AUTHENTICATED
U.S. GOVERNMENT
INFORMATION
GPO

DOES CHINA ENACT BARRIERS TO FAIR TRADE?

JOINT HEARING

BEFORE THE

SUBCOMMITTEE ON RURAL ENTERPRISES, AGRICULTURE AND TECHNOLOGY AND THE SUBCOMMITTEE ON TAX, FINANCE AND EXPORTS

OF THE

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

ONE HUNDRED NINTH CONGRESS

FIRST SESSION

WASHINGTON, DC, MAY 26, 2005

Serial No. 109–18

Printed for the use of the Committee on Small Business

Available via the World Wide Web: http://www.access.gpo.gov/congress/house

U.S. GOVERNMENT PRINTING OFFICE

22–205 PDF WASHINGTON : 2005

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2250 Mail: Stop SSOP, Washington, DC 20402–0001

COMMITTEE ON SMALL BUSINESS

DONALD A. MANZULLO, Illinois, *Chairman*

ROSCOE BARTLETT, Maryland, *Vice Chairman*
SUE KELLY, New York
STEVE CHABOT, Ohio
SAM GRAVES, Missouri
TODD AKIN, Missouri
BILL SHUSTER, Pennsylvania
MARILYN MUSGRAVE, Colorado
JEB BRADLEY, New Hampshire
STEVE KING, Iowa
THADDEUS McCOTTER, Michigan
RIC KELLER, Florida
TED POE, Texas
MICHAEL SODREL, Indiana
JEFF FORTENBERRY, Nebraska
MICHAEL FITZPATRICK, Pennsylvania
LYNN WESTMORELAND, Georgia
LOUIE GOHMERT, Texas

NYDIA VELÁZQUEZ, New York
JUANITA MILLENDER-McDONALD, California
TOM UDALL, New Mexico
DANIEL LIPINSKI, Illinois
ENI FALEOMAVAEGA, American Samoa
DONNA CHRISTENSEN, Virgin Islands
DANNY DAVIS, Illinois
ED CASE, Hawaii
MADELEINE BORDALLO, Guam
RAÚL GRIJALVA, Arizona
MICHAEL MICHAUD, Maine
LINDA SÁNCHEZ, California
JOHN BARROW, Georgia
MELISSA BEAN, Illinois
GWEN MOORE, Wisconsin

J. MATTHEW SZYMANSKI, *Chief of Staff*
PHIL ESKELAND, *Deputy Chief of Staff/Policy Director*
MICHAEL DAY, *Minority Staff Director*

SUBCOMMITTEE ON RURAL ENTERPRISES, AGRICULTURE AND TECHNOLOGY

SAM GRAVES, Missouri, *Chairman*
STEVE KING, Iowa
ROSCOE BARTLETT, Maryland
MICHAEL SODREL, Indiana
JEFF FORTENBERRY, Nebraska
MARILYN MUSGRAVE, Colorado

JOHN BARROW, Georgia
TOM UDALL, New Mexico
MICHAEL MICHAUD, Maine
ED CASE, Hawaii
RAÚL GRIJALVA, Arizona

PIPER LARGENT, *Professional Staff*

SUBCOMMITTEE ON TAX, FINANCE AND EXPORTS

JEB BRADLEY, New Hampshire *Chairman*
SUE KELLY, New York
STEVE CHABOT, Ohio
THADDEUS McCOTTER, MICHIGAN
RIC KELLER, Florida
TED POE, Texas
JEFF FORTENBERRY, Nebraska
MICHAEL FITZPATRICK, Pennsylvania

JUANITA MILLENDER-McDONALD, CALIFORNIA
DANIEL LIPINSKI, Illinois
ENI F. H. FALEOMAVAEGA, American Samoa
DANNY DAVIS, Illinois
ED CASE, Hawaii
MICHAEL MICHAUD, Maine
MELISSA BEAN, Illinois

JOE HARTZ, *Professional Staff*

CONTENTS

WITNESSES

	Page
Pinkos, Mr. Steve, Office of the Undersecretary and Director, US Patent and Trade Office	7
Goodpasture, Mr. Tom, Pride Manufacturing Co., Inc.	17
Iglauer, Mr. Bruce, President and CEO, Alligator Records	19
Lubrano, Mr. Al, President, Technical Materials, Inc.	21
Blackburn, Mr. Dave, Thomas G. Faria Corporation	23
Stallings, Mr. Thomas, Funston Gin Company, Funston Warehouse	27

APPENDIX

Opening statements:	
Graves, Hon. Sam	41
Bradley, Hon. Jeb	43
Barrow, Hon. John	45
Prepared statements:	
Pinkos, Mr. Steve, Office of the Undersecretary and Director, US Patent and Trade Office	49
Goodpasture, Mr. Tom, Pride Manufacturing Co., Inc.	63
Iglauer, Mr. Bruce, President and CEO, Alligator Records	67
Lubrano, Mr. Al, President, Technical Materials, Inc.	71
Blackburn, Mr. Dave, Thomas G. Faria Corporation	83
Stallings, Mr. Thomas, Funston Gin Company, Funston Warehouse	88
Additional Material:	
Discussion of Intellectual Property Theft, Congresswoman Marsha Blackburn (TN-7), Nashville, TN	100

DOES CHINA ENACT BARRIERS TO FAIR TRADE?

THURSDAY, MAY 26, 2005

HOUSE OF REPRESENTATIVES
SUBCOMMITTEE ON RURAL ENTERPRISES, AGRICULTURE AND TECHNOLOGY JOINT HEARING WITH SUBCOMMITTEE ON TAX, FINANCE AND EXPORTS
COMMITTEE ON SMALL BUSINESS
Washington, DC

The Subcommittees met, pursuant to call, at 10:05 a.m. in Room 2360, Rayburn House Office Building, Hon. Sam Graves, Chair, Subcommittee on Rural Enterprises, Agriculture and Technology, presiding.

Present: Representatives Graves, Manzullo, Bradley, Barrow, Udall, Sodrel, Poe, Fortenberry, Udall, Lipinski

Chairman GRAVES. Good morning, everyone. I would like to welcome you to the joint Rural Enterprises, Agriculture and Technology Subcommittee and the Tax, Finance and Exports Subcommittee hearing. It is my pleasure to hold this hearing with Chairman Bradley, and we are going to explore trade barriers with China.

Trade with China has grown faster than any other U.S. trading partner. Currently China is our third-largest trading partner, the second-largest source of U.S. imports, and the fifth-largest U.S. export market. The growth of the Chinese economy, in particular, their exports to the United States, has reached record levels and has created a trade deficit for the United States topping $162 billion in 2004.

There are several reasons for the discrepancies. First, since 1994, the Chinese government has kept its currency pegged at 8.2 yuan to the dollar. While in recent years, the dollar has weakened, the yuan has remained the same against our currency. Many economists estimate the yuan is undervalued by as much as 40 percent, which means Chinese manufactured goods are 40 percent cheaper than our competitors'. Just last week, the U.S. Department of Treasury issued a report on the state of global currencies and called China's currency peg "highly distortionary."

China has experienced economic growth, gains in productivity, a large export sector, and increased foreign investment. Their currency manipulation gives their manufacturers an advantage and creates an enormous disadvantage to ours. It is about time they

stopped cheating and started playing by the same rules that we have to play by.

Second, theft of intellectual property rights is another significant problem that U.S. companies must take into account when dealing with China. It is estimated that counterfeits constitute between 15 to 20 percent of all products made in China and account for about 8 percent of China's GDP. It is also estimated that U.S. companies lose $25 billion annually to copyright violations. While many people believe that the problem is restricted to things like CDs, purses and Polo shirts, it is only the tip of the iceberg.

Many people believe that it is a victimless crime, but, unfortunately, Chinese counterfeiters or pirated items can impact our safety. For example, in 2000, the New York Times reported that Southwest Airlines discovered that counterfeit cables had been installed in 47 of its planes. These cables are used to connect cockpit controls to the engines, the landing gear to control surfaces. One of Southwest Airlines' suppliers had obviously bought counterfeit parts.

Over the last two decades, the U.S. has pressed China to improve its protection of Intellectual Property Rights. While China has passed new laws that provide protection of Intellectual Property Rights, it has done little to enforce these laws, allowing for rampant piracy and counterfeiting. China has got to crack down and be an active part of the solution.

And, finally, while the Chinese have some laws that protect its workers and protect the environment, few are ever enforced. U.S. companies are held to some of the highest standards in the world, and these standards are noticeably absent in China. Chinese companies just do not have to comply with things like OSHA or the EPA. We need to ensure that U.S. firms compete on a level playing field and the global market not be at a competitive disadvantage. These unfair barriers not only affect our economy but also job growth, and much of it is fueled by small business in this country.

Again, I want to thank all of the witnesses that are going to participate today, and I look forward to hearing everybody's statements.

[Chairman Graves' opening statement may be found in the appendix.]

Chairman GRAVES. Ranking Member Barrow. Do you want to give your opening statement?

Mr. BARROW. Thank you, Mr. Chairman.

For many generations, my family has farmed all over eastern and southeastern Georgia, and I learned very early on to appreciate the hard work and sacrifice of our family farmers. Not only is farming an industry with tremendous challenges; it is also an industry that impacts the entire world. Our farmers face the pressures of supplying the world with food and clothing, and this is no easy task. The policies enacted by Congress, as well as by foreign governments, have a major impact on our family farmers. Recognizing this, I would like to thank Chairman Graves and Chairman Bradley for holding this hearing to examine China's impact on fair trade.

I have asked a fellow Georgian to come join us today to talk about the cotton industry in Georgia and nationwide and how China's trade policies are affecting this industry. Mr. Stallings, Tom Stallings, is a cotton producer from Funston, Georgia, and I thank him for taking the trip up here and participating in this hearing.

The ever-increasing number of imports and exports crossing our borders illustrates the importance of the international trade market, particularly in the U.S. In fact, the global economy has grown so much that 80 percent of world economic consumption takes place outside of this country. In today's global market, it is that much more important that our family farmers compete on a level playing field.

Much of this country's success in the world market depends on small businesses and agriculture. Today, 90 percent of exporters are small businesses, and they make up over 50 percent of our nation's GDP. This includes many of our family farms. While access to overseas markets is important to our economy, we need to examine the impact that trade policy has on small business exporters in this country.

China is our third-largest trading partner. We are China's largest overseas market, and China's exports represent 13 percent of U.S. imports. U.S. exports to China have been growing rapidly, but competition from China is one of the biggest threats facing the small business sector of the American economy. Meanwhile, while U.S. exports are increasing, the numbers do not add up. In 2004, the U.S. ran a trade deficit of $162 billion with China, our largest trade deficit with any other country. These figures spell trouble for our trade relationship with China where we sustain a huge imbalance between what U.S. exporters send and what U.S. imports receive in return.

My home state of Georgia plays an integral role in U.S. exports. Georgia exported $16.3 billion in goods in 2003, with agriculture accounting for more than $963 million in sales abroad. Cotton plays a big role in these figures. Cotton is Georgia's top agricultural export, and it is an industry with a unique relationship with China.

Today's hearing will provide us with an opportunity to learn more about the unfair factors influencing U.S.-China trade relations and to examine the intricate relationship that U.S. industries have with China. Specifically, we will hear testimony on unfair trading practices associated with currency manipulation, intellectual property piracy, and a lack of compliance with labor standards and other regulations.

When it comes to setting currency regulations, China is not playing fair. This manipulation makes Chinese exports to the U.S. cheaper and U.S. exports to China more expensive.

When it comes to honoring or defending our property rights, China is not playing fair. Piracy and counterfeiting practices in China are costing U.S. firms billions of dollars in lost sales.

And, finally, when it comes to respecting honest and adequate labor and environmental standards, China is not playing fair. The production of more goods at lower costs should not be done at the expense of public safety, environmental standards, or the rights of workers.

This is the case, and these are the facts, and unless China starts playing by the same rules, rules that they agreed to when they joined the WTO, Chinese exporters will continue to have an enormous advantage over U.S. firms. In the global marketplace, we have got to stand up for American interests. Standing by while small businesses, family farms, and American workers lose out is just not an option. Thank you, Mr. Chairman.

[Ranking Member Barrow's opening statement may be found in the appendix.]

Chairman GRAVES. Next, we are going to hear from Chairman Manzullo, who is Chairman of the full Committee on Small Business. I am very pleased to have the chairman here. He has been very active in trade issues with China and, obviously, represents a very important manufacturing area in the United States.

Thank you for being here.

Mr. MANZULLO. Thank you, Chairmen Graves and Bradley for holding a hearing on this very timely topic. The simple answer to the question, "Does China Enact Barriers to Fair Trade?" I guess, to free and fair trade, the answer is, obviously, yes.

The most recent, monthly, merchandise-trade-deficit statistic with China was $14 billion. We are on a pace this year to eclipse the already massive $162 billion trade deficit from 2004 with China. Many of the challenges to the U.S.-China economic relationship are the same ones that were discussed several years ago, with little progress in sight while our manufacturing and agricultural base hemorrhaged. Last week, the Federal Reserve issued a depressing industrial production report showing a .2 percent decline in April led by motor vehicle manufacturing. The Commerce Department reported yesterday that durable goods orders were up last month but still remained at the same level at the start of the year. While we gained 274,000 jobs last month, we lost 6,000 jobs in the manufacturing sector.

What will it take for this town to recognize that there is a crisis in manufacturing? It seems every month there is another major, U.S. multinational company that announces it will open a leading-edge, global research and development center in China. Just last month, two major U.S. car makers announced that they plan to export vehicles manufactured in China to the U.S. and Europe. To compound that, China is manufacturing the Khiri, they expect to send one million of those to this country each year. That is about one-twentieth, or 5 percent, of all of the cars sold in this country, and GM is involved in a massive lawsuit with Khiri over pirating.

We need to make sure that China plays by the rules of free and fair trade. We can do this by, one, allowing all of our trade laws to apply to nonmarket economies like China. Currently no company can file a countervailing duty trade against China. Market-driven companies in the U.S. cannot compete against state-owned enterprises in China. Passage of Representative Ingrich's H.R. 1216 can go a long way towards rectifying this problem.

Two, let us require China to live up to its prominent, global economic role by letting the markets, not governments, determine the value of their currency. The U.S. Department of Treasury must

find what is obvious to everybody, that China manipulates its currency every day in order to maintain its tight peg to the U.S. dollar. The level has not been changed since 1994, and China is long due for a correction in its currency value to reflect its global economic prowess.

Passage of H.R. 1498, to allow countervailing duty trade cases against companies in countries that manipulate their currency can help in this effort. Also, passage of my legislation, H.R. 2208, would give Treasury the legal room necessary to take action against countries that manipulate their currency like China, which have a large trade surplus with the U.S. but not with the rest of the world.

The reason the U.S. Treasury has not cited China for manipulating the currency is that under the present rules of doing so, you have to show a trade imbalance, both bilaterally and on a multinational basis, and as to the latter, China is not there, although we question the methods that they used to come up with their own figures. H.R. 2208 would change the metrics and make it a lot easier to show that China is manipulating its currency and thus be able to take actions against that country.

Three, we have to continue to fight the Intellectual Property Right piracy in China. As the Chairman of the American-Chinese Interparliamentary Exchange, I have been to China several times, Macau on two of those trips, and it is absolutely rampant what is going on there with the pirating of the CDs and other things. Piracy costs U.S. exporters billions in lost sales. The Administration's Stop program and elevating China to the Priority Watch List are good steps, but, obviously, more needs to be done. Passage into law of H.R. 32, which would crack down on those who traffick in counterfeit goods and services would also help.

The U.S. Trade Representative initiated a WTO case against China on Intellectual Property Rights enforcement, if progress is not made shortly, should also be strongly considered. Mr. Chairman, thank you again for holding this timely hearing.

Chairman GRAVES. Thank you, Mr. Chairman. We are now going to hear from Jim Bradley. Chairman Bradley, I appreciate you working with us on this joint hearing, and I look forward to hearing your statement.

Mr. BRADLEY. Thank you very much, Mr. Chairman. It is a pleasure to be here. Good morning to everyone. I appreciate your joining us here today.

I am also very appreciative of the gentleman from Missouri, Chairman Graves, for conducting this hearing, and I look forward to working on these issues as we move forward.

As all of you know, over the last two decades, China has emerged as a strong international competitor in a wide range of products and has proven to be a critical market for U.S. exports. China's emergence as a leading world economy has provided significant new opportunities for American exporters, and U.S. exports to China have risen sharply in recent years. That rapid growth has raised China from the tenth-largest U.S. export market in 1997 to the fifth-largest today. In fact, between 2000 and 2004, exports to

China accounted for half of the increase in the total U.S. exports worldwide, an increase of $18.5 billion.

Unfortunately, there has been a down side to the unprecedented growth in China's economy as well. The deficit for trading goods with China stands at about $176 billion, having increased rapidly in recent years. It is now the single-largest, bilateral deficit our country has. We are asking ourselves in these hearings and others, what has caused this deficit?

There are numerous trade irregularities that exist between our nations, and this hearing is going to focus on three of them: China's undervalued monetary system, the lack of intellectual property protection and enforcement in China, and the lack of enforcement of Chinese regulations to protect workers' rights and the environment.

In 1994, China devalued its currency by roughly 30 percent and has maintained that value to this date, despite increases in production capability, productivity, quality, foreign direct investment, and other factors that would normally be expected to cause a currency to appreciate. This undervaluation effectively increases the cost of U.S. exports to China and lowers the cost of Chinese exports to America, which only exacerbates the growing bilateral trade deficit between our two nations.

Turning to intellectual property, IP protection is another area of concern for U.S. exporters to China. According to the U.S. Patent and Trademark Office, China is the largest single source of seizures of infringing products by U.S. Customs, roughly 62.5 million, or 66 percent of the total goods seized in Fiscal Year 2003. While some progress has undoubtedly been made between our two nations in this regard, these new mechanisms are not being rigorously enforced by the Chinese officials, leading some industry analysts to estimate that IP counterfeiting and piracy in China costs U.S. copyright firms $2.5 billion in lost sales in 2004.

That is why we are having a hearing today, Mr. Chairman, and I appreciate your leadership on this and look forward to continuing to work with you.

[Chairman Bradley's opening statement may be found in the appendix.]

