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# Trade Sanctions and the Rule of Law: Lessons from China

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The “Rule of Law” is a phrase which comes loaded with tacit assumptions and unarticulated values. As Americans, we associate the concept with due process, the doctrines of natural rights and natural law, an independent judiciary and the institution of judicial review. When viewing legal developments in China and around the globe, we look through a filter created by a shared intellectual heritage. But however positive a role these beliefs have played in the development of the American state, when applied to other nations our assumptions become deterministic; we tend to assume that given a proper legal environment – an independent judiciary, a government constrained by law, and transparent regulation – that sustainable economic growth and a democratic political system will result. Consciously or not, we use our ideas of what a legal system should be to judge the progress, or lack thereof, in developing nations.

This standard of review has become particularly prevalent in the context of American foreign policy and international trade. Both Warren Christopher and Madeline Albright as Secretary of State have made rule-of-law development “... an integral part of [the] agenda as Sec[retary of] State... and ... a central feature of U.S. foreign policy...[because of its] centrality to... promoting democracy and human rights, building free and fair markets, and fighting international crime and terrorism.”<sup>71</sup> Regarding China’s accession to the World Trade Organization (WTO), President Clinton has argued that China’s accession will “draw China into a system of international rules and thereby encourage the Chinese to choose reform at home and integration with the world.”<sup>72</sup> United States Trade Representative (USTR) Charlene Barshefsky, a vocal proponent of China’s bid to rejoin the WTO, said that “... our [WTO] agreement brings China further away from the legal void of the Maoist era, and closer to the rule of law.”<sup>73</sup> Explicitly linking the absence of an effective legal system to the chaos and destruction of the Chinese Cultural Revolution, Barshefsky cited the effect of U.S.-China intellectual property negotiations in strengthening the rule of law in China: “...[T]o develop intellectual property policy is to draft and publish laws; train lawyers and officials; improve and ensure access to judicial procedures – ultimately, to create a culture of rights, due process, and limits on arbitrary state

power where it did not exist before.”<sup>74</sup>

But is this linkage between WTO membership, trade sanctions, and legal development justified? This paper examines the intensive U.S.-China negotiations over intellectual property (IP) rights in the 1990s and the current WTO negotiations with the purpose of describing the effects of U.S. trade policy on the development of Chinese legal institutions. It concludes that the use of trade sanctions to force IP reform in China during the 1990s not only did not promote the rule of law, but actively hindered its development in several key respects. Similar constraints suggest that WTO membership alone is unlikely to promote the rule of law within China; rather, the process of legal development in the PRC will most likely be the outcome of internal dynamics which are beyond either the moral authority or the capacity of the U.S. Government and international institutions to direct. A de-linking of trade policy and rule-of-law programs and a renewed emphasis on NGO and targeted legal-development programs is thus more likely to promote U.S. goals as stated.

Part II of this paper seeks to unpack the notion of the “rule of law”, and define it and its relationship to political liberalization with a functional approach to legal development. Part II will also briefly evaluate legal development and reform in China using this analysis, and present inferences drawn regarding the future of rule-of-law reform in the post-Deng era. Part III presents an historical overview of IP protection under Chinese law through 1979, and Part IV will then focus upon IP development and the Sino-American negotiations from 1979-1995. Part V examines the emphasis on administrative remedies contained within of the 1995 Memorandum of Understanding, and examines the effect measures mandated therein by the U.S. had upon the development of Chinese legal institutions during the past five years. Part VI examines the potential of an alternative emphasis on private, civil law remedies, and the Conclusion at Part VII offers suggestions and observations regarding future development of the rule of law in the PRC.

## I. THE RULE OF LAW AND POLITICAL LIBERALIZATION

### A. Defining the Rule of Law: A Functional Approach

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What elements are necessary to constitute a “legal system”? When applying this analysis to rule-of-law development abroad, it is important to distinguish the functional aspects of a legal system from the broader Western intellectual tradition purportedly derived from a “universal” conception of human nature and divine justice. One cannot cut a limb from one philosophic and religious approach to law, graft it onto a separate intellectual tradition, and expect it to function in a comparable manner. At the same time, however, it is also important not to over-emphasize the legacy of the past; the study of post-Mao China demonstrates the adaptability and pragmatic approach of her people, and their willingness to make dramatic changes in order to advance China’s place in the world order.

A focus on positive law, or the body of law consisting of enacted statutes and regulations, is likewise singly insufficient to describe the complex interaction of law, society, and government. To think of law as commands backed by the coercive authority of the State mistakes obedience for submission; although it may be combined with the threat of harm, the command embodied in law is primarily an appeal to respect for authority. An effective legal system rests upon the legitimacy implied where a police officer lawfully asks you to step out of your car, not when a gunman offers you a choice between your money and your life. In this sense, law can be considered a set of rules which rest upon a perceived and generally accepted *obligation* the citizenry owes to the body politic, and not necessarily an obligation to the rules or the rulers themselves.

It is more useful to think of law in a second sense, as a set of *enabling rules* which facilitate the realization of structured rights and duties within a pre-defined system. This secondary set of rules does not flow directly from State interests; instead, it provides a framework which allows the citizens to organize their affairs in a predictable and consistent manner. Contract laws, for example, do not exist for the direct benefit of the State, but allow the citizen-businessman to conduct his economic affairs with reduced risk. An error in a sales contract between private parties would not be considered an ‘offense’ against the polity, however it may (if sufficiently egregious) deny the citizen-businessman recourse to the legal remedies necessary to enforce it. The State indirectly benefits from the reduced costs of administration (i.e., mediating or otherwise containing disputes which would arise) and also from the role such predictability plays in promoting economic development. Five salient requirements are integral to this system of enabling rules. The first requirement is that enabling rules be *cognizable*, i.e. identifiable as “law” in contrast to existing norms or unwritten rules of obligation. Article X of the General Agreement on Tariffs and Trade (GATT) discusses this requirement in terms of *transparency*, stating the all trade-related “laws, regulations, judicial decisions, and

administrative rulings of general application.... shall be published promptly and in such a manner as to enable governments and traders to become acquainted with them.”<sup>75</sup> Law must be cognizable as separate from the mores and standards which make up society as a whole.

Second, an effective system must include a *judicial mechanism*, or a pre-existing system which allows an authoritative and final evaluation of claims. This system must be able to decide claims with *consistency* and a reasonable level of *efficiency*, lest the unpredictable or uneconomical resolution of claims prevent the legal system from fulfilling its enabling function. Every system of justice is allied with the sovereign, and is influenced by political considerations to a greater or lesser extent. However, where the political considerations come to predominate, the system becomes a mere appendage of policy and consistency is lost in the ebb and flow of political priorities.

Finally, the system must allow for *adaptability within the framework* mentioned above. Rarely do courts render a decision solely in reference to the codes; more often, they frame their judgements as to give the impression that their decisions are the necessary consequence of predetermined rules whose meaning is fixed and clear. In the vast majority of cases that trouble the courts, neither statutes nor precedents in which the rules are allegedly contained allow only one result. In the most important cases, the court is offered a choice. The judge must choose between alternative meanings to be given to the words of a statute or between rival interpretations of precedent. It is only the tradition that judges ‘find’ and do not ‘make’ law that conceals this, and presents their decisions as if they were deductions smoothly made from clear pre-existing rules without intrusion of the judge’s choice. But this final requirement is necessary to ensure the vitality of the system; without it, stagnation would inevitably result.

Enabling rules codify an activity utterly different from performance of duty or submission to coercive control; they represent a system distinct from and superior to one designed to ensure subjugation. Such power-conferring rules are thought of, spoken of, and used by both citizen and state differently from rules which impose duties, and are valued for different reasons. Rules seeking to establish the obligation to obey sovereign commands are ubiquitous; it is the creation of enabling rules and a system to enforce them which constitutes the crucial step from the pre-legal to the legal world.

## B. Law, Development and Legitimacy

The nexus connecting political culture and law is a complex one. A statute is, by itself, meaningless; if it is to be obeyed, it must resonate at some level within the domestic environment it purports to constrain. Laws can be legiti-

mated either by the nature of the regulation (it is not accidental that law and morality frequently overlap) or the process by which they were created.

Why would a sovereign choose to advocate supremacy of the law, rather than supremacy of his own authority? In an insightful study of law and development in Guangdong,<sup>6</sup> Linda Chelan Li argues that Beijing's policy promoting *fazhi guojia* (rule the nation according to law) was well-received in Guangdong Province, historically a place where "heaven was high, and the Emperor far away," in part because of a desire on the part of both central and local governments to establish a rule-based relationship governing tax remittances between the two. During the 1980s, the central-provincial fiscal system consisted of a series of negotiated "contracts," wherein the provincial government was to turn over to Beijing either a fixed amount or a specified percentage of revenue received. While the original intention was to provide a predictable fiscal environment, in the absence of an effective legal system both sides became adept at using loopholes. On top of contractual remittances, for instance, the national government might demand additional payments in the form of new taxes, mandatory purchase of state bonds, or fiscal "loans" which were never repaid.<sup>7</sup> Anticipating this, provincial officials engaged in a wide variety of means to minimize their financial exposure, including diversion of resources into ostensibly separate budgets, generous tax exemptions to key enterprises, and by underreporting income. Both sides came to see themselves as losers in what Ms. Li describes as the "ambiguity game;"<sup>8</sup> Beijing felt that the Guangdong provincial government, which benefited financially from explosive growth in the 1980s and early 1990s, was not shouldering its financial fair share, while the Guangdong government wished to contain Beijing's ability to impose extra-contractual remittances.

As this example illustrates, the power of even an authoritarian sovereign to enforce enacted law is not absolute; decrees can be evaded, subverted, or simply ignored. Indeed, the situation in Guangdong continues to be resolved through the less formal negotiation process and poses a serious impediment not only to the coffers but also to the successful implementation of other policies articulated by the national government. This demonstrates the imperative need for a consistent, rule-based system even in an authoritarian state.

Crafting a legal system which incorporates the disputants and fairly resolves the dispute creates political legitimacy and assures a basic continuity of process. The sovereign, by working within a legal framework, imparts legitimacy to his commands. By expanding the system to include enabling rules as well, the sovereign also integrates disputes normally outside the State sphere within the process, reaps the indirect benefits of dispute-resolution, and promotes a stable environment for economic growth.

### C. *Fazhi Guojia*: Rule of Law, or Rule by Law?

The phrase *fazhi guojia* is generally translated as "rule the nation according to law", but the exact meaning of *fazhi* can imply advocacy of either "rule of law" or "rule by law". The difference is more than mere semantics; the former implies the use of law as a process, potentially in accordance with the view of law as a system of enabling rules, while the latter indicates an instrumental use of law solely as a tool of governance to facilitate social control. This connotation is generally in accordance with traditional Confucian and Communist views of law, and historically has done little to promote law as an enabling system.

