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THE GRAY (GOODS) ELEPHANT IN THE ROOM: CHINA'S TROUBLING ATTITUDE TOWARD IP PROTECTION OF GRAY MARKET GOODS

INTRODUCTION: HUNGRY FOR THE FIRST BITE OF THE APPLE

September 17, 2010: Apple's newest, hottest release, the iPad®, successfully debuted in China,¹ one of the world's largest markets. This was an achievement for Apple® after the disastrous launch of the Chinese iPhone® in 2009,² when the typically dynamic company could not move stock from the shelves.³ The reason? Interested Chinese buyers had long owned iPhones®. Apple's iPhone® debut in China lagged nearly two years behind its introduction to the United States and Europe.⁴ Many Chinese consumers ordered hacked and reprogrammed phones, shipped in from hubs like Prague and New York.⁵ Some of the phones made an even shorter journey as they simply "leaked" into the market from the Chinese factories where they were produced.⁶ Apple's global vision was no match for the dynamic gray market.

The gray market, or parallel market,⁷ occurs when goods intended for one market are redirected, unauthorized, to another.⁸ The goods literally

1. Loretta Chao, *China Gets the iPad*, WALL ST. J. CHINA REAL TIME BLOG (Sept. 17, 2010, 5:30 AM), <http://blogs.wsj.com/digits/2010/09/17/china-gets-the-ipad/>.

2. *Id.*

3. *Id.*

4. Compare Matthew Honan, *Apple Unveils iPhone*, MACWORLD (Jan. 9, 2007), <http://www.macworld.com/article/54769/2007/01/iphone.html>, with Chao, *supra* note 1 (providing date of iPhone debut in China).

5. Peter Burrows, *Inside the iPhone Gray Market*, BLOOMBERG BUSINESSWEEK (Feb. 12, 2008), http://www.businessweek.com/technology/content/feb2008/tc20080211_152894.htm.

6. *Id.*

7. A "gray good" belonging in the "gray market," as defined by the United States, is "a foreign-manufactured good, bearing a valid United States trademark, that is imported without the consent of the United States trademark holder." *K Mart Corp. v. Cartier, Inc.*, 486 U.S. 281, 285 (1988). Thus, the phrase is technically very narrow. However, this concept has been extended and is often used interchangeably with similar provisions for patented and copyrighted materials, such as "parallel market," and need not be manufactured abroad. DAVID R. SUGDEN, *GRAY MARKETS: PREVENTION, DETECTION AND LITIGATION* 4 (2009); Stefan M. Miller, *Parallel Imports: Towards a Flexible Uniform International Rule*, 15 J. COM. BIOTECHNOLOGY 21, 22 (2009). In this Note, "gray good" and "gray market" are used as general terminology indicating products imported through unauthorized channels. However, "parallel import" refers to the verb, due to nuance. "Parallel import," referring to goods, is only used for clarity while mentioning both gray goods and the black market.

parallel those imported through the authorized channel. For example, “Business” authorizes ten units to be sold to a retailer in country A and five to be sold to a separate retailer in country B, pricing the same goods differently to target specific markets. Business is unaware that the retailer in B resells its units to stores in A and C. The stores in A and C have just engaged in parallel importation. Essentially, Business ends up competing with itself, as its lower priced goods destined for B compete against the higher priced goods in A’s market. The purpose of this indirect importation is often to supply the product to a void, like the iPhone’s initial China release, but more likely, it is to undersell the goods intended for that market.⁹ Essentially, those who parallel import from cheaper nations can sell the same product at a lower price than those who use the authorized channel.

Americans today are familiar with the gray market as it affects them. Stores like Costco stock their shelves with affordably priced products often redirected from foreign locales.¹⁰ Textbooks ordered from the internet arrive in College Hill by way of Hong Kong.¹¹ Westerners are comfortable importing goods on a whim from major developing countries like China. Seldom, however, do Westerners contemplate China’s own massive economy and subsequent pull on the gray market.

Some may see parallel imports as a fair extension of the global marketplace.¹² This does, after all, allow companies to reach new markets.¹³ However, the gray market expert David R. Sugden explained, “As the name aptly suggests, gray market goods reside in the murky area of law between legitimacy and illegality.”¹⁴ Many large companies distributing products globally find grounds to litigate,¹⁵ and governments are concerned, too, as they miss out on potential sales tax revenue on the autho-

8. Jorge Espinosa, *What is the Parallel Market?*, THE GRAY BLOG (last visited Sept. 30, 2010), http://espinosaiplaw.com/wordpress/?page_id=5.

9. For an illustration of this concept, see WARWICK A. ROTHNIE, *PARALLEL IMPORTS* 1 (1993).

10. Daniel Fisher, *Costco v. Omega Tests the Power of a Logo*, FORBES ON THE DOCKET BLOG (Apr. 19, 2010, 6:53 PM), <http://blogs.forbes.com/docket/2010/04/19/costco-v-omega-tests-power-of-a-logo>.

11. See Jeff Shelstad, *The Demise of the \$200 Textbook*, GOOD (July 8, 2010), <http://www.good.is/post/the-demise-of-the-200-textbook>.

12. See SUGDEN, *supra* note 7, at 30–31.

13. *Id.* at 60–62. Pricing appropriately for the destination ensures that an article has a better chance of selling in that new market. *Id.*

14. *Id.* at 4–5.

15. See SUGDEN, *supra* note 7, at 297–309 (describing approaches companies may pursue globally.)

rized product's higher price.¹⁶ Additionally, governments are concerned about the lack of regulation of gray market goods—when unauthorized—products used or even ingested by consumers may be tampered with or of inferior quality.¹⁷ Not only does the gray market pose risks and disrupt a company's profitability, it also poses problems for the entity's intellectual property rights ("IPR").¹⁸

Companies may have trademark, patent, and copyright claims from the unauthorized sale and importation of goods.¹⁹ Trademarks help identify a company's products and services by distinguishing them from similar ones²⁰ with the purpose of establishing "goodwill."²¹ They may be symbols, words, names, or devices, among other indicators.²² Copyright protects expression of an idea through original works of authorship, be it a fine painting, video game, or logo design.²³ Concerned companies may defend products bearing copyrighted logos, copyrightable content, or a trademark through various intellectual property laws.

The Supreme Court's recent decision in *Costco v. Omega*²⁴ catapulted the gray market to the top of American and other Western countries' attention.²⁵ Following similar U.S. cases where trademark infringement

16. For a discussion of the tax implications of black market goods, see *id.* at 56–59.

17. Lack of control over one's products opens parallel imports to typical black market problems. *Id.* at 5–6. However, quality control issues may arise from a manufacturer itself. For example, Tic Tacs intended for different markets feature different ingredients and Abercrombie sells lower quality clothing to foreign markets. *Id.* at 16–18. Consumers may be unaware that they are purchasing lesser goods imported through the parallel market.

18. Intellectual Property is the law of patents, copyrights, and trademarks (among others). It protects the intangible, and "the law creates the property by defining what will be protected from others." DONALD A. GREGORY ET AL., INTRODUCTION TO INTELLECTUAL PROPERTY 1–2 (1994). Essentially, it protects ideas and inventions, expression and works of authorship, good will and designations of origin. *Id.* at 2–4.

19. PARALLEL IMPORTS IN ASIA I (Christopher Heath ed., 2004) [hereinafter PARALLEL IMPORTS IN ASIA]. This should not distract from the fact that parallel import issues are mostly economic. ROTHNIE, *supra* note 9, at 3.

20. U.K. TRADE & INVESTMENT, U.K. INTELLECTUAL PROP. OFFICE., HUNTER RODWELL CONSULTING & ROUSE & CO. INT'L, INTELLECTUAL PROPERTY RIGHTS PRIMER FOR CHINA 9 (2008) [hereinafter CHINA IP PRIMER].

21. Michael A. Ugolini, *Gray Market Goods Under the Agreement on Trade-Related Aspects of Intellectual Property Rights*, 12 TRANSNAT'L L. 451, 462 (1999).

22. GREGORY ET AL., *supra* note 18, at 81.

23. See *id.* at 4, 168–69. Logos typically fall under trademark protection but copyright may also be applicable. Compare *id.* at 186–87, with *id.* at 154. Patents protect inventions but are not discussed for purposes of this Note. *Id.* at 2.

24. *Costco Wholesale Corp. v. Omega, S.A.*, 131 S. Ct. 565 (2010).

25. This case was highly visible as leading news outlets across the United States reported its developments. See *Court Ruling in Costco Case Could Affect Discount Retail-*

action was denied because the items in question were genuine, the Swiss watchmaker Omega sued Costco for purchasing and selling watches in the United States that were originally priced and distributed to cheaper markets.²⁶ Omega pursued this action through copyright protection, claiming that its copyrighted logo featured on the underside of the watch makes the entire watch protectable, and thus this sale violated Omega's exclusive control of its copyright.²⁷ The Ninth Circuit determined that the first sale doctrine, a limit on exclusive control after the first sale, only applied to goods "legally made" within the United States.²⁸ Since the watches were made in Switzerland, Omega could continue its control over the copyrighted material.²⁹ The Supreme Court granted certiorari, and businesses and consumers everywhere waited anxiously for clarification on the right to resell copyrighted material.³⁰ However, the Supreme Court's decision further confused matters by affirming Omega's right to control without establishing precedent,³¹ leaving American resellers, consumers, and businesses without clear direction.

ers, N.Y. TIMES, Nov. 9, 2010, at B11 [hereinafter *Court Ruling in Costco Case Could Affect Discount Retailers*].

26. Omega S.A. v. Costco Wholesale Corp., 541 F.3d 982, 983–84 (9th Cir. 2008). As there were only nine words to the Supreme Court decision, this Note refers to the lower courts' discussion of the issues. For an explanation, see Jorge Espinosa, *Supreme Court Will Revisit Quality King Distributors, Inc. v. L'Anza Research Int'l, Inc.*, THE GRAY BLOG, <http://espinosaiplaw.com/wordpress/?p=93> (last visited Oct. 18, 2010). For a possible reason for the split, see Fisher, *supra* note 10; Greg Stohr, *Elena Kagan, the Absent Supreme Court Justice*, BLOOMBERG BUSINESSWEEK (Sept. 23, 2010), http://www.businessweek.com/magazine/content/10_40/b4197031526266.htm.

27. David Kravets, *All Rise: Supreme Court's Geekiest Generation Begins*, WIRED (Oct. 1, 2010), <http://www.wired.com/threatlevel/2010/10/supreme-court-2010-2011-term>.

28. *Omega S.A.*, 541 F.3d at 900.

29. *Id.*

30. *Court Ruling in Costco Case Could Affect Discount Retailers*, *supra* note 25.

31. *Supreme Court's Tie Vote Sustains Swatch Against Costco*, N.Y. TIMES, Dec. 14, 2010, at B7. This decision revolved around the "first sale" doctrine, also known as "exhaustion," which says that copyrightable materials in the form of chattels (tangible objects) may only be controlled by the author during the first sale. Any subsequent reselling is beyond the author's control. See MARSHALL A. LEAFFER, UNDERSTANDING COPYRIGHT LAW 328–31 (2010). *Costco v. Omega* suggests that this could be limited to products within the United States, providing authors of copyrightable materials manufactured outside of the United States perpetual or at least greater control than those from within the United States. *Supreme Court Rebuffs Costco in Copyright Challenge*, FORBES FULL DISCLOSURE BLOG (Dec. 13, 2010, 1:31 PM), <http://blogs.forbes.com/danielfisher/2010/12/13/supreme-court-rebuffs-costco-in-copyright-challenge> [hereinafter *Supreme Court Rebuffs Costco in Copyright Challenge*].

