

Northwestern Journal of International Law & Business

Volume 20
Issue 3 *Spring*

Spring 2000

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Recommended Citation

Daniel C.K. Chow, Enforcement against Counterfeiting in the People's Republic of China, 20 Nw. J. Int'l L. & Bus. 447 (1999-2000)

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Enforcement Against Counterfeiting in the People's Republic of China

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* Professor of Law, The Ohio State University College of Law. B.A., 1979, Yale College; J.D. 1982, Yale Law School. From 1997-99, I was on academic leave and served as in-house legal counsel for a large multinational enterprise with significant investments in China. During this period, I lived in Guangzhou, which is located along China's southeastern border near Hong Kong. My daily work consisted of all general commercial and business matters, but I began to focus a great deal of my time on intellectual property matters because of the seriousness of the trademark counterfeiting and infringement problems that we were experiencing. During this period, I helped to organize the China Anti-Counterfeiting Coalition, an ad hoc group of multinational companies with serious counterfeiting problems in China. I served as Secretary for the Coalition from 1998-99 and was involved in doing research and in drafting papers on counterfeiting for the Coalition. I also participated in actual enforcement work against counterfeiters and was present at numerous meetings with enforcement officials. I was also present at raids of suspected counterfeiters and was allowed to examine goods, documents, equipment, and the suspect premises. In some cases, I was able to sit in on interrogations of suspected counterfeiters. In other instances, I was able to have contact with suspected counterfeiters in less formal settings through the use of various subterfuges, including the use of false identities.

In the fall of 1999, after my return to full-time teaching at Ohio State, I helped to organize and coordinate an exchange on enforcement against counterfeiting under the auspices of the United States Department of State. The first phase of this exchange occurred from November 6-17, 1999 and involved a delegation of US legal experts, including two federal judges, a federal prosecutor, and a special agent of the FBI. This exchange involved meetings in the People's Republic of China ("PRC") with high level Chinese enforcement officials at which the Chinese asked a number of questions and engaged the delegation in numerous exchanges. I also helped to organize and coordinate the second phase of this exchange, which involved a visit by a delegation of Chinese government officials to the United States from May 6-14, 2000. I accompanied the Chinese delegation on visits to various federal agencies, trade associations, and US headquarters of several multinational companies with substantial China businesses. These visits resulted in frank and detailed discussions of issues related to enforcement against counterfeiting. Many of the issues raised in these exchanges are reflected in this Article and it is hoped that this Article can serve as a basis for further exchanges and dialogue on these issues. Although I have served in a number of different roles in China in the past several years, the views expressed here do not represent

I. INTRODUCTION

Trademark and product counterfeiting¹ has now become a major concern for many brand owners doing business in the People's Republic of China.² Estimates by some multinational companies are that counterfeiting in China results in losses in the billions, if not tens of billions, of dollars each year to their businesses, and causes serious and possibly irreparable harm to the goodwill and reputation of their brands.³ Chinese brand owners face counterfeiting problems that are as severe, if not more so, than those plaguing multinational companies.⁴ The recent dramatic increase in exports of counterfeit goods produced in China to countries abroad now raises the concern for some companies that China has become a platform for a global counterfeiting problem.⁵ Although China already has the most significant

those of any organization, entity, or group with which I was affiliated. These views are my own.

Thanks to Dean Gregory H. Williams for his support on this project and my endeavors concerning China. Thanks also to Mr. Seung Baik, Editor-in-Chief, of the Northwestern Journal of International Law & Business for asking me to submit this Article and to Ms. Michele Kunitz, Executive Editor, for her helpful comments and editing. Thanks also to Mr. Craig Bryson for his research assistance.

¹The focus of this Article is on trademark counterfeiting, which should be distinguished from other types of intellectual property violations. For further discussion of the differences between counterfeiting and copyright piracy, see *infra* text accompanying notes 7-12; see also Daniel C.K. Chow, *Counterfeiting in the People's Republic of China*, 78 WASH. U. L.Q. 1, 8-10 (2000).

²According to one source, "[f]oreign companies are being eaten alive by counterfeiters in China." *Stuck in the Middle*, BUS. CHINA, Dec. 6, 1999, available in 1999 WL 2498141.

³There is no scientific method to measure the size of the counterfeiting problem in China. Counterfeiters operate their illegal trade in underground factories and through criminal organizations. As a result, only partial information is available and some extrapolations must be made, but based on available information, the size of China's consumer economy (\$352.7 billion in annual sales), the percentage of total sales reported to be lost from counterfeiting from industry groups (15-20% for some brands), total losses suffered to counterfeiting by US companies worldwide (\$200 billion), and China's role as a leading source of counterfeit products—it is reasonable to assume that the total value of counterfeit products that are available in or originating from China are in the billions or even tens of billions of dollars per year. See Chow, *supra* note 1, at 11-12; see also David Murphy, *Fake Goods at Critical Levels in China*, BUS. TIMES, June 21, 1999, at 5. Estimated annual losses for some well-known companies doing business in China include \$150 million (Procter & Gamble), \$70 million (Nike), and \$24 million (Unilever). See *id.*

⁴See Chow, *supra* note 1, at 13; see also Joseph T. Simone, *Countering Counterfeiters*, CHINA BUS. REV. Jan.1, 1999, at 12, available in 1999 WL 11878204.

⁵See Chow, *supra* note 1, at 10-11; see also *Defenders of the Mark: Companies Battle the Global Trade in Counterfeit and Stolen Goods*, 9 CORP. LEGAL TIMES 97 (1999) (noting that counterfeits made in China are found in more than 100 countries around the world (statement by Harley I. Lewin, intellectual property law expert)).

counterfeiting problem in world history, counterfeiting seems to be still on the rise.⁶

As used in this Article, counterfeiting refers to the unauthorized act by one party of passing off exact duplicates of products with trademarks owned by another party.⁷ Counterfeiting should be distinguished from copyright piracy, which refers to the unauthorized copying of the content of a fixed medium of expression, such as films, musical recordings, and com-

⁶ See, e.g., *Stuck in the Middle*, *supra* note 2, at 1 (China's intellectual property infringement problems already "exceed[s] the worst fears of most foreign investors," but "the [counterfeiting] situation seems to be getting worse, not better."); *China: Crackdown on Fakes Intensifies*, CHINA DAILY, Mar. 16, 1998, available in 1998 WL 7594529 ("In spite of the legislative amplification, the fake-making business seems to still be booming and has even been upgraded.").

⁷ China does not have a law that specifically defines counterfeiting. Rather, counterfeiting is subsumed within the more general wrong of trademark infringement. Article 38, PRC Trademark Law provides:

Any of the following acts shall be an infringement of the exclusive right to use a registered trademark:

- (1) To use a trademark which is identical or similar to the registered trademark in respect of the same or similar goods without the authorisation of the proprietor of the registered trademark;
- (2) To sell goods while knowing that a fake trademark is being passed off as a registered trademark.
- (3) To forge or make, without authorisation, representations of the registered trademark of another person, or to sell forged representations or representations made without authorisation of the registered trademark.
- (4) To cause, in other respects, prejudice to the exclusive right to use the registered trademark of another person.

TRADEMARK LAW OF THE PEOPLE'S REPUBLIC OF CHINA (REVISED) (Zhonghua Renmin Gonghe Guo Shangbiao Fa (Xiuzhen), Di Sanshiba Tiao) (adopted at the 24th Session of the Standing Committee of the 5th National People's Congress on August 23, 1982, revised by the 30th Session of the Standing Committee of the 7th National People's Congress on February 22, 1993, and effective July 1, 1993) art. 38 (PRC) [hereinafter "PRC Trademark Law"]. The catch-all provision referring to causing prejudice to the exclusive trademark right of another person contained in Article 38(4) above is explained by Article 41 of the Trademark Law Implementing Regulations, which provides:

Any of the following acts will constitute an infringement of the exclusive right to use a registered trademark as referred to in item (4) of Article 38 of the Trademark Law:

- (1) dealing in goods which were known or ought to have known to have infringed the exclusive right of another person to use a registered trademark;
- (2) using, as a product name or label, written script or a design which is identical or similar to the registered trademark of another person who uses it on the same or similar commodities, with the similarity being sufficient to cause confusion;
- (3) intentionally providing storage, transport, postage or harbouring offenders in order to facilitate the infringement of the exclusive right of another person to use a registered trademark.

TRADEMARK LAW IMPLEMENTING RULES (Zhonghua Renmin Gonghe Guo Shangbiao Fa Shishi Xize, Di Shihiyi Tiao) (promulgated May 12, 1995) art. 41 [hereinafter "PRC Trademark Law Implementing Rules"].

puter software.⁸ In the recent past, a great deal of attention has been focused on China's production of pirated compact and videodisks, videotapes, and cassette tapes.⁹ Most of these violations involve copyright piracy in which no effort is made by the infringer to pass off the pirated product as produced or distributed by the original copyright owners.¹⁰ By contrast, counterfeiting involves an attempt to pass off the counterfeit as an authentic product by creating a fake product that appears in all respects identical to the authentic product, including using the same trade dress and including the name and address of the manufacturer on the product.¹¹ Issues of prod-

⁸Liability for copyright infringement is set forth in Article 45 of the PRC Copyright Law. COPYRIGHT LAW OF THE PEOPLE'S REPUBLIC OF CHINA (Zhonghua Renmin Gonghe Guo Zhuduo Quanfa) (adopted at the 15th Session of the Standing Committee of the 7th National People's Congress on September 7, 1991 and effective June 1, 1991) art. 45 (PRC) [hereinafter "PRC Copyright Law"].

