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## Why the 2020 U.S.-China Trade Agreement Needs Anticorruption Provisions for the Protection of Intellectual Property

Daniel C.K. Chow

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## Why the 2020 U.S.-China Trade Agreement Needs Anticorruption Provisions for the Protection of Intellectual Property

### Cover Page Footnote

BA, JD, Yale University. Bazler Chair in Business Law, The Ohio State University Michael E. Moritz College of Law. Thanks to Thomas J. Schoenbaum for his helpful comment and to Natasha Landon, Moritz Reference Librarian, and Amy Pratt, Moritz 2L, for their assistance with this article.

**WHY THE 2020 U.S.-CHINA TRADE AGREEMENT NEEDS ANTI-CORRUPTION PROVISIONS FOR THE PROTECTION OF INTELLECTUAL PROPERTY**

DANIEL C.K. CHOW\*

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INTRODUCTION

On January 15, 2020, the United States and the People’s Republic of China (PRC or China) signed Phase I of the U.S.-China Economic and Trade Agreement (USCTA), which suspended a two-year trade war between the world’s two largest economies.<sup>1</sup> Proclaimed by the United States as a breakthrough, the USCTA contains commitments by China to purchase \$200 billion in U.S. goods and services and to implement substantial new protections for U.S. intellectual property (IP) rights.<sup>2</sup> Aside from China’s purchase commitments, the most touted parts of the USCTA are China’s new comprehensive commitments on intellectual property and its new dispute resolution mechanism.<sup>3</sup> The first two chapters of the USCTA deal exclusively with IP rights, with a focus on trade secrets and technology transfer.<sup>4</sup> These provisions show a primary focus on criminal enforcement and also promote

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\* BA, JD, Yale University. Bazler Chair in Business Law, The Ohio State University Michael E. Moritz College of Law. Thanks to Thomas J. Schoenbaum for his helpful comment and to Natasha Landon, Moritz Reference Librarian, and Amy Pratt, Moritz 2L, for their assistance with this article.

1 Ana Swenson & Alan Rappeport, *Trump Signs China Trade Deal, Putting Economic Conflict on Pause*, N.Y. TIMES (Jan. 15, 2020), <https://www.nytimes.com/2020/01/15/business/economy/china-trade-deal.html>. The formal name of the agreement is the Economic and Trade Agreement Between the Government of the United States and the Government of the People’s Republic of China, Jan. 15, 2020, [hereinafter USCTA].

2 See USCTA, *supra* note 1, chs. 1–2 (“Intellectual Property” and “Technology Transfer”); see also *id.*, ch. 1, § B (“The United States emphasizes trade secrets protection.”).

3 *Id.*, ch. 1.

4 *Id.*, chs. 1 & 2.

enforcement through civil litigation and administration action.<sup>5</sup> Under the Trump Administration, the United States has vowed to make enforcement of its IP rights a top priority.<sup>6</sup>

As a matter of procedural law, the USCTA has created the ultimate enforcement weapon of IP rights for the United States.<sup>7</sup> For more than two decades, previous U.S. administrations had relied on informal arrangements such as a Memorandum of Understanding (MOU) and high-level dialogues to address U.S. concerns about protection for IP rights.<sup>8</sup> The major flaw in this approach was that these arrangements lacked a formal dispute resolution mechanism and provided no means to enforce China's promises.<sup>9</sup> When China broke its promises to protect IP, the U.S. response was to enter into another MOU and only see this frustrating slow dance with China repeat itself.<sup>10</sup> Under the Trump Administration, the United States has adopted a more bellicose attitude towards China that is embodied in the USCTA.

In contrast with the informality of prior arrangements, the USCTA has the formality and structure of a treaty and contains a new and path-breaking dispute resolution mechanism.<sup>11</sup> Under all prior U.S. trade agreements, the parties submitted disputes to a neutral and independent arbitration tribunal or to the World Trade Organization (WTO).<sup>12</sup> Under the USCTA, no third-party tribunal has been established, and no recourse to the WTO is possible.<sup>13</sup> The parties are to resolve disputes face-to-face. As Robert Lighthizer, the United States Trade Representative (USTR), has declared, "The only arbitrator I trust is myself."<sup>14</sup>

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5 See generally *id.*; see *infra* Part II.A.1.d.ii.

6 U.S. INTEL. PROP. ENFORCEMENT COORDINATOR, ANNUAL INTELLECTUAL PROPERTY REPORT TO CONGRESS 11 (2019).

7 This does not mean, however, that the procedural weapon created by the USCTA is lawful under international law. To the contrary, the USCTA dispute resolution mechanism is in violation of several key tenets of the World Trade Organization's General Agreement on Tariffs and Trade and its Dispute Settlement Understanding. See Daniel C.K. Chow, *A New and Controversial Approach to Dispute Resolution Under the U.S.-China Trade Agreement of 2020*, 26 HARV. NEGOT. L. REV. 31, 53-55 (2020). It would, however, be futile for China to file a complaint in the WTO because the United States has already disabled the WTO dispute settlement system. See *id.* at 48. China's obligation to purchase \$200 billion in goods and services is also in violation of the WTO. See *id.* at 33.

8 See *infra* Part I.A.

9 There are no provisions for dispute resolution in the 1992 U.S.-China MOU on intellectual property. See Memorandum of Understanding Between the Government of the People's Republic of China and the Government of the United States of America on the Protection of Intellectual Property (1992), [https://tcc.export.gov/Trade\\_Agreements/All\\_Trade\\_Agreements/exp\\_005362.asp](https://tcc.export.gov/Trade_Agreements/All_Trade_Agreements/exp_005362.asp) [hereinafter 1992 MOU].

10 OFF. OF U.S. TRADE REPRESENTATIVE, U.S. FACT SHEET FOR THE 27TH U.S.-CHINA JOINT COMMISSION ON COMMERCE AND TRADE – FACT SHEET (2016); David J. Lynch, *Trump Signs Partial Economic Deal with China, Calls Trade Pact a 'Momentous Step'*, THE WASHINGTON POST (Jan. 15, 2020, 9:00PM), [https://www.washingtonpost.com/business/economy/trumps-new-china-deal-cements-emergence-of-managed-trade/2020/01/15/7892c446-372b-11ea-bf30-ad313e4ec754\\_story.html](https://www.washingtonpost.com/business/economy/trumps-new-china-deal-cements-emergence-of-managed-trade/2020/01/15/7892c446-372b-11ea-bf30-ad313e4ec754_story.html).

11 What is referred to as a treaty under international law can be either a treaty or an executive agreement under U.S. law. As a technical matter, the USCTA is an executive agreement that the President or its delegate, the United States Trade Representative (USTR), can enter into without the need for subsequent congressional approval. The dispute resolution provisions of the USCTA are contained in Chapter 7 of the USCTA, *supra* note 1 ("Bilateral Evaluation and Dispute Resolution").

12 Chow, *supra* note 7, at 35, 45.

13 *Id.* When the United States enters into a trade agreement, the agreement may contain treaty obligations as well as provisions incorporating obligations under the WTO agreements. When a dispute involves WTO obligations, the parties may choose to resolve them either under the treaty dispute resolution mechanism or the WTO dispute settlement system. *Id.* at 42.

14 *Id.* at 53.

Under the USCTA, the United States has a unilateral right to declare China in breach of its treaty and WTO obligations.<sup>15</sup> Moreover, under the USCTA, the United States also has the unilateral right to impose trade sanctions on China.<sup>16</sup> The USCTA forbids China from retaliating against the United States and only allows China the option of withdrawing from the treaty.<sup>17</sup> If China withdraws from the USCTA, however, the United States could reinstate the punitive tariffs that created the trade war that the USCTA suspended.<sup>18</sup> Once the United States finds China in breach, China will have to suffer tariffs no matter what it decides. The United States will be able to impose tariffs on China either by invoking the USCTA dispute resolution mechanism or by reinstating the tariffs that the USCTA suspended.

If China finds itself trapped and seeks to raise a complaint in the WTO against the United States, China will find that such a recourse will be futile.<sup>19</sup> Before entering into the USCTA, the United States had already paralyzed the WTO dispute settlement mechanism, hurling the WTO into a life-or-death crisis.<sup>20</sup> The WTO was made to suffer this grievous blow because it committed the malfeasance of repeatedly ruling in WTO dispute settlement cases against the United States.<sup>21</sup> China's only recourse is to go through the USCTA dispute resolution mechanism, which is under complete U.S. control, or to withdraw and suffer the consequences. The United States has boxed China into a no-win situation and has closed off all exits.<sup>22</sup>

While the USCTA creates a path-breaking procedure for dispute resolution that has created a formidable weapon for the United States, the same cannot be said about the substantive provisions of the USCTA. For the USCTA to become truly effective, the United States must also have substantive provisions that address the major concerns of MNCs in IP enforcement through China's legal system that were not successfully addressed by prior U.S. approaches. Otherwise, MNCs will continue to be frustrated in their day-to-day operations by IP violations and by hurdles to effective on-the-ground enforcement when using judicial and administrative authorities in China. While the USCTA is the ultimate enforcement weapon, using the USCTA means elevating a dispute to the bilateral level due to some breakdown in enforcement of PRC laws on the ground level. Elevating the dispute could result in trade sanctions imposed by the United States and the attendant increased tensions between the two nations. If the enforcement of China's IP laws on the ground functioned smoothly and effectively, there would be no dispute that would need to be resolved on the bilateral level or otherwise. Ensuring the effective enforcement of China's IP laws on the ground is thus a critical element to the overall success of the USCTA.

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15 *Id.* at 36, 59.

16 *Id.* at 53.

17 *Id.* at 36.

18 *See Trump: U.S. to Suspend Scheduled Tariffs After Reaching Deal with China*, REUTERS (Dec. 13, 2019, 10:41 AM), <https://www.reuters.com/article/us-usa-trade-china-trump/trump-us-to-suspend-scheduled-tariffs-after-reaching-deal-with-china-idUSKBN1YH1T3>; Thomas Franck, *Trump Halts New China Tariffs and Rolls Back Some of the Prior Duties on \$120 Billion of Imports*, CNBC (Dec. 13, 2019, 3:53 PM), <https://www.cnbc.com/2019/12/13/trump-says-25percent-tariffs-will-remain-but-new-china-duties-will-not-take-effect-sunday.html>.

19 Chow, *supra* note 7 at 36.

20 *Id.* at 36-37.

21 *Id.* at 34-35.

