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From Infringement to Innovation: Counterfeiting and Enforcement in the BRICs

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J. Benjamin Bai,* Keith D. Lindenbaum,** Yi Qian,*** and Cynthia Ho****

MR. LEV: We're going to get started again for the final panel.
I'd like to again thank Foley & Lardner for being the Premier sponsor of this event. There will be a reception immediately afterward so I won't say anything else at the end. But just one word. I'd also really like to thank Jones Day and Ben Bai for being here as well from Dallas, because they're sponsoring this particular panel.

If you're here getting CLE credit, this is important, in order to get the CLE credit we need you to fill out those two forms that you got in your CLE materials and either give them to me or Jodie, who is in the back of the room, or just leave them on the table in the Atrium where you registered, and we'll make sure that your certificates get e-mailed to you.

So without any other words I'll leave it to Professor Ho to start the panel.

MS. HO: Hi, Everybody, and thanks for sticking with us on a beautiful Friday afternoon in Chicago. I think we've got a really exciting panel, so I'm happy that you're all with us.

I don't want to spend a long time on introduction of speakers because I want to leave plenty of time for their presentations and discussions, so let me just briefly introduce you to our speakers and sort of the general topics.

We're basically building upon what we talked about in the last panel. The last panel we got sort of a detailed overview generally of the laws in the various BRIC countries, so what we're going to do in this panel is move more towards enforcement issues. So I've got three panelists to talk about three slightly different issues.

We've got Benjamin Bai from Jones Day who is going to first talk about infringement and enforcement using China as a case study.

And then Keith Lindenbaum from Foley & Lardner is going to talk about enforcement in BRIC countries in generally.

And finally Yi Qian is going to talk about I think mostly China.

MS. QIAN: Actually, most general.

MS. HO: General again, but I think the real distinction that she's going to bring is an economic perspective.

So I think we're going to have a really interesting discussion here amongst our panelists, and then finally we'll open it up for discussion.

* Panel speaker. Dr. Bai is a partner with the law firm Jones Day.
** Panel speaker. Mr. Lindenbaum is a partner with the law firm Foley & Lardner LLP.
*** Panel speaker. Ms. Qian is an assistant professor in marketing at Northwestern University Kellogg School of Management.
**** Panel moderator. Ms. Ho is an associate professor of law at Loyola University Chicago School of Law.
So obviously we've got both practicing attorneys with global IP experience, as well as an academic perspective.

So without further ado, I'll let Benjamin get started.

MR. BAI: Thank you, Cynthia.

Let's do something fun here because you're tired. You're thinking, "Gosh, how am I going to sit through this next hour, especially when Professor gets up and talks about economic theory." Let's do a show of hands. How many of you have heard China has IP enforcement problems, raise your hands.

(A show of hands.)

MR. BAI: You haven't heard? Anyone else? You haven't heard China has got IP problems? Everyone, right?

I'm not going to ask -- please keep your hands up. I'm not going to ask you to tell me who has personally enforced IP, because I know there are law students here, so the question is who has personally enforced IP or heard of someone who personally enforced IP, keep your hands up.

UNIDENTIFIED SPEAKER: In China?

MR. BAI: Sorry?

UNIDENTIFIED SPEAKER: In China?

MR. BAI: Yes. I'm talking about China. Okay. Look around. There are still quite a few hands here. So what are the results? Did you lose or did you win?

UNIDENTIFIED SPEAKER: Win.

MR. BAI: You won. What about the rest of the hands?

UNIDENTIFIED SPEAKER: I think it's an ongoing process still.

UNIDENTIFIED SPEAKER: We lost, but not in court. There were government officials involved and they covered the whole thing so we couldn't even sue.

MR. BAI: They covered the whole thing. Let's talk about that. The reality is a lot of people have heard of problems, enforcement problems in China, but I will have data to show you that not a whole lot of people went into China and enforced their IP.

Rule No. 1, IP rights are private rights. If you don't enforce your rights, you should not cry foul on the sideline. This is true in the U.S., this is true in China, and anywhere else in the world. Rule No. 2, subject to some exceptions, IP rights are territorial, especially patent rights.

Copyrights are different. You know, China is a member of the Berne Convention so you can have copyrights created here and enforceable in China, which people have done.

Trademark, sort of halfway in between. If you don't have a patent in China, you can't complain these guys are infringing your patents. In fact, I made a lot of money by clients who came to me and said five years ago, "I didn't file a patent application in China, now these bad guys are knocking me off." Instead of going into China to enforce a patent, we had to come up with a very complicated scheme to enforce their rights. How to do it? Because if you have a patented component made in China where you don't have a patent right, when you import it into the U.S. I can file an ITC proceeding, I can sue them in District Court. But do you know how expensive that is? An average patent litigation case going from start to finish going through trial, $3.5 million. In China I can do it for half a million dollars for a very complicated case. So this is sort of the reality.
If you don't file in China, then there is -- when it comes to time to enforce your rights it is very expensive. And also they make things in China and then ship it around the world, you have to file also in Korea, Japan, Germany, France and U.S., and you know what, only the good old United States has broad discovery procedures. So what you ended up having is in most jurisdictions you don't have discovery, you don't have evidence of infringement, you can't even get into court. But if you had filed a patent application in China, you would have solved all these problems.

With that background, let me get into my presentation. Julie Lee laid a very good foundation for my speech, so I'm not going to repeat what she said. In China it has a two track enforcement system, which is unique. In the U.S. you only go to courts, other than customs agencies which are ineffective, as ineffective as Chinese customs. You almost have no hope of finding infringing goods just because there are so many shipments coming in and out.

In China you can go to various agencies for trademark, copyright and patent infringement, and the vast majority of these cases, administrative cases involve Chinese parties just because most foreign parties don't know about it. It is actually quite effective if it is simple cases.

What Wall Street Journal or New York Times didn't tell you is in 2005 China became the largest, the most litigious country in the world for IP disputes. This is sort of the double digit growth that they saw in terms of IP suits filed in Chinese courts, these are courts of first instance. While the economy is going through double digit growth, so are their lawsuits.

I'm not going to go through all these statistics. Just look at 2005 because this is sort of the watershed year for China. China saw 13,000-and-some lawsuits, whereas United States saw about 11,000. There are a similar number of patent cases. I'm a patent lawyer and I specialize in patent cases, so these cases are more interesting to me.

