September 16, 2020

Edward Gresser
Chair of the Trade Policy Staff Committee
Assistant United States Trade Representative for Trade Policy and Economics
Office of the United States Trade Representative

VIA ONLINE SUBMISSION

Re: Comments of Engine Advocacy on China's WTO Compliance, Docket No. USTR-2020-0033

Dear Mr. Gresser:

Engine is a non-profit technology policy, research, and advocacy organization that bridges the gap between policy makers and startups. Engine works with government and a community of thousands of high-technology, growth-oriented startups across the nation to support the development of technology entrepreneurship through economic research, policy analysis, and advocacy on local and national issues. We appreciate the opportunity to submit these comments in response to the United States Trade Representative's ("USTR's") request for comments concerning China's compliance with World Trade Organization ("WTO") commitments.

I. Intellectual Property Rights Enforcement

Balanced and certain IP enforcement frameworks are critical for innovation and startup growth and success. Efforts in China to implement such balanced law and procedures should be commended. Indeed, in recent years, China has explored changes to its patent laws, some of which signal positive developments. But some legal changes China is contemplating lack sufficient safeguards against abuse and lack the fairness and equity embodied, for example, in U.S. patent law and the Trade-Related Aspects of Intellectual Property Rights ("TRIPS") agreement.[1] The comments Engine submits here focus on a few areas where Chinese law appears to be trending towards imbalance, uncertainty, and creating opportunities for abuse, signaling tension with obligations under TRIPS.

Overall, China should be discouraged from adopting imbalanced, uncertain IP enforcement frameworks. Otherwise, startups seeking to expand into Chinese markets would face increased risk of abusive patent litigation and uncertainty about how accusations of infringement would be handled. And those smaller,

[1] Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1C, 1869 U.N.T.S. 299, 33 I.L.M. 1197, *available at* https://www.wto.org/english/docs_e/legal_e/31bis_trips_01_e.htm [hereinafter "TRIPS"].

younger companies with fewer resources and less in-house legal expertise would stand to lose the most due to a patchwork of imbalanced laws across the globe.

A. Startups need balanced, consistent IP enforcement frameworks across the globe

It is critical for IP frameworks, including those in China, to focus on improved enforcement of legitimate rights. And at the same time, it is essential to pursue enforcement policies with an eye toward avoiding abuse of the system. The availability of balanced, certain, and consistent IP enforcement across the globe makes it easier for startups to grow and compete internationally.

Balance is essential in IP enforcement Without it, those who obtain questionable patents can easily use them as a threat, to coerce startups to settle frivolous assertions or hinder startup growth—at worst using questionable patents to stop startups in their tracks. For example, when the remedies for accused infringement are unjustifiably high and disconnected from the value of the purported invention, even the lowest-quality (invalid) patents become an effective bludgeon against innovative startups.

These concepts are also baked into compliance with WTO obligations. Importantly, TRIPS calls for IP enforcement procedures "applied in such a manner as to avoid the creation of barriers to legitimate trade and to provide for safeguards against their abuse." Likewise, under TRIPS, IP enforcement procedures should be "fair and equitable," and "not be unnecessarily complicated or costly, or entail unreasonable time limits or unwarranted delays."[2] As detailed below, were China to adopt certain recently proposed amendments in its patent laws, it would conflict with these provisions of TRIPS.

Finally, it is difficult for any business to navigate a patchwork of legal regimes across the globe. This is particularly true for startups. If startups have to maneuver a Chinese legal system, for example, where courts and administrative agencies take different approaches to resolving infringement complaints and awarding damages, that would hurt their ability to expand to and compete in China.

B. Certain proposed changes to China's patent laws would create uncertainty and opportunities for abuse

Over the past two years, China has released proposed amendments to its patent laws.[3] Of note, two areas of the proposed amendments cause concern: administrative adjudication of infringement and disproportionate relief.

Administrative adjudication of infringement: China recently proposed allowing administrative adjudication of infringement, where the same agency that examines and issues patents would be

[2] TRIPS art. 41.1, 41.2.

[3] *See, e.g.*, Aaron Wininger, *China Releases Draft Amended Patent Law for Comment*, China IP Law Update (July 5, 2020), https://www.chinaiplawupdate.com/2020/07/china-releases-draft-amended-patent-law-for-comment/; Mark Cohen, *Public Comment Draft of Patent Law Revisions Released by NPC*, China IPR (Jan. 4, 2019), https://chinaipr.com/2019/01/04/public-comment-draft-of-patent-law-revisions-released-by-npc/.

authorized to evaluate infringement and award damages.[4] Instead of opening up such administrative adjudication, it is better—and more consistent with TRIPS—to have courts adjudicate infringement. While the administrative agencies that issue patents are well suited to tasks of patent examination, including adjudication of post-issuance validity disputes, there are a number of reasons why they should not adjudicate infringement and damages.