22 The U.S. strategy is clever and effective, but that does not mean that it is lawful. *See id.* at 53-60.

At present, the USCTA contains an omission of one of the most important barriers to effective IP enforcement on the ground in China. MNCs have been plagued for years by systemic corruption by both government and business entities that create barriers to effective enforcement of their IP rights.<sup>23</sup> Problems of corruption occur in different variations in both criminal and civil enforcement and when dealing with government or business entities. Problems of corruption are especially serious in three illustrative areas that are the focus of this article.

First, in the case of the criminal enforcement of trade secrets—one of the primary areas of focus in the USCTA—issues of corruption by government entities are especially serious, as they arise at the threshold level in the criminal enforcement procedure.<sup>24</sup> In addition, while all corruption issues create headaches, corruption issues involving enforcement of trade secrets is a “bet the company” type of problem because it implicates liability under the U.S. Foreign Corrupt Practices Act (FCPA), which prohibits bribes paid to foreign officials.<sup>25</sup> In response to demands for payments from PRC enforcement authorities for the performance of their services, MNCs routinely make these payments either directly or through private investigation agencies under the employ of MNCs.<sup>26</sup> While these payments may be tolerated by the PRC government, the U.S. Department of Justice (USDOJ) is an aggressive enforcer of the FCPA and could consider these payments to be illegal bribes.<sup>27</sup> The USDOJ has its own mandate that is independent of the mandate espoused by the United States Trade Representative who championed the USCTA. An FCPA investigation is a major disruption of a company’s business, and the prospect of the draconian sanctions under the FCPA, which include imprisonment of company officers, is enough to create major waves of fear and anxiety in corporate boardrooms in the United States and other countries.<sup>28</sup> It is ironic that the major protagonist for MNCs in enforcing their trade secrets might not be the PRC government but the U.S. government.

Second, aside from the issue of illegal payments, China’s judicial system is notorious for the corrupt use by parties of ex parte contacts with judges in order to influence the result of legal proceedings.<sup>29</sup> These types of ex parte contacts are commonly used and can be highly effective in influencing the result of an IP case.<sup>30</sup> In most instances, the party will not approach the frontline judge directly, but will instead approach a higher level government official or a higher level judge that sits on the appellate court overseeing the trial.<sup>31</sup> The party will ask the

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23 CKGSB Contributor, *China Becomes Tougher for MNCs, But All Is Not Lost*, FORBES (Sept. 10, 2014, 10:00AM), <https://www.forbes.com/sites/ckgsb/2014/09/10/china-becomes-tougher-for-mncs-but-all-is-not-lost/#3b6a04353648>

24 See *infra* Part II.A.

25 See 15 U.S.C. § 78dd-1 (2018) (anti-bribery provision).

26 This practice is based on the personal experience of the author, who worked as an in-house lawyer for a large multinational company with substantial IP assets in China. The author has also discussed this practice with IP lawyers currently working in China.

27 See Joe Palazzolo, *From Watergate to Today, How FCPA Became So Feared*, THE WALL ST. J. (Oct. 2, 2012, 12:01 AM), <https://www.wsj.com/articles/SB10000872396390444752504578024791676151154>.

28 See *id.*

29 Jerome A. Cohen, *A Looming Crisis for China’s Legal System*, FOREIGN POLICY (Feb. 22, 2016, 10:15 AM), <https://foreignpolicy.com/2016/02/22/a-looming-crisis-for-chinas-legal-system/>.

30 *Id.*

31 Xin He & Kwai Hang Ng, “It Must Be Rock Strong!” *Guanxi’s Impact on Judicial Decision Making in China*, 65 AM. J. COMP. L. 841, 855 (2017).

higher level official or judge to exert influence on the lower level judge.<sup>32</sup> Skillful influence peddlers never use money, but rely on professional or personal contacts (or “guanxi”) with the higher level judge or official.<sup>33</sup> Under current PRC law, such influence peddling falls into a gray area of the law; current PRC Criminal Law defines bribery as requiring the exchange of “money” or “property” and excludes the use of intangible benefits.<sup>34</sup> The use of *guanxi* has a venerable history in China, long predating the PRC, which may be one explanation for why it is so prevalent.<sup>35</sup> Many observers find that the use of *guanxi* is the most serious problem of corruption in the PRC civil court system.<sup>36</sup> There is a high probability that a defendant in an IP litigation brought by an MNC will attempt to influence the outcome of the case through ex parte contacts with the judge.<sup>37</sup>

Third, in the case of the growing problem of counterfeit and infringing goods sold through the Internet, online counterfeiters frequently give business bribes to employees at PRC e-commerce platforms.<sup>38</sup> In exchange, the e-commerce platforms give the operators, i.e., online merchants, favorable treatment such as the ability to delete negative consumer comments.<sup>39</sup> Employees at e-commerce platforms will also tip off internet counterfeiters that a complaint has been filed or that the counterfeiters are being investigated by Chinese authorities.<sup>40</sup> One area where these illicit arrangements are most pernicious is registration. In exchange for business bribes, e-commerce platforms are notoriously lax in conducting entity registration and verification of new online operators.<sup>41</sup> Instead, counterfeiters are allowed to use false names and addresses and can disappear into the “vast expanse of cyberspace” at the first sign of trouble—only to reappear in short order under a new name and address.<sup>42</sup> This is particularly harmful because China has a sophisticated system of entity verification that if used properly can accurately identify, locate, and deter counterfeiters.<sup>43</sup> The rigorous enforcement of these registration and verification requirements should have an immediate salutary effect in deterring counterfeiters who harbor a great fear of capture and arrest.

Although these problems have proven to be intractable in the past, and although the current version of Phase I of the USCTA does not address these issues, there is still an opportunity to address them. The USCTA presents an unprecedented opportunity to address these endemic issues because the United

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32 *Id.*

33 *Id.* at 841, 855, 864–65.

34 *See infra* text accompanying note 167.

35 *See, e.g.*, SOCIAL CONNECTIONS IN CHINA: INSTITUTIONS, CULTURE, AND THE CHANGING NATURE OF GUANXI 3–20 (Thomas Gold et al. eds., 2002); John H. Dunning & Changsu Kim, *The Cultural Roots of Guanxi: An Exploratory Study*, 30 WORLD ECON. 329, 329–30 (2007).

36 *See* Cohen, *supra* note 29.

37 A recent study shows that litigants attempt to use ex parte contacts to influence the result of judicial cases in over half of all cases. *See* He & Ng, *supra* note 31, at 842.

38 *See* Daniel C.K. Chow, *Alibaba, Amazon, and Counterfeiting in the Age of the Internet*, 40 NW. J. INT'L L. & BUS. 157, 181–82 (2020) [hereinafter Chow, *Counterfeiting in the Age of the Internet*].

39 *Id.*

40 *Id.* at 182.

41 *Id.* at 193.

42 *Id.* at 186.

43 *Id.* at 192–93.

States can directly affect China's domestic legislation through the USCTA.<sup>44</sup> Under the treaty, China has an obligation to implement legislation affecting the treaty provision or otherwise be subject to sanctions.<sup>45</sup>

While Phase I of the USCTA has now been completed, the United States and China are in the process of negotiating Phase II to address some of the remaining and most contentious issues that were left out of the earlier negotiations.<sup>46</sup> The United States could include new provisions to address these corruption issues as an amendment or revision to the Phase I agreement or by new provisions in the Phase II agreement.

This article will proceed as follows. Part I examines the role of the USCTA in promoting IP protection in China. Learning from China's past failure to follow through on its IP commitments, the USCTA allows the United States to unilaterally declare China to be in breach of its USCTA and WTO obligations. The United States can also unilaterally impose sanctions on China, whose only recourse is to withdraw from the USCTA. As a matter of procedural law, the USCTA provides every possible advantage to the United States. Part II will then examine major problems of government and business corruption in the IP enforcement process in three areas: demands for payments by PRC enforcement authorities, the use of ex parte contacts to influence the results of civil litigation, and the use of business bribes in e-commerce platforms that have contributed to an explosion in online sales of counterfeit products. Part III explains that the United States and IP owners still have the opportunity to address these substantive issues by supplementing the USCTA's IP sections with effective anti-corruption provisions. Part III also proposes guidelines and suggestions for the drafting of these provisions.

## I. THE USCTA'S NEW APPROACH TO IP PROTECTION

The first chapter of the USCTA deals with a group of longstanding IP issues that the United States has thrust to the top of its IP agenda with China. Chief among these issues is trade secret protection, which has emerged as the most urgent IP issue for MNCs in China.<sup>47</sup> Other issues concern trademark squatting,<sup>48</sup> a patent term extension to compensate for delays in the approval

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44 The USCTA creates direct obligations on China to enact domestic legislation. This obligation can be inferred from the language of the treaty. For example, Article 1.3:2 provides "China shall define 'operators' in trade secret misappropriation to include all natural persons, groups of persons, and legal persons." USCTA, *supra* note 1, art. 1.3:2. China has a duty to define "operators" as so prescribed in its domestic legislation.

45 *Id.*

46 See Jessica Bursztynsky, *Trump Trade Advisor Peter Navarro Lists What the US Wants from China in 'Phase Two' Trade Deal*, CNBC (Jan. 16, 2020, 8:14 AM), <https://www.cnbc.com/2020/01/16/peter-navarro-lists-usdemands-from-china-in-phase-two-trade-deal.html>.

47 See Daniel C.K. Chow, *Navigating the Minefield of Trade Secrets Protection in China*, 47 VAND. J. TRANSNAT'L L. 1007, 1008 (2014) [hereinafter Chow, *Navigating the Minefield of Trade Secrets*]. For trade secrets provisions, see USCTA, *supra* note 1, arts. 1.3–1.9.

48 USCTA, *supra* note 1, art. 1.24 (bad faith registration of trademarks). For a discussion of this issue, see Daniel C.K. Chow, *Trademark Squatting and the Limits of the Famous Marks Doctrine in China*, 47 GEO. WASH. INT'L L. REV. 57 (2015) [hereinafter Chow, *Trademark Squatting*].



process,<sup>49</sup> counterfeit medicines,<sup>50</sup> and counterfeits sold on e-commerce platforms.<sup>51</sup> Although the United States has complained about these issues for years, China has failed to make sufficient progress to appease the United States, leading the Trump Administration to adopt a radical new approach under the USCTA.