One shocking statistic is that of 13,000 cases, there are only less than 300 cases that involved foreign litigants, defendants as well as plaintiffs. Now, you can draw the conclusion. The whole world says China doesn't protect IP, so this perception became reality and people don't go into China and enforce their rights. As private rights, how can you even cry foul when you don't enforce your own rights? I've said enough so I'm not going to repeat this.

Also on the legislative front, China has seven forms of IP crimes. I'm not going to read through my slides, and you don't need to read it either because it is Friday afternoon, 4:00. To summarize, for certain serious cases of copyright, trademark infringement cases it is criminal. The seriousness is defined by the number of copies or economic losses you cause -- that infringers have caused to the rights holder. If that is the case, then it is criminal, and each year 300-some people were sentenced to jail for IP infringement.

Now, let me compare this to the United States. How many people went to jail last year for IP crime? I would say no more than ten.

So United States filed a WTO complaint about what? About this IP criminal code. There are two complaints. One is market access, which has nothing to do with IP. Another is pretty much copyright issues. They were complaining about the threshold for criminal -- the criminal statute to kick in is instead of 1,000 copies. If you sold more than 1,000 copies then some of these codes will kick in.
¶42 The Chinese Supreme Court just issued an interpretation about a week before this complaint was filed, and lowered from 1,000 to 500. That was not good enough for the USTR. They said, "Well, you know, there is still a safe harbor because if someone sold 499 then he's not criminal. Well, yes, he's not criminal, but there are civil remedies.

¶43 I debated yesterday in Washington, DC, with the USTR on this issue. I said these laws are TRIPS compliant. So if there is any TRIPS scholars here, I'm willing to debate with any one of you. These laws are more than TRIPS compliant. It has got more -- basically China has gone further than the United States. I actually challenge anyone to find similar criminal codes in the United States. I challenged the USTR to find me codes, and he said, "Yes, we do. In the U.S. we do." But he couldn't quote me the sections, so you draw conclusions.

All right. Let me talk about some of the fun stuff. How do you sue? They're only two years of the statute of limitations, so you've got to do it very quickly and it is a known or should have known standard. So if you don't do it, two years go by real quickly. There are ways to toll this statute of limitations. This is a very quirky Chinese law. I don't think I have time and I'm not going to explain this, how to do it.

¶45 There are declaration of non-infringement, which are similar to DJ actions. So instead of being a defendant you could bring a lawsuit to be a plaintiff.

¶46 In China there are two instance court systems. The first instance is a trial court with appeal goes to the second instance. IP cases are mostly started in intermediate courts with appeal as a matter of right goes to the higher court. There are cases where you can file in the High People's Court as the first instance case and with appeal going to the Chinese Supreme Court. The reason sometimes you want to do that is for -- to avoid bias and maybe if you want more sophisticated judges to handle your case.

Also I say this to you: The justices in the IP court on the Chinese Supreme Court are more educated than some of our judges. They speak English really well, they have electrical engineering degree. I have currently a case before the Beijing Higher Court, and normally there are three judges who hear cases, and two of them have technical backgrounds. The lead judge has an electrical engineering background. My case relates to telecommunications, so I actually feel comfortable because I'm representing the defendant and I know if I get a sophisticated judge we have a shot.

¶48 Venues are similar so I'm going to skip to what you're familiar with. Forum shopping is extremely important. If you ended up in a wrong forum, you have no chance of winning, just like if you ended up a lawsuit in Angleton, Texas, you have no chance of winning either. You probably don't know where Angleton, Texas, is. That is where Merck lost its Vioxx trial. I guess it's a bad joke or it is just a Friday afternoon.

¶49 Rules of evidence. This is where, this is where the problems come from. It is not that China doesn't protect IP. China needs to revamp its rules of evidence of civil procedure. A lot of people are barking up the wrong trees saying you got to amend your patent law or trademark law, but to enforce IP you've got to get into Chinese courts and you got to evidence, right? There is no discovery, and the plaintiff has the burden to prove infringement. If you don't have a case, you can't file a complaint and say, "I'm going to do discovery. I think I've met my Rule 11 obligation so I'm going to do discovery. There is no discovery to be had." If you don't have it now, you're not going to get it later. That is the problem.
So a lot of cases where we know these guys are infringing, but we have a copy from our friends who works there and he showed us the drawings, we knew these guys are infringing, but with this evidence you can't go into court because that's not original. The Chinese courts demand original.

The rules of evidence are drafted with these fundamental thesis, that people cannot be trusted and given the chance they will lie and don't trust any experts because they can be bought, their opinions are worthless. So when you bring two experts to fight in Chinese courts, guess what, they hire their own expert. They disregard your experts and they hire their own expert.

Oral testimonies are almost given no weight, so that's why you can't drag someone in and say, "I saw this guy do it." It is not going to work.

So those are the quirky aspects of rules of evidence in China that makes litigation extremely difficult. Is it different from the rest of the world? No. Germany is exactly the same way. I had cases in Germany, it is the same situation. U.K. got some limited discovery that is helpful. And the French similar to Germany except they have the seizure order. China has the seizure order too, which I will get to.

The point is there are systematic issues which don't relate to substantive law. The substantive law is actually pretty good. When it comes to procedure stuff, it is up to China to change it. It is not up to us to cry foul. And also it is up to us to understand it so we can help our clients to win, to navigate through these procedural hoops.

How do you gather evidence if you have no discovery? Well, this should not surprise you. You hire a private investigator. It sounds like we're doing divorce cases. Or the more common way is if there is an infringing product on the market you do what's called a notarized purchase. Any evidence in China is preferably -- should be preferably notarized. And then you can use criminal proceedings or administrative proceedings first to discover some evidence.

Police in China have unlimited power. Let me emphasize this word unlimited. So nobody can do discovery, but they can do discovery. So if your case rose to the level of criminal offenses, then get the police involved. That means you've got to build a relationship years before this thing happened. If, say, you don't pay attention to the police and all of a sudden you have a problem, you go there and say, "Take this $50,000 and please help me." It doesn't work.

I'm kidding. You can't bribe.

The most powerful one is evidence preservation. It is similar to the French seizure order. You go to court and you say, "Your Honor, these guys may destroy evidence if you don't issue an order, if you don't go there and preserve evidence." And normally they will do it and that's how you can get evidence.

