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CROUCHING PATENTS, HIDDEN ANTI-MONOPOLY

The rising influence of China's web of IP policies.

BY DAVID YANG

AS CHINA HAS TRANSFORMED FROM AN EXPORT-CENTRIC FACTORY to the world to an innovator of new technology, its IP landscape has evolved at breakneck speed. Now the world's second largest economy, China has adopted policies that encourage the indigenous ownership of IP—but make it harder for foreign corporations to enforce their IP against Chinese companies.

In 2016, the Chinese State Intellectual Property Office (Sipo) received over 1.3 million invention patent applications and granted approximately 400,000 invention patents. (See Sipo IP News, Feb. 8, 2017.) Domestic applicants sought roughly 75 percent of these patents—in sharp contrast to 10 years ago, when foreign applicants outnumbered domestic. (See Sipo IP News, Jan. 25, 2017.)

On the heels of this record-breaking year, China's State Council announced the latest five-year plan. Its 2017 plan calls for the doubling of indigenous patent ownership by 2020 and more than a doubling of licensing royalties (from foreign companies)—from US\$4 billion to \$10 billion per year by 2020. Given the general success of the prior five-year plans, it is likely that China will attain the goals of this plan.

This dramatic increase in domestic patent filings is no accident. It began years earlier with China's 2006 indigenous innovation plan, also known as the National Medium- and Long-Term Plan for the Development of Science and Technology (2006-2020). Since proposing that plan, China has invested significantly in its judicial court system to encourage IP enforcement. In 2016 alone, the Chinese court system adjudicated 146,000 civil intellectual property

rights cases (See Sipo IP News, March 15, 2017), a 46 percent increase over the previous year.

ENFORCEMENT AGAINST CHINESE COMPANIES GETS HARDER

While China has encouraged the enforcement of domestically owned IP, it has also implemented and enforced anti-monopoly laws that make it harder for certain foreign entities to enforce their own IP.

Article 55 of the Chinese Anti-Monopoly Law (AML) prohibits abusive behavior by IP owners. What qualified as abusive or anti-competitive behavior, however, was not explicitly defined in the AML. After a lengthy drafting process, the State Administration for Industry and Commerce (SAIC) issued the Provisions on Prohibition of Abuse of Intellectual Property Rights to Eliminate or Restrict Competition (AML IPR Regulation) in April 2015. Of particular interest to foreign IP owners are the articles addressing patent pools and standard-essential patents (SEPs). The regulations define abusive behavior by a pool member to include: (1) restricting another member from licensing independently of the patent pool; (2) restricting pool members or licensees from independently developing technologies; (3) forcing licensees to grant back improvements; and (4) forbidding licensees from challenging the validity of licensed patents.

It is worthwhile to note that, while the prohibition on forced grant backs may seem unremarkable from an antitrust perspective, when combined with China's indigenous innovation policy, the prohibition favors Chinese

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counterparts of foreign-invested joint ventures. Specifically, the indigenous policy seeks to “enhanc[e] original innovation through co-innovation and re-innovation based on the assimilation of imported technologies.” In other words, the indigenous innovation policy encourages domestic companies to assimilate and improve the technology of foreign partners as a strategic goal. At the same time, the AML IPR Regulation prohibits any forced grant back (to the foreign licensor) of the enhanced technology. The end result is encouragement for Chinese companies to harvest foreign technology, enhance the harvested technology, develop IP assets from the enhancement and thereby erect barriers or to otherwise seek licensing revenues from the licensor of the foreign technology.

The Chinese courts have also enforced the AML in ways that apparently favor domestic entities. For example, in the well-known case of *Huawei v. InterDigital*, the Guangdong High Court in 2014 held that InterDigital, a U.S.-based patentee, violated the AML and its FRAND commitments by suing Huawei in the United States while patent-licensing negotiations were ongoing. To the alarm of many observers, the Guangdong High Court remarked that “Huawei is good at using antitrust laws as a counter-weapon, which other Chinese companies should study.” The court added that “domestic enterprises [should] break through technical barriers in the development of space for their own gain, through bold use of antitrust litigation.” The High Court therefore has expressly encouraged domestic companies to use the AML against foreign competitors, including those who enforce foreign patents against Chinese companies outside China.

Another well-known case concerning AML enforcement is the investigation of Qualcomm by the National Development and Reform Commission (NDRC). In 2015, the NDRC concluded its investigation by fining Qualcomm US\$975 million (or 8 percent of Qualcomm’s annual revenues from China in the prior year) for engaging in various anti-competitive behaviors. These included abusing its market dominance and charging excessive royalties. Significantly, the NDRC concluded that any holder of SEPs should be deemed to have market dominance. At the same time, the NDRC did not explicitly identify any objective standards for determining excessiveness, making it more difficult for SEP owners to determine what constitutes reasonable royalty.

The overall effect of the indigenous innovation policy, the five-year plans, and the judicial and administrative enforcement of the AML (notably against foreign IP owners) indicates that China’s carefully orchestrated web of IP policies is working as intended—to tip the global IP balance in China’s favor. As Chinese companies step farther into the global spotlight and increase their brand recognition (e.g., DJI drones, Huawei phones, and Faraday Future electric cars), and as foreign companies continue to pursue growth in the Chinese consumer market, it is more important than ever to invest resources to develop and implement a successful Chinese IP strategy.

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