

The Impact of the "Schneider" Case on the IP Strategies of Foreign Investors



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I. The impact of the "Schneider" case on the IP strategies of foreign investors.

There has been a growing concern among foreign investors in China regarding the explosion of registrations for utility models by Chinese companies, containing prior art belonging to western companies or even common knowledge in a specific technical field. Shortcomings in the Chinese enforcement system could lead to an increase of infringement lawsuits from Chinese companies against foreign investors based on these utility models. In a developing and politicized judicial system, these lawsuits can be successfully used by Chinese companies as a valuable, even unfair, competitive tool.

Such fears may be recognized because of the "Schneider" case. The Chinese company Chint Co. Ltd filed a patent infringement action against the Chinese subsidiary of Schneider Electric of France. The lawsuit was based on a utility model of an electric

circuit breaker that the French company had patented earlier in China. Foreign investors have become concerned that in similar cases, the Chinese judicial system will not guarantee them sufficient protection because of the lack of independence from political and local economic lobbies.

The German Association of Mechanic Industries (Verband Deutscher Maschinen- und Anlagebau) has expressed uncertainties in two interviews on January 2, 2008 in the "Financial Times Deutschland"¹ and on January 3, 2008 in the German magazine "Der Spiegel"². The legal advisor for the German Association of Mechanic Industries has cited the "Schneider" case as an example of unfair practices by Chinese industries and the lack of protection offered by the Chinese judicial system for foreign inventions. Consequently, the Association has suggested to its members that their inventions would be safer locked away instead of applying for patent registration in China, thus exposing them to unwanted risks of

duplication, and later to infringement suits. Without commenting on the position of the German Mechanic Industries, concerns resulting from the "Schneider" case have arisen among foreign investors in China. This case appears to set a trend inconsistent with the declarations of Chinese government officials regarding the modernization and improvement of the IP enforcement in China and with the principles on enforcement of IP rights set forth in the *WTO-Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)* of 1994, which finds application in China as well.

From the perspective of a foreign IP practitioner in China, it is important to comment on issues from the judgment in the "Schneider" case.

II. Analysis of the Controversial aspects of the Judgment of the Wenzhou Intermediate People's Court.

a) Novelty criteria vs. Scope of Protection

The Defendant Schneider had

rejected the assertion of infringement of the utility model of Chint by pleading the prior art defense. Schneider claimed that the alleged infringed circuit breakers were designed and produced in implementation of an earlier Chinese patent held by Schneider. They claimed that the French company's utility model had applied for patent protection earlier than Chint's utility model. The Wenzhou Intermediate People's Court accepted Schneider's right to plea the implementation of an earlier patent application.

In order to verify the technical content published in the earlier application, the Wenzhou Intermediate People's Court decided to apply art. 2.3, Part II, Chapter 3 of the *Patent Examination Guidelines* which is the

document which is devoid of any in-depth explanation about the Court's decision to apply a certain legal norm or standard of evaluation rather than another. In particular, after noticing the absence of any relevant provisions regulating the determination of the content of an earlier patent application in relation to a plea of implementing an earlier patent, the Court decided to apply the above mentioned norms of the *Patent Examination Guidelines* on the determination of a patent's novelty without explaining the interpretative process leading to this a choice. To this regard we initially observe that "reasoning" of judicial decisions, intended as the explanation of the logic and legal interpretative process through which the Court has reached

mind the function of a civil Court in a patent infringement case, the Court could have found that there are norms and standards of evaluation, which are more appropriate to this case than on the examination of novelty by the Patent Office. In particular, we refer to the norm of Art. 56 *Patent Law* on the determination of the scope of protection of a patent.

Actually, the choice of the standards for the determination of the scope of protection rather than those on the determination of novelty would have appeared consequential with the Court's own legal reasoning regarding the general admissibility in the Chinese patent infringement litigation of the plea of implementation of the earlier patent. In this respect the Court could have found guidance in the vast practice of the Chinese Courts in the past years regarding determination of the scope of protection of patent in infringement lawsuits, which was also consolidate in the "*Several Questions Concerning Patent Infringement Judgements Opinion*" (hereinafter the "*Opinion*") issued by the Beijing High People's Court on September 29, 2001. We notice that the Court had already cited the Opinion in this case as an authoritative interpretation of the law. However, there is no explanation by the Court of the reason for applying 2.3 Part II, Chapter 3 of the *Patent Examination Guidelines* and to exclude the use of alternative tests. In this respect, and beyond any final consideration on the appropriateness of the law applied by the Court in this instance, the "procedere" of the Court appears to be arbitrary and leaves the reader an impression of a selection of the applicable law dictated by pre-determined considerations of non-legal nature. Apparently the use of the norms on novelty from the *Patent Examination Guidelines* in determining the scope of protection