Chairman GRAVES. Thank you, Mr. Chairman. Any other statements?

Mr. SODREL. A short statement. I think, in the opening statements, and I would also like to thank Chairman Graves, Chairman Bradley, and Chairman Manzullo for having the hearing, the case has been stated very well in terms of statistics and problem, but just as some anecdotal stories, the Ninth District of Indiana depends heavily on manufacturing and agriculture, and those are two ways our folks make a living. Keller Manufacturing in Cordon, Indiana, had 1,000 employees six years ago; they have 50 today. We have experienced, both with small machine shops, tool and die shops, manufacturers all over the Ninth District have found their employment curtailed because of Chinese trade and unfair practices in China.

So it is a really serious issue in southern Indiana, and I think we need to take appropriate action. Thank you for the opportunity to be here today this morning.

Chairman GRAVES. Thank you.

Mr. POE. Thank you, Mr. Chairman. Thank you very much. I appreciate this hearing being held. As a former judge in Texas for over 20 years, I believe strongly that people who cheat and steal should have consequences for that conduct. It is obvious we know the problem,—the Chinese are harboring pirates and cheats and thieves—and I hope we can find some solutions as to what the United States is going to do about it because of the consequences here in the United States to American workers, but also there should be consequences abroad for stealing, cheating, and pirating. Thank you, Mr. Chairman.

Chairman GRAVES. Thank you very much.

Mr. UDALL. Thank you, Chairman Graves, and I appreciate you holding this hearing today. Many of the opening statements, I think, covered very well the topics we are going to address today, and I would agree with all of those statements.

The only thing I would like to add is that I do not think that when we deal with China, we have a level playing field, and you can look at a number of areas. The trade deficit has been mentioned. Low wage workers are an area where there is absolutely no doubt, we do not have a level playing field. There are no labor standards. In many cases, with these recent exposes, we have seen child labor used specifically to produce their products and thus lower the prices, and that is something I do not think we can tolerate.

In addition, the human rights situation, I think, is deplorable. We are talking about these large education camps, people that cannot practice their religion, and there is really, in many cases, no rule of law, it seems to me, in terms of people's rights and their ability to be treated fairly in a legal system.

So with that, I look forward to the hearing and look forward to hearing from our witnesses.

Chairman GRAVES. Thank you very much.

We have two panels today, and, obviously, all of the statements made by the Members on the Committee and the panelists will be placed in the record in their entirety.

Our first panel is Steve Pinkos. He is with the Office of the Under Secretary and Director with the U.S. Patent and Trade Office, and we are looking forward to hearing. We actually had someone from your office in our district talking about some of the patent infringements that have taken place, and it is extremely interesting, and I look forward to hearing your testimony.

STATEMENT OF STEPHEN M. PINKOS, U.S. PATENT AND TRADEMARK OFFICE

Mr. PINKOS. Thank you very much, Mr. Chairman. Thank you, Chairman Graves, Chairman Bradley, Chairman Manzullo, Ranking Member Barrow, other members of the Subcommittees. I appreciate the opportunity to come join you all today in a discussion on some of the issues that we are facing in China. My alleged area of expertise is intellectual property. That is what we handle at the U.S. Patent and Trademark Office. It is the one executive branch agency that solely focuses on intellectual property. Currency, agriculture, textiles, labor issues are not necessarily my bailiwick, but I would be happy to entertain what questions I could, but I will focus my testimony on the intellectual property situation in China.

The Bush administration and Secretary Gutierrez fully understand that intellectual property is critical to the competitiveness of our economy and that U.S. industries, both large and small, face enormous challenges in protecting their intellectual property overseas, particularly in China, and we know that U.S. businesses, as it has been alluded to, lose billions of dollars per year from IP theft abroad.

An effective intellectual property framework requires not only effective laws on the books but effective enforcement and administration of those laws, and we have seen some progress in China and other countries in putting the laws on the books that may be required by the WTO obligations, but the administration and enforcement of those laws is often sorely lacking or deficient, China being the prime example.

There, again, as it has been alluded to, the problems run the gamut, from piracy of movies and software, devastating those industries in China, and the music industry to counterfeiting of all types of consumer goods, electrical equipment, pharmaceuticals, and, as Chairman Manzullo said, even a whole car.

We know there is a huge counterfeiting problem in a country when a company is willing to make the investment in a production line for a counterfeit good, knowing that there are probably no implications from their own government.

That is a huge concern, and there are safety concerns that go along with that: exploding electronic devices, pharmaceuticals that do not have the active ingredients so your mother or father or mine could be taking blood pressure medicine for several months that has none of the intended effect.

So there is a whole range of issues that are of concern to, I know, you all and, of course, the Bush administration. We have made dealing with U.S. IPR problems a top priority, and I just want to go through a few of the things that we are working on. Much of it is covered in the written testimony, if you have a chance to look at that, and I would be happy to entertain some questions.

One thing that is going on this week is there is a U.S.-China Joint Commission on Commerce and Trade that has been set up, and there is an IP working group that is co-chaired by John Dudas, the Under Secretary of Commerce for Intellectual Property and Director of the US PTO, and Josette Shiner from the USTR's office. They are meeting with Chinese counterparts this week and pressing them very hard to implement an IPR action plan to address some specific problems.

Part of the equation is that companies need to protect their rights in China. They need to actively go and get patents and protect their trademarks there because there is no such thing as an international patent or an international trademark, so they do have to seek protection in the individual countries. Obviously, we have 4,000 patent examiners and over 300 trademark examiners, so we have developed a lot of expertise in that area. So we are working with their administrative offices to improve their systems so when American companies do go there to try to protect their rights, there is an adequate system in place.

So we are spending a lot of time training there, and we are training on enforcement issues as well. That is, as was touched upon earlier, a big part of the equation. So we run programs throughout China, not just in Beijing but the other provinces, training judges and prosecutors and legislators and administrative officials on how to enforce intellectual property laws and also the general value of intellectual property and how eventually it will be helpful to their economy, and in the long term, cheating, stealing, and pirating is not the way to develop an economy.

Many of you may have traveled to China and know a lot of the small business community staff has been there. We have placed an IPR attache in the embassy there that has really reaped some good benefits. It is a unique position that we have established with the State Department. All he does, Mark Cohen, is focus on IPR issues, so he is really building a strong relationship not only with the U.S. businesses there but also with the Chinese government and trying to make some inroads there.

It is interesting that the Chinese have taken some steps. They have a massive public-interest campaign. They prosecute people now and then. Some of the counterfeiting sales has gone underground, but there is no question. All you have to do is go there or see some of the products coming into the United States in the huge amount of seizures that Customs is making to know that the problem is continuing.

I see that my time is expiring, so having worked for Chairman Sensenbrenner for several years and Mr. Hyde on the Hill, I have deep respect for the red light. I would be happy to take your questions and just emphasize that we are committed, the Bush administration, the USPTO, Commerce Secretary Gutierrez, to working closely with the administration,—like-minded trading partners around the world is a big factor in the equation—and working with Congress to continue to address this problem. I am increasingly optimistic that we are making some progress, but we have got to push more on some other levers to hopefully see real results.

[Mr. Pinkos' statement may be found in the appendix.]

Chairman GRAVES. You mentioned making progress, obviously. Can you tell us what areas? Are we seeing real progress, or is it superficial?

Mr. PINKOS. It is sporadic, and it is not sustained. For example, we help the Chinese to have more effective laws on the books, including copyright Internet laws, but then we see mild enforcement

or not pervasive enforcement, and it does not bleed down to the provincial level necessarily.

The U.S. government has a complex bureaucracy. Well, they have taken it to new heights there. So a lot of times, we do not even know the best people to deal with. But we have made progress in getting some better laws on the books. We have made some progress in pressing some particular cases. For example, the Chinese were not adopting the trademark principle of a widely recognized trademark, like Coca-Cola or Nike, that it is written into general trademark law that they should receive recognition without having to file the particular paperwork. We have pressed them on that and seen some results.

So, case by case, little by little, we are seeing a little bit of results, but, again, no question that there is still a huge problem.

Chairman GRAVES. Let me ask you this. What can U.S. businesses do to protect themselves, other than revealing what their latest-and-greatest product is? It is obviously easy to obtain that. What can they do?

Mr. PINKOS. Well, first of all, they do need to take the step of actually filing for a patent or filing a trademark application because you do not have the protection otherwise, at least within China. You may have it in the United States if they try to export it here.

You have to take that first step, and we are really trying to do a lot to educate especially small businesses, because the big multinationals, they have their teams of lawyers, and they know what they need to do. But we are reaching out specifically to small- and medium-sized businesses. We have a public awareness campaign that we are launching in June. We are going to have an event here in D.C. that we would love for you all to attend. We will get the information to your staffs.

But we are also going around the country doing small business seminars. We had our first one this week in Utah where over 200 small businesses were represented, and we talked to them about the international landscape, what is out there. You may have your product, and you are selling it just in the Western Hemisphere, but it may be something that is easily copied and will be manufactured in China and tried to be exported back to Central America or something. So we educate them about what may happen to them and what steps they need to protect their intellectual property.

Chairman GRAVES. Mr. Barrow?

Mr. BARROW. Thank you, Mr. Pinkos. I appreciate your being here today. I want to ask you some questions that come at this from the small business perspective, and then I want to ask you a couple of broader questions.

First of all, you mentioned the fact that seminars are being held around the country to try and emote an awareness on the part of the small business community as to the assistance available. What efforts are being made to make sure that the small business com-

munity is even aware of these outreach programs? How are you all reaching out to the small business community?

Mr. PINKOS. Part of the program that we are going to launch in June is we are trying the target publications that small businesses often rely on. We are going to do some Internet advertising. We will probably do some paid media advertising and target other sorts of small business conventions and things like that that are occurring in small businesses.

They participate in local chambers of commerce, reaching out and trying the partner with the NFIB to get out the message that we do have resources to help, that we have an 800 number they can call and talk to an attorney for some advice. The government attorney cannot give them the real legal advice like a regular attorney can, but they can reach out to our office through that and through a new Web site the U.S. government has established called stopfakes.gov.

Mr. BARROW. What you just said touches on a point that you made before, and that is, to contrast the resources that are available to giant corporations that are able to put up a fight in their own defense, and that just only brings to mind the obvious problem that small businesses have. It is one thing to advise small business as to how to acquire the rights that they own in their property; it is another to provide a remedy for them. And basically tell folks how they can go about getting a patent and what they need to be able to do in order to be able to, first, secure their rights on their property is not really doing anything. A right without a remedy is worthless.

What really is it going to take for this culture of compliance and respect for foreign property rights really to bleed down, to use your phrase, in the Chinese economy? What is it going to take? You mentioned that the progress we are making is inch by inch, and little by little, we are getting there, but what is it really going to take for us to create a climate or a culture of acceptance of the rights of foreign intellectual property in the Chinese economy?

Mr. PINKOS. Ultimately, it will take a recognition by the Chinese that it is beneficial to their interests, and that can come about in several ways: one, through their own economic development. Chinese innovators are starting to feel the pain themselves in the sense that they are developing a product, they are investing the money in it, and somebody in another province—they are equal-opportunity counterfeiters. They do not just counterfeit American products or European products, so that is part of the equation.

Ultimately, also, I think that world pressure on the Chinese not just from the United States because they certainly have other markets they can turn to. It is not just Boeing; there is Airbus. There are plenty of competitors, so I think it is going to take a sustained world effort to convince them that it is not in their best interest, and there are mechanisms through the WTO and other sort of international fora to try to accomplish that.

Mr. BARROW. Well, I hear what you are saying, but stamping out counterfeiting at home in the domestic market does not do us any good if counterfeiting persists with respect to the intellectual property rights of foreign intellectual property owners. If you stop the counterfeiting of Chinese intellectual property in the Chinese economy, you have not done anything to protect the rights of American intellectual property in the Chinese economy.

That is one concern I would have, but, secondly, what is the world pressure going to have to look like? What form is it going to have to take in order to be able to produce the effect that we all think we are entitled to?

Mr. PINKOS. One, I think it has to take just a unified perspective, in the sense that we have to be on the same page, and other countries do not have to be looking for their own little economic angle and try to curry favor, so to speak, with the Chinese. Ultimately, I think that it may be something that is examined or played out in the World Trade Organization.

Mr. BARROW. Can you expand on your answer?

Mr. PINKOS. Well, China is a member of the World Trade Organization. They have obligations, including enforcement of intellectual property laws, and no one has ever brought a case in the World Trade Organization on an enforcement. Usually, it is that you do not have laws on the books that comport with WTO obligations, or you pass something that conflicts with WTO obligations, so it is sort of a new, novel approach, but the obligations are there on the books. I think the administration, at this point, is assessing fully what we are doing in China, what is working, what is not working, and what other avenues we have to address.

Mr. BARROW. Is the administration prepared to take our case to the WTO, the case that laws on the books do not amount to nothing if they are not being enforced?

Mr. PINKOS. We are examining that issue right now.

Mr. BARROW. When do you think the administration is prepared to take a position on that?

Mr. PINKOS. I am not certain, is the answer to that. There are a couple of things that have to be in line. One, we have to gather the evidence. Some of it seems quite obvious on its face. There are some small businesses, in particular, that are losing their whole livelihood, but that is good evidence. Evidence from multinational corporations is sometimes a little more difficult to come by because they do not want to be singled out by the Chinese and have retribution placed upon them.

So one of it is the evidence-gathering process, making sure that we could win a case, and it would have the effects that we hope that it would, and enlisting, hopefully, some support from other trading partners internationally.

Mr. BARROW. Thank you, sir. Thank you, Mr. Chairman.

Chairman GRAVES. Chairman Bradley?

Mr. BRADLEY. Thank you very much, Mr. Chairman.

It would appear that the administration has heightened the scrutiny on China not just on intellectual property in the last several months, inasmuch as the tariffs on apparel, the Senate taking action on a 25-percent tariff. So these are all pushing in that direction.

I guess my questions are, number one, what leverage do you have, does the administration have in the patent office, to better enforce the laws? That would be Question No. 1. Number 2: Is there a need for Congress to take action to give you more authority to enforce the laws? Answer those first, and then I will ask my next question.

Mr. PINKOS. The answer to your second question: I do not know that Congress could give us more authority to enforce the laws. We do not have the authority to enforce laws in China, obviously.

Mr. BRADLEY. Not enforce the laws, but is there something that we could be doing to give you greater leverage, and what leverage do you have other than WTO?

Mr. PINKOS. I think the level we have involves a lot of the other issues that have come up today. It is multifaceted, multi-issues. Some of the other issues related to agriculture or textiles and other industries can relate and play into IP. Basically, a lot of it is diplomatic leverage and pressure from high-level officials, all the way up to the president, and building pressure internationally. Ultimately, we do have some trade sanction, not being with the USTR, but there are some trade-sanction possibilities that are out there that we have.

Mr. BRADLEY. Well, sort of following up on my colleague, Mr. Barrow's, question, we all went through, in the last session of Congress, the debate about FISC-ETI, and that was a result of the European Union taking action against the United States at the WTO. It would seem to me, based on your testimony and the information that all of us were talking about in our opening statements, that cases are out there to be made. Clearly, you have to have the example, and you have to have done the homework to bring a case that is going to succeed at WTO because you do not want to fail.

I think it is pretty straightforward, I agree, and I suspect all of us would agree that this has, so far, been a very bipartisan hearing, which is refreshing, and I would urge, my voice certainly, that your office continue to pursue this and build that case so that knowing what happened and how we had to change our corporate tax laws last year because of FISC-ETI and the European Union case, that we also build that case to WTO because it would appear, and that is what I was getting to in my first question, the leverage that we have, more than anything else, is WTO. We know what WTO sanctions meant for us in FISC-ETI. Turning the table, I

think, would be the most helpful, especially in this area of patent law. We probably have more opportunities there than we do in currency. We will turn to that in the next panel. So I would urge you to keep the pressure on and build that case.

Mr. PINKOS. I appreciate that, sir.

Chairman GRAVES. Mr. Udall?

Mr. UDALL. What programs does your office have in place to protect the intellectual property of U.S. small businesses?

Mr. PINKOS. Well, first of all, in our fee schedule, we have quite a discount for small- and medium-sized enterprises. We try to make it affordable, but there is some cost associated with it. We also have people in our office who are focused on small business concerns. We try to have a very helpful Web site. A lot of small inventors will go to the Web site, and it will have information about who they can contact in the office, and we will try to provide them direct assistance.

Every year, we have a specific, independent inventors' conference that is widely attended. Last year, it was up in Concord, New Hampshire. But now we are really expanding that through these seminars around the country. In fact, we were in Utah just Monday and Tuesday of this week, and we will be going to several other cities and focusing on China as well. We did one in Baltimore that was China specific.

So it is basically we are trying to reach out because we have people at the office who can assist them and explain to them the steps they need to take to protect their rights.

Mr. UDALL. But as I understand it today, you are not asking for any new authority in order to protect the intellectual property of U.S. companies.

Mr. PINKOS. No, sir.

Mr. UDALL. Is it possible for a small U.S. business that does not export to be a victim of intellectual property piracy?

Mr. PINKOS. Yes, it is.

Mr. UDALL. What would be that company's remedies?

Mr. PINKOS. Somewhat limited. As I have mentioned, there is no international patent or international trademark, so that is one of the things we try to touch upon is that even if you are not thinking about marketing in China, if you have the resources, which I know a lot of companies do not, but it may be beneficial to protect your rights there, so you would have a remedy of going in and trying to enforce your rights there.

Mr. UDALL. When you say there is no international patent, is there a push to do that in any of the forums that exist out there

on an international basis, that it is respected by all of the countries in the world?

Mr. PINKOS. What we work on rather extensively is, at least, harmonization of laws so the process is easier, once you have a patent in one country, to apply in another country. There is a treaty out there called the Patent Cooperation Treaty that is administered through the World Intellectual Property Organization that helps with that. Probably, you would have immense sovereignty issues here in the United States if, for example, somebody was granted a patent in Brazil, and they wanted to say this should be good in the United States. A lot of people in the United States might have qualms with the standards that they set and want some sort of review to occur in the United States.

I am not sure there would be the political support for a full, internationally recognized patent examined on one country automatically accepted in another, but if we come closer together on what the standards are and the formalities, then I think that will be helpful, and that is what we are striving to achieve.