First, patent disputes are the type of complex cases between private parties which should be decided by courts. Indeed, this is consistent with TRIPS's mandate that "Members shall make available to right holders civil judicial procedures concerning the enforcement of any intellectual property right . . ."[5] Courts have well-established procedures to govern such disputes, and TRIPS spells out fundamental procedures common in the judicial system which provide fairness to the parties in infringement disputes.[6]

Second, if an administrative agency has the authority to both examine and issue patents, enforce them, and award damages, this would call into question the independence and fairness of both the patent examination and enforcement systems housed within the administration.[7]

Third, the specific approach China has proposed for allowing dual administrative and judicial adjudication is unclear. There are no articulated standards for when a dispute could or would be taken to the administrative agency versus the court. Dividing enforcement authority in this way will increase uncertainty for startups and open doors for inconsistent legal standards, forum shopping, and abuse.

Punitive damages & injunctive relief: Recent proposals in China would also over-amplify the damages and relief available in patent cases, creating a fertile foundation for abuse. In fact, one commenter has noted that a main objective of China's amendment process "is to increase the penalties for infringement and the amount of compensatory damages."[8] For example, China has proposed allowing greater punitive damages in patent cases, multiplying the damages award up to five times. China has also proposed lowering the burden of proof for a patentee seeking damages.[9] And other portions of Chinese law purport

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[4] *See, e.g.*, Mark Cohen, *Translation of Draft Patent Law Available*, China IPR (July 4, 2020), https://chinaipr.com/2020/07/04/translation-of-draft-patent-law-available/ (linking to unofficial translation of patent law amendments, first and second reading, proposed Articles 69 and 70 provide for administrative adjudication).

[5] TRIPS art. 42.

[6] *E.g.*, TRIPS art. 42-49.

[7] *See, e.g.*, Mark Cohen, *Why the Proposed Amendments to the Patent Law Really Matter . . . and Maybe Not Just For Patents*, China IPR (Sept. 6, 2012), https://chinaipr.com/2012/09/06/why-the-proposed-amendments-to-the-patent-law-really-matter-and-maybe-not-just-for-patents/ (further explaining that a 2012 draft law to allow administrative enforcement would "return[] China to its state of IP affairs before WTO accession, when local IP offices . . . had the authority to award damages in administrative cases").

[8] Andrew Liu, *Patent Litigation in China: Overview*, Thomas Reuters Practical Law (May 1, 2020), https://uk.practicallaw.thomsonreuters.com/8-620-4407?__lrTS=20191025142758892&transitionType=Default&contextData=(sc.Default)&firstPage=true (response to question 38).

[9] Cohen, *supra* note 4 (proposed Article 71 addresses increased damages and the burden of proof); *see also* Hui Zhang *et al.*, *The 4th Amendment of PRC Patent Law is Coming*, Kluwer Patent Blog (June 14, 2019), http://patentblog.kluweriplaw.com/2019/06/14/the-4th-amendment-of-prc-patent-law-is-coming/.

to favor injunctions as the standard approach to sanctions in IP cases.[10] To embody TRIPS's call for fairness, equity, and safeguards against abuse, the relief available for patent infringement should be more measured and connected to the value of the purported invention and the facts of each case.[11]

Disproportionate remedies, untethered from the facts of a case, play into the hands of abusive litigants. Such remedies give patent owners—including patent assertion entities ("PAEs") and owners of questionable patents—the power to shut down startups or credibly threaten to shut them down. The possibility of unduly high damages or the ready availability of injunctions creates significant leverage to settle even frivolous lawsuits.[12]

Were China to move further toward automatically increasing the amount or severity of remedies in patent cases, it would arbitrarily inflate the value of all patents (including questionable patents or those that cover trivial features of complicated products or services), and strip courts of their proper role in weighing relevant facts and context when fashioning equitable and monetary relief. And without the ability for courts to scrutinize the facts of a case and award the appropriate relief, the significant leverage of high damages or an injunction would exist equally for questionable (i.e., invalid) patents that are not infringed.

