Forcing Creativity: An Analysis of Chinese IP Subsidies and How They Should Be Assessed Under Existing International Trade Agreements

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FORCING CREATIVITY: AN ANALYSIS OF CHINESE IP SUBSIDIES AND HOW THEY SHOULD BE ASSESSED UNDER EXISTING INTERNATIONAL TRADE AGREEMENTS

Taylor Stemler

TABLE OF CONTENTS

I. INTRODUCTION ........................................................................................................................... 29

II. PATENT SUBSIDIES..................................................................................................................... 29
   A. Overview of China’s Current and Former Patent Subsidy Program ................................... 30
   B. Effects of the Chinese Patent Subsidy Program .................................................................... 33

III. TRADEMARK SUBSIDIES .......................................................................................................... 38
   A. Overview of China’s Current and Former Trademark Subsidy Program ......................... 38
   B. Effects of the Chinese Trademark Subsidy Program ............................................................. 41

IV. TREATMENT OF CHINESE SUBSIDIES UNDER WTO TRADE RULES................................. 46
   A. Overview of Relevant International Agreements and the National Treatment Principle .......... 46
   B. Chinese IP Subsidies Under the SCM and TRIPS Agreements .......................................... 48
      i  The SCM Agreement Violation ......................................................................................... 49
      ii. The TRIPS Agreement Violation ...................................................................................... 56

V. CONCLUSION ............................................................................................................................. 59
I. INTRODUCTION

The number of Chinese applications for patents and trademarks has drastically increased over the past ten years.¹ This increase in filings can be at least partially attributed to subsidy programs offered to domestic applicants by the Chinese government.² These subsidies, offered for both foreign and domestic intellectual property (“IP”) acquisitions, may have significant consequences internationally.³ This paper asserts that by backing these initiatives, China violates the national treatment principles of the TRIPS Agreement and ignores its obligations under the Agreement on Subsidies and Countervailing Measures.⁴ Rather than expending their own resources in attempting to solve the problems posed by the subsidized filings, World Trade Organization (“WTO”) members should seek to enforce these international agreements and curtail China’s continued violations.

II. PATENT SUBSIDIES

In 2019, China filed the most international patent applications out of any other country in the world.⁵ In doing so, China ended the US’s streak of being the biggest user of the Patent Cooperation Treaty’s (PCT) international patent filing system since its inception in 1978.⁶ Similarly, as of 2019, China was the fourth largest user of the US patent system.⁷ Even more

¹ Mitchell Hamline School of Law, 2021. For biographical information, see: https://www.linkedin.com/in/taylorstemler/. I would like to thank Renee Kraft for providing the inspiration to write on this topic and for all of her thoughtful feedback and guidance on this article. I would also like to thank the Cybaris Law Review team for all their help editing. All errors are my own.
² See infra Parts II and III.
³ See infra Sections II.A and III.A.
⁴ See infra Part IV.
⁶ Id.
⁷ The number of Chinese patent filings in the US came in just behind the US, Japan, and South Korea. See USPTO, Patent Counts by Origin and Type, Calendar Year 2019 [hereinafter Patent Counts by Origin 2019],
staggering is the dramatic rate of increase in Chinese filings at the USPTO, up 93% over the previous 10 years. Although China has experienced a significant period of technological growth over the past decade, one major factor to which the increase in Chinese patent filings has been attributed is its patent subsidy program.

A. Overview of China’s Current and Former Patent Subsidy Program

The number of patent applications filed and granted by a country has historically been used as a metric for gauging that country’s level of innovation. Although on its face, measuring patenting activity would appear to be a logical way of gauging innovation, these measurements can be distorted by other incentives driving parties to increase patent filings. One other incentive may include, for example, signaling a company’s value to potential investors when seeking to secure financing, as owning a large patent portfolio can provide an aura of legitimacy, regardless of the strength of the constituent patents. Governments may also wish to increase the amounts of patent held by domestic entities for similar reasons. Increased patent activity within or from a country may signal to others that the country is a hotbed of innovation, spurring an increase in foreign direct investment.


10 USPTO, TRADEMARKS AND PATENTS IN CHINA 3 (2021) [hereinafter TRADEMARKS AND PATENTS IN CHINA].


13 Foreign direct investment is generally attracted through developing strong domestic technological capacity and IP rights. Given how technological capacity has historically been measured using patent filing activity, it is likely that an increase in patent filing within a country would signal an increase in technological activity and foreign direct investment. See Keith E. Maskus, Intellectual Property Rights and Foreign Direct Investment, (Ctr. for Int’l Econ. Stud., Policy Discussion Paper No. 0022, 2000),
To increase the number of patents held by domestic entities, China has created new incentives to file patent applications in China and the rest of the world. Among the incentives are reduced prison sentences, tax breaks, patent commercialization subsidies, individual housing benefits, application filing and examination subsidies, and subsidy awards for granted patents.

Patent application and grant subsidies, the focus of this section, were first developed in the late 1990s and have been launched in other provinces in China throughout the early 2000s. Given that each Chinese province is responsible for its own patent promotion and enforcement, the amounts of, and eligibility requirements for the subsidies vary by province. In some cases, the subsidies cover the entire filing or examination fee for a given application. According to the US Patent and Trademark Office (“the USPTO”), many of the subsidies even provide financial incentives greater than the cost of obtaining the patent itself.


16 Id.


19 Id. Interestingly, many of the Chinese patent subsidies mirror those provided by the Soviet Union for inventors certificates under the Act Concerning Inventions and Technical Improvements. Among other things, the Soviet incentives included access to priority accommodations, schools, and research positions. See Francis Hughes, Soviet Invention Awards, 55 ECON. J. 291, 291–292 (1945).


22 Id.

23 TRADEMARKS AND PATENTS IN CHINA, supra note 10, at 7.
For example, in Beijing, applicants could earn as much as 20 million yuan ($3 million USD) in foreign patent subsidies in a given year. Interestingly, the per patent subsidy for an applicant seeking a foreign patent, 50,000 yuan ($7,500 USD) is significantly higher than the 1,000 yuan ($150 USD) subsidy offered to an applicant seeking a domestic, Chinese patent.\(^{24}\) Not only do Chinese cities offer attractive subsidies to applicants, but certain sub-city districts also offer additional monetary subsidies to applicants that can be combined with the city level subsidies.