Mr. UDALL. Thank you very much. Thanks, Chairman Graves.

Chairman GRAVES. Thank you, Mr. Udall. Mr. Sodrel?

Mr. SODREL. I do not have any questions at this time. Thank you.

Chairman GRAVES. Mr. Poe?

Mr. POE. Thank you, Mr. Chairman.

Thank you again, Mr. Pinkos, for being here today.

Based on what you said, it seems like China has adopted the flag of the skull and crossbones when it comes to international theft and piracy and cheating, especially when it comes to American products and counterfeiting American products.

I have three questions for you. First, what happens to those counterfeit goods when they come to the United States, and they are seized?

Mr. PINKOS. I am not completely certain, and, in fact, I think that they are not all destroyed. I would have to check with my colleagues in the Customs Department. I think H.R. 32 may address that as well, that just recently was considered by the House. So I could get back to you on that.

Mr. POE. The second question is, of the numerous industries that you have mentioned and that the other members that are going to testify have said in their statements, which one do you personally think in the United States is hurt the most because of the counterfeiting and fraud by the Chinese?

Mr. PINKOS. Currently, I would probably say copyright industry specifically because software piracy is, I believe, up over 90 percent, and software now, or copyright-related industries, is now the

single-largest U.S. export, and it is not just movies and music but also software and publications and other sorts of things.

Mr. POE. Could you give me a monetary amount on that, roughly speaking?

Mr. PINKOS. I do not have the figure off the top of my head, but some of the private sector witnesses after me may. It is in the tens of billions of dollars, I believe, but I do not know the precise figure, sir.

Mr. POE. A lot of money. The last question was, do other countries have the same problem that we do when it comes to this type of fraud, and what are they doing about it?

Mr. PINKOS. Yes. Other countries are experiencing the same problems, and I do not even think that they are as aggressive as the U.S., necessarily. Some are. The EU and Japan, in particular, are trying the make a difference in China. But interestingly, it is not just developed countries. They are seeing in Morocco counterfeit Moroccan CDs that were produced in China and made their way to Morocco. Border countries along China's borders are seeing their products counterfeited in China.

So I think it is a great opportunity to reach out to not just the normal trading partners but to developing countries as well to elicit their support in addressing this problem.

Mr. POE. Thank you very much. I look forward to the administration's vigorous enforcement of international law as well as protecting American businesses.

Mr. PINKOS. Thank you, sir.

Mr. POE. Thank you, Mr. Chairman.

Chairman GRAVES. Mr. Fortenberry?

Mr. FORTENBERRY. No questions at this time, Mr. Chairman. Thanks.

Chairman GRAVES. I do not think we have any more questions at this point. We are going to go ahead and seat the second panel. I do want to tell everybody that we are going to have a vote sometime between 11 and 11:30, which may disrupt us for a little bit. It should not be too terribly long, but we will go ahead and seat the second panel.

Mr. Pinkos, I appreciate you being here and coming over today. I appreciate your testimony. We, obviously, have a very tough problem there and a very tough problem to try to enforce, but I appreciate what your office is trying to do. Thank you for being here.

Mr. PINKOS. Thanks for having me. I appreciate it. Thank you.

Chairman GRAVES. In the interest of time, we will go ahead and continue. For the witnesses' information, that little light box in front of you kind of gives you an idea of where you are in your testimony, and we ask that you try to limit it to five minutes. The red light will come on when that time is up.

Now, I do not throw anybody out for going over. If you have got something to say, I encourage you to say it, but in the interest of time, so we can get through all of our witnesses and the questions, please at least try to observe that, but, again, we are not too hard core when it comes to that.

Our first panelist is Tom Goodpasture with Pride Manufacturing in Liberty, Missouri, which is my district. Tom, I appreciate you coming out; it is a long way. Obviously, many of the panelists have come a long ways today, and I very much appreciate you being here on a very important issue as pertains to small business, and I look forward to hearing your testimony. We will go through all of the panelists, and then we will go to questions. Tom?

STATEMENTS OF TOM GOODPASTURE, PRIDE MANUFACTURING COMPANY, INC.

Mr. GOODPASTURE. Thank you, Chairman Graves, and thank you, all of the Committee, for having me here. I appreciate the opportunity.

My name is Tom Goodpasture, president and owner of Pride Manufacturing, a small machine shop in Liberty, Missouri. In 2002, we purchased a minority of stock in a manufacturing firm in Ninbo, China. The principal owner is a family member, and Pride Manufacturing wanted to use this association primarily as a sales tool. It has been an interesting process that has given me a new insight into the China market. I have never been to China, but I will be traveling there this fall on a study mission trip with the NTMA [National Tool and Machine Association].

The unlevel playing field for us as American manufacturers has make it impossible to compete. At Pride Manufacturing, our cost burden over wages, including benefits, averages in excess of 35 percent. In China, there are no labor laws, no EPA laws, no OSHA laws, no health insurance, and no retirement plans. The biggest benefit provided is buying the workers lunch.

I routinely talk to customers and representatives of large and small American manufacturers who feel the only way they can survive is to buy in China. At Pride, we purchased a $300,000 robot-loaded CNC lathe to do a job for Mercury Marine. The cost of the part was approximately $3. We were producing on the most up-to-date equipment and technology available, yielding under a 5 percent profit margin. We were six months into the project, and the purchasing agent found that he could buy in China for 50 percent, and it was gone.

Customers buying China are willing to accept the 5 to 10 percent or more scrap level at this time, which has to be sorted and quality controlled here. There is no way to recoup the loss, but they feel the competition is "buying" China, so they must also. The rate of defect would not be allowed from U.S. manufacturers.

Many companies are starting their own plants or attempting to partner with the Chinese firms to produce their products. Some succeed, many fail, and there are many horror stories along the way. The common theme from my entire group of associates who have anything to do with China is, "Regarding business, you cannot trust the Chinese."

Why have we embraced the idea and monetarily forced U.S. manufacturers to by China to be competitive? I believe that China has made the wise, wise choice to purchase their future in the world of manufacturing at our expense and demise. With all of the challenges of doing business with China, if the Chinese currency was correctly valued, I wonder how many would actively be pursuing services there? With that correct exchange rate, it is my belief that China could no longer be competitive in the world market of manufacturing.

I do not believe that the average Chinese shop operates nearly as efficiently or accurately as shops in the U.S. That is the major reason for my fall trip: to verify or alter my opinion. With this undervalued exchange rate, China is buying, and we are, either knowingly or blindly, selling 100-plus years of technology in a very short time. China wins, and we lose.

About the time of Desert Storm, I remember a huge controversy when an American cutting tool company was found to have allowed one of their tools to get in the hands of a non-allies machine shop. That tool was found to be producing weaponry that could be used against us. I realize that trade laws were different then, but should the idea of our security and technology protection be drastically different?

Recently, I made a list of what I consider to be top technology cutting tools and e-mailed it to an associate in China. I wanted to see what was available there. Every tool on my list was available on the open market in China, most at a cost with an exchange rate of slightly less than they can be bought here. If they are in China, they could be anywhere.

The patent laws of America have been trashed. The Chinese have absolutely no loyalty to the patent laws of America or any other business deal. They get their hands on a product, take it apart, reverse engineer it, and bring it back on the market at a greatly reduced price. Some of our customers and associates with patented products have found that there is apparently no recourse or, in many case, even traceability to these acts of piracy.

Recently, China was involved in the manipulation of our steel prices and availability by buying large amounts of scrap steel. It is a win-win for them. They need the steel scrap for their production, and at the same time, our material prices are being driven up. That created a material shortage, making us less competitive in the world market. It equates to allowing penny collectors to control the value of our dollar. The price of steel being tied to the scrap steel price and availability is wrong and needs to be reevaluated. We just rebuild our ability to produce steel and other raw materials.

I was at the General Dynamics Land System Division in Detroit on a sales call a few weeks ago. GD makes the armored vehicles for our military. The procurement specialist told me that they are

having a difficult time getting armor steel. In one instance, he had to request that a vendor machine a part requiring three-quarter-inch-thick material out of three-inch just to make deliveries. We are paying in many cases two to three times what we were paying a year ago, and often the required materials are not available or have very long lead times.

I stated earlier that I do not believe that China, on a level playing field, can be competitive. I also believe that, given time, that will change. At the rate we are handing off all that we know, that process can go very quickly. The longer the exchange rate can be artificially deflated, the bigger the jump start. I believe in fair trade, but let us keep it fair.

I have always considered myself very fortunate to be in the manufacturing industry. I find myself, on a day-to-day basis, not only loving what I do but passionate about the industry I serve. If profits are driven out of manufacturing, then it goes into survival mode. We can longer expand technology, properly train new craftsmen, and maintain our facilities. Eventually, we will lose what has made us strong. I believe the country that has the highest ability to manufacture will be the world leader. We have for a long time held that position, but we are quickly becoming a service society and more concerned with the trade than the make. Why would we give our manufacturing capabilities away to a country that we cannot even trust in a business deal? China wins; we lose.

[Mr. Goodpasture's statement may be found in the appendix.]

Chairman GRAVES. Thank you, Mr. Goodpasture.

We are next going to hear from Bruce Iglauer, who is President and CEO of Alligator Records in Chicago, Illinois, and you are here representing the Recording Industry Association of America today. I appreciate you being here and look forward to hearing your testimony. I think you have a time constraint, too.

Mr. IGLAUER. I have a plane, but I would very much like to participate.

Chairman GRAVES. Absolutely.

Mr. IGLAUER. So let us worry about your business, and I will worry about mine.

Chairman GRAVES. Okay. I look forward to hearing what you have to say.

STATEMENT OF BRUCE IGLAUER, ALLIGATOR RECORDS

Mr. IGLAUER. Mr. Chairman, members of the Subcommittees, my name is Bruce Iglauer. I am president, founder, and owner of Alligator Records. I founded Alligator Records by myself 34 years ago in Chicago, the world capital of the blues. It was fueled by my passion for the blues, a uniquely American music full of emotion and history. I founded Alligator in a one-room apartment with only $2,500 and almost no experience in the record business.

I built an artist roster from among the bluesmen and blueswomen who were formed in little clubs on Chicago's south and west side African-American ghettos. Over the years, with a roster of wonderful talent, Alligator has built a catalog of 230 albums, recording blues artists from all over the USA. I am proud of the fact that literally hundreds of musicians and their families have been able to survive and thrive as a result of the work Alligator has done to bring them to a worldwide audience. After 34 years, royalties from the sales of our recordings are not only supporting the artists and the songwriters but also their children and their grandchildren.

The music of Alligator Records is not pop music. It will never be embraced by the multinational companies that market the big hits. Alligator is like literally hundreds of small, independent American labels across the country, labels that record blues, jazz, traditional folk music, classical music, spoken word, gospel, and bluegrass. Alligator, like those labels, is dedicated to recording and preserving music of great cultural importance. Because there is an audience for this music, but not a huge one, it has become the province of independent labels like ours. No one in the independent record business is getting rich, but because we have developed a core audience around the world who love our genres of music, we are able to survive and continue to record this valuable music that we love.

Unfortunately, the survival of companies like mine is threatened today on a worldwide basis by piracy. The last several years have been extremely tough ones for my industry. The piracy of our music, physical and on line, has been the major reason for our problems. In rough terms, the combination of growing global physical piracy, easier Internet piracy, and illegal CD burning generated a 20-percent sales decline in the record industry since 1999. In the case of Alligator, my company, the declining income since 1999 is closer to 35 percent. I have had to cut back on the number of recordings we release and lay off staff members because of the decreased worldwide market for legitimate recordings as a result of piracy.

The impact of the music industry revenue crash has been profound in human and creative terms. There are hundreds of small companies in the U.S. that add to America's culture and our cultural diversity that have been severely affected by this wave of piracy. Successive rounds of job losses have occurred in our companies, small and large companies, and there have been additional job losses associated with the closing of literally thousands of record stores in the USA.

The creative costs may be even more troubling. Artist rosters have been slashed dramatically as record companies can no longer afford to carry as many developing artists as they would like to. Piracy robs the music industry, whether the major labels or independents like Alligator, of the capital it needs to invest in developing artists. The result is that fewer artists are finding the financial support they need to put food on their tables.

American recordings are sold all over the world. For my company, our international business is about 25 percent of our overall income. Sales of American recordings in the rest of the world add significantly to our nation's trade balance and ultimately to our na-

tional welfare. Our nation's welfare is reduced, and our composers, artists, and all of the employees of record companies, small and large, suffer when foreign governments permit our recordings to be pirated in their countries.

When it comes to ripping off American sound recordings, China is one of the worst. The magnitude of record piracy there eclipses any other country. China is potentially the biggest market in the world for American music, maybe even bigger than the USA. With the growth of the Chinese economy and their huge population, the potential for massive sales of American music in China in the next few years is great. It could be a huge boon to independent companies like Alligator. It is not a matter of if our music will be pirated in China but, rather, when. Once that happens, this expanding market will be forever lost to Alligator.

China has made some limited progress of improving its antipiracy laws. It runs some raids and seizes lots of pirated products. But more deterrent penalties are almost never imposed, and piracy continues to thrive.

The challenge for all of us as Americans is to get China to impose penalties on large-scale pirates operating there that truly discourage such piracy. Unless and until they do, not much is likely to change. The U.S. government must press China harder to strengthen their antipiracy enforcement regimes. The current systems in these countries do not work. Unless the U.S. uses each and every option available to it, it will continue to face the same situation we do today for the foreseeable future: overwhelmingly pirate markets and lost opportunities for legitimate U.S. companies.

Without wanting to sound melodramatic, I sincerely believe the survival of the American independent record industry is absolutely dependent on stopping the worldwide piracy in music. Thanks for inviting me to testify today.

[Mr. Iglauer's statement may be found in the appendix.]

Chairman GRAVES. Thank you, Mr. Iglauer.

We are next going to hear from Al Lubrano,—did I get that right?—

Mr. LUBRANO. Yes, you did.

Chairman GRAVES. —who is president of Technical Materials, Inc., from Lincoln, Rhode Island, and you are here representing the National Association of Manufacturers. I look forward to hearing what you have to day. Thank you for being here.

STATEMENT OF AL LUBRANO, TECHNICAL MATERIALS, INC.

Mr. LUBRANO. Good morning, Chairman Graves, Chairman Bradley, members of the Committee. My name is Al Lubrano. I am the president of Technical Materials, Inc., a small manufacturer of engineered materials systems primarily for the electronics industry. In addition to other markets we serve, we are also part of the auto industry supply chain and sell to many of the major auto manufacturers' biggest suppliers. We have approximately 200 employees located in Lincoln, Rhode Island. I also serve as chairman of the

Rhode Island Manufacturers Association, which represents over 200 companies in our state. That is my pro bono job.

I am pleased to testify today on behalf of the National Association of Manufacturers. As a member of NAM's China Policy Subcommittee, I participated in the development of our 2005 China Trade Agreement Agenda that included vigorous participation and resulted in a consensus from both large and small NAM member companies. The fact that we developed a separate China policy shows how important this is to our members.

Mr. Chairman and members of the Committee, I am here to tell you that manufacturing here in the United States has some serious problems, and we must, we must, address the China issue. We are in favor of free, fair trade. The NAM seeks a positive and balanced trading relationship with China that reflects market forces as closely as possible. Without a doubt, China has emerged as a leading world economy, and this has meant significant new market opportunities for many NAM members. However, many members' companies see prices of Chinese so low that it is impossible for them to compete. Others see their customers moving to China and cannot find new ones to replace them.

I have seen this in my own company. As a result of fierce Chinese competition, I have seen many of our customers lose their business because their customers' customers have sought refuge in one of two strategies: either outright moving of production to China or forcing purchasing from lower-cost Chinese manufacturers. Some of our customers tell us that their customers will only pay the "Chinese price." This is a recent favorite of purchasing at Ford Motor Company.

The picture is not entirely grim. We can overcome China's low-wage-rate advantage through innovation and the use of technology. I have brought an example of how we can do that here today. Right now, at TMI, we are selling high-technology, plating material systems to companies in China that have not been able to procure the high-quality product or service they need from any Asian supplier.

In addition, we have recently developed a new material system for the computer disk drive industry using innovative technology and TMI proprietary processes. That material is here today. These are called "suspensions for disk drive arms" used in the computer industry. We sell these to a U.S. company, purely technology driven, committed to manufacturing in the United States.

Our technology and innovation have kept us ahead of the game with some of our customers, but I can tell you, it is not going to be enough if we do not address the problems in our trade with China and address these problems soon. NAM predicts that our trade deficit with China is on track to reach $225 billion, billion. There is no question that eliminating the severe yuan undervaluation is essential to creating more balanced and sustainable trade flows.

China is a tough competitor with low wage rates and many other artificial advantages which can be overcome. What we should not have to deal with is currency so undervalued that China has to spend $2 billion a year to artificially keep it low. That is just not right. Would a considerably strong Chinese yuan have beneficial effects? It certainly would for a lot of U.S. companies.

When the NAM started talking about this problem almost two years ago, we were only one voice. Now Treasury, the European Central Bank, the IMF, Asian Development Bank, Canada, and many others are all making the same point: It is time for China to act. We were disappointed that in its recent report the Treasury Department did not cite China for currency manipulation, but we are pleased with the much tougher message to China by Secretary Snow. The focus must now be October as an absolute deadline. China must act by then.

We look to keep pressing this issue, and, in addition, there are concerns that China's industries may benefit from a wide array of government subsidies. As chairman of the Rhode Island Manufacturers Association, I hear from member companies that when they try to bid for a contract against Chinese manufacturers of the same product, the Chinese price is below their cost of raw materials, below the raw material cost. This is clearly an artificial manipulation.

Earlier this year, NAM recommended to the USTR that the administration develop a WTO case to deal with what President John Engler calls "China's grand larceny on a massive scale."

Mr. Chairman, the issues I have outlined today are having serious and negative effects of manufacturing in this country. We have an obligation to see that America's manufacturing base stays strong. We can do that within the rules of the international trading system, but we must not be timid in the insistence that those rules be enforced. Thank you very much.

[Mr. Lubrano's statement may be found in the appendix.]

Chairman GRAVES. Thank you, Mr. Lubrano.