I'm going to skip all this procedural stuff and I will show you a couple cases where international companies have won in China. Julie had a couple references to Starbucks and 3M cases, which I'm also familiar with, but I just want to have a couple more cases to actually show you.

Hansgrohe makes high-end bath and shower products. They are extremely successful in China. They sued this infringer in China and this is the result. They asked for -- because their damages, their loss is not huge in China, so they asked for 500,000 RMB and they got 334,000 RMB. This is about 70 percent of what they asked for.
Anyone who litigates in the U.S. knows if you get 70 percent of what you ask for, that's a damn good result. I'm not going to get into the detail.

Another one is a very famous trademark and copyright infringement case that involves ETS and GMAC. Beijing New Oriental School is a school that prepares students to take those GRE, GMAT, and TOEFL exams. Some of the students from China they almost got perfect scores. It's all because of the good work done by Beijing New Oriental School. Years ago they went to ETS and GMAC and asked for a license, and they were told to go to hell. So they said, "Okay, I'm just going to copy." So they did, and they got slammed with about a million dollar judgment for copyright and trademark infringement. The appeal -- the appellate court said, well, there is not really copyright -- there is not really trademark infringement because it is a fair use. I'm not going to get into why they did it. But copyright infringement, yes. So they shaved the damages award by 30 percent.

This still represents one of the largest damages award in China for IP infringement that involves foreign parties. 700,000, not bad by the Chinese standard.

The point is, in fact judges told me, privately and publicly Chinese judges say that. Give me the right evidence, I will award $100 million, but you've got to prove it. The difficulty lies that there is no discovery in China, so how do you prove that. And if you're not in China, operating in China, then you really don't have a loss. Your loss is theoretical.

Just like Microsoft claimed that they lost billions of dollars due to piracy. That's a theoretical loss too.

Okay. Talking about a software company. Autodesk is extremely successful in China. The reason why is they go after everyone who infringes their software. It is easier for them to do because they sell high-end software. It is CAD, AutoCAD. It is worth a lot of money, it used by architectural firms, so it is easy to target these companies.

The result? They asked for -- in this case essentially they got almost what they asked for, so that's really pretty good, and they also got some litigation expenses as well.

So all these cases demonstrate that if you know how to litigate in China, with the right evidence you can win. Nothing is easy in China. Doing business in China is not easy. This go to China and get rich quick scheme is not going to work, but if you understand the system and you have to adapt from U.S. or European mentality to this Chinese unique legal system you are going to do well.

And with that I'll end my speech and thank you for your attention.

MR. LINDENBAUM: Thank you all so much for staying until the end of the day.

I'm going to start off with the conclusion just in case we don't get there. I'm going to tell a story. My son, who is now getting ready to go to college, when he went into high school we got him his own computer that he could use in his own room. We gave it with one caveat, being the intellectual property attorney that I am, that he could do no file-to-file sharing for MP3 files for music. You would think that we had punished him beyond reproach. That they ought to call in social services for this sort of decree in our house. A tantrum like we hadn't seen since he was about three. How could you? Everybody does it, was his biggest defense. Though I stuck to my guns, and what did we do? We bought
him an I-Pod. Along comes I-Tunes and everybody is happy. Parents and relatives and grandparents give him I-Tune gift cards for the holidays and he's happy.

¶72 The lesson here, I'm going to suggest, is that we need to look for alternative economic models. We do it here in the U.S. We can do it in the BRICs. You heard Benjamin Bai talk about the wonderful enforcement in China, so you would think that there would no more infringement, that it would all go away. But the fact is that there is more to -- there is more to enforcement than just having a good legal system and having a good court.

¶73 I'm going to talk about seven strategies. The first one is the legal structure. You have to have this. This is sort of a cornerstone. You have to have a fundamental legal structure. For me to argue to my son that he can't do it, it has to be against the law, that was successful, at least on my end.

¶74 Sanctions and coercion. We in the U.S. use sanctions and coercion. We've used it historically to force all the BRIC members, Brazil, Russia, India and China, to adopt the Paris Convention, Berne, TRIPS. And we're still using coercion today. Just this week the U.S. announced tariffs on glossy paper coming out of China, and of course we filed a complaint with the WTO which will play out.

¶75 Enforcement. You have to have enforcement. If you can't enforce your rights, this is key.

¶76 But these three things alone are not enough. Publicity. You have to be able to publicize your company, the good things your company is doing and the fact that enforcement here has a public benefit.

¶77 Education and training has to start at a very young level. You know, we again asked the question of our school where we sent our son, "Do you educate that stealing MP3 files is wrong?" Of course the answer there is no. You'll see in China they have an eighth grade program directed towards education for piracy.

¶78 Corporate citizenship. You need to view if -- for our corporate clients we counsel them that if you're going to be in China you should be perceived positively and that will help you a long way to get the public and government on your side.

¶79 And finally the conclusion, alternative economic models. There must be an alternative economic model that makes sense. I think it will work not only in the software and MP3, but it will work in pharmaceuticals and other areas as well.

¶80 Okay. Legal Structure. Paris Convention goes back to 1883. Before 1883 you had to file your patent in all countries simultaneously around the world. Now if you're a member of the Paris Convention you can file in one country and have one year to file in others. The Berne Convention covers copyright materials and was adopted in 1886. TRIPS, more recently in 1994, this addressed the question of uniformity. Just because you have patent laws doesn't mean that they're uniform, and if you don't protect certain types of rights that doesn't make all that much of a difference. And finally you have to have penalties, you have to have some bite to these laws, both civil and criminal.

¶81 Let's talk a little about sanctions and the effectiveness of sanctions and coercion. We'll talk about an example in each one of the BRIC countries.

¶82 Russia. You know, we're still using, by the way, the idea of sanction and coercion with Russia, arguing with them and negotiating with them over WTO. If you look at the list of who is on the WTO, really Russia is one of the few really more industrialized countries that is not a member of the WTO, and a large issue of contention has been IP
rights. So we've used this WTO carrot as sort of a way of inducing Russia to improve its IP position.

¶83 India. We throw out a loss of aid, and they've adopted to TRIPS. China. We've had this cycle of threat and sanctions and tariffs with China for a number of rounds now. It turns out that we'll threaten China, as we did, or impose tariffs. China will threaten to impose tariffs back. And then there will be some negotiation, and then we end up with an agreement, and then the infringement continues.