#### 1. The Confucian Tradition as Rules of Obligation

Chinese law from the Qin Dynasty (221-206 B.C) through the Qing (1611-1911 A.D.), characterized by commentators as "overwhelmingly penal in emphasis,"<sup>9</sup> serves as a clear example of obligatory law, or rules seeking to establish subjugation to the body politic. What make the Chinese case unique, and has engendered sharp debate amongst commentators, is the utilization of both *li* (moral ritual) and *lu* (positive law) in creating the system of obligatory rules. The Legalist tradition emphasized the use of positive law as an instrument of governance, to insure social control and provide standards for the imposition of punishment. This instrumental utilization of law was placed subordinate to the Confucian tradition, in which a well-ordered society would arise from moral persuasion and the example of virtuous leaders with minimum reliance upon laws as a supplemental tool. As noted China authority Willam Alford writes:

[The] Chinese neither saw public, positive law as the defining focus of social order nor divided it into distinct categories of civil and criminal. Chinese thought arrayed the various instruments which the state might administered and social harmony maintained into a hierarchy ranging downward from heavenly reason (*tianli*), the way (*tao*), morality (*de*) ritual propriety (*li*) customary (*xixu*) community contracts (*xiang ye*) and family rules (*jia cheng*) to formal law (*lu*).<sup>10</sup>

The result was a system which relied extensively upon the regional magistrates and their Confucian moral training; law was reserved as a tool of last resort for those individuals who could not be persuaded to follow the path of moral enlightenment.

As a result, the Tang Legal Codes, which were preserved virtually *in toto* in succeeding dynasties up until 1911, contain little of what Western scholars would think of as civil law. While the Codes dealt with succession and inherit-

ance, marriage, family, and quite thoroughly with criminal law, commercial and economic matters were largely left to the provenance of merchant guilds.<sup>11</sup> Even the inclusion of family law in the Codes was intended to advance State interests; clan members were expected to maintain order within their lineage, and were responsible for the conduct of their members.<sup>12</sup> Thus, whether broader social standards formed an “implicit” framework supplying legal standards where the *lu* was silent, as has been suggested by some scholars,<sup>13</sup> is irrelevant; both were instruments used almost exclusively for purposes of State administration and the maintenance of social harmony.

## 2. Marxism-Leninism and Law

Marxism-Leninism viewed law as a tool of exploitation, a mere mechanism designed to insure the perpetuation of the ruling class. In June 1949, one month after the Communist forces gained effective control of China, the Chinese Communist Party (CCP) issued directives repealing all laws made by the Nationalist Party (KMT).<sup>14</sup> The CCP, true to their ideological heritage, emphasized that the fundamental task of the socialist legal system was to consolidate proletarian dictatorship of the people, and suppress the enemies of the fledgling socialist state.<sup>15</sup> Article 4 of the 1954 Constitution of the PRC imitated the socialist construction of the Soviet Constitution, with the stated objective of “... wip[ing] out gradually the exploiting class... and build[ing] up a socialist country.” From 1954 to 1960, some 148 laws and statutes were enacted, and 731 administrative regulations were promulgated. Only a few non-criminal statutes dealt with private activity, and most of these were concerned with the political needs of socialist transformation and the establishment of socialist public ownership.<sup>16</sup>

Beginning with the Anti-Rightist Campaign in 1957 and continuing into the Great Proletarian Cultural Revolution (1966-1976), the legal system and its functionaries fell under political attack. Lawyers were jailed for defending clients charged with political subversion, and judges were persecuted for “rigidly” placing law above the People’s Revolution, a “reactionary view”. Many were exiled to the countryside, imprisoned, or criticized. In 1958, the Beijing government began to merge public security organs with people’s courts and procurators, into one Ministry of Politics and Law. As part of this process, the number of court personnel was drastically cut; in 1956, there were as many as 41,483 judges, lawyers, and staff, but by the end of 1958 there were 32,068, a reduction of 22.7 percent.<sup>17</sup> Also beginning in 1958, most civil disputes were directly dealt with by the mediation committees of the People’s Communes, and the total number of civil cases filed with the court between 1957 and 1960 decreased by nearly 40 percent.<sup>18</sup>

During the peak years of the Cultural Revolution, the legal system as a distinct entity effectively ceased to exist; in many parts of the country, cases were tried illegally by executive agencies, the leaders of people’s communes, and by various working groups and Revolutionary Councils in violation of the Constitutional provision that specified “judicial power is exercised by the people’s court.”<sup>19</sup> When cases were tried, political slogans and the decisions of individuals – not rule-based standards - prevailed.

## 3. Opening the Door:

### Legal Reform in China after 1978

Examination of the post-Mao legal reforms fully illuminates the dichotomy between law as a system of sovereign-enforced rules of obligation and law as a system of enabling rules. Initially viewed in the aftermath of the Cultural Revolution as a tool to reassert Party control, Deng Xiaoping’s policy of promoting *fazhi guojia* has grown to encompass genuine reform. The purpose of this final section of Part II is to provide an analytical context for understanding developments of intellectual property law by examining the thrust of legal reform after 1978.

In a speech given at the closing ceremony for the Central Working Conference of the Eleventh Party Congress in 1978, Deng Xiaoping announced four slogans to guide Party officials in the promotion of *fazhi guojia*.<sup>20</sup> The four slogans - *youfa keyi* (law for people to follow), *youfa buyi* (laws where people currently do not obey), *zhifa buyan* (laws not strictly enforced) and *weifa buyu* (lawbreakers not caught) outlined Deng’s perception of the failures of the existing legal system, and his emphasis indicated the primary goal of the resurrected legal system was to restore the authority of the Communist Party. Indeed, one source reports that Party leadership originally preferred the expression “strengthening the law and the legal system” to “strengthening the rule of law”, because of concerns regarding the latter’s potential implications for broader political reform.<sup>21</sup> Deng’s “new” policy echoed the traditional instrumentalist conception of law as a tool for facilitating subjugation to the sovereign.

The promotion of *fazhi guojia*, however, also included elements which set the stage for the development of deeper legal reform. Beijing recognized the importance of a legal system capable of supporting economic development; as one official stated, the “market economy is a legal economy”, *i.e.* a healthy market is a regulated one.<sup>22</sup> Growing out of Beijing’s successful experiments with agricultural reforms in the early 1980s, privately run enterprises were allowed under an amendment to the 1988 PRC Constitution. More importantly, however, the State began to construct a system of legal rules to promote economic de-

velopment, technology transfer, and foreign investment. Private economic interests were explicitly (if grudgingly) recognized. While this was done with the goal of promoting national development, the existence of laws protecting private interests and the first hesitant steps toward development of concomitant legal protections and an infrastructure to enforce them, represented a positive step gain for the rule of law.

As the legal reforms progressed, Beijing began to utilize law as an alternative to existing internal Party systems to bring the abuses of lower officials to light. The Administrative Litigation Law (ALL),<sup>23</sup> passed in 1990, allows private citizens to challenge certain types of administrative decisions in court, and the State Compensation Law, passed in 1992, allows recovery by private citizens for damages caused by narrowly defined categories of official misconduct. The Administrative Supervision Law,<sup>24</sup> passed in 1996, limits the power of officials to administer penalties and punishments, and specifically requires officials to adhere to vaguely-defined principles of transparency, legal authority, and due process in making their decision. Since the passage of the Administrative Penalties Law in 1996, some 35,000 cases of corruption and/or mistreatment by state officers were prosecuted under its aegis; in 1999 alone, 51,370 cases were filed.<sup>25</sup> Significantly, two-thirds of the judgements on these cases were decided in favor of the citizen-plaintiff.<sup>26</sup>

It is important to emphasize that these measures are not intended to promote popular, democratic rights vis a vis the government; rather, they represent an attempt to force lower officials to conform with standards articulated in Beijing. The new Legislation Law (Legislation Law), enacted by the National People's Congress (NPC) on March 15, 2000, seeks to clearly establish the NPC (and the Party) as the final arbiter of the law and its application. The Legislation Law formally establishes the legal hierarchy amongst the Constitution, laws, various administrative orders, rules, and regulations at the national and local levels. Articles 71-73 require that all administrative regulations must expressly identify their legal authority, and be published in designated official publications (Article 77). The Legislation Law further lays out required legislative procedures, including timely notification, quasi-public meetings or discussions, and three readings before the legislative committees and the full legislative body. But the Legislation Law also grants the NPC Standing Committee sole authority to interpret laws (Art. 42), subject to an override by the full NPC. Only the NPC and the NPC Standing Committee may declare a law or regulation unconstitutional, or invalid because of conflict with a higher statutory authority. The Supreme People's Court, the State Council, various Ministries, and local agencies are explicitly denied authority to interpret the constitutionality or validity of any stat-

ute (art 90). The evident intent of this statute is to retain sole authority for law and legal reform in the hands of the legislature, and ultimately the Communist Party.

#### D. America, China, and the Rule of Law

Modern Chinese law exists in a transient state; the present legal system is intended to provide enabling rules and rights only so far as they strengthen the rule of the Communist Party. Yet within the system exist nuclei which represent a genuine departure from the traditional utilitarian approach to law. The compromises Beijing has created formally recognize the importance of a private sphere of action in facilitating economic growth, and also recognize (at least conceptually) the importance of a legal system to enforce them. Legal mechanisms to effectively enforce the rights so created, however, are notably absent.

This paper now turns to an examination of the interaction between American trade policy and legal development in China. Part III will begin with a historical overview of intellectual-property protection in China.

## II. EARLY DEVELOPMENT OF INTELLECTUAL PROPERTY PROTECTION

### A. Emperors and Intellectual Property

The earliest historical records dealing with intellectual property rights in China indicate the concern of officials with publication and republication of works related to the imperial throne. Han dynasty regulations (circa 200 B.C.), for example, barred the unauthorized reproduction of the Confucian Classics.<sup>27</sup> The Classics and accompanying commentary served as one of the most important ideological bases legitimizing the rule of the Han Emperor, hence the concern of the Court with their ideological orthodoxy.

A proclamation by the T'ang Emperor Wenzong in AD 835 similarly evinced concerns regarding control over works related to Imperial authority. The proclamation, which became part of the T'ang Code and was adopted by later dynasties, prohibited the unauthorized reproduction of calendars, almanacs, and items which could be used in prognostication which were at the time being produced in the southern regions and distributed throughout China.<sup>28</sup> Questions of time and astronomy were central to the Emperor's role as the link between human and heavenly events, and so were tightly controlled by court astronomers. Works of prognostication were also of concern because of their potential use in predicting the dynasty's downfall. Before its

collapse, the emperors of the T'ang dynasty also prohibited the unauthorized copying and distribution of state legal pronouncements, official histories, and the reproduction, distribution, or possession of works related to the "devil works", the competing faiths of Buddhism and Taoism.<sup>29</sup>

The Song Dynasty (960 – 1279 AD) saw a marked increase in the production of printed materials. The invention of moveable type by Bi Sheng around the year 1000 had profound effects on the manufacture of printed materials because of the complexity of the Chinese language.<sup>30</sup> Because of the rapid spread of printed works, the Zhenzhong Emperor ordered private printers to submit works they intended to publish to local officials for prepublication review in order to control heterodox materials.<sup>31</sup> Persons failing to obtain official review prior to printing works that were neither subject to exclusive state control nor banned altogether might suffer one hundred blows with the heavy bamboo cane and destruction of their printing blocks;<sup>32</sup> however, no laws forbade reproduction by any printer of works that had been authorized by Imperial censors.