This controversy is not unique to the United States. Regardless of American laws about the American market, large emerging economies are clamoring for the same goods as the rest of the world, but at lower prices. China, well known for its exports, is one of the world's largest economies³² with the world's largest population,³³ and is thus naturally a dynamic importer.³⁴ Over 12% of its \$954.3 billion imports³⁵ come from Japan and another 7.66% from the United States.³⁶ China, as an extremely populous importer of expensive goods, is ripe for parallel importation issues.

Those attune to IPR around the world should carefully watch the issue of gray goods. China is already branded with a scarlet ©, as it is often labeled a “chronic and notorious abuser of IPR.”³⁷ This is particularly important considering that China today is the third largest trading nation³⁸ and is obligated to protect IPR through a series of treaties.³⁹ Copyright and trademark laws with respect to trade are loosely enforced in China, and though improving, it is dubious whether China is ready to address IPR to the same degree as the developed world. This potentially poses problems for companies hoping to protect against parallel imports in China by asserting IPR claims.

China shed its Communist regime only a few decades ago, and a new capitalist market quickly sprung up in its void.⁴⁰ Although China became obligated to protect intellectual property upon joining the World Intellectual Property Organization (“WIPO”) in 1980⁴¹ and World Trade Organ-

32. See GORDON C. K. CHEUNG, *INTELLECTUAL PROPERTY RIGHTS IN CHINA: POLITICS OF PIRACY, TRADE AND PROTECTION* 5 (2009).

33. As of July 2010, China's population was 1,330,141,295. CENTRAL INTELLIGENCE AGENCY (CIA), *THE WORLD FACTBOOK, EAST & SOUTHEAST ASIA: CHINA* (2010) [hereinafter *WORLD FACTBOOK*], available at <https://www.cia.gov/library/publications/the-world-factbook/geos/ch.html> (follow “Download Publication” hyperlink).

34. The CIA *World Fact Book* lists China as the third largest purchasing power and the sixth largest “real growth rate” in the world. *Id.*

35. 2009 estimate. *Id.*

36. *WORLD FACTBOOK*, *supra* note 34.

37. SUGDEN, *supra* note 7, at 306; see also Greg Creer, *The International Threat to Intellectual Property Rights Through Emerging Markets*, 22 *WIS. INT'L L.J.* 213, 218–19 (2004).

38. Susan Ariel Aaronson, *How Disciplining China Could Save the WTO*, VOXEU.ORG (Feb. 9, 2010), <http://www.voxeu.org/index.php?q=node/4581>.

39. PETER GANEA & THOMAS PATTLOCH, *INTELLECTUAL PROPERTY IN CHINA*, at xiii (Christopher Heath ed., 2005).

40. See Creer, *supra* note 37, at 213, 218.

41. *Treaties and Contracting Parties*, WORLD INTELLECTUAL PROP. ORG. [WIPO], http://www.wipo.int/treaties/en/Remarks.jsp?cnty_id=35C (last visited Nov. 10, 2010) [hereinafter *WIPO, Contracting Parties*]. The WIPO is a United Nations agency that

ization (“WTO”) in 2001,⁴² the concept of intellectual property itself may be incompatible to Chinese culture. Intellectual property’s concept of the ownership of the intangible is often regarded as incompatible with socialism’s discouragement of ownership, which still maintains a large Chinese allegiance.⁴³ Ownership itself may be an amoral concept under Eastern philosophy,⁴⁴ posing large problems for a Westernized nuanced argument against parallel importation.

This Note posits that China’s protection of copyrights and trademarks for parallel goods will continue to be limited, as demonstrated by recent judicial decisions, even with the looming possibility of international action. This analysis must be addressed through the lens of Chinese IPR obligations and enforcement in addition to the gray market. Part I explores the emergence and ambiguous illegality of the gray market. Part II assesses China’s legal obligations, both internationally and intranationally, to protect copyrights and trademarks, including potential policing of gray market goods. Part III analyzes China’s erratic enforcement of IPR as illustrated by the recent *Shanghai Unilever Co. Ltd. v. Commercial Importing and Exporting Trading Co. of Guangzhou Economic Technology Developing District, Hui Zhong Fa Shi Chu Zi* and *Michelin Group v. Tan Guoqiang and Ou Can*⁴⁵ cases, among others. Part IV proposes a possible solution in the face of a world pushing for stricter protections from the gray market.

seeks reasonable international intellectual property standards. *What is WIPO?*, WIPO, http://www.wipo.int/about-wipo/en/what_is_wipo.html (last visited Dec. 21, 2010).

42. *Member Information: China and the WTO*, WORLD TRADE ORG. [WTO], http://www.wto.org/english/thewto_e/countries_e/china_e.htm (last visited Oct. 18, 2010) [hereinafter WTO, *Member Information*]. The WTO is an international organization designed to facilitate trade negotiations and policies for member governments. *Understanding the WTO: What We Do*, WTO, http://www.wto.org/english/thewto_e/whatis_e/what_we_do_e.htm (last visited Dec. 21, 2010).

43. Creer, *supra* note 37, at 220.

44. *See id.* (explaining that ownership “is suspect to possible illegalities and disgrace”).

45. Most Chinese cases are not available in English, if they have been published at all. Few primary sources were available at the time of drafting this Note. The author relies on experts’ (practicing attorneys, scholars, and professors) recounting of the decisions. This Note features the most complete case citations possible without actual access.

I. INTO THE DEEP GRAY OCEAN: AN IN-DEPTH DISCUSSION OF THE GRAY MARKET

“Globalization . . . is as old as ambition.”⁴⁶ Even though globalization is not novel, today it possesses a new instantaneous element, mostly due to the internet’s free flowing commerce.⁴⁷ Although technology transformed humankind’s ability to reach the corners of the world, international trade would not look as it does today without a recent shift in global political status. Only two decades ago, the world was divided by ideology and matching trade barriers. With the transformation of physical barriers, “the 1990s became a watershed decade of intangible barrier removal.”⁴⁸ In the span of twelve years, the Berlin Wall fell and China joined the WTO, opening previously quartered off areas of the world for trade with other nations.⁴⁹ From these new economies, fueled by technology, the gray market exploded.

Although the gray market’s channels were carved by shifting global policy and technological advancement, industry itself is instrumental in supplying the market with product.⁵⁰ Sugden asserts that by dumping inventory to meet short-term sales goals, companies undermine their long term plans.⁵¹ Discount retailers like Marshalls and TJ Maxx then sell the same products as traditional retail outlets, at much lower prices.

Of more international concern is global pricing strategy. In order to penetrate international markets and achieve some level of sales success, companies will price goods to sell in a nation’s specific market.⁵² However, this has unintended consequences. A company may price a bicycle for \$300 in the United States, but only \$250 in Brazil and \$180 in Mexico. Businesses in the United States will buy the bicycles from Mexico at \$180, incur the shipping costs, and still be able to sell the bikes for \$250 in the United States, underselling those bikes that were priced for the American market.

Controlling distribution channels prevents underselling as well as other harms. Black market goods, which may harm consumers and brands, often intermingle with parallel imports that are out of the brand’s control.⁵³ The term gray market itself reflects this possible contamination. Gray

46. SUGDEN, *supra* note 7, at 29.

47. *Id.* at 32.

48. *Id.* at 37.

49. *Id.* at 37–38.

50. *See id.* at 40–41.

51. *Id.*

52. Espinosa, *supra* note 8.

53. For discussion of a case study on the intermingling and counterfeit baby formula, see SUGDEN, *supra* note 7, at 53.

market has many definitions including the traditionally illegal,⁵⁴ but most accurately refers to “goods diverted from a brand owners’ authorized sale channel.”⁵⁵ While industry numbers are disputed,⁵⁶ the impact of the parallel market is economically significant.

As discussed in the Introduction, in much of the world, parallel importation is not automatically illegal. In fact, it is in line with WTO free trade principles.⁵⁷ Additionally, industry continuously chooses to host production in countries that are notorious for leaks.⁵⁸ Companies’ willingness to provide this vulnerability paired with the concept of free trade creates rampant parallel importation. However, industry’s displeasure with international markets is substantial as well. Companies and their parent nations subsequently found a creative way to address this issue: intellectual property.

Intellectual property is an increasingly important barrier to the gray market, particularly trademark and copyright.⁵⁹ It may seem curious that companies attempting to crack down on parallel importation pursue intellectual property litigation. They are, after all, the same products by the very same companies, not counterfeit products. However, both trademark and copyright provide circuitous causes of action for parallel importation. By protecting creative content or a brand, companies may be able to

54. *Id.* at 4.

55. *Id.* (quoting DAVID M. HOPKINS ET AL., COUNTERFEITING EXPOSED 10 (2003)).

56. Grant Gross, *US Panel Looks at Intellectual Property Violations in China*, PC WORLD (June 15, 2010), http://www.pcworld.com/businesscenter/article/198901/us_panel_looks_at_intellectual_property_violations_in_china.html. Some have raised concern that consumers who purchase products at a fraction of the true price are not the same consumers that would buy the item at its original, elevated price. Peter Yu of Drake University recently suggested that these markets may even benefit Americans by further disseminating American democratic culture. Peter K. Yu, *Three Questions that Will Make You Rethink the U.S.-China Intellectual Property Debate*, 7 J. MARSHALL REV. INTELL. PROP. L. 412, 425 (2008) [hereinafter Yu, *Three Questions*].

57. Miller, *supra* note 7, at 24. Free trade principles refer to the WTO’s fair competition policy, which is reflected in its “system of rules dedicated to open, fair and undistorted competition.” *Basics: Principles of the Trading System*, WTO, http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact2_e.htm (last visited Nov. 8, 2010) [hereinafter WTO, *Principles*]. There is a logical tension between free trade principles and the monopoly afforded to IPR holders, but protection stimulates investment. See ROTHNIE, *supra* note 9, at 8.

58. See SUGDEN, *supra* note 7, at 102–03.

59. *Id.* at 5. It is important to note that copyright and trademark are technical and intricate concepts, and vary among nations, although reciprocity is often available internationally. This brief overview is not intended to fully assess the facets of copyright and trademark, but instead this Note assumes that one has followed proper copyright or trademark procedures and has a claim regarding infringement.

prevent the sale of the underlying good and the corresponding financial blow.

Trademarks “associate a product with a particular [unique] source,”⁶⁰ developing consumer trust and loyalty.⁶¹ Trademarks include logos, slogans, names, and even physical characteristics of the product.⁶² Companies argue that the gray market undermines its trademark, and thus destroys public trust of the brand, through dilution⁶³ and harm to goodwill.⁶⁴ Avoidance of the authorized distribution channel can create vulnerabilities from lack of warranty or quality control,⁶⁵ which may actually make the same product materially different, and thus violative of a product’s trademark.⁶⁶

Copyright in the United States and other nations is arguably more akin to traditional property rights than trademarks.⁶⁷ Copyright provides a (limited) right of distribution⁶⁸ and a right of performance,⁶⁹ among others, which are useful in two ways. First, copyright offers traditional protection to creative original works like books or software.⁷⁰ Publishers constantly struggle against the stream of books coming from external markets.⁷¹ The second way copyright can be used to protect against gray goods is slightly less obvious, and arguably weak. Companies may liti-

60. *Id.* at 242.

