ORAL REMARKS BY SHAUN DONNELLY ON BEHALF OF

THE NATIONAL ASSOCIATION OF MANUFACTURERS

BEFORE THE

INTERNATIONAL TRADE COMMISSION

PANEL 2

CHINA: EFFECTS OF INTELLECTUAL PROPERTY INFRINGEMENT AND INDIGENOUS INNOVATION POLICIES ON THE U.S. ECONOMY

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Good morning, Chairperson Aronoff and members of the Commission.

I am Shaun Donnelly, Senior Director, International Business Policy at the National association of Manufacturers (NAM). I am pleased to speak this morning on behalf of the NAM before the International Trade Commission on "China: Intellectual Property Infringement, Indigenous Innovation Policies, and Frameworks for Measuring the Effects on the U.S. Economy." We are very pleased that the ITC is holding this important session as one element in its work in responding to the April 19 request from the U.S. Senate Committee on Finance for in-depth reports in these important issues related to Intellectual Property Rights (IPR) and Indigenous Innovation in China.

The NAM is our nation's largest industrial trade association, representing small and large manufacturers in every industrial sector and in all 50 states. Its membership includes both large multinational corporations with operations in many foreign countries, including China, as well as small and medium manufacturers with little or no involvement in international trade.

The NAM has long recognized the importance of IPR in promoting, protecting and incentivizing innovation in the U.S. economy. And, in turn, innovation is critical to economic growth, global competitiveness, exports, and job creation. The NAM has for many years had an active IPR subcommittee. But earlier this year, our Board of Directors approved the creation of an additional special NAM Task Force on International Intellectual Property Rights to focus more specifically and more aggressively on the growing volume of IPR problems origination outside our borders and their impact here at home. And I can assure you, Commissioners, that China was front and center among our companies and our board they established this new Task Force.

The new Task Force, chaired by the Vice President for Intellectual Property Rights at ITW, is off to a very busy start. We are working closely with all the relevant agencies of the U.S. Government, including the new White House-based U.S. Intellectual Property Enforcement Coordinator, Victoria Espinel, with whom our Task Force has already had an excellent meeting.

The fundamental message of American manufacturers is that strong, aggressive, international IPR protections are critical to the continued growth, competitiveness and success of U.S. manufacturers, small and large. IPR is not a niche issue. IPR is not, as some allege, a concern limited to a few large corporations or to a few important sectors such as pharmaceuticals, software and entertainment. Those sectors are certainly on the front lines of the international IPR battlefields and have been for some time and we are certainly proud to claim them as manufacturers and active members of the NAM. But today's, and more importantly tomorrow's, defining reality is that all American manufacturers rely on strong IPR protections here at home and around the world.

In few, if any, manufactured goods sectors these days is the U.S. the low-cost producer of basic, "commoditized" products. Our manufacturing base, our manufacturing strategies, and our American manufacturing jobs are based on producing high-quality products, hi-tech manufacturing processes and products, cutting-edge design, high-quality branding, trademarks, and reputations based on product and service quality. All those competitiveness factors come back to IPR.

Our Manufacturers' IPR agenda is a comprehensive one, including strengthening and updating our own IPR domestic legislation and enforcement programs, ensuring adequate U.S. Government funding, and advocating strong U.S. international policy initiatives including: negotiation of a strong Anti-Counterfeiting Trade Agreement (ACTA); opposition to expanded and ill-conceived compulsory licensing proposals whether in the pharmaceutical, environmental technologies or any other sector; and restoring the relevant international organizations including the World Intellectual Property Organization (WIPO), World Customs Organization (WCO) and the World Trade Organization (WTO) to their appropriate roles in promoting IPR and combating counterfeiting and piracy.

The Impact of Counterfeiting and Piracy

We strongly endorse the efforts of the Administration, the Congress and of the International Trade Commission, including via this hearing and other ongoing research and analytical work, to assess the impact of international IPR counterfeiting and piracy on the United States. Developing detailed data and metrics in this critical area is very challenging. We at the NAM are prepared to contribute to this effort.

Conceptually, I think it is important to focus on several major areas in terms of the cost or risk to the United States from international counterfeiting and piracy:

- The direct economic loss of foregone sales revenues, exports and corporate profits.

- The direct impact on employment, job loss and reduced hours for U.S. workers, in affected industries.

- The direct costs imposed on U.S. manufacturers, especially SMMs, to combat piracy and counterfeiting in China – investigation and litigation costs,

- translations, staff and executive time devoted to the issue, travel costs, etc.

- The indirect costs of damage to product reputation and brand names which are counterfeited and pirated.