#### A. APPROACHES UNDER PREVIOUS U.S. ADMINISTRATIONS

Soon after China opened its economy to foreign investment from MNCs in the 1980s, the United States began to complain about problems concerning IP protection and enforcement.<sup>52</sup> During this initial wave of foreign investment in MNCs in China, most MNCs sought to establish a joint venture with a local partner that could navigate the local legal and political environment.<sup>53</sup> When MNCs establish a joint venture in China, the business entity begins as an empty vessel that must receive essential inputs in the form of capital and technology.<sup>54</sup> For example, when Procter & Gamble (P&G) set up its first joint venture in 1988 in Guangzhou in Southern China,<sup>55</sup> P&G also injected capital and transferred technology in the form of patents, trademarks, and trade secrets to the joint venture.<sup>56</sup> The capital is used to purchase land-use rights, buildings, machinery, and equipment.<sup>57</sup> At this point, the joint venture would have all of the physical structures and tools necessary to manufacture P&G's products; however, the joint venture still needed access to P&G's technology. Without access to P&G's proprietary technology, the joint venture would lack the know-how to manufacture the shampoo, laundry detergent, and toothpaste that the company sought to produce and sell in China.<sup>58</sup> In a pattern that would be repeated many times, almost as soon as P&G's joint venture began production, illegal underground factories sprouted up nearby.<sup>59</sup> These underground factories

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49 USCTA, *supra* note 1, art. 1.12 (patent term extension). For a discussion of this issue, see Daniel C.K. Chow, *Three Major Problems Threatening Multi-National Pharmaceutical Companies Doing Business in China*, 19 COLUM. SCI. & TECH. L. REV. 46 (2017).

50 USCTA, *supra* note 1, art. 1.18 (counterfeit medicines); *see* Chow, *supra* note 49.

51 USCTA, *supra* note 1, art. 1.13–1.4 (online infringement and counterfeits). For a discussion of this issue, *see* Chow, *Counterfeiting in the Age of the Internet*, *supra* note 38.

52 *See* RAMI M. OLWAN, *INTELLECTUAL PROPERTY AND DEVELOPMENT: THEORY AND PRACTICE* 71–72 (2013); Bryan Mercurio, *The Protection and Enforcement of Intellectual Property in China since Accession to the WTO: Progress and Retreat*, CHINA PERSPECTIVES, July 2012, at 23, 24.

53 DANIEL C.K. CHOW & THOMAS J. SCHOENBAUM, *INTERNATIONAL BUSINESS TRANSACTIONS: PROBLEMS, CASES, AND MATERIALS* 499 (4th ed. 2020).

54 *Id.* at 503.

55 *Procter & Gamble Announces Joint Venture with China*, UPI (July 6, 1988), <https://www.upi.com/Archives/1988/07/06/Procter-Gamble-announces-joint-venture-with-China/2947584164800/>.

56 The author was head of the legal department for P&G's China operations and was involved firsthand in drafting joint venture agreements and in enforcing the company's intellectual property rights.

57 CHOW & SCHOENBAUM, *supra* note 53, at 503.

58 *Id.*

59 Daniel C.K. Chow, *Anti-Counterfeiting Strategies of Multinational Companies in China: How a Flawed Approach is Making Counterfeiting Worse*, 41 GEO. J. INT'L L. 749, 763 (2010) [hereinafter Chow, *Anti-Counterfeiting Strategies*]. While serving as in-house counsel for a multinational company based in China, the author determined that relatives or friends of employees at the MNC would help set up an illegal factory and would obtain IP and business information from the employees.

flooded the market with counterfeits and knock-offs of P&G's products.<sup>60</sup> Problems of rampant counterfeiting and piracy arising from China's opening to foreign investment in the 1980s led the United States to begin a Section 301 investigation of China's IP practices in April 1991.<sup>61</sup>

In 1992, the United States and China entered into a Memorandum of Understanding (MOU) on the Protection of Intellectual Property to address and resolve these IP disputes.<sup>62</sup> The MOU established an approach that the United States followed until the United States broke new ground with the USCTA in 2020. Although the terms are used imprecisely, under international law, an MOU is considered to be an agreement that is less formal than a treaty, shorter in length, and is sometimes considered to be a general framework under which further agreements will be reached.<sup>63</sup> As a reflection of the informal nature of the MOU, in 1995 China responded to U.S. demands in the 1992 MOU in a letter written to the USTR.<sup>64</sup> After China joined the World Trade Organization (WTO) in 2001,<sup>65</sup> the United States and China continued to work on an informal basis to deal with IP and other trade issues. During the first two decades of the new millennium, the United States worked on these issues through bilateral dialogues, including the U.S.-China Joint Commission on Commerce and Trade (JCCT) and the U.S.-China Strategic & Economic Dialogue (S&ED), to attempt to address some of the U.S. concerns.<sup>66</sup> At times, the discussion on intellectual property in the dialogues would result in an agreement, such as the 2011 Cooperation Framework Agreement signed in Chengdu, China.<sup>67</sup> At other times, China would make specific commitments on intellectual property at the end of a round of discussions in the JCCT or the S&ED.<sup>68</sup>

The most serious flaw in this informal approach is that commitments under the JCCT, the S&ED, MOUs, and other agreements lacked any dispute resolution and enforcement procedure. As a result, the United States was left

60 XIAOWEN TIAN, *MANAGING INTERNATIONAL BUSINESS IN CHINA* 161 (2016).

61 WAYNE M. MORRISON, CONG. RESEARCH SERV., IF10708, *ENFORCING U.S. TRADE LAWS: SECTION 301 AND CHINA* (2018), [https://digital.library.unt.edu/ark:/67531/metadc1248239/m2/1/high\\_res\\_d/IF10708\\_2018Aug02.pdf](https://digital.library.unt.edu/ark:/67531/metadc1248239/m2/1/high_res_d/IF10708_2018Aug02.pdf).

62 1992 MOU, *supra* note 9.

63 See generally Aaron Messing, Note, *Nonbinding Subnational International Agreements: A Landscape Defined*, 30 *GEO. ENV'T. L. REV.* 173, 188–90 (2018).

64 People's Republic of China Intellectual Property Rights Memorandum of Understanding—1995 Action Plan (Feb. 26, 1995), [https://tcc.export.gov/Trade\\_Agreements/All\\_Trade\\_Agreements/exp\\_005363.asp](https://tcc.export.gov/Trade_Agreements/All_Trade_Agreements/exp_005363.asp). The Letter contained an appendix containing a more detailed action plan to change to China's IP laws. *Id.*

65 See *China and the WTO*, WORLD TRADE ORG., [https://www.wto.org/english/thewto\\_e/countries\\_e/china\\_e.htm](https://www.wto.org/english/thewto_e/countries_e/china_e.htm) (last visited June 1, 2020) (“China has been a member of the WTO since 11 December 2001.”).

66 OFF. OF U.S. TRADE REP., *supra* note 10; EXEC. OFF. OF THE PRESIDENT, STATEMENT ON BILATERAL MEETING WITH PRESIDENT HU OF CHINA, (2009); U.S. DEP'T OF THE TREASURY, *U.S.-CHINA STRATEGIC ECONOMIC DIALOGUE* (2009).

67 U.S. DEP'T OF STATE, *AGREEMENT BETWEEN THE UNITED STATES OF AMERICA AND CHINA* (2011), <https://www.state.gov/wp-content/uploads/2019/02/11-1121.1-China-Trade-Intellect-Property-Rights-Cooperation.pdf>.

68 See OFF. OF THE U.S. TRADE REP., *FINDINGS OF THE INVESTIGATION INTO CHINA'S ACTS, POLICIES, AND PRACTICES RELATED TO TECHNOLOGY TRANSFER, INTELLECTUAL PROPERTY, AND INNOVATION UNDER SECTION 301 OF THE TRADE ACT OF 1974*, at tbl.I.1 (2018), <https://ustr.gov/sites/default/files/Section%20301%20FINAL.PDF> (“China's Bilateral Commitments Relating to Technology Transfer, 2010–2016”).

with no formal means of holding China to its commitments, which went largely unfulfilled. This process led to years of U.S. frustration:

As is happening today, IP got injected into the trade process, but the waltz was long and slow. The USTR would complain of China's failure to halt piracy of US-created goods; the two countries would enter into a MOU [memorandum of understanding] in which China would agree to clean up its act; three years later the USTR would identify continuing violations and come back and say, "this time we really mean it;" and the two countries would enter into another, more detailed MOU, and so on.<sup>69</sup>

The United States' dissatisfaction with China as it danced around its commitments was not limited to China's IP practices but extended to China's other trade commitments. The United States believed that China was not following through on its legal commitments under the WTO in many different areas of trade in addition to intellectual property.<sup>70</sup> With the ascension of Donald J. Trump to the U.S. presidency in 2016, U.S. criticism of China took on a decidedly more bellicose tone. In 2017, U.S. frustration with China reached a boiling point, resulting in the following warning from the Trump Administration:

For more than 15 years, the United States has relied on cooperative high-level dialogues to effect meaningful and fundamental changes in China's state-led, mercantilist trade regime. These efforts have largely failed. *Accordingly, the United States intends to focus its efforts on enforcement going forward. The United States is determined to use every tool available to address harmful Chinese policies and practices.*<sup>71</sup>

The United States had announced that henceforth in its relationship with China, it would forgo the carrot of negotiation in favor of brandishing the stick of enforcement.

#### B. APPROACH UNDER THE USCTA

True to its word, the United States adopted an enforcement-based approach to IP protections under the USCTA. The USCTA has the structure and formality of a treaty, not the relaxed approach of an MOU, and offers a radical new approach to dispute resolution and enforcement. The longstanding practice of the United States under prior trade agreements and bilateral investment treaties was to establish an independent and neutral arbitration tribunal that had the full

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69 Sharon Driscoll, *Intellectual Property and China: Is China Stealing American IP*, SLS BLOGS: LEGAL AGGREGATE (Apr. 10, 2018), <https://law.stanford.edu/2018/04/10/intellectual-property-china-china-stealing-american-ip/> (interview with Professor Paul Goldstein).

70 OFF. OF U.S. TRADE REP., 2017 REPORT TO CONGRESS ON CHINA'S WTO COMPLIANCE 3 (2018), <https://ustr.gov/sites/default/files/files/Press/Reports/China%202017%20WTO%20Report.pdf>.

