



Best Practices: Intellectual Property Protection in China

Intellectual property (IP) is a longstanding, critical concern for companies operating in China. IP enforcement has placed consistently among US-China Business Council (USCBC) member companies' top 10 issues since USCBC began its annual membership survey, and concern about IP enforcement remains a major factor shaping company operations and plans in China. Though China has created a set of IP laws that generally adhere to international standards over the last 20 years, and has made efforts to protect and enforce IP rights, insufficient implementing regulations and judicial interpretations, significant procedural barriers, and uneven enforcement continue to frustrate the efforts of companies to protect their IP in China. At the same time, counterfeiters and infringers in China are more sophisticated and increasingly deploy advanced reverse-engineering techniques, adopt legal measures such as preemptive filing and patent challenges, and find new ways to infiltrate legitimate distribution networks and to build their own parallel networks.

Two decades in the trenches have equipped multinational corporations with hard-won experience and a set of strong preventive best practices. Companies must move beyond internal controls and proactively engage outside parties to protect their IP. To be successful in China, companies should develop an integrated IP protection strategy based on the nature and extent of the IP problems they face in China and on a realistic assessment of internal goals and resources.

This best practices document will lay out key strategies and tactics that companies should adopt in their attempt to identify and protect their IP in China, both to prevent IP problems and to tackle IP infringement. To protect their IP in China, companies should follow several steps:

Craft a Corporate IP Protection Strategy

- Make IP protection a core responsibility of the entire China management team, not merely a function of the legal counsel's office, and dedicate resources appropriate to the company's IP protection goals.
- Regularly communicate the value of protecting IP to all employees, business partners, and customers. As the level of IP consciousness among Chinese citizens grows slowly, it is particularly important that companies instill a sense of "ownership" of company IP among staff.
- Conduct an initial IP audit of internal controls and an IP survey of external problems and issues, with regular follow-up reviews.

Adopt Preventive Measures to Protect IP

Register IP in China

If a company does not file its copyrights, patents, and trademarks in China, it has no rights in China. Companies should register their works in China as early as possible.

- **Copyrights** Though registration is not required, entities should consider registering their works with the National Copyright Administration, since registration provides a public record and serves as useful evidence in court.
- **Patents** Companies should file applications with the State Intellectual Property Office for both core and fringe technologies that they plan to use in China and ensure that their patents

are properly translated before filing. Companies conducting research and development in China should be aware of the impact on patents from recent laws and regulations, including the Corporate Income Tax, Antimonopoly, and Patent laws.

- **Trademarks** Companies should register their brands' English and Chinese names with the China Trademark Office. When filing, they should carefully select the product categories and sub-categories in which to file, and check China's online trademark database for similar trademarks filed by competitors and infringers, including marks filed in categories outside a company's core products. Companies should be aware that the backlog of trademark applications in China is significant and growing, with applications often taking several years to be approved.
- **Trade secrets** A trade secret in China must be technical or operational information that is unknown to the public, economically beneficial to the owner, and reasonably protected by the owner. PRC law also requires that the secret have "practical applicability" and that the company take practical steps to protect it. Trade secrets are often difficult to protect in court because of the high burden of proof placed on plaintiffs. Though trade secrets cannot be formally registered in China, companies should still craft and document internal policies and strategies to protect trade secrets, as such documentation is critical evidence in a trade secrets dispute. Companies can do many of the things listed below to protect their trade secrets as well as their other IP.

Control the production process

- Compartmentalize critical steps in the design and production processes for products involving IP—and the equipment used to manufacture these products—so that no employee has access to all the information needed to copy IP;
- Keep vital designs and latest-generation technologies in their home countries, bringing to China only IP that makes business sense for China;
- Classify information according to IP sensitivity, laying out which employees have what level of access to the information; and

- Consider incorporating into the production process technologies and techniques that are difficult to copy, such as chemicals, foils, inks, labels, papers, stamps, and threads.

Focus on human resources

- Run background checks on key hires and include noncompete and nondisclosure agreements in contracts;
- Share IP information with employees on a "need-to-know" basis;
- Educate employees about the firm's confidentiality requirements, and about consequences of IP violations;
- Track data flows and file transfers (both paper and electronic), and closely monitor the entry and exit of flash disks, portable hard drives, laptops, and sensitive paper documents;
- Control and monitor employee access to sensitive equipment and facility areas; and
- Conduct exit interviews with departing employees to recover any sensitive materials and remind them of confidentiality obligations.

Carefully select and monitor suppliers and distributors

- Select partners with a demonstrated understanding of the value of IP, especially those with brand images and reputations of their own to protect;
- Conduct comprehensive due diligence on suppliers and distributors prior to any agreement and on a regular basis afterward;
- Include IP protection clauses in all contracts and agreements;
- Manage supplier, vendor, and distributor relationships through multiple personnel to limit the ability of local staff to abuse business networks; and
- Review information that could be sent to third parties before transmission to ensure that it is not sensitive, or that the benefits of sending it outweigh the risks of it being leaked.