⁹Disputes between the United States and China over copyright protection in the early 1990s almost led to a trade war. See Robert B. Frost, Jr. *Intellectual Property Rights Disputes in the 1990s Between the Republic of China and the United States*, 4 TUL J. INT'L & COMP. L. 119 (1995). For a review of the copyright negotiations between the US and China, see id; see also, Marcus W. Brauchli, *Shenfei Stake Stirs Thorny U.S. Issue that Foreign Firms May Abet Theft*, ASIAN WALL ST. J., Jan. 5, 1995, available in 1995 WL-WSJA 2131402; Joseph T. Simone, *Damming the Counterfeit Tide: New Laws Promise Foreign Trademark Owners Much-Needed Protection*, CHINA BUS. REV., Nov. 1, 1993, available in 1993 WL 10862142. The dispute now appears to be resolved because of China's nationwide crackdown on copyright piracy. See, e.g., Duncan Hughes, *Copyright Pirates Face Big Penalties as Laws Get Tough*, S. CHINA MORNING POST, May 27, 1995, available in 1995 WL 7528438.

¹⁰Consumers who buy pirated copyrighted goods, such as computer software, compact disks, or videotapes want the content of the product. So long as the content of the product has been duplicated at a high level of quality (easily done with modern technology), these consumers generally are not concerned whether the product is actually manufactured by the copyright owner. Indeed, many consumers in China believe that inexpensive pirated copyrighted goods provide an important benefit to the consumer because so many consumers would be unable to buy the more expensive genuine product. Many of these consumers are also fully aware that they are buying a pirated product. In the case of counterfeit goods, however, many consumers are deceived by what they purchase and fewer consumers believe that such counterfeit goods serve the interests of consumers. At the same time, there does appear to be a less affluent segment of the Chinese population that will knowingly purchase counterfeit goods. These consumers believe that many counterfeit goods are of at least equal quality to local brands but carry a prestige that local brands lack. Also some consumers who knowingly purchase counterfeit goods will adjust their usage of the goods accordingly. For example, a consumer will use a counterfeit detergent to wash work clothes but not bed sheets and a counterfeit soap to wash his hands but not his face.

¹¹Counterfeiting should also be distinguished from other less serious forms of trademark infringement, which involve partially copying the trademark and the package design of another party. In most cases, illegal and unlicensed underground factories manufacture counterfeits, whereas other types of less serious trademark infringements are committed by lawful and licensed enterprises. Trademark infringement in China is also a serious problem but is generally viewed as less harmful by brand owners. Moreover, counterfeiting on any scale is criminal activity, whereas trademark infringement is generally an administrative or civil matter.

uct quality are not generally at stake in copyright piracy cases because modern technology allows for copies that are in many cases identical in quality to that of the original. Product quality and consumer rights can be an issue where counterfeit products are involved because the counterfeiter often seeks to pass off a product of lesser quality in the guise of a well-known brand name.¹²

Many visitors to China often are surprised by the plentiful supply of counterfeit goods in obvious and open display in China's many street markets, wholesale markets, and small and medium sized retail establishments. For example, in Silk Alley, located next to the United States Embassy in Beijing, street hawkers do a brisk business in selling counterfeits of many famous trademarks, including some American brands, to passers-by in plain view of the US Embassy. In downtown Beijing, a large wholesale market sells counterfeit goods right in the heart of the city, located in a densely populated area next to hotels, businesses, and residential sections and the offices of numerous government enforcement authorities. All over China, this scenario seems to be repeated in both large urban areas and in the smaller (by China's standards) mid-sized cities and also in China's many vast rural areas.

This situation causes significant frustration and consternation for many foreign and local brand owners, many of which are struggling to turn a profit in an increasingly competitive and difficult business environment.¹³ Some foreign and local brand owners in China now spend several hundred thousand to several million dollars annually on enforcing their rights against counterfeiters.¹⁴ Brand owners have no difficulty in identifying and locating manufacturers and sellers or in bringing enforcement actions.¹⁵

¹²For a discussion of consumer issues associated with counterfeiting, see Chow, *supra* note 1, at 12-13.

¹³Some multinational investors have learned some sobering lessons since the almost euphoric days of the 1980s and have had to scale back expectations and to rethink their China strategies for the long-term. A common expression used by the Chinese to describe relations between a foreign investor and its local Chinese partner is "same bed, different dreams." Many local partners are state-owned enterprises run by life-long Communist Party members who have little understanding of free market principles. On the other side, some foreign investors may be prone to cultural bias and feelings of superiority. Differences in management styles and management goals also create conflicts. For a general discussion of lessons learned, see Daniel C.K. Chow, *The Limited Partnership Joint Venture Model in the People's Republic of China*, 30 *LAW & POL'Y INT'L BUS.* 1 (1998); Daniel C.K. Chow, *Reorganization and Conversion of a Joint Venture into a Wholly-Foreign Owned Enterprise in the People's Republic of China*, 73 *TUL. L. REV.* 619 (1998). For a penetrating analysis of one of the earliest joint ventures in China and its many travails, see JIM MANN, *BEIJING JEEP: A CASE STUDY OF WESTERN BUSINESS IN CHINA* (1997).

¹⁴This observation is based upon the author's numerous discussions with multinational companies doing business in China and based upon the author's own experience.

¹⁵In some instances, the local joint venture partner or others within the foreign investor's organizations (including distributors or suppliers) in China may be involved directly or indi-

Rather, as alluded to above, the targets can be so numerous that brand owners, given budget constraints, have to be selective in how many enforcement actions they seek to bring in any period.¹⁶ There is no lack of raids and seizures of counterfeit goods, but brand owners are routinely frustrated by the lack of resulting penalties and sanctions that effectively punish counterfeiters and create deterrence against recidivism.¹⁷ In addition, brand owners have been lobbying for several years now for increased criminal sanctions in the form of convictions and imprisonment only to find that achieving criminal sanctions continues to be rare and difficult.¹⁸ In China today, it is simply the case that counterfeiting has become a very lucrative trade for some, and that many counterfeiters simply do not fear the consequences of being caught and punished.¹⁹ In many instances, counterfeiters may view law enforcement as a cost of doing business.²⁰

The reasons for the lack of effective enforcement and deterrence are complex and varied and a comprehensive discussion of all of these reasons is beyond the scope of this Article.²¹ Rather, this Article focuses on issues relating to the interpretation and enforcement of China's current laws against counterfeiting, and on several systemic features of China's legal and administrative system relating to enforcement of intellectual property rights. In recent years, China has enacted a number of laws designed to protect intellectual property rights of all kinds, in part due to pressure from the United States.²² Although China's current set of laws still appears to con-

rectly in counterfeiting. This creates issues of internal corporate security for the foreign investor and lie outside the scope of this Article. However, based upon the author's experience, involvement of persons within the foreign investor's own organization in counterfeiting is not an uncommon occurrence in China.

¹⁶Many brand owners find that fees and expenses for raid actions can quickly mount up, without any significant results. See Anupa P. Mathew, *News From the United Arab Emirates: Electrical Industry Fights Counterfeiting*, GULF NEWS, Dec. 18, 1999, at 1.

¹⁷See *infra* text accompanying notes 44-46.

¹⁸See *infra* text accompanying note 75.

¹⁹For a discussion of penalties and sanctions, see *infra* text accompanying notes 41-52 & 63-75.

²⁰For a review of the average fines and penalties imposed in counterfeiting cases, see *infra* text accompanying notes 44-45.

²¹A major problem not examined in this Article is local protectionism, which refers in this context to the protection afforded to counterfeiters by local government enforcement entities. Local protectionism is more of a social and political problem, as opposed to a problem of interpretation and enforcement of laws. For a detailed examination of local protectionism and its role in the growth of counterfeiting, see Chow, *supra* note 1, at 21-25.

²²See, *supra* note 7, for a list of intellectual property rights protection laws. For additional laws, see also ADMINISTRATION OF TRADEMARKS IN FOREIGN TRADE PROVISIONS (Duiwai Maoyi Jinji Heduo Ji Gongshang Xingzheng Guanli Ju Guanyu Duiwai Maoyi Zhong Shangbiao Guangli De Guiding) (promulgated by the Ministry of Foreign Trade and Economic Co-operation ("MOFTEC") and the State Administration for Industry and Commerce ("SAIC") on May 12, 1995 and effective August 1, 1995) (PRC); RECOGNITION AND ADMINISTRATION OF WELL-KNOWN TRADEMARKS TENTATIVE PROVISIONS (Chiming Shang-

tain some gaps, the central issue today is not with a lack of adequate legal weapons but with the interpretation, application, and enforcement of the law through the use of a massive bureaucratic government and regulatory structure in place before China's current reforms were launched. This Article addresses these issues.