61. “The brand is a contract between a brand owner and its consumers.” *Id.* at 5. Since the gray market is often indistinguishable from the authorized, the stolen, and the counterfeited, weak brand control can destroy consumer confidence. *Id.* at 5–6.

62. CHINA IP PRIMER, *supra* note 20, at 9.

63. SUGDEN, *supra* note 7, at 244. Dilution can be either “tarnishment” or “blurring.” *Id.* at 244–45.

64. *See id.* at 257–59.

65. Donna K. Hintz, *Battling Gray Market Goods with Copyright Law*, 57 ALB. L. REV. 1187, 1189 (1994).

66. SUGDEN, *supra* note 7, at 260–81.

67. ROTHNIE, *supra* note 9, at 186.

68. *Basic Notions of Copyright and Related Rights*, WIPO Int’l Bureau, 6–7, WIPO/IPTK/MCT/02/INF/10 (Nov. 2001), available at http://www.wipo.int/copyright/en/activities/pdf/basic_notions.pdf; see also Tan Leng Cheo & Partners, *Copyright Law and Parallel Imports* (Aug. 28, 2001), http://www.accountlaw-tax.com.sg/Website_tlc/ws-parallel%20import.htm (a discussion of this right and its possible infringement in the United States and Singapore, with a brief discussion of Australia as well).

69. INTRODUCTION TO INTELLECTUAL PROPERTY, THEORY AND PRACTICE 155 (WIPO ed., 1997). A right of performance creates exclusivity in the rights to “perform” video games, music, and other entertainment articles.

70. ROTHNIE, *supra* note 9, at 154.

71. *See* AUSTRAL. GOV’T PRODUCTIVITY COMM’N, RESTRICTIONS ON THE PARALLEL IMPORT OF BOOKS 1.1 (2009), available at http://www.pc.gov.au/_data/assets/pdf_file/0004/90265/books.pdf.

gate the sale of their goods based on a logo or other designed or written material attached to a product rather than the product itself.⁷² However, countries are often uneasy about allowing trademark or logo protections to be employed in a manner that acts as a barrier to trade.⁷³

The first sale doctrine is often a limit to IPR and may also be called “exhaustion of rights” or simply “exhaustion.” After the first sale of a trademark protected, patented,⁷⁴ or copyrighted good, the intellectual property holder’s rights are literally exhausted, and so the importer is free from this constraint.⁷⁵ While this doctrine and its application vary tremendously worldwide, it is often acknowledged on at least a regional level.⁷⁶ Application of this concept can legally facilitate the gray market.⁷⁷

II. CHINA’S IPR LAWS AND OBLIGATIONS

Understanding China’s domestic and international IPR obligations is essential for finding possible avenues to combat gray goods. IPR has largely been imposed on China by the Western world through a complex

72. As mentioned above, this is the angle that Omega pursued in *Costco v. Omega*. See *Omega S.A. v. Costco Wholesale Corp.*, 541 F.3d 982 (9th Cir. 2008).

73. See *Quality King Distrib. Inc. v. L’Anza Research Int’l, Inc.*, 523 U.S. 135, 153 (1998).

74. This Note focuses on trademark and copyright, as parallel importation of patented goods has received much attention due to the pharmaceutical industry. For information on this topic, see Bryan A. Liang, *Fade to Black: Importation and Counterfeit Drugs* 32 AM. J. L. & MED. 279, 287–88 (2006). For a different angle, see Ben Sihanya, *Patents, Parallel Importation and Compulsory Licensing of HIV/AIDS Drugs: The Experience in Kenya*, WTO, http://www.wto.org/english/res_e/booksp_e/casestudies_e/case19_e.htm (last visited Mar. 3, 2011).

75. ROTHNIE, *supra* note 9, at 128, 237, 495.

76. For the defense as applied to trademark, see SUGDEN, *supra* note 7, at 282–84; copyright, *id.* at 218–32. As previously mentioned, the boundaries of this doctrine in the United States are unclear. The EU does not follow the first sale doctrine, but instead compensates authors for resale through the idea of “droit de suite.” The UK is waiting to see how this develops in the United States. For more on first sale internationally, see Theo Papadopoulos, *The First-Sale Doctrine in International Intellectual Property Law: Trade in Copyright Related Entertainment Products* 2 ENT. LAW 40, 50–59 (2003); see also LEAFFER, *supra* note 31, at 339 (for a discussion of droit de suite).

77. Exhaustion is multifaceted. It can be applied regionally, nationally, or even internationally. Thus, currently, one may resell intellectual property within the EU, but outside of the EU one may not resell that good without a continuation of the author’s rights. Miller, *supra* note 7, at 24, 36–37. For the purposes of this Note, which focuses on whether China meets its IP obligations in regard to the gray market, evidenced by the Chinese judiciary and options moving forward, the nuances are tangential. For in depth discussion, see *id.*

system of treaties.⁷⁸ Although China has made tremendous efforts to assimilate, it still lags behind in meeting widely accepted IPR standards.⁷⁹ As gray goods have tenebrous legal status in global treaties,⁸⁰ it is unlikely that treaties provide adequate foundation to pursue action against the gray market despite enhanced IPR standards. However, China potentially faces disputes over gray goods with large trading nations even despite consensus on parallel import legality in the Western world.

A. An Evolution

In 1903, China addressed Western IPR concerns for the first time by entering into a treaty with the United States providing foreigners with formal IPR protections.⁸¹ Additional attempts to implement IPR protections continued throughout Chinese history, but these were not as successful as intended (from the Western perspective), partly due to “wars, warlordism, famines, revolutions, and political struggles.”⁸² Efforts were further diminished in the communist post-World War II era when the Chinese Communist Party took control and nationalized commerce, effectively undermining the idea of private or exclusive rights, including expression.⁸³

China emerged from communism to join the world market in 1978, eager to participate and “put IPRs as one of the priorities on its reform agenda.”⁸⁴ In a big step toward hallowing IPR, China joined the WIPO in

78. CHEUNG, *supra* note 32, at 16.

79. For the specific example of software piracy, see Sewell Chan, *China Agrees to Intellectual Property Protections*, N.Y. TIMES, Dec. 15, 2010, at B4. For a broader look at the evolution of China’s intellectual property measures, see generally WILLIAM ALFORD, *TO STEAL A BOOK IS AN ELEGANT OFFENSE: INTELLECTUAL PROPERTY LAW IN CHINESE CIVILIZATION 1–8* (1995).

80. SUGDEN, *supra* note 7, at 298–99.

81. CHEUNG, *supra* note 32, at 32. The treaty “granted copyright, patent, and trademark protection to Americans in return for reciprocal protection to the Chinese.” Peter K. Yu, *The Second Coming of Intellectual Property Rights in China* 6 (Benjamin N. Cardozo Sch. of Law, Yeshiva Univ., Occasional Papers in Intellectual Property Law, No. 11, 2002) [hereinafter Yu, *Second Coming*], available at www.peteryu.com/2dcoming.pdf.

82. Yu, *Second Coming*, *supra* note 81, at 3. China introduced copyright law in 1910, patent law in 1912, and trademark law in 1923, all of which were reworked after Guomindang came to power in the late 1920s. *Id.* at 6–7. “Although these laws appeared on paper, they offered foreigners very limited intellectual property protection.” *Id.* at 6. This failure may be attributed to the government’s disappointment that China’s IPR protection “would not affect China’s semi-colonial status.” *Id.* at 7.

83. *Id.* at 7.

84. SHAHID ALIKHAN, *SOCIO-ECONOMIC BENEFITS OF INTELLECTUAL PROPERTY PROTECTION IN DEVELOPING COUNTRIES* 64 (2000).

1980.⁸⁵ Over the next two decades, China joined the WIPO's Paris Convention,⁸⁶ the Madrid Agreement in 1989, and the Madrid Protocol in 1995.⁸⁷ Importantly, China joined the WIPO's Berne Convention in 1992.⁸⁸ The Berne Convention allows a member country to seize illegal and intellectual property infringing products when imported or found within its borders.⁸⁹ Foreign works are protectable under the Berne Convention and do not need to be registered with the nation to be recognized,⁹⁰ enhancing a foreign owner's ability to protect goods in member nations like China. Even though Berne "lacks any enforcement mechanism,"⁹¹ the effect on China was immediate.⁹² Approximately 60% of lite-

85. WIPO, *Contracting Parties*, *supra* note 41.

86. The Paris Convention for the Protection of Industrial Property emerged in 1883 and protects industrial property like patents and trademarks. *WIPO Treaties—General Information*, WIPO, <http://www.wipo.int/treaties/en/general/> (last visited Nov. 10, 2010). China joined the convention in 1985. *Contracting Parties—China*, WIPO, http://www.wipo.int/treaties/en/ShowResults.jsp?search_what=C&country_id=38C (last visited Nov. 10, 2010).

87. The Madrid Agreement Concerning the International Agreement on Marks, Apr 14, 1891, 828 U.N.T.S. 389; Protocol Relating to the Madrid Agreement Concerning the International Registration of Marks, *adopted* June 27, 1989, WIPO Pub. No. 204(E) [hereinafter Madrid Protocol]. As of 2010, eighty-five countries are in the Madrid Protocol. Madrid Protocol, *supra*. The Madrid Protocol and Agreement are known collectively as the Madrid system, and create a multination trademark recognition system. *Summary of the Madrid Agreement Concerning the International Registration of Marks (1891) and the Protocol Relating to that Agreement (1989)*, WIPO, http://www.wipo.int/treaties/en/registration/madrid/summary_madrid.html (last visited Nov. 10, 2010).

88. PETER FENG, *INTELLECTUAL PROPERTY IN CHINA* 90 (2d ed. 2003). The Berne Convention emerged in 1886, when the world collectively addressed intellectual property rights. Berne Convention for the Protection of Literary and Artistic Works, Sept. 9, 1886, 17 U.S.C. 104, 1 B.D.I.E.L. 715 [hereinafter Berne Convention]. The Berne Convention established an administrative body which became the World Intellectual Property Organization in 1967. Convention Establishing the World Intellectual Property Organization, July 14, 1967, 21 U.S.T. 1770, 828 U.N.T.S. 3 (last amended Sept. 28, 1979). The United Nations later absorbed the organization in 1974. Agreement between the United Nations and the World Intellectual Property Organization, G.A. Res. 3346 (XXIX), U.N. Doc.A/RES/3346 (XXIX) (Dec. 17, 1974). With 164 signatories, the Berne Convention is accepted by most trading nations. *Contracting Parties—Berne Convention*, WIPO, http://www.wipo.int/treaties/en/ShowResults.jsp?treaty_id=15 (last visited Nov. 10, 2010) [hereinafter *Contracting Parties—Berne Convention*].

89. Creer, *supra* note 37, at 214.

90. CHINA IP PRIMER, *supra* note 20, at 15. However, registration is often recommended as "proof." *Id.* The Berne Convention only requires "production" of enumerated expressions, leaving "legislation in the countries of the Union to prescribe that works in general or any specified categories of works shall not be protected unless they have been fixed in some material form." Berne Convention, *supra* note 88, art. 2, ¶¶ 1–2.

