

Recent Trends in Chinese Practice on Patent Damage Awards

While the holiday is just around the corner, the IP field has been flooded with various news. In a unanimous but short opinion, the United States Supreme Court handed a huge victory to Samsung on December 6, 2016, tossing out nearly \$400 million in damages it was ordered to pay to Apple in their long-running patent infringement case. Specifically, the Supreme Court reversed the Federal Circuit's Samsung v. Apple decision on damages and held that a design patent infringer's liability may be limited to the profits of individual product components (historically, patent owners were entitled to the infringer's profits from the sale of the entire product). While unambiguous in its holding, the opinion offers no clarity as to how courts should decide when profits can be recouped based on the entire article or when they must be limited to profits associated with individual components.

While excessive and unpredictable damages have been questioned in the U.S., China has been criticized for not awarding damages properly (i.e., patentees have not been adequately compensated), which consequently cannot serve as an effective deterrent to patent infringements and protect the incentives to innovate.

However, on December 8, Beijing IP Court ordered the defendant Hengbao Co. Ltd. to compensate the plaintiff Beijing Zhiqui Data System Co. Ltd the economic losses of RMB 49 million and a reasonable attorney fee of RMB 1 million, which became the highest damage award ordered by Beijing IP Court since its establishment in November 2014.

This short article briefs statute specifications and judicial interpretations regarding computing patent infringement damages, and introduces newest developments in China.

Statute Specification on Damage Awards

The Patent Law of the People's Republic of China (2008, "the Patent Law") provides the necessity of damage awards in a patent infringement action and articulates the methodologies of computing patent infringement damages, which have been specified in Article 65 of the Patent Law. According to the specification, the damages shall be determined in the order of: (i) patentee's losses; (ii) infringer's profits; (iii) patent royalties; and (iv) statutory damages between RMB 10,000 and RMB 1,000,000.

In practice, the determination encompasses great difficulty and simplicity; difficulty because it puts all burden on the plaintiff to evidentially prove his/her losses, infringer's profits, or patent royalties; simplicity because it creates a simply statutory damages scheme for a people's court to arbitrarily decide damages for over 90% of cases;² which ultimately result in relatively low damage awards in China.

Application of Methodologies and Judicial Interpretations

¹ Referred to a patentee or an interested party, individually or collectively

² The Legal Department of China Patent Agent (H.K.) Ltd., Theory and Practice Related to Patent Infringement Damages, CHINA PATENTS & TRADEMARKS, NO. 4, 12 (2009), which reviewed patent infringement cases between 2007 and 2008, stating "[a]mong all the 416 judgments imposing damages, only one was adopted the method of the 'infringement profits,' four were adopted the method of the 'appropriate multiple of license royalties,' and the remaining 411 were adopted the method of statutory damages." Id. at 17. In other words, about 99% of damages were decided applying the statutory damages methodology.

Patentee's Losses

The first, and the most preferred, methodology in determining patent infringement damages is based on the actual losses of the patentee. While the Patent Law is silent with respect to how the actual losses be calculated, the Several Provisions of the Supreme People's Court on Issues Concerning the Law Applicable in the Trial of Patent Disputes (Fa Shi [2001] No. 21, "the Judicial Interpretations"), in Article 20, ¶2, provide guidance on the calculation, basically, from the following formulae:

$Actual\ losses = (total\ number\ of\ lost\ sales) \times (reasonable\ amount\ of\ profit\ for\ each\ patented\ product);$ or

$Actual\ losses = (total\ number\ of\ infringing\ products\ sold) \times (reasonable\ amount\ of\ profit\ for\ each\ patented\ product).$

However, this methodology, in reality, became technically impossible to be relied upon, because of, for example, the patentee's unwillingness and/or inability to disclose either the number of lost sales or the profits of the patented product, the patentee's lack of actual patented product sales, no actual losses due to the market demand and its elasticity, and suffered losses that might be attributed by other factors (e.g. shrinking of the market or increased costs for raw materials).

Infringer's Profits

Once the patentee fails to prove entitlement to his/her actual losses, calculation will be shifted to infringer's profits. The Judicial Interpretations,

in Article 20, ¶3, provide a calculation to:

Infringer's profits = (total number of infringing products sold) x (reasonable amount of profit for each infringing product).

Similarly, this methodology is difficult to be relied upon due to, for example, great difficulties to obtain financial information such as accounting books from the infringer because China has no "evidence discovery" procedure equivalent to that under U.S. law, and because poor record keeping practice in China makes it inaccessible to the profits of a specific infringing product.