By contrast, in the U.S., injunctive relief in patent cases is premised on long-standing and traditional concepts of equity, where patent owners are only entitled to injunctive relief when the facts of the case indicate it is appropriate.[13] This levels the playing field in patent assertion, freeing accused infringers to proceed with invalidity and non-infringement defenses without the risk of suffering existential loss (e.g., damages they cannot afford or having their products pulled from the market).[14] This is particularly important for startups. Many startups would, understandably, be unwilling to risk an injunction or damages that exceed the value of the company, and instead err on the side of settling cases of questionable merit. Balanced IP laws that limit punitive damages and award injunctions based on equitable considerations give startups more freedom to fight back against frivolous claims.

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In sum, China should be discouraged from imposing draconian remedies for patent infringement and it should not pursue administrative adjudication of infringement. Were China to adopt certain proposed

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[10] Aaron Wininger, *China's Supreme People's Court Draft Opinions on Increasing Sanctions for Intellectual Property Infringement*, National Law Rev. (July 30, 2020), https://www.natlawreview.com/article/china-s-supreme-people-s-court-draft-opinions-increasing-sanctions-intellectual.

[11] *See, e.g.*, Mark Cohen, *On Avoiding "Rounding Up the Usual Suspects" In the Patent Law Amendments . . .*, China IPR (Jan. 23, 2020), https://chinaipr.com/2019/01/23/on-avoiding-rounding-up-the-usual-suspects-in-the-patent-law-amendments/ (arguing that adequate, predictable, compensatory civil remedies should be a priority).

[12] *See, e.g.*, Brian T. Yeh, Cong. Research Serv., R42668, *An Overview of the "Patent Trolls" Debate* 12-14, 18 (2013) (describing leverage PAEs can exert when injunctive relief is available).

[13] *eBay Inc. v. MercExchange, LLC*, 547 U.S. 388 (2006).

[14] *See, e.g.*, eBay *Decision Levels Patent Litigation Playing Field*, Buchanan Ingersoll & Rooney (Apr. 5, 2011), https://www.bipc.com/ebay-decision-levels-patent-litigation-playing-field.

amendments to its laws, it would create uncertainty and a fertile foundation for abusive patent assertion. U.S. startups and innovators seeking to expand in the Chinese market could (and would likely) be subject to such uncertainty and abuse. Moreover, some of the changes China has considered would conflict with its obligations under TRIPS. A more consistent global framework—where patent damages are reasonable, injunctions are available only when equity and the facts of the case indicate such relief is appropriate, and where adjudication of patent infringement and damages are conducted by the courts—will promote a level playing field where startups are better able to compete and innovate. And that will embody TRIPS's mandate to avoid barriers to trade, avoid abuse of the patent system, and foster fairness and equity.

II. Cross-Border Data Flows and Data Localization

The growth of the Internet is largely responsible for the strength and vibrancy of the American startup ecosystem. It enables founders to engage in marketplaces across the globe, often without brick-and-mortar places of business in the countries in which their users reside. But that global reach is directly impacted by restrictive government policies that place barriers on the flow of data. Such boundaries on data flows are cost prohibitive, limiting user choice and the ability of startups to grow—both in the U.S. and abroad.

While the World Trade Organization formed before the broad usage of the Internet (and therefore lacks modern digital trade frameworks), certain provisions, like the General Agreement on the Trade in Services ("GATS"), may be relevant when considering if a WTO member is in fact meeting its obligations if they embrace restrictions on the cross-border flow of data and data localization requirements.[15] And modern trade agreements are speaking to digital trade where the WTO may fall short.[16] For example, the U.S.-Mexico-Canada Agreement ("USMCA") and the U.S.-Japan Trade Agreement contain provisions that call for the free flow of data, with limited exceptions.[17] These agreements acknowledge the growing economic role of digital trade and emphasize the importance of eliminating barriers to the trade in services between nations. USTR should consider efforts by China to restrict the cross-border flow of data and data localization measures when considering whether China is in compliance with its WTO obligations.

A. Restricting cross-border data flows and mandating data localization limits startup growth

When foreign governments require data localization and limit cross-border data flows, it inhibits innovation and the ability of startups to engage with users globally. Government policies that restrict the flow of data and require data localization are often couched as necessary to preserve privacy or security, but in actuality these policies—sometimes intentionally—merely have the effect of favoring domestic

[15] Justin Sherman, *The U.S. is Waging War on Digital Trade Barriers*, Wired (April 10, 2020), https://www.wired.com/story/the-us-is-waging-war-on-digital-trade-barriers/.

[16] Joshua P. Meltzer, *Data and the Transformation of International Trade*, Brookings (March 6, 2020), https://www.brookings.edu/blog/up-front/2020/03/06/data-and-the-transformation-of-international-trade/.

