

**Marleigh Grayer Ryan College Student Writing Prizes Competition**  
Undergraduate Submission

INTELLECTUAL PROPERTY RIGHTS IN CHINA:  
CAPACITY AND INCENTIVE FOR PROPER ENFORCEMENT IN CHINA

Submitted by:

Kevin H. Keeper  
Saint Lawrence University

Mailing Address:  
4102 Garrison Street NW  
Washington DC, 20016  
Kevin.Keeper@gmail.com

Spring 2008

## Abstract

Effectively protecting intellectual property rights (IPR) is linked intricately to human health. Consider the recent epidemic involving the production of heparin, a common pharmaceutical drug used for blood thinning. The heparin which caused allergic reactions in the United States and Germany derived from Chinese manufacturers. The questions that arose regarded placement of blame and how to prevent future occurrences. China has met the criteria for joining the World Trade Organization which means that it met the criteria for intellectual property rights enforcement. Despite this presumed qualification, the intellectual property enforcement regime in China remains weak. This weakness is due to a number of factors including bureaucratic structures and poor incentives for implementation. China has national legislation and the complementary bureaus charged with the implementation of IPR, yet the problems of counterfeiting and general intellectual property violations persist. Why has China's legislation been poorly reflected in their enforcement regime and what can the global community do to contribute proactively to the improvement of this intellectual property enforcement regime? One answer is to address the enforcement capacity limitations and the incentive structures of IPR implementation rather than negotiate and debate legislation for China which has proved fruitless. The findings of this study offers insight not just for intellectual property enforcement, but to all other realms of international legislative implementation in China.

## 1. Introduction

Heparin is a common blood thinner used in surgery and other medical treatments. This drug is commonly derived from pigs. Although the heparin is derived from the intestines of pigs, oversulfated-chondroitin sulfate, found in pig cartilage, is chemically similar to heparin. In unregulated manufacturing practices it is not impossible nor is it unlikely that manufacturers may try to mix this placebo drug with heparin to increase yield. Oversulfated-chondroitin sulfate is cheaper and in greater abundance than is the active ingredient of heparin and its addition to heparin is undetectable unless the product is tested to separate these two chemicals specifically. It is unlikely to require this specific test without suspicion of this type of contamination. Using the placebo, one might observe, is an easy way to increase yields, save money, and improve profit margins. Markets are driven by supply and demand and when prices are such that incentive exists to capitalize on output, the sense of ethics sometimes trumps the desire to turn profit. This becomes a public concern when those prescribed heparin, in need of the medical treatment it provides, begin to have allergic reactions and, in the worst cases, are killed by the counterfeit

drug. This was the case in early 2008 and the international trade regimes involved are sorting out how to delineate blame and responsibility and how to ensure that like problems do not persist in international trade.

The heparin scare is not a unique or anomalous occurrence for Chinese manufacturing. In the last decade China has become entangled in a series of intellectual property violations. Other recent examples of international threats to human health originating in China include, but are not limited to cases involving pet food, human food, cough medicine and toothpaste. Last spring a pet food traced back to China was killing animals and the production was halted and foods recalled. Also last year it was found that shrimp from China was unsafe and potentially harmful for human consumption. Two years ago there were a series of alleged deaths in Panama caused by cough medicine from China. In El Salvador toothpaste from China was found to have toxic levels of diethylene glycol, a chemical used also for thickening antifreeze. The US Food and Drug Administration (FDA) issued warnings about Chinese toothpaste soon thereafter.

The first place one might look to investigate the source of these mishaps is the international legal agreements of trade between China and their respective trade partners. This yields a surprising result as, on the surface, it appears that China has strong laws and equally strong bureaucracies to carry out these laws.<sup>1</sup> The ineffectiveness of manufacturing regulation, then, is not due to a lack of international legislation. An enlightening example of this imbalance can be observed in the case of America's Mattel Inc. in the summer of 2007. The paint used for America's Mattel Inc. products made in China was found to contain toxic levels of lead. Using our prior investigative approach we might look at Chinese legislation which reflects the

---

<sup>1</sup> "Reading the *China Intellectual Property Yearbook*, one is immediately struck by what seems to be a vast coordinated administrative network to protect intellectual property in China. Standing alongside the State Intellectual Property Office (*Guojia zhishi chanquan ju*, or SIPO) and housed in the same building (the former China Patent Bureau) is the Patent Bureau within SIPO (*Guojia zhishi chanquan ju zhuanli ju*), which has more than a dozen functional departments. Together with the dazzling array of speeches, statistics, and reports on enforcement activity, this leads one to conclude that the IPR bureaucracy, including patent, copyright, and trademark management, is a well-oiled machine spearheaded by SIPO." Andrew C. Mertha, *The Politics of Piracy: Intellectual Property in Contemporary China*. New York: Cornell U.P., 2005, p. 108

concurring international legislation. This reveals an astonishing discovery as the Chinese paint standards require that consumer products contain no more than 90 parts of lead per million. To put this in perspective, the US allows up to 600 parts per million.<sup>2</sup> This illuminates the reality that Chinese legislation is not followed and henceforth efforts to improve legislation will unlikely have any effect on the improvements of IPR protection in China.

The burning question now is “what product will be recalled next?” This is a depressing question as it suggests surrender of the abilities of our international trade regimes to ensure safe and regulated manufacturing. Need one fear or question everything with the “Made in China” label? Worse yet, as in the case of heparin, some manufactures, such as Baxter International of Wisconsin who is responsible for the heparin distribution in the US, use raw materials from China without advertising the fact. How, then, does one know that a daily vitamin or a daily medication does not originate from manufacturers in China? Should this be a concern? The reality is that yes, one should be concerned about the origin of their medications. In the case of heparin, the concerns about safety have led to accusations that the United States Food and Drug Administration (FDA) is at fault for allowing such products to enter the American marketplace. Others point out that it should be the responsibility of the US distributors. Restricting the inflow of counterfeit goods, however, only indirectly disrupts the production of counterfeit goods. The source of the problem is the manufacturing and production sites. Therefore, Chinese enforcement regimes and capacities need revamping to ensure the safety of the international community of consumers.

## **2. China’s Capacity to Enforce Intellectual Property Legislation**

One of the major problems with implementing legislation in China originates with the delineation of responsibility within their administrative structure. This administrative structure is

---

<sup>2</sup> Barboza, David “Why Lead in Toy Paint? It’s Cheaper” [The New York Times](#) (Sep 11, 2007)

often referred to as a muddled matrix of bureaucracies and power relationships. This matrix of power relationships complicates the enforcement capabilities of the administration. The matrix of bureaucracies, referred to by multiple scholars as a “fragmented authoritarianism,”<sup>3</sup> is an imperfect system in which loopholes and poor enforcement persists.

It is naïve and inaccurate to assume that the Chinese Central government has the will or the capacity to enforce IP laws. For example, the Chinese copyright bureaucracy is too weak to protect the interests of China’s own copyright laws and regulations. This has poor implications for their capacity to secure the interests of foreign counterparts.<sup>4</sup> A fragmented authoritarianism in China burdened by “deep jurisdictional cleavages” among bureaucracies makes uniform implementation of any national policy difficult.<sup>5</sup> This is most problematic when trying to apply Western concepts to the Chinese administrative system. Such is the case for intellectual property.

