented by the parties, are inconsistent with those specific provisions of the TRIPS Agreement.

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