71 *Id.* at 25 (emphasis added).

power to rule against the United States.<sup>72</sup> Under prior trade agreements, whenever the dispute involved both a treaty and a WTO obligation, the complainant could choose to bring the claim either with the treaty arbitration tribunal or the WTO.<sup>73</sup>

Under USCTA, no dispute resolution tribunal is established.<sup>74</sup> The two nations are to resolve the dispute without the aid of a third party.<sup>75</sup> If the parties are unable to come to an agreement to resolve the dispute, the complaining party has the right to impose trade sanctions.<sup>76</sup> Although this right is available to either party, in practice, the United States will be the complaining party as all of the new obligations under the USCTA are imposed on China.<sup>77</sup> In addition, the complainant must bring all claims, including those involving WTO obligations arising under the treaty, under the USCTA process.<sup>78</sup>

The dispute resolution mechanism under the USCTA must be understood in the larger context of U.S. goals concerning the WTO dispute settlement system. On December 10, 2019, only about one month before the parties entered into the USCTA, the WTO dispute settlement system became crippled due to the actions of the United States.<sup>79</sup> Due to U.S. intransigence in refusing to approve new members to the Appellate Body to replace retiring members, the number of panel members fell below that necessary to convene a quorum.<sup>80</sup> As a result, the Appellate Body became paralyzed, and all decisions entered under the WTO dispute settlement system became effectively unenforceable.<sup>81</sup>

The United States decommissioned the Appellate Body due to its malfeasance in repeatedly ruling against the United States. According to the U.S. view, the Appellate Body betrayed an understanding reached with the United States that it would rule strictly in accordance with the text of the WTO

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<sup>72</sup> Chow, *supra* note 7 at 36.

<sup>73</sup> *Id.*

<sup>74</sup> See USCTA, *supra* note 1, at ch. 7 (“Bilateral Evaluation and Dispute Resolution”). The USCTA requires the establishment of a Bilateral Evaluation and Dispute Resolution “Arrangement” consisting of high-level trade officials from both parties. *Id.* at art. 7.2:1. No arbitration tribunal, however, is to be established. *Id.*

<sup>75</sup> *Id.* at art. 7.4.

<sup>76</sup> *Id.* at art. 7.4:4.

<sup>77</sup> A review of the USCTA reveals that all new obligations are imposed on China. At the end of many of the articles in Chapter imposing substantive obligations relating to IP, the article states: “The United States affirms that existing U.S. measures afford treatment equivalent to that provided for in this Article.” See, e.g., USCTA, *supra* note 1, at art. 1.3:3.

<sup>78</sup> There is no provision in USCTA Chapter 7, the dispute resolution chapter, for bring an action in the WTO. See generally USCTA, *supra* note 1.

<sup>79</sup> Understanding on Rules and Procedures Governing the Settlement of Disputes art. 17.1, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, 1869 U.N.T.S. 401, 33 I.L.M. 1125 (1994); Ken Roberts, *World Trade’s Demise Scheduled for Dec. 10*, FORBES (Nov. 27, 2019), <https://www.forbes.com/sites/kenroberts/2019/11/27/world-trades-demise-scheduled-for-dec-10/#a1d1d292412e>; Adam Behsudi & Finbarr Bermingham, *The End of World Trade as We Know It*, POLITICO (Nov. 20, 2019), <https://www.politico.com/news/2019/11/20/world-trade-end-donald-trump072257>.

<sup>80</sup> Chow, *supra* note 7 at 38.

<sup>81</sup> Daniel C.K. Chow, *U.S. Trade Infallibility and the Crisis in the World Trade Organization*, 2020 MICH. ST. L. REV. 599, 601, 610 (2020). A nation that violates any WTO agreement will be able to freeze the WTO dispute settlement process in its tracks so that any adverse WTO decision against it cannot be enforced. Once a WTO panel reaches a decision, the losing party can file an appeal to the Appellate Body. The WTO cannot adopt the decision until the appeal is completed which has now become impossible due to the paralysis of the Appellate Body. The decision is suspended indefinitely in a legal limbo and so cannot be enforced against the losing party. *Id.*

agreements;<sup>82</sup> instead, the Appellate Body engaged in unauthorized and illegitimate “judicial activism.”<sup>83</sup> The USCTA offers a parallel dispute resolution mechanism under which the United States can resolve both USCTA and WTO claims against China.<sup>84</sup> In an ominous development for the WTO, the USCTA indicates that the United States does not intend to repair the flaws of the WTO dispute settlement system, but to replace it with a process in new trade agreements that is under complete U.S. control.<sup>85</sup> The United States has delivered a decisive two punch body blow to the WTO: the United States first crippled the WTO dispute settlement mechanism and then created an alternative forum to deal with IP disputes with China that it dominates and controls.

The USCTA also offers an unprecedented opportunity for the United States to determine the content of China’s internal legislation. The USCTA creates treaty obligations on China that it must implement through domestic legislation.<sup>86</sup> For example, Article 1.3:2 of the USCTA states, “China shall define ‘operators’ in trade secret misappropriation to include all natural persons, groups of persons, and legal persons.”<sup>87</sup> Under the USCTA, China *must* enact or amend its laws to give effect to this provision or else be subject to trade sanctions.<sup>88</sup> This treaty mechanism now allows the United States to directly address the endemic problems of corruption by requiring detailed and specific domestic legislation in China using textual language drafted by the United States as guidelines, an opportunity that has never been available in the past.<sup>89</sup>

The result of the USCTA is that the United States has an uncontestable unilateral right to determine that China is in violation of its treaty and WTO obligations and to impose trade sanctions on China. Article 7.4:4(b) of the USCTA details this procedure:

If the Parties do not reach consensus on a response, the Complaining Party may resort to taking action based on facts provided during the consultations, including by suspending an obligation under this Agreement or by adopting a remedial measure in a proportionate way that it considers appropriate with the purpose of preventing the escalation of the situation and maintaining the normal bilateral trade relationship. If the Party Complained Against considers that the action by the Complaining Party pursuant to this subparagraph was taken in

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82 *Id.* at 627.

83 *Id.* at 627–31.

84 *Id.* at 626–31.

85 *Id.* at 635–36.

86 Under U.S. jurisprudence, the USCTA is a non-self-executing treaty, i.e. a treaty that has no direct effect within the legal system of the parties. *See* CHOW & SCHOENBAUM, *supra* note 53, at 35. The parties must implement the treaty’s obligations through domestic legislation. *Id.* By contrast, a self-executing treaty has direct effect within the domestic legal order of the parties and needs no domestic implementing legislation. *Id.* How does one determine whether the treaty is self-executing or non-self-executing? The most common approach is to examine the intent of the treaties as evidenced in the treaty language. *Id.*

87 USCTA, *supra* note 1, art. 1.3:2.

88 This language that “China shall define ‘operators’” indicates that this is a non-self-executing treaty. *Id.* The text of the treaty clearly contemplates that China will fulfill this obligation through a domestic legal rule. If China fails to implement the obligation, then China is in breach of the USCTA.

89 A detailed search of past agreements with China has not revealed any mechanism similar to this aspect of the USCTA in the past.

good faith, the Party Complained Against may not adopt a counter-response, or otherwise challenge such action. If the Party Complained Against considers that the action of the Complaining Party was taken in bad faith, the remedy is to withdraw from this Agreement by providing written notice of withdrawal to the Complaining Party.<sup>90</sup>

“Suspending an obligation” would include disregarding an agreed upon trade concession, such as the WTO tariff rate for Chinese goods as set forth in the United States’ tariff schedule.<sup>91</sup> Once the obligation is disregarded or suspended, the United States can raise the tariff above the WTO rate. A “remedial measure” referred to above includes the imposition of trade sanctions, such as punitive tariffs (i.e. tariffs in addition to the WTO tariff), a complete trade ban of all goods, or a quota (i.e. a numerical restriction on import trade volumes).<sup>92</sup> In response, China would be prohibited from taking retaliatory measures so long as the United States acted in good faith.<sup>93</sup> China’s only option is to withdraw from the USCTA.<sup>94</sup>

In the USCTA, the United States has now created an enforcement weapon for its IP rights against China that is far more potent than any that had previously existed. If the United States believes that China is in breach of any of the treaty’s IP provisions or WTO obligations, the United States can act unilaterally to impose trade sanctions on China. The USCTA forbids China from retaliating and allows China only the option of withdrawing from the USCTA. If China does withdraw, however, then the punitive tariffs that the United States suspended as a result of the USCTA could be then be reinstated. China is now trapped in a no-win situation in which punitive tariffs will be imposed no matter what China chooses to do. China is also boxed into using the USCTA to resolve its disputes as going through the WTO has now become futile.

## II. THE NEED FOR ANTI-CORRUPTION PROVISIONS IN THE USCTA

While the drafters of the USCTA created a powerful enforcement procedure, they overlooked major problems in the substantive provisions of the USCTA. Consistent with the overall U.S. emphasis on enforcement, the substantive provisions of the USCTA emphasize enforcement, with a particular focus on criminal enforcement.<sup>95</sup>

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90 USCTA, *supra* note 1, art. 7.4:4(b).

91 DANIEL C.K. CHOW & THOMAS J. SCHOENBAUM, INTERNATIONAL TRADE LAW: PROBLEMS, CASES, AND MATERIALS 88 (3d ed. 2017).

92 The variety of trade sanctions available to the United States in a putative trade emergency are set forth in 19 U.S.C. § 2253(a)(3) (A)–(C) (1994) (describing tariff increases and quantitative restrictions).

93 USCTA, *supra* note 1, art. 7.4:4(b).

94 *Id.*

95 The USCTA has at least seven provisions that deal with criminal enforcement. *See generally*, USCTA, *supra* note 1.

### A. *FCPA ISSUES*

The drafters of the USCTA's criminal provisions left a significant gap in the treaty by failing to deal with the pervasive and intractable problem of corruption in the PRC criminal legal system that has burdened IP owners for years. For IP owners, the most significant issue concerning corruption in China is not with ramifications in the PRC legal system, but with the U.S. legal system; the major protagonist in legal issues involving corruption is not the PRC government but the U.S. government. Corruption in the PRC criminal enforcement system implicates the U.S. Foreign Corrupt Practices Act,<sup>96</sup> which is enforced by two U.S. government authorities: the U.S. Department of Justice (USDOJ) and the Securities and Exchange Commission (SEC).<sup>97</sup>

The anti-bribery provisions of the FCPA prohibit a U.S. company, its officers, and employees from making payments to a foreign official for the purpose of obtaining or retaining business.<sup>98</sup> This provision is routinely implicated in the use of the PRC criminal enforcement system by IP brand owners.

#### 1. *Payments to China's Authorities in Trade Secrets Enforcement*

##### a. *The Public Security Bureaus*

Under PRC law, the Public Security Bureau (PSB), China's police, must initiate any criminal case by beginning an investigation, including criminal trade secrets and other IP cases.<sup>99</sup> The PSB is charged with protecting PRC citizens from crime and in maintaining public safety.<sup>100</sup> The PSB's first priority is on the

<sup>96</sup> See generally, USCTA, *supra* note 1.