¶84 In Brazil there has been pressure to protect pharmaceuticals in the 1980s. And this was -- because they didn't, we applied tariffs, they countered with other tariffs on things that matter to our industries. Like Xerox, Dow, Ford and Carrier all complained on the tariff that the U.S. imposed. The U.S. imposed tariffs on Brazilian industry and that comes back to hurt the U.S. because we have our products manufactured in Brazil.

¶85 So now let's take a look at -- in terms of fosters retaliation, China is a good example of this, as I mentioned. So this week, as I said, we placed tariffs on glossy paper, about 21 percent. What do you think the response will be? Do you think that China will immediately address whatever the grievance is of the U.S. or do you think they'll begin to formulate tariffs of their own? I'm going to guess that they're going to begin to formulate tariffs of their own.

¶86 We filed a complaint in the WTO. Do you think that China won't look for other reasons to file their own complaint in the WTO? I'm going to guess that they're going to do the same. There will be some negotiations, there will be some settlement, and the infringement will go on.

¶87 You know, this last point here that's on the slide. Beside the -- even if sanctions are effective in getting the government to say they're going to do things and to pass certain laws, unless you address the underlying reasons for piracy and counterfeiting, and that is poverty, unemployment, and in the issue of pharmaceuticals it's a moral imperative, you're not going to solve the problem.

¶88 Again, I think that an alternative economic model is really what's going to be key here in winning over and asserting rights in the various countries.

¶89 Let's talk about enforcement. These examples are put out by the IIPLA. The IIPLA puts out a report every year, the International Intellectual Property Alliance. They estimated that there were $13 trillion worth of trade losses in the U.S. due to piracy of software and copyright-related materials. Brazil, $158 million, Russia $1.7 trillion. So it's significant numbers.

¶90 The motivation for these numbers I think is clear. In India you have 8,000 pending cases, 70 convictions in 2006. So even though India may have robust laws on the book and a mechanism for enforcement, if you only have 70 convictions you can sense that something else is at work here.

¶91 The statistics for Russia. 3,400 individuals convicted of copyright infringement of which five served a prison term. This one I think is somewhat suspect, as Benjamin pointed. We have ten people in prison from the U.S. and I don't know that this number is particular relevant.

¶92 Let's talk about the strategy of publicity. Example, this is Heinz Corporation in China. They had companies that copied their delivery trucks, copied their uniforms, and copied their product. What did they do? First of all they worked with local enforcement agencies, the local government to go in and raid these companies. What they did is they
paid reporters to cover these raids to try to give publicity and visibility to the governing agencies that were actually doing their job.

Coupled with that they had a public campaign that talked about not the importance of intellectual property but rather spoke to the importance of public safety. The baby formula of these companies was unregulated, wasn't safe, not necessarily following the appropriate formula. They appealed to the public safety concepts within the citizenship, and have had a lot of success using this -- this strategy.

Education and training. Just because you have laws on the books doesn't necessarily mean that people know what they need to do. My son being an example. Not educated that this is an important quality, an important feature. And I think that if we raise all of our children that it is okay to copy MP3 files, what will happen when they go to college and become members of corporate boards or corporations? What will be their ethics and ethos in making decisions about whether or not to copy?

So you have to educate not only your government agencies but your citizenship as well. And China, I think to their credit here, has a middle school program entitled "Say No to Piracy, Starting With Me." Reminiscent of our "Just Say No" to drugs. But I think you need to start fairly young. Obviously it's going to be quite a long time before these eighth graders will be in positions of corporations that will make decisions, but I think you need to start when they're this young in order to have an impact.

Here is an example of a telecommunications company in China taking a strategy of donating to local charities. Here they had a publicity campaign that they were committed to China, that they were going to invest locally in China, and they began to educate people in that.

It sort of reminds me of the Japanese car companies in this country. I worked before I went to law school in Detroit where we had -- where the Japanese car companies were not viewed highly. But what did they do? They came in and built plants in this country. They hired local workers. So it took the union -- beside the fact that they were not all unionized, it took away the argument that there was no benefit to Americans for buying Japanese. And, of course, today we see the Japanese car companies are very successful, and I think that many of us do not feel that when we buy Japanese we're somehow unpatriotic because we are supporting jobs in the south and wherever they have plants.

So this telecommunication company in China took the same sort of approach, investing in China, giving to local charities, making people feel that that company has Chinese interests at heart.

I'm on the international business team at Foley & Lardner and my focus is Israel, so I spend a lot of time in Israel. I bring this up as an example. By the way, Israel, if you look at Priority Watch List, is often up there with the BRICs. The "I" could be Israel or Ireland just as well as it could be India except the size is not as impressive. But they do have the same sort of challenges, they're also a developing country trying to come up to Western standards.

But recently U.S. Commerce Deputy David Sampson, this is February of this year, was in Israel, and during a visit he made a point of pointing out the companies that are doing business in Israel, and not the fact that they're doing business but their corporate citizenships, the charities that they run.
¶101 Let me go through these because they're interesting; they're all related to education. Microsoft has training for underprivileged youth in over 100 centers throughout the country using computers and using their system. Intel has a program to introduce teens to high tech, to improve their advanced technology and self-esteem, but it's education based. Motorola, a program to promote education, technology training, advanced math classes. IBM has programs in poor schools. Again, notice all education. Cisco, after-school computer training programs in the underprivileged areas. And this is not only something that the independent companies talk about but also our trade representatives talk about as, well, the idea that these companies want to create in the mind of Israelis that what is good for IBM is good for Israel.

¶102 Let's talk about the alternative economic model, which is really what I want you to take away from here. This is an example in Brazil, Nike. Nike had the manufacturing rights for football jerseys for the Brazil football teams. And, of course, by football we mean soccer. Nike came out with a shirt for 170 -- is Brazil dollars? Whatever the Brazilian currency is. The pirated version was sold for 20. So you can see the ratio is, what, eight, nine-fold. When there is that gap it is difficult to convince anybody not to buy the pirated. So what did they do? They revamped their marketing. They came up with a different jersey, a little simpler, a little less cost, and they put it at a price point that was only twice that of the pirated version and had great success. I think you will find most populations with some education there will be a response to want to buy the official jersey as opposed to the pirated one, but that gap has to be reasonable.