We are next going to hear from Dave Blackburn with the Thomas G. Faria Corporation,—is that Uncasville?—

Mr. BLACKBURN. Uncasville.

Chairman GRAVES. —Uncasville, Connecticut. He is here representing the National Marine Manufacturers Association. Thank you, Mr. Blackburn, for being here.

STATEMENT OF DAVE BLACKBURN, THOMAS G. FARIA CORPORATION

Mr. BLACKBURN. Thank you, gentlemen, for allowing me the opportunity to address you today.

In an article recently published in the Washington Times, Arnold Beichman, a Hoover Institution research fellow, made the following statement: "The huge Communist Chinese mainland, government and people, is guilty of committing grand larceny on a scale only comparable in contemporary history to the expropriation of private property during the Nazi and Bolshevik revolutions."

If one has any doubts about the veracity of Mr. Beichman's statement, one only needs to educate themselves in the details of the drama that is playing itself out on your watch. Our relatively small company of 350 employees is one of the vast multitude of U.S. manufacturers whose products are being copied with impunity by

the Chinese. We produce engine-monitoring instrumentation, including such products as tachometers, speedometers, fuel gauges, et cetera. The level of technology incorporated in these devices ranges from relatively simple to quite sophisticated. During our history, we have supplied such well-known companies as Ford, Chrysler, Caterpillar, and Harley Davidson. We are currently the largest supplier of instrumentation to the marine industry and the sole supplier of every instrument panel installed in 100 percent of the combat-ready Humvees now serving in Iraq and around the world.

The marine industry is represented here in Washington by the NMMA, the National Marine Manufacturers Association, that represents over 1,500 corporations and businesses. I sit on the board of directors of that organization.

The marine industry supplies the products that provide a boating experience to over 72 million Americans annually on the 13 to 14 million boats that are registered in the United States. This industry also contributes over $30 billion a year to the nation's economy, as well as over $7 billion a year in wages. It is twice the size of the cruise ship industry.

While my company serves multiple marketplaces, I cite these facts about the marine industry because it was one of the large, U.S. marine, boat-building conglomerates that was approached by the Chinese with an offer to sell identical counterfeits of our products, including our address in Uncasville, Connecticut, at approximately one-third of our average sales price. In addition, this is an industry that is rife with opportunity for the counterfeiters to steal more American jobs and technology.

The sad fact is that there is almost no area of American manufacturing that is not exposed to Chinese theft, and up until now there is little to nothing that is being done about it by our government. In fact, our government, in an indirect way, has reinforced this unethical behavior by supporting the admission of this country of minimal business ethics to the WTO.

A little over 50 years ago, over 40 percent of the jobs in the United States were represented by manufacturing. Today, that number is closing in on 10 percent and dropping rapidly. A significant driver of this statistic is the number of jobs that have been lost to counterfeiting of American products.

The supervisor of my shipping department once worked for an American company that was founded in 1847. Not too many years ago, they employed 2,000 people. In the 1980's, the Pacific Rim began a systematic program of copying their catalogs and products. Today, the company is no longer in existence.

I know there are some among us who have countered that this is not a problem because we are replacing these manufacturing jobs with service jobs. What I clearly do not understand is how anybody can equate a $22-an-hour job, which is the average rate in manufacturing nationally, to an $8-an-hour job at Wal-Mart, our nation's largest retailer. Wal-Mart, by the way,—I have heard two different estimates—if they were a separate individual nation, they would be the third-to-the-sixth-largest trading partner for mainland China.

There is more at issue here than just economics. There is a real threat to public safety. The counterfeit gauge that is shown in Ex-

hibit 1, which is now in the possession of the secretary of commerce's office, is not accurate. I assume we would all be appalled if we found out that a half dozen troops in a Humvee were shot and killed because their engine failed at a time of crisis due to inaccurate instruments in the vehicle that failed to warn them of an impending engine failure at a most inopportune time.

I trust that perhaps one or more of you might own a boat. If you do, you might be sensitive to the prospect of coming through a dangerous inlet or breakwater only to have your engine run out of fuel due to an inaccurate fuel gauge.

Over a year ago, another small company just down the road from us, Pfizer, Inc., received a complaint from one of its Lipitor customers that in her recent prescription the pills tasted strange. After laboratory analysis, it was determined that the pills were counterfeited. This revelation led to the removal of over 16 million doses of the drugs from pharmacy shelves around the country. Virtually any popular medication is a target. If any of you take a prescription drug, you are a potential victim. I have attached a publication by the National Association of Boards of Pharmacy—it is Exhibit 2—that lists drugs susceptible to counterfeiting. I would encourage you to read it. It might scare you to death.

The scope of the unethical activities of these pirates appears to be limitless. In addition to copying other companies' products, they are aggressive in taking steps within their own governmental infrastructure to steal trademarks, avoid establishment of a legal presence in the United States, engage in activities to allow patents, and even use the threat of violence to protect their ill-gotten market position selling counterfeit products in countries around the world. I had one of our sales representatives have his life, as well as his family's lives, threatened if we interfered with their sales of our counterfeited product in Colombia.

The Chinese government has disallowed Pfizer's patent for Viagra. One of the requirements for gaining trademark registration in China is that you must have a "well-known mark." China recently determined that Toyota was not a well-known mark. An individual named Ma Zhongbo in China is attempting to register a trademark as we sit here.

Some might question why the Chinese government seems to be complacent or often illogical in their determinations. Perhaps some of the reason for this lies in the fact that the government has a vested interest in the economic gain to be realized through unethical behavior.

A business associate of mine who has been in the plant that is counterfeiting our product indicated to me that the managing director of the factory that is producing the counterfeited product is the head of the local Chinese Communist Party, and the facility is government owned. I have been told this is not an unusual set of circumstances and is more the rule than the exception.

Given these facts, I am not surprised that enforcement is difficult to obtain, and punishment is tokenism, at best. After all, given the facts, are we not asking the government to actually punish itself, given the relationship it has with many of these counterfeiters? When was the last time you asked your child, after committing an

improper act, to punish himself or herself and be repentant, and they actually did so? Have we really become that naive?

About five months ago, I testified before the U.S. China Commission. My recommendations to the Commission included the initiation of a case before the WTO based upon the failure of China to meet the requirements of WTO member economies. Those requirements include laws for the protection of intellectual property and the enforcement and imposition of penalties for noncompliance. These requirements clearly have not been met.

In a report released on March 25th of this year, the Commission has, in fact, now recommended that disputes be filed by the United States in the WTO against China and that a 25-percent, across-the-board tariff be established on Chinese-produced products sold in this country. It is encouraging to me that a government entity is actually stepping up to the plate with a firm, concise, precise recommendation to take action.

I am not an economist or a necessarily astute student of international political equations, just a businessman. However, as with many issues in life and as a business person, I see a problem with retaliatory actions taken by us that can result in a number of counteractions by the Chinese. We are all painfully aware of the huge budgetary deficits and national debt that exists. A painful reality is that last year China held the position of the second-largest holder of foreign U.S. Treasury debt, second only to Japan. In addition, China had a net increase in U.S. holdings for the year, whereas Japan, the largest foreign holder, had a net decrease in holdings.

Recently, a comment by South Korea that they might shift some of their investment to the euro sent our stock market into an immediate tailspin. The panic subsided only after a clarification of South Korea's position was issued. What would happen if the second-largest holder of our foreign debt decided to move away from the dollar?

In any event, the situation facing U.S. manufacturers such as us and the gentleman sitting next to me and the other people at this table is, indeed, daunting. We are faced with competition whose labor costs them an average of 65 cents an hour, far less regulatory complexity, and a cooperative governmental alliance, albeit unethical at times. We cannot stop competition. However, we are faced with unfair competition from an international player who does not play by the rules, at least not by the WTO's rules or their own government's. Ironically, they often do play by the rules of the law in the U.S. which often favor their rights over our own rights. At times, our own government appears to be disengaged in any firm resolve to address this problem.

A quote that I have used before but keeps ringing in my ears is a statement by the former chairman of the Sony Corporation, Akio Morita. In a speech to a group of high-level business executives, he said, specifically at American manufacturers, "A world power that loses its manufacturing capacity will cease to be a world power." I hope that his prophecy does not become an epitaph for the tombstone of American manufacturing. Thank you.

[Mr. Blackburn's statement may be found in the appendix.]

Chairman GRAVES. Thank you, Mr. Blackburn.

We are going to pause for just a minute, run and take this vote real quick. We should not be very long at all. Mr. Stallings, I apologize for that, but we will be back and resume at that point. So we will just take a few minutes to run over there, vote, and be back.

[Whereupon, at 11:24 a.m., a brief recess was taken.]

Chairman GRAVES. Again, I apologize for the interruption, but votes are, obviously, one of the things that we do here.

Next, we are going to hear from Thomas Stallings with the Funston Gin Company and the Funston Warehouse in Funston, Georgia. He is here representing the National Cotton Council of America.

Mr. Barrow, do you want to say anything in introduction?

Mr. BARROW. I appreciate the introduction. Go ahead.

STATEMENT OF THOMAS STALLINGS, FUNSTON GIN COMPANY, FUNSTON WAREHOUSE

Mr. STALLINGS. Thank you, Mr. Chairman. Thank you and the members of the Subcommittees for inviting me to discuss trade with China. Representative Barrow, I would like to thank you for your assistance during my visit here.

I am a cotton producer and the owner of Funston Gin Company and Funston Warehouse in southwest Georgia. I serve as a member on the board of directors of the National Cotton Council.

There are few international trading relationships more complicated or dynamic than that of U.S. cotton and China. The U.S. cotton industry is exporting an ever-increasing amount of cotton fiber to China. At the same time, our long-standing and best customer, the U.S. textile industry, continues to contract in the face of the competition from textile imports. China is the most competitive textile and apparel manufacturer in the world, and with the elimination of all quotas on January 1st of this year, China is rapidly becoming the dominant supplier of textile and apparel products in world trade.

This development has ramifications for the U.S. textile industry. A few statistics will illustrate the dynamic nature of the trading relationship between the U.S. cotton industry and China. In 1998, China imposed quotas on cotton imports and imported only 359,000 bales of cotton from all countries. In 2004, China imported a total of 8 million bales, and at least 4 million of those bales were supplied by the U.S. In 2005, China will import a total of 15 million bales of cotton. At the same time, China's exports of cotton products to the U.S. continue to increase dramatically while U.S. mill consumption of cotton has declined, from 11 million bales to 6 million bales. During the same period, U.S. consumers have increased their purchases of cotton products at retail, but almost 90 percent of all purchases are imports.

With that brief background, I can better address your question. The answer is, yes, China does have barriers to fair trade and engages in practices that provide unfair advantages to its manufacturers. The cotton industry is deeply concerned by the use of tax

rebates to encourage exports. We are troubled by the widespread use of subsidized or forgiven loans provided to China's domestic textile industry, and we believe that the maintenance of an undervalued currency constitutes an unfair trade practice.

As a small business operator, I know it is impossible to compete with another firm that enjoys a 30-percent cost advantage due to an undervalued currency and that probably has access to free capital in the form of loans that do not have to be repaid. I also know that the U.S. textile firms are concerned about the piracy of their fabric designs and unauthorized use of their logos and brands, which they have spent millions of dollars developing.

When a part of the cotton industry enjoys the benefits of a growing trade in raw cotton, there are problems. We have consistently expressed our concerns with the way China has implemented its market-access commitments under the WTO Accession Agreement. We have worked closely with USDA and USTR to attempt to convince China to modify its administration of tariff rate quotas.

Recently, China has announced its intention to impose a variable rate tariff on imports of cotton over the TRQ. This will affect the price of cotton to the mills, and we are trying the determine whether this new tariff would effectively amount to a price support for Chinese cotton farmers. We have also worked with USDA, USTR, the Chinese government and industry to resolve contractual issues, arbitration practices, and quality standards.

Mr. Chairman, China is a dominant factor in the world cotton and textile markets. It is imperative that the U.S. cotton industry continue to cultivate China as a customer for our fiber. It is also critical that we work with Congress and the administration to insist that China honor her WTO commitments. That is why we are actively supporting efforts to convince China to move to allow her currency to be valued by the market. We also support the use of textile safeguards, as authorized under the WTO Accession Agreement, to allow the U.S. industry to adjust to the elimination of quotas.

As a business operator, I contend that the adjustments cannot be accomplished as long as Chinese manufacturers have the competitive advantages provided by an undervalued currency, tariff rebates, nonperforming loans, and unchecked piracy of valuable designs and brands. We welcome China to the WTO, and we value her as a trading partner, but she must be held accountable to the rules and the commitments of the WTO membership.

Mr. Chairman, again, I thank you for allowing me to testify, and I will be pleased to respond to any questions at the appropriate time.

[Mr. Stallings' statement may be found in the appendix.]

Chairman GRAVES. Thank you, Mr. Stallings.

I am going to start out with questions. I am going to tend to direct them, but feel free, if I have not necessarily directed a question towards you, and you would like to give some input, do not hesitate. My first question is for Mr. Goodpasture and Mr. Lubrano.

I am curious, as far as customers go, have you had customers tell you they are holding you to the so-called "China price," or are you

having problems with that as far as customers more interested in price rather than quality, that they are willing to sacrifice quality? Do they know that many of these counterfeited products coming out of China are inferior, I guess you might say, to those products you are producing? Did I make myself clear enough?

Mr. LUBRANO. Yes. I will give you two examples. It is typically our customers' customers who have said to us that they have been forced by people like the auto industry to a China price, and they just cannot do it. So the purchasing people in that industry will go look at what they can buy the product from China for and then say to the manufacturer, "You can have this business, but this is the price I am going to pay," and in some cases, it is below the cost of raw materials.

I have seen that. It has happened. Our customers' customers have talked to them, our customers have talked to us, and what happens is the whole supply chain loses the business. So we lose it, our customers lose it, and their customers lose it.

I can also give you an example of counterfeiting, the cheaper product. I was with a company in Italy recently that buys product from us. They manufacture relays. The name of the company is Fender, and the director of purchasing handed me two relays. I looked at them, and I said, "Okay. What is your point?" His point was, one of them was not his; it was a counterfeit product from China that was selling at about two-thirds of what he could sell the product for. His company had spent, he told me, over $300,000 on lawyers. The lawyers were promised a meeting. The Chinese government was going to take these people to task. The lawyers got there, and they could not find the company. So those are two real-life examples of exactly what we talked about.

Mr. GOODPASTURE. I had a meeting Tuesday before I left for here with a current customer that I have that said, if we could not drop prices, they would have to be forced to go to Asia, and they are already. It is kind of ironic. At this point, we are in kind of a unique position, and we have not been affected because we are a job shop that can go different directions.

So my response was, now is a good time because I know the quality is lower in China, and I know that they would have a difficult time getting these particular parts made, but that will change with time. There is high tech going over there. We have a vision system that is very high tech. I was talking to OGP, and their biggest customer is China right now. They make high-tech stuff. So it is going to change, and they are going to get better, and they will own the world of manufacturing if we do not do something.

Chairman GRAVES. Mr. Iglauer, have you had labels, your actual label, counterfeited or just printed in China?

Mr. IGLAUER. The honest answer is I do not know because the Chinese counterfeit products that are being manufactured in China right now are primarily being distributed in China. I have a distributor in Hong Kong who has been trying the set up a distribution deal for us in China, a legitimate one, and at this point, he

is being told the marketplace is not there partly because of the marketplace being flooded with counterfeit goods.

As to whether it is specifically my product, I cannot answer that. I can tell you that my product is regularly counterfeited in Russia and makes its way into eastern Europe, and the counterfeits are brilliant. They are gorgeous. They sound great, they look great, and the artists, songwriters, and the record company who invest make nothing.

Chairman GRAVES. How did you figure out, I guess, when you saw that first counterfeit?

Mr. IGLAUER. Actually, I have deejays in Lithuania who play my music on the radio, and they sent them to me and asked me if we had manufactured those. It was a shocker because they were so good.

Chairman GRAVES. Mr. Blackburn, you handed out some material. It obviously looks like the same thing. I would be interested in your reaction the first time, or how you figured out the first time that obviously some of your products out there were not your products.

Mr. BLACKBURN. Actually, the first time was back around 1990 or so, and that was in the South American market where we knew the Chinese were counterfeiting our product. It was a small part of our overall business, so we did not pursue it aggressively. This is the first time that I have had a situation where they have actually approached one of my larger domestic customers in an attempt to sell a product. In fact, that customer was in their factory and hand carried the sample back to me, so there was no doubt about the authenticity of it as a counterfeit.

There was one visual characteristic that made it obvious it was not ours, and it was a little wrinkle in the bezel. It is the type of cosmetic flaw that we would not let out of our factory, and most people would not even notice it, but because it is our business and our product, I did. We put it on a test stand, and it was grossly inaccurate. That particular item was a volt meter.

Unfortunately, the counterfeits are so good, and they carry our name, address, our inspector's initials on them, a CE label of ours, that in our warranty department, if it came in and was a counterfeited gauge, most of my people would not recognize it as a counterfeited gauge. We would pay warranty costs and replace the instrument and suffer from our reputation in the field.

Chairman GRAVES. Obviously, looking at the pictures, they have got the patent number on there and everything.

Mr. BLACKBURN. I saw one counterfeit where we had a nick in a case mold where foreign material had created a nick in the mold itself, and they had even duplicated the nick in the case.

Chairman GRAVES. Mr. Barrow?

Mr. BARROW. Thank you, Mr. Chairman.

Shifting gears for a second from the subject to widespread theft of property rights as an unfair trading practice to the subject to currency manipulation, I want to ask Mr. Stallings, help put this in context for us. Can you tell us how the Chinese policy of pegging its currency to the value of the U.S. dollar helps Chinese agricultural producers and hurts American agricultural producers?

Mr. STALLINGS. Yes, Congressman Barrow. The pegging of the currency tends to keep the U.S. cotton products higher. It also inflates the Chinese cotton products for the Chinese producer, but in the counterbalance of things, the U.S. dollar will be priced higher, and the Chinese currency will be lower. Therefore, you could buy, as an example, from Fruit of the Loom. It would not be the same t-shirt. It has the same label. The thread count is different. But you could buy three Chinese Fruit of the Loom t-shirts for the price of one U.S. t-shirt. Wal-Mart and Target are flooded with those. The devaluation of the currency is a very, very important thing that we need to control.