91. Ugolini, *supra* note 21, at 453.

rature titles published in China in 1994 were new,⁹³ indicative of the effective incentive of IPR for innovation.

Regardless of China's improvements, the United States aggressively pursued IPR reform in China, with U.S.-Chinese disputes budding in the early 1990s.⁹⁴ This watch-dog attitude stems from the United States' tremendous interest in China's protection of IPR, as American sales of goods and services to the Chinese market was recently valued at 98.4 billion USD per year.⁹⁵ American rumblings gave way to trade tête-à-tête, punctuated by the United States' investigation and mutual sanctions,⁹⁶ with crisis averted at the last minute by the Sino-American Memorandum of Understanding on the Protection of Intellectual Property in 1992.⁹⁷ China promptly improved patent and trademark protections and upgraded its copyright provisions to satisfy the Berne Convention.⁹⁸ Over the next two years China and the United States negotiated twenty times,⁹⁹ repeating the same quarrel and, again, culminating in agreement (the Agreement Regarding Intellectual Property Rights) in February of 1995.¹⁰⁰ But tensions returned in 1996.¹⁰¹

92. ALIKHAN, *supra* note 84, at 64.

93. *Id.*

94. CHEUNG, *supra* note 32, at 32–33. The United States pursued IPR protection against China in 1991, via Section 301 of the Trade Act of 1974. *Id.* at 33. Section 301 enables the President to “investigate and impose sanctions on countries engaging in unfair trade practices that threaten the United States’ economic interests.” Yu, *Second Coming*, *supra* note 81, at 9.

95. Figure from 2009 referring to multinational American companies engaging in business with China. Victoria Slind-Flor, *Volkswagen, Krka, Pink Floyd: Intellectual Property*, BLOOMBERG BUSINESSWEEK (Dec. 16, 2010), <http://www.businessweek.com/news/2010-12-16/volkswagen-krka-pink-floyd-intellectual-property.html>. While exact numbers are difficult to obtain due to the issue's complexity, intellectual property violations cost American businesses hundreds of millions, if not billions, of dollars per year. *See generally* U.S. INT'L TRADE COMM'N [USITC], CHINA: INTELLECTUAL PROPERTY INFRINGEMENT, INDIGENOUS INNOVATION POLICIES, AND FRAMEWORKS FOR MEASURING THE EFFECTS ON THE U.S. ECONOMY, at xiv–xvi (2010), available at <http://www.usitc.gov/publications/332/pub4199.pdf>. The ability of the U.S. to address these situations is substantial, as TRIPS itself was borne of U.S. complaints regarding the loss of \$50 billion from weak IPR enforcement. CHEUNG, *supra* note 32, at 12.

96. Yu, *Second Coming*, *supra* note 81, at 9.

97. CHEUNG, *supra* note 32, at 5.

98. Yu, *Second Coming*, *supra* note 81, at 10.

99. CHEUNG, *supra* note 32, at 33.

100. Yu, *Second Coming*, *supra* note 81, at 11.

101. CHEUNG, *supra* note 32, at 33.

In response to world expectations,¹⁰² China finally joined the WTO on December 11, 2001.¹⁰³ In doing so, China agreed to follow the WTO's rules regarding trade,¹⁰⁴ as participation is hinged on its compliance.¹⁰⁵ Members of the WTO are subject to a set "scope" or "minimum standards" of IPR legal protection.¹⁰⁶ Through the WTO, China is bound to the important Agreement on Trade-Related Aspects of Intellectual Property Rights ("TRIPS"),¹⁰⁷ which structures intellectual property rights' protection with respect to trade globally.¹⁰⁸ TRIPS guidelines establish a skeleton for intellectual property as it overlaps with trade,¹⁰⁹ including incorporation of the Berne Convention's standards for copyright¹¹⁰ and the Paris Convention's scope for trademarks.¹¹¹ Of particular relevance to China, TRIPS' creation under the General Agreement on Tariffs and

102. GANEA, *supra* note 39, at xiii.

103. WTO, *Member Information*, *supra* note 42.

104. SUGDEN, *supra* note 7, at 307.

105. CHEUNG, *supra* note 32, at 12.

106. CHINA IP PRIMER, *supra* note 20, at 11. TRIPS emerged from the GATT's Uruguay Round, merging trade and intellectual property protection globally, and now exists as part of the WTO package. Beatrice Lindstrom, Note, *Scaling Back TRIPS-Plus: An Analysis of Intellectual Property Provisions in Trade Agreements and Implications for Asia and the Pacific*, 42 N.Y.U. J. INT'L L. & POL. 917, 923 (2010). TRIPS requires WTO nations to observe the Berne, Paris, Rome, International [for the Protection of Performers] Conventions, as well as the Treaty on Intellectual Property in Respect of Integrated Circuits (IPIC Treaty). *Overview: The TRIPS Agreement*, WTO, http://www.wto.org/english/tratop_e/trips_e/intel2_e.htm (last visited Dec. 22, 2010).

107. Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1C, 1869 U.N.T.S. 299 [hereinafter TRIPS Agreement].

108. *Intellectual Property: Protection and Enforcement*, WTO, http://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm7_e.htm (last visited Dec. 21, 2010).

109. Notably, it establishes "most favored nation treatment" in Article 4, meaning no special incentives for a favorite trading nation. TRIPS Agreement, *supra* note 107, art. 4; *see also* WTO, *Principles*, *supra* note 57. The WTO explains that if you "[g]rant someone a special favour (such as a lower customs duty rate for one of their products) [] you have to do the same for all other WTO members." However, this is a limited concept. *Id.* Similarly, TRIPS requires "national treatment" in Article 3, meaning that each nation must treat the parties as it would its own nationals. TRIPS Agreement, *supra* note 107, art. 3; *see also* WTO, *Principles*, *supra* note 57. "Member countries may not discriminate against nationals of one country and in favor of nationals of other countries, whether those other countries are WTO members or not." Ugolini, *supra* note 21, at 455. However, these guidelines are not to be confused with one's IP rights being the same everywhere—in fact, they may not be recognized at all outside of one's home nation, under the concept of territoriality. CHINA IP PRIMER, *supra* note 20, at 11.

110. TRIPS Agreement, *supra* note 107, art. 9.

111. *Id.* art. 15.

Trade (“GATT”) also allows developing nations “to use bargaining power and secure trade-offs in negotiating favourable terms.”¹¹² In accordance with TRIPS, China greatly improved its intellectual property protections¹¹³ and is technically in compliance with TRIPS standards.¹¹⁴

China claims that it is in compliance through its enforcement actions as well.¹¹⁵ TRIPS features obligatory enforcement provisions.¹¹⁶ It creates a duty to exercise “effective action against any act of infringement of intellectual property rights.”¹¹⁷ The breadth of these enforcement provisions runs from civil to criminal, administrative to judicial, and even to border control.¹¹⁸ TRIPS explains that administrative decisions may be subject to judicial review.¹¹⁹ However, under TRIPS there is no “obligation to put in place a judicial system for the enforcement of intellectual property rights distinct from that for the enforcement of law in general,”¹²⁰ nor does it require redistribution of resources for IPR enforcement.¹²¹ Thus, although diverse enforcement mechanisms are established in TRIPS, a nation does not have any substantive duty to fund enforcement beyond that which already exists. With no required funding obligations, improvements to enforcement risk being nominal only.

China’s legal opacity is in direct tension with its TRIPS obligations. TRIPS requires transparency for IPR enforcement as to “[l]aws and regulations, and final judicial decisions and administrative rulings of general application.”¹²² China, however, only publishes a few of its judicial deci-

112. CHEUNG, *supra* note 32, at 12–13; *see also* TRIPS Agreement, *supra* note 107, pmb1.

113. *See* Kate Colpitts Hunter, *Here There Be Pirates: How China is Meeting its IP Enforcement Obligations Under TRIPS*, 8 SAN DIEGO INT’L L.J. 523, 533–40 (2007). For details on China’s domestic intellectual property laws, *see infra* notes 157–81 and accompanying text.

114. CHINA IP PRIMER, *supra* note 20, at 15. *See infra* notes 157–81 and accompanying text.

115. Konstantina K. Athanasakou, *China IPR Enforcement: Hard as Steel or Soft as Tofu? Bringing the Question to the WTO Under TRIPS*, 39 GEO. J. INT’L L. 217, 234 (2007).

116. Lindstrom, *supra* note 106, at 924.

117. TRIPS Agreement, *supra* note 107, art. 41, ¶ 1; *see also* Tobias Bender, *How to Cope with China’s (Alleged) Failure to Implement the TRIPS Obligations on Enforcement*, 9 J. WORLD INTELL. PROP. 230, 230 (2006).

118. TRIPS Agreement, *supra* note 107, pt. 3.

119. *Id.* at art. 41, ¶ 4.

120. *Id.* at art. 41, ¶ 5.

121. *Id.*

122. *Id.* art. 63, ¶ 1.

sions and shields its internal regulations from the public.¹²³ Nonetheless, China may claim exemption through a loophole. Confidential information may be omitted if it “would impede law enforcement or otherwise be contrary to the public interest or would prejudice the legitimate commercial interests of particular enterprises, public or private.”¹²⁴ China could claim publishing judicial decisions regarding IPR violations would provide a roadmap for infringers. China’s adherence to transparency may be weak,¹²⁵ but arguably so is the actual obligation if it features such a large exemption.¹²⁶

Even with enhanced enforcement provisions, TRIPS simply does not prohibit gray goods.¹²⁷ TRIPS does provide measures for suspension of IP violative goods before they enter a market,¹²⁸ but “does not require any WTO member to establish border measures for gray market goods, whether or not the goods are being imported from a country which is part of the same customs union as the country of importation.”¹²⁹ Additionally, Article 6 of TRIPS specifically addresses, or rather dodges, the doctrine of first sale or “exhaustion.” Regarding dispute settlements, TRIPS “shall [not] be used to address the issue of the exhaustion of intellectual property rights.”¹³⁰ China, with excuses from general IP enforcement and transparency, faces no specific barrier when it comes to gray goods under TRIPS, and thus its international obligations are likely impotent in the face of the gray market. Additionally, TRIPS’ avoidance of exhaustion suggests that the treaty as a whole is not applicable to parallel importation. Without specific provisions delineating TRIPS applicability, its obligations are not strong enough to change China’s gray market.

123. For a discussion of court transparency, see MARTIN DIMITROV, *PIRACY AND THE STATE: THE POLITICS OF INTELLECTUAL PROPERTY RIGHTS IN CHINA* 106–08 (2009).

124. TRIPS Agreement, *supra* note 107, art. 63, ¶ 4.

125. Athanasakou, *supra* note 115, at 233.

126. China claims that its selected disclosures constitute important information and decisions, and thus it is in compliance. It claims that those decisions that remain undisclosed are not included under TRIPS’ transparency obligations. For more information, see *id.* Additionally, judicial decisions may be increasingly important in China, and thus transparency may be improving. DIMITROV, *supra* note 123, at 106–07.

127. Ugolini, *supra* note 21, at 461.

128. *Id.*

129. *Id.* at 465.