Generally, to be eligible for a subsidy, the applicant must be either an enterprise, public institution, governmental organization, or social organization registered within the city offering the subsidy.\(^{25}\) Thus, to qualify for a subsidy, the patent application must be owned by a Chinese entity.\(^{26}\) If the application is later assigned to a non-Chinese entity, the entire subsidy may be revoked or required to be repaid.\(^{27}\)

Recently, the Chinese National IP Administration (“CNIPA”) announced a plan to cancel or phase out all patent subsidies.\(^{28}\) This change in policy was said to be an attempt to curb the improper filing behavior of Chinese applicants and encourage the filing of higher quality patents.\(^{29}\) The announcement requires that all funding for patent application filing and

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\(^{24}\) Id. Although the cost of obtaining a US patent (about $7,500 USD) is significantly higher than that of a Chinese patent (about $950 USD), the discrepancy between the subsidies is far from proportional to the difference in costs of patent acquisition between the two countries. See How Much Does a Patent Cost in Major Countries?, GREYB (2020), https://www.greyb.com/patent-cost/ [https://perma.cc/DYU3-DK8L].


\(^{27}\) Id.

\(^{28}\) Guójià Zhīshì Chǎnquán Jú Guǎnyuè Jīnnyībù Yánghé Guìfán Zhuānlì Shēnqǐng Xíngwéi De Tōngzhī (国家知识产

\(^{29}\) China to Cancel All Patent Subsidies, XINHUANET (Feb. 5, 2021), http://www.xinhuanet.com/english/2021-02/05/c_139724293.htm#:~:text=5%20(Xinhua)%20%2D%2D%20China%20services [https://perma.cc/TZ3C-ZXMS].
prosecution activities by Chinese provinces and the CNIPA be halted by June of 2021.\textsuperscript{30} Although provinces are still permitted to provide subsidies for granted patents until 2025, these subsidies must not exceed 50\% of the official fees paid in obtaining the patent right.\textsuperscript{31} Importantly, the notice does not apply to sub-provincial local IP departments and is not directed to state agencies other than the CNIPA.\textsuperscript{32} Thus, these other entities may be free to continue disbursing patent subsidies despite the proposed change in policy.\textsuperscript{33}

B. \textit{Effects of the Chinese Patent Subsidy Program}

The USPTO has suggested that the Chinese subsidy programs have contributed to a decrease in the commercial value of Chinese national patents.\textsuperscript{34} In doing so, the USPTO cites the proportionately low rate at which domestic Chinese national patent recipients file for international patent protection.\textsuperscript{35} In the US, 80\% of US national patent applicants file for international protection.\textsuperscript{36} Comparatively, 5\% of Chinese national patent applicants seek international protection.\textsuperscript{37} From this data, the USPTO concludes that Chinese applicants may recognize the minimal value of the patent, which would provide only a minor return on investment.\textsuperscript{38} When considered with the fact that many Chinese patent subsidies for international filings are contingent upon the granting of the international patent, it may be that Chinese applicants are skeptical about the likelihood acquiring a patent right. This could be due to a...

\textsuperscript{30} Id.
\textsuperscript{31} Id.
\textsuperscript{33} Id.
\textsuperscript{34} TRADEMARKS AND PATENTS IN CHINA, supra note 10, at 10.
\textsuperscript{35} Id.
\textsuperscript{36} Id. It is important to consider, however, that despite the relatively low percentage of Chinese national applicants filing internationally, China is still the number one user of the PCT. \textit{China Becomes Top Filer}, supra note 5.
\textsuperscript{37} Id. at 10.
\textsuperscript{38} Id.
recognition that the discovery relates to an insignificant technical advancement or because of prior difficulties seeking protection abroad when compared to experiences at Chinese patent office.\textsuperscript{39} However, the USPTO’s conclusion that Chinese patents are less valuable merely because of the low rate of international filing could overlook the fact that much of the market for Chinese innovation may be domestic.\textsuperscript{40} Domestic applicants may just recognize the lack of incentive to file abroad since so much of their market is located within China.\textsuperscript{41} Therefore, using the international filing rate as a value metric for Chinese patenting may be problematic.

A likely more direct measure of the value of subsidy-driven Chinese patents is their successful commercialization.\textsuperscript{42} Here, the USPTO notes that China lags behind other countries, as the WIPO 2020 Global Innovation Index ranks China 44th in the measure of IP receipts as a percentage of total trade.\textsuperscript{43} Thus, the USPTO concludes that despite having received more national patent applications than all other offices in the IP5 combined,\textsuperscript{44} the licensing revenue generated from these patents is underwhelming compared to the other offices in the IP5.\textsuperscript{45} Although licensing may be a useful indicator, basing the value of Chinese patents solely off of these numbers could overlook the fact that licensing is a relatively sophisticated medium of patent commercialization. As a developing country, Chinese patentees may have yet to fully appreciate the value in licensing their patent rights. The WIPO 2020 Global Innovation Index ranks China fifth in high-tech net exports as a percentage of total trade.\textsuperscript{46} Thus, China appears

\textsuperscript{41} \textit{Id.} at 16.
\textsuperscript{42} TRADEMARKS AND PATENTS IN CHINA, supra note 10, at 10.
\textsuperscript{43} \textit{Id.} at 9.
\textsuperscript{44} \textit{Id.} at 3 n.2.
\textsuperscript{45} WIPO, \textit{GLOBAL INNOVATION INDEX 2020} 239, 256, 272, 312, 337, 339 (2020) (ranking Japan and the US at 1st, the United Kingdom at 8th, Germany at 17th, Korea at 18th, and China at 44th).
\textsuperscript{46} \textit{Id.} at 239.
able to extract value from its patents in ways other than licensing them, which could undermine the USPTO’s suggestion that they are of poor quality. Still, regardless of what method of valuation is used, researchers seem to agree that after enacting the subsidies, Chinese patent quality has not kept up with the surge in patent filings.47

Another effect of the patent subsidies is that firms may be splitting up inventions into more patent applications.48 Thus, when provided financial subsidies per application, firms choose to file patents in an inefficient manner. In doing so, firms waste both administrative patent office and firm resources while their innovation rate remains relatively unchanged.49

Finally, increased domestic patenting may have a defensive effect internationally. Many companies possess a certain amount of institutional knowledge that may not rise to the level of a “patent worthy” discovery. Companies choose to forego patenting for various reasons. For instance, if the discovery would be difficult to commercialize, companies may decide that the return on investment in seeking patent protection is insufficient to recover the costs of seeking a patent in the first place.50 In this case, it may be economical for the firm to forego patenting or try protecting the advance as a trade secret. If, however, the costs of obtaining patent protection were lessened, or eliminated completely, companies may be more inclined to seek patent protection over these types of discoveries.