Mr. BARROW. And it seems to me, when talking with earlier witnesses about the difficulty of marshaling the evidence to support various claims that we have of unfair trading practices, this seems to be the one that is the most straightforward, the one that can be brought with the least amount of difficulty because we can see directly what the cause-and-effect relationship is. Thank you.

I want to direct another question, if I can. Do you have something you want to add, Mr. Stallings?

Mr. STALLINGS. I would add that knit goods, since January 1st when quotas came off, they are up 800 percent from China.

Mr. BARROW. Directing a question to the other members, I want to talk about energy practices and energy costs in the Chinese economy as opposed to ours. Congressman Graves and I are co-authoring a bill that is seeking to fix what is broke [sic] with the natural gas futures market in this country, and it raises a question in my mind as to whether or not Chinese manufacturers are encountering the same kind of problems that American producers and American manufacturers are encountering with respect to energy costs. Are they experiencing the same problems? Do they have any of the difficulties that American producers and manufacturers are having with respect to the cost of energy?

Mr. IGLAUER. Our experience has been, when I am over there talking to some of our customers who actually put facilities there, that energy is not reliable. Places will have to shut down because they cannot get electricity. Depending on where you are, that is more of a problem. If you are in a remote area, it is more of a problem. If you are around Shanghai or Beijing or Shenzhen, it tends to be less of an issue, but they are having some problems with energy.

Mr. BARROW. Reliability is an issue that would seem to work in our favor.

How about the price? How about the price?

Mr. IGLAUER. It does not seem to be price. It seems to be reliability more than anything else, from my experience. I am over there a few times a year.

Mr. BARROW. Are there subsidies in the energy market that you all are aware of? For example, do they have any difficulty in the natural gas market, for example, the stability of the price of natural gas?

Mr. IGLAUER. I do not know the answer to that.

Mr. BARROW. Thank you, Mr. Chairman.

Chairman GRAVES. Mr. Bradley?

Mr. BRADLEY. Thank you, Mr. Chairman.

There has been a lot of discussion about currency this morning, and certainly anybody that reads the Wall Street Journal or any of the other business presses would know that there has been a lot of oaring back, if you will, on the whole currency problem and whether if there are adjustments, and the Chinese currency floats to the dollar as opposed to pegged to the dollar, that it would really help American manufacturing, and, in fact, some people have even said it could destabilize the world economy. Do any of you have any thoughts on the efficacy of removing the peg and having a floating currency and what, if any, positive impacts there will be, and could you try to quantify that?

Mr. IGLAUER. I would caution that there are no silver bullets. I think fixing the currency and letting it float should be a remedy that we take, in that everything is supposed to be governed by a free market economy, and that will certainly make the situation fair with respect to our currency, but I think that I would throw some caution to the wind here, too. It is more than just a currency issue, and you have heard from colleagues here today that it is a much broader-based issue than that.

Mr. GOODPASTURE. I would say that the 8.3, if it is a true currency right now, manufacturers would be buying at 8.3 plus shipping, and they are not. Average costs that manufacturers are buying in China for is around 40 percent, 50 percent what they would pay here. So if that was changed to where it could float, that could be a primary source, but if that does not work, I think tariffs is the only vent. We have got a mass exodus of large corporations not only buying from China but going to China and setting up factories. The longer that continues, the more pressure our government is going to get because people are not going to want to lose once they make the huge investments in Chinese factories to now just, all of a sudden, that monetary change where they were buying

for 40 percent, and now maybe they are even, even. So I think tariffs should possibly be an answer behind the exchange.

Mr. LUBRANO. There is one issue we did not discuss, too. The fact that the currency is undervalued also makes it a lot more attractive for foreign investment in China, and that is a huge problem as well. We really have not touched on that subject here today.

Mr. BRADLEY. More a question to Mr. Lubrano from the NAM perspective. Would NAM be supportive of implementing those 27-percent tariffs that the Senate has talked about?

Mr. LUBRANO. I know the NAM position is that we have to follow the IMF and the WTO and do things in a manner that is consistent with what we are trying the accomplish and not go off and ignore those because once you set that kind of precedent, I think the NAM is concerned, and rightfully so, that you could lead to chaos, and I would say that the NAM position of going through the IMF and the WTO is the appropriate way to go.

Mr. BRADLEY. And has the administration been aggressive enough in pursuing WTO remedies?

Mr. LUBRANO. I cannot speak for NAM, but if you are asking me, I would say absolutely not.

Mr. BRADLEY. Even despite the fact that Secretary Snowe and Secretary Rice have highlighted recently currency problems.

Mr. LUBRANO. I think the example of how the WTO can effectively work has been cited earlier with respect to the FISC and what remedies were imposed through an appropriate channel: going to the WTO, making the case, U.S. losing, and then tariffs.

Mr. BRADLEY. U.S. winning, I think you mean.

Mr. LUBRANO. We lost, and the Europeans imposed tariffs.

Mr. BRADLEY. Oh, in Europe, yes. That was the point I was making earlier.

Mr. LUBRANO. I think we need to take the gloves off and use the same kind of remedies. I mean, we are getting killed.

Mr. BRADLEY. Would all of you agree with that?
All. Yes.

Mr. BRADLEY. And would you all agree that that is our best remedy?

Mr. STALLINGS. I think it stretches all the way across to all of the industry that is represented here today. The benefits that you have with the WTO; we had no control over China, but now it is in the WTO, and the rules and the remedies are in place. They

need to be enforced, the same as Brazil entered their challenge against the cotton program.

It is evident that China is definitely not complying with the WTO, and they have a two-sided door that we are exporting cotton into that country, and they are our customer. They are our largest customer, but they only let mills use U.S. cotton that are exporting it back to the U.S., and then the mills that they run their cotton, it is consumed domestically in China, and they also price it however they want to price it.

Mr. BLACKBURN. The fact of the matter is that China is not abiding by the rules as a member of the WTO, and they have been in the WTO for a number of years now. They have consistently flaunted those regulations, made false promises, have not provided any type of enforcement, and we still are talking about bringing a case against them. There is a mechanism in place, but we have to do more than talk; we need to do something.

Mr. BRADLEY. Thank you.

Chairman GRAVES. Mr. Lipinski?

Mr. LIPINSKI. Thank you, Mr. Chairman. Thank you, all of the witnesses, for your testimony today. I represent a district that has lost thousands of manufacturing jobs. We still do have some manufacturers left, and I am continually hearing from them very similar concerns that you all have said today. Just hearing you again on these things really is frustrating and infuriating that this is going on, and it seems like nothing is being done to stop the rampant piracy—they are letting it occur, the Chinese government, and sometimes, as we have been told, they are actually doing it—and also the very much undervalued currency which they have pegged.

There are a lot of questions I have. I just want to focus on two sort of broad questions. It seems to me that this is being done because the Chinese government has determined that if they can do this for long enough, they can take the manufacturing out of other countries, establish it in China, and maybe sometime down the road they will decide that they will play fair, but at that point, they will have robbed other countries, especially the United States, of the manufacturing.

So two broad questions: First of all, and I want to hear briefly from each of you, is it possible in the industry that you represent if tomorrow we went and did all of these things that we have talked about here that the government needs to do to try to halt this loss of manufacturing jobs, first of all, can we ever gain back any of this manufacturing; and the other question is, is there a point at which you see there is almost no turning back, that we will have lost so many jobs in the industry that you are here representing that that will be it? Is there a tipping point, and do you think there is a time anywhere, say, how many years in the future, where essentially we will have almost killed off that industry in this country? So I will start with Mr. Goodpasture.

Mr. GOODPASTURE. It is never too late, but it is late. It would be very difficult. We have given them a lot of technology. Because of the American presence in China, it is like it is okay to send our top technology over there. There is very sophisticated equipment that is now being bought, and China is the main purchaser of it. The main market is in China.

So I think it is late. If the brakes were put on completely, they have that technology. Whether they can develop it on their own, I do not know, but I will see that this fall.

Mr. IGLAUER. The potential for China to reverse itself from being a country that is stealing copyrighted materials to being a consumer of copyrighted materials would ideally lead to more jobs here. They might not be the same jobs that have been lost, but I could foresee China as the largest consumer, as I said before, of American music in the world. It is the largest country in the world. There is an international fascination with American music.

Could they produce it there legally? Yes, under license, paying the owners of the copyrights who thus pay the artists and composers who create it. Could that marketplace create more jobs at the creative end, at the artist-and-composer end, in the United States? Absolutely. Those people are losing their jobs because American record companies are shrinking as a result of worldwide piracy.

So I can foresee a new batch of jobs being created which would not necessarily be the same batch of jobs that have been lost.

Mr. LUBRANO. I believe in American ingenuity, and I think, as I go around the country and look at what our customers are doing and what we are doing, if these other issues were fixed, I really believe it would stem the tide. I agree it is late, but it is not too late, and I think what I would like to see is not handouts but a partnership between the American manufacturing community and our government where we were working together more closely to get these problems resolved, and we are getting help to get our cost structure in line.

N.A.M. has put a survey together with the Manufacturing Alliance. Right out of the box because of rules, regulations, and other things placed upon American manufacturers, we come out of the box with a 22-percent disadvantage versus our top ten trading partners. Well, you take 22 percent, and you take anywhere from 20 to 40 percent of the undervalued yuan, I mean, right out of the box, we are almost 60 percent behind the eight ball. If those things got fixed, I think, with American ingenuity, we could certainly compete much more effectively on a global basis.

Mr. BLACKBURN. I believe that ultimately China, and we have not mentioned India, a country who is soon to take over China as the most populous nation on earth and is really a very central area of high-technology development, that ultimately that area of the world will be the manufacturing center of the world. There is little that we can do, I think, to stop that from happening. There are too many forces in place that are driving that. A great many of them

are economic. Certainly, some are cultural and have to do with government policy.

Anything that we could do to slow that down, and I think that is all we can do is slow down the transfer of manufacturing and manufacturing jobs to the Pacific Rim, would be helpful. Certainly, letting the currency float so we are not dealing with a $22- to 65-cent-an-hour, cost-of-labor differential would help. Anything that could be done in terms of, as my associate next to me mentioned, more of a working partnership between our governments and our industries working together on regulatory fronts that are, at times, very burdensome and that our counterparts in China do not have to deal with are an issue.

I am not supporting that we loot our ground water and do a lot of things that the Chinese are doing, but somehow we have to take actions that will help to level the playing field and, at the very least, eliminate unethical behavior. That is really a core issue here, is the unethical behavior.

I wonder how the Chinese would react if the U.S. Patent and Trade Office said, "Because you are not complying, we are not going to accept any more applications for Chinese patents, and any Chinese company that has patents here, we are not going to enforce them." That is what they are doing to us. We are, I think, too ethical and too moral a country perhaps to do that, but that, quite frankly, after dealing with folks from the Pacific Rim for the last 25 years in business, it is the only language they understand. That is the reality.

I think that the way in which American manufacturing will be able to maintain some presence in the worldwide manufacturing community is through innovation, through quick deliveries. There are basically three or four things that determine why you go to a supplier or a manufacturer. Number one is price. Number two is quality, although Dr. Demming would say it should be the other way around, but we no from experience that that is not the case. The last is delivery performance.

So the way we are, as a company, fighting it is with delivery performance with quality. We cannot compete on price. My people do not make 65 cents an hour. I guess the bottom line is I look at these barriers and say, "I am a combat veteran. I really believe in this country." My board of directors are saying, "Why the hell do not you move the production to China?" Well, I just do not want to do that. If things keep going on the way they are, I am not going to have any choice. I hope I am retired by then because I do not want to be in a position where I have to do that to survive. That might have strayed a little bit from your question.

Mr. LIPINSKI. Thank you.

Mr. STALLINGS. I, too, feel that America brings a lot of honesty and integrity and quality to everything we produce, and I like to buy on quality rather than price. I would rather sleep on a nice sheet with good thread count that brings comfort to me than I have one that the first time it goes to the cleaners, it comes back, and all of the thread is coming out of it. And quality means a lot in the cotton industry, the textile industry.

Fifty percent of our mills have already closed, 70 percent in Bangladesh. The Bangladeshis are unemployed. They do not draw unemployment insurance. They do not have any means to protect themselves from what the Chinese are doing to them. In all of your lesser-developed countries,—we have helped in sub-Saharan Africa, places that we have got a textile industry that was growing and booming the same as ours in 1988—it is already destroyed. But it is never too late to do something about it. You can rebirth an industry, but the biggest thing I see as a stumbling block is that we go into the WTO, and we sign all of the rules and regulations, and we agree to comply, but we do not enforce the rules and regulations upon the ones that we trade with. We do not have to reinvent the wheel; we just have to enforce the regulations that is already in place.

Mr. LIPINSKI. Thank you very much.

Mr. FORTENBERRY. Thank you, Mr. Chairman, for holding this very important hearing, and thank you, gentlemen, for your insightful testimony.

I am going to attempt to summarize some of the complexities that we have heard today. I would like you to comment on that, and then I am going to move into two questions I would like those of you who feel they would like to respond to those, if you are interested.

In regards to the unfair-competitive-advantage question we are talking about here, it comes down to three categories of things, it seems to me: the counterfeiting issue; the issue of currency manipulation; and then other economic inequalities, such as unfair government subsidization, lax regulations, environmental and otherwise, and unfair labor practices when compared to our country.

But let us look at this loss of economic opportunity to China from two ends of the same question. The first is, and if you could comment on this, what do you see in regards to targeting particular manufacturing industries, either by subsidization of the government or willingness to take long-term losses, until there is market capture as a stated intention or policy of Chinese officials or Chinese officials working in close cooperation with other international business entities?

Second, let us discuss the mechanics of what you just suggested that you do not want to do. How would you move your firm to China? What are the mechanics as to how that happens? How do American firms and otherwise enter into agreements and with whom to accomplish that end? My understanding, if you approach the Chinese with the intention of moving a facility there, you are guaranteed a certain amount of labor, a certain amount of output every day. That is the way it happens.

But I would like any of you who have insight into those two questions to please comment.

Mr. BLACKBURN. I do not know about the other gentlemen, but I fairly regularly get letters from folks either in the States that have migrated here from mainland China or people in mainland China themselves who have offered their services to help me set up

factories. I would imagine, based on some of the experiences that have been related to me, that I could probably move the entire factory there and have it operational in three months.

Mr. FORTENBERRY. Again, with a guaranteed labor cost and a guaranteed output.

Mr. BLACKBURN. They will build the building for me.

Mr. FORTENBERRY. Who?

Mr. BLACKBURN. There is usually an intermediary because the government does not want to be identified, I do not think, themselves, but you know the government is behind it to a great extent.

An individual who is the president of a large buying association who actually imports a fair amount of goods from China for the marine industry was talking to a company—I believe it was about building a fiberglass plant. So they had some fairly serious discussion. He wanted to know about the facility and how long it would take to build it, and they said, Oh, not long. He went back three months later, and there was a 250,000-square-foot building erected sitting ready for operation. He had not even made any promises yet.

Mr. FORTENBERRY. Anybody else?

Mr. LUBRANO. I think the situation is very different in different regions. I think the one overriding thing that we experience as we deal with the Chinese and we export product to China,—we have a lot of product going to Malaysia, a fair amount of product going into China, and there are tremendous opportunities now in some products that we make for sales in China—the issue for us is when we sell to a company in China. For example, we have a customer, a Singaporean company, who moved their manufacturing into China. Once the manufacturing gets into China, and you are dealing and getting product into China, the first question I am asked when I go there, and I will be there next week, is, when are you putting up your facility? We need local content. The government is requiring local content.

So there is pressure for suppliers to set up in China. Relative to how you do that depends on what you are trying the do and varies tremendously area by area. I think our approach is probably going to be the joint venture route ultimately. The biggest concern we have, as stated before, is, how do I protect our intellectual property? Our company is priority processes, intellectual property.

I have heard so many horror stories about people setting up facilities there, and before they are even in production, there is another factory half a mile away producing the same product that has got all of the drawings, all of the processes. And one company I know of, High Technology Ovens,—I heard the story the other day—in Minnesota, they never even got to produce anything. They just packed it up and left after investing millions of dollars. So these are more the concerns.

How you do it, I think, is dependent on where you are going to be, who you are interfacing with, and what the Chinese customers you are trying the sell to are trying the force you to do. I hope I answered your question.

Mr. FORTENBERRY. Well, it is obviously complex. It cannot be summarized in a simplistic fashion because of regional issues, because of intermediaries, other perhaps unknown, behind-the-scene players that may be government officials or maybe not. I understand the complexities. But I think you understand the key point, and if any of you want to discuss the other issue as well: Do you know of intentional targeting of particular small manufacturers in this country where there has been unfair subsidization by the Chinese government through various means in order to capture a particular market, sustaining long-term losses in order to capture a particular market, running someone here out of business?

Mr. BLACKBURN. I believe the subsidy comes somewhat indirectly again. My understanding is, and this could be provided through an intermediary or a joint venture situation, if you go to the Chinese government with a pro forma business plan, they will build a factor for you at little to least cost going forward. However, your retention of that lease depends upon you realizing your business plan and filling the factory up.

Now, the easiest way to do that is to pick a product that is popular somewhere in the world, any product—there are no products that are immune to this right now, none—to copy it because you avoid the R&D, you avoid all of the NRE expenses up front that we have to build into our prices. Maybe you sell it outside the United States. The rest of the world is still a very large market, and you fill the factory up. You would have to do it quickly. You only have so much time to do that, or you lose your lease, and you lose your free factory. So that is not a direct subsidy. We get into, I guess, the definition of the word, "direct" and "indirect." It is reasonably direct when somebody provides you with a manufacturing facility basically free of cost.

Mr. FORTENBERRY. That is a form of economic inequality that does not exist on this side, and I think that is what we are getting at, is to try to level the playing field so that we can fairly compete, not to shut down competition, not to shut down trade, which can be very beneficial to all persons on either side of the globe, but to ensure that we have a level playing field. I think that is the bottom line here. Thank you all for your insights.

Chairman GRAVES. Any other questions? Mr. Barrow? Mr. Bradley? Jeff, any?