130. TRIPS Agreement, *supra* note 107, art. 6.

B. International Scrutiny

China faces “severe scrutiny”¹³¹ over its TRIPS and WTO Accession Protocol enforcement obligations,¹³² which could evolve into formal action to curb parallel importation despite the aforementioned ambiguities. The United States, in particular, uses the WTO as a means of influencing China. For example, the Office of the United States Trade Representative creates an annual *Report to Congress on China’s WTO Compliance*.¹³³ The report from 2004 includes a proactive plan for IPR advancement in China, establishing goals of infringement reductions and more intense enforcement.¹³⁴ China took this commission seriously, perhaps acknowledging IPR’s gravity for the first time, and attacked rampant violations at the local level, a critical source of weakness in Chinese enforcement.¹³⁵ Although there was some progress from this collaboration, China still lacked the level of control desired by Western nations.¹³⁶

China could face a WTO suit regarding parallel importation. China’s WTO status channels its bilateral disagreements through the WTO dispute settlement framework.¹³⁷ The Dispute Settlement Understanding (“DSU”) offers consultations, and if the issue remains unresolved, it then escalates into a panel review culminating in a report for the parties’ com-

131. China again agreed to pursue transparency, most favored nation status, and national treatment in the WTO Accession Protocol. Athanasakou, *supra* note 115, at 230.

132. *Id.* at 217.

133. *Archives*, USTR.GOV, <http://www.ustr.gov/about-us/press-office/reports-and-publications/archives> (last visited Dec. 16, 2010).

134. CHEUNG, *supra* note 32, at 34. The agreement set out the following pertinent goals:

- (1) significantly reduce IPR infringement levels;
- (2) take steps by the end of 2004 to increase penalties of IPR violations . . .
- (3) crackdown on IPR violators by conducting nation-wide enforcement action and increasing customs enforcement actions . . .
-
- (5) launch a national IPR education campaign.”

Id., (citing OFFICE OF THE U.S. TRADE REPRESENTATIVE (USTR), 2004 REPORT TO CONGRESS ON CHINA’S WTO COMPLIANCE 59 (2004)).

135. CHEUNG, *supra* note 32, at 34.

136. *Id.* at 35.

137. See *A Summary of the Final Act of the Uruguay Round*, WTO, http://www.wto.org/english/docs_e/legal_e/ursum_e.htm#Understanding (last visited Dec. 20, 2010).

pliance.¹³⁸ The United States has pursued the WTO dispute settlement process against China eleven times since China joined the WTO, and another four times with the European Union.¹³⁹ The last case brought by the United States against China was decided in 2010,¹⁴⁰ demonstrating commitment to this method.

Although recent utilization of the DSU indicates that the U.S. has some faith in this method, decisions have been mixed and even unsuccessful for the United States. Most notably, the United States pursued DSU solutions with China in 2007¹⁴¹ regarding China's disposal and penalty threshold for infringing goods, and IPR protection and enforcement.¹⁴² The United States claimed China dodged TRIPS by having an impracticably high eligibility threshold in implementing criminal sanctions against pirates and IP violators.¹⁴³ China defended its enforcement system, dividing the infringements between high profile criminal cases and smaller administrative cases.¹⁴⁴ Agreeing mostly with China, the WTO did find that China's auctions of contraband essentially pushed the items into the stream of commerce again.¹⁴⁵ The United States cited another claim concerning China's lack of copyright protection for banned works. The WTO found that China violated TRIPS by denying copyright protection to certain works, even though China may prohibit the works.¹⁴⁶ Although the United States did not achieve its desired outcome, its small win in

138. Parties also have the option to seek alternate settlement arrangements (arbitration, etc.) and there is an appellate process. *Id.*

139. *Disputes by Country/Territory*, WTO, http://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm (last visited Mar. 10, 2011). Compare this to India's four times and the United Kingdom's three times. *Id.*

140. This case was over car parts. *Id.*; see also Elizabeth Williamson & Tom Barkley, *U.S. Beats China in Tire Fight*, WALL ST. J., (Dec. 13, 2010), <http://online.wsj.com/article/SB10001424052748703727804576017473322868118.html>. This is not without irony, as one of the key cases in Chinese parallel importation is *Michelin* regarding tires. The United States also requested consultations three more times in 2010. *China – Measures Affecting Imports of Automobile Parts*, WTO, http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds340_e.htm (last visited May 28, 2011).

141. Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362 (Apr. 16, 2008); see also Athanasakou, *supra* note 115, at 236.

142. Athanasakou, *supra* note 115, at 218.

143. Peter K. Yu, *The US-China WTO Cases Explained*, MANAGING INTELL. PROP., Oct. 2009, available at http://www.peteryu.com/managingip_362.pdf.

144. *Id.*

145. *Id.*

146. *Id.*

this case and success in later ones suggest that it will likely pursue DSU under the WTO again.

The United States clearly takes China's treaty compliance seriously and uses WTO disputes as a way to mold China's intellectual property protection. The United States International Trade Commission continues to monitor China's intellectual property infringements and responses.¹⁴⁷ With *Costco v. Omega's* stalemate further muddying the right of first sale in the United States,¹⁴⁸ the issue of parallel importation is about to explode.¹⁴⁹ A dissatisfied United States (or any other IPR rich nation)¹⁵⁰ could pursue WTO suit, despite TRIPS' explicit exclusion of exhaustion, under the veil of pure copyright or trademark law. In fact, the U.S. declared in the 2010 Special 301 Report¹⁵¹ that it "will continue pursuing the resolution of WTO-related disputes announced in previous Special 301 reviews and determinations,"¹⁵² which includes, of course, issues with China.

Beyond the WTO, China could also face sanctions from the United States, among others.¹⁵³ The United States' 2008–2009 Chamber of

147. Gross, *supra* note 56.

148. *Supreme Court Rebuffs Costco in Copyright Challenge*, *supra* note 31.

149. For discussion of *Costco v. Omega*, see Samuel Brooks, *Note, Battling Gray Markets through Copyright Law: Omega, S.A. v. Costco Wholesale Corporation*, 2010 B.Y.U.L. REV. 19 (2010); Daniel Fisher, *Costco v. Omega is About Much More than Cheap Watches*, FORBES FULL DISCLOSURE BLOG (Nov. 5, 2010, 1:01 PM), <http://blogs.forbes.com/danielfisher/2010/11/05/costco-v-omega-is-about-much-more-than-cheap-watches>.

150. See Bender, *supra* note 117, at 240.

151. This report is prepared under the authorization of the Trade Act of 1974 §182, 19 U.S.C. 2242 (2010); see also JOHN T. MASTERSON, INTERNATIONAL TRADEMARKS AND COPYRIGHTS: ENFORCEMENT AND MANAGEMENT 18–19 (2004). The report identifies countries that "deny adequate and effective" IPR protection or "deny fair and equitable market access" to Americans with IPR of concern "priority foreign countries" including those with policies that have an "adverse impact (actual or potential)" on American goods. 19 U.S.C. § 2242 (2010). The 301 report operates under the blessing of the WTO, and the Uruguay Rounds Agreement Act even concluded that fully compliant members may rightfully be candidates for 301 reports. After IPR-threatening nations have been identified, an investigation must transpire under provided parameters. Upon the report's completion, an affirmative decision will be treated as the basis for potential retaliation. MASTERSON, *supra*, at 19–20.

152. AMBASSADOR RON KIRK, OFFICE OF THE USTR, 2010 SPECIAL 301 REPORT 16, [hereinafter USTR 2010 SPECIAL 301 REPORT], available at http://bangkok.usembassy.gov/root/pdfs/2010_special_301_report.pdf.

153. See *id.* The negative attention does not come exclusively from the United States, however. The European Union has been nearly as concerned, and Japan is afraid of the risk of "serious damage" posed by China's IPR laxness. Athanasakou, *supra* note 115, at 220–21. "TRIPS-plus" agreements, bilateral efforts to provide protection beyond TRIPS'

Commerce Report recommended that China be more vigilant on regional violative “hotspots,” allocate greater resources for IPR enforcement, launch criminal investigations focused on the wealthy and the powerful, and focus on “transborder cases” of violative goods (specific to gray goods) and “potentially dangerous products”¹⁵⁴ (arguably, unscreened tires that create peril for drivers). The Chamber of Commerce complained in this report that in spite of the Chinese government’s constant actions, very little has actually changed.¹⁵⁵ However, more aggressive steps from the United States and other countries may create significant and detrimental trade tensions.¹⁵⁶

C. Contemporary Chinese Law as is Pertinent to Parallel Importation

While China has only had a few decades to absorb Western IPR, “[m]ost Western lawyers find the [Chinese] body of [intellectual property] law comprehensive, systematic and wholly familiar.”¹⁵⁷ Mainland China’s national laws do not ban nor restrict parallel importation.¹⁵⁸ However, pursuant to worldwide pressure, China developed a substantial IPR statutory scheme which may be used to support anti-gray market claims, notably the Trademark Law of the People’s Republic of China in 1982 and the Copyright Law of the People’s Republic of China in 1990.¹⁵⁹

boundaries, have sprouted in an effort to protect trade. Lindstrom, *supra* note 106, at 919. Many TRIPS-plus “preferential trade agreements” cater specifically to industry in the stronger country, including parallel importation problems. *Id.* at 918, 985–65. However, stricter agreements may stoke trade tensions as well. *Id.* at 965.

154. U.S. CHAMBER OF COMMERCE, CHINA’S WTO IMPLEMENTATION AND OTHER ISSUES OF IMPORTANCE TO AMERICAN BUSINESS IN THE U.S.-CHINA COMMERCIAL RELATIONSHIP 28 (2008–2009), available at <http://www.uschamber.com/sites/default/files/international/asia/china/files/chinawtosinglepages.pdf>.

155. *See id.* at 8.

156. Colpitts Hunter, *supra* note 113, at 548–51.

157. CHINA IP PRIMER, *supra* note 20, at 14.

158. Angela Wang & Co., *Parallel Importation of Goods in Hong Kong and Mainland China: Part II- Mainland China*, HG.ORG (Apr. 30, 2008), <http://www.hg.org/article.asp?id=5150>. Hong Kong, although increasingly absorbent of mainland China’s policies, has its own laws regarding parallel importation. *See* Alison L. Morr, Comment, *Hong Kong’s Copyright Ordinance: How the Ban on Parallel Imports Affects the U.S. Entertainment Industry and Hong Kong’s Free Market*, 21 HASTINGS COMM. & ENT. L.J. 393, 399 (1999).

159. CHEUNG, *supra* note 32, at 66. The Copyright Law was amended in 2001. *Id.* While contemporary Chinese trademark law originated in 1982, it was most recently updated in 2001 with implementing regulations in 2002. CHINA IP PRIMER, *supra* note 20, at 15. China has been revising this law since 2008. *EU-China Workshop on Revision of*

Chinese trademark law does not expressly prohibit parallel importation.¹⁶⁰ However, there are potential protections within the statutory text for those with trademarks registered in China, via Articles 50 and 52 of the Trademark Law of the People's Republic of China. Article 52(1) explains that trademark violations include “[using a mark] that is identical or similar to another’s registered trademark on identical or similar goods, thereby misleading the public.”¹⁶¹ While it is not intuitive that one would be misled by authentic products, goods entering unauthorized channels may not go through traditional safety screening processes.¹⁶²

Article 52 details the broad array of acts that could constitute an infringement:

- (1) Use of a trademark that is the same as or similar to a registered trademark for identical or similar goods without permission of the trademark registrant;
- (2) Sale of any goods that have infringed the exclusive right to use any registered trademark;
-
- (4) Change of any trademark of a registrant without the registrant’s consent, and selling goods bearing such replaced trademark on the market; or
- (5) Other acts that have caused any other damage to another’s exclusive right to use a registered trademark.¹⁶³

the Trademark Law, Beijing (Oct. 27–29, 2010), NAT’L PEOPLE’S CONG., http://www.ipr2.org/index.php?view=article&id=1292%3Aeu-china-workshop-on-revision-of-the-trademark-law&option=com_content&Itemid=235 (last visited May 29, 2011). The patent law was also added in 1984 as part of this statutory scheme. CHEUNG, *supra* note 32, at 66. For details on specific provisions, see GANEA, *supra* note 39.