Although the discussion in this Article is limited to counterfeiting in China, many of the issues discussed are endemic to the Chinese legal system as a whole, and apply also to other intellectual property rights, such as copyright piracy and patent infringements.²³ Moreover, many of the themes raised in this Article also illuminate the current state of the nascent Chinese legal system as a whole and how its capacity is tested as it continues the struggle to keep pace with China's many economic reforms and accompanying social changes.²⁴ Part I of this Article begins with a review of the enforcement system against counterfeiting in China and examines the legal problems that prevent more effective enforcement in China.²⁵ After reviewing China's current issues, this Part will then analyze and suggest different ways of viewing and handling some of the same issues, based in some measure on United States law and practice.²⁶ No attempt is made here to criticize the Chinese government for its current efforts in enforcing trademark rights against counterfeiting. Rather, this Article is intended to present China with some alternative ways of viewing and handling some of these difficult issues and to serve as a basis for exchange and dialogue between the United States and China. Part III concludes with some observations about the future of counterfeiting in China.

biao Rending He Guanli Zhanxing Guiding) (promulgated by SAIC on August 14, 1996 and immediately effective) (PRC); COMPUTER SOFTWARE PROTECTION RULES (Jisuanji Ranjian Baohu Tiaoli) (passed by the State Council on May 24, 1991, promulgated June 4, 1991, and effective October 10, 1991) (PRC); PATENT LAW OF THE PEOPLE'S REPUBLIC OF CHINA (REVISED) (Zhonghua Renmin Gonghe Guo Zhuanli Fa (Xiuzheng)) (amended at the 4th Session of the Standing Committee for the 6th National People's Congress on March 12, 1984, and also amended by decision adopted at the 27th Session of the Standing Committee of the 7th National People's Congress on September 4, 1992) (PRC) [hereinafter "PRC Patent Law"]; IMPLEMENTING REGULATIONS OF THE PATENT LAW OF THE PEOPLE'S REPUBLIC OF CHINA (Zhonghua Renmin Gonghe Guo Zhuanli Fa Shishi Xize) (adopted by the State Council on December 12, 1992 and promulgated by the Patent Office of the People's Republic of China on December 21, 1992) (PRC) [hereinafter "PRC Patent Law Implementing Rules"].

²³ Counterfeiting is generally viewed by brand owners as the most serious of their intellectual property problems. See *Stuck in the Middle*, *supra* note 2, at 1.

²⁴ For a general review of China's economic reforms and China's attempts to adjust and keep pace, see Daniel C.K. Chow, *An Analysis of the Political Economy of China's Enterprise Conglomerates: A Study of the Reform of the Electric Power Industry in China*, 28 LAW & POL'Y INT'L BUS. 383 (1997).

²⁵ See *infra* text accompanying notes 36-56, 63-75 & 93-95.

²⁶ See *infra* text accompanying notes 57-62, 76-92.

II. THE PRC ENFORCEMENT SYSTEM

Because China's enforcement system places a heavy emphasis on administrative enforcement, the discussion below begins with a review of this area.²⁷ Criminal and civil enforcement have not played significant roles in enforcement against counterfeiting, but there may be more activity in these areas in the future as brand owners press for change. The following discussion can be divided into three main areas: administrative, criminal, and civil enforcement.

A. ADMINISTRATIVE ENFORCEMENT

Administrative enforcement power over counterfeiting in China is currently not centralized in a single entity, but is divided among a number of different administrative entities. The Administration of Industry and Commerce ("AIC") has primary jurisdiction over trademarks, including matters of registration, administration and enforcement.²⁸ Another administrative body, the Technical Supervision Bureau ("TSB") has authority over product quality and consumer protection issues, and as a result, also has enforcement power over counterfeit goods.²⁹ In some instances, brand owners can also seek enforcement from the Patent Administration Office, based upon its jurisdiction over patent rights,³⁰ and from the General Administration of Customs, based upon its jurisdiction over China's national borders, where imports or exports of counterfeit products are involved.³¹

China's numerous enforcement options can be traced to certain features of the pre-reform government regulatory structure still in place today. China divides the economy into vertical sectors and assigns complete authority over a sector to an administrative body. Thus, the AIC has full authority within its sector over trademarks, among other industrial and commercial activities, including the power of enforcement for breach of

²⁷In this context, administrative enforcement refers to actions by a government regulatory body that has supervisory and administrative power over an economic sector. This should be contrasted with the work of the police, prosecutors, and courts, which do not administer and regulate economic sectors.

²⁸See, PRC Trademark Law, art. 1, 2 & 38; PRC Trademark Law Implementing Rules, art. 42.

²⁹See PRODUCT QUALITY LAW OF THE PEOPLE'S REPUBLIC OF CHINA (Zhonghua Renmin Gonghe Guo Chanpin Zhilinao Fa) (promulgated Feb. 22, 1993 and effective Sept. 1, 1993) art. 12 (PRC) [hereinafter "PRC Product Quality Law"]; PROTECTION OF THE RIGHTS AND INTERESTS OF CONSUMERS LAW OF THE PEOPLE'S REPUBLIC OF CHINA (Zonghua Renmin Gonghe Guo Xiaofeizhe Quanyi Baohu Fa) (promulgated Oct. 31, 1993 and effective Jan. 1, 1994) art. 34 (PRC) [hereinafter "PRC Consumers Law"].

³⁰See PRC Patent Law, art. 60; PRC Patent Law Implementing Regulations, art. 77.

³¹See CUSTOMS LAW OF THE PEOPLE'S REPUBLIC OF CHINA (Zonghua Renmin Gonghe Guo Haiguan Fa) (adopted by the 19th Session of the Standing Committee of the 6th National People's Congress on Jan. 22, 1987 and effective July 1, 1987) Arts. 3 & 4 [hereinafter "PRC Customs Law"].

trademark rights.³² The TSB has authority over all areas concerning product quality and consumer rights and has the power to deal with counterfeits because many counterfeit products are of inferior quality and implicate consumer fraud, health, and safety.³³ The same holds for the Patent Administration Office and the General Customs Administration of Customs—these entities also have authority over counterfeiting that can be traced to their full authority over the vertical economic sectors that they regulate and administer.³⁴

Counterfeiting often cuts across several vertical sectors, and as a result, a number of parallel enforcement actions through different enforcement entities can arise. Although this system of parallel enforcement entities raises some long-term issues of efficiency for China, many brand owners actually prefer to have the current system involving a number of parallel and competing enforcement authorities because of the many options that it offers.³⁵

1. Raids and Seizures

An administrative enforcement action normally involves a raid conducted by enforcement officials of the counterfeiter's premises and a seizure of counterfeit goods, labeling, packaging, and equipment.³⁶ Administrative entities have authority to initiate enforcement actions on their own, but such actions require the identification and location of a target counterfeiter. Because many enforcement entities lack the personnel and resources to conduct on-going investigations, the number of actions initiated by enforcement authorities is limited and makes up only part of their overall enforcement activities. Many brand owners hire investigative agencies to track down and locate counterfeiters and then bring such information in the form of a complaint before administrative enforcement authorities.³⁷

³² See PRC Trademark Law, art. 38.

³³ See PRC Product Quality Law, art 12; PRC Consumers Law, art. 34.

³⁴ See PRC Patent Law; PRC Customs Law, arts. 3 & 4.

³⁵ For the long term, a centralized agency administering a national trademark law and practice is probably a better use of China's resources.

³⁶ For powers of the AICs to confiscate and destroy materials used in connection with counterfeiting, see PRC Trademark Law Implementing Rules, art. 43.

³⁷ These investigations are conducted by professional investigative agencies hired by brand owners. Most companies are reluctant to do this type of work themselves because the work can be dangerous and there are reports of instances of counterfeiters assaulting undercover operatives whose identities are discovered. A thriving and lucrative industry in intellectual property investigations now exists in Mainland China and in Hong Kong. The costs of a typical investigation, depending on its degree of difficulty, can range from \$1000-\$5000. Fees for arranging and conducting an enforcement action through the authorities add an additional \$2000-\$3000. If the brand owner also engages legal counsel for the raid, this will add another \$2,000-\$3,000. In total, a typical raid action will cost between \$8,000-\$10,000. Given that some brand owners can conduct as many as two or three raids each week, the costs quickly mount. To cut some costs, some brand owners have attempted to internalize some of this work by hiring in-house counsel, but the nature of the work, and its

Once the brand owner has located the counterfeiter, the brand owner will then file a complaint before the administrative authorities at the appropriate time.³⁸ Timing is important; most brand owners seek to catch manufacturers of counterfeit goods in the act of manufacturing the product or sellers of counterfeit goods with stocks of counterfeits on the premises in order to facilitate criminal and administrative prosecutions. As a result, these investigations can be time consuming and dangerous since the most effective means of investigation involves introducing an operative who assumes a false identity and infiltrates the counterfeiter's inner circles and operations.

Once the brand owner decides to act and file a complaint, the authorities often act swiftly.³⁹ In many instances, within minutes of the filing of a complaint by the brand owner, administrative authorities will organize a raid and seizure action.⁴⁰ The brand owner and its investigators who know the location of the counterfeiter will often then accompany the authorities on the raid action. Once at the premises, the authorities will demand entry, seize counterfeit goods, related paraphernalia, equipment, and in some instances, automobiles, trucks, and motorcycles found on the premises. Raids are often dramatic, cause confusion and panic among counterfeiters on the premises, and occasionally involve violence.

2. *Sanctions and Penalties*

While many brand owners are impressed by the ease and speed with which they can obtain raid actions, most are dissatisfied with the resulting sanctions and penalties imposed upon those determined by authorities to have violated relevant laws. After the raids, the authorities will review all available evidence and decide whether the brand owner's rights have been violated.⁴¹ Under the *Trademark Law Implementing Rules*, AICs have authority to impose maximum fines of up to 50% of the counterfeiter's ille-

accompanying risks to security and personal safety, require extensive outside help even when these cases are managed by in-house legal counsel.

³⁸The right of a trademark owner to file a complaint with the AICs is set forth in article 42 of the PRC Trademark Law Implementing Rules. See PRC Trademark Law Implementing Rules, art. 42.