The law regarding publication and dissemination of works underwent relatively few changes from the Song until the Ming dynasty (1644-1911). The system of imperial censorship appears to have lost vitality during this time; despite the formal legal continuation of the Song censorship system, the Qianlong emperor in 1744 found it necessary to re-issue a decree requiring pre-publication review to "preserve the moral integrity of the State."<sup>33</sup> Thirty-four years later, in 1778 the Qing Emperor again directed the re-institution of a strict system of local prepublication review.<sup>34</sup> The limited effect of the two decrees is likely attributable to the fact that many of the literati either were government officials, or were closely related to them, and were themselves responsible for the existence of the printed materials.

At the close of the Ming there existed no centrally promulgated legal protection for either proprietary symbols or inventions, except for those relating to the imperial family<sup>35</sup> or protection for marks placed on goods made exclusively for imperial use.<sup>36</sup> During the Ming and Qing, however, an informal system of guild registration and protection of marks was instituted, where a manufacturer could register his trade mark with other guilds or occasionally with a local magistrate.<sup>37</sup> In the event of trademark infringement recourse to local officials could occasionally be had by imploring the magistrate to prevent fraud and unfairness; in one case, sericulturalists in Shanghai were able to get the local magistrate to order that infringement of their unique mark be stopped.<sup>38</sup> These remedies, however, were not found in the legal code, and hence were dependent upon the ability of the manufacturer to appeal to local trade guilds and officials.

## B. The End of the Dynasties: IP in the Late Qing and Warlord Period (1911-1927)

Piracy became a major problem with the wide dissemination of Western learning within China. Initially dismissive, intellectuals and government officials began to realize the importance of "barbarian learning" in establishing a modern, militarily capable nation. Many Chinese felt that unhindered translation and reprinting of Western books was justified as necessary.<sup>39</sup>

The same time period evidenced a boom in IP consciousness in the West, as the growth of industrialization made ideas more valuable in the commercial sense. In 1883 the International Union for the Protection of Industrial Property was signed; commonly referred to as the Paris Convention, the organization provided international protection for patents and trademarks. In 1886 the International Union for the Protection of Literary and Artistic Property was formed;<sup>40</sup> the so-called Berne Convention addressed issues of copyright protection amongst the Western nations.

The Chinese were not, however, signatories to either convention. Western rights holders could register marks with Imperial Maritime Customs Service, established in 1854 and controlled by Western powers (primarily the British), but such registration would be effective only inside the treaty ports.<sup>41</sup> Accordingly, in 1903 the U.S. sought to include an agreement protecting intellectual property with a broader trade agreement. The final agreement, the Treaty with China for the Extension of the Commercial Relations (Treaty of 1903),<sup>42</sup> provided that intellectual property protection would be extended on reciprocal basis, after the Chinese had established a patent office and adopted a patent law, but did not set a date for establishing such an agency or providing interim protection.<sup>43</sup> The agreement specifically excluded translations of Western works done by Chinese.<sup>44</sup>

Conflict over the implementing measures prevented the establishment of an IP legal regime. A short-lived copyright law was promulgated in 1910;<sup>45</sup> it was abrogated on the founding of the Republic in 1912, but re-enacted in substantially same form in 1915.<sup>46</sup> The law did not purport to put the Treaty of 1903 into effect, and gave limited copyright protection to Chinese authors only. Because the Treaty of 1903 specified that protection was to be accorded in the "same way and manner and subject to the same conditions"<sup>47</sup> as trademark protections, the Chinese government contended, it was premature to issue a more complete copyright law until the trademark law "goes into force and proves acceptable and effective." The proposed trademark law, in turn, was delayed due to disputes between the Chinese Ministry of Commerce, the Customs Service advisors, and the foreign powers, and was not adopted until almost two decades later.<sup>48</sup>

In the interim, foreign groups commenced negotiations amongst themselves designed to provide reciprocal protection in the treaty ports. The U.S. and France exchanged diplomatic notes agreeing to extend bilateral protections in 1911,<sup>49</sup> and by 1919 the agreements covered all the Western treaty ports. Thus, an American national who registered in Italy would be able to bring action before the Italian Consular Court in China against a person subject to the jurisdiction of that court.<sup>50</sup>

Not surprisingly, relatively few cases of copyright infringement were brought. The G&C Merriam case, brought in the Shanghai Mixed Court in 1923, demonstrates the difficulties faced in securing judicial protection of copyrights in the era. G&C Merriam had spent several years preparing a bilingual version of Webster's Dictionary for sale in the Chinese market. However, before the dictionary could be released, Merriam managers discovered the Commercial Press in Shanghai had already begun to distribute its own virtually identical version. Merriam brought suit in 1923 at the Mixed Court in Shanghai, invoking both the copyright and trademark provisions of the treaty of 1903 between the U.S. and China. The Mixed Court found, however, that the dictionary did not fall within the limited class of American works entitled to copyright protection, but did fine the Commercial Press for using a seal on the cover which was very similar to that used on the Webster's Dictionary; the court accordingly fined the Shanghai printer 1,500 *liang* of silver but did nothing to halt continued publication.<sup>51</sup>

Throughout the late Qing and Republican era, the Chinese government remained focused on control over ideas and the maintenance of order, rather than protection of private economic interests. Registration of newspapers and magazines was required by government edicts issued and re-issued in 1907, 1908, and 1909.<sup>52</sup> Rulers seemed more interested in using the guise of legal development to promote their legitimacy than any genuine desire to see reform; Republic President Yuan Shikai wished to be known as the Hongxian (Great Constitutional) Emperor in the belief that this would demonstrate his self-professed abiding commitment to the rule of law,<sup>53</sup> despite his intention to restore the monarchy and abolish the Republic.

William Alford convincingly argues that much of the motivation behind the development of intellectual property laws during this period stemmed from the promises of Western powers to end the extraterritorial status of the treaty ports, when and if domestic Chinese law had improved enough to maintain order and enforce the rights of foreign traders. The outcome — development of formal legal protection, but little or no improvement in enforcement mechanisms — reflected these ulterior motives behind the formation of the laws. When the Western powers proved reluctant to relinquish control, the Chinese proved similarly un-

willing to develop new intellectual property laws or enforce existing ones.<sup>54</sup>

### C. The Nationalist Period (1927-1949)

The collapse of the Republic and the formation of the Nationalist Party (GMD) ushered in an active period of legal development. Foreign-trained Chinese and German legal advisors were brought in to draft a new Constitution and a modern legal code.

In 1928, a new Copyright Law was passed. Protection under Chinese law was extended to foreign nationals on a reciprocal basis if the copyrighted works were "useful to the Chinese [people]," for a period not to exceed 19 years.<sup>55</sup> Whether the work was "useful" under the law was determined by the Ministry of Internal Affairs. This same Ministry had authority to block registration of foreign and domestic works where the work "obviously goes against the doctrines" of the GMD or where "the release of the work is prohibited by other laws."<sup>56</sup> These restrictions were amplified in the Publication Law<sup>57</sup> and its implementing regulations: according to Article 19, registered works could not contain anything "intended to... undermine the Guomindang" or violate the Three People's Principles [of Sun Yatsen], "to overthrow the Nationalist Government or to damage the interests of the Republic of China", to "destroy public order" or to "impair good customs and habits". A permit was required for all works to be published, regardless of whether a copyright was sought; failure to obtain a permit could result in imprisonment, fines, seizure of publications, and destruction of the type.<sup>58</sup>

Protection for trademarks also required registration with the central government, which had authority under Article 2 of the 1930 Trademark Law to bar marks it deemed prejudicial to public order or marks which utilized the portrait or name of Dr. Sun Yatsen, the plum blossom (symbol of Guomindang), or other signs evocative of the national government or the Guomindang Party.

Under the terms of the Trademark Law, Chinese nationals received 30 years of protection, while foreigners received 10 years. The U.S. objected to the new Trademark Law as conflicting with the provisions of the 1903 Treaty, and the Nationalist government agreed not to apply the 10-year limit to American nationals and to drop the requirement that the copyrighted works be "useful" to the Chinese.<sup>59</sup> The U.S. also concluded the Treaty of Friendship, Commerce and Navigation with Nationalist China on November 4, 1946; article IX provided for a system of mutual obligation with respect to intellectual property laws.<sup>60</sup>

While the internal chaos and problems wrought by civil war with the Communists added to the difficulty of developing the legal infrastructure, the tension between the perceived need for strong State control and the requirements

of an capable, politically independent judiciary proved to be the largest impediment to promotion of the rule of law. Harvard-trained political scientist Qian Duansheng concluded during the last years of the Nanking era that “in draftsmanship the codes are, on the whole, well done. If they have not been duly enforced, it is... because of the inaccessibility of the courts, the incompetence of the judges, and especially, the interference of authorities other than judicial in the administration of justice.”<sup>61</sup> In the words of a generally sympathetic 1945 report by the Subcommittee of the National Foreign Trade Council in New York, “adoption of suitable statutes relating to Patents, Trademarks and Copyrights will not be enough if China is to derive any real benefit.... No matter how sound a law may be, it is of no value if it is not enforced.”<sup>62</sup>

#### D. Intellectual Property in a Socialist Economy (1949-1976)

Reflecting both their Marxist-Leninist and Confucian heritage, the Communist Party did not seek to protect intellectual property when it came to power in 1949. In June of that year, all laws made by the GMD were repealed.

The Communist Party did, however, pass laws designed to smooth the transition between the capitalist and socialist systems. The Provisional Regulations on the Protection of Invention Rights and Patent Rights, adopted on August 11, 1950, provided a 2-track system of incentives and protection for patents. The State could grant the inventor a ‘certificate of invention’ which would allow the inventors in State enterprises recognition and a monetary bonus determined as a percentage of the savings realized by their invention. The State retained formal ownership and control over the dissemination of the invention. Alternatively, the State might issue patents vesting inventors with ownership and fundamental control, thereby entitling them to receive whatever royalties might be negotiated. Inventions which concerned national security or “affected the welfare of the great majority of the people” would automatically fall under the first category.