160. Paul B. Birden, *Trademark Protection in China: Trends and Directions*, 18 *LOY. L.A. INT’L & COMP. L.J.* 431, 472 (1996). Chinese law prohibits any trademark use or registration if “a reproduction, imitation, or translation of another person’s trademark not registered in China and likely to cause confusion.” (emphasis added). CHINA IP PRIMER, *supra* note 20, at 18.

161. (中华人民共和国商标法实施条例) [Implementing Provisions for the Trademark Law of the People’s Republic of China] [promulgated by the St. Council, Aug. 3, 2002, effective Sept. 23, 2002], art. 50(1).

162. For more on this, see *infra* notes 217–22 and accompanying text.

163. (中华人民共和国商标法) [Trademark Law of the People’s Republic of China] (promulgated by Standing Comm. of the Fifth Nat’l People’s Cong. Aug. 23, 1982, effective Dec. 1 2001), art. 52 [hereinafter Trademark Law (P.R.C.)]. Paragraph (1) of Article 52 has been used as the grant in the past, but (5) is curiously broad. See *Protection Against Parallel Imports in China*, VIVIEN CHAN & CO. CHINA NEWSL., July 2010,

Paragraph (4) explicitly prohibits rebranding a trademark, which is seen during parallel importation,¹⁶⁴ although commentators believe that this is only targeting “passing off” one brand as another.¹⁶⁵ While paragraphs (1) and (2) are straightforward, (5) provides a gaping opportunity to argue a nontraditional case of infringement; “damage,”¹⁶⁶ which is undefined, is sufficient to constitute infringement.¹⁶⁷ Arguably, lack of control over pricing and distribution channels may damage the interests of a trademark holder.¹⁶⁸ However, an investigation into the legislative intent of Article 52(5) has shown that the act did not include parallel importation as a type of infringement.¹⁶⁹ Without proof that it was deliberately excluded, though, 52(5) may still offer a cause of action.

Copyright protection is sometimes pursued for gray market mitigation, as trademark is often inadequate.¹⁷⁰ However, China’s copyright protections are no savior as they lack a general prohibition on importation of copyright infringing goods.¹⁷¹ Although imperfect, it does provide a right of distribution,¹⁷² which was the right used to pursue *Costco v. Omega* in the United States.¹⁷³ Another possible source of protection is §15(2) of

http://www.vclawservices.com/sources/publications/vcc_newsletter_2010_04.pdf [hereinafter *Protection Against Parallel Imports in China*].

164. PARALLEL IMPORTS IN ASIA, *supra* note 19, at 28. This simply means affixing a new trademark on a protected good. *Id.*

165. *Id.* Passing off constitutes “selling goods of another produce with one’s own trade mark without consent.” *Id.* Thus, it is essentially marketing another’s product as one’s own.

166. Other translations have used the term “prejudice.” *Id.*

167. Laurie Self & Jason Ma, *Amending China’s Trademark Law*, IP WORLD, June 2009, at 20.

168. As previously discussed, trademark owners are representing a product to be a certain quality. Bypassing quality control tests, potential commingling with counterfeit products, and a possible lack of prestige by less expensive pricing, all potentially injure the trademark holder’s business. Additionally, forcing a business to compete against itself due to underselling may damage projected profits. See Hintz, *supra* note 65, at 1189–90, for more discussion.

169. PARALLEL IMPORTS IN ASIA, *supra* note 19, at 28.

170. SUGDEN, *supra* note 7, at 213. China’s copyright legislation is based on the 1990 law, updated in 2001, and implementing regulations in 2002. FENG, *supra* note 88, at lvii–lviii. It was most recently updated in 2010. 中华人民共和国著作权法 [Copyright Law of the People’s Republic of China] (promulgated by the Standing Comm. Nat’l Cong., Feb. 26, 2010, effective Apr. 1, 2010) [hereinafter Copyright Law (P.R.C.)].

171. Between Section 46’s eleven enumerated infringing acts and Section 47’s eight, parallel importation is not touched upon. PARALLEL IMPORTS IN ASIA, *supra* note 19, at 30.

172. “The right to make the original or reproduced version of a work available to the public by sale or donation” Copyright Law (P.R.C.), art. 10, ¶ 6.

173. *Omega S.A. v. Costco Wholesale Corp.*, 541 F.3d 982, 983–84 (9th Cir. 2008).

the Provisions on the Implementation of International Copyright Treaties, § 15(2), which states that a copyright holder may prohibit importation of his or her works if the originating country fails to offer protection.¹⁷⁴ Additionally, Article 4 states that “copyright owners shall not violate the . . . laws and shall not harm the public interest. The State shall supervise and administrate the publication or dissemination of works in accordance with the law.”¹⁷⁵ The phrase “public interest” could support its application to the gray market, but a look at the phrase’s evolution suggests that the legislature likely intended to address censorship, not parallel importation.¹⁷⁶ With no statutory acknowledgement of the gray market¹⁷⁷ or exhaustion,¹⁷⁸ and broad caveats for governmental discretion, copyright protections for parallel goods have no substantial inhibition. These fragments reflect how IPR protection for parallel importation in China is often a piecemeal, industry-by-industry method.

The trademark laws provide for civil remedy. With that, compensation or damages are available¹⁷⁹ and administrative agencies may seize and destroy infringing items and tools.¹⁸⁰ Similar procedures exist for copyright infringement. Courts and administrative agencies may confiscate items and tools of infringement, with “damages of up to RMB 500,000” and the possibility of preliminary injunction.¹⁸¹

In order to implement these laws, China created administrative bureaus and substantial penalties.¹⁸² These administrative organizations help fill

174. 实施国际著作权条约的规定 [Provisions on the Implementation of International Copyright Treaties] (promulgated Sept. 25, 1992, effective Sept. 30, 1992), art. 15, ¶ 2.

175. Copyright Law (P.R.C.), art. 4.

176. 1990’s version stated, “Works that are prohibited by law from publication and dissemination shall not be protected by this Law. A copyright owner in exercising his copyright shall not violate the Constitution or the law, nor injure public interest.” Copyright Law (P.R.C.), (promulgated by the Standing Comm. of the Seventh Nat’l People’s Cong. Sept. 7, 1990, effective June 1, 1991), art. 4. This evolved into “[w]orks that are prohibited from publication or dissemination, as specified by law, shall not be protected under this Law. In exercising copyrights, the owners thereof shall not violate the Constitution or any other laws, and shall not harm the public interest.” Copyright Law (P.R.C.), (promulgated by the Standing Comm. of the Seventh Nat’l People’s Cong. Oct. 27, 2001, effective Oct. 27, 2001), art. 4.

177. Angela Wang & Co., *supra* note 158.

178. Zhao Ye & Xu Jing, *Software Resale, A Copyright Puzzle*, IP BULLETIN (2008), available at <http://www.kingandwood.com/article.aspx?id=Software-Resale-A-Copyright-Puzzle&language=en>.

179. FENG, *supra* note 88, at 300.

180. Yu, *Second Coming*, *supra* note 81, at 28.

181. *Id.*

182. Athanasakou, *supra* note 115, at 222.

the gaps created by a “fledgling court system.”¹⁸³ In the odd web spun from a changing government and fractured governance with weight held by localities, it is not terribly surprising that these administrative offices are “subordinate to the local governments on the county level.”¹⁸⁴ This fragmentation is a significant hurdle for those pursuing claims. While there are statutory copyright and trademark protections that may be applicable to the gray market, Chinese enforcement is patchy at best.

III. CHINA'S ENFORCEMENT FAILURE

Chinese IPR enforcement is lacking. Although China claims progress, 79% of counterfeit seizures at U.S. borders originate in China.¹⁸⁵ With timid and infrequent administrative fines, infringers see administrative actions as simply “a cost of doing business.”¹⁸⁶ Additionally, China imposes an extremely high financial and volume threshold before initiating criminal proceedings.¹⁸⁷ China must overcome several hurdles in order to improve enforcement of IPR, including geographical size, heterogeneous cultures, local protectionism, and decentralization.¹⁸⁸ Due to fragmentation and scale, the country faces “schizophrenic” and inconsistent local regulations.¹⁸⁹ China gestures at enforcement but has not yet adequately addressed the IPR disaster within its borders.¹⁹⁰ The judicial branch tracks the patterns of what little enforcement does exist. Copyright decisions uphold the idea of first sale while trademark decisions are patchy and inconsistent as to whether parallel importation of trademark protected goods will be seen as trademark infringement.

A. China's Recent Judicial Decisions Regarding the Gray Market

Although judicial decisions may illuminate what truly occurs within China's borders, it is important to note that China's legal system is uniquely structured. Chinese case law has no formal weight, but “exemplary” decisions do guide lower courts.¹⁹¹ Scholar Martin K. Dimitrov speculates that judicial precedent is increasingly important as China

183. GANEA, *supra* note 39, at xiv. China's judiciary was remodeled for WTO accession. BENDER, *supra* note 117, at 235.

184. GANEA, *supra* note 39, at xiv.

185. GROSS, *supra* note 56 (citing a statistic from The Business Software Alliance).

186. USTR, 2010 SPECIAL 301 REPORT, at 20–21 (2010).

187. *Id.* at 20.

188. YU, *Three Questions*, *supra* note 56, at 421.

189. *Id.* at 423.

190. This is not to say that China has done absolutely nothing. The 2010 301 Report lauds the recent Chinese crackdown on piracy. USTR, *supra* note 186, at 19.

191. FENG, *supra* note 88, at 33.

grows.¹⁹² By its nature, case law is reflective of China's true application of its statutes, a pure example of the state of enforcement. However, case law is typically not accessible.¹⁹³ This means that China essentially prevents those outside the court system from any clear view of enforcement of its statutes and international obligations, perhaps in violation of TRIPS transparency requirements.

Applicable copyright cases are scant.¹⁹⁴ However, in 2008, China decided a case regarding exhaustion and copyright within its borders. *Shanghai Shanjun Industrial Ltd. & Zheng Feng v. Shanghai Jiliang Software Technology Ltd.*¹⁹⁵ ("Zheng Feng") involved legally obtained software that was resold twice after its first sale. In a novel move, the Shanghai High People's Court applied the theory of exhaustion.¹⁹⁶ The court declared, "[o]nce the copyright work . . . [is] initially sold, or gifted to the public under the license of the copyright owner, the copyright owner will no longer enjoy the right to control further sale of the work or its copies."¹⁹⁷ This concept has also been put forth by Beijing's High People's Court,¹⁹⁸ implying consistency throughout China regarding ex-

192. DIMITROV, *supra* note 123, at 107.

193. Some cases are published in the *PRC Supreme People's Court Gazette*. *Id.* at 32.

194. At time of publication of this (cited) guide just six years ago, there were no decisions pertinent to the parallel market. PARALLEL IMPORTS IN ASIA, *supra* note 19, at 31. However, since then, it appears at least one has occurred.