³⁹The description in this paragraph is based upon the author's own experiences as in-house legal counsel for a multinational enterprise in China from 1997-99.

⁴⁰In many instances, the brand owner and the authorities have already gotten to know each other during a pre-raid dinner and karaoke party held the night before. Entertaining enforcement officials has become a regular (and some say expected) practice among brand owners. See David H. Freedman, *Chinese Copycats Are Leaving International Brands Fit to be Tied*, FORBES MAG., Apr. 5, 1999, at 51.

⁴¹Where the TSB is involved, it will decide whether the counterfeit goods are of an inferior quality or violate the rights of consumers. See PRC Product Quality Law, art. 12; PRC Consumers Law, art. 34.

gal turnover and up to 5 times the profit earned by the counterfeiter.⁴² AICs also have authority to order compensation measured either by the counterfeiter's profits or by the damages suffered by the brand owner.⁴³ A review of recent statistics indicates, however, that implementation of these provisions has resulted in fines and compensation awards that fail to deter counterfeiters.

Of the 14,736 cases enforced by the AIC at all levels nationwide in 1998, the total compensation awarded by AICs to brand owners was about \$600,000, or about \$41 dollars per case.⁴⁴ Total fines assessed against counterfeiters were about \$10.4 million, or about \$699 per case.⁴⁵ At these levels, most counterfeiters simply view these penalties as a minor annoyance and the cost of doing business in a lucrative trade.⁴⁶

What about products, equipment and other materials seized? The confiscation of materials can constitute substantial losses to the counterfeiter, but most authorities will sell these materials at an auction where the counterfeiter, his associates, or others seeking to enter the illegal trade may be the purchaser.⁴⁷ Where possible, authorities will erase the offending trademark from the counterfeit products before selling the products at a public auction.⁴⁸ Where equipment has been seized and can be used for lawful purposes, authorities will also sell equipment at a public auction.⁴⁹ Only in those relatively unusual instances where the trademark cannot be eliminated without destroying the products and where the equipment cannot be used for lawful purposes will authorities destroy all materials seized,⁵⁰ usually at the expense of the brand owner.⁵¹ Some brand owners will feel compelled

⁴² See PRC Trademark Law Implementing Rules, art. 43.

⁴³ See PRC Trademark Law, art. 39.

⁴⁴ See STATE ADMINISTRATION OF INDUSTRY AND COMMERCE 1998 ANNUAL REPORT at 15 (PRC) [hereinafter "SAIC 1998 ANNUAL REPORT"].

⁴⁵ See *id.* Similar statistics exist for the previous year. In 1997, AICs at all levels nationwide brought 15,321 counterfeiting and trademark infringement actions. See STATE ADMINISTRATION OF INDUSTRY AND COMMERCE 1997 ANNUAL REPORT at 11 (PRC) [hereinafter "SAIC 1997 ANNUAL REPORT"]. Total fines assessed were \$10.4 million or \$679 per case. See *id.* Total compensation paid to brand owners was approximately \$614,000 or \$40 per case. See *id.*

⁴⁶ For the size of the trade in counterfeit goods, see Murphy, *supra* note 3.

⁴⁷ In many cases, the auction price for used equipment and counterfeit goods is less than the replacement costs for these materials.

⁴⁸ See PRC Trademark Law Implementing Rules, art. 43 (iii).

⁴⁹ See PRC Trademark Law Implementing Rules, art. 43(iv). This provision only establishes the power of authorities to confiscate equipment and is not sufficiently detailed to describe the practice of how authorities sell confiscated equipment through auction—this observation is based upon the author's own experience.

⁵⁰ See PRC Trademark Law Implementing Rules, art. 43(v).

⁵¹ Many authorities ask the brand owner to pay for the costs of renting a space and for the materials needed to destroy counterfeit goods. The reasons given are usually that the authority lacks the resources to pay these costs.

to purchase seized materials at public auctions in order to prevent these materials from returning to the counterfeiter in question or coming into the possession of other questionable parties that may seek to enter this illegal trade.⁵²

3. *Reasons for Inadequate Fines and Compensation Awards*

A number of factors help explain why fines and compensation awards are relatively low. Current law does not require mandatory minimum fines against counterfeiters—as a result, all decisions on the amount of fines is within the discretion of the relevant administrative authority. Most administrative authorities awarding compensation do so on the basis of the profits earned by the counterfeiter.⁵³ In most instances, this calculation is determined by the AICs on the basis of the counterfeiter's total revenues minus a deduction for the counterfeiter's production and sales costs.⁵⁴ In general, because counterfeiters lack written or documentary records, these determinations are made by administrative authorities on the basis of the counterfeiter's own oral representations of its profits and costs.⁵⁵

Most observers of the current enforcement system believe that awards of compensation based upon actual damages to the brand owner would be more effective in both compensating the brand owner and in serving as a deterrent. Administrative authorities, however, seldom use the alternative standard based upon damages to the brand owner.⁵⁶ Most administrative enforcement officials are not lawyers and have not received training in law, economics, or statistics. As a result, most are not comfortable with making complicated damage calculations that involve extrapolations from existing information concerning revenues, profits, and other data. Rather, most administrative authorities find that using the compensation standard, based upon the counterfeiter's profits, to be a simpler method to apply.

4. *Analysis and Comparison*

In other jurisdictions such as the United States, a plaintiff in a civil action against a counterfeiter is entitled to recover “(1) defendant's profits, (2) any damages sustained by the plaintiff, and (3) the costs of the action.”⁵⁷ In assessing profits, the plaintiff is simply required to prove the defendant's sales. The burden of proof shifts then to the defendant to demonstrate all

⁵²This observation is based upon the author's own experience with the AICs in China.

⁵³This observation is based upon the author's own experience in enforcing trademark rights in China.

⁵⁴See *supra* note 52.

⁵⁵See *id.*

⁵⁶See *id.*

⁵⁷15 U.S.C. § 1117(a) (West 1999).

elements of costs or deductions claimed.⁵⁸ Failure to satisfy this burden will result in no costs deducted from the defendant's total sales. The total amount of sales attributable to the counterfeit is calculated based upon the price of the genuine product and not that of the counterfeit product. Courts in the United States have discretion to adjust the sum of damages higher or lower depending upon the circumstances.⁵⁹ In cases where the act of counterfeiting is intentional, courts are required, in the absence of attenuating circumstances, to enter judgment for three times such profits or damages, whichever is higher, along with an award to the plaintiff of reasonable attorney's fees.⁶⁰

Unlike the United States, China does not have provisions for statutory damages. The advantage of statutory damages is that it obviates the need to calculate damages in each case. The availability of such an option under Chinese law, if set at certain levels, may help to address the problem of awards that do not adequately compensate the brand owner for damages suffered. Under United States law, in a civil action involving a counterfeit trademark, the plaintiff may elect, at any time before a final judgment is entered by the court, to recover statutory damages instead of actual damages and profits.⁶¹ Statutory damages range from between \$500 to \$100,000 where the actions were not willful and up to \$1,000,000 where the counterfeiting was willful.⁶²

B. CRIMINAL ENFORCEMENT

China determines criminal liability for counterfeiting based upon a bright-line standard measured by the amount of sales of counterfeit products, currently set at a minimum of about \$6,000.⁶³ All criminal actions

⁵⁸ *See id.*

⁵⁹ *See id.*

⁶⁰ *See* 15 U.S.C. § 1117(b) (West 1999).

⁶¹ *See* 15 U.S.C. § 1117(c) (West 1999).

⁶² *See id.*

⁶³ Article 140 of the Criminal Code provides:

A producer or distributor who mixes up or adulterates products with fake and shoddy materials, passes fake imitations for genuine ones, sells second-class goods at first-class goods' prices, or passes unqualified products as qualified ones, when the sale amount is not less than RMB 50,000 yuan nor more than RMB 200,000 yuan, shall be sentenced to a fixed-term imprisonment of not more than two years or criminal detention, and may in addition or exclusively be subject to a fine of not less than 50% of nor more than two times of the sale amount. If the sale amount is not less than RMB 200,000 yuan nor more than RMB 500,000 yuan, the sentence shall be a fixed-term imprisonment of not less than two years nor more than seven years and may also include a fine of not less than 50% of nor more than two times of the sale amount. If the sale amount is not less than RMB 500,000 yuan nor more than RMB 2,000,000 yuan, the sentence shall be a fixed-term imprisonment of not less than seven years, and may also include a fine of not less than 50% of nor more than two times of the sale amount. If the sale amount is more than RMB 2,000,000 yuan, the sentence shall be a fixed-term imprisonment of fifteen years or life imprisonment, and may also include a fine not less than 50% of nor more than two times of the sale amount or confiscation of property.

must be initiated by the Public Security Bureau ("PSB"), China's principal police organization.⁶⁴ This usually happens according to the following patterns: First, some cases initially brought by administrative authorities are transferred to the PSBs because the amounts in question indicate criminal liability or other serious circumstances are involved, such as death or serious injury to consumers.⁶⁵ Second, third parties can approach the PSBs with a complaint or other information leading to a suspected counterfeiter. Third, the PSBs have the power to initiate criminal actions on their own initiative, based upon their own investigations.⁶⁶

Once the PSBs begin an investigation, they then decide whether sufficient cause for criminal liability exists. If so, the PSBs will then transfer the case to the Procuratorate, China's principal prosecutorial organ.⁶⁷ The Procuratorate will then decide whether to file a criminal action in court and proceed to trial.⁶⁸ Once the PSBs decide to transfer the case to the Procuratorate, it is likely that the Procuratorate will file a criminal complaint and eventually obtain a criminal conviction against the counterfeiter. As a

1997 Criminal Code of the People's Republic of China (adopted at the Second Session of the Fifth National People's Congress on July 1, 1979 and revised at the Fifth Session of the Eighth National People's Congress on March 14, 1997), in WEI LUO, *THE 1997 CRIMINAL CODE OF THE PEOPLE'S REPUBLIC OF CHINA: WITH ENGLISH TRANSLATION AND INTRODUCTION* 85 (1998) [hereinafter "PRC Criminal Code"]. Other provisions also provide for criminal liability, including art. 213, which states:

Anyone who uses a trademark identical to a registered trademark on the same type of goods without the permission of the owner of the registered trademark and the circumstances are serious, shall be sentenced to a fixed-term imprisonment of not more than three years or criminal detention, and may in addition or exclusively be sentenced to a fine. If the circumstances are exceptionally serious, the sentence shall be a fixed-term imprisonment of not less than three years nor more than seven years, and a fine.