[17] *Id.*

companies over foreign competitors.[18] These policies in particular harm startups, which often lack the resources to build physical facilities in every country where they have users or customers. While larger companies might be able to decide where to house servers based on the size of a country's market, small startups would simply be unable to compete, let alone survive, when faced with complying with such restrictions.[19] Moreover, those companies that can afford to store data in countries across the globe will likely simply elect to pass the cost of doing so onto their users, including small businesses.[20] Therefore, countries that enact restrictive data flow measures or that require data localization may enable the success of domestic companies at the expense of foreign startups, who simply do not have the resources to comply with local law.

B. China's data restrictions limit market entry

China has previously indicated a belief that WTO member states should be able to regulate on issues pertaining to data flows—and to allow for a flow of information only so long as privacy, public interests, national security, and network security are maintained.[21] Moreover, China's behavior generally does not support a free-flow of data. Instead, policies like China's recently announced Global Data Security Initiative embrace "cyber sovereignty," and include data localization requirements.[22] China also restricts data flows by way of wholesale blocking of websites, as opposed to less restrictive mechanisms.[23]

The broad restrictions on the cross-border flow of data mandated by the Chinese government can be viewed as a non-tariff barrier to trade. As was noted under USTR's 2019 report, the restrictions Chinese law specifically puts in place on cross-border data flows, including data localization requirements, limit the ability of U.S. businesses, including startups, to enter the Chinese market and impairs their ability to engage in activities fundamental to the course of business.[24] Also noted in the report, a number of policies the Chinese government has pursued "do not appear to be in line with the non-discriminatory, non-trade restrictive approach to which China has committed."[25] Instead, the data flow restrictions serve to limit what content is available in local markets and also serve to enable the growth of domestic companies at the expense of foreign competition.[26] Moreover, China's cybersecurity law goes so far as to require local

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[18] Rachel F. Fefer *et al.*, Cong. Research Serv., R44565, *Digital Trade and U.S. Trade Policy* (2019), *available at* https://fas.org/sgp/crs/misc/R44565.pdf.

[19] Engine, *Startups Need a Global Internet, Not Data Borders* (Sept. 2, 2018), https://medium.com/@EngineOrg/startups-need-a-global-internet-not-data-borders-71726b5ad0b7.

[20] *Id.*

[21] Nigel Cory, *Why China Should be Disqualified from Participating in WTO Negotiations on Digital Trade Rules*, ITIF (May 9, 2019), https://itif.org/publications/2019/05/09/why-china-should-be-disqualified-participating-wto-negotiations-digital.

[22] Rita Liao, *China Presents Global Standard for Data Security*, TechCrunch (Sept. 8, 2020), https://techcrunch.com/2020/09/08/china-presents-global-standard-for-data-security/.

[23] Cory, *supra* note 21.

[24] United States Trade Representative, *2019 Report to Congress on China's WTO Compliance* (Mar. 2020), https://ustr.gov/sites/default/files/2019_Report_on_China%E2%80%99s_WTO_Compliance.pdf.

[25] *Id.*

[26] Meltzer, *supra* note 16.

storage for a broad range of data, including personal and financial data.[27] But these data flows represent value for companies—one 2014 study found that data flows were responsible for generating $2.8 trillion in value.[28] And strict data localization policies, like those found in China, undermine the value of data and instead raise costs for businesses—costs that could box startups out of competition.[29] As was noted in the 2019 report, restrictions on data flows and requirements for the local storage of data reduce or eliminate the ability of American firms to fully avail themselves of market access in China. Not only is this bad for U.S. startups to grow in China, but it is bad for innovation on a global scale.[30] USTR should be wary of any attempt by WTO members to restrict data flows and to require data localization.

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Thank you again for the opportunity to provide these comments. We appreciate USTR's interest in and efforts to promote technology and innovation and maintain U.S. competitiveness in the global economy. Startups are an essential component of our innovation economy, developing some of the most exciting new technologies and making outsized contributions to economic and job growth. We encourage USTR to continue to weigh the interests of the startup community and ensure that its efforts support startup growth and success on the global stage.

[27] Cory, *supra* note 21.

[28] Cody Akeny, *The Costs of Data Localization*, Tech Wonk Blog (August 17, 2016), https://www.itic.org/news-events/techwonk-blog/the-costs-of-data-localization.

[29] United States Trade Representative, *supra* note 24.

[30] Akeny, *supra* note 28.