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norm regulating the determination of a patent novelty by the examiners of the Chinese Patent Office. The Court concluded that the drawings of the earlier patent, without any written explanation or reference in the patent claims, could not constitute references for the determination of the patent content. In this way the Court concluded that some of the features present in the alleged infringing products, which were corresponding to those disclosed in the utility model of Chint, were not disclosed by the earlier patent. Therefore, the Court rejected the substantial foundation of the defendant's plea of implementing the earlier patent.

A reading on this part of the judgment leaves doubts to a foreign observer that correct norms were applied. This impression is firstly induced by the reading of the

a certain determination or decision instead of another, is indeed one of the requirements of art. 41 TRIPS. This article is binding upon Chinese judges in force of China's accession to this treaty and of article 142 of the *General Principles of Civil Law* of China of 1986.

The fact that the Court decided to determine the novelty of the earlier patent rather than its scope of protection strikes the reader. It is evident that the Court, without explanation, had decided to ignore the fact that Chinese Civil Courts in an infringement case cannot judge the novelty of a patent but can only determine its scope of protection. In fact, it is not reasonable to state, as the Court did, that there are no specific provisions for recognizing the technical content published in the earlier application. By application of analogical interpretation, keeping in

of the earlier patent application of Schneider offered to the Court a more favorable tool to neutralize the evidence of the Defendant than those on the determination of the scope of protection. In particular, art. 2.3. *Patent Examination Guidelines* allows little room for the interpretation of the description and drawings of a patent.

In fact it cannot be excluded that by choosing to apply the norms and the related judicial practice on the determination of the scope of protection to the earlier patent application, rather than those on the determination of novelty, the Court could have reached a different conclusion as to the scope of protection of the earlier patent application. In particular, in accordance with the standard of determination of a patent scope of protection offered by the Opinion of the Beijing High Court (so called "eclectic interpretation" principle), which is also a principle common

system and most European national patent systems such as the German, Italian, and French³.

Such a *procedere* would have made the decision of the Court appear to be well founded and motivated rather than arbitrary as it appears to be.

b) Suspension for Confirmation of Validity.

Also worth of notice appears the decision of the Court not to suspend the infringement lawsuit in favor of the still pending invalidation procedure in spite of Chint's voluntary limitation of the scope of protection of its utility model in the parallel Invalidation procedure. This decision appears to be in conflict with accepted principles of law in China and abroad. Also, the decision of not suspending the infringement procedure, when the scope of disclosure of the Chint utility model is still uncertain, appears against any consideration of relevant aspects

and Patent tribunals, which in turn have the sole responsibility to hear patent invalidation suits.

According to the *German Patent Law*⁴ and judicial practice⁵, the voluntary limitation of the Patent claims either within an invalidation procedure before the Patent Court or in an ad hoc "limitation procedure" before the Patent Office, have retroactive effect to the date of registration of the patent. Therefore, the patent will be valid in the limited form since the time of its original registration. German law and legal case law are unanimous in stating that a voluntary limitation of the patent claims by the patentee will bind the Court of a related infringement case, which will have to take into account these limitations in light of the determination of the scope of protection of the disputed patent⁶. In Germany as in China the judge of the infringement lawsuit has indeed discretion over the decision whether suspending or not the lawsuit in favor of the invalidation procedure. However, such discretion cannot be devoid of any reason and motivation. If, in spite of a voluntary limitation of the patent disclosure and therefore in a situation of uncertainty regarding the content of the disputed patent, the judge still decides for not suspending, such decision will have to be motivated. However an explanation of the reasons leading the Court to the decision not to suspend the infringement procedure is not to be found in the Judgment.