Generally, undisclosed, private information cannot be used to invalidate or serve as a bar to obtaining patent rights.51 This is because the information is not known to the public.52 If then,

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49 Id. at 22.
50 See supra, note 39 and accompanying text.
51 See PATENT LAW OF CHINA, supra note 21, art. 22.
52 Id.
Chinese entity A opted to forego patenting a discovery while failing to make a public disclosure, and entity B attempted to obtain a Chinese patent on that discovery, Chinese entity A may be unable to prevent entity B from doing so.\(^53\)

The above hypothetical may prove problematic in the eyes of some institutions, such as the Chinese government, where entity B is a foreign enterprise. Patent protection allows one to obtain monopoly profits from a market.\(^54\) Generally, a domestic patent holder is more likely to reinvest its monopoly profits within its domestic country instead of reinvesting other foreign countries.\(^55\) Conversely, a foreign patentee is more likely to reinvest more of these profits in a foreign country.\(^56\) Thus, generally speaking, granting patents to a foreign entity may result in that entity extracting monopoly profits from the granting country using the patent right, and reinvesting these profits overseas.\(^57\)

In another hypothetical, if Chinese entity A were to instead have gotten a patent on the discovery that it might have otherwise chosen not to disclose, entity B would be foreclosed from obtaining a Chinese patent on the discovery.\(^58\) At the same time, entity A’s Chinese patent would serve as worldwide prior art.\(^59\) Because of this prior art affect, entity B may also face difficulty patenting this discovery in another foreign country.\(^60\) Thus, Chinese entity A would hold an

\(^{53}\) However, entity A would likely still be allowed to use the patented technology as a prior user. *See* Patent Law of China, *supra* note 21, art. 69.


\(^{56}\) See *Id*.


\(^{60}\) Whether a foreign patent office is likely to cite a Chinese patent application as prior art during prosecution is another story. Still, in most countries, the Chinese patent application could serve as invalidating prior art to a foreign patentee seeking to assert their rights in the invention. *Certain Aspects of National/Regional Patent Laws*, WIPO (2020).
exclusive monopoly in the Chinese market, thereby preventing the situation where a foreign entity exports monopoly profits from the Chinese market. Meanwhile, entity A retains its ability to compete in the foreign market, thereby ensuring that Chinese entity A has the opportunity to export profits from the foreign marketplace back to China.

Evidence of this theory’s application in the development of the Chinese subsidy policy is lacking, and it is unlikely that this defensive effect served as a major goal behind enacting the subsidies. However, at least one study has found evidence of Chinese protectionism in the prosecution of patents in China, it was careful to note that this effect only appeared in technological areas of strategic importance.\(^6\) Considering these findings, it’s at least plausible that China may be interested in restricting the growth of foreign patenting, at least in some technological areas. This paper does not suggest that the Chinese subsidies are the sole, or even a major cause of any fluctuations in rate of patents granted to foreign applicants. Nor does it suggest that these policies have even been effective in restricting foreign patenting. Still, based on the theoretical considerations outlined above it’s possible that they have some incremental effect. To be sure, China does have an incentive to roll back the subsidies to focus applicants on increasing patent quality.\(^6\) Still, because of the theoretical potential protectionist effect, China may also have an incentive to re-institute or halt the additional the elimination of these programs. This is because, by incentivizing domestic patenting by Chinese entities, China may effectively decrease the likelihood of monopoly profits being exporting by foreign patent holders while increasing the likelihood of imported profits from Chinese firms competing abroad.

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\(^6\) Paolo Beconcini & Elisa Li, *New Procedures Indicate China’s Patent System is Now Focused on Quality, not Quantity, of Patents*, SQUIRE PATTON BOGGS (Feb. 14, 2021), https://www.iptechblog.com/2021/02/new-procedures-indicate-chinas-patent-system-is-now-focused-on-quality-not-quantity-of-patents/ [https://perma.cc/RVE9-6D2B] (noting that this change in policy was said to be an attempt to curb the improper filing behavior of Chinese applicants and encourage the filing of higher quality patents),
III. TRADEMARK SUBSIDIES

Chinese trademark subsidies are just as troubling, if not more, than its patent subsidies. The increase in the number of trademark applications filed in China is staggering, with China’s trademark office recording 92% more trademark applications in 2018 than the US, the next leading office.63 Not only have these subsidies contributed to an explosion in the number of trademark applications filed by Chinese applicants in China,64 but they have also yielded a large uptick in the amount of Chinese filings in the US. While US national filings from domestic applicants doubled between 2008 and 2018, US filings submitted by Chinese applicants increased thirty-one fold during that same period.65 In 2020, the number of Chinese trademark applicants surpassed US applicants at the USPTO for the first time.66

A. Overview of China’s Current and Former Trademark Subsidy Program

Since at least the mid-2000s, China has maintained a subsidy program to incentivize applicants to secure trademark protection both in China and abroad.67 As of 2021, localities within China have adopted over 70 trademark subsidy measures.68 The USPTO continues to caution that China is increasing its incentives for Chinese entities registering trademarks abroad.69

63 WIPO, WORLD INTELLECTUAL PROPERTY INDICATORS 2019 90 (2019). When adjusted for population, the statistics are only slightly less striking, with China recording 62% more trademark applications. Id.
64 Id. The vast majority of applicants were residents of China. Id.
65 Compare WIPO, WORLD INTELLECTUAL PROPERTY INDICATORS 2010 86 (2010), with id. at 96.
68 TRADEMARKS AND PATENTS IN CHINA, supra note 10, at 3.
69 Id. n.11.
In many instances, Chinese trademark subsidies outweigh the costs of filing a trademark application in the US. For example, in 2013, Shenzhen Province in China authorized subsidies for filing trademarks internationally.\(^70\) Eligibility for these subsidies generally depends on residence or corporate registration within the city granting the subsidy.\(^71\) In Shenzhen, the amount of the subsidy varies depending on where in the world the trademark application is being filed.\(^72\) For applications registered in the U.S., an applicant is awarded RMB 5,000 (about $760 USD). Meanwhile, as of 2015, the cost to file a trademark application with the USPTO has hovered around $250.\(^73\) Thus, under subsidy programs like the one in Shenzhen, it becomes economically rational for a Chinese entity to file for trademark rights in the US even if they have no intention of using the mark.\(^74\)

As of 2019, Shenzhen Municipal Administration for Market Regulation announced that it would be lowering its subsidies available for applicants filing in the U.S. and other foreign countries to RMB 1,000 (approximately $150 USD).\(^75\) Likewise, in January of 2020, the CNIPA...
announced a plan to clean up, and in some instances eliminate, subsidies for IP. However, just a few months later, the Chinese government directed its state-owned enterprises to increase their international filings by 50%. In stating this goal, China cited the need to promote innovation and creativity. To meet these goals, Chinese subnational governments will need to continue to increase the availability of subsidies and other non-market incentives.