195. Shanghai Shanjun Indust. Ltd. & Zheng Feng v. Shanghai Jiliang Software Tech. Ltd., (Shanghai Interm. People's Ct., May 14, 2008), http://ipr.chinacourt.org/public/detail_sfws.php?id=18193. (This source is in Chinese.) As China does not publish many of its cases, the four important cases discussed in this Note have imperfect citations. As the details of the cases have been explained by experts, this Note uses the most formal names and citations used in the experts' discussions.

196. Zhao Ye & Xu Jing, *supra* note 178.

197. *Id.*

198. Answers of the Beijing High People's Court to Certain Questions Regarding the Trial of Cases Involving Copyright Disputes, Beijing High People's Court, Jing Gao Fa Fa [1996] No. 460.

18. Is a person who has purchased the reproductions of a work distributed upon authorization of the copyright owner allowed to resell such reproductions without the consent of the copyright owner?

Answer: Once a certain volume of reproductions of a work has been distributed upon authorization of the copyright owner, the copyright owner's sale right in such volume of reproductions of the work shall be deemed to have been used up and shall be prohibited from being used any longer. With respect to reproductions of the work distributed upon authorization of the copyright owner, others' resale of such reproductions purchased by them shall be exempted from consent of the copyright owner. *Id.*

haustion. However, future cases will be necessary to see if copyright exhaustion is truly emerging as Chinese policy.

Trademark, on the other hand, appears to be growing as a method of protection against parallel importation in China. *Shanghai Unilever Co. Ltd. v. Commercial Importing and Exporting Trading Co. of Guangzhou Economic Technology Developing District, Hui Zhong Fa Shi Chu Zi ("LUX")*¹⁹⁹ was the first parallel importation case ever tried in China, to mixed results.²⁰⁰ LUX, a popular soap brand, faced parallel importation issues in mainland China. In September of 1997 and again in 1998, the plaintiff secured appropriate licensing with Unilever for use of the LUX trademark in China.²⁰¹ The plaintiff publicized its newly obtained license and filed with the State Trademark Office and General Administration of Customs.²⁰² In 1999, customs officials in Guangdong seized nearly 900 boxes of LUX soap created for the Thai market, en route to China from Thailand.²⁰³ The plaintiff brought suit against the parallel importer, claiming that it violated the company's exclusive right to use its trademark, and asked for the court to enjoin the defendant from importing and selling LUX soap, apologize publically, and reimburse the plaintiff for its losses.²⁰⁴

The parallel importer claimed that since the soap truly was authentic, there could be no violation. Additionally, the parallel importer claimed that this case was a "typical" parallel import instance, with properly trademark protected goods intended for sale in Thailand.²⁰⁵ The court rejected this argument, saying it lacked sufficient documentation of proper licensing for Thailand, much less China.²⁰⁶ It held that because the trademark was published, it violated trademark law by failing to show that the product originated from the owner of the trademark or that such importation was approved by the trademark owner.²⁰⁷ This lack of

199. *Shanghai Unilever Co. Ltd. v. Commercial Imp. & Exp. Trading Co. of Guangzhou Econ. Tech. Developing Dist., Hui Zhong Fa Shi Chu Zi* (Guangzhou Interm. People's Ct., June 1999). A more developed citation was unavailable at the time this Note was drafted.

200. Yang Jinqi, *Trademark Infringement in Parallel Import*, 62 CHINA PATENTS AND TRADEMARKS (IP QUARTERLY), no. 3, July 2000, at 31; see also PARALLEL IMPORTS IN ASIA, *supra* note 19, at 28–30.

201. Jinqi, *supra* note 200.

202. *Id.*

203. *Id.*

204. Angela Wang & Co., *supra* note 158.

205. PARALLEL IMPORTS IN ASIA, *supra* note 19, at 29.

206. *Id.*

207. Jinqi, *supra* note 200, at 32.

authorization was fatal.²⁰⁸ The court ordered three remedies: financial compensation of LUX's loss, an order to stop importation of LUX soap, and the court added that the defendant must issue a public apology in the regional newspaper.²⁰⁹

Critics of the decision were dissatisfied by the way the court dodged the question of whether parallel importation is illegal under trademark law.²¹⁰ By denying that this case was actual parallel importation, the court left ample room for maneuvering. The showmanship around the decision, namely the public apology, may indicate that the court wanted to make a grand public statement regarding Chinese enforcement.

However grand the *LUX* conclusion may have been, in 2000, the *Fahuayilin Trading Co. v. Beijing Century Hengyuan Tech. & Trading Ltd.*²¹¹ (“*An’ge*”) case deviated from its course.²¹² The court in *An’ge* addressed similar arguments as in *LUX*, that the plaintiff’s exclusive license was violated and that this constituted unfair competition. The court, instead of following the logic delineated by *LUX*, held that the defendants were just employing typical legal business operations, agreeing with the defendant’s assertion that the parallel importer followed proper procedure.²¹³ The judge explained that a contract between two parties could not be imposed upon a third party.²¹⁴ Additionally, highlighting a loophole in the statutes, the judge stressed that nothing says that the people who buy the products “must be the direct consumers or users.”²¹⁵ Essentially, Beijing’s *An’Ge* authorized like situations only with respect to wholesale purchasers, not the full scope of parallel importation.²¹⁶

The 2009 *Michelin*²¹⁷ decision created further discomfort in the treatment of trademark infringement by gray goods. The Michelin Group sued two tire dealers who were importing, without permission, real Mi-

208. See *Protection Against Parallel Imports in China*, *supra* note 163.

209. Jinqi, *supra* note 200, at 32.

210. *Id.*

211. *Fahuayilin Trading Co. v. Beijing Century Hengyuan Tech. and Trading Ltd.* (Beijing, 2002). A more complete citation was unavailable at the time this Note was drafted. See also Grace Li, *China*, PHARMACEUTICAL TRADEMARKS 2009—A GLOBAL GUIDE 7, 8 (2009), available at <http://www.worldtrademarkreview.com/issues/Article.ashx?g=4e74f91e-6b26-44f0-a03f-286269affea5>.

212. *Protection Against Parallel Imports in China*, *supra* note 163.

213. *Id.*

214. *Id.*

215. *Id.*

216. Li, *supra* note 211.

217. *Michelin Grp v. Tan Guoqiang & Ou Ca* (Changsha Interm. People’s Ct Apr. 24, 2009).

chelin tires.²¹⁸ The court held that, similarly to *LUX*, the trademark included right of importation. However, the decision turned on the fact that the Michelin trademark implied that the tires underwent official quality control testing.²¹⁹ The gray tires entered China indirectly and thus were never subject to government testing via the China Compulsory Product Certification (3C) system.²²⁰ Without this quality control, these tires were essentially different products. The court pointed out that subsequently, the tires were technically illegal.²²¹ The court was concerned that unknowing consumers would then attribute any faulty tires to Michelin, thus damaging the trademark and company's reputation.²²²

Michelin seems to build further support for trademark protection as a barrier to the gray market. However, the logic of the decision may have created a significant loophole. If a product is not directly related to safety, and does not receive mandatory tests, it is unclear if it would face a similar barrier.

In the aftermath of these three trademark cases, it appears that the Chinese judiciary is trying to show some support for the protection of international trademarks. However, the quality loophole, legality of parallel goods, lack of judicial weight, and general unavailability of published cases make application of trademark law subject to whim. Additionally, *LUX's* newspaper apology appears suspiciously cosmetic, publically announcing a rights holder's success. It is possible that China may just be diverting attention from an agenda of development and satisfying one of the world's largest economies. Paired with the apparent enforcement of exhaustion, it seems that gray goods face limited restrictions under intellectual property laws in China. Rights holders' success appears to be at the discretion of the judiciary.

B. Potential Reasons for Weak IPR Enforcement and Disincentive to Prevent Parallel Imports

Placing the above cases in context, China's relationship with IPR enforcement is tenuous for many reasons. Although development is often said to require IPR,²²³ this may not be the case in China. Experts conflict

218. *Protection Against Parallel Imports in China*, *supra* note 163; *see also* Fu Haiying, *Trademark Infringement in Parallel Importation*, CHINA LAW INSIGHT (Oct. 21 2010), <http://www.chinalawinsight.com/2010/10/articles/intellectual-property/trademark-infringement-in-parallel-importation>.

219. *Protection Against Parallel Imports in China*, *supra* note 163.

220. *Id.*

221. *Id.*

222. *Id.*

223. ALIKHAN, *supra* note 84, at 1.

on the value of such protections to developing economies. Innovation is a key element to a blossoming economy, and continued growth may rely on innovative advancements.²²⁴ Contrary to the traditional belief that there exists a “positive correlation between high protection and [research and development] . . . Overprotective terms may actually limit innovation.”²²⁵ With enormous resources and quick change, China has seen “various truncated, if not zigzag, ways of development.”²²⁶ Thus, it is not surprising that it may experience growth without traditional IPR protections. However, this is not unique to China. The United States, arguably China’s biggest critic, did not sign the Berne Convention in 1886 with the rest of the Western world,²²⁷ leaving famed authors like Charles Dickens underprotected by contemporary standards.²²⁸ Instead, the United States protected its developing economy at the detriment of international IPR holders.²²⁹ The United States officially joined the Berne convention over a century later in 1988, at that time with a ferocious and long dominant economy.²³⁰

Some argue that China will correct its IPR policies when the economy is stronger,²³¹ as the United States did. Primarily, large companies born of such a vibrant economy will require their own protections.²³² Perhaps China is already at this stage. After winning the opportunity to host the Chinese 2008 summer games, China created Olympics-specific laws, enabling criminal punishment for the unauthorized selling of products with the Olympics logo.²³³ China finally had something to lose with lax IPR protections.²³⁴ However, even with new protections, new laws were

224. Lindstrom, *supra* note 106, at 921.

225. *Id.*

226. CHEUNG, *supra* note 32, at xiii.

227. Many nations signed the original, with official implementation in 1887. *Contracting Parties—Berne Convention*, *supra* note 88.