Well, I appreciate all of the witnesses being here today. This has obviously been extremely informative, and we have a tremendous opportunity, I think, in China. But when we put our manufacturers and businesses at such a competitive disadvantage, it does not matter whether it is through currency manipulation or overregulation or piracy or labor issues, you know, it is an extreme disadvantage.

Mr. Bradley and I are going to, and, I think, Mr. Barrow obviously wants to be a part of it, too—we are going to explore what we can do through our Committees, through our staff, to put some more pressure on the Administration to try to work through some of these remedies, try to hold China accountable through some of the policies that are already in place, try to enforce some of the WTO regulations trying the keep China in check as much as possible. But we are going to see what options we have.

We will, obviously, take these findings and turn them over to other Committees that have jurisdiction in this area, but I do appreciate all of the witnesses coming today. I know you have traveled, many of you, a long distance, and that does mean a lot to us, and I appreciate what you all are doing, and I hope you hang in there and are very profitable. Thank you very much for being here today. This hearing is adjourned.

[Whereupon, at 12:30 p.m., the Subcommittee was adjourned.]

Good Morning and welcome to the joint Rural Enterprise, Agriculture and Technology Subcommittee and the Tax, Finance and Exports Subcommittee hearing. It is my pleasure to hold this hearing with Chairman Bradley as we explore Chinese barriers to trade.

Trade with China has grown faster than with any other U.S. trading partner. Currently, China is our third-largest trading partner, the second-largest source of U.S. imports, and the fifth-largest U.S. export market.

The growth of the Chinese economy, in particular their exports to the United States, has reached record levels and has created a trade deficit for the United States topping $162 billion in 2004.

There are several reasons for the discrepancies.

First, since 1994, the Chinese government has kept its currency pegged at 8.2 yuan (pronounced: u-en) to the dollar. While in recent years, the dollar has weakened, the yuan has remained the same against our currency. Many economists estimate that the yuan is undervalued by as much as 40 percent, which means Chinese manufactured goods are 40 percent cheaper than their competitors.

Just last week, the U.S. Department of Treasury issued a report on the state of global currencies and called China's currency peg "highly distortionary."

China has experienced economic growth, gains in productivity, a large export sector, and increased foreign investment. Their currency manipulation gives their manufacturers an advantage and creates an enormous disadvantage to ours. It's about time they stop cheating and start playing by the same rules.

Second, theft of intellectual property rights is another significant problem that US companies must take into account when dealing with China. It is estimated that counterfeits constitute between15 - 20 percent of all products made in China and account for about 8 percent of China's GDP. It is also estimated that US companies lose $25 billion annually to copyright violations.

While many people believe that this problem is restricted to CDs, purses or polos, it is only the tip of the iceberg. Many people believe that it is a victimless crime; unfortunately, Chinese counterfeits or pirated items can impact our safety.

For example, in 2000 "The New York Times" reported that Southwest Airlines discovered that counterfeit cables, had been installed in 47 of its planes. These cables are used to connect the cockpit controls to the engines, landing gear and rudders. One of Southwest Airlines suppliers had bought counterfeit parts.

Over the last two decades the U.S. has pressed China to improve its protection of intellectual property rights (IPR). While China has passed new laws that provide protection of IPR, it has

done little to enforce these laws, allowing for rampant piracy and counterfeiting. China needs to crack down and be an active part of the solution.

And finally, while the Chinese have some laws that protect its workers and protect the environment, few are ever enforced. U.S. companies are held to some of the highest standards in the world and these standards are noticeably absent in China. Chinese companies do not have to comply with an OSHA or EPA.

We need to ensure that US firms compete on a level playing field in the global market and not be at a competitive disadvantage. These unfair barriers not only affect our economy but job growth, much of it fueled by small business, in this country.

I am pleased to recognize Representative Barrow for his opening statement.

Subcommittee on Tax, Finance, & Exports
Opening Statement of Chairman Jeb Bradley
Hearing:
Does China Enact Barriers to Fair Trade?

May 26, 2005

Good Afternoon. Thank you all for coming today. I would like all of you for coming, especially witnesses who have traveled great distances to be with us here today.

I am also very appreciative of the Gentleman from Missouri, Chairman Graves, for agreeing to work with me on this hearing. I am very much looking forward to working with him, and all of you on the issues raised at today's hearing.

As you all know, over the past two decades China has emerged as a strong international competitor in a wide range of products and has proven to be a critical market for U.S exports. China's emergence as a leading world economy has provided significant new opportunities for American exporters and U.S. exports to China have risen sharply in recent years.

That rapid growth has raised China from the 10th largest U.S. export market in 1997 to the 5th largest in 2004. In fact, between 2000 and 2004, exports to China accounted for half of the increase in total U.S. exports worldwide—an increase of $18.5 billion.[1]

Unfortunately, there has been a downside to the unprecedented growth in China's economy as well. The deficit for trade in goods with China stands at about $176 billion. Having increased rapidly in recent years, it now is the single largest bilateral deficit America has. We are forced to ask ourselves what as caused this deficit?

While numerous trade irregularities exist between our two nations, this hearing is going to focus on three of the most prevalent—China's undervalued monetary system, the lack of Intellectual Property protection enforcement in China, and the lack of enforcement of Chinese regulations to protect workers' rights and the environment.

In 1994, China devalued its currency by roughly 30 percent and has maintained that value to this day -- despite increases in production capability, productivity, quality, foreign direct investment, and other factors that would normally be expected to cause a currency to appreciate.

This undervaluation effectively increases the cost of U.S. exports to China and lowers the cost of Chinese imports to America—which only exacerbates the growing bilateral trade deficit between our two nations.

Intellectual property (IP) protection is another area of concern for U.S. exporters to China. According to the U.S. Patent and Trademark Office, China is the largest single source of seizures of infringing products by U.S. Customs—roughly $62.5 million, or 66% of total goods seized, in fiscal year 2003.

In 1991, the United States threatened to impose $1.5 billion in trade sanctions against China if it failed to strengthen its IPR laws. Although China later implemented a number of new IPR laws, it often failed to enforce them, which led the United States to once again threaten China with trade sanctions.

The two sides reached a trade agreement in 1995, when the Chinese government pledged to take immediate steps to stem IPR piracy by cracking down on large-scale producers and distributors of pirated materials and prohibiting the export of pirated products. The agreement also mandated the establishment of mechanisms to ensure long-term enforcement of IPR laws and providing greater market access to U.S. IPR-related products.

While some progress has undoubtedly been made between our two nations in this regard, these new mechanisms are not being rigorously enforced by Chinese officials, leading some industry analysts to estimate that IP counterfeiting and piracy in China cost U.S. copyright firms $2.5 billion in lost sales in 2004.

Yet another problem creating tension between our two nations is China's record on worker rights and environmental protections. American workers are without a doubt the most productive in the world, but they are being pitted against Chinese workers who have very little, if any, wage, health, or safety protections.

Regardless of your productivity, ingenuity, or persistence—if a rival shop owner has 1/20th of the labor costs you do, it's almost impossible to compete—even when that rival shop is half a world away in China.

It's not just wage considerations that put American businesses at a disadvantage. Our government heavily regulates safety and environmental concerns—regulations and enforcements that are severely lacking in China. Again—when you don't have to comply with the literally hundreds of Occupational Health and Safety Administration and Environmental Protection Agency regulations, you're going to have a leg up on the competition.

It is my hope that our two nations can continue to work together to ensure a level playing field when trading. I am very eager to hear the testimony to be presented today, and again, thank you all for being here today.

Before we begin, however, I would like to yield to the gentle lady from California, Ms. Millender-McDonald, the Ranking Member for the Subcommittee on Tax, Finance, and Exports.

---

[i] See testimony of Douglas Holtz-Eakin, Director, CBO Budget Office, before House Ways and Means Committee, April 14, 2005

STATEMENT
of the
Honorable John Barrow, Ranking Member
Subcommittee on Rural Enterprises, Agriculture and Technology
Joint Hearing on "Does China Enact Barriers to Fair Trade"
House Committee on Small Business
May 26, 2005

Thank you Mr. Chairman.

For many generations back, my family has farmed all across eastern and southeastern Georgia. And I learned very early on to appreciate the hard work and sacrifice of our family farmers. Not only is farming an industry with tremendous challenges, but it's also an industry that impacts the entire world. Our farmers face the pressures of supplying the world with food and clothing, and this is no easy task. The policies enacted by Congress, as well as by foreign governments, have a major impact on our farmers. Recognizing this, I'd like to thank Chairman Graves and Chairman Bradley for holding this hearing to examine China's impact on fair trade.

I've asked a fellow Georgian to come join us today to talk about the cotton industry in Georgia and nationwide, and how China's trade policies are affecting this industry. Mr. Stallings is a cotton producer from Funston, GA, and I thank him for taking the trip up here and participating in this hearing.

The ever-increasing number of imports and exports crossing our borders illustrates the importance of the international trade market – particularly in the U.S. In fact, the global

economy has grown so much that 80 percent of world economic consumption takes place outside of this country.

In today's global market, it's that much more important that our family farmers compete on a level playing field. Much of this country's success in the world market depends on small businesses and agriculture. Today, 97 percent of exporters are small businesses, and make up over 50 percent of our nation's GDP. This includes many of our family farms.

While access to overseas markets is important to our economy, we need to examine the impact that trade policy has on small business exporters in this country.

China is our third-largest trading partner. We are China's largest overseas market, and China's exports represent 13 percent of U.S. imports. U.S. exports to China have been growing rapidly – but competition from China is one of the biggest threats facing the small business sector of the American economy.

Meanwhile, while U.S. exports are increasing, the numbers don't add up. In 2004 alone, the U.S. ran a trade deficit of 162 billion dollars with China, our largest trade deficit with any other country. These figures spell trouble for our trade relationship with China, where we sustain a huge imbalance between what U.S. exporters send and what U.S. importers receive in return.

My home state of Georgia plays an integral role in U.S. exports. Georgia exported 16.3 billion dollars in goods in 2003, with agriculture accounting for more than 963 million dollars in sales

abroad. Cotton plays a big role in these figures. Cotton is Georgia's top agricultural export, and is an industry with a unique relationship with China.

Today's hearing will provide us with an opportunity to learn more about the unfair factors influencing U.S.–China trade relations, and to examine the intricate relationship that U.S. industries have with China. Specifically, we will hear testimony on unfair trading practices associated with currency manipulation, intellectual property piracy, and a lack of compliance with labor standards and other regulations.

When it comes to setting currency regulations, China isn't playing fair. This manipulation makes Chinese exports to the U.S. cheaper, and U.S. exports to China more expensive.

When it comes to honoring or defending our property rights, China isn't playing fair. Piracy and counterfeiting practices in China are costing U.S. firms billions of dollars in lost sales.

And finally, when it comes to respecting honest and adequate labor and environmental standards, China isn't playing fair. The production of more goods at lower costs should not be done at the expense of public safety, environmental standards, or the rights of workers.

This is the case and those are the facts. And unless China starts playing by the same rules, rules they agreed to when they joined the WTO, Chinese exporters will continue to have an enormous advantage over U.S. companies.

In the global marketplace, we've got to stand up for American interests. Standing by while small businesses, family farms, and American workers lose out is just not an option.

Thank you.

STATEMENT OF

STEPHEN M. PINKOS

DEPUTY UNDER SECRETARY OF COMMERCE FOR INTELLECTUAL PROPERTY
AND
DEPUTY DIRECTOR OF THE UNITED STATES PATENT AND TRADEMARK OFFICE

BEFORE THE

Committee on Small Business

Subcommittee on Rural Enterprises, Agriculture and Technology Policy
Subcommittee on Tax, Finance and Exports

United States House of Representatives

"Does China Enact Barriers to Fair Trade?"

MAY 26, 2005

Introduction

Chairman Graves, Chairman Bradley, Ranking Member Barrow, Ranking Member Millender-McDonald, and Members of the Committee:

Thank you for this opportunity to appear before you to discuss international intellectual property (IP) piracy and counterfeiting problems and the Department of Commerce's role in protecting IP abroad. Secretary Gutierrez is keenly aware of the increasing significance of IP protection for American businesses and innovators and has made combating piracy and counterfeiting a top priority for the entire Department. As Deputy Under Secretary of Commerce for Intellectual Property and Deputy Director of the United States Patent and Trademark Office (USPTO), I am dedicated to marshalling U.S. government efforts to reduce the toll that IP theft takes on American IP owners. I am very appreciative of the Subcommittees' interest in addressing additional ways to protect U.S. IP owners' assets, and I commend you for holding today's hearing on China.

Scope of Global IP Piracy and Counterfeiting Problem

Increasingly, both the United States and our trading partners are relying on IP to drive economic growth. This is because competitive success in a market economy depends more and more on the IP assets held by an institution -- from the skills of its employees to the results of its latest research. IP-based businesses, such as the software and entertainment industries, now represent the largest single sector of the U.S. economy.

According to the International Intellectual Property Alliance, U.S. copyright industries continue to lead the U.S. economy in their contributions to job growth, gross domestic product (GDP), and foreign sales/exports. Between 1977 and 2001, the U.S. copyright industries' share of the GDP

grew at an annual rate more than twice as fast as the rest of the U.S. economy. In 2002, the U.S. "core" copyright industries' activities accounted for approximately 6 percent of the U.S. GDP ($626.6 billion).[1] In 2002, the U.S. copyright industries achieved estimated foreign sales and exports of $89 billion, leading all major industry sectors, including motor vehicles (equipment and parts), aircraft and aircraft parts, and the agricultural sector.[2]

Unfortunately, the economic benefits of capitalizing on intellectual property rights (IPR) have captured the attention of pirates, organized crime, and terrorists. The global criminal nature of IP piracy has effects in other areas as well. As former U.S. Attorney General John Ashcroft reported: "In addition to threatening our economic and personal well being, intellectual property crime is a lucrative venture for organized criminal enterprises. And as law enforcement has moved to cut off the traditional means of fund-raising by terrorists, the immense profit margins from intellectual property crimes risk becoming a potential source for terrorist financing."

USPTO and DOC Efforts to Combat Problem

Given these threats to U.S. economic interests and our national security, the USPTO and our colleagues in the Department of Commerce are working hard to curb IP crime and strengthen IP enforcement in every corner of the globe. Indeed, former Secretary Evans heavily emphasized this issue, and Secretary Gutierrez has indicated it is a top priority for the entire Department. Because American IP owners compete in a global marketplace, we must expand our efforts to promote IP protection internationally. We must make sure that American IP owners have sufficient knowledge and legal tools to fight piracy and counterfeiting. We also must provide foreign countries technical assistance on drafting and implementing effective IP laws and promoting the effective enforcement of IP rights.

American Inventors Protection Act of 1999

The passage of the American Inventors Protection Act of 1999 (AIPA) (P.L. 106-113) set the stage for the USPTO to advise the President, through the Secretary of Commerce, and all Federal agencies, on national and international IP policy issues, including IP protection in other countries. USPTO is also authorized by the AIPA to provide guidance, conduct programs and studies, and otherwise interact with foreign IP offices and international intergovernmental organizations on matters involving the protection of intellectual property.

Our established Offices of International Relations and Enforcement carry out the functions authorized by the AIPA. These include (1) working with Congress to implement international IP treaties; (2) providing technical assistance to foreign governments that are looking to develop or improve their IP laws and systems; (3) training foreign IP officials on IP enforcement; (4) advising the Department of State and the Office of the U.S. Trade Representative (USTR) on drafting/reviewing of IP sections in bilateral investment treaties and trade agreements; (5) advising USTR on intellectual property issues in the World Trade Organization (WTO); and (6) working with USTR and industry on the annual review of IP protection and enforcement under the Special 301 provisions of the Trade Act of 1974. The USPTO also represents the United States in United

[1] "Copyright Industries in the U.S. Economy: The 2004 Report," Stephen E. Siwek, Economists Inc., prepared for the International Intellectual Property Alliance. "Core" industries include: newspapers, publishing, recording, music, motion pictures, radio, television broadcasting and computer software.
[2] Id.

Nation bodies, such as the World Intellectual Property Organization (WIPO), to help set the international standards for IP protection and enforcement.

National Intellectual Property Law Enforcement Coordination Council (NIPLECC)

The USPTO serves as the co-chair of the National Intellectual Property Law Enforcement Coordination Council (NIPLECC), which is tasked with coordinating domestic and international intellectual property law enforcement. NIPLECC was launched in 1999 to ensure the effective and efficient enforcement of intellectual property in the United States and worldwide. NIPLECC's coordination activities ensure that government enforcement efforts are consensus-based and non-duplicative. NIPLECC has developed a comprehensive database that includes all recent IP law enforcement training provided by the U.S. government and many associations to developing and least developed nations. It is also developing legislative suggestions to improve domestic IP laws related to enforcement. We look forward to continuing our efforts in NIPLECC.

Strategy Targeting Organized Piracy (STOP)

Further, the Strategy Targeting Organized Piracy (STOP) Initiative, which has been developed over the last year, is the most comprehensive U.S. government-wide initiative ever advanced to demolish the criminal networks that traffic in fakes, stop trade in pirated and counterfeit goods at America's borders, block bogus goods around the world, and help small businesses secure and enforce their rights in overseas markets. I will discuss this important initiative in more detail later.

Enforcement Training and Technical Assistance

The USPTO provides a variety of IP enforcement training and technical assistance activities. These programs are designed to foster respect for IP, encourage governmental and right holders' efforts to combat infringement, and promote best practices in the enforcement of IPR. Our technical assistance and capacity building initiatives grew out of a desire to promote IP protection and assist developing countries in meeting their obligations under the WTO's Trade-Related Aspects of Intellectual Property Rights (TRIPs) Agreement. In addition, we have responded to an increasing number of requests by foreign governments for such training and technical assistance activities. Our efforts have had positive results in some countries, measured by decreasing levels of IP piracy and counterfeiting, and the implementation of stronger legal protections in many of the countries in which we have provided such training. Still, much work remains, including in China, where IP theft has not decreased.

Today, our efforts are aimed at: (1) assisting developing and least developed countries to meet international standards in the protection and enforcement of IP; and (2) assisting administrative, judicial, and law enforcement officials in addressing their enforcement issues.