Reasonable Royalties

In the event that neither the patentee's losses nor the infringer's profits can be calculated, the third methodology, damages based on patent royalties, will apply. The Judicial Interpretations, in Article 21 ¶4, specify

[...] [A] people's court may reasonably determine the amount of compensation as between one and three times the value of the usage fees payable for the patent license according to the type of patent concerned, the nature and circumstances of the infringement, the amount of the usage fees payable for the licensing of the patent, the nature, scope, and period of validity of the patent license, and other factors...

Here unlike the practice in the U.S., the royalty refers to an "established royalty," as evidenced by a prior registered license agreement.³ Thus, it is difficult to apply the "patent royalty" methodology due to non-existence of prior registered license agreements or payment. Even if the patent has been licensed, uncertainties exist as it is usually up to the court's discretion which "reasonable multiple" should be used.

Statutory Damages

Per the principle of "who claims and who bears the burden of proof," a patentee who fails to evidentially prove its losses, the infringer's profits and the patent royalty, is, ultimately, relegated to a statutory damage award ranging between RMB 10,000 and RMB 1,000,000. Although simple and easy to apply, this methodology bears an arbitrary nature and unsatisfactory award amount. Moreover, the fact of difficulty and thus unavailability to the damages calculated from the three other methodologies leads to the dominant usage of a statutory damage award.

³ "Regulations on Patent License Agreements Recordal" (No. 62), Rule 19 specifies that "the patent administrative department may use a license agreement, where the type, duration, royalty calculation and amounts are recorded, as a reference for determining the infringement damages and for mediation."

Judicial Interpretations on Burden Shift of Evidence Production

Due to the difficulties for patentee to meet its evidentiary burden of proof on damages, the Several Provisions of the Supreme People's Court on Issues Concerning the Law Applicable in the Trial of Patent Disputes II (Fa Shi [2016] No. 1, "the Judicial Provisions II"), provide:

Article 27. [...] When the patentee supplied preliminary evidences and account books and information related to the infringement activities are under the control of the infringer, the court can order the infringer to provide such account books and information. If the infringer refuses to comply with the request by the court, the court can determine the profit made by the infringer based on the patentee's claim and evidences.

New Trends

Government Commitment

On November 4, 2016, the CPC Central Committee and the State Council issued "Opinions on Perfecting Property Protection System to Protect Property Rights," which clearly stated the commitments to intensify the punishments of intellectual property infringement, to increase the maximum of statutory damages, and to introduce punitive damages for willful infringements on patent rights or copyrights.

Beijing IP Court Measures—Increasing Damage Awards

Since 2015, Beijing IP Court has greatly increased the amount of compensation for infringement and reasonable expenditure of litigation. In afore-mentioned case, Beijing Zhiqui Data System Co. Ltd v. Hengbao Co. Ltd., Beijing IP Court calculated the damages from the plaintiff's loss based on the total number of infringing products sold and a reasonable amount of profit for each patented product, where Beijing IP Court conducted its own investigation and evidence collection into 12 banks nationwide including Bank of China to acquire the number of infringing products the defendant sold, and accordingly reached at a calculation of actual loss RMB 48.142 million. In considering other infringing factors, the Court finally issued a damage award of actual loss RMB 49 million and a compensation of attorney fee RMB 1 million.

Even for statutory damages when no other methodologies were available, Beijing IP Court has surpassed the upper limit of RMB 1 million in the "dynamic balance valve" patent infringement case, and ordered the defendant to pay an economic loss of RMB 1.5 million after considering the factors of the defendant's business scale, subjective malice, patented

products and the alleged infringing product price, and industry profits.

Beijing IP Court Measures—Shifting the Burden of Evidence Production to Defendant

Recently, Beijing IP Court has reduced the plaintiff's burden of proof on damages by avoiding a mechanical application of "who claims and who bears the burden of proof" principle and shifting the burden of evidence production to defendant. Effectively relying upon Judicial Interpretations II, Article 27, the Court has clarified, in many cases, the burden of proof of the defendant and the legal consequences of refusing to provide evidence without justification.

In a trademark infringement case (trademark "Qianggu" in Chinese), Beijing IP Court ordered the defendant to submit relevant evidence

regarding the actual operation of the company and clarified legal consequences of non-submission. When the defendant refused to provide the ordered accounting books and other information, the Court granted a total of RMB 10 million damage award based on the plaintiff's claimed loss and reasonable expenses.

In sum, as discussed above, several of the more notable patent rulings from Beijing IP Court, as well as people's courts nationwide, have been associated with relatively large damage awards. These rulings were in line with the Chinese government commitment on intellectual property rights enforcement, and have provided some additional guidance regarding how patent damages might be calculated with a particular focus on "burden shift."

The newsletter is not intended to constitute legal advice. Special legal advice should be taken before acting on any of the topics addressed here.

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