The enforcement agency for IP in China, the State Intellectual Property Office (SIPO) is based on the organizational model of the U.S. Patent and Trademark Office.<sup>6</sup> What exists now in China is a “technically proficient but relatively weak bureaucratic agency” in charge of IP enforcement.<sup>7</sup> This is because SIPO in China is separated into three separate *xitong* (thematic bureaus of the informal administrative structure in China).<sup>8</sup> The workability of these three *xitong* is highly unlikely as “jurisdictional turf battles, power asymmetries, and competition over scarce resources” trump any incentives for harmonious implementation and procedural development.<sup>9</sup>

---

<sup>3</sup> Lieberthan, Kenneth (1995) Governing China: From Revolution Through Reform. New York: W.W. Norton & Company; Oksenberg, Michel (2001) “China’s Political System: Challenges of the Twenty-First Century” The China Journal No. 45 (Jan 2001) pp 21-35; Dimitrov, Martin (2008) “The Resilient Authoritarians” Current History (Jan 2008); Mertha, Andrew C. (2005) The Politics of Piracy: Intellectual Property in Contemporary China Cornell University Press: New York (Page 26)

<sup>4</sup> Mertha, The Politics of Piracy, p. 15

<sup>5</sup> Ibid. p. 27

<sup>6</sup> Ibid. p. 108

<sup>7</sup> Ibid. p. 117

<sup>8</sup> “patents fall under the science and technology *xitong*, copyright falls under the propaganda and culture *xitong*, while trademarks fall under the finance and economics *xitong*.” Ibid. p. 28

<sup>9</sup> Ibid. p. 29

This means that each respective *xitong* is at odds with the other two and in fighting for power and institutional longevity.

The aforementioned challenges are possible to overcome. The correct delineation of responsibility can supersede the problems identified above. The Chinese administrative structure can be an effective enforcement regime if the incentive structure for cooperation trumps the incentive to ignore or allow the violations to persist.<sup>10</sup> This conundrum is best explained by examining the case of trademark enforcement.

### **IPR Enforcement in China – Lessons from the Success of Trademark Protection**

In a particularly revealing case study conducted by Andrew Mertha, the reasons for why trademark law is implemented successfully in some parts of China is (1) the power-relations between the agencies involved (SAIC and the SQTSB) has been beneficially competitive; and (2) the exogenous pressure from foreign business has supplemented the lack of domestic incentives and pressures.<sup>11</sup> The following is a summary of Mertha's findings.

There are two agencies currently overlapping and competing for authority rights over trademark law. The State Administration for Industry and Commerce (SAIC or simply AIC when speaking of a regional branch) and the State Quality Technical Supervision Bureau (SQTSB or simply QTSB when speaking of a regional branch) are both technically responsible for trademark protection. Officially, the SAIC has the sole responsibility for trademark enforcement. The reality of the matter, however, is that the SQTSB has “carved out a substantial niche for itself with the ongoing crackdown against counterfeit products in China.”<sup>12</sup> Several of Mertha's

---

<sup>10</sup> For example, Mertha discusses the relationship between a state office with informal power and a provincial office with formal power in Sichuan. The Intellectual Property Rights Working Office lacks any formal power yet were successfully influential on the national level was because Duan Ruichun, the director of the IPRWO, was able to exert commanding influence over Song Jian, his Sichuan Science Technology Commission (SSTC) counterpart. It was in Duan's interest to gain the favor of the U.S. Congress and so he carried out this responsibility by responding to Song's reports of the IPR community personnel, removing personnel who were reported to violate the interests of the IPRWO and the U.S. Congress. Ibid. p. 102-107

<sup>11</sup> Ibid. p. 176

<sup>12</sup> Ibid. p. 184

interviewees explained that “the AIC investigates markets, while the QTSB investigates factories and warehouses.”<sup>13</sup> The QTSB found their way into this enforcement market to capitalize on the profits to be made from kickbacks and money to be collected from the foreign government payments.<sup>14</sup> Additionally, the QTSB, by combating trademark, secures “larger budgets, more staffing, power and prestige.”<sup>15</sup> Mertha has gone as far as to credit the incentives provided by foreign business as being a driving factor in the strengthening of the QTSB and the AIC.<sup>16</sup> The significant point to be made here is that the nature of the foreign pressure was “cooperative rather than confrontational.”<sup>17</sup>

The cooperative role of foreign business in trademark enforcement has been a critical component in the success of this trademark legislation implementation. Foreign business can provide incentive for enforcement that is lacking in the Chinese government structure. Many times those charged with implementing legislation are not to benefit from implementation and therefore lack incentive to do so. When local IP violators provide kick-backs and bribes to the local implementing firms it becomes more favorable for the implementation agencies to accept the bribes and neglect the national legislation. This conundrum was identified by foreign business working against trademark violations. The local AICs are charged with trademark protection while the SAIC retains the income generated from trademark registration.<sup>18</sup> As witnessed in the Wuhua district, the AIC can earn seventy times their annual budget by collecting bribes rather than enforcing IP law.<sup>19</sup> This lack of incentive for the local AIC to

---

<sup>13</sup> Ibid. p. 190

<sup>14</sup> One of the interviewees of Mertha’s accounts said “‘to be very clear, the competition [is] over money.’ Issuing fines, collecting fees, and obtaining side payments from trademark rightholding ‘clients’ provide these enforcement agencies with extrabudgetary revenue impossible to secure through normal budgetary allocation processes.” Ibid. p. 189

<sup>15</sup> Ibid. p. 190

<sup>16</sup> Ibid. p. 201

<sup>17</sup> Ibid. p. 209

<sup>18</sup> Ibid. p. 178

<sup>19</sup> “when asked why such a market openly selling illegal VCDs was allowed to function, one provincial official said that the unit charged with assisting the Wuhua district cultural market management office with enforcement was the same unit that collected the rents from the various retailers—the Wuhua district AIC...A conservative estimate would place the average monthly fee of each stall at three thousand yuan.

enforce national law requires some sort of balancing entity. This is where foreign entities play a significant role in reorienting the incentive structures to favor AIC enforcement. Rather than cope with the loss, foreign businesses can proactively reorient the incentive structure by providing just enough capital for local enforcement agencies to trump what income would otherwise be collected in bribes.

Mertha points out that although national policy is important, “Institutional structure and organization incentives are central to understanding compliance outcomes” and henceforth the crux of IP compliance issues.<sup>20</sup> Valuable insight regarding the prospect of enforcing national legislation in China is captured in literature about Intellectual Property Rights (IPR) enforcement in China. The lessons learned from analysis of this bureaucratic system can be applied to other bureaucracies. Furthermore, the strengthening of IPR enforcement will benefit and impact the interests of the other bureaucracies such as the SFDA, especially important in cases such as heparin. Heparin is also an example of an instance in which the IPR concern couples with the safety aspect, an SFDA concern. This paper, then, is interested in the evolution of IPR enforcement in China and what realistic potential there is for improved enforcement. To improve the enforcement capabilities of the administration, one must understand the undercurrents of Chinese ideologies, of which certain elements of Confucian constitute a pivotal part, and the role of intellectual property in China prior to trades with the West.