As an aside, regardless of how Chinese subsidies for trademark applications are handled in the future, the incentive for Chinese applicants to file US trademark applications in the US may remain unchanged. Amazon, almost a government in its own right, now provides preferential treatment to sellers who can demonstrate proof of a registered trademark. For many sellers who sell inexpensive everyday objects, building a brand is unimportant to the success of their operation. Thus, all that matters to these sellers is to secure a registered trademark that they can submit to Amazon and use to gain admission into its preferred Brand Registry program. Given that nearly half of Amazon’s top sellers are based in China, and that many of

[72x709]
these Chinese sellers thrive in low-cost market, it is possible that this increase in Chinese applications is here to stay.

B. Effects of the Chinese Trademark Subsidy Program

It is difficult to say exactly how much of the increase in Chinese trademark applications in the US is attributable to Chinese subsidies or the seller incentives provided by Amazon. For the purposes of this paper, no attempt will be made to parse out the effects attributable to one incentive or the other. Rather, the effects of the increase in Chinese filings will be examined more generally under the assumption that both incentives contribute to this phenomenon.

With this huge increase in demand for US trademarks by Chinese applicants, some attorneys have carved out a specialty in serving these clients. However, although it keeps US attorneys employed, this influx in Chinese applications may prove problematic for the US trademark system. Some of the Chinese applications merely seek to protect random strings of English character letters that have nothing to do with the goods or services with which they are applied for. In other cases, applicants seek protection over random combinations of English language words. Often, these marks are successfully registered, as US trademark law recognizes marks that have nothing to do with the goods with which they are classified, as fanciful or arbitrary. Fanciful and arbitrary marks are especially strong and are typically easier to register than other marks that are suggestive or descriptive of the products with which they relate.

The US requires actual use, or an intent to use the mark before one is entitled to register a trademark. Many trademark users opt to plan ahead and secure registration on an intent to use

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83 McLaughlin, supra note 81, at 1805–06.
84 Diakun, supra note 67. The leading attorney representing Chinese clients before the USPTO filed 9,922 trademark applications in 2020, which equates to more than 27 applications per day. Id.
85 McLaughlin, supra note 81, at 1804.
86 Id. at 1811.
basis, as it this allows them to secure priority over their mark early on. The applicant is then later required to submit proof of their use of the mark. This is typically done by submitting a photo to the USPTO, which is called a “specimen.” Alternatively, if one is already using the mark, they can apply for trademark protection with a use-based application, in which they can submit a specimen with their application.

In many cases, Chinese applicants fraudulently claim use of the mark based on doctored specimens submitted to the USPTO.88 For example, the same picture of a pair of shoes with a photoshopped tag sporting the candidate mark could be reused for multiple different trademark applications.89 Interestingly, almost always, these fraudulent specimens are submitted with marks registered in conjunction with apparel goods or scientific instruments on a use-based application.90 One study has found that 66.9% of these use-based applications for apparel goods included fraudulent specimens, of which 38.9% proceeded to be registered by the USPTO.91 Once these applications are registered by the USPTO, the applicant can then apply for Chinese subsidies or seek admission to Amazon’s Brand Registry program.

This large influx of fraudulent marks imposes serious administrative burdens on the USPTO.92 The surge in filings has significantly bogged down trademark examiners and has caused the USPTO to look into increasing their hiring.93 It is unclear how these applications will impact the USPTO in the long term, as much of the USPTO’s budgeting is based on the

88 Gerben, supra note 74.
89 Id.
90 Diakun, supra note 67. NICE Classes 25 and 9, respectively. Id.
92 McLaughlin, supra note 79, at 1806 (discussing burdens on the USPTO and problems with how nonsense marks, which technically qualify as “fanciful,” prevent legitimate users from securing rights in legitimate pronounceable marks with similar spelling).
93 Diakun, supra note 66.
expectation that owners will renew their marks and pay additional fees. In the likely case that many of these marks go unrenewed, this could lead to a significant gap in the USPTO budget.

These fraudulent marks also harm US trademark stakeholders. The massive influx of bogus Chinese trademark applications exacerbate the problem of trademark depletion, which creates obstacles for those attempting to register and use legitimate trademarks. Trademark law rests on the assumption that there is an unlimited supply of potential trademarks. However, quite the opposite is true. Nearly all the words that Americans use on a daily basis are now registered or are confusingly similar to a registered mark. Because of this, new applicants are forced to seek longer, more complex, and less effective marks. As more fraudulent marks are registered, this issue of trademark depletion continues to worsen as the number of viable trademarks continues to decrease.

Furthermore, to protect their existing trademark rights, US trademark owners must enforce their marks against later infringers. A failure to do so could result in the erosion of the trademark holder’s trademark rights. Many trademark owners use monitoring services to look out for any confusingly similar marks that new applicants are seeking to register. Once an application for a confusingly similar mark is filed, the owner must then oppose the mark or run

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95 Id.
96 Beebe & Fromer, supra note 91, at 217.
97 Id. at 223.
98 Id.
99 Id.
100 Id.
101 Id. at 224.
the risk of the new applicant impinging the owner’s rights. These proceedings to oppose marks can be expensive, especially when they become more frequent due to the large number of fraudulent applicants. Thus, companies seeking to maintain their rights are forced to expend significant resources doing so. This may also serve to diminish the perceived value in owning a US trademark as these rights become more expensive and difficult to maintain.

