Whose Patent Is It, Anyway?

A rival says that GS Magic Stor stole some design elements of the hard drives it sells to Apple Computer for the mini iPod.

By HOWARD FRENCH
Published: March 5, 2005

GUIYANG, China - Each shift, 200 workers, most of them women in smocks and bibs, labor in a factory tucked away in hilly farmland outside this city assembling a single product, one-inch hard drives.

As China's emerging industrial centers go, Guiyang is an obscure outpost, bearing little resemblance to the booming factory towns of the east coast. And yet, as much as any other place in China this hard drive assembly may be at the front line of an intense global struggle to dominate high-tech manufacturing.
The tiny storage device this factory churns out is the heart of one of the world's hottest consumer electronics items, the mini version of Apple Computer's iPod. Sales to Apple represent a huge triumph for GS Magic Stor, an offshoot of a struggling state-owned carmaker that is so obscure that even in China few are familiar with the name. The problem with this ringing success story, according to a better-established rival, Hitachi Global Storage Technologies, which has factories in China and also supplies miniaturized drives to Apple, is that the Chinese company stole crucial elements of the design.

GS Magic Stor denies this charge, which Hitachi has made in a suit filed in Federal District Court in Northern California. In a recent online forum the company's president ridiculed Hitachi's claim, likening it to someone's asking carmakers to pay design rights to the inventors of the horse and buggy. A Hitachi official, who refused to comment further, said that GS Magic Stor could characterize the Hitachi patents however it wished, "but the plain and simple matter is they haven't expired." Hitachi's highly technical complaint specifies several areas where it says its designs were infringed by Magic Stor.

Apple, which was not named in Hitachi's suit, would not comment. Even if Hitachi wins the suit, that would do nothing to stop Magic Stor from continuing to produce its miniature hard drives in China, although some analysts say that Apple would be forced for image reasons, if nothing else, to drop Magic Stor as a supplier.

For Western companies competing with China as well as those doing business here, the issue goes well beyond the fate of one obscure company or of a single technology, however valuable. In one sector after another, companies warn that China's swift industrial rise is being greased by brazen and increasingly sophisticated theft of intellectual property.

The issue of intellectual property theft has been a fixture on the trade agenda between the United States and China for years, with visiting American officials routinely stopping at the famous Silk Market in Beijing to highlight the sale there, like all over China, of cheap knockoffs of toys, clothing, software and DVD's.

The Chinese government has recently razed the market, but the counterfeit activity has been moving relentlessly upscale, with General Motors, Cisco, Sony and Pfizer, just to name the most high-profile companies, complaining that their designs or formulas for everything from cars and PlayStations to routers and Viagra, have been violated.
"Until recently, when China began putting intellectual property laws in place, for the past 40 years, all patents were owned by the government, and could be shared by any company that was willing to use them," said Paul Gao, a Shanghai-based expert on consumer electronics and automotives at McKinsey & Company. "The Chinese government actually encouraged this, and that has left a deep impression on companies that intellectual property is there for anyone to use it."

Experts say the practice of copycat production is also fueled by the fierce competition among Chinese companies and provinces to join the global economy. "With the extreme fragmentation of industry, you see a lot of subscale players that are trying to survive in the market on their own," Mr. Gao added. "They don't have the budget for research and development or the scale to compete. If they pay a licensing fee, they consider they are essentially imposing a death penalty on themselves."

Like many people on the receiving end of accusations of intellectual property theft here, GS Magic Stor's president, Zhu Baolin, fiercely denies his company has done anything wrong, and goes so far as to say that the lawsuit is an act of desperation by a foreign enterprise unable to compete with his Chinese company.

"We don't blame Hitachi for what they are doing," said Mr. Zhu, a 25-year electronics industry veteran. "We just want Chinese people to know we created our own product, and that we face a lot of pressure. This will happen a lot in the future in the knowledge industry, but we will still work hard to grow."

Beyond the case of Hitachi versus Magic Stor, many Chinese legal experts simply deny there is any special problem with theft of intellectual property in China. "It may look like it's a China problem, but it's a worldwide problem, just like piracy on the Internet, and it exists in America as well," said Zhang Ping, a law professor at Beijing University, and one of China's leading experts on intellectual property rights. "There are many problems with fake products, with low levels of technology. These can't be counted as intellectual property violations. They are just cheap fakes."

Like many people professionally involved with this issue here, Ms. Zhang denied that China was a leading violator of intellectual property rights, which she acknowledged was still a relatively new concept in China. She also said that the country's efforts at improving enforcement, though steady, would require more time to reach the standards of intellectual property rights in many advanced industrialized countries.

Lawyers who represent Western companies embroiled in intellectual property disputes in China, however, point to major loopholes in Chinese law and in the country's trademark and patent system as parts of the problem. Many Chinese patents, for example, are granted without any examination of their originality, making it easy for local companies to claim others' innovations as their own.

While foreign experts also point to progress in the country's courts and especially in the richer provinces along the country's east coast, they say that local and provincial governments, eager to bolster their economies, sometimes subsidize patent filings for local companies and provide pointers to them on how to beat foreign claims of infringement.
Even the Shanghai government speaks of building a "great wall of patents" to protect local companies.

"Once upon a time, the counterfeeters in China ran away when you came after them," said Xiang Wang, a lawyer specializing in intellectual property rights at White & Case in Shanghai. "Today, they don't run away. Indeed, they stay put and they sue us. More and more Chinese companies are taking a so-called legal approach, taking advantage of serious weakness in the Chinese legal system."

One of the most problematic areas, experts say, are joint ventures between foreign and Chinese companies, which are legion. When the joint venture dissolves, or sometimes even while it remains active, the Chinese party makes use of the technology or manufacturing processes illegally. A perennially told war story in business circles here involves the foreign factory owner who makes a wrong turn while driving to his plant only to discover an exact copy of his factory on the other side of the mountain.

Although this story might be apocryphal, Mr. Wang said he saw cases all the time that are not so different in their details. "We have a client in the power business who found that one of his key employees had quit and joined a competitor, revealing confidential information to him straight away, and filing patents of these materials which were literal copies of the original technology," he said. "When our client warned he would sue over patent infringement, the Chinese company said it was also planning to sue. 'And by the way,' they asked, 'what patent are you talking about? This is our patent now.' "

The New York Times Online Edition Special Offer: 1 Week Free
• Job Growth Rises, to Delight of Investors
• Citgo’s Status Is Giving Houston the Jitters
• Jurors in the Ebbers Trial Begin Their Deliberations
   Go to Business