Build internal lines of communication on IP

- Establish an internal fraud hotline, as well as an outside hotline for confidential communication with suppliers, distributors, customers, and other third parties to report counterfeiting; and

- Build a database of company infringement cases and infringers and make it available to key employees across the company's China offices.

Engage IP enforcement bodies

- Build relationships with government officials at multiple levels in IP-related government agencies and courts relevant to the company's industry, well before any problems arise; and
- Educate local officials responsible for allocating the resources for and enforcing IP protection about the company's IP protection needs. For companies facing problems with exported counterfeits, this includes recording IP with the General Administration of Customs in Beijing and educating local Customs officials to watch for these goods.

Work with outside IP service providers and industry associations

- Engage with industry associations, including both IP-specific and industry-specific associations, to exchange best practices for IP protection, identify repeat offenders, and, if appropriate, to develop collective strategies and actions;
- Build ties with, and conduct due diligence on, IP service providers and investigative firms; and
- Work with local and national media as appropriate to address negative publicity that could accompany an IP case against a domestic company.

Search for cases of infringement

- Send representatives to visit trade fairs, such as the Chinese Export Commodities Fair (Canton Fair), and industry trade shows to look for counterfeiters;
- Review distribution networks at all levels regularly for weak links and possible entry points for counterfeit products;
- Monitor IP publications, including the PRC Patent and Trademark gazettes, for new patents and trademark applications to see if they infringe on the company's IP; and
- Check the Internet regularly for infringing domain names and for websites that are used as platforms for counterfeit products. These

include online auction sites such as Alibaba and Taobao.

Confront IP Infringement

Contact infringers and their service providers

- Send cease-and-desist (C&D) letters to infringers. C&D letters can be a cost-effective way to stop infringement in some cases, especially those involving small infringers. These letters, however, also alert infringers that a company is aware of their presence, which could prompt them to move, change names, or otherwise alter their operations in ways that could inhibit a company's ability to gather evidence; and
- Work with Internet marketplaces and Internet service providers to remove infringing goods from websites and to take down websites selling infringing materials.

Pursue infringers through official channels

Companies should utilize the various official channels available to halt infringement in China, weighing company resources, timelines, and the strengths and weaknesses of the adjudicator before determining which route to pursue. Available channels include administrative cases, as well as civil and criminal cases in China's courts.

- **Administrative actions** If requested, administrative authorities—particularly the local administrations of industry and commerce—can carry out raids and investigations to check for IP infringement.
 - **Pros** These actions are easier and faster than civil or criminal suits, can halt IP infringement, and can result in fines. Many companies and administrative agencies have significant experience using administrative channels, making the process easier.
 - **Cons** Although administrative agencies carry out raids, companies should be prepared to undertake significant preparatory investigations before submitting a request for administrative action to local authorities. In addition, infringers cannot be sentenced to jail time.
- **Civil cases** Civil suits are heard by specialized intellectual property tribunals in China's civil courts, generally with the court of first instance being an Intermediate People's Court.

- **Pros** In addition to halting infringement, civil suits also allow the rights holder to recover damages and to receive injunctive relief. Civil courts may be better equipped to handle complex cases when administrative authorities are unable to make a determination of infringement.
- **Cons** Civil suits can be costly and time-consuming. Companies bear the responsibility of collecting evidence but do not benefit from a formal discovery process and often have difficulty getting outside evidence admitted to the court. The burden of proof in these cases lies with the plaintiff. These cases can take even longer when an infringer initiates patent invalidation proceedings with the State Intellectual Property Office or a trademark opposition case with the China Trademark Office, suspending the suit pending a decision.
- **Criminal cases** Criminal cases are first investigated by local public security bureaus (PSBs), which then transfer cases to criminal tribunals in the People's Court with appropriate jurisdiction. The court of first

instance usually falls at the sub-provincial level.

- **Pros** Judges in criminal cases can not only order infringement to stop, but also sentence IP violators to jail time;
- **Cons** Criminal actions are difficult to set in motion, as they can be transferred from administrative authorities only if the infringement value meets minimum thresholds. In practice, these thresholds are extremely difficult to meet, even when infringers have a sizable inventory of infringing goods, because of inadequate records of sales by infringers and the Chinese practice of basing the value of the infringing goods on the market price of the infringing goods (instead of the market price of the legitimate product). The IP rights holder must generally undertake all of the investigative work and package a complete case for the local PSB, as local police may lack the necessary resources to conduct a thorough investigation. In practice, many PSBs are reluctant to tackle difficult or complicated cases.