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Real And Present Danger: Patent Litigation In China

Law360, New York (June 10, 2009) -- What have Microsoft, Samsung Electronics and Schneider Electric in common? They have all been sued for patent infringement in China.

In October 2008, Microsoft was sued by China E-Commerce Info-Tech Co. Ltd. for patent infringement at Xi'an Intermediate Court over Chinese invention patent ZL200510022721.3 relating to RSS information exchange. The parties are waiting for a trial.

In April 2007, Samsung was sued by Holley Communications Co. Ltd. for patent infringement at Hangzhou Intermediate Court over Chinese invention patent ZL02101734.4 relating to CDMA/GSM dual mode mobile communication devices.

In December 2008, the Hangzhou court issued an injunction against Samsung and awarded RMB 50 million ($7.35 million) in damages to Holley (1 USD equals about 6.8 RMB).

In June 2006, a Chinese subsidiary of France-based Schneider Electric was sued by the Chint Group for patent infringement at Wenzhou Intermediate Court over Chinese utility model patent 97248479.5 relating to circuit breakers.

In September 2007, the Wenzhou court issued an injunction against Schneider Electric and awarded RMB 334.8 million ($49.2 million) in damages to Chint. Schneider Electric appealed to Zhejiang Province High Court. Before the appeal was concluded,on April 15, 2009, Schneider Electric and Chint announced a global settlement under which Schneider Electric agreed to pay Chint RMB 157.5 million ($23 million).

With counterfeit luxury goods, substandard food products and pharmaceuticals, and pirated DVDs from China continuing to make the headlines in the West, China's emergence as the most active patent litigation jurisdiction in the world since 2006 has been little noticed.

Over 4,000 new patent infringement cases were filed with Chinese courts in each of 2007 and 2008. A small but rapidly increasing percentage of those cases — about 5 percent — involved Western companies.

In most of those cases, Western companies have won. However, the significant wins by Chinese companies as patent holders against Western companies have launched a new era in patent enforcement

and business competition in China, in which Western companies are increasingly sued as the alleged infringers.

The litigation between Chint and Schneider Electric provides some valuable lessons for Western companies.

A Tale of Two Forums: Intermediate Court and the Patent Re-Examination Board

Most patent litigations in China involve a patent infringement lawsuit before a specialized IPR tribunal of an Intermediate Court and a patent invalidation proceeding in the Patent Re-examination Board (PRB) of the State Intellectual Property Office (SIPO).

Over 60 Intermediate Courts around China can hear patent infringement cases, but PRB in Beijing has the exclusive jurisdiction to hear validity challenges to Chinese patents.

Schneider Electric is a global leader in electrical power distribution products and industrial control and automation equipment and apparatus. Based in Wenzhou, Chint is a leading supplier of low-voltage electrical power products in China.

In the fiercely competitive global market for electrical power distribution equipment, patent litigations are not unusual, but usually Western companies like Schneider Electric are the patentees/ plaintiffs claiming infringement by Chinese companies.

However, things changed in 2006, when Chint, without warning, sued Schneider Electric for infringing a utility model patent granted to Chint in 1999.

In its defense, Schneider Electric argued what Chint claimed in the utility model patent related to circuit breaker technology that Schneider Electric had been using for more than 15 years in numerous countries, including China.

Chint is a prominent private company based in Wenzhou, Zhejiang Province, a prosperous coastal city south of Shanghai. Chint gained home court advantage by filing its complaint against Schneider Electric in July 2006 with the Wenzhou Intermediate Court, requesting RMB 500,000 ($73,500) in statutory damages.

Schneider Electric immediately filed a patent invalidation petition with the PRB, which held oral hearings in December 2006. In April 2007, the PRB made a decision to maintain the validity of the Chint patent, stating that the prior art references submitted by Schneider Electric were insufficient to invalidate the Chint patent.

Schneider Electric appealed the PRB decision to Beijing No. 1 Intermediate Court and Beijing High Court in

succession. Beijing High Court decided in March 2009 to uphold the PRB decision.

Schneider Electric's invalidation case was hamstrung by China's existing patent law, which does not recognize prior use or sale outside of China as proper prior art.

The Chinese government recognized the shortcomings of this rule and has amended the patent law to adopt the absolute novelty standard, which will go into effect on Oct. 1, 2009. Unfortunately, Schneider Electric couldn't benefit from this upgrade of patent law.

While the invalidation case was moving along at the PRB, Chint, with the assistance of the Wenzhou Intermediate Court, obtained financial information regarding Schneider Electric's sales and profits on the allegedly infringing products.

Chint increased its damages request to RMB 330 million ($48.5 million). Wenzhou Intermediate Court held its trial in April 2007 and made its decision in September 2007. Schneider Electric appealed the decision to Zhejiang High Court, which held three hearings in March and April 2009 until the parties announced their global settlement on April 15, 2009.