### **The Culture of Economic Prowess and Collective Property**

To understand how and why IPR violations occur in China, one must consider China’s manufacturing economy as an historical evolution. Firstly, China has achieved incredible growth

---

Multiplied by twelve months and two hundred stalls, the figure comes to about 7,200,000 yuan (about \$871,700), a substantial sum for a single market to pay out to an urban district government in the interior of China. To put this into perspective, this amount is more than *seventy times* the annual budget for the Provincial Press and Publications/Copyright Bureau investigation team. . . In this situation, one that is replicated throughout China, everybody is satisfied except the owners of the intellectual property being violated.” Ibid. p.186

<sup>20</sup> Ibid. p. 3

in the past few decades due to their economic reforms. Any effort to implement laws which threaten this growth will, understandably, be met with resistance. Secondly, the concept of intellectual property is not inherent in the Chinese political or social ideology.<sup>21</sup> When international legislation is forced upon a culture which has a different ideology to that which precedes the legislation, one can begin to understand why an incentive structure needs to be developed to mend this caustic divide between ideology and formal policy.

Considering the historical development of manufacturing growth in China, the sub-par production of heparin is not so unlike the unusable steel produced during Mao's Great Leap Forward. During that time localities were encouraged to focus their efforts on the output quantities of the production of steel and, consequently, the quality of the steel produced was sub standard and even unusable in most cases. The fever of output and development trumped any movement for standards or production regulations. Something similar is happening in China today. Let us consider the heparin example once more. Some of the suppliers for SPL were simply a few workers in the kitchen of a small home slaughtering pigs and gathering the necessary ingredients. These practices are like the "backyard steel" produced during Mao's time. Not only is this a questionably unsanitary practice, but it may also explain where the contaminants originated. Why are these producers incorporated in the manufacturing processes? It is simply a matter of the pride of fulfilling a national ambition of economic growth while, and many times innocently, sacrificing the expenses of quality and care.

The Chinese state is empowered because of their economic prowess. First and foremost in their political strategy is to further economic growth. China is largely credited as being the next superpower and, considering the recent historic trajectory of their Gross Domestic Product (GDP)

---

<sup>21</sup> "In contrast to the West, whereby it is generally accepted that at least some of the inventor's rights are inseparable from the invention itself, that his or her rights are 'embedded' within it, the socialist approach to intellectual property is based on the assumption that it is impossible to separate the inventor's activity from the society of which the inventor is a part." Ibid. p. 25

and their economic output, China is no doubt creditworthy. The strength of China lies in their economy and the government knows this. As long as economic growth allots prosperity and seemingly satisfactory wealth for its citizens it would be counterintuitive to threaten the stability of China's citizenship by enforcing foreign ideology or any legislation which would slow or limit the growth of China's economy. China has long put off liberalizing their political institutions or granting human rights because the growth of their economy continues to take precedent. Such limitations and delays in reform are reminiscent of their disincentives to regulate a flourishing manufacturing economy.

Despite this political resistance, however, China has adopted regulations on manufacturing which respect intellectual property legislation. These national laws, however, have yet to be implemented effectively. The national adherence to IPR is challenged by ideals of economic prowess. One example provided by Mertha is an interviewee who admits that many Chinese are more concerned with getting "the invention out into the open quickly" and to avoid delaying the benefits to the economy that would occur in the lead time toward securing a patent.<sup>22</sup> This economic fever also supersedes the incentive for local administrators to enforce IP laws.<sup>23</sup> When the administrators have to choose between growing their local economic industry or implementing adopted national legislation, they will understandably choose the former.<sup>24</sup>

Secondly, one must understand that IPR is a foreign concept for China and other socialist societies. Confucian ideology, for example, purports that innovation and ideas are a product of

---

<sup>22</sup> Ibid. p. 99

<sup>23</sup> "often the priorities of these front-line enforcement agencies (or their immediate superiors) will compete with, even run counter to, the imperatives of IPR protection." Ibid. p. 15

<sup>24</sup> In addition to the lack of incentives for enforcement of IP, the disincentives, in terms of the legal repercussions, are equally as weak. For example, the criminal punishment for counterfeiting is "imprisonment of not more than three years, and/or a fine." Hason, Averie K. and Jean E. Shimotake "Global Interdependence and International Commercial Law: Recent Developments in Patent rights for Pharmaceuticals in China and India" Pace International Law Review (Spring2006) Vol. 18, p. 313

an individual within a society and therefore the innovation belongs to the society as a whole.<sup>25</sup> During Mao's time, for example, when Marxist ideology was a strong base of political identity, intellectual property would have been seen as theft from the masses. Mertha explains that socialist societies see it as "impossible to separate the inventor's activity from the society of which the inventor is a part."<sup>26</sup> In addition to this ideological divide, historically, copying and has been encouraged in China. Artists and publishers, in fact, were expected to copy and reproduce in order to propagate and disseminate knowledge and technology. Imitating and copying was even seen as forms of flattery.<sup>27</sup> Where then, did this modern concept of intellectual property begin to take root in China?

The evolution of intellectual property began in the 1950s when the state saw a need to encourage innovation. The Provisional regulations of the Protection of Invention rights and Patent Rights of 1950 were meant to "provide patent protection and rewards to the inventors, but the ownership of the inventions remained with the State."<sup>28</sup> Although it was an adoption of modern IP, being that the invention is owned by the State, this concept was still incongruent with the Western concept of IPR. China's first comprehensive Western-style intellectual property law, the Patent Law of the People's Republic of China, was adopted in 1984 following negotiations with the United States.<sup>29</sup> Real enforcement of this law or any like-law, however, had not begun until 2001, when China was admitted to the World Trade Organization (WTO).<sup>30</sup> Clearly, then, the concept of IP was introduced relatively recently to Chinese society and henceforth problems with implementation should be expected. Because IP is not a "homegrown" concept, there must

---

<sup>25</sup> Johnson, Ryan P. (2006) "Steal this Note: Proactive Intellectual Property Protection in the People's Republic of China" Connecticut Law Review (Jul 2006) Vol. 38, p. 1009

<sup>26</sup> Mertha, Andrew *The Politics of Piracy*, p. 25

<sup>27</sup> Hason, Averie K. and Jean E. Shimotake (2006) "Global Interdependence and International Commercial Law: Recent Developments in Patent rights for Pharmaceuticals in China and India" Pace International Law Review (Spring2006) Vol. 18, p. 310

<sup>28</sup> Ibid. p. 305

<sup>29</sup> Ibid. p. 305)

<sup>30</sup> "Much of local patent work [early in SIPOs years] focused on propaganda to educate the general public about the new Patent Law and to persuade inventors to patent their inventions." Their role was simply to educate and lacked any real enforcement structure. Mertha, Andrew *The Politics of Piracy*, p. 91

be adequate incentive for enforcement to persist and only in the last few years have solutions and successful efforts been made by Western parties.

It becomes clear now why the counterfeiting of heparin occurred in China. With a nationalist drive towards economic output coupled with a lack of historic ideology similar to IP, it seems irrational to believe that Chinese legislation would even exist for the protection of this Western originated concept. The root of safe production of heparin and like products, however, relies upon sound legislation backed up with solid enforcement. The following section, then, explores the evolution of intellectual property law in China to understand better the first piece of the aforementioned formula for prevention of future contaminated consumer products.

