



## **United States International Trade Commission Hearing:**

China: Intellectual Property Infringement, Indigenous  
Innovation Policies, and Frameworks for Measuring the  
Effects on the U.S. Economy

and

China: Effects of Intellectual Property Infringement and  
Indigenous Innovation Policies on the U.S. Economy

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Chairman Aranoff and members of the Commission, thank you for holding this hearing today and allowing me to testify.

*Please note that my testimony today reflects my own personal views and do not necessarily reflect the positions or views of my firm or our clients.*

From May 2005 to March 2008 I had the privilege of serving as the first U.S. Coordinator for International Intellectual Property Enforcement. My mission was to coordinate and leverage all of the resources of the U.S. federal government to protect American IP at home and abroad. Nowhere was this challenge greater than when addressing China.

Today, I hope to provide the Commission with constructive insight on two areas:

1. First, what is the policy framework for engaging China on IP matters – in other words, what is in the toolkit for the U.S. government as it tackles this problem?
2. Are these tools sufficient to address rising concerns regarding lax Chinese IP enforcement and indigenous innovation policies?

### **The Policy Framework**

To make any effective strategic decisions, I believe it is important to first assess and appropriately characterize the tools at your disposal. While some may differ, I'm convinced there is no silver bullet to the challenges posed by China. Rampant piracy and counterfeiting continue to plague U.S. industries ranging from entertainment and software to pharmaceuticals and auto parts. Criminal enforcement for IP theft is nearly non-existent in China and civil enforcement is time-consuming, expensive and unpredictable. IP theft in China is increasingly a health, safety and security matter. And adding to the complexity, China and the U.S. frequently square off in diplomatic arenas to espouse very different views regarding IP policy and enforcement.

So, while U.S. officials try to crack down on fake golf clubs and apparel in Silk Alley, support industry efforts to address online piracy, address local protectionism in provincial courts, dispute provisions in the new indigenous innovation policy, and seize fake Nikes arriving from China at the Port of Long Beach, they are also confronting Chinese diplomats in Geneva who are attacking initiatives such as the U.S.-led Anti-Counterfeiting Trade Agreement.

However, the U.S. also works in constructive ways with China. The U.S. Patent and Trademark Office and China's State Intellectual Property Office have engaged in a number of collaborative training and work-sharing programs, including an MOU signed in May to extend bilateral cooperation on patents.

In addition, U.S. law enforcement and their Chinese counterparts have worked on a number of major joint criminal prosecutions in recent years.

To encourage China to improve its IP system and strengthen its enforcement a complex continuum of policies, programs, events, agencies, organizations and other entities must all be understood and maximized. Clearly, this is a frustrating approach that challenges CEOs, Government Agencies and Cabinet officials alike. This complexity is clearly not lost on the Chinese either, who are expert at prolonging discussions, providing confusing and misleading information and making just enough progress to stave off major actions.

### **The U.S. Policy Toolkit**

So with this as a backdrop, here is an overview and analysis of some of the specific tools the U.S. government has developed to engage with China:

First, there are a range of **significant bilateral fora** such as the U.S.-China Joint Commission on Commerce and Trade (JCCT) and the more recently developed U.S.-China Strategic and Economic Dialogue (S&ED). These processes involve Cabinet-level officials and have occasionally proven effective at securing broad IP-related commitments from the Chinese government. This level of engagement is useful and necessary for several reasons. First, by establishing specific commitments and meeting with Chinese counterparts on a regular basis, it is possible to at least attempt to measure progress on tangible things such as changes to Chinese law, establishment of law enforcement mechanisms for U.S. rights holders, increased criminal prosecutions and legalization of software. These processes also lead to a better understanding of the details and objectives driving Chinese policy. Lastly, these fora often get senior Chinese officials “on the record” speaking about the importance of IP protection and enforcement. This can have a positive ripple effect across their government especially when attempting to work throughout the many Chinese provinces.

Despite some progress over the years, it has become increasingly clear that these efforts must also begin to take on a much more comprehensive and strategic role in addressing the systemic competitive challenges that China presents. The Chinese indigenous innovation policy, for example, clearly fits within the context of the S&ED as it is both “strategic” and “economic”. It is a wide-ranging set of industrial policies that forces the U.S. to address issues ranging from IP to standards and government procurement. The impact and severity of these policies are clear, and in recent weeks senior U.S. officials including Secretary Geithner, U.S. Trade Representative Ron Kirk and Deputy Secretary of State James Steinberg have all raised concerns with the Chinese.