¶103 Okay. So what's my conclusion? The use of sanctions solely to create legal systems and enforcement is just not sufficient. As long as the underlying problems remain that the gap between the pirated version and the non-pirated version is significant, we're going to find ourselves with continuous infringement problems in these countries.

¶104 It requires a multifaceted approach. Cooperation with local and national government officials for government. You have to have publicity in the right areas to support those efforts. Enforcement in a positive way. Corporations must be actively involved in the communities through education and training and other sort of corporate citizenship efforts.

¶105 And, finally, I think most importantly, like the example of I-Tunes, where we're no longer making kids buy entire albums but for $1 you can buy the song of your choice, you have to have an alternative economic business model that makes sense for the population and the group that you're trying to pursue.

¶106 Thank you very much.

¶107 (Applause.)

¶108 MS. QIAN: So thanks, Dan and Jodie, for inviting me here and for organizing this program. Thank you for the persistent people who stayed here and for the newcomers.

¶109 So I would like to talk about economics of intellectual property rights and antitrust, and in particular I have three papers around this topic. One is a forthcoming paper in the Review of Economics and Statistics, whether patent protection -- domestic patent protection in the pharmaceutical sector could stimulate more domestic innovation using a cross-country analysis over two decades for about over 80 countries. And then the second paper I will say a few words about is going from innovation to infringement, the flip side of IPR, which is counterfeits and imitations. So I explore the pricing and marketing effects of counterfeits and imitations. And then the final paper I have, which I
will not talk about, I will not have time to talk about in the presentation but I will be
happy to talk about after the talk, is how to balance patenting and antitrust.

So let's focus on the first paper first. The rationale for patent policies really focuses
on that after we provide the promised ex post rewards for inventors then we could help to
stimulate incentives to innovate ex ante. However, there are numerous theoretical or
practical counter arguments for that. The ones I list here basically include Scotchmer and
Green's paper discussing why patenting and intellectual property rights protection could
stifle sequential innovation where innovations build upon each other. And some other
international scholars discuss that in the current environment where we have very
sophisticated patent systems in the Western countries like U.S., U.K., et cetera, additional
patent laws are not going to help stimulate anymore innovations. And there are also case
studies done on individual countries by Lerner and Jaffe, and others, how patent laws
affected domestic innovation in each particular country, such as the U.S., Italy, Canada,
et cetera.

But the problem with these are that the empirical findings have been largely
inconclusive, so some papers found that patent has positive stimulation effect but others
find the opposite fact in Italy. And by looking at the whole country in one paper you
cannot generalize to the entire world, and that's what TRIPS agreements are trying to,
is to generalize intellectual property rights to the whole world based on the assumption that
patent laws have similar effects on stimulating innovation for different countries.

That's where I pick up the research thread, whether national intellectual property
rights protection is beneficial to developing countries.

Now, the argument for implementing patent laws in developing countries is that it
could somehow stimulate national patent -- national innovations in several ways. One is
that additional patent laws may provide favorable environment to try out innovations
locally. And another one is individuals had to switch from imitative activities to
innovative activities once the country implements IP laws. Perhaps the most heated
debate comes from how much innovation could be stimulated, and the least controversial
argument I came up by PhRMA was that because these developing countries currently
who do not have patent laws may not have the market to stimulate innovation for these
developing countries' specific diseases.

So the argument is that after a group of countries who implement patent laws
together they could provide more incentives for global innovation for these country-
specific diseases. We haven't seen that so far, even after TRIPS has been implemented.
And very little empirical research has been done for non-OECD countries, and that's why
I tried to bring together a sample that contains both the developed countries and
developing countries.

In terms of methodology I'll go relatively brief, but just to highlight that. Because
we cannot observe counterfactual outcomes of patent protection, that's what if the country
did not implement their domestic patent law what would have happened; therefore, using
international comparisons could provide important leverage. So by comparing countries
of similar characteristics besides domestic patent laws, any difference in their innovation
outcome could mean more comfortably attributed to the patent law difference.

So I begin with a rigorous study design to construct a database that approaches the
ideal experimental data given the limitations of observational studies, meaning that the
data I get is from tracing the historical data instead of doing a true experiment. The way I
construct the database to approach experimental design is to use a matching algorithm to establish comparable country pairs to ease the reverse causality concern, which is sometimes called endogeneity. Then I do panel analysis on the selected sample countries.

So let me highlight the key findings, so that if I lose you in the next few slides at least you have the take-home lesson.

National patent protection alone does not stimulate domestic innovation, as estimated by the citation-weighted U.S. patent count awarded to innovators in different countries. And I also use alternative measures for innovation such as domestic R&D and exports in the pharmaceutical industry, that's how much Chinese pharmaceutical companies export to the U.S. market.

Second, national pharmaceutical patent implementation seems to accelerate innovations in countries where they already have the innovative potential. And the innovative potential is measured by higher development level, education attainment and economic freedom.

And further, there appears to be an optimal level of intellectual property rights regulation above which further enhancement of protection reduces innovative activities. And I'll show you a figure showing that result.

So basically these results are quite intuitive. What it says is that any hope that we can base our innovations simply on patent systems is false hope. What we really need is a combination of infrastructure, one piece of which could be a sound patent system, together with your innovative potential, that's your development level, education attainment, and economic freedom. And it's important to balance your intellectual property rights regulations according to your country-specific needs.

So here is a figure that shows. The pink line is the complete sample countries and the blue line is highly enforced countries, and this traces out the innovativeness of these countries relative to the year they implemented their domestic pharmaceutical innovation, product innovation in particular. So what you see is a downward slope trend for the highly enforced countries relative to the pink for the complete set.

Let me just say a few words about how I overcome some practical limitations in drawing that causal inference. First practical limitation in looking at the affects of patent protection on domestic innovation is that there is not a single time line when all the countries in the treated group, which is the newly patented group, start implementing their patent laws at the same time. So what I do is to define five periods accordingly as reference periods. I group the countries that started their pharmaceutical patent laws as similar times together.

And another key concern is the endogeneity, which is your reverse causality of national patent laws. As some of the previous panelists said, a lot of countries implemented patent laws when they actually have more innovations to be patented. So that could be the reverse causality if we just look at the correlation of figures between patent law and the innovation level.