### **3. The Evolution of Intellectual Property Law in China**

To assess accurately the prospect of Intellectual Property Rights (IPR) enforcement in China, one must review the process by which intellectual property (IP) became national law in China. One disincentive for enforcement is revealed quite quickly in this review as IP is a relatively new concept for Chinese society and henceforth enforcement has been met with resistance. As discussed earlier, the Chinese society, being socialist in nature, believes that innovation cannot be separated from the society in which the innovator is a part. IP legislation in China has evolved through a series of bilateral and multilateral negotiations in which their concession of adopting stricter IP legislation has been for the consequential benefits of continued and improved global trade. The adoption of IP is just that, an adoption of a foreign concept, and China did little more during these negotiations than “drag their feet” and seek to “move as little as possible from the status quo” as they sought to improve or maintain their economic standing in the global marketplace.<sup>31</sup>

---

<sup>31</sup> “At the end of the day, whether before or after China’s accession to the WTO, that which becomes policy to be implemented locally in China does not begin at the negotiating table. Rather, it is formed in the United States through the interaction of the relevant IPR associations,

The bilateral and multilateral negotiations have been spearheaded by the United States. The US has been pressuring China to adopt IP legislation so as to protect American innovators ideas abroad.<sup>32</sup> Negotiations have taken place with the United States Trade Representative (USTR) in the 1990s and the World Trade Organization (WTO) in the late 1990s until their admission in 2001. The US and many in the IPR community believe that by applying external pressure to Beijing in the way of threats or incentives, improvements in IPR enforcement will permeate through China's business sectors.<sup>33</sup> The following is a review of the evolution of the IP legislation in China to assess what impact the US and other entities are having on the prospect of effective IP enforcement.

### **Sino-American Negotiations**

China first began to develop Western-style intellectual property legislation following stipulations of a treaty with America signed in 1979.<sup>34</sup> In accordance with this treaty, China became a member of the World Intellectual Property Organization (WIPO), passed a trademark law in 1982, and a new patent law in 1984. Despite these hopeful signs of IPR development in China, it soon became clear that the legislation was nothing more than lip service. These original IP laws were largely ineffective and in the late 1980s, the US engaged China in a series of Special 301 reviews until finally labeling them as Priority Foreign Country, the highest offending status of the United States Trade Representative (USTR).

---

which, in turn, takes place under the institutional framework of a domestic U.S. law, specifically Special 301. The role that Beijing has taken on in this process has been to resist as many of these demands as possible. Those that Beijing ultimately accepts become national policy, which is then implemented throughout the country." Ibid. p. 67 & 76

<sup>32</sup> The US remains the strongest force of pressure for China's IPR legislative development. After 1996 China's IPR evolution, which had formerly been pressured by the US for reasons of bilateral trade, were now a product of China's interest in gaining admission to the WTO. Although on the surface it appears that they are now answering to the WTO, it was the US during the Uruguay round that played a crucial role in the development of the TRIPS Agreement. In 2001, China once again amended their IPR laws to qualify for admittance to the WTO based on stipulations for the TRIPS Agreement. Officially, China was accepted to the WTO on December 11, 2001. Johnson, Ryan P. *Steal this Note* p. 1005

<sup>33</sup> Mertha, Andrew *The Politics of Piracy*, p. 2

<sup>34</sup> Johnson, Ryan *Steal this Note* p. 1009

Special 301 was a result of the United States 1988 Congressional amendment to the Trade Act of 1974. The amendment was meant to give the USTR authority to identify and regulate trade relations with countries deemed unable or inefficient in protecting US intellectual property interests. Special 301 gives the USTR the power to instigate a six month intensive series of negotiations by assigning countries with labels according to their IP protection records.<sup>35</sup> The labels, in order of severity beginning with the least, were Watch Country, Priority Watch Country, and Priority Foreign Country.

In 1991, the USTR elevated China to Priority Foreign Country thereby initiating a wave of trade wars which precipitated the Memorandum of Understanding (MOU) between China and the United States in 1992. The MOU, an amendment of China's 1984 Patent Law, compelled China to revamp and improve their intellectual property laws.<sup>36</sup> This MOU also marks the first time that patent law was to include pharmaceutical products.<sup>37</sup> In 1993, soon after the excitement of reaching an agreement settled, the reality of futility shone through. A representative of the Business Software Alliance argued that despite the MOU, "the US software industry had 'direct losses of \$322 million in China...[and] ninety-four percent of all packaged software in use in China is estimated to be pirated.'"<sup>38</sup> The USTR once again elevated China to Priority Foreign Country in 1994.

Peter Yu has coined the Sino-America IP negotiations as a "cycle of futility" in which both countries find themselves in a stalemate where neither US nor Chinese interests are effectively advanced.<sup>39</sup> Yu explains that the cycle as follows:

---

<sup>35</sup> Office of the United States Trade Representative (USTR) "2007 Special 301 Report" (April 2007)

<sup>36</sup> The MOU called on China to "strengthen patent protection, accede to the Berne Convention on copyright, treat software as a literary work deserving of protection without registration, limit the classification of previously published materials as 'in the public domain,' promulgate trade secret protection, and develop trademark protection procedures." Johnson, Ryan *Steal this Note* p. 1010

<sup>37</sup> Hason and Shimotake *Global Interdependence and International Commercial Law* p. 306

<sup>38</sup> Mertha, Andrew *The Politics of Piracy* p. 46

<sup>39</sup> Yu, Peter K. (2005) "Still Dissatisfied After All These Years: Intellectual Property, Post-WTO China, and the Avoidable Cycle of Futility" *Georgia Journal of International and Comparative Law* Vol. 34

The United States began by threatening China with trade sanctions (oftentimes with an ancillary threat that it would not renew China's most-favored-nation status). China then responded by threatening the United States with retaliatory sanctions of a similar amount. After several months of negotiations, both countries would agree to an eleventh-hour compromise that usually led to a written document. While intellectual property protection improved during the first few months immediately after reaching the agreement, the piracy and counterfeiting problems revived once international attention was diverted. Within a short period of time, American businesses again complained to the US government, and the cycle repeated itself.<sup>40</sup>

This adequately summarizes the events because once again in 1996, the USTR elevated China to Priority Foreign Country. Yu warns that if certain proactive measures are not taken soon, we could find ourselves subject to this "cycle of futility" for years to come. Despite these warnings, in 2005 the USTR placed China on the Priority Watch List and has engaged Chinese officials in an analytical review of their enforcement capacities. Ironically, despite these seemingly sound agreements the lives of consumers, not just in the US, but any country with trading relations with China, are still under threat. In light of these past failures of the "top-down" approach to IP implementation in China, it has become necessary to investigate new means by which to improve IP protection.

### **Sino-US Trade Relations Today**

Although the USTR recognizes the efforts of Chinese officials working to protect intellectual property rights, they still consider China to be far off the mark of acceptability in regard to IP agreements. Some of the improvements recognized by the USTR include accession to the WIPO Internet Treaties and other computer software related protections. Also, as mentioned before, there has been a rise in the number of anti-piracy efforts, which included the increased number of patents and court cases. Despite these improvements, however, the US copyright industries has reported that China's piracy and counterfeiting levels remained high in 2006. They report that an "estimate that 85 percent to 93 percent of all copyrighted material sold in China were pirated,

---

<sup>40</sup> Ibid.

indicat[ing] little or no improvement over 2005.”<sup>41</sup> Additionally, in 2006, the number of IPR infringing products seized at the US border originating in China totaled 81 percent, up twelve percent from 2005.<sup>42</sup>

Most recently, as per the 2007 Special 301 Report, China is to remain on the Priority Watch List and continue to undergo monitoring.<sup>43</sup> The Special 301 report issued by USTR is an annual publication reporting the state of IPR protection and enforcement worldwide. What is significant in this report is that the USTR is recommending the US to engage actively the World Trade Organization Dispute Settlement Board (WTO DSB) in addressing the issue of IP violations in China. The US has sought to challenge China to improve their efforts in this regard by addressing three key issues: criminal prosecutions, rules for disposal of IPR infringing goods, and disallowing goods awaiting Chinese censorship approval from entering the market in the meantime.<sup>44</sup>