Lesson 1: All Chinese Courts are Rocket Dockets

Western companies used to multiyear patent litigation in U.S. federal district courts will be shocked to find that all Chinese courts qualify as rocket dockets.

The usual time frame for resolution of a patent dispute where both parties are incorporated in China is six months from the filing of the complaint until the first instance trial. It takes only three months for the appellate court to hear an appeal.

In addition to the potential advantage of surprise, the lack of a formal discovery process in Chinese courts accentuates the plaintiff's advantages.

Litigants need to be prepared with their arguments and rebuttal as soon as the case is filed. With only six months before a case is over, litigants need to marshal their evidence well in advance of the court filing date.

Given the element of surprise, Western companies would be well advised to be thorough in their freedom to operate analysis and meticulous in their record-keeping and evidence gathering to ensure that they are able to respond quickly to litigation which could come from any corner of China.

Lesson 2: Do Not Wait to Be Sued

A party concerned about a potential patent infringement lawsuit by a competitor should consider declaration of noninfringement action and patent invalidation action to preempt the first-mover advantage of the patentee.

When a patentee sends a warning letter to a competitor, the alleged infringer may initiate a declaration of noninfringement action away from the patentee's home court.

As data on Chinese IPR litigation becomes more widely available, litigants are no longer limited to anecdotal information in selecting a forum.

The win-loss record of Western companies in a particular Intermediate court, the experience level of local IPR judges and the economic influence and political connections of parties in a jurisdiction are among the factors deserving careful consideration in selecting forum for patent litigation.

When there is no warning letter from the patentee, the concerned party may still be able to launch a preemptive strike by using China's liberal patent invalidation regime.

Any individual or organization can bring a proceeding before the PRB to invalidate a patent. It usually takes the PRB less than six months to hold an oral hearing and to decide the case shortly afterward.

Because Chinese utility model patents and design patents are not substantively examined, they tend to be vulnerable to well-prepared invalidation challenges.

Conversely, if the challengers are time-pressed to come up with prior art that satisfies the stringent evidentiary requirement of PRB, their challenges may be unsuccessful.

Western companies should take note that preemptive invalidity challenges may be a low cost and effective way of reducing the risks of patent infringement lawsuits in China. Chinese companies frequently file invalidation challenges against competitors' patents.

The PRB received over 2,000 new invalidation petitions in 2008. Western companies need to be vigilant in monitoring grants of utility model and design patents under China's first to file system and be prepared to act quickly.

Lesson 3: Do Not Look Down on Utility Model Patent

Western companies often ignore a low cost and expeditious method of building a patent war chest in China, i.e., filing for utility model and design patents.

Utility and design patents offer a shorter duration protection than that of invention patents (10 years vs. 20 years). These patents are not substantively examined and typically issue within a year from filing.

A utility model patent is granted for any new technical solution relating to the shape, structure or their combination, of a product, which is fit for practical use.

A design patent covers any new design of the shape, pattern or their combination, or the combination of color with shape or pattern, of a product, which creates an aesthetic feeling and is fit for industrial

application.

Under the newly amended Chinese patent law, for the same invention, an applicant can in appropriate circumstances file for both a utility model patent and an invention patent simultaneously.

When the utility model patent is granted in a matter of several months to a year, the patentee can take infringers to court. The utility model patent is replaced when the invention patent is granted, thus providing a full 20-year protection for the invention.

Although owning more than 50 percent of invention patents in China, Western companies typically have very weak utility model and design patent portfolios in China, accounting for as little as 1 percent and 10 percent respectively of the total granted patents in these areas.

However, as the Chint v. Schneider Electric case reveals, utility model patents can have remarkable economic value.

A robust portfolio of utility model and design patents should be built alongside an invention patent portfolio to fully utilize the potential of the patent system in China.

It Pays to Learn How to Litigate Patents in China

Historically, international companies treat their Chinese patents like the patents of other developing countries.

However, a confluence of factors, namely, a large market, relative low cost of patent procurement, a centralized national court system and speedy trials, are elevating Chinese patents to be among the most valuable national patents in the world.

Relative to the large size of their patent portfolio in China and frequent complaints of infringement, Western companies have been reluctant users of the Chinese court system.

This reticence flies in the face of the statistics that Western IP holders win most cases they file against infringers.

According to recent data, Western companies have a great chance of success litigating in IP courts in China, with about a 90 percent “win rate” in Zhejiang and Shanghai.

“Use our courts before criticizing them,” Chinese IP judges are telling Western companies complaining about weak enforcement in China.

--By Tony Chen (pictured) and Mark Cohen, Jones Day

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