The legislation also empowered the Central Bureau of Technological Management of the Finance and Economic Committee and the General Administration of Commerce to set terms of protection for patents and certificates of invention for periods of three to fifteen years, and to establish the rates at which holders of certificates were to be rewarded. Further control was exercised through provisions of the regulations that required the working of patents within two years and forbade transfer of patent rights without the Central Bureau’s permission.

Trademarks were to be protected under the 1950 Procedures for Dealing with Trademarks Registered at the Trademark Office of the Former Guomintang Government and the Provisional Trademark Registration. The system al-

lowed trademarks used under the Guomintang to be re-registered. The measure, intended as an appeal to the remaining industrialists, allowed them to seek at least nominal protection for their marks. Few did, and as the economy moved toward socialism the need diminished.<sup>63</sup> Copyright law was severely diminished under the new Communist rules. Building on an intellectual heritage that emphasized the external origins of knowledge and the educational importance of wide dissemination, the Party instituted a system where writers and poets were directly employed by the State. Remuneration was based upon their salary and a small payment based on the number of copies printed at the state-run printing press. Since private presses no longer existed, royalties likewise became an antiquated notion. While the writers nominally had the right to prevent unauthorized alteration of their work, ownership and the right to dissemination rested with their employer, the State.<sup>64</sup>

As the transition to a socialist economy accelerated, IP laws were amended to reduce their stated concern with property rights and their reliance on material incentives. On November 3, 1963, the State Council supplanted the Provisional Regulations on the Protection of Invention and Patent rights with two sets of permanent regulations – the Regulations to Encourage Inventions and the Regulations to Encourage Improvements in Technology.

The new regulations struck patent protection from the law, and specified that new inventions and improvements in technology were to be the exclusive property of the state. Even the awarding of the ‘invention certificates’ was discontinued. Consistent with the notion that “in giving awards, politics should be in command, extensive ideological work carried out, and the principle of combining honorary awards with materials awards maintained”, the material awards provided for by the new regulations called for far lower payments than the precious schedules.<sup>65</sup> The new recognition was to be complemented by a set of honorary awards, ranging from certificates and banners to applications of one’s name to the invention and free trips to worker’s resorts.<sup>66</sup>

The chaos of the Cultural Revolution shifted the focus from observance to law to adherence to political dogma. Regulations and rights were largely ignored in the maelstrom which followed; formal authority was delegated to an uncertain and constantly changing milieu of revolutionary committees and local leaders. During the period from 1966 to 1976, intellectuals were the victims of a series of political campaigns. In the early 1960s, a campaign was waged against those in the party who allegedly sought to protect capitalist legal rights, including copyright.<sup>67</sup> Beginning in 1973, the Gang of Four, with Mao Zedong’s support, asserted that intellectuals were not proletarians and that protection of their work would constitute a protection of “bourgeois” rights. Intense conflict between radicals and

intellectuals continued and did not end until the death of Mao and the arrest of the Gang of Four in August 1976.

#### E. Conclusions

The lack of a clear economic rationale for the protection of intellectual property and the continuous emphasis on the State power to control ideas resulted in a system where intellectual property was inadequately protected. Where Western powers sought to establish legal protections, at times quite literally at gunpoint, the result was an adequate system of positive law which was not enforced. In terms of legal development, the system thus created continued to ensure the subjugation of ideas and commerce to State interests, and lacked the infrastructure necessary to create a true system of enabling rules.

### III. INTELLECTUAL PROPERTY LAW IN THE ERA OF REFORM

#### A. Creating an IPR Regime

At the National Science Conference in 1978, Deng Xiaoping announced the rehabilitation of the intellectuals as part of a sweeping change in the Chinese political landscape. Intellectuals were recast as part of the proletariat, and property was no longer classified as a “bourgeois right.”<sup>68</sup> In December 1978, the State Council re-issued the 1963 Patent regulations, which reinstated monetary and honorific awards for inventors.<sup>69</sup> Drafting of trademark, patent and copyright laws was soon under way.

The passage of a revised Patent Law<sup>70</sup> in 1984 was heralded in the Chinese press as “signaling the dawn of a new era in Chinese economic and legal development.”<sup>71</sup> The new legislation clearly established the validity of the inventor’s economic rights, but again placed them subordinate to the interests of the State. The Patent Law moved away from invention patents in favor of “utility” patents, under which the grantee received protection for a 5 year term, or monetary rewards and no rights. Article 29 allowed foreigners who had filed patent applications abroad a 12 month priority period in which to seek protection in China, but made no such concession to Chinese nationals. Article 14 of the law vested the State Council and provincial governments with the authority to compel state entities to license patents they held, subject only to the requirement that such a step be taken “in accordance with the state plan” and that a fee (determined by the state) be paid. Articles 51 and 52 provided that patents held by foreigners or Sino-foreign joint ventures were also subject to compulsory licensing if the patentee failed within a three-year period to make the patented good, utilize the patented process, or license another person to do so. The Patent Law also did not

offer protection for pharmaceutical products and chemical processes, a shortcoming which would cause considerable conflict with the U.S.

Article 1 of the Trademark Law, passed in 1982, offered protection for trademarks based on their role in “fostering development of socialist market economy.” Article 6 emphasized the role of the Trademark Law in maintaining quality of goods offered in the marketplace, and its importance in preventing consumer deception. Typical of Chinese legislation, the Trademark Law enumerated a fairly comprehensive list of rights, but failed to articulate how these rights were to be enforced. The State Administration of Industry and Commerce (SAIC) was empowered under Article 31 to cancel trademarks, impose fines, and refer violators of the law for more serious punishment, but it did not specify the procedures by which this was to be accomplished, or the standards which should be used.

Copyright was first addressed in General Principles of Civil Law, passed in 1986. Article 94 provided the following vague recognition of copyright:

Citizens and legal persons, shall enjoy rights of authorship (copyright) and shall be entitled to sign their names as authors, issue and publish their works and obtain remuneration in accordance with the law.

At the time, no statutory guidance determining an author’s remuneration existed.

A more complete Copyright Law was passed on September 7, 1990. The law reserved the exercise of copyright rights to the author’s work unit, rather than to the author themselves.<sup>72</sup> Broad fair use provisions allowed state organs the right to make use of materials free of charge in the “execution of official duties,” while acting with restraint sufficient to avoid prejudicing, “without reason,” the rights of owners.<sup>73</sup> “Works prohibited by law to be published and disseminated” were not entitled to copyright protection, and Article 4 further enjoined rights holders from “violat[ing] the Constitution and the law, or infring[ing] upon the public interest” while exercising their copyrights. The State Administration of Press & Publications was placed in charge of administering the copyright system, again with very little explicit statutory direction.

The final phase of the initial legislation was the passage of the Computer Software Regulations<sup>74</sup> in October of 1991. The regulations did not cover programs embedded in silicon chips, and also contained broad “fair use” provisions. Article 31 specifies that similarities between newly developed and preciously existing software will “not constitute infringement of... copyright... if the similarity is necessary for the execution of national policies, laws, regulations and rules... or for the implementation of national technical standards.” Article 31 does not further define these terms, nor does it require compensation for affected soft-

ware developers. Further, software developed by state enterprises within China that is of “great significance to national interests and public interests” shall potentially be subject to government expropriation.<sup>75</sup> Finally, all software published prior to the issuance of the regulations on June 4, 1991 is effectively presumed to have been in the public domain.

## B. IP Protection and U.S. Trade Policy

During the 1980s and 1990s, the shift from manufacturing to intellectual-property based industries in the United States accelerated rapidly; between 1977 and 1996, copyright industries grew at 4.6 percent annually, nearly three times the national average.<sup>76</sup>

This development became imperiled, however, by the electronic medium copyrighted products utilize. The most valuable intellectual property (“IP”) assets – software, music, and movies – have become increasingly easy to illegally duplicate, due to the proliferation of low-cost replication technology.<sup>77</sup>

The United States developed domestic legislation to limit the market access of countries who (by U.S. standards) offer inadequate levels of IP protection. Under Section 301 of the Trade Act of 1974 (Section 301),<sup>78</sup> the United States Trade Representative (USTR) may take action against nations based on “an act, policy or practice” which “denies benefits to the United States under any trade agreement” or simply “restricts United States commerce.”<sup>79</sup> The USTR may designate a nation as a “priority foreign country”, when the perceived violations are particularly egregious, or place the country on the “priority watch list” or the lesser “watch list”, which advise the targeted nation of the USTR findings and require continued monitoring.<sup>80</sup> After a further affirmative determination of infringing trade practices, the USTR may impose countervailing duties, enter into binding agreements, or suspend or withdraw trade benefits to that country.<sup>81</sup>

In order to protect “an increasingly important component of national wealth”<sup>82</sup> and alleviate the economic distortion piracy creates in the world marketplace, the U.S. has also sought to link intellectual property protections with international trade regimes. The United States successfully campaigned for the adoption of the 1994 Agreement on Trade-Related Aspects of Intellectual Property Rights (“TRIPS”)<sup>83</sup> as part of the Uruguay Round revisions to the General Agreement on Tariffs and Trade (“GATT”). TRIPS incorporates previous multilateral intellectual property accords, notably the Berne Convention for the Protection of Literary and Artistic Works<sup>84</sup> (“Berne Convention”) and the Universal Copyright Convention<sup>85</sup> (“UCC”), and expands the scope of protection afforded to intellectual property under the auspices of the World Trade Organization. Al-

though TRIPS is not self-executing (each nation must “determine the appropriate method” of implementation),<sup>86</sup> it will eventually apply to all members of the WTO.

## C. Sino-American Negotiation of IP Protections, 1989-1992

The importance that Washington attached to IP protection was apparent from the outset of renewed economic relations with China. In July 1979, the PRC agreed as part of the Agreement on Trade Relations to offer IP protection for American goods, again on a reciprocal basis.<sup>87</sup> American dissatisfaction with the 1982 Trademark Law and the 1984 Patent Law, and frustration over delays in the passage of a copyright law, led the USTR to consider imposing trade sanctions following the passage of the 1988 U.S. Omnibus Trade Act (Trade Act) with its Section 301 provisions.<sup>88</sup> In May 1989, the U.S. and China concluded a Memorandum of Understanding (MOU) under which the U.S. agreed to delay imposing sanctions so the Chinese could have more time to comply with the provisions of the Trade Act. In 1991, then-USTR Carla Hills identified China as a “Priority Foreign Country,” and examined the imposition of sanctions for China’s failure to protect copyrights and offer patent protection for American pharmaceuticals and other chemicals. American losses to Chinese patent infringement and industrial piracy in the late 1980s and early 1990s was estimated to be approximately US \$400 million.<sup>89</sup> Intensive negotiations resulted in the signing of a second MOU in January 1992, just before U.S. trade sanctions were to go into effect.