The USTR attributes China’s failures in IP to, among other causatives, “chronic underutilization of deterrent criminal remedies.”<sup>45</sup> This is partially caused by a perpetual underfunding of administrations. These enforcement entities, for example, have to consider counterfeit enforcement costs as operating costs and henceforth may opt not to become active enforcers when their budget is tight. There are a number of other barriers to IP protection identified which echo some of the aforementioned arguments in this paper including the strength of the legal system.<sup>46</sup> To gain better insight into the problems and scope of barriers facing IPR enforcement regimes, the USTR conducted a special provincial review (SPR) from April of 2006 to April of

---

<sup>41</sup> Office of the United States Trade Representative (USTR) “2007 Special 301 Report” (April 2007)

<sup>42</sup> Gonzalez, Gloria (2007) "Intellectual property theft is top risk for firms with operations in China; International pressure placed on China to effectively enforce laws" Business Insurance (Mar 26, 2007)

<sup>43</sup> USTR “2007 Special 301 Report”

<sup>44</sup> *Ibid.*

<sup>45</sup> *Ibid.*

<sup>46</sup> *Ibid.*

2007 which provides some insight as to why enforcement is lacking in specific localities.<sup>47</sup> These steps are an important move for the USTR as it suggests their recognition of the futility of national legislation adoption and an understanding of the importance to move beyond negotiations to begin implementation assistance.

Why have these negotiations been so futile? One of the most significant problems with these negotiations, and largely a reason for the lack of implementation, is that while the US wanted substantive results, China was satisfied with symbolic resolutions.<sup>48</sup> Some have argued that China has implemented IP laws with full awareness that such legislation would not reflect real enforcement as the state lacked capacity to implement the terms of the agreements.<sup>49</sup> The process was entirely lip service to satisfy American interests. One possible reason for this negligence is that the Sino-US negotiations were asymmetrical in which only China was required to implement the terms of the agreement while the US simply chose whether or not to defect from the agreement.<sup>50</sup> Those interested in pressuring China through negotiations will be wrought in frustration upon China's recent achievement. China has been granted a shield from US pressures by their accession to the World Trade Organization.

### **Accession to the World Trade Organization – What Does it Mean for IP Protection?**

There are contradicting opinions regarding the impact that China's accession to the WTO will have on intellectual property protection agencies and enforcement efforts in China. Some believe that it is a great step forward and that the TRIPS Agreement will pressure China to continually improve their legal system to comply with all of the expectations of the Agreement. Others point out that the expectations of the Agreement are too weak to have any real impact on

---

<sup>47</sup> Ibid.

<sup>48</sup> Mertha, Andrew, *The Politics of Piracy*, p. 14

<sup>49</sup> Mertha, Andrew and Robert Pahre (2005) "Patently Misleading: Partial Implementation and Bargaining Leverage in Sino-American Negotiations on Intellectual Property Rights" *International Organization* (Summer2005), Vol. 59, Issue 3, (Page 697)

<sup>50</sup> Ibid.

China's IP enforcement regimes. Others still suggest that China's accession to the WTO has actually weakened the US's ability to exert real influence on China because of the procedural requirements of the WTO Dispute Settlement Board (DSB).

Although China's bureaucracy is currently unable to enforce IP legislation, this does not mean that further codification of IP legislation is futile. The skeleton framework is being developed today and there is reason to believe that this entity will flesh out over time. Some authors criticize those who purport that China is unwilling to enforce IP or unable by pointing out that intellectual property in China is a relatively new concept and the resulting implementation will take time. Yu, for example, says quite simply that "China needs more time, and twenty-five years are just not enough."<sup>51</sup> The criticism and profession that Beijing is unable and unwilling to enforce IP are premature. Ryan Johnson points out that China's accession to the WTO "may already be stimulating positive changes, promoting economic reform and the concepts of legal transparency and national treatment for foreign businesses."<sup>52</sup> The maturation of China's IP bureaucracy is taking place today and even the past five years have seen tremendous results as mentioned earlier in terms of the number of court cases and active patents.

One of the resounding issues with China's accession to the TRIPS Agreement is that the stipulations of the Agreement are simply too weak to have any impact on China's enforcement regimes. The TRIPS Agreement requires that member states provide effective IP enforcement but inadequately defines what constitutes "effective" protection.<sup>53</sup> Article 41, paragraph 5 of the Agreement states that member countries are not required to "put in place a judicial system for the enforcement of intellectual property rights distinct from that for the enforcement of law in

---

<sup>51</sup> Yu, Peter, *Still Dissatisfied After All These Years*, p. 11

<sup>52</sup> Johnson, Ryan, *Steal this Note*, p. 1019

<sup>53</sup> Yu, Peter, *Still Dissatisfied After All These Years*, p. 2

general, nor does it affect the capacity of Members to enforce their law in general.”<sup>54</sup> John Hillary and Niccolo Pantucci of the Center for Strategic and International Studies of Washington D.C. lament that “TRIPS is maddeningly vague. The agreement demands good faith efforts at enforcement.”<sup>55</sup> Because China’s enforcement of IP is no worse than their efficacy in enforcing tax collection, they are not actually violating this stipulation. The US, then, has no adequate argument in this respect because China is actually honoring the Agreement. The US is unable to file a general complaint about China’s enforcement capacity as the structure of the WTO DSB does not support this unfocused complaint.<sup>56</sup>

Now that China is part of the WTO it has the ability to point to the TRIPS specifications for IP enforcement and claim that they comply with these requirements, thereby damaging the authority of the US in IP negotiations. Hence, the US can no longer engage China in bilateral negotiations on the grounds of IP violations as they have in the past. Instead, the US must pursue the procedures set forth in the TRIPS Agreement. Part Five of the TRIPS Agreement lays the foundation for procedures by which member nations can settle disagreements that might arise. These procedures are to be undertaken by the WTO Dispute Settlement Board (DSB) to reach a Dispute Settlement Understanding (DSU). The United States has utilized this procedure by initiating 19 of the 27 DSUs undertaken.<sup>57</sup> The US, however, has not engaged China in a DSU, although the USTR has recommended it in recent years. The prospect for engagement is becoming more of a reality in recent years as US Trade Representative Susan C. Schwab was

---

<sup>54</sup> World Trade Organization (WTO) “Marrakesh Agreement Establishing the World Trade Organization Annex 1C, Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994

<sup>55</sup> Hillary, John and Niccolo Pantucci (2007) “The U.S. Escalates its WTO Complaint against China” Commentary publication from Center for Strategic and International Studies Washington D.C. (Aug. 31, 2007)

<sup>56</sup> Yu, Peter, *Still Dissatisfied After All These Years*, p. 2

<sup>57</sup> Johnson, Ryan, *Steal this Note*, p. 1018

quoted in 2007 suggesting that the WTO engage China in dispute resolution regarding China's persistent violations of intellectual property rights.<sup>58</sup>

Peter Yu strongly opposes the US pursuing this course of action with China for a number of reasons, most notably the prospect that the US will probably lose the case, or rather as the DSU is conducted, walk away with only a partial win.<sup>59</sup> Yu's final reservation about the US using the DSB to address China's failed IP enforcement regime is the ramifications such actions might have for future trade relations between the US and China.<sup>60</sup> Consider the fact that China is a recently admitted member undergoing long-term reforms to comply with the multilateral agreements. Any attacks on this sincere legal evolution must be well aimed so as not to stifle or retard the process of real state-capacity building. Yu advises that the US administration "be patient as [China] learns to become a respectable member of the international trading body."<sup>61</sup>

### **Signs of Hope**

There is reason to believe that strengthening China's IPR enforcement regime is possible. China has displayed a willingness and desire to improve protection of intellectual property and like-areas of regulation. For example, last summer they convicted Zheng Xiaoyu, head of the State Food and Drug Administration (SFDA), with charges of corruption and publicized his execution. Zheng, during his nearly ten-year term with SFDA, allegedly approved six medicines which turned out to be fake, approved the falsification of a number of documents and, among other crimes, accepted cash and gifts worth US\$ 832,000.<sup>62</sup> Zheng was sentenced to death on May 29 of 2007 and hung soon thereafter. This is one of a number of high profile corruption cases aimed at reinforcing the trend toward no tolerance.