Partly in reaction to the negative effects of this influx of Chinese registrations, the USPTO sought to combat the issue by requiring foreign applicants to engage US attorneys and provide an email address for each application. Still, likely because of the willingness of US attorneys to serve this massive demand, along with the ease of obtaining an email address, Chinese filings continued to increase. In December 2020, the US enacted the Trademark Modernization Act of 2020 (“TMA”). The TMA called for the USPTO to implement procedures to allow third parties to challenge pending applications and suspicious registrations. Although the TMA does equip parties to challenge certain applications or registrations, it still requires trademark owners to expend their own resources doing so and lacks any means of prospectively addressing the large influx of Chinese applications.

Others have proposed prospective solutions for how the USPTO ought to address this issue. One solution is to institute a trademark bar, similar to the USPTO’s patent bar, where

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104 Beebe & Fromer, supra note 91, at 246–247.
106 See Diakun, supra note 66 and accompanying text.
107 Lince, supra note 105.
109 Lince, supra note 105.
practitioners must register with the USPTO to practice in front of the office.\footnote{Miriam Richter, Address at the USPTO Trademark Pub. Advisory Comm. 100–104 (Nov. 1, 2019) (transcript available at https://www.uspto.gov/sites/default/files/documents/TPAC_Transcript_20191101.pdf [https://perma.cc/5G8Z-N5BN]).} Doing so could make it easier for the USPTO to crack down on practitioners who file trademark applications for clients who submit fraudulent specimens.\footnote{Id.} This would likely put some of the onus on practitioners to scrutinize the filing and would filter out some of the most egregious applications.\footnote{Id.}

Another suggestion is to enlist a specialized examining unit trained to spot and flag fraudulent applications.\footnote{Stephen Lee, Chief Intellectual Property Counsel for Target, Remarks Before the Senate Committee on the Judiciary 4 (Dec. 3, 2019) (transcript available at https://www.judiciary.senate.gov/imo/media/doc/Lee%20Testimony1.pdf [https://perma.cc/CW9Y-N534]).} Similar measures have been taken in the cannabis space, where the USPTO maintains a specialized unit of examining attorneys assigned to handle cannabis related filings.\footnote{Trevor Little, Speculation Mounts Over USPTO Special Cannabis Unit as Practitioners Vent Anger Over Examination Delays, WORLD TRADEMARK REVIEW (last visited Apr. 8, 2019), https://www.worldtrademarkreview.com/brand-management/speculation-mounts-over-uspto-special-cannabis-unit-practitioners-vent-anger [https://perma.cc/WUH2-ATVJ].} This unit seeks to assist applicants in registering trademarks for cannabis related products, while not allowing registration of marks for federally illegal cannabis itself.\footnote{Id.} Like the cannabis examining unit, a specialized fraud detection unit could be trained to handle risky applications and detect fraudulent specimens.\footnote{Id.} One possibility here is to assign all incoming Chinese applications to this specialized unit. Ironically, however, doing so would likely violate international treaties like the TRIPS Agreement—the very same agreement which this paper argues some of the Chinese subsidies violate.\footnote{See Section IV.B.ii.} A more viable solution would be to assign this unit all incoming use-based trademark applications in the apparel or scientific instrument
classifications. Given that most of the fraudulent applications appear in this category, it seems likely that such an approach could screen out most of these problem applications.

Finally, other suggestions include gathering more information about foreign applicants’ eligibility for government subsidies, requiring the USPTO to make a more in-depth inquiry about applicants’ use in commerce, or provide an incentive (or subsidy) for successful challenges or marks at the USPTO. One commentor even suggests mobilizing US law school IP clinics to challenge specious trademark claims using the third-party opposition system created by the TMA. While potentially effective, all of the approaches above require additional effort and expense for US shareholders or the US government. Therefore, a more efficient approach to addressing issues caused by the Chinese subsidies may be to challenge the subsidies themselves, rather than the individual applications they help create.

IV. TREATMENT OF CHINESE SUBSIDIES UNDER WTO TRADE RULES

A. Overview of Relevant International Agreements and the National Treatment Principle

One of the most important international agreements in existence is the General Agreement on Tariffs and Trade (“GATT”). Originally implemented in 1948, the GATT is the foundation for many other multilateral trade agreements. The GATT generally applies to international regulations pertaining to trade in goods. One of the basic principles that each country agrees to in signing onto the GATT is the principle of national treatment. Under this

119 Id.
120 Id.
124 GATT, supra note 121, art. III.
principle, in the context of international trade, member countries are not permitted to tax, regulate, or enact other laws which afford protection to domestic products. The national treatment rule endorsed by the GATT is, however, limited by several enumerated exceptions. Among the specific exceptions is that “[t]he provisions of this Article shall not prevent the payment of subsidies exclusively to domestic producers . . . .” The reason for this exception is said to be a recognition of subsidies as an important governmental policy tool.

Still, in recognition that subsidies may have a negative impact on trade, the WTO member countries enacted an additional Agreement on Subsidies and Countervailing Measures (“SCM”). The SCM limits the general permissibility of subsidies under the GATT and further defines which types of subsidies are to be permitted and prohibited. The SCM defines a subsidy as any (i) financial contribution, (ii) by a government within a member country, (iii) which confers a benefit. If a government action qualifies as a subsidy, the SCM prohibits the subsidy if, for example, it is “contingent . . . upon export performance.” The definition of export performance under the SCM is intentionally broad and includes cases where the facts demonstrate that the subsidy is “tied to actual or anticipated exportation or export earnings.”

The GATT refers to IP rights only briefly in one section. Understanding the need to provide minimum substantive legal protections for IP internationally, members of the WTO

125 Id. art. III:1.
126 See generally id. art. III.
127 Id. art. III:8(b).
130 Id.
131 Id. art. I.
132 Id. art. III:1(a).
133 Id. n.4.
134 GATT, supra note 127, art. XX:(d) (“[N]othing in this agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures . . . necessary to . . . [protect] patents, trade marks and copyrights . . . .”).
developed the Agreement on Trade Related Aspects of Intellectual Property Rights ("TRIPS Agreement"). Under this agreement, countries agree to implement minimum standards for IP protection and enforcement. Among other types of IP, the TRIPS Agreement applies to both patents and trademarks.