PRC Criminal Code, art. 213. The terms, referring to serious and exceptionally serious consequences, are not further defined in the statute. Authorities have interpreted the 1993 guidelines issued by the Supreme People's Procuratorate to indicate that profits of RMB 20,000 or total turnover of RMB 100,000 constitute serious circumstances. Discussions between the author and the Supreme People's Court and the Ministry of Public Security indicate that these guidelines are no longer in effect after the enactment of the new Criminal Code in 1997 and there are currently no guidelines for interpreting these terms.

⁶⁴ See PEOPLE'S POLICE LAW OF THE PEOPLE'S REPUBLIC OF CHINA (Zhonghua Renmin Gonghe Guo Gongan Fa) (adopted at the 12th meeting of the Standing Committee of the Eighth National People's Congress on Feb. 28, 1995, promulgated by Order No. 40 of the President of the People's Republic of China on Feb. 28, 1995 and effective as of the same date) art. 1 & 2 (PRC) [hereinafter "PRC Police Law"].

⁶⁵ See, e.g., PRC Trademark Law, art. 40.

⁶⁶ See PRC Police Law, art. 6(1).

⁶⁷ See PUBLIC PROCURATORS LAW OF THE PEOPLE'S REPUBLIC OF CHINA (Zhonghuo Renmin Gonghe Guo Jiancha Guan Fa) (adopted at the 12th meeting of the Standing Committee of the Eighth National People's Congress on Feb. 28, 1995, promulgated by Order No. 39 of the President of the People's Republic of China on Feb. 28, 1995 and effective as of July 1, 1995) art. 1 & 2 (PRC) [hereinafter "PRC Procurators Law"].

⁶⁸ See PRC Procurators Law, art. 6.

practical matter, PSBs accept cases for investigation only when sums involved are high, when serious issues of corruption are involved, or when death or serious injury to consumers has occurred.⁶⁹

1. Proof and Evidence

To establish proof of sales of counterfeiting goods above the \$6,000 threshold, the current practice of administrative authorities, police, prosecutors, and courts is to require direct physical evidence in the form of receipts, accounts, ledger books, or tax documents.⁷⁰ Most PSBs will require such evidence before proceeding any further with a criminal investigation.⁷¹ This creates a significant hurdle because most counterfeiters do not keep physical records of their activities, and any records recovered are written to disguise counterfeiting activity.⁷²

What about any counterfeit goods, packaging, and equipment seized on the premises? In China today, such materials are not considered evidence of sales within the meaning of the Criminal Code.⁷³ PRC authorities read the requirements of the law to require evidence of completed sales—currently this can be satisfied only by physical evidence of a completed sale in the form of a receipt or similar document or by the counterfeiter's oral confession.⁷⁴ Materials seized on the counterfeiter's premises, no matter how large the amount, are not considered proof of sales and are not considered to be a basis from which proof of sales can be inferred.

These evidentiary standards are one reason that criminal prosecutions are rare. In 1998, of 14,736 trademark infringement and counterfeiting cases brought by AICs of all levels nationwide, only 35 cases, or 1 in every 421 cases, were transferred by administrative authorities to police and prosecutors for criminal prosecution.⁷⁵ No information is available on how many of these cases actually resulted in criminal convictions.

⁶⁹The PSBs have limited personnel and resources and tend to use such resources for crimes involving violence and harm to persons. Intellectual property crimes are viewed as having lower priority.

⁷⁰This observation is based upon the author's own experience in pursuing criminal convictions for counterfeiting cases in the PRC and confirmed by discussions with judges, prosecutors, and lawyers in the PRC during the author's visit with a group of US experts on counterfeiting in Nov. 1999. See also *The Tools You Can Use*, BUS. CHINA, Jan. 3, 2000, at 5, available in WL 2164483, at 3 (noting that threshold for criminal liability is based on proof of prior sales).

⁷¹See *id.*

⁷²This observation is based upon the author's own experience in China.

⁷³See *The Tools You Can Use*, *supra* note 70, at 3.

⁷⁴See *id.*

⁷⁵See SAIC 1998 ANNUAL REPORT, *supra* note 44, at 15. In 1997, of the 15,321 trademark infringement and counterfeiting cases brought by all levels nationwide by the AIC, only 57 cases, or 1 in 269 cases, were transferred to judicial authorities for criminal prosecution. See SAIC 1997 ANNUAL REPORT, *supra* note 45, at 11.

2. *Analysis and Comparison*

While China is somewhat unusual in using a bright-line standard for criminal liability, this approach is workable so long as the standards for proof and evidence are realistic and attainable. The requirement of direct physical evidence, however, is difficult to satisfy in most cases.

(a) Criminal Liability

In the United States, courts often rely on indirect evidence of counterfeiting, both to establish criminal liability and damages.⁷⁶ Thus, eyewitness testimony by accomplices, associates, or undercover agents concerning counterfeiting activity can be used to establish criminal liability. Any counterfeit goods found on the premises will also support an inference of liability. Courts are also able to extrapolate and draw inferences from the presence or absence of evidence. For example, courts may extrapolate the amount of counterfeit sales based upon the amount of goods seized upon the premises. Where the defendant is missing business records, the court may, in some circumstances, make an inference of illegal activity based on the absence of such records because lawful businesses usually keep financial and business records.

(b) Criminal Attempt

In the United States, evidence that may not be sufficient to establish liability for a substantive criminal offense may be sufficient to establish liability for a criminal attempt.⁷⁷ For example, take a case where authorities seize counterfeit goods and equipment used to produce counterfeits on the premises of an alleged counterfeiter. In the United States, courts may use this evidence to establish criminal attempt to violate laws against the production and sale of counterfeit goods, even if such evidence is not sufficient to establish violations of the substantive laws against counterfeiting.

Such an approach may help to address China's issues of requiring direct physical evidence of sales. Evidence that may not be acceptable as proof of sales, such as goods and equipment found on the premises, may be sufficient to establish criminal attempt to violate laws against counterfeiting. While this approach would be consistent with China's current laws

⁷⁶ See Lydia Pallas Loren, *Digitization, Commodification, Criminalization: The Evolution of Criminal Copyright Infringement and the Importance of the Willfulness Requirement*, 77 WASH. U. L.Q. 835, 893-896 (1999). See also *United States v. Yamin*, 868 F.2d 130, 133-134 (5th Cir. 1991) (circumstantial evidence held sufficient to sustain a conviction for conspiracy to traffic in counterfeit goods).

⁷⁷ See, e.g., 18 U.S.C. § 2320(a) (West 1999) ("Whoever intentionally traffics or attempts to traffic in goods or services and knowingly uses a counterfeit mark on or in connection with such goods or services shall . . . be fined not more than \$2,000,000 or imprisoned not more than 10 years, or both . . .").

against criminal attempt,⁷⁸ few enforcement authorities in China appear to have considered this approach for several reasons. In general, brand owners have not attempted to bring claims based upon criminal attempt but have focused most of their efforts on establishing the substantive offenses against counterfeiting. As brand owners continue to pursue various innovative and creative options in their battle against counterfeiters, they may begin to press claims based upon criminal attempt. Such new efforts should draw official attention to these claims and require authorities to decide whether claims against counterfeiters based upon criminal attempt are viable under the PRC criminal system. In addition, the initial determination on whether to pursue a criminal investigation is made by officials of the PSB, a police organization, who generally do not have legal training and may not have sufficient professional knowledge or background in law to pursue cases based upon complex legal concepts such as attempt. More experience and training in this area for the PSB (and prosecutors) may help to make recognition of criminal attempt to engage in counterfeiting a cognizable offense under PRC criminal law.

(c) Landlord-Tenant Culpability Issues

Liability for counterfeiting in China currently focuses on manufacturers and vendors of counterfeit products and does not generally extend to other significant actors in the counterfeit trade. Brand owners tend to focus on manufacturers based on the view that this attacks the source of the problem.⁷⁹ Some brand owners also target large vendors, but liability for a sale can be difficult to establish because of the requirement that the sale was made with knowledge that the goods were counterfeit.⁸⁰ Brand owners and authorities have not focused on large-scale distributors or wholesale markets, which play a crucial role in the trade in counterfeit goods.

In large wholesale markets in China, there are typically hundreds even thousands of individual vendors renting booths, stalls, or small stores from a landlord that typically has invested in and helped to establish the wholesale market.⁸¹ These large wholesale and distribution centers are organized,

⁷⁸ Article 23 of the PRC Criminal Code provides:

A criminal attempt refers to a case where an offender has already begun to commit a crime but is prevented from completing it for reasons independent of his will. An offender who attempts to commit a crime may, in comparison with one who completed the crime, be given a lighter or mitigated punishment.