---

<sup>58</sup> Hillery and Pantucci *The U.S. Escalates its WTO Complaint against China*

<sup>59</sup> Yu, Peter, *Still Dissatisfied After All These Years*, p. 1

<sup>60</sup> *Ibid.*, p. 4

<sup>61</sup> *Ibid.*

<sup>62</sup> AP "China executes former head of food and drug safety watchdog" *International Herald Tribune – Asia – Pacific* (Jul 10, 2007)

In addition to public corruption cases, there has been a sincere effort to provide measurable improvements in IP-related records. The National Working Group for IPR Protection has been instrumental in coordinating this effort by producing annual Action Plans which address ways in which China has and should continue to improve their intellectual property protection regimes.<sup>63</sup> This entity is charged with the task of coordinating the State Council to communicate IP-related interests of the state to all pertinent bureaucracies. The reality, however, is that this group lacks any formal power. The hope is, however, that this power relationship will evolve over time as the incentives for IP compliance continue. Signs of success, since 2003, for example, are that there has been a 60% increase in the number of trademark applications, there are now 850,000 active patents (twice that of five years ago). Additionally, the number of lawsuits regarding IP cases has more than doubled.

The international community has begun to recognize some of the improvements being made in intellectual property enforcement in recent years. The World Intellectual Property Organization (WIPO) has reported, for instance, that there has been an eight-fold increase in the number of patent filings by Chinese residents between 1995 and 2005.<sup>64</sup> The Chinese government has taken measures to improve their enforcement capacity. According to the International AntiCounterfeiting Coalition Inc, China has increased the number of “convictions for infractions by 52% and seizures of goods by nearly 100%.”<sup>65</sup> The Economist recently reported that since 2003, the number of trademark applications has grown by 60% while the

---

<sup>63</sup> National Working Group for Intellectual Property Rights Protection <http://english.ipr.gov.cn/en/index.shtml>

<sup>64</sup> World Intellectual Property Organization (WIPO) website accessed on April 17, 2008 <http://www.wipo.int/portal/index.html.en>

<sup>65</sup> Gonzalez, Gloria (2007) "Intellectual property theft is top risk for firms with operations in China; International pressure placed on China to effectively enforce laws" Business Insurance (Mar 26, 2007)

number of patents has nearly doubled (now 850,000).<sup>66</sup> Additionally, since 2003, the number of lawsuits regarding IP has more than doubled.<sup>67</sup>

Intellectual property protection is not limited to China. Globally, pirated and counterfeit goods are burdening legitimate markets with significant levels of lost revenue. It is estimated that US\$600 billion annually is lost globally while roughly US\$250 billion is lost by US businesses.<sup>68</sup> Improvements on the Chinese case could be used as models to improve the state of intellectual property protection on the global scale.

#### 4. Suggestions for A Way Forward

The cultural and political obstacles to solving the piracy problem in China will not be eliminated by a harsh imposition of Western notions of IP, and, unfortunately, creating a broad understanding of intellectual property ‘rights’ among the Chinese is not a simple, quick endeavor.<sup>69</sup>

Ultimately, the solution to the piracy problem is that private businesses must provide consideration for the protection they expect to receive in China, in the form of benefits to the populace or the government.<sup>70</sup>

--Ryan Johnson

#### Reorienting the Struggle

External pressure in the form of legislative negotiation has proved largely ineffective in producing results on the implementation front within China’s intellectual property regime. Johnson points out that “top-down” change in intellectual property protection in China neglects the “cultural differences and practical incapacities.”<sup>71</sup> The US and other governments can pressure Chinese officials to improve their legislation and enforcement practices by imposing trade sanctions or tariff penalization, but the real stage for improvement is not Beijing but the localities and specific entities charged with enforcement. Johnson points out that it is important

---

<sup>66</sup> The Economist "850,000 lawsuits in the making; Doing business in China" The Economist (Apr 12, 2008) U.S. Edition, Business Section

<sup>67</sup> Ibid.

<sup>68</sup> Johnson, Ryan, *Steal this Note* p. 1005

<sup>69</sup> Ibid., p. 1023

<sup>70</sup> Ibid., p. 1038

<sup>71</sup> Ibid., p. 1023

to move beyond pointing out the inefficiencies of the national-level pressures and rather to provide suggestions on how to break the “cycle of piracy” rampant in China.<sup>72</sup> Each of his suggestions stems from the belief that change must be driven by businesses actively trading with China today.

Andrew Mertha is a strong proponent of the belief that national policy and external pressures on Beijing are important in some respect, but believes that even more important are the efforts to pressure localities charged with implementation.<sup>73</sup> The reality is that managing and enforcing IPR occurs at the local level and henceforth any real improvements in this enforcement must be aimed at the needs and capacity of these localities.<sup>74&75</sup> Mertha points out that Policy and regulation “must pass through China’s Byzantine network of bureaucracies before it is translated into actual policy outcomes.”<sup>76</sup> He believes that the shifting pressure from the top-down (Sino-US negotiations) to a lateral (foreign businesses setting up investigation firms) has been successful and should be replicated in future enforcement efforts.<sup>77</sup>

Developing private investigative bodies to protect the interests of foreign businesses has proved successful in enforcing trademarks and could be replicated in other sectors. Many have argued that, since Chinese regulatory bodies are “demonstrably unfit” for IP protection, “any company accepting Chinese exports with official quality or safety certificates theoretically could be held liable for problems that subsequently emerge.”<sup>78</sup> In light of this threat and of their vested

---

<sup>72</sup> Ibid., p. 1030

<sup>73</sup> Mertha, Andrew, *The Politics of Piracy*, p. 3

<sup>74</sup> Ibid.

<sup>75</sup> “It should be clear that I am *not* arguing that laws are not important, but rather that how they are used depends on far more than simply the substance of the laws themselves. It is necessary to look at the institutions charged with upholding the law. Usually, such an approach focuses on the legal-judicial process. Indeed, this was where I had begun my own research. But it quickly became apparent—even obvious—to me that the lion’s share of activity was not taking place in judicial courts. The vast majority of mediation and enforcement was being undertaken by the administrative enforcement bureaucracies that have been analyzed in this book. Exclusively concentrating on the formal legal process—or, for that matter, on the administrative enforcement bureaucracies—provides an incomplete picture of how the law is utilized and enforced in China.” Ibid., p. 223

<sup>76</sup> Ibid., p. 5

<sup>77</sup> Ibid., p. 210

<sup>78</sup> Economist Intelligence Unit ViewsWire, published on June 12, 2007, accessed on April 25, 2008 on [http://www.economist.com/agenda/displaystory.cfm?story\\_id=9325404](http://www.economist.com/agenda/displaystory.cfm?story_id=9325404)

interest in securing IPR and quality compliance, private foreign entities should bear the financial cost of vamping Chinese enforcement capabilities.