<sup>97</sup> Foreign Corrupt Practices Act, 15 U.S.C. § 78dd-1, et seq. (1977). The USDOJ enforces the anti-bribery provisions, 15 U.S.C. § 78dd-1, -2, -3, and the SEC enforces the books and records provision, 15 U.S.C. § 78m(b).

<sup>98</sup> 15 U.S.C. § 78dd-2 provides:

It shall be unlawful for any domestic concern . . . or for any officer, director, employee, or agent of such domestic concerns or any stockholder thereof acting on behalf of such domestic concern, to make use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay, authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of anything of value to . . . any foreign official . . . in order to assist such domestic concern in obtaining or retaining business . . .

In outline form, the statute, 15 U.S.C. § 78dd-1, -2, -3, prohibits:

- (1) Issuers, domestic concerns, and any person
- (2) from making the use of interstate commerce
- (3) corruptly
- (4) in furtherance of an offer or payment of anything of value
- (5) to a foreign official
- (6) for the purpose of influencing any act of that foreign official in violation of his or her duty in order to obtain or retain business.

The FCPA can present particularly treacherous issues for MNCs in China. See Daniel C.K. Chow, *China Under the Foreign Corrupt Practices Act*, 2012 WIS. L. REV. 573 (2012).

<sup>99</sup> Zonghua Renmin Gongheguo Gong'an Xingzheng Chufa Fa (中華人民共和國公安行政處罰法) [Public Security Administrative Punishment Law of the People's Republic of China] (adopted at the 17th meeting of the standing committee of the Tenth National People's Congress on Aug. 28, 2005, effective Mar. 1, 2006) art. 77, translated at <https://www.cecc.gov/resources/legal-provisions/public-security-administration-punishment-law-chinese-text> [hereinafter PRC Public Security Administrative Punishment Law].

<sup>100</sup> The Ministry of Public Security's responsibilities are "[t]o prevent, stop, and investigate criminal activities; [t]o fight against terrorist activities;" and "[t]o maintain stability and order[.]" among

prevention and punishment of violent crimes, as these activities threaten public safety and security.<sup>101</sup> As a consequence, the PSB views economic crimes, such as theft of trade secrets from wealthy MNCs or the sale of counterfeit products, as a lower priority.<sup>102</sup> As the PSB perceives its primary role to protect society from violent crime, the PSB can be reluctant to pursue economic crimes where the only “victim” is an MNC with deep pockets that has suffered a financial loss that means lower profits.<sup>103</sup> As a result, the PSB will usually ask an MNC for a “case fee” in order to initiate a criminal case.<sup>104</sup> The case fee is framed as an administrative fee to cover the costs of the PSB’s investigation.<sup>105</sup> For example, a criminal investigation might involve travel and expenses such as hotel and meals.<sup>106</sup> As the PSB has a limited budget and its priority is on violent crime, the PSB believes that wealthy MNCs should reimburse the PSB for the cost of the investigation so that it will be able to have sufficient resources to discharge its primary duty to protect society from violent crime.<sup>107</sup>

While the PRC has undertaken a well-publicized anti-corruption campaign for the past several years, the targets of this campaign are political enemies of Xi Jin Ping, China’s President and Chairman of the Communist Party.<sup>108</sup> The targeted persons derive personal financial gain by accepting bribes, which allows Xi to remove them from office and punish them.<sup>109</sup> A “case fee” made to the PSB is not funneled to the private bank account of any PSB official. Instead, it is made to the PSB’s coffers and used to defray its expenses in conducting the investigation.<sup>110</sup> As a result, the case fee is a type of payment that is not the target of China’s current crackdown on corruption and is still routinely demanded.<sup>111</sup>

Not only is the case fee routinely demanded but it is also usually paid by the MNC.<sup>112</sup> This transaction now implicates the FCPA. The case fee is a payment to a “foreign official,” and a quid pro quo is involved.<sup>113</sup> In exchange for the case fee, the PSB will initiate a criminal investigation.<sup>114</sup>

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others. *Ministry of Public Security*, P.R.C. STATE COUNCIL (Aug. 25, 2014) [http://english.www.gov.cn/state\\_council/2014/09/09/content\\_281474986284154.htm](http://english.www.gov.cn/state_council/2014/09/09/content_281474986284154.htm).

101 PRC Public Security Administrative Punishment Law, *supra* note 99, art. 1.

102 *Ministry of Public Security*, *supra* note 100. The list of duties for the Ministry of Public Security do not even list economic crimes, indicating their relatively low priority. *Id.*

103 This observation is based on the author’s own experience as in-house counsel for an MNC in China, as a legal consultant and expert witness, and on recent conversations with lawyers working on IP matters in the PRC.

104 *Id.*

105 *Id.*

106 *Id.*

107 *Id.*

108 Daniel C.K. Chow, *The Myth of China’s Open Market Reforms and the World Trade Organization*, 41 U. PA. J. INT’L L. 1, 34–35 (2020) [hereinafter Chow, *The Myth of China’s Open Market Reforms*].

109 *Id.*

110 *See supra* note 103.

111 *Id.*

112 *Id.*

113 The FCPA requires that the payment be made to a “foreign official.” *See* 15 U.S.C. § 78dd-1(a)(1). The quid pro quo is the exchange of money with the foreign official for a benefit given in return to the MNC.

114 Case fees are not required by law. *See generally* PRC Public Security Administrative Punishment Law, *supra* note 99. Thus, the MNC cannot use the defense under the FCPA that the payment was lawful under the written laws of the PRC. *See* 15 U.S.C. § 78dd-1(c)(1) (affirmative defense for payments “lawful under the written laws and regulations of the foreign official’s . . . country”).



The last element of an FCPA violation is that the payment must be made for the purpose of “obtaining or retaining business.”<sup>115</sup> This element is commonly referred to as the business nexus test.<sup>116</sup> Even if the payment is a bribe to a foreign official, it is not an FCPA violation unless it is made for the purpose of obtaining or retaining business.<sup>117</sup> In *United States v. Kay*, the Fifth Circuit rejected a narrow reading of the business purpose limited to obtaining or renewing government contracts.<sup>118</sup> In that case, executives of American Rice Inc., a Houston-based corporation, paid bribes to Haitian officials to understate the value of American Rice’s imported rice to Haiti.<sup>119</sup> By having its imports undervalued, American Rice paid significantly lower customs duties and sales taxes on the imports to Haiti customs authorities.<sup>120</sup> While American Rice admitted that it made such payments, it argued that the payments did not violate the FCPA as they were made for the purpose of lowering costs, not to retain or obtain business.<sup>121</sup> The district court agreed with American Rice and dismissed the indictment against it.<sup>122</sup>

On appeal, the Fifth Circuit reversed and held that the facts of the case could, but not necessarily, support an indictment.<sup>123</sup> The Fifth Circuit found that paying a bribe to foreign officials to lower taxes lawfully owed allows the company to reduce operating costs, freeing up capital that can be used to benefit the company in its business and to create advantages over competitors.<sup>124</sup> For example, due to cost savings from lower taxes, the company could make a lower bid for a government contract to the detriment of its competitors.<sup>125</sup>

A case fee given to the PSB could be viewed as having a business nexus under the expanded and flexible approach of the Fifth Circuit. By paying the fee to the PSB, the IP owner is able to induce the PSB to bring a criminal investigation against the suspected infringer or counterfeiter. In China, counterfeiters are interested in profits but are also extremely risk adverse and sensitive to brand protection efforts.<sup>126</sup> They seek to obtain the greatest profit but at the lowest risk of capture and punishment.<sup>127</sup> Once it becomes known among counterfeiters that a company is willing to aggressively pursue pirates through the use of the PSB, counterfeiters will migrate away from that company’s products to a different product that is not as aggressively defended.<sup>128</sup> For example, suppose that two MNCs, A and B, make successful and competitive brands of shampoo at the high end of the market that are counterfeited in large quantities. If Company A aggressively uses the PSB to pursue counterfeiters but B does not (or has not begun to do so), these criminals

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115 15 U.S.C. § 78dd-1(a).

116 See generally Tiffany Lu, *The Obtaining or Retaining Business Requirement: Breathing New Life into the Business Nexus Provision of the FCPA*, 18 FORDHAM J. CORP. & FIN. L. 729 (2013).

117 15 U.S.C. § 78dd-1(a)–(b).

118 *United States v. Kay*, 359 F.3d 738 (5th Cir. 2004).

119 *Id.* at 740–41.

120 *Id.* at 741.

121 *Id.* at 749.

122 *Id.* at 740.

123 *Id.* at 759–60.

124 *Id.*

125 *Id.*

126 See *supra* note 103.

127 *Id.*

128 *Id.*

will avoid counterfeiting A's brand and begin to counterfeit B's brands instead. Company A "retains" business by avoiding losses due to counterfeiting and also benefits by harming its competitors by shifting counterfeiting from its brands to those of its competitors. The USDOJ might consider these facts to satisfy the "business nexus" test as expounded by *United States v. Kay*.

An even more problematic issue arises with respect to the practice of some PSBs in asking for a "reward" for each capture and arrest of a counterfeiter or infringer.<sup>129</sup> As an arrest and detention by the PSB creates great fear in counterfeiters, MNCs always press the PSB for arrests.<sup>130</sup> When faced with these pressures, the PSB will sometimes ask for a "reward," i.e. a payment of several thousand dollars for each arrest.<sup>131</sup> The PSB's justification is that capturing and arresting a counterfeiter intent on evading capture is an intensive activity with higher costs that must be reimbursed.<sup>132</sup> Under the FCPA, these payments might also be considered to be an illegal quid pro quo and might also satisfy the business nexus test as explained above.

#### b. *Private Investigation Companies*

Many MNCs in China hire private investigation companies to assist in the protection of their IP rights.<sup>133</sup> Not only do these companies have experience in hunting suspects, but in some types of IP cases, such as counterfeiting, there are risks to the personal safety of the MNC's employees.<sup>134</sup> For these reasons, MNC will outsource this job to persons who are trained to do this dangerous work.<sup>135</sup> Private investigation companies are not strictly regulated by the PRC and thus can attract some nefarious characters who might be little different from the petty criminals that they pursue.<sup>136</sup> In some cases, the private investigation company will pay the case fee to the PSB or other enforcement authorities.<sup>137</sup> In addition, the private investigation company will usually not inform the MNC that payments have been made, but will submit an expense report to the MNC that disguises the payments as other innocuous expenses.<sup>138</sup>

Using private investigation companies that pay case fees to PRC authorities will not immunize MNCs from liability under the FCPA. Section 78dd-1(a)(3) prohibits a U.S. company from making a payment to "any person, while knowing that all or a portion of such money . . . will be . . . given . . . to any foreign official."<sup>139</sup> The definition of "knowing" includes awareness that a "result is substantially certain to occur."<sup>140</sup> The use of case fees is well-known in the IP protection industry in China, and it is also widely known that some private investigation companies engage in blatantly illegal conduct outside the

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129 The author has personal knowledge of this practice, as he was present in a meeting with a PSB when this request was made.