The 1992 MOU focused on technical legal improvements to the Chinese IP regime, and the commitments therein were undertaken with great rapidity. China’s required accessions to the Berne Convention and the Geneva Phonograms Convention were accomplished in October 1992 and April 1993 respectively. Also in October 1992, China acceded to the Universal Copyright Convention, an action not required under the 1992 MOU. The NPC also issued regulations in September 1992 designed to implement the conventions and the terms of the MOU. The 1990 Copyright Law was amended, and the computer software was recognized under Chinese law as a literary work under the Berne Convention.<sup>90</sup> Consistent with Articles 1 and 2 of the MOU, China amended its 1984 patent law to extend protection for chemical and pharmaceutical products<sup>91</sup>, and presented instruments of accession to the Patent Cooperation Treaty on September 13, 1993. Consistent with the requirements of Article 4 of the MOU, the Anti-Unfair Competition Law, adopted on September 2, 1993, specified eleven types of actionable unfair competition, including infringement of trade secrets belonging to another party.<sup>92</sup>

By 1993, however, the piracy problem had worsened. While significant legal reform had taken place, enforce-

ment measures remained inadequate. From July 1993 through February 1995, a series of 21 intensive negotiations took place. Following a October 1993 visit to Beijing where then-Deputy United States Trade Representative Charlene Barchefsky characterized Chinese enforcement efforts as “essentially absent,”<sup>93</sup> USTR Mickey Kantor placed China on the 301 Priority Watch List. In its March, 1994 National Trade Estimate Report, the Office of the USTR found piracy in China to be rampant, particularly in the areas of audio-visual materials, publishing, and computer software.<sup>94</sup> The decision of whether to include China as a Priority Foreign Country was postponed sixty days; following the postponement, the USTR found that the Chinese government remained unwilling to take action against major IPR pirates, and on June 30, 1994 designated China a Priority Foreign Country.<sup>95</sup> Following a six-month investigation, the USTR proposed US\$1.08 billion in sanctions, mostly directed at goods originating from Guangdong Province.<sup>96</sup> Beijing retaliated with similar sanctions, but, as in 1991-92, the parties were able to reach a last-minute agreement, the 1995 Memorandum of Understanding.

#### IV. ADMINISTRATIVE ENFORCEMENT OF IP RIGHTS: THE 1995 MOU

The 1995 MOU committed the Chinese to substantial IPR enforcement measures, most of them focused on improved administrative protection of IP rights. The attached “Action Plan,” designed by the State Council Working Conference on Intellectual Property Rights (“IPR Working Conference”), proposed major changes in how IP rights were protected.

First, the IPR Working Conference became a national-level coordinating body for the various administrative agencies charged with IP protection. The self-ascribed purpose of the IPR Working Conference was to “coordinate and organize enforcement activities among provinces”<sup>97</sup> and to “achieve uniform and effective protection and enforcement of intellectual property rights[.]”<sup>98</sup> 22 Intellectual Property Working Conferences were to be created in the provinces and directly administered municipalities, to “organize and instruct the relevant authorities within regions and departments to investigate and substantially reduce infringement of intellectual property rights.”<sup>99</sup> Personnel of the National Copyright Administration (NCA), the State Administration for Industry and Commerce (SAIC), the China Patent Office (CPO), and the Ministry of Public Security (PSB) were directed to coordinate their activities under the regional IPR Working Conference. Significantly, the burden of enforcement was placed on local government; the People’s Governments at each level were called upon to furnish the “necessary guarantees” in terms of personnel, facilities, and operating budgets.<sup>100</sup>

Second, the powers of the administrative enforcement agencies were clarified and, in some cases, greatly expanded. Each enforcement agency was explicitly authorized in cases where “there is reason to believe” that infringement had taken place, to enter and search the premises, review the businesses’ books and records, and seal suspected goods and the implements used to make them.<sup>101</sup> When infringement was found, the enforcement task force had the authority to impose fines, order an end to the production, and seize infringing goods and the materials used in manufacture.<sup>102</sup> Suspected infringers could also be turned over to the People’s Procurate for criminal proceedings. These actions could be taken *ex officio*, on their own initiative, or on receipt of a right holder’s petition. In areas where the problem was “especially serious”, an ad hoc enforcement group was to be set up to take sustained action.<sup>103</sup> A fourth agency was added to the anti-piracy collage: the Chinese Customs service was revamped with American technical support, and granted the power to inspect and detain all infringing goods passing through China’s borders. Rights holders could apply to the Customs service if they suspected infringement, but the service was also expected to take action *ex officio*.<sup>104</sup> “Severe administrative penalties”, both financial and administrative, were to be imposed against infringers.<sup>105</sup> Finally, guidelines for patent, trademark, and copyright protection were to be published by the responsible agencies, and agencies were required to respond in writing to rightholder petitions within specific time frames.

Third, the 1995 MOU called for increased scrutiny of optical media production. Beginning March 1, 1995, all manufacturers were required to print a Source Identification Code, or SID, on all CDs and CD-ROMs produced. Further, every CD factory was to undergo re-registration, and those involved in pirate activity would be “subject to administrative and/or judicial penalties, commensurate with the level of infringement.”<sup>106</sup> The inspection and re-registration process was to be completed by July 1, 1995.<sup>107</sup>

Fourth, a system of intensive training and propaganda was to be established, in order to educate not only industry, but average citizens and government officials as well. Intellectual Property laws were to be incorporated into the State’s “knowledge-of-law” awareness program, “with the aim of providing training on intellectual property rights for over 50 percent of officials at or above the county and departmental ranks in all departments within one to two years.”<sup>108</sup> Additionally, 80 percent of persons in charge of research institutes, large and medium-sized enterprises, and educational institutes were to undergo IP training.<sup>109</sup> IP educational programs were launched at Beijing University, among others, and publicity campaigns were designed to spread information about IP laws and the importance of respecting them.

Finally, IP violations were to be included in the “Strike Hard Against Crime” campaign, a period of heightened criminal enforcement activity. For these periodic campaigns, additional manpower was allocated from the PSB and the People’s Procurate to punish infringers. Punishments and fines were increased for the duration of the campaign, and the State press featured articles about leading trials. In the 1995 MOU, the special enforcement period was to begin March 1, a week after the 1995 agreement was signed, and continue for six months. The campaign was to focus on key geographical regions<sup>110</sup> and specific sectors, such as audio-visual products, computer software, sound recordings, trademarks, patents, and unfair competition.<sup>111</sup> Where infringing activity in a particular region was not significantly reduced by August 31, the term of the special enforcement would be extended beyond the six-month period.<sup>112</sup>

### 1. Enforcement of the 1995 MOU

Under the 1995 MOU, the Chinese made a considerable commitment to reduce IP piracy. However, despite official claims that “China has . . . strictly fulfilled its obligations under [the MOU],”<sup>113</sup> enforcement remained lax, and piracy continued to grow dramatically. Under the 1995 MOU, the Chinese were obliged to close seven infringing plants and investigate and close all other pirate CD plants within three months. By November 1995, however, the USTR found that “[t]o our great dismay, China has instead re-registered . . . all but one of the CD factories.”<sup>114</sup> Production of pirated CDs continued to increase; by February of 1996, most analysts estimated the number of pirate plants at twenty-nine or more.<sup>115</sup> Moreover, production in many CD plants had shifted from music CDs to the higher value-added CD-ROMs, and exports of both CDs and CD-ROMs had not demonstrably declined. Finally, many of the administrative measures either belatedly implemented or entirely ignored. The commitment to require SID codes, for example, was not instituted until January 1996,<sup>116</sup> and even then, the State Press and Publication Administration’s order was only sporadically implemented.

Appearing before the Senate Subcommittee on East Asian and Pacific Affairs, then-Deputy USTR Charlene Barshefsky stated that although piracy at the retail level had been addressed, the Chinese had done little to attack the continued production and export of pirated goods.<sup>117</sup> The U.S. was particularly incensed that 29 known pirate CD factories remained in operation. China was warned that its implementation of the 1995 MOU would lead to another round of sanctions, greater than those previously considered.

China vociferously claimed compliance with the 1995 MOU – Lee Sands, the Assistant USTR for China and Ja-

pan, returned from an information-gathering trip to Beijing with literally scores of official Chinese documents<sup>118</sup> – but the U.S. demanded hard evidence of IP crackdowns.

China once again pledged to crack down on pirate production, this time providing a self-imposed June 1, 1996 deadline.<sup>119</sup> On March 13, China announced it had shut down three pirate factories, and another three were shut down on April 21.<sup>120</sup>

The U.S., however, was not satisfied with these measures; on April 30, 1996, the USTR named China a Priority Foreign Country under Section 301. On May 15, Acting USTR Barshefsky released a list containing US \$3 billion worth of Chinese goods which would be sanctioned if China did not take steps to improve implementation of the 1995 agreement.<sup>121</sup> Chinese officials threatened retaliatory sanctions on a similar scale.<sup>122</sup> As before, the U.S. and China reached a last-minute deal in June 1996 (the “1996 Agreement”).

The Chinese government agreed to more thoroughly implement four key provisions of the 1995 MOU: (1) closure of 15 infringing CD factories; (2) reinstatement of the Special Enforcement Period; (3) strengthened border enforcement, and (4) increased market access.<sup>123</sup> The Chinese government closed the Guangdong factories by revoking their business licenses, seizing materials and machinery used to produce bootleg goods, and prosecuting the persons responsible.<sup>124</sup> Additionally, the Chinese government announced a moratorium on construction of new CD plants, and banned the importation of any new CD presses.<sup>125</sup> Responsibility for enforcement was shifted to the Ministry of Public Security, which added thousands of enforcement officials to the IP enforcement effort.<sup>126</sup> Customs also stepped up enforcement efforts, seizing 20,000 pirated CDs and VCDs at Beijing Airport, and 16,000 CDs at the Hong Kong border.<sup>127</sup> The Chinese government also pledged to procure only legitimate software for use in government and research facilities. Finally, market access was again addressed; quotas on the import of foreign films were to be dropped, and China agreed to allow U.S. companies to co-produce movies, plays, and dramas for domestic audiences.

### 2. The 1995 MOU: Five Years Later

The 1999 “Report on Intellectual Property” recently released by the Chinese State Intellectual Property Office (SIPO) claims that in the five years since the 1995 MOU, some 72,000 suspects have been detained by the MPS and more than 79 plants producing optical-media products have been closed.<sup>128</sup> The National Administration of Press and Publications (NAPP) states that in last 5 years, 6,546 pirate “dealers” have been subjected to jail terms and 12, 179 copyright violators have been fined.<sup>129</sup> The USTR, citing China’s success in reducing export of pirated CDs, has

moved China from the Priority Foreign Country list to the less onerous Watch List.<sup>130</sup>

Detailed examination of the situation reveals that progress has in fact been much more limited. While trade sanctions were successful in promoting legislative revision at the national level, they were unsuccessful in promoting development of the infrastructure necessary to make those changes viable in the long term.