- The risk to consumer health and safety from unsafe counterfeited and pirated products.

Compiling, extrapolating, and estimating these total costs is truly a daunting task but we at the NAM are pleased that the Administration, the Congress and the ITC are focusing seriously on these questions.

China

Unfortunately, the stark reality is that China remains Ground Zero for international product counterfeiting and piracy. Despite considerable efforts over many years by various U.S. Government agencies and some international partners as well as some efforts by Chinese government authorities, progress has been minimal. The U.S. Customs and Border Protection (CBP) and the U.S. Immigration and Customs Enforcement (ICE) agencies, both part of the Department of Homeland Security, recently reported that in U.S. FY 2009, China continued to be the number one source country for counterfeit and pirated goods seized at U.S. borders, accounting for 79 percent of total seizures and $ 205 million in value. The top sectors of IPR-infringing products seized included footwear, consumer electronics, apparel, computers/hardware, pharmaceuticals, toys/electronics games, and jewelry. Beyond the economic and job losses to U.S. companies and workers, many of these counterfeit and pirated products raise potentially serious health and safety risks for American consumers.

NAM member companies, small and large and in a wide range of product sectors ranging from pharmaceuticals and personal care products to auto parts and chemicals, report increasing instances of counterfeit and pirated products showing up in U.S. and international markets. And, as noted above, in the vast majority of cases, those IPR-infringing products trace their roots, directly or indirectly, back to China. We have urged the U.S Intellectual Property Enforcement Coordinator and key U.S. Government agencies to focus explicitly on China in the development of the national IP Enforcement Strategy which we await with great interest. Enforcement of IPR rights in China by American companies is very challenging and costly. The IPR culture and the effort vary widely around the different regions of China; some problems seem stuck on central government/provincial/local differences.

But it is certainly clear that when the Chinese authorities decide that an IP-infringing product has an unacceptable political message or threatens a major Chinese interest, they seem to have the ability to stamp out the infringing product very quickly and very effectively. So the capability for improved Chinese enforcement is, I believe, proven to exist.

There are some important policy problems which our government needs to keep pushing aggressively with the Chinese authorities. Currently 99 percent of copyright and trademark counterfeiting cases in China are enforced administratively, rather than criminally. In these circumstances, counterfeiters can foresee that, if convicted, they would simply receive a fine, a mere cost of doing business, not a real deterrent. A greater number of cases must be referred for serious criminal prosecution.

In addition, in a case when there is a counterfeiting conviction, the equipment used to produce the counterfeit goods must be destroyed. Far too often under current Chinese law and practice, it is too easy for Chinese counterfeiters to leave the courtroom and pick right back up with the same tools of their criminal trade, the machines used to produce those counterfeits.

Small and Medium Manufacturers

All U.S. manufacturers face major IPR challenges in and from China. All of us need strong U.S. Government support in combating Chinese counterfeiting and piracy. But is especially critical that the U.S. Government focus increasingly on the challenges faced in this area by U.S. small and medium-sized manufacturers (SMMs). Some SMMs that have never even exported their products still find counterfeit versions of their patented and trademarked products showing up in international markets, for sale over the internet, and even for sale here in the U.S.

The NAM recognizes the efforts made by various U.S. government agencies, including under the on-going Strategy Targeting Organized Piracy or "STOP" program, but much more needs to be done. SMMs need more assistance in understanding the international IPR environment - laws, regulations, remedies, and risks in key markets including China – to help them take proactive measures and try to avoid IPR problems around the world.

But when SMMs and other smaller companies, through no fault of their own, find themselves facing IPR problems in a place like China they need strong support from all the relevant U.S. government agencies. And that support from the various agencies needs to be fully coordinated. It appears that some other foreign governments, for example Japan, have been more proactive and have provided more resources and hands-on support for their smaller companies in combating IPR piracy in China. Our Government needs to study what has and hasn't worked for other partner governments in China and develop a more-focused, more-coordinated, better-resourced and more-aggressive program to assist our SMMs in combating IPR counterfeiting and piracy in China. Our SMMs deserve at least a level playing field in terms of support from our government in combating IPR theft in china.