228. CHINA IP PRIMER, *supra* note 20, at 14.

229. SUGDEN, *supra* note 7, at 307.

230. Berne Convention Implementation Act of 1988, 17 U.S.C. § 101 (1989).

231. See CHEUNG, *supra* note 32, at 20–21.

232. SUGDEN, *supra* note 7, at 307.

233. Geoffrey Fowler, *China’s Logo Crackdown*, WALL ST. J., Nov. 4, 2005, at B1; see also Doris E. Long, *Protection in China, Post-Olympics*, NAT’L L.J. (N.Y.), Aug. 18, 2008, available at http://www.jmls.edu/academics/ip_law/NLJ%20-%20Doris%20Long%20IP%20China%20Article%20Aug%2018%2008.pdf. China made “[a] significant advance in IP protection by broadening the potential administrative avenues for relief and providing a more rational basis for determining fines and penalties.” *Id.*

234. Elizabeth Ferrill, *Clearing the Swamp for Intellectual Property Harmonization: Understanding and Appreciating the Barriers to Full TRIPS Compliance for Industrialized and Non-Industrialized Countries*, 15 U. BALT. INTELL. PROP. L.J. 137, 169 (2007).

no match for China's "serious and entrenched"²³⁵ IPR problems, and Olympic products were still counterfeited, although to a lesser degree.²³⁶

Regardless of the potential governmental changes ahead, China faces tremendous cultural roadblocks. Chinese communist rule imposed a moral and philosophical understanding that, "[a]uthors thus create literary and artistic works for the welfare of the State, rather than for the purpose of generating economic benefits for themselves."²³⁷ The sin of ownership paired with the Maoist suppression of independent thought and the criticism of the "intelligentsia"²³⁸ created a notion of distrust and disrespect of the Western concept of ownership. In particular, all inventions that would be patentable by individuals in today's society belonged to the government during that era, and China recognized nominal trademark abilities and no copyright protection.²³⁹

Additionally, China's Confucian roots pose a far deeper stumbling block.²⁴⁰ "Imitation and reproduction of ideas, art and scholarship are considered tokens of honor and respect . . .," thus, ". . . protection of intellectual property rights is not a concept that first easily into a Confucian society, where copying is often and integral part of the learning process."²⁴¹ Additionally, the remains of Confucianism may have created an "entrenched tradition of regarding laws as an inefficient, arbitrary, and cumbersome instrument for governance."²⁴² The Chinese culture that met

235. Yu, *Three Questions*, *supra* note 56, at 420–21.

236. Long, *supra* note 233.

237. Yu, *Second Coming*, *supra* note 81, at 18. "Maoist" refers to Mao Zedong, who led China as the Chairman of the People's Republic of China during the communist era. See JONATHAN CLEMENTS, MAO ZEDONG 91–93 (2006). "Intelligentsia" refers to the intellectual social class. See ALFORD, *supra* note 79, at 63–65.

238. Yu, *Second Coming*, *supra* note 81, at 18–19 (discussing ALFORD, *supra* note 79, at 63–64).

239. Ferrill, *supra* note 234, at 157.

240. Confucius, the philosopher, inspired Chinese lifestyle for "more than two millennia." *Confucianism*, ENCYCLOPEDIA BRITANNICA, <http://www.britannica.com/EBchecked/topic/132104/Confucianism>, (last visited Dec. 20, 2010). For a detailed discussion as it pertains to this Note, see ALFORD, *supra* note 79, at 19–28.

241. CHEUNG, *supra* note 32, at 20.

242. Yu, *Second Coming*, *supra* note 81, at 24. "The Chinese lived by the concept of *li* (rites), rather than the concept of *fa* (law)." *Id.* Under this conceptual perspective, laws are not "a detailed, comprehensive and self-containing rule system, justifiable on ideological as well as jurisprudential grounds, with coherent principles and well defined concepts." They also can be "incomplete, incoherent, ideologically compromising, as well as broadly and vaguely termed pending further administrative and judicial experience in its implementation." *Id.* at 25 (quoting FENG, *supra* note 88, at 11). Additionally, laws are often flexible and can be ephemeral. *Id.*

the world just thirty-two years ago was bred to be intellectual property protection averse.

Another facet complicating Chinese compliance is that the Chinese economy is arguably too big,²⁴³ with too much growth, too fast.²⁴⁴ The most populous nation in the world is suddenly faced with consumerism transformative of “. . . China’s economic landscape as well as contest[ing] Chinese people’s acceptance and compliance of the global norms.”²⁴⁵ Since China joined the market societies of the world, “and the call for ‘getting rich is glorious,’” it has been forced to partner its cultural norms (discussed above) with “the thrust of the ‘get rich first’ mentality.”²⁴⁶ This economic momentum paired with traditional IPR averse values threatens Western IPR notions and protection.

Beyond the fact that China’s current stage of society may be incompatible with IPR protection, the Western world does not provide productive guidance on parallel importation. *Costco v. Omega* sent an unclear message about the United States’ position on parallel importation, shirking a declaration or disavowal of the international application of the first sale doctrine.²⁴⁷ Additionally, as Peter Yu points out, between Canal Street’s knock-off watches and College Hill laptops playing illegally downloaded mp3s, the United States arguably doesn’t prioritize IPR enforcement itself.²⁴⁸ Accordingly, IPR protection is low on the United States-China agenda, below nuclear nonproliferation and currency exchange, or “at the top of the second list.”²⁴⁹ If IPR protection itself is secondary, parallel importation is tertiary despite economic interests. Logically, the quality of the U.S.’ persuasion on this topic is likely commensurate with its prioritization.²⁵⁰

Paired with jurisdictional confusion and decentralization,²⁵¹ Confucian and communist beliefs impede IPR protection. The nation’s rapid growth

243. CHEUNG, *supra* note 32, at 21.

244. “The sheer scale of China’s growth, as her economy expands vigorously (at around 10 per cent a year), brings bad as well as good consequences.” CHINA IP PRIMER, *supra* note 20, at 14.

245. CHEUNG, *supra* note 32, at xiv.

246. *Id.* at 97.

247. *Supreme Court Rebuffs Costco in Copyright Challenge*, *supra* note 31.

248. Yu, *Three Questions*, *supra* note 56, at 416. “Even in the United States—or, for that matter, any other developed country—the protection of intellectual property rights is generally considered to be of lower priority than the resolution of such domestic problems as the prevention of murders, burglaries, robberies, thefts, arsons, assaults, and distribution of narcotics and child pornography.” *Id.*

249. *Id.* at 414–16.

250. *Id.* at 415.

251. DIMITROV, *supra* note 123, at 274.

further hinders IPR protection, but may eventually incentivize copyright and trademarks enforcement. Conflicting messages from the United States do not clarify the issue's importance. Thus, a new strategy is necessary.

IV. LOOKING FORWARD

The scarcity and inconsistent nature of China's published judicial decisions indicates that its IPR enforcement is still virtually nonexistent when compared to the number of violations. Thus, pragmatically, the problem of gray goods in China should be addressed directly. This requires a two pronged action: enhanced Chinese IPR enforcement and creation of a specific action for gray goods across borders.

There is a patchwork of suggested solutions throughout the international community. Some solutions focus on China's internal growth. Yu suggests increasing public awareness; however, there have already been significant advancements toward educating the public in China,²⁵² to little avail. Most suggestions require international involvement. Some have suggested establishing an international venue for disputes addressing intellectual property.²⁵³ This may not be successful as many countries would have to "surrender" significant sovereignty.²⁵⁴ Emerging and developing economies like China would likely not join for protectionist development reasons,²⁵⁵ undermining the purpose. Other proposed solutions include taxing imports on all intellectual property to build a fund for enforcement,²⁵⁶ but this penalizes creation and does not address cultural attitudes. Additionally, there will be difficulty convincing emerging economies to use this money for the sole purpose of IPR enforcement, when larger problems (infrastructure, energy, etc.) loom. It has also been suggested that the wealthy economies should subsidize enforcement of IPR in foreign nations,²⁵⁷ a strange bedfellow of technology transfer. This would penalize Western creation in favor of developing nations' native IPR, and would face similar problems as the previous solutions.

252. Peter K. Yu, *Conference-U.S.-China Trade: Opportunities and Challenges: Still Dissatisfied After All These Years: Intellectual Property, Post-WTO China, and the Avoidable Cycle of Futility*, 34 GA. J. INT'L & COMP. L. 143, 152 (2005).

253. Creer, *supra* note 37, at 242. Creer suggests that an international court would force emerging nations, like China, to be measured by the same standard as the rest of the world. *Id.*

254. *Id.*

255. See Lindstrom, *supra* note 106, at 921-22.

256. Creer, *supra* note 37, at 242.

257. *Id.* at 243.

Even if the nations of the world embraced such solutions, these ideas miss the essence of the problem: the gray market is not illegal as it exists without trademark or significant copyright violations, and thus needs to be targeted directly. The deliberate distance from the gray market in TRIPS arguably allows parallel importation. WTO member countries need not adopt border measures as to “goods put on the market in another country with the consent of the right holder.”²⁵⁸ Additionally, TRIPS does not require members to “devote more resources to intellectual property enforcement than other areas of law enforcement.”²⁵⁹ Without muscle from the strongest applicable treaty, China’s behavior is unlikely to change.

The logic is very simple: make parallel importation illegal globally. However, the simplicity of such an argument faces fatal hurdles. It is doubtful that the world will agree universally on all the facets of the parallel importation problem, as the United States has no clear official policy and international treaties deliberately sidestep the issue. Even if consensus is reached, it will take time to get the many trading nations of the world to literally “sign on” to such a treaty. Thus, it must be approached from a more creative angle.

Pragmatically, the United States and other nations need to be forthcoming about their concern regarding parallel products. As parallel imports mingle with black market goods in the gray market, the former are arguably less damaging than counterfeited goods, and thus may be prioritized below counterfeits. In the interim, however, major companies are losing significant sums of money. While this may just be the downside of a global economy, if the corporations of the United States, European Union, and others are so highly impacted, the parent nations must be proactive. Companies should be vigilant themselves, and proactively pursue existing enforcement mechanisms,²⁶⁰ but further international trade negotiations must transpire.

To effectively address parallel importation, the United States, Japan, Australia, and China, or ideally all of the major trading nations (with essential Chinese participation), must create a treaty, targeting gray goods, through the avenue of trademark protection. This treaty must use explicit language, stating that such violations in pursuit of the gray market, in excess of an agreed amount, will be subject to a specific and uniform punitive trademark violation/parallel import tariff. With internationally

258. Ugolini, *supra* note 21, at 461 (quoting TRIPS Agreement, *supra* note 107, art. 51, ¶ 13).

259. Yu, *Three Questions*, *supra* note 56, at 418 (citing TRIPS Agreement, *supra* note 107, art. 41, ¶ 5).

260. Long, *supra* note 233.

agreed price equalization, a limitation to right of first sale could be preserved if a nation so chooses, but governments could temper the effect of gray goods on industry. China will need to enforce this provision, seeking out violations and taxing gray goods. Unfortunately, this likely depends on China's emergence as a developed nation.

Given this time lag, reality will likely show that companies who benefit from globalization will have to accept the bad with the good. IPRs are only valid in the state in which they are granted,²⁶¹ and it is important to remember that even in the United States such rights are not absolute. These companies, who have been lobbying countries for protection and thus international action, may have to approach the market knowing the consequences and taking preventative measures that account for potential parallel importing, like dubbing films in the target language.²⁶²

CONCLUSION

While China has implemented an impressive, comprehensive written statutory system protecting intellectual property to Western standards, copyright and trademark claims from parallel importation are not gaining the traction seen in developed countries around the world. China's weak IPR enforcement pertaining to parallel imports is highlighted by its patchy judicial decisions. While it appears that the first sale doctrine exists to some degree, limiting copyright claims, trademark protection continues to compete with parallel importation. Although at least three cases have been decided on the topic, and the only clarification is that safety inspections of a product will alter the product's status. Instead, China seems to simply gesture to its international treaty obligations, but still hides behind its ability to grow its economy and cultural differences. While WTO action from the United States and European Union could follow, this process is proving impotent. Unless there is a specific pact and tariff, parallel importation will likely remain one of the negatives (from the corporate and developed nation perspective) of globalization. In order to compete globally, one must set prices to sell in each market, and the gray market is an undeniable side effect. While there is some legal protection in affluent developed countries, this issue may deepen the schism of development.

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261. Ugolini, *supra* note 21, at 453.

262. Peter K. Yu, *The Copyright Divide*, 25 CARDOZO L. REV. 331, 436 (2003).

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