Like the GATT, the TRIPS Agreement also requires adherence to the rule of national treatment. Under this principle, member countries are not permitted to treat member country nationals any less favorably than its own nationals with regard to IP protection. "Protection," as it is defined in the TRIPS Agreement includes “the availability, acquisition, scope, maintenance, and enforcement of intellectual property rights . . . .” Put more simply, the national treatment clause in the TRIPS Agreement prohibits discrimination between nationals of a member’s own country and nationals of another member’s country in regards to securing or enforcing IP rights. This national treatment principle serves the important purpose of eliminating domestic barriers to IP protection between WTO members. Unlike the GATT, the TRIPS Agreement provides only for very limited and specific deviations from the national treatment rule.

B. Chinese IP Subsidies Under the SCM and TRIPS Agreements

136 TRIPS Agreement, supra note 141.
137 See id. part II.5 and part II.2.
138 GATT, supra note 127, art. III.
139 Id.
140 TRIPS Agreement, supra note 141 n.3.
143 TRIPS Agreement, supra note 141, art. 3.
China is a member of the WTO and is party to the GATT, SCM and TRIPS Agreements. Thus, under these agreements, China is required both to abide by the national treatment principle enunciated in the TRIPS Agreement and to refrain from providing prohibited subsidies under the SCM. In enacting its subsidies for patent and trademark applications domestic and abroad, China likely violates its obligations under both the SCM and the TRIPS Agreement.

\[i\]. \textit{The SCM Agreement Violation}

By offering subsidies to Chinese applicants contingent on their acquisition of foreign IP rights, China likely violates article 3.1(a) of the SCM.

\[1\]. \textit{The Chinese IP Subsidies Qualify as “Subsidies” under the SCM}

As noted before, Article 1.1 of the SCM defines a subsidy as a (i) financial contribution, (ii) by a government within a member country, (iii) which confers a benefit. Here, the cash payments provided by the Chinese government to Chinese nationals for their acquisition of foreign IP rights qualify as subsidies. First, a financial contribution has been defined by WTO Appellate Bodies as a transfer of economic resources by the grantor.

\[^{144}\text{Amendment of the TRIPS Agreement, WTO, https://www.wto.org/english/tratop_e/trips_e/amendment_e.htm} \] (listing China as a signatory to the TRIPS Agreement); \[^{145}\text{Trade Guide: WTO Subsidies Agreement, INT’L TRADE ADMIN. https://www.trade.gov/trade-guide-wto-subsidies} \] (noting all WTO members are parties to the SCM); \[^{146}\text{Understanding the WTO: The Organization, WTO, https://www.wto.org/english/thewto_e/whatis_e/tif_e/org6_e.htm} \] (listing China as a member of the WTO).

\[^{147}\text{See supra Section IV.A.}\]

\[^{148}\text{See SCM, supra note 135 and TRIPS Agreement, supra note 141.}\]

the cash payments provided to applicants by the Chinese government represent a transfer of economic resources, Chinese currency, by the grantor, the Chinese government.\textsuperscript{150} Second, many of the cash payments are offered by Chinese provincial governments,\textsuperscript{151} which are governments within China—a member country of the WTO.\textsuperscript{152} Third, the benefit provision of the SCM has been interpreted to require that a recipient receive a financial contribution on terms more favorable than the open market.\textsuperscript{153} Here, the cash payments from China render foreign IP filings by applicants receiving the payments cheaper than if they were to file from another country. Given that the Chinese payments meet the requirements under article 1.1 of the SCM, they qualify as subsidies under the agreement.

2. The Chinese Subsidies Are De Facto Export Subsidies

Next, the subsidies provided by China to Chinese applicants filing abroad are prohibited under the SCM insofar as they are contingent on export performance.\textsuperscript{154} Such prohibited export subsidies may be either \textit{de jure} export subsidies, or \textit{de facto} export subsidies.\textsuperscript{155} \textit{De jure} export subsidies occur when the subsidy is contingent \textit{in law} on export performance, based on the words of the relevant legislation.\textsuperscript{156} \textit{De facto} export subsidies, are inferred from the totality of the surrounding facts.\textsuperscript{157} The difference between \textit{de facto} and \textit{de jure} export subsidies has been described as “what evidence may be employed to prove that a subsidy is export contingent.”\textsuperscript{158}
Here, the Chinese legislation only provides for subsidies where applicants seek or obtain foreign patent protection and does not explicitly require exportation of goods or services.\(^{159}\) Thus, the legislation alone would likely be insufficient evidence to prove that the subsidies are \textit{de jure} export subsidies contingent on export performance.\(^{160}\) Instead, the Chinese subsidies should be analyzed under \textit{de facto} export subsidy law and should be examined in light of the surrounding facts.

3. The De Facto Export Subsidies Are Prohibited under Article 3.1(a) of the SCN

This contingency requirement has been interpreted by the \textit{Canada—Aircraft} Appellate Body to require that there be (i) a granting of a subsidy, (ii) that is tied to, (iii) anticipated export earnings.\(^{161}\) Regarding the Chinese subsidies, the first element is met, insofar as the Chinese government grants a subsidy by providing domestic applicants monetary payments that meet the requirements of Article I:1 of the SCM, as discussed above.

Next, skipping to the third element, the subsidies were granted in anticipation of export earnings. The Appellate Body in \textit{Canada—Aircraft} clarified that the “meaning of the word ‘anticipated’ is ‘expected.”’\(^{162}\) Acquiring IP rights generally confers the exclusive rights to use, exclude, license, or sell using a particular trade name or technology within the granting country.\(^{163}\) In some cases, such as in the Amazon Brand Registry Program, US trademark owners even are given preferential treatment and exclusive promotion to customers.\(^{164}\) Although some IP rights may be more valuable than others, working the foreign patent or trademark can be

\(^{159}\) See, e.g., Shenzhen Patent Application Funding, supra note 70.
\(^{160}\) See id.
\(^{162}\) Id. at ¶ 172.
\(^{163}\) \textit{What Are Intellectual Property Rights?}, WTO, https://www.wto.org/english/tratop_e/trips_e/intel1_e.htm#:~:text=Intellectual%20property%20rights%20are%20t
\(^{164}\) See McLaughlin, supra note 79 at 1805.
expected to provide financial earnings to the owner in the form of increased sales or profits.\textsuperscript{165} These financial earnings may be derived from products exported from China, in which case the exports are driven by the underlying IP right.\textsuperscript{166} Thus, one could likely expect to incur such export earnings as a result of the patent or trademark protection, paid for by the Chinese subsidy.