One of the problems with the incentive structure for IP enforcement, as mentioned earlier, is that the Central Government provides inadequate operating expenses to carry out the necessary actions of enforcing IP. Many pirating entities have capitalized on this disincentive by providing “kickbacks” and bribes to the local enforcement officials for allowing their operations to persist.<sup>79</sup> It would take little for foreign entities to trump these kickbacks and counterbalance the disincentives. To be very clear, however, this does not simply mean throwing money at the problem, as Mertha astutely points out.<sup>80</sup> It requires a sincere understanding of the intricacies of the organization structure and incentive structures of the bureaucracies charged with IPR enforcement.

As Mertha explained in the case of trademark enforcement, partnerships between private investigative firms and the government administrative bodies are a viable and proven success option. This is an area which has seen growth in recent years as the number of investigative firms was only about “fifteen at the end of 1999 and have mushroomed since then.”<sup>81</sup> The interplay between private investigators and Chinese government agencies is critical to successful enforcement of IPR. Mertha notes that “the former lay the groundwork and absorb the costs, the latter provide the official authority (i.e., legitimacy and legality) and take the credit.”<sup>82</sup> As long as foreign entities conform to this power relationship there is no reason why this example cannot be replicated in other IP-related issues or other international legal issues in China. It is important

---

<sup>79</sup> Mertha, Andrew, *The Politics of Piracy*, p. 19

<sup>80</sup> *Ibid.*, p. 194

<sup>81</sup> *Ibid.*, p. 196

<sup>82</sup> *Ibid.*, p. 166

for the foreign entities to allow the administration to save face and also to be willing to incur the costs (bribes are often expected) for carrying out their interests.<sup>83</sup>

### **Incentives and Culture**

In order to create a culture of enforcement in China it is important to introduce intellectual property in such a way that the Chinese populace will be interested in adhering to the law. For example, when Chinese (and the majority of developing countries as well) perceive IP as a means by which foreign companies can secure profit abroad, they will understandably be averse to any legislation which supports this endeavor. If, however, these same individuals were to understand IP protection as serving their interests, they may be more adept to favoring companies which respect IPR. Ryan Johnson suggests that companies should try to create this culture by launching marketing campaigns aimed at branding IP with quality assurance.<sup>84</sup> For example, simply pointing out the dangers and effects of counterfeit pharmaceuticals could have significant effects on the survival of these companies. Rather than focusing on punishments and government regulations, agencies for change should popularize the interests of consumer health and product quality. Such efforts will circumvent critical obstacles to IP adoption present in Chinese culture. This was successful, Yu points out, when a factory in China producing fake Heinz baby food was found and publicly raided.<sup>85</sup> The footage of the raid was shared and as one would expect the consumers were upset. This re-focused the concern of IP to one related to the health of the local citizens rather than to the interests of the foreign corporation looking to protect their profits.

---

<sup>83</sup> Ibid.

<sup>84</sup> Johnson, Ryan, *Steal this Note*, p. 1031

<sup>85</sup> Yu, Peter, *Still Dissatisfied After All These Years*, p. 10

One of the problems with the aforementioned scenario lies in the assumption that Chinese have the ability to opt to choose the higher quality and protected product.<sup>86</sup> To curb piracy, than, one must also find ways to provide products to consumers in China at prices they can afford so as to combat the temptation to purchase the lower priced counterfeit good. Duracell succeeded in this effort by establishing a manufacturing plant in China to lower shipping costs.<sup>87</sup> Because most Chinese have very limited expendable income, the pricing of legitimate goods is inappropriate. Therefore, providing lower-priced legitimate alternatives to the pirated goods, which maintain a higher quality, will create the incentive to honor purchasing the legitimate product. Such has been the practice of Hollywood industries who provide dubbed and sub-titled versions of American films.<sup>88</sup> This allots their distribution in China while Westerners would not opt to purchase a dubbed and sub-titled film even if the price is far less than that of its domestic counterpart. This solution of re-pricing, however, is easier said than done for many businesses considering the costs incurred in the process.

Another way to improve the culture of IP protection is to marry Chinese capitalists to the monetary benefits had by successfully protecting IP. This can be done by establishing joint-venture businesses in China.<sup>89</sup> The foreign entity is benefiting from the *guanxi* network provided by the Chinese partner. These local partners will develop a real vested interest in the protection of their products IP license and share this concern with their *guanxi* networks. It is important to provide incentives which Chinese markets will absorbed willingly. Because they are interested in profit, rather than introducing restrictions and limitations, marry them to the profits to be had by the protection of intellectual property. Yu echoes this argument by suggesting that local partners

---

<sup>86</sup> State agencies charged with controlling the sales of pirated products argue that “because the legitimate products are too expensive, consumers create the demand for a black market in pirated goods...these officials are content to look the other way while such activity takes place for several reasons that combine economic and social/political considerations.” Mertha, Andrew, *The Politics of Piracy*, p. 19

<sup>87</sup> Johnson, Ryan, *Steal this Note*, p. 1034

<sup>88</sup> Yu, Peter, *Still Dissatisfied After All These Years*, p. 8

<sup>89</sup> Johnson, Ryan P. *Steal this Note*, p. 1036

“will provide the internal push for legal reforms and will protect the reformist leaders from being criticized for kowtowing to foreign interests.”<sup>90</sup>

China is still a major source of counterfeit pharmaceuticals.<sup>91&92</sup> This is such a problem, in fact, that the government will not approve clinical trials of any drugs manufactured in China unless those drugs are approved for use abroad.<sup>93</sup> Despite these problems, Novartis has begun the development of a medical research facility in Shanghai valued at \$100 million.<sup>94</sup> The reason for this is to improve the research and development in China in hopes of creating a hub comparable to Cambridge, Massachusetts or Basel, Switzerland. This will capitalize on the international fervor of Shanghai where academics and business are improving and growing. The most encouraging result of this may be that, as per a goal mentioned earlier, this might marry the Chinese to the profits to be had by intellectual property if Novartis research and development in this Shanghai facility becomes successful.

### **Discussion and Conclusion**

As Mertha demonstrated through an analysis of the trademark regime in China, exogenous pressure can have a positive effect on the formation, implementation and enforcement of policy. The critical components of this success include understanding the state capacity already existing and addressing the incentive structures which may be limiting real enforcement. The success of trademark enforcement in this case can be learned from and applied to other realms of IPR and ought to be applied to other issue areas as well. It seems as though Mertha has uncovered a skeleton model for real protection and this model can be manipulated to appease the interests of

---

<sup>90</sup> Yu, Peter, *Still Dissatisfied After All These Years*, p. 7

<sup>91</sup> Johnson, Ryan, *Steal this Note*, p. 1021

<sup>92</sup> “China’s relatively short patent law history and fractured judicial system, the risk of counterfeiting and the difficulty with patent enforcement remain decisive factors in companies’ considerations as to whether to make and sell patented pharmaceuticals in China.” Hason and Shimotake, *Global Interdependence and International Commercial Law*, p. 315

<sup>93</sup> The Economist “A novel prescription; Novartis” The Economist (Nov 11, 2006) U.S. Edition. Business Section

<sup>94</sup> Ibid.

international trading partners if enacted upon. The only missing pieces are widespread knowledge and proper investments.