Motivation was more necessary because the need for suspension in this case appeared well founded after the Court had also excluded the fulfillment of the condition for non suspension indicated in article 9(2) of the *"Several provisions of the Supreme People's Court on Issues Relating to the Application of Law to Adjudication*

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to article 69 of the *European Patent Convention of 1973*, the evaluation of the relevance of the drawings of the earlier patent would have been conducted through the test of a person skilled in the art (technical expert).

What in fact appears remarkable is the fact that the evaluation of the earlier patent claims, description, and drawings were indeed conducted by the Wenzhou Intermediate People's Court itself, out of its common sense, instead than through the appointment of a person skilled in the art. Whatever the test chosen for determining the scope of protection, this should have been carried out through a person skilled in the art. This is a common and accepted standard in most legal systems including among other the EU patent

of judicial economy and judicial management. There is no doubt that the decision of the Court might ultimately lead to conflicting and contradictorial judgments in the infringement and invalidation procedures.

In China as in other countries the voluntary limitation of the patent claims would surely be binding on the judge of a parallel infringement procedure (*Estoppel*). It might be interesting to have a look to the norms of another legal system. In this case, I suggest a look to Germany because their IP laws have strongly inspired the modern Chinese IP laws. In addition, both legal systems are based on the separation of competence between the civil Courts that are exclusively responsible for the decision of patent infringement suits

of *Cases of Patent Disputes*⁷ of June 19, 2001. In fact this norm provides that the suspension is not necessary if the judge finds out that the allegedly infringed product was indeed implementing a known technology, or per analogy an earlier patent application. Given that the Court had reached the opposite determination, that is the allegedly infringed product was not implementing any earlier technology or patent, and that moreover Chint had limited the scope of protection of its patent, thus creating uncertainties about its content, the suspension appeared to us as a necessity. Any decision to the contrary should have been strongly explained by the Court, but this was not the case.

c) Amount of Damages Awarded

The amount of damages awarded in this case is remarkable and we are not aware of cases where comparable damages were awarded against Chinese infringers in favor of a foreign claimant. Also, with regard to the determination of damages, it is our experience that in cases where western companies are the plaintiffs, Chinese Courts rarely authorize Auditing of Chinese infringers' books. Even if courts cannot refuse a request for evidence preservation of such accounting books, they will however subject it to conditions, such as an unmotivated request of exorbitant monetary deposits, which are virtually difficult to fulfill and therefore will discourage the foreign plaintiff to give execution to the order.

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III. Final Remarks

The Judgment in "Schneider" gives rise to concern. In particular, it shows the lack of proper judgment drafting and the almost complete absence of explanation and reasoning on which important decisions as to law, facts and evidence are made. This leaves the impression of a judgment characterized by uncertainty

It will not be surprising that western companies in the future collide with the floating mines represented by aggressively registered utility patents held by Chinese companies. The trend is set and the "Schneider" case provides a precedent from which others might take encouragement.

However, there are not only negative signs coming from the enforcement of IP rights in China. Beside the Schneider case, a growing number of successes of western plaintiffs show that it is possible to successfully enforce IP rights in China.

Therefore, it would be premature to recommend that foreign IP holders stop registering IP rights in China. The lack of registration of a patent in China will lead the foreign investor to renounce active licensing strategy in China. In addition, we should consider that, thanks to its registered patent and under optimal trial preparation before the higher judicial instances, Schneider still has an opportunity to win this case. Without registered Chinese IP rights, however, the chances would be substantially lower.**IP**

Reference:

1. "Firmen verzichten auf Patente" of Kirsten Bialdiga, Financial Time Deutschland, January 2, 2008, URL <http://www.t-online-business.de/c/13/84/94/06/13849460.html>.
2. "Lieber in den Panzerschrank" by Stefan Schulz, Spiegel Online, January 3, 2008, URL: <http://www.spiegel.de/wirtschaft/0,1518,526453,00.html>.
3. See art. 69 ECP, art. 14 German Patent Law, article L 613-2.1 of the French Code de la Propriété Intellectuelle, article 51 of the Italian Codice della Proprietà Industriale.
4. See articles 64 and 81 of the German Patent Law.
5. Bundes Patentgericht in GRUR 1987, 810, 812.
6. For leading cases see BGH GRUR 1962, 577 Rosenzüchtung.
7. Art. 9: "(...) However, under one of the following circumstances, the proceeding may not be suspended: (...) 2) where the defendant's evidence is sufficient to prove that its or his used technology has been known to be public."

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