So to overcome that -- let me talk a few more words about this reverse causality first.

So why do we think that patent policy could be endogenous, which means it could be deterministic by the domestic circumstances. So since the '80s USA and Western nations pressed developing countries to implement patent laws. So to some extent this is
an outside force forcing these developing countries to implement their patent law, so in that sense it could say these patent implementations is some sort of running shock. But to the extent that patent implementation is still voluntary, and a lot of countries like Japan, Switzerland and China excluded pharmaceutical industries from their national patent law at the beginning, also reflects that country has the decision making power and that they could base their patent implementation on their local conditions. So that's the endogeneity part that I tease out using the matched algorithm.

So what I do is to use a statistical method to match the countries that newly implemented patent laws in the pharmaceutical industry with one country that never had patent protection up to that reference period and another country that always had patent protection, so basically I'm making two weight comparisons. So I compare each country that has just implemented pharmaceutical patent laws with a country that never had patent protection and with another country that always had patent protection, and I do this two-way comparison to check the robustness of results.

And how I constructed my sample countries is that I first identified the set of countries who implemented pharmaceutical patent laws during the two decades I have data on, and with that I use different legal documents and some previous literary research to identify these countries. And then I matched these countries with the other countries I just mentioned according to the country's characteristics. So that included development level, GDP, GDP per capita, PPP, price control policies in the pharmaceuticals, pharmaceutical industry outputs and employment, the size of the industry for that particular country, and then education levels, et cetera.

So after that I came up with this table of matched countries. So here China implements its domestic pharmaceutical patent law in 1991, and I match it to India which didn't have patent law for these periods. So India didn't implement pharmaceutical until much later, in the end of 1999, 2000. So India is the control country in my sample.

And then let's look at Brazil in 1996. Oh, I remember, Brazil implemented domestic patent laws in pharmaceutical industry in 1997 so it's after the time where I have corresponding lateral year innovation outcome measured, so it is also in the control group. It is in one of the control groups there. Okay, we can find it later. These are the several countries that always had patent laws up until that -- you know, before that reference period.

So basically I'm comparing the innovation outcomes a few years, one year after the implementation up to ten year after for these treatment countries.

And I'll skip this. This is just some details of how to match the samples.

Let me just say with one slide why I used the U.S. patent cited -- citation-weighted U.S. patent awards as an estimate for innovation. So first of all patent count and R&D expenditure are highly correlated in cross-section, and the shifts of R&D concord with patenting level. So we can think of R&D as innovative input and patents awarded in the U.S. as innovation output. So both are very good innovation outcomes. Both are very good innovation estimates.

The U.S. patent counts can provide a uniform base for comparison across countries. So because we are dealing with a lot of countries in the sample and each country has their own patent, general patent laws. So if I use the patent awards in domestic country, then the country that never had any patent -- never had patent laws would have zero count in patent counts, right? So it makes the comparison unscientific, so that's why I used the
U.S., the patents awarded to the innovators in each country that are taken up in the U.S. patent office. And I rest assured as I looked at the data that a lot of innovators from different countries took out patents in the U.S. patent office way before they had their own domestic patent laws.

¶135 Around 64 percent of international patents in 1975 are patented in the U.S., and this number increased sharply in recent years. So by using the U.S. patent counts I'm really capturing the very important innovations all throughout.

¶136 And using the citation weight is basically to correct for the quality differences among the different patent -- different innovations. And I also control for the propensity to patent in the U.S. by controlling for how a country trades with U.S. historically. So we can think of an argument that countries that traded with U.S. more frequently would take on more patents in the U.S. because they see more markets, market potentials there. And after taking that into account in the regression than the U.S. patent count can serve as a better estimate for the innovation estimate.

¶137 Let me also talk about my second paper on the impact of counterfeits. So basically I spent almost two years to gather data in China. I sample shoe companies in China for, again, a very long time span, from 1993 to 2004. I looked at these authentic shoe companies' responses to the entrance of their counterfeits, and these authentic shoe companies in China includes multinational corporations like Nike, Adidas, et cetera, and also the Chinese originated famous brands, to name a few.

¶138 What I found is when their counterfeits enter the market these authentic companies innovate to distinguish themselves better in consumer's minds from the counterfeits. And the type of innovation they engage is to input more advanced technologies in producing shoes, from Italy mainly, and they produce better, more sophisticated shoe surfaces, better patterns that are harder to imitate, and better materials they use, especially shoe surface and shoe bottom, the back. But the bottom part of the shoe actually we see least changed as the counterfeits enter. And they raise their authentic prices accordingly to accommodate the cost increase due to more advanced material and technology, and also they've raised their prices about a level that's captured in the cost change to signal their quality.

¶139 Interestingly they also invested in their own enforcement. They established their own brand protection offices where they would send their own employees to monitor the market and they would report to the government where they found fake shoes and the government would help them to track these counterfeits down. And there is where the relationship comes in to play most. So a company that has better relationship with the government gets more immediate attention in tracking down counterfeits.

¶140 And they also do vertical integration, by which I mean they established their company store instead of doing retailing, instead of selling to the retailer.

¶141 And all these are quite effective in helping them deterring counterfeit.

¶142 So thank you very much, and I would like to discuss with you more.

(Applause.)

¶144 MS. HO: Thank you to our panelist for not only a fascinating discussion but making my job very easy as the timekeeper. I thought I was moving people along, but you're all done.

¶145 So we have a good amount of time for discussion, so I'd like to open it up for questions that people have.
MR. OROZCO: My question is for Ben. Thinking about the issue of getting damages or just putting some teeth into the enforcement in China, who has the burden to conduct this factual discovery to ascertain what is the damages question and how does that technical hurdle impact what is the ultimate question of the judiciary figuring what the damages issue is?

MR. BAI: Excellent question. We heard again and again even if you win in China you're not going to get much money. That's actually true because plaintiff has the burden to prove not only infringement but also damages. Damages are normally calculated in the following order: Lost profit to the right holder or infringer's gain; or the next one is reasonable royalty for patent cases and some other case but not for all; then the last category is what's called statutory damages, which are now capped at 500,000 RMB, which is about $60,000. So that's the sequence of determining damages.