It is improper to assume that the Central Government in China is to blame for the lack of intellectual property protection. The tendency to do so oversimplifies and omits the real problems, which are the capacity and incentives for local officials to implement national legislation. China's legislative regime for intellectual property and implementation has been evolving over the past thirty years and these evolutions have improved the system, yet this route is limited in immediate relief. For immediate relief, foreign entities must address the problems at the local levels and fill gaps in the Central Government as they persist.

It is clear that the current enforcement practice is imperfect. Successful exogenous pressure will identify and fill the voids of incentive and capacity. Those which have achieved this are doing so by utilizing the administration already in place and applying the necessary pressure and incentives. Therefore, as long as public scrutiny continues to pressure foreign businesses to bear the cost of implementation voids in China, the system can be effectively vamped and secured.

One must not become blind to the faults of the United States or Germany when criticizing the allowance of counterfeited goods to be traded internationally. A trade, in fact, involves two parties, both of which share the responsibility for regulation and quality control. Similarly to the problems faced by the Chinese government, the United States government is faced with operative challenges. The United States Food and Drug Administration (FDA) is currently discussing how to ensure that other heparin-like incidents do not occur in the future. The Government Accountability Office has recently produced a report suggesting that this regulative goal can be achieved, but at a very high cost. This high cost, it should be noted, would ensure that the FDA international regulatory bodies in China visit these manufacturing sites as often as

they do visit domestic manufacturing sites. This, however, may be an insignificant and unsuccessful attempt given the complexity and liquidity of the counterfeit regimes in China. Therefore, although the FDA certainly bears the responsibility to protect US citizens, their capacity to address this problem may be ill-suited and inefficiently deployed. This realization may shed more light on the argument favoring the introduction of third party entities (i.e., the foreign businesses involved in the trades) to bear the cost and responsibility for regulated trade. If, as it has been proven, China and the US share similar government capacity limitations, the logical conclusion is to delineate responsibility to a third party.

If we are to assume that enforcement implementation will be successful, we need to employ the businesses conducting trade with China to bear the cost of the regulations. The organization of these enforcement entities must mimic that of the trademark case which Mertha shares. This was a demonstration of successful exogenous pressure and any body interested in applying such pressure should capitalize on this model. Therefore, in the case of heparin, the pharmaceutical companies importing these drugs from China should bear the cost of regulative enforcement and create trademark-like investigative firms in the localities of China in which they conduct business. The replication of Mertha's trademark model could prove to be the proactive solution to persistent problems of consumer safety resulting from internationally traded goods.

### Bibliography

Boyle, Elizabeth (2006) "Book Review: The Politics of Piracy: Intellectual Property in Contemporary China" Law and Society Association, University of Massachusetts Law Society Review (Dec 2006) 40 Law & Soc'y Rev. 981

Cabrera, Luis (2007) "The Inconveniences of Transnational Democracy" Ethics & International Affairs Vol. 21, Issue 2, pp 219-238

Carothers, Thomas (2006) Promoting the Rule of Law Abroad: In Search of Knowledge  
Carnegie Endowment for International Peace: Washington D.C.

Checkel, Jeffrey T. (1999) "Why Comply? Constructivism, Social Norms and the Study of International Institutions" ARENA Working Paper

Duncan, Christopher (2002) "Out of Conformity: China's Capacity to Implement World Trade Organization Dispute Settlement Body Decisions After Accession" American University International Law Review Vol. 18, pp 399 - 507

Gonzalez, Gloria (2007) "Intellectual property theft is top risk for firms with operations in China; International pressure placed on China to effectively enforce laws" Business Insurance (Mar 26, 2007)

Hason, Averie K. and Jean E. Shimotake (2006) "Global Interdependence and International Commercial Law: Recent Developments in Patent rights for Pharmaceuticals in China and India" Pace International Law Review (Spring2006) Vol. 18, pp 303 - 315

Hillery, John and Niccolo Pantucci (2007) "The US Escalates its WTO Complaint against China" Commentary publication from Center for Strategic and International Studies Washington D.C. (Aug. 31, 2007)

Johnson, Ryan P. (2006) "Steal this Note: Proactive Intellectual Property Protection in the People's Republic of China" Connecticut Law Review (Jul 2006) Vol. 38, pp 1005-1039

Lieberthal, Kenneth (2004) Governing China: From Revolution Through Reform. New York: W.W. Norton & Company

Mansfield, Edward D. et. al. (2002) "Why Democracies Cooperate more: Electoral Control and International Trade Agreements" International Organization (Summer2002), Vol. 56, Issue 3, pp 477-513

Mertha, Andrew C. (2005) The Politics of Piracy: Intellectual Property in Contemporary China  
Cornell University Press: New York

Mertha, Andrew and Robert Pahre (2005) "Patently Misleading: Partial Implementation and Bargaining Leverage in Sino-American Negotiations on Intellectual Property Rights" International Organization (Summer2005), Vol. 59, Issue 3, p695-729

Office of the United States Trade Representative (USTR) "2007 Special 301 Report" (April 2007)

Oksenberg, Michel (2001) "China's Political System: Challenges of the Twenty-First Century" The China Journal No. 45 (Jan 2001) pp 21-35

Steinberg, Richard H. (2002) "In the Shadow of Law or Power? Consensus-Based Bargaining and Outcomes in the GATT/WTO" International Organization (Spring2002), Vol. 56, Issue 2, pp 339-374

"China's Action Plan on IPR Protection 2008" published by the State Intellectual Property Office (March 18, 2008)

Wilson, Lindsay (2003) "Investors Beware: The WTO Will Not Cure All Ills with China" Columbia Business Law Review pp 1007-1030

World Trade Organization (WTO) "Marrakesh Agreement Establishing the World Trade Organization Annex 1C, Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994

Yu, Peter K. (2005) "Still Dissatisfied After All These Years: Intellectual Property, Post-WTO China, and the Avoidable Cycle of Futility" Georgia Journal of International and Comparative Law Vol. 34

---- (2000) "From Pirates to Partners: Protecting Intellectual Property in China in the Twenty-First Century" American University Law Review Vol. 50

Zhonghua, Yan, ed. National Working Group for IPR Protection Office "China's Action Plan on IPR Protection 2007" published by the State Office of Intellectual Property Protection (April 23, 2007)

#### Bibliography of News Sources

AP "China source of half EU's dangerous Goods" International Herald Tribune (Apr 17, 2008)

AP "China executes former head of food and drug safety watchdog" International Herald Tribune – Asia – Pacific (Jul 10, 2007)

Barboza, David "China Orders New Oversight of Heparin, With Tainted Batches Tied to U.S. Deaths" The New York Times March 22, 2008

----- "Why Lead in Toy Paint? It's Cheaper" The New York Times (Sep 11, 2007)

Economist "850,000 lawsuits in the making; Doing business in China" The Economist (Apr 12, 2008) U.S. Edition, Business Section

Economist "A novel prescription; Novartis" The Economist (Nov 11, 2006) U.S. Edition. Business Section

Harris, Gardiner "Tainted Drugs Put Focus on the F.D.A." The New York Times March 17, 2008

Hooker, Jake and Walt Bogdanich “Scientists Near Source of Altered Heparin” The New York Times March 19, 2008

Pollack, Andrew “California Delays Plan to Track Prescription Drugs” The New York Times March 26, 2008

Zamiska, Nicholas and Heather won Tesoriero “Drug Headache: As Pfizer Battles Fakes in China, Nation’s Police are Uneasy Allies” Wall Street Journal Jan 26, 2004