### 1. Export has shifted from optical media to counterfeit goods.

While the export of optical-media goods appears to have rapidly declined, the export of counterfeit goods poses a more serious problem. According to the 1998 Annual Report of the Recording Industry Association of America, active measures undertaken by mainland administrative agencies have led to a dramatic drop in the production and export of counterfeit CDs.<sup>131</sup> All 15 of the optical media facilities referenced in the 1996 Agreement have been shut down or converted to legitimate production, and the provisions for round-the-clock inspection appear to have been implemented. Indeed, many pirate operations have shifted production to Hong Kong and Macao, and the PRC is now a net importer of pirated optical media products.<sup>132</sup> Despite its own active efforts to crack down on piracy, Hong Kong was placed on the Priority Watch List by the USTR in May of 1998 because of a 3.5 percent growth in illegal production.<sup>133</sup> Commentators have suggested that the relative disparity of possible criminal sentences (Hong Kong law allows a maximum of 2 months imprisonment for counterfeiting, as opposed to the 7 years allowed under PRC law)<sup>134</sup> has played a role in this shift. Macao has also become an active supplier of pirated goods to other Pacific Rim nations.<sup>135</sup> These measures have had little effect on end-user piracy, however, as music, audio, and software CDs remain readily available in the mainland market.<sup>136</sup>

At least some export of high-value CD-ROMs appears to be continuing. John Chen, Chief Executive Officer of Sybase, Inc., a California-based maker of database systems, reported continuing problems with pirated software exported from the PRC. "They [the Chinese] not only copied our software, they were exporting it to Southeast Asia. You could see pirated copies in Singapore, Hong Kong and Malaysia."<sup>137</sup>

The mainland has become a major market to and exporter for manufacturers of counterfeit goods. One scholar working with the China Anti-Counterfeiting Coalition assessed the problem as "the most serious counterfeiting problem in the history of the world."<sup>138</sup> In May 2000, agents of Gillette and local officials seized 48,000 knockoff Parker pens, and some 4 million replacement "Gillette" razor blades. Much of the packaging had been rendered into Korean and Rus-

sian for export to those countries.<sup>139</sup> In a similar raid, Chinese officials seized more than 1 million fake Duracell batteries which had been loaded onto container ships bound for Spain and Malaysia.<sup>140</sup>

State-owned enterprises play a major role in the production and export of counterfeit goods. Japanese motorcycle manufacturer Yamaha invested some US \$93 million in three motorbike and engine manufacturing joint ventures in the early 1990s. The booming market for motorbikes has, however, not helped sales; within four months of launching a new model, says Masayuki Hosokawa, chief representative for the Beijing office, "copies of our machines came onto the market, and we lost money on the project." Hosokawa estimates that 88 local manufacturers, some state-owned, are copying Yamaha's popular 125cc scooter and selling it for some US \$1,450 versus the US \$2,300 the real ones fetch. Hosokawa also estimated that some 110,000 counterfeit Yamaha motorcycles were exported to the U.S., Europe, and South America in 1998.<sup>141</sup>

While sustained political action was able to reduce copyright infringement, the failure to the 1995 MOU to institutionalize legal reform within the Chinese system has simply shifted the problem to another sector, i.e. manufacturing and export of counterfeit goods.

### 2. Prevalence of local protectionism.

Standards and commitments articulated in Beijing have not been successfully implemented on the local level. Local protectionism is widespread, and poses the single most significant problem for those seeking enforcement of their rights. The trade in counterfeit goods has become "a vital portion of some local economies, providing employment of otherwise unemployable workers and generating significant revenue for the local economy."<sup>142</sup> In most jurisdictions, officials at the county and municipal level control appointments, dismissals, job transfers, salaries, housing, and other benefits for local enforcement agencies, public security officers, and judges. Higher level units of the enforcement agencies may control policies or reverse erroneous decisions of at the lower level, but are powerless to dismiss or sanction lower level officials for misconduct. Thus, faced with a choice between disobeying or ignoring a directive from a higher-level unit, and displeasing the local mayor who can terminate employment or arrange an undesirable job transfer, many local officials not surprisingly choose the former. When Kroll & Associates raided a factory producing fake Japanese motorcycles in Southern China, they had to bring in provincial-level authorities because the local police refused to cooperate.<sup>143</sup>

### 3. Lack of effective sanctions.

The Chinese press reported that some 400 individuals were convicted of copyright violations under the criminal law in 1996, and that another 300 were convicted in 1997 and 1998.<sup>144</sup> However, criminal convictions based solely on violation of intellectual property laws appear to be quite rare.<sup>145</sup>

Part of the problem is that cases are rarely transferred from administrative authorities to police and prosecutors for criminal prosecution. According to the 1997 SAIC Annual Report,<sup>146</sup> of the 15,321 trademark infringement and counterfeiting cases brought nationwide, only fifty-seven cases were transferred to judicial authorities for prosecution. In 1998, of the 14,736 trademark infringement and counterfeiting actions brought, only thirty-five cases were so transferred.<sup>147</sup> This low rate of transfer may result from an institutional cellularity which prevents effective cooperation between parallel enforcement authorities. It may also be a reluctance to part with the spoils of enforcement; under Chinese law, if a case is transferred from SAIC to the MPS, all seized goods, contraband, fees and fines payable are transferred as well.

Part of the problem is that new evidentiary and legal standards may be difficult to satisfy. New interpretations of Articles 214-217 of the Criminal Law issued by the Supreme People's Court on December 11, 1998 doubled the minimum threshold necessary for the imposition of criminal sanctions. The minimum threshold is now RMB 50,000 (US\$6,250) for individual violations and RMB 200,000 (US\$25,000) for institutional violations.<sup>148</sup> In addition, the courts have interpreted the RMB 50,000 threshold must be met by evidence of actual sales.<sup>149</sup> Thus, a warehouse filled with infringing goods would not allow imposition of criminal sanctions without evidence the merchandise was actually sold.

Fines are also too low to impose sufficient deterrent upon counterfeiters. The 15,321 cases brought by SAIC in 1997 resulted in total fines of RMB 86.34 million, or an average fine of US \$679 per case. Total compensation paid to trademark owners was RMB5.1 million, or an average of US \$40 per case.<sup>150</sup> In 1998, 14,216 actions resulted in total assessed fines of RMB85.5 million, or an average of US\$699 per case, and total compensation was RMB5 million or US\$ 41 per case. Part of the problem is that administrative enforcement agencies, because they rely in part upon fines for operating expenses, have a vested interest in seeing violations continue.<sup>151</sup> The incentive is to impose a relatively low fine that the counterfeiter can economically regard as a cost of doing business.

As with the imposition of criminal sentences, the problem is also one of evidentiary standards. Under Article 43 of the Trademark Law Implementing Rules,<sup>152</sup> for example, SAIC is directed to impose a maximum fine of up to fifty

percent of the illegal turnover or up to five times the profit obtained from the counterfeiting activity. SAIC also has authority to order the counterfeiter to pay compensation based on the infringer's profits or damages suffered by the trademark owner.<sup>153</sup> Because most counterfeiters do not keep detailed business records, it may be difficult for right holders to definitively demonstrate that the fine is inadequate.

#### 4. Corruption

Some local enforcement agencies ask for payment of "case fees," reimbursement of costs, and gifts such as mobile phones from rights holders before they will commence enforcement actions.<sup>154</sup> Case fees reportedly range from RMB 1,000 to RMB 5,000 (US \$120 - \$600), depending on the size of the case, but can be as high as RMB50,000 (US \$6000) for actions conducted by the MPS.<sup>155</sup> In one instance, a local MPS official asked a brand owner for a reward of RMB 50,000 per arrest per suspected counterfeiter.<sup>156</sup> Government agencies also routinely ask companies to reimburse the cost of lodging when required, the cost of hiring trucks to move confiscated goods, and the cost of storing the goods in a private warehouse.<sup>157</sup> According to one observer, "government officials at all levels regard power in their hands as a rare resource, and those who come to them with requests are 'clients' with whom they will strike various deals of 'power versus money.'" <sup>158</sup>

While the use of trade sanctions arguably may have accelerated development of IP legislation, it could not create the institutional infrastructure necessary for civil enforcement of the rights the new laws created. The demands of American negotiators placed tremendous pressure upon nascent Chinese legal institutions, and finding them unable to keep pace, discarded them for expeditious short-term administrative and criminal law remedies. The resulting reliance upon State ministries and police agencies to enforce what are in essence private, economic interests had a deleterious effect upon the rule of law within China as it strengthened the authoritarian hand of the Chinese state while acting as a barrier to further development of private, civil law remedies. The 1995 agreement *obligated* the PRC government to "consolidate [control over] all printing firms,"<sup>159</sup> to step up "state supervision and monitoring of the distribution of publications,"<sup>160</sup> to establish enforcement task forces authorized to "enter and search any premises" and "review books and records..." of private businesses.<sup>161</sup> The 1996 "Strike Hard At Crime" campaign, which included criminal enforcement of IP laws in accordance with U.S. demands, also led to thousands of arrests and 3,500 executions.<sup>162</sup> The measures have succeeded in slowing the growth of certain types of piracy, but unquestionably cast a

dark shadow over the development of law in China during a formative period.

## 5. Development of Civil Law Remedies

The existing IP regime, with its emphasis on administrative and criminal remedies, does not provide an effective remedy for rights holders in China. As the examples above illustrate, enforcement of IP rights is dependent upon the financial ability and political will of local and regional authorities to take action, and as such is vulnerable to corruption and arbitrary enforcement. While trade sanctions were able to achieve a reduction in the production and export of optical media goods, this short-term success was achieved only through the compelled initiative of the national government in Beijing and is not likely to be sustainable. In contrast, development of private civil remedies would take advantage of a decentralized structure driven by individual actors in the legal system.

Pursuant to the 1992 MOU, specialized intellectual property courts (“IPCs”) were set up in more than 20 provinces and municipalities, including Beijing, Shanghai, Guangzhou, Shenzhen, Fuzhou, Puijian, Haikou, Zhuhai and Shantou. Chinese courts of general jurisdiction have the power to issue orders for the preservation of evidence,<sup>163</sup> and award damages in a civil action, including reasonable costs of investigation and legal fees,<sup>164</sup> but the creation of specialized IP courts was intended to address concerns of foreign claimants by providing access to justices with specialized training and knowledge of foreign languages. From 1991 to 1995, the People’s Courts heard 15,543 IP cases, of which 3,080 concerned patents, 2,600 concerned copyright, 907 concerned trademark, and the remaining 8,956 concerned technology contract and other miscellaneous cases.<sup>165</sup> Further development of this system would not rely as greatly on government funding or policy priorities, and would provide more consistent and reliable protection for IP rights than dependence upon Chinese administrative agencies and bureaucrats.