PRC Criminal Code, art. 23.

⁷⁹ Among other provisions, liability for producing counterfeiting goods can be established under article 38 of the PRC Trademark Law and article 140 of the PRC Criminal Code. See PRC Trademark Law, art.38; PRC Criminal Code, art 140.

⁸⁰ See PRC Trademark Law, art. 38(2).

⁸¹ Wholesale markets all throughout China serve the key role of providing distribution channels for goods that cannot enter the market through normal distribution channels. With-

well financed, and may be the most significant organized crime entities in the counterfeit trade in China. In some of these markets, a large majority of these vendors are selling counterfeit goods, up to 80 or 90% in some cases.⁸² Some of these landlords have placed signs in the markets warning against the sales of counterfeit goods, and have inserted covenants against the commission of illegal activities in the leases signed with individual vendors.⁸³ These actions are designed to protect these landlords against liability for the actions of their tenants, as opposed to discouraging such illegal activities. In some cases, these landlords may be a local government entity, such as the local AIC, charged with the regulation of markets but also with enforcement against counterfeiting.⁸⁴

Although there can be little doubt that these landlords are encouraging, protecting, or at least tolerating these illegal activities on the rented premises,⁸⁵ Chinese law does not currently appear to recognize liability of the landlord for the activities of these tenants. However, brand owners do have arguments for landlord liability based on an interpretation of existing laws.⁸⁶ For example, while landlords do not produce or sell counterfeit goods in violation of applicable laws, it can be argued that landlords “deal in”⁸⁷ counterfeit goods or “facilitate” counterfeiting by providing “storage,

out these wholesale markets, counterfeit goods could not reach retail outlets and the consumer. Many smaller wholesalers or retailers will pour over wholesale markets on a monthly or weekly basis and purchase counterfeit goods for resale to other retail outlets or to consumers. Many wholesale markets are located in densely populated areas and convenient to traffic. For a more detailed discussion of these wholesale markets and their vital role in the trade in counterfeit goods, see Chow, *supra* note 1, at 14-17; see also *Stuck in the Middle*, *supra* note 2, at 3-4.

⁸² See Chow, *supra* note 1, at 17.

⁸³ This observation is based upon the author's own experience in investigating wholesale markets in China—the author was able to review several leases entered into between tenants and landlords and make numerous visits to wholesale markets.

⁸⁴ Prior to China's economic reforms, the AICs typically established and managed wholesale markets. For further discussion, see Chow, *supra* note 1, at 22-23.

⁸⁵ Based upon the author's own experience, the involvement of landlords in the counterfeit trade appears to be well known to most consumers.

⁸⁶ Landlords are arguably in violation of the catch-all provision Article 38(4) of the PRC Trademark Law because they “cause, in other respects, prejudice to the exclusive right” of the trademark owner. PRC Trademark Law, art. 38(4). This provision is further amplified by Article 41 of the PRC Trademark Law Implementing Rules. PRC Trademark Law Implementing Rules, art. 41.

⁸⁷ Article 41(2) imposes liability where an entity “deals in goods that one knows or should know to be goods that infringe another's exclusive right to use a registered trademark.” See PRC Trademark Law Implementing Rules, art. 41(2). Knowledge can be inferred from the low prices charged for the goods, sometimes one half to one third of the price of the genuine product. In other cases, knowledge can also be inferred where the market has been frequently raided and where counterfeit goods make up a large percentage (up to 90% in some wholesale markets) of all goods sold.

transportation, mailing or concealment⁸⁸ in violation of Article 41 of the *PRC Trademark Law Implementing Rules*.⁸⁹ To date, however, no brand owner has attempted to bring an action directly against landlords in wholesale markets or against the corporate entity that organized the market using the *PRC Trademark Law, PRC Trademark Law Implementing Rules* or any other laws. Most brand owners limit their actions to raids against individual wholesale vendors within the market, which can have several hundred to several thousand such vendors. In the United States, under some circumstances, a landlord may be held liable for the activities of its tenants.⁹⁰

(d) Lesser Criminal Offenses

The laws related to counterfeiting in China do not appear to draw distinctions between various degrees of criminal liability and levels of criminal culpability. While it is true that the penalties for criminal violations become more severe as the amount of sales of counterfeit goods increases, no distinction is drawn concerning the type of crimes involved. Moreover, any conviction under the current *PRC Criminal Code* results in a minimum term of imprisonment of at least two or three years, depending upon the relevant criminal provision.⁹¹ The severity of the punishments involved may be one reason for the high threshold for a criminal conviction and for the difficulty experienced by trademark owners in achieving such convictions.

United States law draws distinctions between various degrees of criminal culpability, treating certain types of criminal offenses as more serious than others. Depending upon the circumstances, a certain type of criminal conduct can be classified as a felony, a serious criminal offense, or as a misdemeanor, a less serious criminal offense. Drawing a distinction between various levels of criminal culpability may permit enforcement authorities in China to have more flexibility in imposing criminal liability on counterfeiters. For example, a counterfeiting offense that is classified as a minor crime may involve only a short term of imprisonment, such as 3 to

⁸⁸ See *PRC Trademark Law Implementing Rules*, art. 41(3) (imposing liability for “intentionally provid[ing] conditions facilitating the infringement of another’s exclusive right to use a trademark such as storage, transportation, mailing or concealment.”). The intent element of Article 41(3) seems to impose a scienter requirement beyond knowledge as set forth in Article 41(1), but to date there are no legislative history materials or any other materials that provide further illumination of these terms. A landlord’s tender of premises used for selling counterfeits appears also to differ from storage facilities or facilities that conceal the activity.

⁸⁹ See *PRC Trademark Law Implementing Rules*, art. 41.

⁹⁰ See, e.g., B.A. Glesner, *Landlords as Cops: Tort, Nuisance & Forfeiture Standards Imposing Liability on Landlords for Crime on the Premises*, 42 *CASE W. RES. L. REV.* 679, 743-756 (1992) (discussing federal drug laws that allow forfeiture of a landowner’s property because of the illegal behavior of his or her tenants).

⁹¹ See, e.g., *PRC Criminal Code*, art. 140 (two years); *PRC Criminal Code*, art. 213 (three years).

6 months, a punishment that should still have deterrent effect given the stigma and social consequences of imprisonment in China.

(e) Aggregating Criminal Offenses

It is unclear whether Chinese law permits the aggregation of several separate offenses for the purpose of satisfying the legal requirements for a criminal conviction. For example, if a counterfeiter were caught in three separate incidents with sales in each discrete incident failing to exceed the \$6,000 requirement but with aggregated sales from all three incidents exceeding the \$6,000 figure, would this result in criminal liability? The PRC Ministry of Public Security has acknowledged that such an approach is possible but to date no definitive guidelines or official position has been promulgated supporting the aggregation approach. In the United States, discrete incidents can be aggregated for the purpose of determining knowledge, intent, and seriousness of the offense to find criminal liability.⁹²

C. CIVIL ACTIONS

Civil litigation has not emerged to date as a practical or viable option for brand owners in most cases. This difficulty can be traced to problems of evidence collection and the general inability to obtain immediate relief from courts in the form of temporary restraining orders or preliminary injunctions. The filing of a civil action against a counterfeiter may not be useful if the plaintiff cannot also obtain an immediate court order restraining the defendant from destroying or disposing of evidence, such as an existing stock of counterfeit goods, equipment, or records, if any.

Obtaining evidence in the absence of temporary restraining orders and seizure actions also makes civil litigation an unattractive option. Most brand owners find that the best method for obtaining action is through a raid and seizure action, but such procedures are normally not available through

⁹² See, e.g., *United States v. Riles*, 928 F.2d 339 (10th Cir. 1991) (drug offenses that are part of the same course of conduct can be aggregated for purposes of determining the seriousness of the base offense level under federal law); *United States v. Abod*, 770 F.2d 1293, 1297 (5th Cir. 1985) (noting that Congress permitted aggregating of separate incidents in order to meet minimum threshold amount of \$1000 for credit car fraud). Under United States law, an offense can be viewed as part of a pattern of continuing criminal activity, thus meriting a more severe punishment. Under recent amendments to the Federal Racketeer Influenced Corrupt Practices ("RICO"), trading in counterfeit goods is considered to be a predicate offense in a pattern of continuing criminal activity, thus constituting a RICO violation and allowing the imposition of a maximum RICO penalty of 25 years imprisonment and a fine of twice the proceeds of the illegal activity. See David J. Goldstone & Peter J. Toren, *The Criminalization of Trademark Counterfeiting*, 31 CONN. L. REV. 1, 72 (1998). Additionally, the seriousness of an offense or any prior convictions for violating intellectual property rights will also affect the application of Federal Sentencing Guidelines and result in a stiffer sentence. See Michael Coblenz, *Intellectual Property Crimes*, ALB. L.J. SCI. & TECH. 235 (1999).

civil courts. Rather, the raid and seizure action must normally be pursued through administrative authorities such as the AICs. Once the AIC has seized evidence, brand owners have generally found it difficult to get such evidence transferred to courts for civil litigation. There are currently no guidelines on the transfer of such evidence and in the absence of such guidelines, evidence may become destroyed or lost after seizure by the AICs. In addition, many AICs will seek to auction off seized equipment and products (after removing the offending counterfeit mark)⁹³ and are unlikely to transfer such evidence to courts and forego the revenues that would otherwise be obtained through public auctions. While some trademark owners have attempted to pursue litigation after raids made by AICs, most have found that such obstacles make it difficult to get evidence transferred from administrative authorities to courts. Moreover, some courts will not accept jurisdiction while the case is still pending before an administrative authority.⁹⁴ As a result, plaintiffs must wait until the AIC issues a final decision in the matter, which usually takes up to three months.⁹⁵ By the time the decision is issued, the evidence and the suspect may have long disappeared from the scene.