In \textit{Canada—Aircraft}, the Panel also elaborated on the meaning of “export performance” by distinguishing “export performance” from “technological benefits to Canada.”\textsuperscript{167} In \textit{Canada—Aircraft}, a project’s subsidy was conditioned on the technological benefits provided to Canada.\textsuperscript{168} The Panel acknowledged that some of the projects with higher technological and economic benefits may indeed yield an increase in an exports or export earnings.\textsuperscript{169} However, the technological benefits could not be considered synonymous with export performance, given that they lacked information for the grantors to select projects on the basis of export performance.\textsuperscript{170}

Although one might analogize these subsidies to the Chinese IP subsidies, the two are distinguishable. While the \textit{Canada—Aircraft} subsidies were conditioned on technological benefits to Canada,\textsuperscript{171} the Chinese subsidies are conditioned on procurement of an IP right in the \textit{US}.\textsuperscript{172} Utilization of the technological benefits to Canada may or may not result in increased export performance.\textsuperscript{173} The technological benefits could be retained solely within Canada and

\begin{itemize}
\item\textsuperscript{165} \textit{Valuation of Intellectual Property Rights} 20, RCIS (2020).
\item\textsuperscript{166} \textit{Cong. Res. Serv.}, RL34292, \textit{Intellectual Property Rights and International Trade} 6 (2020) (“Intellectual property generally is viewed as a longstanding strategic driver of . . . exports.”).
\item\textsuperscript{167} Panel Report, \textit{Canada—Measures Affecting the Export of Civilian Aircraft, Recourse by Brazil to Article 21.5 of the DSU}, ¶ 5.33, WTO Doc. WT/DS70RW (adopted May 9, 2000) [hereinafter Panel Report, \textit{Canada—Aircraft} (Article 21.5—Brazil)].
\item\textsuperscript{168} Id.
\item\textsuperscript{169} Id.
\item\textsuperscript{170} Id.
\item\textsuperscript{171} Id.
\item\textsuperscript{172} See, e.g., Shenzhen Patent Application Funding, \textit{supra} note 70.
\item\textsuperscript{173} Panel Report, \textit{Canada—Aircraft} (Article 21.5—Brazil), \textit{supra} note 167, ¶ 5.33.
\end{itemize}
provide for the benefit to Canada without ever being exported. Thus, the technological benefits to Canada have independent value aside from their export potential. Working the foreign-owned US IP right, on the other hand, results in export earnings from increased sales generated by the competitive advantage conferred by the US IP right. Unlike the technological benefits to Canada, these foreign IP rights generally lack any value aside from the competitive advantage they provide in the US marketplace.174 Whereas Canada sought to subsidize anything providing technological benefits to itself, regardless of whether it is exported, under this measure, China only subsidizes procurement of the competitive advantage, in the form of an IP right, in the US. By only subsidizing the procurement of this increased ability to compete in the US marketplace, China effectively only “select[s] projects on the basis of increased export performance.”175

Admittedly, a strong counterargument exists to the contention that the procurement of US IP rights can be synonymous with export performance. The argument here would be that regardless of whether the IP right turns out to be profitable and therefore actually leads to export performance, the subsidy for its procurement is still granted. Thus, because there is no penalty or revocation of the subsidy for failing to profitably work the IP right, in some cases, the subsidy would be granted despite the lack of any export performance. This argument has been considered and rejected by at least one WTO Panel.176 Although the Panel agreed that the argument had merit regarding actual export earnings, the argument fails to rebut the prima facie showing that a subsidy would not have been granted but for anticipated export earnings.177 Thus, because

175 Panel Report, Canada—Aircraft (Article 21.5—Brazil), supra note 167, ¶ 5.33.
176 Id. ¶ 9.343.
177 Id. ¶ 9.343.
Chinese subsidized IP rights yield *anticipated* export earnings, the fact that they do not penalize applicants who’s rights do not ultimately produce export profits is not fatal to this analysis.

Another potential counterargument may be that a Chinese owner of a US IP right need not necessarily produce the protected product in China. They could have the product made in the US and collect earnings on the product without ever having exported it into the US. This argument fails for two reasons. The first is a practical point. Comparatively speaking, Chinese manufacturing costs are significantly lower than the US.\(^{178}\) It is one of the reasons that China has been coined “the world’s factory.”\(^ {179}\) Moving manufacturing operations outside of China would likely be economically irrational for these Chinese owners of US IP rights.\(^ {180}\) Second, the mere fact that some of the subsidized products are manufactured abroad “does not dissolve the export contingency arising in the first set of circumstances[]”–domestic production and subsequent exportation.\(^ {181}\) Even if some protected products were manufactured outside of China, under this holding, the Chinese acquisition of US IP rights can still be considered synonymous with export performance.

Finally, the second element, whether the subsidy is *tied to* the export earnings, likely applies to the Chinese IP subsidies. The *Canada—Aircraft* Panel elaborated on this element, stating that the nature of the required conditionality is that “one of the conditions for the grant of the subsidy is the expectation that exports will flow thereby.”\(^ {182}\) In ascertaining whether the

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\(^ {179}\) Id.

\(^ {180}\) See id.


subsidy is tied to the anticipated exportation, the Appellate Body in *EC and Certain Member States—Large Civil Aircraft*, established the export inducement test, clarifying that export contingency must be inferred from factors including the: “(i) design and structure of the measure granting the subsidy, (ii) the modalities of operation set out in such a measure, and (iii) the relevant factual circumstances surrounding the granting of the subsidy that provide the context for understanding the measure’s design, structure, and modalities of operation.” Various Panels and Appellate Bodies have found different factors relevant in this analysis. One such factor is the ratios test, wherein the ratio of export earnings with the subsidy is compared to the situation without the subsidy.

As noted in previous sections, the Chinese government provides cash rewards for the successful granting of IP rights. For example, at least one of the cash reward subsidies states that “[a]pplicants who have obtained invention patents from the United States Patent and Trademark Office . . . will receive a grant of 40,000 yuan each.” Here, the measure enacting the subsidy is designed and structured so that the provision of the subsidy is explicitly contingent on the condition that an applicant have obtained a US invention patent. As discussed in above, IP rights, such as patent rights, confer an expectation of export earnings. Thus, the measure here is structured so that the provision of the subsidy is explicitly conditioned upon expected export earnings.