The results of the 1995 MOU evidence the disparity between policy goals advanced in Beijing and the difficult conditions faced by local officials. A potential advantage to private enforcement remedies is that it reduces to a minimum the number of layers between policymakers and implementation;<sup>166</sup> the parties come before the court with a specific dispute which the court resolves by direct reference to the original text of the policy, i.e. law promulgated by the national legislature. To date, recourse to the courts has not been a tool widely employed by rights holders.<sup>167</sup> Administrative enforcement is faster, less expensive, and more reliable. Recent developments in IP legislation and judicial reform, however, indicate the existence of a continued emphasis on promoting development of a modern legal sys-

tem. Working with this consensus among reformers offers the best long-term hopes, for IP protection and ultimately for the rule of law.

### A. Continued Development of IP Legislation

The continued development of legislation governing intellectual property legislation and the judicial system point to the existence of an effective coalition in the national legislature supporting further development of the rule of law. While some of the impetus for reform undoubtedly stems from external considerations, most prominently China’s still-ongoing bid to join the WTO, it is also clear that Deng Xiaoping’s vision of a nation governed by law continues to resonate within the Chinese government.

A new Patent Law was enacted on August 25<sup>th</sup>, 2000 by the Standing Committee of the NPC and Jiang Zemin signed it into law immediately thereafter by Presidential Order No. 36.<sup>168</sup> The new law revised 36 of 69 articles to bring the law into conformity with WTO standards. The revised law imposes a legal duty of confidentiality upon patent agencies who prepare patents for clients,<sup>169</sup> and offers more protections for patent rights holders in the event of compulsory licensing.<sup>170</sup> The legislation also expressly grant the patent right holder the right to seek preliminary injunctive relief, provided certain conditions are met,<sup>171</sup> which is required by Article 50 of the WTO TRIPS standards. The law provides much-needed clarification of non-infringement situations, specifying criteria required for exhaustion of rights, prior-use rights and “innocent infringement” cases.

The new Patent Law also clarifies legislative authority by restating the State Council’s formal authority to implement rules for management of patent agencies, thus clarifying somewhat the existing murky legislative hierarchy. The law also confers additional explicit administrative powers upon SIPO to make public announcements of infringement, legally demand rectification and indemnification, confiscate illegally gains or fine the infringers up to RMB 50,000 where gains “cannot be proven.” Much of the law is a restatement or amplification of existing powers, but the formal delineation of SIPO authority and clarification of non-infringement use constitutes a credible improvement.

Improvements to the Trademark Law and the Copyright Law are also under way. On November 18, 1998 the State Council approved a new draft bill entitled Amendments to the Copyright Law and transmitted it to the NPC for further review and approval.<sup>172</sup> The NPC committees then began an extensive consultative process across the country; the draft apparently generated heated local debates and was returned for revision. A 1999 draft placed before the Standing Committee of the NPC by various ministries was rejected, and returned to the ministries for its failure to comply with TRIPS and equalize protection for foreigners and

Chinese nationals.<sup>173</sup>

## B. Development of the Judiciary

Part of the very weakness plaguing the Chinese judiciary stems from its rapid development; one survey indicates that the number of judicial personnel increased from 58,000 cadres in 1979 to 292,000 in 1995, of whom 156,000 were judges.<sup>174</sup> By 1997, there were 250,000 judges in the PRC.<sup>175</sup> Such expansive growth would strain any legal infrastructure, and is particularly problematic in a nation where fifty years of Marxist-Maoist ideology and the Cultural Revolution have effectively destroyed the legal profession. Partly because of this shortage, many retired officers of the People's Liberation Army (PLA) were appointed to the bench despite a lack of formal legal or academic training.

A draft revision of the Judges Law currently before the NPC attempts to address some of the problems plaguing the system. The law specifies that those individuals appointed as judges and prosecutors must be graduates of law schools who have been practicing law for at least 2 years, or postgraduates who have practiced for at least 1 year. Those who did not major in law must be "confirmed" as having the same level of legal knowledge, through education or examinations. The law also specifies that heads of courts, People's Procurates, and members of judicial supervision committees should be "selected from among those proven to be high-level legal professionals after passing relevant examinations." Courts and procurators are empowered under the revisions to revoke appointments of judges and prosecutors at the lower level institutions for not complying with procedures and requirements as provided for in the laws.<sup>176</sup>

The Supreme People's Court has also made public a five-year plan for reform. Xiao Yang, president of SPC, cautiously stressed that reform "will be conducted on a gradual basis", and that it "should not be rushed beyond the country's reality."<sup>177</sup> The stated goal of the reforms is to "establish a system where the judicial and supervisory authorities are able to exercise their rights in a just an independent way"<sup>178</sup>. As part of this process, courts in Beijing introduced an open trial system in December 1998. Except for cases closed by the operation of law, any citizen over the age of 18 can enter the court and listen to arguments presented there. The SPC has also begun to publish decisions of selected cases, together with commentary, on the court's web site.

A second systemic weakness which IP courts share with courts of general jurisdiction are the strict limitations which circumscribe the scope of judicial authority. The Chinese Constitution grants the Standing Committee of the National People's Congress sole authority to

interpret the Constitution and the statutes of the PRC.<sup>179</sup> Article 83 of the Organic Law of the People's Courts further emphasizes the proscription, stating that the Supreme People's Court power is limited to "... interpretation of any problems of the concrete *application* of laws or regulations in the course of litigation" [emphasis added].<sup>180</sup> The courts are also required to defer to administrative interpretations of law issued by ministries of the central government. These administrative agencies possess authority to issue regulations to implement specific legislation under grants of power by a legislative body, such as the NPC Standing Committee, but can also exercise inherent power which enables them to issue any rule necessary to carry out their functions. The court must even defer to an agency's interpretation of its own jurisdiction.<sup>181</sup> Given the generally poor quality of legislative draftsmanship and the relative inexperience of Chinese lawmakers with IP in particular, this interpretive straightjacket hinders the ability of the courts to refine and develop legislation. The Legislation Law, discussed *supra* at Part II, presents a mixed blessing for this problem. While the law clarifies the legal hierarchy amongst the Constitution, laws, various administrative orders, rules, and regulations at the national and local levels, and requires that legislation expressly identify its authority and be published, it denies the Supreme Court and the People's Courts at all levels the authority necessary to interpret competing regulations and their relative authority. Under the Legislation Law, a conflict between agencies or laws would presumably be referred to the legislature for correction, an inefficient and time-consuming resolution, at best.

Finally, while few commentators doubt a strong desire on the part of the Chinese leadership to foster a greater respect for and observance of law, the Communist Party's intention to maintain absolute control over the judiciary is equally clear. The same clause of the 1982 Constitution which requires all organizations to obey the law also expresses the absolute supremacy of CCP authority. As Stanley Lubman, a noted scholar of Chinese legal development, writes:

the conventional approach in Chinese doctrine today acknowledges CCP supremacy and treats legislation as an expression of CCP policies and as an instrument to implement those policies. Even after policies have been given legislative expression, they are frequently modified in practice by CCP directives, speeches by leaders, and newspaper editorials. Legislation, then, is at all times dependent on

and potentially secondary to CCP formulation of specific policies.<sup>182</sup>

Transmission and observance of Party directives within the judiciary is primarily assured through strict Party control over the appointment and removal of judges. Selection and retention of chief judges at each level in the hierarchy is decided by the People's Congress of the corresponding level. Appointment and removal of judges above the rank of assistant judge is made by the chief judge, and must be approved by the Standing Committee of the People's Congress legislative body at that level.<sup>183</sup> Despite the availability of graduates from reopened law schools, the practice of appointing former military officers as judges to the People's Courts has continued; as Lubman convincingly argues, the retention of PLA personnel probably stems from their perceived loyalty to the Communist Party as a "soldier of the state."<sup>184</sup>

### C. Cases of Note

Despite these admittedly considerable difficulties, recent cases demonstrate the increasingly competent and effective resolution of intellectual property claims in the Chinese courts. The cases also demonstrate the Court's growing familiarity with complex issues of intellectual property rights in the Internet age, and illustrate some of the technical shortcomings which must be overcome if the courts are to provide a truly effective deterrent.

On June 20 of this year, the Beijing Second Intermediate Court handed down judgement over the dispute name "ikea.com.cn". In *InterIKEAS Systems (China) Ltd. v. China International Network Corporation, Ltd. (CiNet)* (hereinafter referred to as IKEA or the IKEA case), the court ordered CiNet's registration of "ikea.com.cn" be terminated immediately because it violated plaintiff's "well-known mark". Plaintiff, the Dutch corporation InterIKEA Systems B.V. had opened home furnishing retail stores in Shanghai and Beijing, but had not previously registered the mark. In its decision, the Court referenced Article 5, Section 2 of the Anti-Unfair Competition Law, Article 6 of the Paris Convention, and a WIPO Final Report on Domain Name Processes in determining what constituted a "well-known mark", explicitly declining to defer to the findings of a SAIC report on the matter. The court's straightforward use of international materials, its willingness to disregard the findings of the SAIC, and the dissemination of its well-reasoned decision demonstrate a considerable degree of legal sophistication.

In *Wang Meng, et al v. Beijing Cenpok Intercom Technology Co., Ltd.* (the Beijing Online case), six renowned writers filed civil suit before Haidan District People's Court in Beijing, charging Beijing Online, one of the largest

Internet access and content providers in China, for unauthorized and illegal distribution of their works via the online service. The authors sought extensive damages, including compensation for economic loss and alleged mental suffering. On September 18, 2000 the district court ruled in favor of the plaintiffs, and awarded Y26,580 (US\$3200) in compensatory damages, but rejected any award for mental distress. The defendant appealed to Beijing First Intermediate People's Court, arguing first that the Copyright Law did not apply to works posted on the Internet. In finding that Internet publication was actionable under the Copyright Law, the court looked to the broad description of author's rights provided by Article 10 and the nonexclusive language of the definition of "exploitation" found in subsection 5 of that article, even if the Internet medium was not explicitly mentioned. The court also rejected arguments that the Internet "posting" should be treated as fair use or permissible statutory license because there was no profit-taking involved, holding that unauthorized reproduction and distribution of copyrighted works over the Internet is likely to cause more damage to the right holder's copyright given the broad scope of transmission possible. The court recognized that neither the facts of the case nor applicable law offered a clear guideline for calculation of damages, and held simply that the lower court's award of compensatory damages was "not unreasonable". While the case again demonstrates solid reasoning and deft statutory interpretation, it also underscores the need for legislative guidance in determining appropriate damages.