If you don't operate in China then you have no lost profit, so really what you're looking for is reasonable royalty. Reasonable royalty has to be reasonable in China. So if you get 10 percent in the U.S. or Europe, the judges will say I'm not going to listen to these kind of evidence. This is purely protectionism at its best. But are they entitled to do that? Totally.

So the point is if you don't have evidence of your own loss, and for whatever litigation strategies you decided not to produce your loss because you may not have enough -- you may not have proof to show that, then infringer's gain is the criteria. Of course, there is no discovery so how do you prove that. You can discover infringer's profit if there is a criminal proceeding or an administrative proceeding where they seize their books. And in China they keep several books, so you have to the seize the right book.

I'm not joking. It is very complicated to do business in China. It amazes me that a lot of companies make tons of money in China. GE makes billions of dollars in China, Dow Chemical makes billions of dollars in China. Nokia. China is Nokia's largest market. I don't understand how they actually make that much money with all these complexities. The point is if you can't discover the infringer's gain, then you're stuck with statutory damages, which is $60,000. And as you read cases coming out of China, a lot of times -- for example, 3M cases, $60,000.

UNIDENTIFIED SPEAKER: This is probably a question that's completely ridiculous.

A couple years ago on the news I remember being told in trademarks, for example, it was a big problem because most people from here were saying the Chinese government is not enforcing trademarks, not enforcing a lot of things like that. When the Beijing Olympics came along they opened a lot of different stores over there and they used their -

MR. BAI: I'm sorry. I can't hear you.

UNIDENTIFIED SPEAKER: The Olympics, the Beijing Olympics of 2008, the government actually for the first time opened stores and held, that's what I'm not sure, I don't know, but they held some trademarks, and for the first time back then they would have enforced differently and personally trademarks through a different method. And I've never heard anything more about this story, but could you comment on has enforcement over the years, over the last ten years in regard, for example, trademarks,
and is the Chinese government now that it is producing goods are they changing the way
they view this generally?

¶155 MR. BAI: Well, in terms of chasing down counterfeits when it comes to
trademark, they are ramping up their efforts. They probably have more people combating
counterfeits more than any other country.

¶156 In terms of judicial enforcement, I really don't think -- it's not like as the Olympics
is approaching they're going to ramp up the enforcement issue. A lot of trademark
problems I can go on and on and give you war stories about the mistakes made by U.S.
trademark lawyers when they advise their clients overseas.

¶157 U.S. is opposite to the world in many regards. First-to-file versus first-to-invent,
use-based trademark rights versus first use first. I'll give you a good example. I have to
talk about Viagra. Viagra -- when Pfizer -- I mean, I hope you're not recording because
Pfizer is a client of ours, but we had nothing to do with the trademark matter. When they
went to China they just got some Chinese trademark agent apply the Chinese mark based
on the phonetic sound of Viagra, and some Chinese knock-off artist came along and said,
"My gosh, I'm going to register "Big Brother." In Chinese it's called "Way Good." But it
has a very strong masculine connotation, "Big Brother." I am going to register this mark
as my mark. And Pfizer discovered that and they said, "Oh, good, this mark is really
good. I'm going to sue them and get the mark back." Guess what, they lost. It is first-to-
file. Whoever files first wins the game.

¶158 And if I -- I mean, we can go through all the analytical steps and we'll conclude
Pfizer will lose. Pfizer should lose because it is first-to-file system. You didn't think
about the catch name, so it is your fault.

¶159 So I can give you many, many stories where U.S. trademark lawyers, U.S. patent
lawyers made mistakes based on U.S. mentality. And when you go overseas, especially
China, it basically treads foot on them. I mean, that is a good example of that. If you
thought about a better way to, you know.

¶160 UNIDENTIFIED SPEAKER: But the fact that China, for example, is producing
brands of cars and producing its own product and all sorts of new development, does that
affect the way the government and the people -- I mean, when you're enforcing somebody
else's trademarks it's one thing, but when you're enforcing your own are they taking a
different position, are they being more pro-Chinese when they're in court than with
foreigners?

¶161 MR. BAI: Well, you're definitely correct in terms of when -- in fact, Chinese
enforcement is going to be driven by the domestic industries. We wanted to target -- I
represent a lot of multinational companies in China. We want to target this flagship -- I
can't name the name. But this flagship company, which is a private-owned company, it
has nothing to do with the government. Just because they represent the Chinese domestic
industry, if we sue them for patent infringement and we probably going to get some local
protectionism or some government intervention. So this is the part when people say
China doesn't protect IP. Perhaps, you know, the government, the judiciary is not totally
independent, so this is going to have a long time to get to neutrality.

¶162 And also this company happens to be the company that has largest patent portfolio.
So if we sue them with one patent, they probably going to sue us with ten patents. So this
is the emerging trend which I didn't get a chance to discuss. I thank you for actually
bringing it up. So we are very nervous if we sue them, and we told the client perhaps we
shouldn't. And turns out the client got sued by a bigger target so we're fighting that war, so we said let's just put this on hold. Now it's two foreign companies fighting patent infringement suit in China. So this is another emerging trend, is a lot of multinational companies are going to start to kill each other in Chinese courts.

MS. QIAN: If I may add a few things. From my research on that counterfeit piece of work, from the data I collected on relationships between an authentic shoe company and the Chinese government, there is absolutely no significant difference between the multinational corporations' relationship with the government and the local Chinese company's relationship with the government.

And if I can stretch a bit and relate to another piece of work I'm doing with two co-authors we're looking at foreign direct investment performance in China. In that we look at whether ethnicity has any advantage. So the hypothesis is the ethnic Chinese investors will do better in China. But now our results do not show that. So foreign, mature foreign investors, investors not from Hong Kong, Taiwan or Macau, they're doing very well in China, especially in recent years.

And also in the Olympics question. Now Chinese government is doing a lot of education in response to Olympics and copyright issues, because one thing in the previous several months a lot of small businesses actually infringed on trademarks unconsciously. So what they were trying to do is simply to congratulate Olympics to come very quickly, and a lot of restaurants do that in their restaurant door, and that actually constituted trademark because they were not sponsor of the Olympic so they could not use that Olympic Beijing trademark. So what the Chinese government do is to send policemen to educate a lot of the local small business and they broadcast TV programs especially talking about copyright issues and the origin of Olympics, etcetera.

UNIDENTIFIED VOICE: I'm wondering of the cases -- this is to Dr. Bai.