Recommendations for U.S. Government Action on Chinese IPR Infringement

I wish that I, or anyone else on this panel or beyond, could lay out a simple remedy or set of remedies to solve the IPR counterfeiting and piracy problems in China. I can't do that; and I doubt any of my colleagues of this or any other panel can either. These are complex and challenging issues. What I can offer for the Commission's consideration is a menu of things we and our member companies feel could usefully be part of an overall U.S. Government approach to the IPR challenges we face in China. In

some areas, we recommend continuation and/or expansion of existing effort but we also include some new ideas. We will continue our dialogue with the administration, the Congress and other interested parties to help address these critical challenges:

- First and perhaps most importantly, it is important that all agencies of the U.S. Government dealing with China recognize that counterfeiting, piracy and broader IPR policy issues are huge problems in China and deserve to be high on the overall U.S.-China agenda. These issues cannot "just" be left to the IPR technicians or to technical agencies and experts to solve. Cabinet members and other top USG official in all relevant agencies need to put IPR problems high on the agenda and to press aggressively with Chinese counterparts for solution to these problems.

- All relevant U.S. government agencies (law enforcement as well as policy agencies) need to coordinate their IPR activities in and with China. This applies to Washington headquarters policy coordination as well as the various agencies represented in the U.S. embassy in Beijing and our U.S. consulates general around China, as well as to U.S. offices (e.g. the U.S. Export Assistance Centers and Small Business Administration offices as well as DHS' Customs and Border Protection and Immigration and Customs enforcement network of border posts) around the country.

- The role of the new U.S. Intellectual Property Enforcement Coordinator (IPEC) in the Executive Office of the President (EOP) is critical. The NAM strongly supported the establishment of the U.S. IPEC as part of the "PRO-IP" legislation in 2008. We look forward to the first coordinated IPEC National IP Enforcement Strategy. We anticipate that China will be an explicit priority focus of that overall strategy.

- Education and outreach to the U.S. business community, especially Small and Medium Manufactures on the challenging international IPR environment is critical. Some good work has been done but much more effort and more proactive approach are needed. And China needs to be a critical element of that education and outreach effort. The NAM stands ready to assist in any way we can in getting the word out.

- The Office of the U.S. Trade Representative (USTR) has enjoyed some success in taking, either in connection with other international partners or alone, IPR-related dispute settlement cases against Chain to the world Trade Organization (WTO). While that process can be long and frustrating, it has delivered results. We encourage USTR to continue to work closely with U.S. industry to identify priority problems which can lend themselves to that WTO dispute settlement cases.

- We encourage the Administration to develop a major program of hands-on assistance targeted for American small and medium manufacturers facing IPR challenges in China. We need a strong interagency "one-stop shop" here in the U.S. easily accessible on the internet and via an 800 number that can provide basic background information but also open the door to customized support (legal advice, support from the U.S. Embassy/consulate staff on the

ground in China, assistance with translations and interpretations, etc). Other developed countries, including Japan, seem to have found ways to provide this sort of support. Our government should be doing no less.

China's Indigenous Innovation Policy

I also want to say a word about another critical issue on the Commission's agenda – China's new Indigenous Innovation policy. This is a critical issue and again is one of broad concern to U.S. manufacturers across the board. Like the broader IPR issues, Indigenous Innovation is not a niche issue affecting only large multinational companies or only a few "High Tech" sectors.

China's interest in developing industries that drive innovation is a legitimate one, shared by many countries. Many NAM member companies have contributed to the development of China's innovative capacity through their R&D and other investments in China. But there are real concerns that the approach taken in the 2009 Circular No. 618 would exclude a significant number of U.S. firms in a wide range of government purchases, while not achieving the goals China has set.

The NAM has joined a number of key U.S. business organizations in expressing our concerns to both the U.S. and the Chinese government, including providing detailed comments on the April 2010 directive, which made efforts to address a number of foreign-invested firms' concerns.

We support the outcome of the recent U.S.-China Strategic and Economic Dialogue (S&ED) that reaffirms that "innovation policies will be consistent with the following principles: non-discrimination; support for market competition and open international trade and investment; strong enforcement of intellectual property rights; and, consistent with WTO rules, leaving the terms and conditions of technology transfer, production processes and other proprietary information to agreement between individual enterprises."

We will also look to the agreed-upon intensive expert and high-level discussions to ensure that foreign firms in China have equal access in any new innovation measures or product lists. We hope this engagement will include input and participation from the private as well as the public sector. Given China's commitments at the time of its WTO accession, we also look for China to step up the process of negotiation and accession to the WTO's Government Procurement Agreement. China's revised offer, due shortly, needs to include participation by sub-federal and state-owned enterprises (SOEs).

Conclusion

I appreciate the opportunity to appear before the commission today and look forward to an ongoing dialogue with Commission staff working on these important reports for the Senate Finance Committee. Please let us know how we at the NAM can assist further in your important effort. I would be pleased to try to any questions you might have.