130 *Id.*

131 *Id.*

132 *Id.*

133 See Chow, *Anti-Counterfeiting Strategies*, *supra* note 59, at 763-64.

134 *Id.*

135 *Id.*

136 *Id.*

137 See Chow, *Navigating the Minefield of Trade Secrets*, *supra* note 47, at 1035.

138 *Id.* at 1037.

139 15 U.S.C. § 78dd-1(a)(3) (2021).

140 15 U.S.C. § 78dd-1(f)(2)(A)(i) (2021).

purview of MNCs. Employees with the MNC that work with private investigation companies are likely to have knowledge of these practices. In addition, if the private investigation company is deemed to be an “agent” of the MNC, then the proscription of §§ 78dd–1(a) and –2(a) apply as the issuer or domestic concern is directly liable for actions committed by its agents.<sup>141</sup> Under these circumstances, funneling payments through the conduit of private investigation companies would not immunize MNCs from prosecution under the FCPA.

### *c. Accurate Record Keeping*

In addition to its anti-bribery provisions, the FCPA also contains a books and records provision that applies only to issuers of securities under the Securities and Exchange Act.<sup>142</sup> As many U.S. multinationals have stock that is traded on public stock exchanges in the United States, many MNCs are subject to the books and records provision. These provisions provide, in relevant part, that every issuer “shall make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer.”<sup>143</sup> The purpose of this provision is to prevent companies from hiding illegal payments by mischaracterizing them or by omitting them altogether in their reports to their shareholders.<sup>144</sup>

Under this provision, any MNC with stock publicly traded in the United States is required to disclose payments of case fees to its shareholders. Independently of whether MNCs have violated the anti-bribery provisions of the FCPA, MNCs that are issuers may also be in violation of the books and records provisions if they fail to record and accurately disclose payment of case fees and other payments (as further discussed below) to PRC officials. Failure to satisfy the books and records provisions could trigger an investigation by the U.S. Securities and Exchange Commission and lead to civil liability.

### *d. Judicial Appraisal Authorities*

#### *i. Criminal Cases*

Enforcement of trade secrets in China involves special problems concerning the use of judicial appraisal authorities, which are state-owned entities that have the expertise to deal with the sometimes arcane scientific and technical issues involved in trade secrets.<sup>145</sup>

In many criminal trade secrets cases, judicial appraisal authorities play an important role. Unlike in the case of counterfeit goods, it is not apparent to PRC authorities, such as the PSB, when a violation has occurred in the case of a trade secret. For example, if an MNC seeks to file a criminal counterfeiting case with

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<sup>141</sup> 15 U.S.C. §§ 78dd–1(a), –2(a) (2021).

<sup>142</sup> 15 U.S.C. § 78m(h)(2) (2021).

<sup>143</sup> 15 U.S.C. § 78m(b)(2)(A) (2021).

<sup>144</sup> See *Kay*, 359 F.3d at 758.

<sup>145</sup> See Decision of the National Standing Committee on the Administration of Issues Concerning Judicial Administration, arts. I & II (adopted at the 14th Session of the Standing Committee of the 10th National People's Congress on Feb. 28, 2005, effective Jan. 1, 2006). Entities engaged in judicial appraisal must be approved and registered by PRC authorities. See *id.* art. VI.

the PSB, the MNC will need to make a preliminary showing that a crime has occurred. All the MNC must do is display a copy of the trademark registration certificate issued by PRC authorities proving that it is the owner of the trademark.<sup>146</sup> Then the MNC can display a sample of a counterfeit product using its trademark and submit a statement that it did not authorize the manufacture of the counterfeit. These two simple steps alone—that the MNC is the trademark owner and it did not authorize the counterfeit—will satisfy PRC authorities that an IP violation has occurred. In the case of trade secrets, however, making such a preliminary showing is far more complex. For example, suppose that an MNC approaches the PSB and claims that an enzyme formula used in making laundry detergent and protected as a trade secret has been stolen and is now being used by a competitor. Among other requirements, the MNC will need to show that the enzyme formula used in the competitor's product is a copy of the enzyme formula used in the MNC's own detergent.<sup>147</sup> Even if the MNC has chemical studies purporting to show this result, the PSB is not qualified to review such a study. The PSB are enforcement officials who lack any formal training in intellectual property and the scientific knowledge necessary to read and understand any such offer of proof. Many other trade secrets could involve scientific, mathematical, and engineering concepts that are not accessible to ordinary law enforcement officials or to any persons not trained in these fields.

Like other PRC authorities, the PSB has no interest in bringing a trade secrets criminal case that lacks a legal foundation and exposing itself to claims of exceeding its authority or abuse of power. In cases involving trade secrets, the PSB will often refer the matter to a judicial appraisal authority that has the expertise to conduct a scientific analysis and to conclude whether a trade secret has been copied.<sup>148</sup> Once a judicial appraisal authority issues a report that the suspect has copied the MNC's trade secret, the PSB can proceed with the investigation to determine whether a theft of the trade secret has occurred.<sup>149</sup> The PSB is now protected by the official report and cannot be charged with the unlawful exercise of its authority.<sup>150</sup>

The problem lies in the judicial appraisal authority's demand for a fee for its services. Like most state entities in China that perform a service, the judicial appraisal authority expects to be paid a fee.<sup>151</sup> As the PSB has referred the matter to the authority to continue its investigation, the PSB should pay the fee, but the PSB will usually demand that the MNC pay the fee instead.<sup>152</sup> Having already paid the PSB a case fee, the MNC is now expected to also pay the judicial appraisal authority for its analysis and report, a fee that should be paid by the PSB. In other cases, the MNC will first approach the judicial appraisal authority on its own, knowing that it will need to submit a report to the PSB before the

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146 This observation is based on the author's own experience working with the PSB.

147 See Law of the People's Republic of China Against Unfair Competition (promulgated by the Standing Comm. Nat'l People's Cong., Sept. 2, 1993, effective Dec. 1, 1993), art. 10.

148 See generally Brian J. Safran, *A Critical Look at Western Perceptions of China's Intellectual Property System*, 3 U. P.R. BUS. L.J. 135 (2012).

149 *Id.*

150 *Id.*

151 Yi Xue, *Trade Secrets 2020: China*, CHAMBERS & PARTNERS (Apr. 30, 2020), <https://practiceguides.chambers.com/practice-guides/trade-secrets-2020/china> (referring to fees to be paid to judicial appraisal authority).

152 Chow, *Navigating the Minefield of Trade Secrets*, *supra* note 47, at 1037.

PSB will take any action. To obtain the report, the MNC will also need to pay a fee to the judicial appraisal authority.<sup>153</sup>

In these scenarios, the MNC could once again be viewed as “paying” for enforcement services. This scenario also takes on the appearance of the MNC paying for an official report that makes a finding in its favor. The outcome of the report by the judicial appraisal authority is critical to the criminal investigation because if the report finds that the trade secret has not been copied, then the PSB will terminate the investigation. In other words, the MNC is paying for the report but has a strong interest in a positive result. Once again, the MNC finds itself in a compromised position and one that might implicate the FCPA. If the MNC pays the fee to the judicial authority, it is paying for a report that has official legal authority and that may result in a ruling in its favor. The USDOJ might consider this payment to be an illegal payment under the FCPA’s anti-bribery provisions.

An even more unfortunate situation arises when the PSB or the judicial appraisal authority demands additional fees after the initial fees have been paid.<sup>154</sup> The judicial appraisal authority might inform the MNC that it needs additional payments in order to complete the report.<sup>155</sup> The judicial appraisal authority might claim that the analysis is more complex than anticipated and that more time and resources must be expended to complete the report.<sup>156</sup> The PSB might make similar demands.<sup>157</sup> The MNC is now under strong pressure to comply and begins to feel trapped and exploited by a series of never ending demands for payment.

## ii. *Civil Cases*

So far this discussion has focused on the use of judicial appraisal authorities in criminal cases, but a civil proceeding involving trade secrets might also require the use of such authorities. Under the new burden-shifting rules of the USCTA in trade secrets cases, the plaintiff has the initial burden of making a prima facie showing that a trade secret has been stolen, at which point the burden shifts to the defendant to show that it did not steal the trade secret.<sup>158</sup> Although the plaintiff might be able to show a prima facie case to the satisfaction of the court without the use of a report from a judicial appraisal authority, that might not be possible in cases involving complex claims and technical issues. The plaintiff might need to obtain a report from a judicial appraisal authority to satisfy its initial burden before the court. These types of civil cases could also involve payments by the plaintiff to the judicial appraisal authority for a report as part of its prima facie case. Once again, the payment might implicate issues under the FCPA.

This discussion has been merely illustrative of the problems involving demands for payments by PRC authorities that plague MNCs. This Article has focused on the most sensitive and problematic demands, but demands can also

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153 See Xue, *supra* note 151.

154 This observation is based on the author’s own experience working as an in-house counsel in China.

155 Xue, *supra* note 151.

156 *Id.*

157 *Id.*

158 USCTA, *supra* note 1, at art. 1.5(2)(a).

arise in many other contexts. For example, if administrative authorities seize counterfeit goods, the authorities may decide to store them in a warehouse and then later destroy them.<sup>159</sup> The authorities might ask the MNC to reimburse the costs of storage and destruction of the goods.<sup>160</sup> There appears to be a pervasive attitude among PRC authorities that MNCs have abundant financial resources and that they should therefore be expected to assume some of the costs of investigations and enforcement actions by PRC enforcement authorities, which have limited resources and different priorities.<sup>161</sup> This is a pervasive and longstanding problem and can be manifested in many different contexts other than those used as illustrations in this section.