A second area of focus must be the **effective use of all of our trade tools**. The U.S. Trade Representative’s Office conducted a China Top-to-Bottom Review in 2005 and today USTR’s Special 301 Report obviously remains a major tool in identifying our the key IP concerns in China.

In April, 2006 the U.S. filed the first IP-related case against China at the World Trade Organization. Last year, the WTO largely sided with the U.S. on two of its key complaints [finding that several aspects of China's legal regime for protecting and enforcing intellectual property rights are inconsistent with China's obligations under the WTO Agreement on Trade-Related Aspects of

Intellectual Property Rights (TRIPS Agreement) and that China's restrictions on the importation and distribution of copyright-intensive products run afoul of WTO rules].

China joined the WTO voluntarily and has benefitted greatly from its membership. We must remain committed to ensuring that they abide by the rules and take the necessary steps when they don't. In addition, it is obviously important to continue to pressure China to join the WTO's Government Procurement Agreement to promote openness and competition within China's \$82 billion government procurement market.

Next, it is crucial that the U.S. continue to **stress the importance of law enforcement and customs cooperation** with China. Piracy and counterfeiting are major economic threats to the U.S. and are increasingly perpetrated by organized and sophisticated criminal organizations.

The U.S. – China Joint Liaison Group, led by DOJ and the Chinese Ministry of Public Security, allows for extensive collaboration and has resulted in a number of large criminal enforcement operations against organized piracy and counterfeiting in China.

In terms of strengthening and expanding the efforts of U.S. law enforcement, the National IPR Coordination Center led by U.S. Immigration and Customs Enforcement is also a tremendous resource. The IPR Center has the ability to coordinate all law enforcement functions and works extensively with experts in the U.S. private sector.

### **The Effectiveness of U.S. Efforts**

Are these tools sufficient to address rising concerns regarding lax Chinese IP enforcement and indigenous innovation policies?

While the U.S. has made some progress with China by working bilaterally, attempting to enforce trade rules and attacking criminal organizations, it is clear that we are probably treading water at best. It is common to hear China experts say that, "China will protect IP when it's in their interests to do so." This raises the obvious questions of, what can we do to speed the arrival of that day, and what will it mean for the U.S. when it arrives?

China seems to be in a period of trial and error when it comes to policies to protect IP and promote innovation, however its current indigenous innovation policies provide an initial view of their intention - to leverage a number of policy tools to meet the goal of innovation-led economic growth through Chinese national champions.

Over the long term, it seems clear that the U.S. needs to take a more holistic approach to address threats posed by China's IP and innovation policies. There needs to be a process to clearly prioritize the issues that the U.S. government is going to address and determine how it can uniquely impact them. We need to develop a consistent and standardized process through which key government agencies work with U.S. industry to determine our most critical IP and innovation

policy concerns and then establish strategies to address them. These strategies would include a mix of bilateral engagement, use of trade tools, law enforcement work and private sector action among other things. Congress and the Administration must also do a better job of coordinating. The Chinese are quite disciplined and always speak with one voice. We often lack the type of focus and single-mindedness that is necessary.

Too often it seems, engagements with the Chinese happen in isolation and are driven on the U.S. side by the need for short term "deliverables". This is understandable and it is to some extent an indication of the difference between U.S. and Chinese approaches. U.S. officials tend to seek specific commitments that can be measured over time, and that open the Chinese market. The Chinese are focused on buying time and nurturing domestic industries. For example, the 2005 commitment by China to complete its software legalization program was lauded in the U.S. but has had little impact. As Robert Holleyman, President of the Business Software Alliance recently stated in the Wall Street Journal, "79% of all software used in (China) is illegally copied, and this costs U.S. software makers \$7.6 billion annually."

We often lack the patience, persistence and penchant for industrial policy to match the Chinese in terms of setting long term goals that benefit our economic interests and leading industries. But China lacks (for now) the ability to create true paradigm-changing innovations and its inability to tolerate creative destruction is a competitive advantage for us. We must, however, develop mechanisms to leverage all the policy and enforcement tools at our disposal that will endure through changing Administrations and political pressures.

I appreciate the opportunity to participate in this important set of hearings and I look forward to your questions.