Compensation awards to successful plaintiffs have been generally low by western standards because courts apply the same laws and methods for determining damages as those applied by administrative authorities, and statutory damages are unavailable.⁹⁶ Some plaintiffs have achieved some good results through the recently established Intellectual Property Divisions of the intermediate People's Courts in some jurisdictions.⁹⁷ However, the civil litigation system in the PRC continues to lag behind the administrative enforcement system in terms of resources, expertise, and power.

1. Analysis and Comparison

Civil litigation continues to be an unattractive option because of the lack of immediate injunctive relief and the lack of a mechanism providing plaintiffs with the opportunity to gather evidence during a raid for civil litigation.

In the United States, a plaintiff may appear *ex parte* before a federal court and apply for both a seizure order for counterfeit goods and a temporary restraining order ("TRO") against a suspected counterfeiter.⁹⁸ If the

⁹³ See *supra* text accompanying notes 47-49.

⁹⁴ Applicable law provides for a civil litigation option after administrative remedies have been exhausted. See PRC Trademark Law Implementing Rules, art. 43.

⁹⁵ See *The Tools You Can Use*, *supra* note 70, at 1.

⁹⁶ See *supra* text accompanying notes 44-46.

⁹⁷ See PETER FENG, INTELLECTUAL PROPERTY IN CHINA 24 (1997).

⁹⁸ Such relief requires the posting of security by the plaintiff in the form of a bond. If the plaintiff ultimately prevails in the case, then the security is released to the plaintiff. If the defendant prevails, the security is used to indemnify the defendant against any damages suf-

court decides to grant the plaintiff's application, the plaintiff is then entitled to go to the premises accompanied by a federal marshal and seize the goods. At the time of the raid, the plaintiff also serves a copy of the TRO and the complaint upon the defendant. The terms of the TRO often prohibit the defendant from engaging in any further infringing activity and also prohibit the defendant from disposing of any evidence upon pain of contempt sanctions (including imprisonment) for the violation of the court order. Under federal practice, the TRO is effective for ten days within which time a hearing must be held in order to determine whether the court should issue a preliminary injunction, *i.e.*, an order that continues the prohibitions contained in the TRO until the final resolution of the case before the court.⁹⁹ Once the preliminary injunction is issued, the case can then proceed to trial where the court can determine what remedies should be granted to a prevailing plaintiff. The plaintiff can also apply for a hearing on the preliminary injunction before the expiration of the ten-day period. In most instances, the parties agree to settle the case without a trial and the court enters a consent decree. In some instances, the final resolution of the case may involve a permanent injunction, a court order that permanently bars the defendant from engaging in certain activities, the violation of which may result in criminal liability and imprisonment.

These provisional remedies discussed above allow a brand owner to immediately stop a counterfeiter from engaging in additional harmful conduct at the same time (or before) a complaint is filed in civil court. This type of provisional relief does not appear to be a viable option under China's current judicial system and without this type of mechanism,¹⁰⁰ few

ferred through the actions of the plaintiff. For a discussion of the federal injunction process, see generally FED. R. CIV. P. 65. For a discussion of injunctions in connection with intellectual property cases, see Jason R. Berne, *Court Intervention but Not in a Classic Form: A Survey of Remedies in Internet Trademark Cases*, 43 ST. LOUIS U. L.J. 1157, 1162-1163, 1208-1209 (1999).

⁹⁹ See FED. R. CIV. P. 65.

¹⁰⁰ According to Judge Dong Tianping, Division Head, Intellectual Property Rights Tribunal, Supreme People's Court, the equivalent of the TRO and preliminary injunctive relief is available through a combination of Articles 92, 93 & 97 of the PRC Civil Procedure Law. Interview with Judge Dong Tian Ping, Division Head, Intellectual Property Rights Tribunal, Supreme People's Court (May 16, 2000). Article 97 provides for "advance execution," allowing a court at any time upon the application of the plaintiff—even before the complaint is filed—to issue an order prohibiting the defendant from taking certain actions, including continuation of counterfeiting or infringing activity where "urgent circumstances require advance execution." See PRC CIVIL PROCEDURE LAW. (adopted at the 4th Session of the 7th National People's Congress on April 9, 1991, promulgated by Order No. 44 of the President of the People's Republic of China on April 9, 1991 and effective as of the same date) art. 97 (PRC) [hereinafter "Civil Procedure Law"]. Articles 92 & 93 provide for the preservation of property (or evidence) through an application by an interested party (which application can be made before the filing of a complaint) and upon the posting of security. Within 48 hours, the court must decide whether to issue an order and if such an order is issued court officials will proceed to the site and seal the area, preventing evidence from being lost, hidden, or de-

plaintiffs in China will find civil litigation a viable option against counterfeiters.

III. LONG TERM ISSUES IN ENFORCEMENT AGAINST COUNTERFEITING IN CHINA

This part examines certain long-term systemic issues relating to enforcement against counterfeiting. These issues relate to structural features of the current enforcement system and to long-term issues of training, personnel, and resources.

A. COORDINATION AMONG VARIOUS ENFORCEMENT ENTITIES

China's regulatory structure, which divides the economy into vertical sectors, has resulted in a number of parallel enforcement mechanisms. In some instances, this system has led to bureaucratic and professional rivalries among the various enforcement agencies, resulting in behaviors that may frustrate effective enforcement. For example, in a case where an AIC has conducted a raid and has seized evidence indicating criminal liability, the transfer by the AIC of the case to police and prosecutors will require that the AIC also transfer all materials seized at the site.¹⁰¹ This means that the AICs will need to forgo all fines and penalties, will be unable to auction off any seized goods, and will have less to state on their annual reports of activities on which their performance and professional advancement is judged.¹⁰²

The establishment of guidelines concerning the work of the various enforcement entities, procedures for cooperation and coordination, and rules for the transfer of cases may help to alleviate some of these problems.¹⁰³

B. PUBLIC VERSUS PRIVATE ENFORCEMENT

As set forth earlier, China's current enforcement system places heavy emphasis on public enforcement against counterfeiting, mostly through administrative authorities such as the AICs or TSBs.¹⁰⁴ Up to 85% of all

stroyed. Civil Procedure Law, arts. 92 & 93. The applicant then has 15 days to bring an action in court; if no suit is filed within this 15 day period, the court will cancel the property preservation. Civil Procedure Law, art. 93. According to Judge Dong violations of any of the orders discussed above can result in imprisonment for the offender. The author's own experience in China indicates that few brand owners are aware of these procedures and that it is unclear whether courts will in practice enforce these procedures as described above.

¹⁰¹ See *The Tools You Can Use*, *supra* note 70, at 4.

¹⁰² See *id.*

¹⁰³ Another possibility is to centralize all enforcement powers in a single administrative entity, but this may not be a practical alternative in China's current political climate. Any shifts in power and resources from current entrenched distributions may give rise to political resistance by those entities currently enjoying such power and its accompanying prestige.

¹⁰⁴ See *supra* text accompanying notes 28-31.

counterfeit enforcement actions are brought by administrative authorities.¹⁰⁵ This feature can be attributed to China's historic centrally planned economic system in which most aspects of the economy were planned, controlled, and administered by the State. This system may have worked well when fewer private rights, interests, and free market transactions were at stake under China's pre-reform economy. Under present conditions, however, emphasis on public enforcement presents some disadvantages for brand owners.

For example, the AIC is primarily a regulatory and enforcement body, charged with the general administration of economic enterprises and the general development of commerce.¹⁰⁶ As a result, the AIC is not focused upon vindicating private rights. In the enforcement area, the AIC tends to focus on imposing fines and penalties on the counterfeiter and is not focused primarily on protecting the rights and interests of the trademark owner. Similarly, the TSB is charged with protecting the rights of the consumer and also is not primarily concerned with protecting the rights of the trademark owner.¹⁰⁷ As a result, neither body is focused on making the trademark owner whole by awarding compensatory damages commensurate with the actual losses suffered. Awards of compensation, when made, tend to be minor in comparison to actual losses suffered.¹⁰⁸

By contrast to Western nations, the PRC has not to date created strong tools for private enforcement where the focus is on both compensatory damages to the trademark owner and the development of remedies specifically geared towards the protection of the private plaintiff's rights. For example, remedies such as attachment and forced sale of the defendant's property, freezing bank accounts, and permanent injunctive relief (backed by civil and criminal sanctions) have not been developed in the PRC. In countries like the United States, private enforcement through civil litigation, or the threat thereof, assumes a major role in the protection of intellectual property rights.¹⁰⁹

¹⁰⁵ This figure is based on the author's discussions with PRC administrative enforcement officials, judges, prosecutors, and lawyers during the author's trip to the PRC as part of a delegation of US experts on intellectual property law. *See supra* note *.

¹⁰⁶ *See, e.g.*, PRC Trademark Law, arts.1 & 2.

¹⁰⁷ *See supra* text accompanying note 33.

¹⁰⁸ *See supra* text accompanying note 44; *see also* SAIC 1997 Annual Report, *supra* note 45.