Trade-Related Aspects of Intellectual Property Rights Agreement (TRIPs)

At the conclusion of the Uruguay Round in 1994, the resulting TRIPs Agreement presented WTO members with new obligations and challenges. The TRIPs Agreement sets minimum standards of protection for the various forms of IP and requires WTO members to provide for "enforcement procedures ... that permit effective action against any act of infringement of intellectual property rights." The TRIPs Agreement includes detailed provisions on civil, criminal and border enforcement measures designed to provide the owners of IP with the tools to protect and enforce

their rights. Today, Developing Countries obligations' under the TRIPs Agreement have fully entered into force. Least Developed Countries have until 2006 to comply with the bulk of the provisions, including the enforcement obligations.

Over the last several years, the USPTO has assisted countries around the world in establishing adequate enforcement mechanisms to meet their obligations under the TRIPs Agreement. In bilateral negotiations, we work closely with USTR to seek assurances from our trading partners of even higher levels of IP enforcement than those set forth in the TRIPs Agreement. We provide technical advice through the annual Special 301 process, the GSP review, the TRIPs Council review of implementing enforcement legislation, and in the negotiation of free trade agreements (FTAs).

Our approach to the on-going FTA negotiations has been to build upon the TRIPs Agreement. In other words, our negotiating position is that these trade agreements should follow a "TRIPs Plus" format by, among other things, expanding the minimum standards set out in the TRIPs Agreement. For example, by incorporating provisions of the WIPO Copyright Treaty and WIPO Performances and Phonograms Treaty, the FTA updates copyright protections and enforcement for the digital environment. In our advisory capacity, we will continue to work with the Department of State and USTR to conclude FTAs that reflect the level of protection and enforcement of IP rights in the United States.

Intellectual Property Issues and USPTO Approach in China

Due to the rapid increases in piracy and counterfeiting in China, we recognize that U.S. companies face enormous IPR protection and enforcement challenges in these countries and that their losses are mounting daily. At the same time, the pressures of the competitive global marketplace, criminal elements, and protectionist and non-tariff barriers, make these challenges increasingly more sophisticated. That is why the USPTO's team of experts has developed comprehensive work-plans to address the rising IP problems facing these countries. While the USPTO does not have the lead on trade policy issues, which is the mandate of USTR, we have devoted significant resources to making progress in improving China's IPR regimes for our industries, right holders and this Administration.

The Bush Administration understands that IP is a vital component of our nation's economy and that this Administration's focus on combating global piracy and counterfeiting has produced a solid track record of real results. The STOP Initiative, which I mentioned earlier and will discuss in more detail later, is a continuation of these efforts by providing additional tools to protect American workers from counterfeiters and pirates who are robbing billions of dollars from the U.S. economy.

China

The U.S. has long been concerned about IP protection dating back to the founding of our country. For example, Gilbert Stuart's Athenaeum portrait of George Washington was replicated without authorization by a Philadelphia merchant, who was later sued for copyright infringement. Our first engagement with China on IP dates back to the early 20th century. In early 1903, at the end of the Qing dynasty, the U.S. government entered into the first bilateral agreement between China and the United States to protect IP. Our first commercial agreements in the 1970s with the People's Republic of China contemplated that China improve its IP system. Our current Ambassador to China, Clark Randt, was involved in some of these early negotiations.

Unfortunately, problems persist and our concerns about IP enforcement in China continue to grow. Despite China's membership in the WTO and its requirement to comply with the TRIPs Agreement, as well as a series of bilateral commitments made over the past 10 or more years, the lack of effective IP enforcement in China is a major problem for U.S. business interests, costing billions of dollars in lost revenue and perhaps tens of thousands of U.S. jobs. While China has done a generally good job of creating laws to comply with its WTO commitments, IP enforcement problems remain pervasive. These problems run the gamut from rampant piracy of movies and business software to counterfeiting of consumer goods, electrical equipment, automotive parts, and pharmaceuticals.

I was very pleased that Secretary Gutierrez stated the following during his confirmation hearing with respect to intellectual property rights: "We actually lived through this as a food company, ironically, where we found that our brand was actually being copied and used in some markets and obviously without any authorization. One of the great assets that we have as a country is our brands, our technology. I think this is a matter to focus on. I think it is a big issue." Secretary Gutierrez also cited IP protection as a key issue in U.S. trade ties with China, and he has reiterated his commitment to addressing this issue to me.

IP Problem in China

Estimates from the computer software and automotive parts industries are illustrative of the scope of the problem. The software industry estimates that more than 90 percent of all software installed on computers in China in 2003 was pirated.[3] The automotive parts industries estimate that counterfeit automotive parts production costs the industry billions of dollars in lost sales. China is a leader in counterfeit goods in this industry.

In the automotive arena, most counterfeiting involves parts that need to be replaced frequently, such as oil filters, headlamps, batteries, brake pads, fan belts, windshields, and spark plugs. For example, DaimlerChrysler, BMW, Audi, Volvo, Mitsubishi, and Toyota report that even though a factory in Guangdong Province has been raided three times in a two-and-a-half-year period, it has been allowed to continue making windshields stamped with their brand names for sale in the world market. One industry group estimates that legitimate automotive companies could hire 210,000 more employees if the counterfeit auto parts trade is eradicated.[4]

According to the World Health Organization (WHO), 10 percent of the medicines in the world are counterfeit, with China being one of the main centers of counterfeit production. Rudolph Giuliani offered the following testimony before a Senate Committee in June of last year:

> "An August 30, 2002, Washington Post story cites the Shenzhen Evening News in reporting that an estimated 192,000 people died in China in 2001 because of counterfeit drugs. Another news story reported that as much as 50 percent of China's drug supply is counterfeit (Investor's Business Daily dated October 20, 2003)."[5]

---

[3] Ibid. Key Findings: BSA and IDC Global Software Piracy Study.
[4] Motor and Equipment Manufacturers Association, September 2003.
[5] *See* Statement of Rudolph W. Giuliani before the Senate Government Affairs Committee, Permanent Investigations Subcommittee, *Oversight Hearing on Safety of Internet Drugs* (July 16, 2003).

While no definitive statistics exist on total U.S. job losses attributable to IP piracy and counterfeiting in China, there is no doubt piracy and counterfeiting deprive the government of billions of dollars of much needed tax revenue, cost thousands of jobs, and injure the domestic software industries.

China's Enforcement Issues

The Chinese IPR enforcement environment today is complicated by a variety of different Chinese and foreign interests, including Chinese industrial policies, trade policies, the interests of foreign investors, and the interests of Chinese domestic enterprises. In this environment, our right holders increasingly look to adequate enforcement of criminal IPR laws in implementation of China's WTO commitments as a key to reducing counterfeiting and piracy rates in China. China, it should be noted, does not lack for quantitative enforcement. Each year, tens of thousands of enforcement actions are undertaken. However, these actions are typically pursued by administrative agencies, which impose non-deterrent penalties.

This Administration has been pressing China to impose prison sentences and/or stiffer fines on violators of IPR since fines and other penalties imposed are too modest and provide little or no deterrence. In December 2004, two branches of China's government – the Supreme People's Court and Supreme People's Procuratorate (prosecutor) issued a new "Judicial Interpretation" for criminal IPR infringements. The new Interpretation expanded the scope of violations punishable by prison sentences by lowering the value threshold necessary to initiate a prosecution, but on the enforcement side took a significant step backwards with respect to violations committed by repeat offenders. The new Interpretation was also deficient in many other areas of concern to industry and foreign governments, including, for example, coordination among China's civil and administrative systems as well as the relationship with other IP laws. Furthermore, the new Interpretation complicated matters by allowing infringing goods to be valued based on their street value, not their legitimate value, thus sanctioning declarations by the infringer as a measure for determining whether or not Chinese valuation thresholds were met dictating prosecution. Equally disconcerting was that unfinished or offsite products were exempt in assessing that value.

Many of the challenges that China encounters are at least partially due to deficiencies in its own system, including extensive corruption, local protectionism, and lack of interagency coordination. Some of the issues we have raised with Chinese colleagues include: the use of mandatory sentencing guidelines for IPR crimes; support for specialized IPR courts which have greater independence from local financing and control; establishing appropriate procedures for investigation, prosecution, and conviction of IPR criminals; and effectively addressing trans-border IPR crime, as well IP crime committed over the Internet.

It is important to recognize that there is a Chinese domestic constituency also seeking enhanced IPR protection and enforcement, and that pirates and counterfeiters do not necessarily discriminate against Americans or just against Americans lacking political influence. As the economy grows, domestic interest in IP, particularly in the more developed cities on China's seaboard, is increasing dramatically. China's deficient IP protection and enforcement hinders Chinese software engineers, inventors, and movie producers who have to struggle with a severely deficient domestic market as their principal source of income. Chinese IP owners have become increasingly vocal proponents of stronger IP protection. One indication that IPR is attaining increased domestic importance is the number of trademark applications received by the Chinese Trademark Office (CTO). For the past two years, the CTO received more trademark applications than any country in the world. The State

Intellectual Property Office is also growing rapidly and receives some of the highest number of filings for patent applications worldwide.

Growing domestic interest in IP protection and enforcement may be of small comfort to U.S. industry when the impact of piracy and counterfeiting on U.S. industry appears to be growing. U.S. Government statistics show a worsening situation. For example, USTR's 2004 Special 301 Report states that during 2003, 66 percent of all of the IPR-infringing goods seized at the U.S. border came from China.[6] Many industries also increasingly suspect that the Chinese government, by restricting market access, is providing free rein for counterfeiters, pirates, and criminals to exploit the void created by the lack of legitimate products. Many U.S. companies also complain of industrial policies that help create conditions for production of infringing products. Counterfeit Viagra, for example, dominates the Chinese market, while the legitimate product has been hampered by market access restrictions. Pirated movies appear in the Chinese market long before censors have approved the legitimate product. Other high-tech companies complain of standards setting, such as in wireless networking technology, which limits introduction of legitimate products or mandates technology transfer.

USPTO's Efforts in China

Under the direction of this Administration, the USPTO has been working extensively to reduce piracy and counterfeiting activity in China. First, we provide technical support to all agencies of the U.S. Government that are addressing these issues, including USTR, the Department of Commerce/International Trade Administration (ITA), the U.S. Department of Justice, the Department of Homeland Security, and the State Department.

The USPTO has an established team of experts on Chinese IP matters, which includes IP attorneys with detailed knowledge and background on patents, trademarks, copyrights, enforcement issues, and WTO/WIPO issues. Our cooperation with other U.S. government agencies extends beyond the trade agenda to providing support on strategies and to addressing transnational crime and transnational trade in counterfeit goods, as well as other issues.

TRIPS review. For example, we take an active role in the annual review of China's TRIPs commitments at the WTO, including primary responsibility for drafting many of the TRIPs-related questions. Three USPTO officials attended China's WTO review last year. We also actively participate in the APEC Intellectual Property Experts Group, which plays a constructive role in developing regional standards for IP, including cooperation on enforcement matters. Further IP initiatives in China supported by the USPTO are described below.

IP attorney at U.S. embassy. For two summers, with the active support of U.S. Ambassador Clark Randt, we stationed one of our IP enforcement attorneys, who is fluent in Mandarin, in our embassy in Beijing to help with IP enforcement issues in the region. Last fall, the USPTO was proud to continue this support by detailing this individual as attaché to the U.S. Embassy in Beijing for a three-year appointment to continue our Government's efforts to combat piracy and counterfeiting. This is the first time the USPTO has sent an official abroad for an extended period of time to assist in improving IP protection in a specific country, which highlights the seriousness of IP violations in China. Having an attaché stationed in China has enhanced the USPTO's ability to work with

[6] http://www.ustr.gov/Document_Library/Reports_Publications/2004/2004_Special_301/2004_Special_301_Report_Section_306.html.

Chinese government officials to improve IP laws and enforcement procedures in addition to assisting U.S. businesses to better understand the challenges of protecting and enforcing their IPR in China.

Meetings with Enforcement Officials and Other Influences. One of the greatest challenges in China is ensuring that localities fully enforce national laws. To that end, the USPTO has held meetings with numerous local copyright, trademark, judicial, police, and prosecutorial enforcement officials throughout China to ensure that local officials fully understand their international obligations. We have hosted numerous delegations at the USPTO, with the objective of addressing this challenge. We have also worked with U.S. non-governmental organizations in support of rule of law efforts and training programs, including a Temple University program and Franklin Pierce Law School's annual summer program on intellectual property law in Beijing for American and Chinese law students.

Training. Recent efforts in China that we have supported include: training on criminal IPR with the support of the British Government and China's Ministry of Public Security; training on patent data protection and patent linkage with the State Intellectual Property Office and State Food and Drug Administration; training on "business methods patents" with the State Banking Regulatory Commission, State Council Legislative Affairs Office and the Development Bank of China; training with the World Customs Organization on border measures and criminal IPR; participation in Chinese sponsored programs on IP protection in Shanghai and on IPR strategies for multinational companies in Beijing; and a joint U.S. Semiconductor Industry Association and Chinese Semiconductor Industry Association training program on IPR in high tech industries, to name but a few.

Bilateral meetings with trade groups. We have also participated in a range of bilateral meetings and consultations with visiting U.S. trade associations such as the Intellectual Property Owners, U.S. Information Technology Office, Research and Development Pharmaceutical Association of China, Quality Brands Protection Committee, American Bar Association, International Federation of Phonographic Industries, Motion Pictures Association, Entertainment Software Association, Business Software Association, Association of American Publishers, U.S. Chamber of Commerce, to name just a few. We have also worked with some of these organizations to host enforcement conferences in such major cities as Beijing, Shanghai, Guangzhou, Wuhan, Nanjing, and Chengdu.

Both domestically and in Beijing, we have provided briefings for visiting congressional and judicial delegations, and we have provided training for State Department and Commerce Department officials at our various consulates, including participation at a regional training program in Hong Kong sponsored by the Economic Bureau of the State Department. Working with the Department of Commerce's Technology Administration and the International Intellectual Property Institute, we have provided technical assistance on copyright protection in Dalian and Shenzhen.

Public relations efforts. The USPTO continues to work through our own office of public affairs and the public diplomacy offices of the Embassy and consulates on providing an informed perspective on IP matters to the Chinese public and Chinese decision makers. Additionally, we are supporting State Department efforts to provide informational materials on U.S. IP practices to the Chinese public. We have also had several meetings at Chinese Universities. Under Secretary of Commerce for Intellectual Property and Director Jon W. Dudas delivered a talk at Qinghua University, one of China's leading law and engineering institutions, on IP protection. In addition, my staff has delivered presentations at Sichuan Normal University Law Faculty, Qinghua Law Faculty, People's

University and other institutions, as well as appearing on several television shows and being featured in newspaper articles.

Supporting Businesses and Working with Law Enforcement in China

Apart from these advocacy and training efforts, we are involved in developing practical strategies to support our businesses in handling problems in China. We have worked extensively with the Commerce Department on improving methods for handling business complaints involving unfair IP practices in China and have become involved with the STOP Initiative whereby we handle complaints involving IP, many of which involve China. We have worked on two leading programs associated with the U.S. Embassy involving IP: a "toolkit" on IP matters for U.S. businesses on the Embassy's website, and the "IPR Roundtable" that the Ambassador hosts each year.

Meetings in China. We have held meetings at the Canton Trade Fair to discuss IPR enforcement and complaints filed. We continue working with ITA, the American Bar Association, and many other organizations to provide better assistance to U.S. small and medium businesses. USPTO attorneys have been meeting with other foreign missions and trade associations to exchange ideas on innovative ways to promote better protection of IPR in China.

Training programs for American businesses. We have participated in training programs for our business people in the United States, to better enable them to forcefully address the IPR challenges they experience in China and, when necessary, bring well-founded complaints to our attention. Typically in conjunction with the Department of Commerce, members of our China team have participated in programs in such cities as: Cincinnati, Ohio; Grand Rapids and Pontiac, Michigan; Charlotte, North Carolina; Miami, Florida; Minneapolis, Minnesota; Wichita, Kansas; St. Louis, Missouri; New York City and Long Island, New York; Waterbury, Connecticut; Boston, Massachusetts; Providence, Rhode Island; Portsmouth, New Hampshire; Fresno, San Jose and San Francisco, California; Salt Lake City, Utah; and Washington, D.C. A major focus of these efforts has been to address problems of small and medium enterprises, although larger enterprises have also benefited from participation in many of these programs as well.

Workshops about China. In addition to our work with the Department of Commerce, our China team is planning to roll out a series of intensive China workshops and seminars in several cities throughout the United States in 2005-2006. The first of these seminars is planned for Detroit, Michigan, in June. The program will provide companies with information about several useful topics, ranging from an overview of the IP protection and enforcement environment in China, specific information on how to file patent and trademark applications in China, how to use China's administrative and judicial systems to enforce IPR, and useful tips about how to locate and hire a local company to investigate IP infringement in China.

Another activity, as part of our ongoing efforts to assist U.S. businesses and IP owners in protecting their rights overseas, includes a seminar on the Chinese criminal justice system for IP offenses that we held in February of this year. The seminar introduced the Chinese criminal justice system to U.S. industry, government agencies, IP owners, and legal practitioners and included information on the recently amended Judicial Interpretation so they may better understand the system and use this information to their full advantage to combat counterfeiting and piracy. We sponsored a follow up program in April of this year.

Our China team has supported a number of programs to advise our companies on how to file a criminal IPR case in China. These programs have already been held in Guangzhou, Beijing, and Hong Kong with an additional program planned for Shanghai. In addition, we provide support to our own law enforcement authorities where possible on IP criminal matters. For example, we have supported the Joint Liaison Group on criminal justice cooperation in its efforts to facilitate better criminal IPR cooperation, and joined in training programs run by a number of different government agencies on criminal IPR matters. Our China team works closely with the Customs Attaché and Legal Attaché at the U.S. embassy as well as the Bureau of International Narcotics and Law Enforcement at the State Department on these matters.

More United States Government Efforts in China. Like Secretary Gutierrez, former Secretary of Commerce Evans believed in the strong enforcement of our trade laws and took innovative and proactive measures to strengthen the enforcement and compliance of our trade agreements. During his tenure, he tasked Commerce agencies, such as USPTO and the new Investigations and Compliance Unit within ITA's Market Access and Compliance Group, to coordinate their efforts to vigorously pursue allegations of IPR violations wherever they occur, especially in China.