Next, the modality of operation of the subsidy is similarly simple. In practice, Chinese applicants who obtain a US patent are eligible for a 40,000 yuan subsidy. Those who do not

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184 Id. at ¶ 1047.
185 Notice on Special Funds, *supra* note 75 art. 7.1 (machine translation).
186 Id.
obtain a US patent are not eligible. To apply for the subsidy, applicants need only submit an application form, qualification materials, receipts, and the patent certificate. Although there are certain limits on the number of subsidies applicants are eligible for within a given year, until they reach that amount, applicants are free to obtain this subsidy. No entities may secure this subsidy without securing the US patent right. Thus, the actual operation of the subsidy works to condition the subsidy on the anticipated export earnings.

Finally, the factual circumstances surrounding the grant of the subsidy indicate that it is tied to export earnings. Over the past 15 years the Chinese subsidies have been in force, Chinese exports have increased by approximately two hundred percent. To be clear, there are likely many other causes for this increase in exportation, but still, under the ratios analysis this sort of circumstantial evidence may support that the subsidies are tied to export earnings.

Because the Chinese subsidies meet the definition of a “subsidy” under the SCM and are contingent on export performance, Chinese subsidies granting payment to Chinese applicants who successfully secure IP protection in the US are likely prohibited under the SCM.

ii. The TRIPS Agreement Violation

It is unlikely that Chinese subsidies to Chinese nationals applying for domestic IP rights would be classified as prohibited export contingent subsidies under the SCM. This is because the domestic IP right would likely not be sufficiently “tied to” anticipated export earnings, or because the domestic IP right would not be considered synonymous with “export earnings”. However, by providing subsidies for Chinese nationals applying these domestic IP rights, China

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187 See id.
188 Id.
189 Id.
190 Id.
likely violates its obligations under the TRIPS Agreement. As noted above, under both the GATT and TRIPS Agreements, member countries must abide by the principle of national treatment.\footnote{See supra Section IV.A.} The GATT defines national treatment specifically as it relates to the imposition of trade barriers.\footnote{GATT, supra note 127, art. III.} The GATT, however, lists domestic subsidies provided to domestic entities as exceptions to the requirement that countries do not discriminate between foreign and domestic entities in their imposition of trade barriers.\footnote{Id. art. III:8(b).} In carving out domestic subsidies, the GATT allows countries to discriminate between foreign and domestic entities in granting subsidies and implicitly acknowledges that such domestic subsidies generally violate the principle of national treatment.

The TRIPS Agreement defines additional rules, that add to “the basic principles of GATT 1994 and . . . relevant international intellectual property agreements[.]”\footnote{TRIPS Agreement, supra note 141 pmbl.} The TRIPS Agreement defines and requires national treatment specifically as it relates to the acquisition and enforcement of IP rights.\footnote{TRIPS Agreement, supra note 141 n.3.} Because it serves as a separate additional agreement, the national treatment rules enunciated in the TRIPS Agreement do not merely restate those of the GATT but provide for enhanced level of IP protection.\footnote{“The protection of intellectual property is one of the three pillars of the WTO, the other two being trade in goods (the area traditionally covered by the General Agreement on Tariffs and Trade (GATT)) and the new agreement on trade in services.” A. Otten & H. Wager, Compliance with TRIPS: The Emerging World View, 29, VAND. J. TRANSNAT’L L. 391, 393 (1996).} Unlike the GATT, the TRIPS Agreement does not contain a domestic subsidy exception to the national treatment rule.\footnote{See generally TRIPS Agreement, supra note 141.} Thus, it would seem that for acquisitions of IP, domestic subsidies provided to domestic citizens violate the rule of national treatment promulgated by the TRIPS Agreement.
Article 31(2)(a) of the Vienna Convention on the Law of Treaties allows consideration of “an agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty.”\(^{199}\) The GATT is “an agreement relating to the [TRIPS Agreement] made between all the parties in connection with the conclusion of the [TRIPS Agreement]” and therefore, may be considered in interpreting the TRIPS Agreement.\(^{200}\) As noted above, the GATT proclaims the national treatment principle but includes a specific exception to immunize domestic subsidies from being held as violations of the principle of national treatment.\(^{201}\) The TRIPS Agreement, while also proclaiming the principle of national treatment, does not include any exceptions that immunize domestic subsidies offered in violation of this principle.\(^{202}\) Therefore, by including a national treatment exception for subsidies in the GATT, which pertains to goods, but not in the TRIPS Agreement, which pertains to IP, it seems as though subsidies for the acquisition of IP rights are not exempted from the national treatment principle in the TRIPS Agreement.

As noted above, the Chinese government currently provides subsidies to Chinese nationals for their application for or acquisition of patent and trademark rights in China.\(^{203}\) These subsidies do not appear to be available to non-Chinese applicants.\(^{204}\) The national treatment rules of the TRIPS Agreement prohibit discrimination between national and foreign applicants seeking to secure IP protection in a member country.\(^{205}\) Providing subsidies to Chinese patent and

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\(^{200}\) *Id.*

\(^{201}\) GATT, *supra* note 127, art. III:8(b).

\(^{202}\) See generally TRIPS Agreement, *supra* note 141.

\(^{203}\) See generally *supra* Sections II.A and III.A.

\(^{204}\) *Id.*

\(^{205}\) TRIPS Agreement, *supra* note 141, art. III.
trademark applicants while denying them to non-Chinese applicants involves discriminating between applicants based on their nationality. Thus, the subsidies provided to the Chinese nationals, which make acquiring Chinese IP rights more expensive for foreign applicants than domestic applicants, violate the national treatment principles of the TRIPS Agreement.

V. CONCLUSION

Chinese applications for patents and trademarks have exploded in number over the past ten years.\textsuperscript{206} To some degree, this increase in filings can be attributed to subsidy programs offered to domestic applicants by the Chinese government.\textsuperscript{207} These subsidies, offered for foreign and domestic IP acquisitions, have legitimate and profound international consequences.\textsuperscript{208} Domestic solutions to these issues would likely require the expenditure of additional resources from the US or other affected countries. However, by sponsoring these subsidy programs, China disobeys national treatment principles enacted under the TRIPS Agreement and disregards its obligations under the SCM.\textsuperscript{209} Thus, WTO members should seek to enforce these agreements to curb China’s continued violations.

\textsuperscript{206} See supra Parts II and III.
\textsuperscript{207} Id.
\textsuperscript{208} See supra Sections II.A and III.A.
\textsuperscript{209} See supra Part IV.