#### B. *THE PROBLEM OF EX PARTE CONTACTS IN CHINA'S CIVIL LITIGATION SYSTEM*

In addition to an emphasis on criminal enforcement, the USCTA also contains many provisions intended to strengthen civil enforcement through court-based IP litigation. In the area of civil litigation, MNCs in China have been plagued for years by the common practice of defendants exploiting systemic weaknesses in the PRC legal system by using *ex parte* contacts to attempt to influence the outcome of civil cases.<sup>162</sup> This type of practice is not limited to IP cases, but applies in general to civil litigation. But as the USCTA was enacted to enhance enforcement through civil litigation—in addition to criminal enforcement—of IP cases, it is important to spell out these problems, as MNC plaintiffs are highly likely to encounter these problems in civil litigation over IP disputes. The discussion of the problems will also be helpful in a subsequent section of this article that will discuss remedial measures.

Civil litigation in China is well-known to be plagued by problems of corruption. In 2016, Professor Jerome Cohen referred to it as a “looming crisis” and explained:

Today there is a huge amount of popular dissatisfaction with the judicial system [in China]. . . . People realize the local courts are full of corruption. . . . *Guanxi*—the influence of relatives, friends, and contacts—is the biggest problem. Whom did judges go to high school with? Who is their cousin? Who is a friend of a friend? These questions permeate the system and often undermine fair adjudication. And, of course, political interference is pronounced. Local government or party officials, or members of the local people’s congress, use their low-visibility powers to adversely affect what might otherwise be independent, fair judgments.<sup>163</sup>

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159 This observation is based on the author’s own experience with administrative authorities in enforcing IP rights in China. The author has also discussed these issues with lawyers currently practicing IP law in China.

160 *Id.*

161 *Id.*

162 See HE & NG, *supra* note 31, at 843.

163 Cohen, *supra* note 29.

In a typical case of most relevance to the present discussion, the party using *guanxi* is a defendant in a case brought by an MNC.<sup>164</sup> The defendant or its lawyers will not approach the front line judge directly but will approach a professional colleague of the judge and one who holds a higher ranked supervisory position;<sup>165</sup> in other cases, the defendant might approach a senior government or Party official.<sup>166</sup> The higher level supervisor or official then approaches the frontline judge involved in the litigation and attempts to influence the outcome of the litigation. The defendant might also approach a relative or friend of the frontline judge.

Although Cohen refers to using *ex parte* contacts to influence a judge as corruption, PRC law is unclear on whether using *guanxi* is illegal. In cases involving the use of *guanxi* by skillful practitioners, no money usually changes hands. Instead, appealing to a sense of professional obligation or a desire to help a relative or friend on the part of a judge is the motivation for favoring the connected party. Some type of return favor to be given to the front-line judge is expected in the future. Under current PRC law, the use of *guanxi* where no money or property changes hands appears to fall within a gap or a gray area. Under China's bribery laws, influencing a judge through *guanxi*, even when there is a quid pro quo involving favors, is not considered bribery so long as no money or property changes hands. PRC Criminal Law provides:

Article 389: Whoever, for the purpose of securing illegitimate benefits, gives *money or property* to a State functionary shall be guilty of offering bribes.<sup>167</sup>

Article 385: Any State functionary who, by taking advantage of his position, extorts *money or property* from another person, or illegally accepts another person's *money or property* in return for securing benefits for the person shall be guilty of acceptance of bribes.<sup>168</sup>

These articles make clear that the giving or accepting of "money or property" is an essential element of the crimes of giving or accepting a bribe. Using non-monetary means to influence a judge or accepting a non-monetary benefit does not fall within the definition of bribery. In addition, there does not appear to be any other provision of law in China that explicitly deals with the use of *guanxi*.<sup>169</sup> To the contrary, *guanxi* is deeply embedded in traditional Chinese culture that long predates the current regime of the Communist Party.<sup>170</sup> The existence of, and tacit acceptance or tolerance of, *guanxi* in China is one

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164 See HE & NG, *supra* note 31, at 863.

165 See *id.* at 862.

166 See *id.* at 846.

167 Zhonghua Renmin Gongheguo Xingfa (中華人民共和國刑法) [Criminal Law of the People's Republic of China] (adopted by the Second Meeting of the Fifth Session of the National People's Congress, July 1, 1979, effective Jan. 1, 1980), art. 389, *translated at* <https://www.cecc.gov/resources/legal-provisions/criminal-law-of-the-peoples-republic-of-china> (emphasis added).

168 *Id.* at art. 385 (emphasis added).

169 The author conducted a review of China's criminal, civil, and administrative laws.

170 See DUNNING & KIM, *supra* note 35, at 329–30.

reason why it is so pervasive, hard to eradicate, and creates a significant systemic weakness in the PRC judicial system that defendants often exploit.

A recent study found that attempting to influence judges through *guanxi* is a common practice in the PRC. The study showed that 52% of PRC judges said that in handling cases they were approached by *guanxi* and that 61% of judges mentioned that within the scope of discretion, they favored the connected parties.<sup>171</sup> Under the right set of circumstances, the use of *guanxi* can be very powerful and effective in influencing a frontline judge:

The Chinese court is a hierarchical institution. A judge's income and promotions . . . are to a large extent determined by her supervisors. *A judge is under strong pressure to deliver if she is approached by someone who is in a supervisory position*; in other words, that person has direct control over her in the bureaucracy. . . . The term "supervisor" goes beyond the immediate boss of the judge; it includes any officials within the judicial system who are in a position to assess the performance of the judge and thus affect her welfare and career prospects. Supervisors thus include division directors or presidents of the court. Supervisors can also include senior judges from the corresponding appellate court. These senior judges determine if a lower-court judge's decision is reversed or remanded, either of which is a strike against her performance record. . . . Local administrative leaders and Party officials are responsible for the appointment and removal of court officials. Local officials in charge of powerful bureaus in the economic sector . . . also play "supervisory" roles as they have de facto control over the court budget and staffing decisions.<sup>172</sup>

The number of persons who can affect the judge's decision can be quite large so skillful influence peddlers in China can have a high success rate in influencing the outcome of litigation. In practice, many PRC law firms boast of their professional ties with government officials and will hire former judges in order to attract clients.<sup>173</sup> The use of ex parte contacts and influence peddling and the longstanding tolerance of such practices in China is a serious systemic weakness of the legal system that is left unaddressed in the current text of the USCTA.

### C. BRIBES AND THE ONLINE SALES OF COUNTERFEITS

The USCTA recognizes that online sales of counterfeits worldwide through e-commerce sites have exploded and created a major problem for IP owners.<sup>174</sup> Article 1.13 of the USCTA deals specifically with the requirement for e-commerce sites to have expeditious and effective notice and take-down

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171 HE & NG, *supra* note 31, at 842.

172 *Id.* at 846 (emphasis added).

173 *Id.*

174 CHOW, *Counterfeiting in the Age of the Internet*, *supra* note 38, at 160.



procedures for postings or webpages that sell counterfeit goods.<sup>175</sup> Article 1.13 is undoubtedly based upon frequent complaints from IP owners that e-commerce sites such as Alibaba and Amazon require IP owners to use convoluted and labyrinthine notice and take-down procedures that only add to their misery and frustration.<sup>176</sup> IP owners have described these procedures as “Kafka-esque”<sup>177</sup> and their use as being imprisoned in “Amazon purgatory.”<sup>178</sup>

No prophylactic or enforcement measure in the USCTA, however, addresses the common problem of online operators who give business bribes to employees at e-commerce sites in China. Online operators in China pay bribes to receive preferential business opportunities that squeeze out competitors.<sup>179</sup> For example, in exchange for bribes, online operators are allowed to delete negative comments and post fictitious ones.<sup>180</sup> Online counterfeiters also give bribes to employees who will then tip off the counterfeiters of investigations launched by PRC enforcement authorities.<sup>181</sup> The common use of business bribes given to employees of e-commerce sites by unscrupulous online operators can undermine the implementation in practice of any of the new provisions of the USCTA.

The most damaging consequence caused by business bribes is the lax implementation of registration and verification requirements for online operators by e-commerce sites.<sup>182</sup> One of the most intractable problems is the use of false names and identities by online counterfeiters.<sup>183</sup> When IP owners attempt to take down a site or listing selling counterfeit goods, they find that registered names and addresses are fictitious and that online counterfeiters quickly vanish into cyberspace.<sup>184</sup>

Due to China’s national policies that require extensive supervision of all aspects of Chinese society, China, ironically, provides the tools that would allow IP owners to identify and locate counterfeiters. For example, Article 23 of State Administration for Industry and Commerce (SAIC) Order No. 60, Measures on the Administration of Online Transactions (MAOT):

The business operator of a third-party transaction platform shall examine and register as business operators the identities of the legal persons, other economic organizations or industrial and commercial sole proprietors that apply for access to the said platform for sale of products or provision of services, establish registration files and conduct regular verification and updating, and *make public the information specified in their business licenses or provide electronic links to their business*

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175 USCTA, *supra* note 1, art. 1.13.

176 CHOW, *Counterfeiting in the Age of the Internet*, *supra* note 38, at 186–87.

177 *Id.* at 186–87.

178 *Id.*

179 CHOW, *Counterfeiting in the Age of the Internet*, *supra* note 38, at 181.

180 *Id.* at 182.

181 *Id.*

182 *Id.* at 193.

183 *Id.* at 186.

184 *Id.*

*licenses in eye-catching locations on its main web pages for business activities.*<sup>185</sup>

The business license referred to in this regulation is issued to every lawful business by PRC Administration for Industry and Commerce (AIC).<sup>186</sup> Every lawful business must apply to the local administrative authorities for a business license and no business entity can lawfully operate without one.<sup>187</sup> The AICs will review the application and verify its information before issuing the official license and registering the company as a lawful business.<sup>188</sup> The business license identifies the correct name and location of the business operator and also includes the name of the business entity's legal representative.<sup>189</sup> Under PRC Company Law, the legal representative is a natural person who is subject to criminal and civil liability for the malfeasance of the company.<sup>190</sup> PRC authorities wanted to ensure that a natural person could be held liable for wrongful acts of the company and that liability could not ultimately rest with the legal entity.<sup>191</sup> By identifying the legal representative, the business license gives IP owners a natural person against whom they can bring a criminal or civil legal action in China independent of the remedy available by using the e-commerce site's notice and takedown procedures.

Each business license contains a unique eighteen-digit number known as the "unified social credit code"<sup>192</sup> that is the business entity's official business registration number.<sup>193</sup> The number can also be used to search a publicly available national database to find the business license and registration information online, including the name of the registering entity, the entity type, and the region of registration.<sup>194</sup>

If e-commerce sites accurately registered online operators, the information on the business license, such as the name and address of the business entity, the name of the legal representative, and the company's unified social credit number will be available to the public as required by PRC law.<sup>195</sup> Most counterfeiters hide behind false names and addresses for fear of identification and capture; if e-commerce sites rigorously verified identities by requiring the display of

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185 Administrative Measures for Online Transactions (promulgated by the State Admin. of Indus. & Com., Order No. 60, Jan. 26, 2014, effective Mar. 15, 2014), art. 23.