The *Microsoft Corporation (China), Ltd. v. Beijing Yadu Science and Technology Group* (the Microsoft case) marks the first time a major software manufacturer went directly after an end user for copyright infringement in China. On November 17, 1998 Microsoft agent China United Intellectual Property Investigation Center (CUIPIC) joined personnel of the SAIC Haidan District Bureau in a raid of the Yadu Building in Beijing, and discovered more than a dozen pirated titles of its software being used on Yadu Group computers. The official investigation report contained certified statements of two engineers of Yadu where they admitted that at least 50 computers in the complex had more than 10 different types of pirated Microsoft software installed. Microsoft sued for RMB 1.5 million in lost profit, investigation and evidence collection costs, litigation and attorney fees, and also asked the court for an injunction barring further use and a public apology as per Article 46 of the Copyright Law and Article 134 of the General Principles of the Civil Law. The defendant was able to dismiss the charges, however, by claiming that it was not the proper party in the lawsuit. The raid was conducted against another company by the same name (Beijing Yadu Science and Technology, Ltd.) which was alleged to be completely independent from Yadu Group, despite the fact that the com-

panies shared office space and retained the same individual as legal representative and Chairman of the Board. It was uncontested that the engineers who admitted to the existence of the pirated software were both employees of Yadu Group. While Microsoft plans to refile against Yadu Ltd., spokesmen expressed concerns that the assets of the subsidiary would disappear. The case demonstrates the necessity for more independent judicial development of case law; in this instance, determining whether to “pierce the corporate veil” decided Microsoft’s rights, and may have a similarly deleterious impact on the ability of Chinese citizens to recover against corporations.<sup>185</sup>

#### D. Conclusion: Development of the Chinese Courts

Clearly, the limited powers and institutional constraints placed upon the Chinese judiciary detrimentally affect its ability to fully protect the rights of claimants before it. It is equally clear that between the priorities of maintaining order and developing the rule of law, the former will have absolute precedence in the minds of the national leadership. Yet the foundation for the development of a system of enabling rules has been laid, and while political independence of the courts cannot be expected, a increasing degree of institutional competence can be expected. A functional approach geared towards improving transparency, consistency, predictability, and the adaptability of the courts is not invalidated by political control at the national level.

The prevalence of local protectionism remains the greatest impediment to the effective adjudication of matters brought before the court. Removing or diminishing the local’s governments direct control over court personnel and finances would reduce this problem, potentially quite significantly. It appears that local protectionism is much less of a problem at courts of the intermediate and higher (provincial) courts, where the corresponding level of government has a much more tenuous connection with local finances.<sup>186</sup>

Except for the new Patent Law, there is no explicit right to preliminary injunctive relief in intellectual property litigation. Article 97 of the Civil Procedure Law, which allows for enforcement prior to judgement provided certain conditions are met, might be interpreted to allow for such measures. More explicit statutory authority would improve the existing regime. Such a measure would offer the plaintiff in copyright and trademark infringement cases the ability to enjoin further violations pending a full hearing; delays in full litigation would benefit the rights holder, and not the infringer. Such a remedy is required under Article 44 of TRIPS.<sup>187</sup>

Finally, the formulation of an effective contempt power is necessary to back up the court’s commands. Article 313 of the 1997 Criminal Law provides that “Whoever refused

to carry out a decision or order made by a people’s court while he is able to carry it out is to be sentenced to not more than three years of fixed-term imprisonment, criminal detention, or be fined if the circumstances are severe.” Currently, orders freezing accounts and assets are flagrantly flouted. Replacing the cumbersome criminal measure with a civil contempt power, enforceable without the necessity of a full-blown criminal trial, would enable to courts to deal more effectively with those who ignore judicial commands. By pursuing targeted, incremental reforms in a less confrontational manner, IP rights holders working in tandem with American policy and reform coalitions in Beijing can bring life to the existing skeletal legal structure.

## VI. CONCLUSIONS

### A. China and the WTO

Since the conclusion of the 1995 MOU, the American political leadership has pursued IP negotiations and rule-of-law reform in the context of China’s bid to rejoin the WTO. A bilateral agreement on China’s accession was concluded on November 15, 1999, and passed through the U.S. Congress only after a heated legislative battle. As part of the agreement, China agreed to implement the TRIPS standards immediately upon accession<sup>188</sup> and to adhere to the transparency standards articulated in GATT Article X(1).<sup>189</sup>

Bilateral agreements were soon concluded between China and the European Union, and final negotiations are currently underway on the integration of the bilateral agreements into a single WTO accession agreement. However, what in the past has been largely a technical exercise has proven to be enormously difficult; in the rush to conclude bilateral agreements (and win domestic constituents) specific measures for the implementation of China’s commitments were glossed over, and disputes over these details have threatened to derail the entire process. Problem areas include licensing procedures, protection of standards and intellectual property, trademarks and copyright, trading rights for foreign companies and China’s state trading companies, and an overall concern about China’s lack of a free, fair and independent judicial system.<sup>190</sup> Beijing’s chief negotiator Long Yongtu argues that the Western nations are trying to renegotiate the bilateral commitments, seeking additional concessions regarding their implementation: “I don’t think WTO-Plus is fair to China. If we accept this, it would set a precedent for other developing counties.”<sup>191</sup>

Examination of China’s efforts to join the WTO and her adherence to previous international accords, however, cast substantial doubt upon whether the agreement will in fact be fully implemented. Indeed, both sides may have unjustified expectations about the impact WTO membership will have.

Zhu Rongji, the architect of China's recent economic reforms, was initially reluctant to seek WTO membership; certainly he seemed less interested than Jiang Zemin and Vice Premier Li Lanqing, apparently because of concerns regarding China's ability to implement free-market standards so rapidly. But as his plans to reform the SOE economy ground to a near-halt, Zhu came to see international influence as an external pressure useful to promoting reforms.<sup>192</sup> Faced with declining foreign investment for the first time in 15 years, China's leaders also hope that WTO admission would boost exports and shore up foreign investment.

Expectations in the West that WTO integration will promote rule-of-law development similarly exaggerate the institutional capacity of the WTO. The WTO dispute resolution procedures, while strengthened by the reforms of the Uruguay Round, still depend in large measure upon the willingness of its members to implement decisions; the ongoing conflict over European Union policies regarding imports of bananas from Latin America demonstrate the importance of voluntary adherence to standards to the success of the trade regime.

China's record of adherence to such international agreements, even outside the context of the IP agreements discussed above, is not positive. In the Market Access Agreement, concluded in 1992, China agreed to eliminate import-substitution policies. For some years, economic planners in China had utilized restrictions on import licenses to spur domestic manufacture of automobile components, pharmaceuticals, power-generating equipment, consumer electronics, and other items. As part of the agreement, China agreed to phase out import licenses and not raise new barriers. Shortly after abolishing import licenses, however, new import registration requirements were initiated for many of the products previously covered by licenses.<sup>193</sup>

China's adherence to the international Multi-Fiber Agreement (MFA) has also been problematic. Under the framework of the MFA, the U.S. and China negotiated a series of bilateral agreements which imposed a quota on textile imports. During the early 1990s, the USTR determined that China repeatedly violated the agreement by transshipment of goods via Hong Kong and Macao. The U.S. Customs estimates the value of the transshipped goods at US \$2 billion annually.<sup>194</sup> In 1997, China and the U.S. reached a four-year textile agreement that strengthened penalties and reduced quotas in 14 apparel and fabric categories where there had been repeated instance of transshipment. But less than one year later, in May 1998, the USTR and U.S. Customs brought an action against China under the agreement, imposing a penalty of US \$5 million for the continued transshipment of textile goods.<sup>195</sup>

Whether a lack of political will or weaknesses in institu-

tional capacities are to blame, the poor implementation of the 1992 Market Access Agreement and the Multi-Fiber Agreement suggest that China's achievement of WTO standards may be a long and circuitous path, largely dependent upon the outcome of internal political and economic dynamics.

## B. Trade Sanctions

The use of high-profile trade sanctions removes what should be technical and legal trade issues to the arena of political debate; as William Alford has observed, the resulting "secular morality plays" dangerously oversimplify the diversity of the actors and interests involved and the complexity of issues they confront.<sup>196</sup> Despite voluminous scholarship exploring the complexities of central-local government relationships in China, for example, American negotiators continued to insist that Beijing's ability to ensure local compliance was simply "a matter of political will." The very real difficulties facing the government in Beijing became lost in a rhetoric charged with righteousness and nationalism, and the appearance of rapid progress became more important than potential long-term effects.

The negotiation and implementation of the IP agreements in the 1990s also evidences the impact such strategies may have on domestic coalitions. Pressures introduced by foreign negotiators become part of the domestic policy environment in Beijing as different coalitions embrace or reject the implications of the sought-for reforms.

As one study notes, the "losers" in this ongoing bureaucratic process are unlikely to abide by policy position issued by the "winners," and will use the dislocations caused by the changes as ammunition against the "winning" coalition.<sup>197</sup> The demands of foreign negotiators, glaringly exposed in a public forum, can force a domestic coalition genuinely interested in reform to choose between the Scylla of foreign demands and a Charybdis of their concomitant domestic implications. The public disclosure of the concessions allegedly offered by Zhu Rongji during his April 1999 visit to the U.S. very nearly wrecked the negotiating process and almost cost Zhu his position; he was mercilessly abused in the state-run Chinese press, with some commentators even referring to the concessions as "Washington's New 21 Demands" in reference to Japan's infamous 1915 attempt to reduce China to colonial status.<sup>198</sup> Indeed, one of the arguments pressed upon the American Congress was that WTO admission would "help the reformers" within the Chinese leadership, conveniently forgetting the Clinton administration's disastrous record in "helping" reformers in Russia.

Finally, the use of high-pressure tactics discredit the message of respect for rights and the legal processes by which

they are protected. The exercise of raw economic power via trade sanctions resurrects the ghosts of imperialism, memories which are very much alive in present-day China. The imposition of additional administrative channels to protect intellectual property jars dissonantly with loudly articulated concerns with human rights and the rule of law, and undermines the legitimacy of legal institutions in the minds of many Chinese.

### C. American Policy and the Rule of Law

While the use of trade sanctions arguably promoted rapid development of positive rules protecting intellectual property, they could not and did not promote genuine rule of law reform. As the Nationalist period demonstrates, the existence of rules alone is meaningless without a system capable of realizing their effective implementation. Nesting a system of enabling rules within the domestic polity is a complex process necessarily unique to local conditions. “Political culture comprises enduring values and practices

central to a nation’s identity, which foreigners perforce should not too readily assume they have either the moral authority or capacity meaningfully to influence.”<sup>199</sup>

That is not to say, however, that there is no role for the U.S. government and Americans to play. The United States has a surfeit of legal experience and knowledge, knowledge which would be well-used to help develop the basic components of legal infrastructure in China. Clinical education programs, exchange programs, and the involvement of NGOs and private actors within the Chinese sphere can aid in the drafting, development, and further study of statutes, and enrich the experience of Chinese law students and lawyers. The involvement of corporations doing business within China can also be a positive element, helping to develop domestic constituencies and breathe life into the formal legal system. Finally, low-profile and targeted use of trading rights can help promote the development of a rule-based market economy. But all parties need to recognize the necessity of a long-term approach, and eschew the high-profile, contentious atmosphere of the secular morality play.

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