¹⁰⁹ For recent examples of the successful use of civil litigation by plaintiffs to protect their trademark rights, see *A.C. Legg Packing Co., Inc. v. Olde Plantation Spice Co.*, 61 F. Supp. 2d 426 (D. Md. 1999); *SNA, Inc. v. Array*, 51 F. Supp. 2d 554 (E.D. Pa. 1999); *World Gym Licensing, Ltd. v. Fitness World*, 47 F. Supp. 2d 614 (D. Md. 1999); *Am. Employers' Ins. Co. v. DeLorme Pub. Co.*, 39 F. Supp. 2d 64 (D.Me. 1999); *Sara Lee Corp. v. Bags of N.Y., Inc.*, 36 F. Supp. 2d 161 (S.D.N.Y. 1999). For a review of trademark infringement litigation basics, see Marcy J. Bergman, *Trademark Infringement Litigation Primer*, 569 PLI/PAT 443 (1999).

C. RELATIONSHIP OF NATIONAL AND LOCAL AUTHORITIES

Recently in response to pressures for more effective action, a number of local governments at the provincial level (one level below the national or central level in Beijing) have enacted local legislation on counterfeiting.¹¹⁰ For example, Guangdong Province, a hotbed of counterfeiting in southeastern China, has recently enacted local legislation that applies stiff fines and penalties for counterfeiting.¹¹¹ While local authorities in Guangdong appear to be vigorous in enforcing these new laws and in collecting fines and penalties, it is still too early to determine whether enforcement of these new laws will actually result in deterrence.

Local legislation in China is lawful so long as the local legislation is not inconsistent with national legislation. The current practice in China does not appear to be concerned with uniformity of local laws, coordination between various provinces and local governments, and coordination between national governments and local governments. Issues of coordination among various jurisdictions and uniformity of local laws may become an issue as more local jurisdictions enact their own legislation.¹¹²

D. INVESTIGATIVE TECHNIQUES

Currently, Chinese authorities do not use as wide an array of investigative techniques as investigative entities in the United States, such as the Federal Bureau of Investigation. They may purchase counterfeit goods in order to collect evidence, but Chinese authorities generally do not engage in other types of investigations. Chinese authorities often rely upon the brand owners to engage a growing private investigation industry for the gathering of evidence against counterfeiters, but such private agencies are limited by law to certain methods and cannot use the array of techniques that would be available to a law enforcement entity.

In the United States, private investigators also serve an important role in assisting government enforcement entities, but government investigators do engage in a wide variety of investigative methods of their own.¹¹³ Many government entities use hidden cameras and audio equipment to document

¹¹⁰For a description of the legislation passed by Guangdong Province, see *The Tools You Can Use*, *supra* note 70, at 5.

¹¹¹*See id.*

¹¹²Unlike China, the United States has a dual system of government at the national and state and local levels. While China and the United States have different systems of government, a study of consideration of federal-state relations on legislative matters and on how uniformity in state law is maintained may be useful.

¹¹³The observations in this paragraph are based on a number of conversations between the author and Mr. Timothy B. Klund, Special Agent, Federal Bureau of Investigation, Charlotte, North Carolina, while we were both in China during an exchange initiative between the United States and China on enforcement of intellectual property rights. For a further description of this exchange, see *supra* note *.

transactions and conversations that are later used as evidence. Government investigators also may assume false identities in an undercover capacity for the purpose of infiltrating counterfeiting rings in order to trace counterfeiting from the retail level back to the source in manufacturing or distribution. Some of these investigations may take months and result in a sting operation against multiple counterfeiters. In cases involving organized crime, government agents may also use wiretaps.

E. TRAINING OF JUDGES AND PROSECUTORS

Many of the judges and prosecutors in China are not lawyers and have received no formal legal training.¹¹⁴ This may be true even for the judges who sit on China's recently established specialized intellectual property courts. While this practice is changing and the younger generation of judges and lawyers are either law school graduates or have legal training, there is still a significant number of existing judges and prosecutors who do not have a legal background. Additional training of these judges and prosecutors in the areas of trademarks and intellectual property would be useful for the long term.

F. NON-LAWYERS AND LEGAL WORK

A serious issue exists where persons without legal training engage in legal work.¹¹⁵ For example, the PSBs are charged to make a preliminary assessment of criminal liability under present law and practice. Unless the PSBs decide that there is sufficient evidence of criminal liability, they will not pursue an investigation and refer the matter to the Procuratorate. The determination by the PSBs is essentially one of legal interpretation and application of laws—i.e., interpreting the provisions of the Criminal Code relating to criminal liability for counterfeiting and reviewing evidence for sufficiency. One reason why PSBs require direct physical evidence of sales in the form of receipts is because PSBs have little or no experience with evaluating indirect evidence, drawing inferences from circumstantial evidence, or making extrapolations based upon existing evidence.

Similarly, the AICs have authority to award compensation based upon damages suffered by the plaintiff, but tend to use the more simple method

¹¹⁴Recent legislative changes now require "professional legal knowledge" as a qualification for judges and prosecutors and training in law for those appointed prior to the enactment of these new laws. See JUDGES' LAW OF THE PEOPLE'S REPUBLIC OF CHINA (Zhonghua Renmin Gonghe Guo Faguan Fa) (adopted at the 12th meeting of the Standing Committee of the Eighth National People's Congress of the People's Republic of China on Feb. 28, 1995, promulgated by order No. 38 of the President of the People's Republic of China on July 1, 1995 and effective as of that date) art. 9(6) (PRC); PRC Public Procurators Law, art. 10(6).

¹¹⁵Current Chinese law does not appear to contain any prohibitions against the unauthorized practice of law by those not trained in the law or without professional legal knowledge.

of making awards based upon the counterfeiter's profits. The alternative method of determining damages would require an evaluation of losses suffered by the brand owner in the form of lost sales revenues, and expectation and consequential damages. These are not evaluations that most AIC enforcement officials, who are not legally trained, would feel comfortable in undertaking. Although not legally trained, AIC officials are expected to hand down administrative decisions interpreting trademark law and rendering final judgment in cases brought against counterfeiters.

The frequent work of persons without legal training in performing difficult legal tasks such as interpretation of laws and deciding issues of evidence offers an additional explanation why effective enforcement against counterfeiting is difficult to achieve. Assigning legal tasks to those without legal training may have posed fewer problems under China's pre-reform economy;¹¹⁶ China's developing economy has now given rise to increasingly sophisticated economic crimes and torts with correspondingly more complex legal issues of evidence, proof, and liability. Many enforcement officials may not have the training, knowledge, or skills to handle properly these more sophisticated legal tasks. For the longer term, China needs to consider whether to recruit more lawyers into its administrative and enforcement systems or to distribute work in a different manner.

IV. CONCLUSION

In the area of enforcement against counterfeiting, the crucial issues for China now lie not in the enactment of new laws, but in the interpretation and application of existing laws. In this area there continue to be a number of significant issues that frustrate foreign and local brand owners in China. Some of these issues—such as proof of criminal liability through indirect and circumstantial evidence and the measure of compensatory damages—appear to test the capacity of China's developing enforcement system to deal with increasingly sophisticated legal issues that are a necessary outgrowth of China's rapid economic and commercial development. Additional training for PRC enforcement entities in this area and consideration of practices by other nations, such as those of the United States, may result in some improvement of these problems.

¹¹⁶China's legal system did not play an important role during China's pre-reform economy where market transactions were rare. Indeed, China abolished its legal system altogether during the chaotic years of the Cultural Revolution and only began to resuscitate the legal system in 1978, in order to support the new reforms. For a first-hand account of the Cultural Revolution and its effects on Chinese institutions, see GAO YUAN, *BORN RED: A CHRONICLE OF THE CULTURAL REVOLUTION* (1987). For an account of the history of China's legal community, see Alison W. Conner, *Training China's Early Modern Lawyers: Soochow University Law School*, 8 *J. CHINESE L.* 1 (1994); Yujie Gu, *Entering the Chinese Legal Market: A Guide for American Lawyers Interested in Practicing Law in China*, 48 *DRAKE L. REV.* 173 (1999).

The Chinese enforcement system also exhibits a number of systemic problems relating to the division of power among enforcement entities, administrative bodies, and the police, prosecutors, and the courts. These systemic issues can also be traced to the Chinese government's struggle to use existing pre-reform government and regulatory structures to keep pace with new economic activities introduced as a result of recent reforms. Addressing both of these types of issues—interpretation and enforcement and systemic issues in the age of reform—should not only help to improve the effectiveness of legal enforcement against counterfeiting, but also help to improve the overall development of China's legal and regulatory system for the future. While some of these changes will improve China's legal system and, in the long term, serve China's national interests, reform in the world's most massive government bureaucracy may not be easy to accomplish. China has complex and massive political and legal systems with many competing interests and segments that are resistant to change which may result in a redistribution and diminution of power and resources. As a result, it cannot be predicted whether and when China will recognize the benefits of making the appropriate adjustments, and begin the task of implementing changes and addressing some of the issues raised in this Article that will lead to more effective enforcement against counterfeiting.¹¹⁷ Obtaining China's political commitment to address these issues and to crackdown on the world's most serious counterfeiting problem is the crucial and difficult task for brand owners in China—and around the world—in the years ahead.

¹¹⁷The critical issue is one of political will. For a discussion of the issue of political will and the social and political costs involved in any serious national crackdown against counterfeiting, see Chow, *supra* note 1, at 39-52.