MR. BAI: The three cases that I briefly talked about? One is a German company, one is U.S. -- the rest of them are U.S. companies.

UNIDENTIFIED VOICE: I'm just wondering, because the IP issue in China doesn't only impact U.S. I mean, we're in U.S. but the rest of Asia actually probably get damage even more severe. I'm wondering, you know, if you see like -- is there any suit actually brought by local, for example, Korea or Taiwan or Central Hong Kong, or are they at the same level in terms of going to court? Or if that's the case did you see a trend of preferential treatment, not necessarily in terms of result but in term of speedy trial or something or additional data?

MR. BAI: I think as soon as a foreign party shows up the judges become a lot more careful. They will take longer time to render decisions and if necessary they will call their boss and say, "How should I rule?" This is the reality of Chinese judiciary.

I don't think there is a whole lot of difference between, say, the Asian foreign companies versus the European or Americans companies. Honda is actively litigating cases. Toyota. Talk to Toyota and they will paint you very gloomy pictures of how horrible things are in China, however they're making tons of monies so I really cannot feel sorry for them.

A lot of the cases you read about -- I can't really talk about GM because GM is our client. Toyota is our client too so I can't really comment on that. But if we look at even their own pictures of -- I mean, Toyota's in-house counsel -- I saw a presentation by
Toyota's in-house counsel showing serious counterfeiting issues in China. I looked at the picture and I said, "I'm an average consumer. I drive a Toyota. I don't think there is actually that close."

§173 So before you really believe what people tell you, really dig deeper and look at the facts and see for yourself whether there is really infringement or not. I looked at Toyota's slide and I said, "Well, I'm an IP lawyer but I'm also an average consumer. I really don't think -- you know, this is 50/50."

§174 So, yes. I mean, it is a long-winded answer to your short question. Yes, there are companies. Japanese companies are extremely active in China.

§175 MS. HO: In the back.

§176 UNIDENTIFIED VOICE: A couple of questions about patents in China. First, that two-year statute of limitations. Does the bar, the start of the clock, is that related to the problems related to discovery? That is do you need like really, really clear and convincing evidence for that clock to start running?

§177 MR. BAI: I'm sorry. I didn't hear the whole question.

§178 UNIDENTIFIED VOICE: You talk about the evidentiary problems with actually getting a case that you can win on infringement, and there is also a pretty tight time line in terms of the statute of limitations from when you know or should have known that you were being infringed. Are those two related? That is, is the standard for when the statute of limitations starts related to how strong a case you can build given that you don't have discovery?

§179 MR. BAI: Well, the clock starts to tick when you know or should have known -- the should have known is really the sinister part. It starts to tick regardless whether you have evidence or not. So long as there is a suspicion of infringement you're starting the clock ticking. One way to hold the limitation is -- this shocked me when I heard it the first time as a U.S. practitioner. You can hold a statute of limitation by sending a warning letter. But then by sending a warning letter you may trigger the DJ action, declaratory judgment, so you have to be careful how you draft the letter so that you can buy some time and on the other hand avoid declaratory judgment. So it is a very fine balance.

§180 Normally I don't tell people there are ways to hold the clock because if you don't do it right then you actually shoot yourself in the foot. So I say this: Don't try this at home.

§181 Did I answer your question?

§182 UNIDENTIFIED VOICE: Yes. And I have another question. How does it work with process patents?

§183 MR. BAI: Process patents? Excellent question.

§184 There are two kinds. If your process made a new product, new not -- not in the sense of novel, just new at the time, at the time you filed the patent application, new meaning new composition, new characteristics, it doesn't have to be patentably new, then the burden of proof shifts to the other side. You file the lawsuit based on the fact that it is a process claim, plus you do have to prove it's new, and then you're all set. The infringers have to come forward with evidence to show that you are using a different process. However, if your process is new but making the same old product that everybody else is making, then you're in trouble. It is very hard.

§185 MS. HO: In the back.
MR. OROZCO: Can any of you comment on this special IP jurisdiction that has been created recently, I think in the special zone called Pudong. Is that the name of it?

MR. BAI: I'm not sure I know what you're talking about.

MR. OROZCO: There is this new type of IP specialized court, I believe, in this area.

MR. BAI: When did you read that?


MR. BAI: 2004. No, that's not correct. In fact, last year Associated Press released something that said China created specialized IP courts, and I was interviewed on that. I said this is totally not true.

In China, what I didn't get a chance to say is there are various divisions within a court. There is one division, normally in No. 3, what's called tribunal. That is IP court. IP judges hear nothing but IP cases. That has been the case for years, there is nothing new about that.

One day Chinese Supreme Court said we going to call these courts IPs, and this is just a change in the name, nothing substantive. So people got excited about that and said China has created a specialized IP court. No, that is really not true.

In terms of Pudong, if you're referring to Pudong, there is a high tech park where they are actively promoting the protection of IP. Lately they started an IP protection forum where there is a service provider and there are government agencies to foster innovation and also IP services. I was actually there at the ceremony because our firm is part of the service providers, but I don't know whether that is what you're you talking about.

MR. OROZCO: It must be. What is the unique role of this organization?

MR. BAI: Well, Zhangjiang High Tech Park is poised to be the next Silicon Valley in China. The Shanghai government is extremely smart in managing this area. They said, well, to be successful as the next Silicon Valley I've got to attract the VCs to come here, I've got to attract the international law firms to come here, so everything has to be up to the international standards, so are IP protections.

So they actually invite law firms to participate. And they invite local law firms as well as international law firms. There is not really a specialized court there. It is really just a way to stimulate innovation.

In that park there is a lot of research centers by multinational companies as well as Chinese biotech and pharmaceutical companies. In the next five years you're going to see some of those companies going IPO either in the Hong Kong stock exchange or London stock exchange, and perhaps NASDAQ. Many millionaires will be made in the next five years.

MS. HO: Did you want to say anything else?

MR. LEV: No. Just thanks to our sponsors at Foley & Lardner for being the Premier sponsor and providing the refreshments. Have fun. And also to Jones Day and McDonnell Boehnen for sponsoring the panels. And also to Fish & Richardson, Brinks Hofer, and Welsh & Katz for being associates. Enjoy.

Thank you very much.

(Applause.)

(The panel discussion, and the symposium, were concluded.)