186 Companies Law of the People's Republic of China (promulgated by the President of the PRC, Order No. 42, Oct. 27, 2005, effective Jan. 1, 2006), ch. I, art. 7.

187 *Id.*

188 See Matt Slater, *What is a China AIC?*, CHINA CHECKUP (Dec. 9, 2013), <https://www.chinachekcup.com/blogs/articles/china-aic> ("China AICs . . . provide official registration records for all companies in their jurisdiction . . .").

189 Companies Law of the PRC, *supra* note 186, at ch. I, art. 7.

190 Zonghua Renmin Gongheguo Minfa Tongze (中華人民共和國民法通則) [General Principles of Civil Law of the People's Republic of China] (adopted at the Fourth Session of the Sixth National People's Congress, Apr. 12, 1986, promulgated by Order No. 37 of the President of the People's Republic of China, Apr. 12, 1986) art. 49, *translated at* <https://www.wipo.int/edocs/lexdocs/laws/en/cn/cn012en.pdf>.

191 *Id.* ch. III, arts. 38, 49.

192 Maarten Beekers, *How to Verify a China Business License in 5 Steps*, CHINA TRADE BLOG (Jan. 11, 2019), <https://chinatradeblog.org/china-business-license-verification/>.

193 Maarten Beekers, *China Business License*, CHINA TRADE BLOG (Jan. 5, 2019), <https://chinatradeblog.org/china-business-license-in-english/>.

194 BEEKERS, *supra* note 192.

195 Administrative Measures for Online Trading, *supra* note 185, at art. 23.

business licenses on their webpages, many counterfeiters would be deterred from using e-commerce platforms to sell their illegal goods.<sup>196</sup> Even if the e-commerce sites only asked for the business entity's 18 digit unified social credit code that alone would be a powerful deterrent. A review of recent webpages of sites selling counterfeit products indicates, however, that no business license is displayed and no electronic links to the business license are made available in direct contravention of Article 23 of MOAT set forth above.<sup>197</sup>

At present, major e-commerce sites such as Alibaba are notoriously lax about and merely "pay lip service"<sup>198</sup> to registration and verification requirements. Online counterfeiters pay business bribes to employees at e-commerce sites to relax their standards, to ignore the requirements of business licenses, and to allow the counterfeiters to assume false identities and fictitious addresses.<sup>199</sup> Without the ability to identify and deter counterfeiters, the effectiveness of the USCTA's provisions enhancing the ease of notice and takedown procedures is undermined. Even if an IP is able to expeditiously take down an illegal site, the counterfeiter will in short order assume a new false name and address and repost the same listing. The simple act of prohibiting business bribes and requiring e-commerce sites to rigorously enforce existing PRC laws on entity registration and verification should have an immediate and significant effect in reducing online sales of counterfeit goods.

### III. CONCLUSION

As a matter of procedural law, the United States created the ultimate enforcement weapon in the USCTA. The United States designed the dispute resolution mechanism to box China into a no-win situation. Once the United States finds China in breach, China will have to suffer tariffs under the USCTA or if China withdraws from the USCTA, China will suffer the reinstated tariffs that the USCTA suspended. As a matter of procedure, the USCTA is innovative and path breaking; it is also clever and ruthless.

By contrast, the USCTA's substantive provisions have fallen short. They have failed to address the pervasive and systemic problem of corruption that creates barriers to on the ground enforcement in China. As this discussion has indicated, problems of government and business corruption occur in many different areas of the legal and administration systems and business sectors related to the protection of intellectual property.<sup>200</sup> The discussion in this article

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196 CHOW, *Counterfeiting in the Age of the Internet*, *supra* note 38, at 192.

197 *See id.* at Appendixes 1-3.

198 *Id.* at 193.

199 *Id.* at 181-82.

200 Moreover, other problems of corruption that are indirectly related to IP protection, such as bribery in the pharmaceutical and health care industry, create additional major problems for MNCs but have not addressed in this article as these issues are outside of its scope. For MNCs in the pharmaceutical industry, a major problem is the common practice of doctors requiring "kickbacks," i.e. payments from pharmaceutical companies for prescribing their medications to patients in China's state-owned hospitals. This practice is common because doctors in the public health sector in the PRC receive modest salaries and supplement their incomes by receiving these payments. The practice is tolerated by the PRC government as a subsidy by pharmaceutical companies to support underpaid doctors. The payment by the MNC pharmaceutical company can be considered quid pro quo or a bribe and a doctor

has focused on some of the most serious and common problems, but corruption is capable of many variations and can occur in many different contexts. The common theme to all of these forms of corruption is the abuse of the PRC legal and administrative apparatus to obtain benefits through the use of money, property, or influence. These problems can create barriers to effective on the ground enforcement by MNCS in China that negatively impact the conduct of their day-to-day business operations. Moreover, they can expose MNCs to significant risks—not from the PRC government—but from the United States government under the FCPA.

Fortunately, there is still an opportunity for the United States to address problems of corruption in IP protection. The United States and China are now in the process of negotiating Phase II of the USCTA.<sup>201</sup> This negotiation will allow the United States to amend the IP provisions of Phase I or to add new provisions to Phase II of the USCTA. There will also likely be future trade negotiations where these issues can be addressed through new provisions. In drafting these new provisions, the United States should be guided by the following considerations.

To address the demand for payments and issues related to the FCPA, the United States should insist on a provision that prohibits the demand by PRC authorities of all fees in exchange for the performance of their duties.<sup>202</sup> This prohibition would include fees that represent reimbursement of costs or expenses used in the performance of their duties, whether these fees are styled as case fees, fees for tests, technical services, or as miscellaneous expenses.<sup>203</sup> These new provisions are necessary due to an entrenched attitude on the part of PRC authorities that MNCs that have deep financial resources and can be expected to contribute to the performance of public services by PRC governmental entities that have limited resources. A more sinister attitude that may also exist in the PRC is that MNCs with deep pockets can be easily manipulated and exploited. Aside from protecting MNCs from liability under the FCPA, such a provision will also help relieve MNCs from the misery of being exploited by PRC authorities.

The United States should clamp down on the use of influence peddling (*guanxi*) by inserting a clause that prohibits the parties from directly or indirectly engaging in ex parte contacts with judges in legal proceedings.<sup>204</sup> The United States should also insist that China define the crime of bribery to include the exchange of non-tangible benefits to influence the result of a legal or administrative proceeding.<sup>205</sup> At present, China's criminal laws only include the

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at a state-owned hospital could be considered to be a "foreign official" under the FCPA. See CHOW, *supra* note 49, at 63.

201 See Bursztynsky, *supra* note 46.

202 For example, "China shall prohibit its government entities, including the Public Security Bureau, the Administrations of Industry and Commerce, and judicial appraisal authorities, from demanding the payment of fees as a condition of performing their duties, whether called case fees, administrative fees, reimbursement fees, or fees for tests, reports, or analysis."

203 See *supra* text accompanying note 202.

204 For example, "China shall prohibit parties in a litigation or their representatives from having ex parte contacts with the judge directly or indirectly through the use of intermediaries, including other judges, government or Party officials, colleagues, associates, friends, or relatives."

205 For example, PRC Criminal Law Article 385 could be amended as follows "Whoever, for the purpose of securing illegitimate benefits, gives money or property or *anything of value* to a State functionary shall be guilty of offering bribes."

exchange of “money” or “property” in the crime of bribery, leaving wide open the opportunity to use *ex parte* contacts (i.e. using *guanxi*) to influence the results of legal proceedings without the use of money or property. The addition of a term also prohibiting the giving of “anything of value” should close this loophole in China’s anti-bribery law.<sup>206</sup> The use of *guanxi* has an extensive history, long predating the PRC, which is endemic to China’s entire legal, administrative, and political system.<sup>207</sup> It is also common in social relationships.<sup>208</sup> A clear directive is required to prohibit its use in criminal or business litigation.

The United States should also amend the USCTA provisions dealing with online sales of counterfeits by adding a specific provision that requires China to amend its criminal laws to prohibit online operators from giving and e-commerce sites from accepting business bribes.<sup>209</sup> A provision specifically limited to bribes in e-commerce is necessary to deter these practices.<sup>210</sup> The United States should also include a provision that specifically requires e-commerce sites to rigorously enforce China’s registration and verification procedures for online operators so that their true identities and locations become publicly available.<sup>211</sup> These actions should have an immediate and positive effect in deterring online sales of counterfeit products.

The current relationship between the United States and China is fraught with many issues and some fundamental concerns, such as the United States’ mistrust of China’s Communist Party,<sup>212</sup> and are far too complex to discuss in this article. This article has focused mainly on the problems of IP protections raised in the USCTA that mainly affect U.S. multinational companies doing business in China. As a matter of procedural law, the USCTA has created the ultimate enforcement weapon that is under the complete control of the United States and that has boxed China into a no-win situation. With regard to substantive issues, however, the longstanding problem of government and business corruption creates barriers to effective on the ground enforcement of IP rights in China. At present, the United States has a rare opportunity through the continuing negotiations of Phase II of the USCTA to address some pervasive and intractable substantive legal issues that have long plagued MNCs in protecting their intellectual property rights in China.

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206 See *supra* text accompanying note 205.

207 See Gold et al., *supra* note 35; see also Dunning & Kim, *supra* note 35.

208 This observation is based on the author’s own experiences living and working in China.

209 For example, “China shall ensure that its criminal laws prohibit all e-commerce platforms, their officers, employees, or agents from demanding or accepting any money, property, or anything of value from online operators during the registration process or thereafter. China shall also ensure that its criminal laws prohibit online operators from offering any money, property, or anything of value to officers, employees, or agents of e-commerce platforms.”

210 See *supra* text accompanying note 209.

211 For example, “China shall ensure that e-commerce platforms rigorously enforce Article 23 of SAIC Order No. 60 and other laws, regulations, or notices regarding registration procedures by requiring that all online operators display their business licenses, the name of the legal representative, and their eighteen-digit unified social credit code on their webpages or websites.”

212 *White House Report Criticizes China’s Economic Policies, Human Rights Violations*, CNBC: POLITICS (May 21, 2020), <https://www.cnbc.com/2020/05/21/white-house-report-criticizes-china-policies.html>.