Delegations to China. In 2003, then-Commerce Secretary Evans led a mission to China and highlighted China's lack of IPR enforcement. The Secretary met with high-ranking Chinese officials and reiterated a continuing concern -- that effective IPR protection requires that criminal penalties for IP theft and fines are large enough to be a deterrent, rather than a business expense.

As a follow-up to the October 2003 trip, Under Secretary and Director Jon W. Dudas led two delegations in 2004 for consultations with senior officials at China's patent, trademark, copyright, and other IP agencies. Our delegation also met with U.S. companies facing IP issues in China. The primary focus of these trips was to further the Administration's goals of improving the IP environment for U.S. companies doing business in China, and specifically of addressing widespread counterfeiting and piracy. We discussed several issues, including the need for improved criminal, civil, and administrative enforcement, the need for protecting copyrights over the Internet and China's accession to the WIPO Internet Treaties.

In January 2005, Under Secretary Dudas traveled to Beijing as part of a second Evans-led delegation. He was fortunate to be able to meet with Chinese Premier Wen Jiabao and Vice Premier Wu Yi to discuss concerns over China's enforcement of IPR of American businesses. Ambassador Randt also hosted the third roundtable on Intellectual Property Rights, which was attended more than 250 government officials and business and industry representatives from the USPTO, the European Union, Japan, and China's IP agencies. In addition to providing the luncheon keynote address during the January roundtable, Under Secretary Dudas announced the USPTO's new plans for IP technical assistance for Chinese IP–related agencies. He was pleased that the USPTO's offers of cooperative assistance were well received, and we are in the process of implementing these as well.

U.S.-China Joint Commission on Commerce and Trade (JCCT) Working Group on IPR

In an effort to address problems in China, the U.S. and China created a "working group on IPR" that resulted from the April 2004 session of U.S.-China Joint Commission on Commerce and Trade. We are pleased that Under Secretary Dudas co-chairs this working group with Deputy U.S. Trade Representative Josette Shiner.

Through the JCCT and other avenues, the U.S. hopes to continue to work with closely with China to improve the situation for U.S. rights holders. During the April 2004 session of the JCCT, China presented an action plan designed to address the piracy and counterfeiting problems faced by U.S. companies. Under the plan, China committed to: (1) significantly reduce IPR infringement levels; (2) issue a judicial interpretation for criminal enforcement of IPR cases by end of year; (3) conduct nation-wide enforcement campaigns; (4) ratify and implement the WIPO Internet Treaties as soon as possible, and (5) agree to establish an IPR working group under the JCCT. In line with the JCCT mandate, the working group will seek to ensure that China significantly reduces IPR infringement to levels consistent with standards required by WTO rules.

Challenges and Recommendations concerning China

While our trips to China have been well received, and we are pleased to note a continuing and increasing awareness among Chinese officials of the importance of IP protection and enforcement, we have not yet seen significant progress on most of the key issues. These issues include enhanced criminal enforcement, a deterrent administrative enforcement system, protecting copyrights over the Internet, and stopping the export of counterfeit goods. We are also interested in other developments, such as China's efforts to develop an IPR Strategic Plan for development of its IP assets, other industrial policy goals, legislative efforts to draft a Civil Code that may include IPR, and general rule of law efforts that could significantly affect the protection of IPR over the long run.

While we fully recognize that China needs to make drastic improvements in its IPR system to ensure that our right holders are fairly protected, we should not underestimate the steps that our businesses and government can take to reduce the risks of piracy and counterfeiting. The USPTO will continue working with small and medium-sized companies on how best to protect their valuable IP rights in China. One particular example is for companies to register all their trademarks promptly in China, especially their Chinese language trademarks. Given the fast pace of China's economic development and the huge volume of trademark applications in China, companies should file for their marks early in their marketing cycle.

Globalization means that competitors can retrieve information about products not yet introduced in their country from a U.S. company's web site. Counterfeiting and piracy also originates from employees, agents, or distributors who have taken confidential information to engage in a competing operation. China's practice regarding protection of trade secrets by former employees who have signed non-compete agreements is different from the United States. We will continue to educate companies on how best to protect their intellectual property rights.

It is especially important we encourage our industries to work with us and the other U.S. agencies involved in improving China's IP protection and enforcement environment by: urging the fair and transparent implementation of China's IPR system; fully exploiting this system; providing us with detailed information on its deficiencies in order to reduce future risks of such activities; and supporting our bilateral and multilateral efforts to reduce the impact of these problems.

The Global STOP Initiative

We are pleased to discuss with you the STOP Initiative, the most comprehensive intergovernmental agency initiative ever advanced to smash the criminal networks that traffic in fakes, stop trade in pirated and counterfeit goods at America's borders, block bogus goods around the world, and help

small businesses secure and enforce their rights in overseas markets. There are several important features of the STOP Initiative that I'll mention:

Hotline and Website

First, the USPTO participates heavily in this initiative by managing a hotline, 1-866-999-HALT, established by the Department of Commerce to help business protect their IPR at home and overseas. The goal of the hotline is to empower U.S. business to secure and enforce their IPR by providing them the information they need to secure their patents, copyright and trademarks, and to enforce these rights here in the U.S. and abroad.

Callers receive information from IP attorneys with regional expertise on how to secure patents, trademarks, and copyrights, and on the enforcement of these rights. Businesses and innovators now have access to a place to learn more about the risks of global piracy and counterfeiting and how to protect their IP rights in both individual countries and in multiple countries through international treaties. In addition, we have established a link from our USPTO website to www.stopfakes.gov on the Department of Commerce's website, which provides in depth detail of the STOP Initiative.

No Trade in Fakes Program

The Department of Commerce is in charge of another important component of the STOP Initiative, the no-trade-in-fakes program that is being developed in cooperation with the private sector. This is a voluntary, industry-driven set of guidelines and a corporate compliance program that participating companies will use to ensure their supply chains and retail networks are free of counterfeit or pirated goods.

Increasing and Communicating Enforcement

The STOP Initiative will raise the stakes for international IP thieves by more aggressively pursuing perpetrators of IP crimes and dismantling criminal enterprises. STOP also seeks to increase global awareness of the risks and consequences of IP crimes through public awareness campaigns, and creating and operating a website publicizing information about international criminal IP enforcement actions.

Building Coalitions

The ultimate success of the STOP Initiative involves building coalitions with many of our like-minded trading partners, such as Japan, the United Kingdom, and France, who have all recently launched similar initiatives. We are seeking to continue working with our partners in the G-8, Organization for Economic Cooperation and Development (OECD) and the Asia-Pacific Economic Cooperation (APEC) forum. Cooperation on new initiatives to improve the global intellectual property environment is essential to disrupting the operations of pirates and counterfeiters.

International Outreach

A delegation of U.S. officials from seven federal agencies, including myself, recently kicked-off our international outreach effort to promote STOP internationally. Last month we visited various capitals in Asia generating much interest and fruitful discussions. On each leg of the trip, U.S. officials shared information on our efforts to combat the theft of inventions, brands and ideas. This

first leg abroad is advancing our commitment by enlisting our trading partners in an aggressive, unified fight against intellectual property theft. Outreach to Asia will be followed by visits to other capitals later in the year, for example, next month we plan on visiting Europe. We have tentatively planned that countries receptive to cooperation on STOP will be invited to attend a meeting in Washington, D.C. (likely in the fall of 2005) designed to formalize their participation and finalize a work plan.

Future STOP Activities

The USPTO has several future planned activities supporting our initiatives under STOP. The first involves our public outreach efforts. In addition to our China-related workshops and seminars for 2005-2006, my staff will also be embarking on an educational road show to various cities in the United States to educate small- and medium-sized business on what IPR are, why they are important, and how to protect and enforce these rights domestically and internationally. The first of these workshops took place earlier this week in Salt Lake City, Utah, and already, we have found an enormous amount of interest in the program. We will replicate this program in other cities throughout several regions of the U.S. in the coming months.

We continue to work in WIPO to seek to simplify, streamline, and improve the cost efficiency of the trademark application process across borders to provide more efficient and less burdensome systems for right holders.

We will continue to work closely with the IP community, STOP team, and you to promote a legislative agenda that is designed to meet the huge challenge of combating piracy and counterfeiting. Tougher enforcement of our international trade laws is necessary for the growth of our economy and the creation of new jobs. In order to fully implement the STOP Initiative, it may be necessary to reassess current legislation.

Conclusion

Mr. Chairman, the requirements on the Department of Commerce and USPTO's expertise in the international arena have grown dramatically in the last few years. These demands will continue to increase in the next few years, along with our obligations to meet our core patent and trademark examination functions.

As we look to the future, however, let me conclude on a positive note. Although by all accounts counterfeiting and piracy appear to be growth "industries," there have been some recent successes in attacking the problem. Between 2001 and 2002, the software industry estimates that software piracy in Indonesia decreased from 89 percent to 68 percent. In South Africa, it fell from 63 percent to 36 percent. The motion picture industry has reported a decrease in piracy levels in Qatar from 30 percent in 2001 to 15 percent in 2002. In Bahrain, there have been dramatic and systemic improvements in IP protection and enforcement over the past few years. These include the signing of numerous international IP conventions and the virtual elimination of copyright piracy and counterfeiting in retail establishments.

There is some reason for optimism. I remain hopeful that with the continued support and partnership of the Subcommittee, we will be able to do even more to provide American businesses and entrepreneurs with the IP knowledge and protection they need. Clearly, in terms of the

economy and national security, much is at stake. That is why our dedicated team of experts will continue to work tirelessly to protect American products all around the globe.

Thank you very much.

PRIDE
MFG. CO., INC.

1050 E "H" HIGHWAY
LIBERTY, MO. 64068
TELEPHONE: (816) 781-6765
FAX: (816) 415-8044

Testimony at joint subcommittee hearing before the House Small Business Rural Enterprise, Agriculture and Technology Subcommittee and Tax, Finance and Exports Subcommittee.
"Does China Enact Barriers to Trade?" May 26th, 2005

My name is Tom Goodpasture – President, and owner of Pride Manufacturing Co., Inc.- a small machine shop located in Liberty, MO. In 2002 we purchased a minority of stock in a manufacturing firm in Ningbo ,China. The principle owner is a family member and Pride Mfg wanted to use this association primarily as a sales tool. It has been an interesting process that has given me a new insight into the China market. I have never been to China, but will be traveling there this fall on a Study Mission trip with the NTMA (National Tool and Machine Association).

The unlevel playing field for us as American manufacturers makes it impossible to compete. At Pride Mfg. our cost burden over wages, including benefits averages in excess of 35 %. In China there are no labor laws, no EPA laws, no OSHA laws, no health insurance, no retirement plans. The biggest benefit provided is buying the workers lunch.

I routinely talk to customers and representatives of large and small American manufacturers who feel the only way they can survive is to buy in China. At Pride, we purchased a $300,000.00 Robot Loaded CNC Lathe to do a job for Mercury Marine. The part cost was approximately $3.00; we were producing on the most up to date equipment and technology available and yielding under a 5% profit margin. We were 6 months into the project and the purchasing agent found that he could buy in China for 50 % and it was gone. Customers buying China are willing to accept the 5-10% or more scrap level, which has to be sorted, and quality controlled here. There is no way to recoup the loss, but they feel the competition

is "buying" China, so they must also. That rate of defect would not be allowed from a U.S. manufacturer. Many companies are starting their own plants or attempting to partner with Chinese firms to produce their products. Some succeed, many fail and there are many horror stories along the way. The common theme from my entire group of associates who have anything to do with China is. **"Regarding business, you cannot trust the Chinese".**

Why have we embraced the idea and monetarily forced US manufacturers to buy China to be competitive? I believe that China has made the wise choice to purchase their future in the world of manufacturing at our expense and demise. With all of the challenges of doing business with China, if the Chinese currency was correctly valued, I wonder how many would actively be pursuing services there? With that correct exchange rate, it is my belief that China could no longer be competitive in the world market. I do not believe the average Chinese shop operates nearly as efficiently or accurately as shops in the U.S. That is the major reason of my fall trip, to verify, or alter my opinion. With this undervalued exchange rate China is buying and we are either knowingly or blindly selling 100+ years of technology in a very short time. **China wins – we lose!**

About the time of Desert Storm I remember a huge controversy when an American Cutting Tool Company was found to have allowed one of their tools to get in the hands of a non-allies machine shop. That tool was found to be producing weaponry that could be used against us. I realize that the trade laws were different then, but should the idea of our security and technology protection be drastically different? Recently I made a list of what I consider to be top technology cutting tools and emailed it to an associate in China. I wanted to see what was available there. Every tool on my list was available on the open market in China, most at a cost with exchange rate of slightly less than they cost here. If they are in China, they could be anywhere.

The patent laws of America have been trashed. The Chinese have absolutely no loyalty to patent laws of America or any other business deal. They get their hands on a product, take it apart, reverse engineer it and bring it back on the market at a greatly reduced price. Some of our customers and associates with patented products have found that there is apparently no recourse or, in many cases, even trace ability to these acts of piracy.

Recently, China was involved in manipulation of our steel prices and availability by buying large amounts of scrap steel. It's a win-win for them. They need the steel scrap for their production and at the same time our material prices are being driven up. This situation created a material shortage, making us less competitive in the world market. It equates to *allowing penny collectors to control the value of our dollar*. The price of steel being tied to the scrap steel price and availability is wrong and needs to be re-evaluated. We must re- build our ability to produce steel and other raw materials. I was at General Dynamics Land System Division in Detroit on a sales call a few weeks ago. GD makes the armored vehicles for our military. The procurement specialist told me that they are having a difficult time getting armor steel. In one instance he had to request that a vendor machine a part that required ¾" thick material out of 3 inch thick material in order to make the required delivery. We are paying in many cases two – three times what we were paying a year ago. Often the required materials are not available or have very long lead times.

I stated earlier that I do not believe that China, on a level playing field, can be competitive. I also believe, given time that will change. At the rate we are handing off all we know that process can go very quickly. The longer the exchange rate can be artificially deflated, the bigger the jump-start. I believe in fair trade, but let's keep it fair.

I have always considered myself very fortunate to be in the manufacturing industry. I find myself on a day-to-day basis not only loving what I do, but passionate about the industry I serve. If profits are driven out of manufacturing, then it goes into survival mode.

We can no longer expand technology, properly train new craftsman and maintain our facilities. Eventually we will lose what has made us strong. I believe the country that has the highest ability to manufacture will be the world leader. We have for a long time held that position, but we are quickly becoming a service society and more concerned with the trade than the make. Why would we give our manufacturing capabilities away to a country that we cannot even trust in a business deal? **China wins – we lose!**

Thank you

President of Alligator Records

Before the

United States House of Representatives

Committee on Small Business

Subcommittee on Rural Enterprise, Agricultural and Techonology

And the

Subcommittee on Tax, Finance and Exports

Joint Subcommittee Hearing

On

"Does China Enact Barriers to Fair Trade

May 26, 2005

Mr. Chairmen and Members of the Subcommittees, my name is Bruce Iglauer. I would like to thank you for asking me to testify today. I founded Alligator Records myself, 34 years ago, in Chicago, the world capital of the blues. It was fueled by my passion for the blues, a uniquely American music full of emotion and history. I founded Alligator in a one-room apartment with only $2500 and almost no experience in the record business. I built my artist roster from among the blues men and women who performed in the little clubs in the South and West Side Chicago African-American ghettos. Over the years, with a roster of extraordinary talent, Alligator has built a catalog of 230 albums, recording blues artists from all over the USA. I'm very proud of the fact that literally hundreds of musicians and their families have been able to survive and thrive, as a result of the work that Alligator has done to bring them to a worldwide audience. After 34 years, royalties from the sales our recordings are not only supporting the artists, but their children and grandchildren.

The music that Alligator records is not pop music—it will never be embraced by the multi-national companies that market the hits. Alligator is like literally hundreds of other small, independent labels across the country. It is dedicated to recording and preserving music of great cultural importance. My friends who own other labels record jazz, traditional folk music, classical, spoken word, alternative country, gospel, bluegrass and ethnic music. Because there is an audience for this music, but not a huge one, it has become the province of the independent labels like mine. No one in the independent record business is getting rich, but because we've developed a core audience around the world who love our genres of music, we're able to survive and continue recording this valuable music that we love. Unfortunately, the survival of companies like mine is being threatened today on a worldwide basis by piracy.

My company sells its recordings all over the world. International sales are an important part of our business.

Thank you for the opportunity to appear today to discuss problems facing small American businesses in China's and for permitting me to describe the widespread piracy of our music sound recordings in China. Such piracy damages our business and it hurts our employees. I have submitted my longer written testimony for the record.

The business of making sound recordings –composing the music and lyrics, singing and recording the song, producing, manufacturing, marketing, distributing and retailing the finished product – is a business that Americans do extremely well. Our recordings recordings are sold all over the world. These sales add significantly to our nation's trade balance and ultimately to our national welfare. Conversely, our nation's welfare is reduced and our composers, artists and all the employees of record companies—small and large—suffer when foreign governments permit our recordings to pirated in their countries.

When it comes to ripping off American sound recordings, China is one of the worst. The magnitude of record piracy there eclipses any other country. This has been a point of conflict between our countries for years.

I understand that China has made some limited progress in China terms of improving its anti-piracy laws; it runs lots of "raids" and seizes lots of products. But more deterrent penalties are almost never imposed.

China's organized crime gangs, the manufacturers and distributors behind the face of poor street vendors, consider these periodic seizures and fines as a mere "cost of doing business." Indeed, even with the destruction of product and the payment of a fine, it is still a highly profitable business. And, in any case, the street vendors are often is back on the street the following day.

Until China imposes truly deterrent penalties for copyright piracy, nothing is really going to change for US companies—small or large—and China will remain in violation of its various commitments it has made to the United States to effectively address this problem. The challenge for American industry and the US Government is how to get the Chinese to live up to these promises.

Before I close, I want to say a word about Russia, which is fast becoming the next China. Lawlessness, physical danger, and corruption are part of the daily challenges we face in trying to protect our rights in Russia. These are much wors in Russia than in China.

Russia is producing far more sound recordings than needed and exporting them all over the world, ruining my industry's markets in those countries as well. In addition, Russia is tolerating one of the world's worst online music pirates, an entity named "Allofmp3.com" which I describe in detail in my written testimony.

But we have a unique opportunity with Russia. They very much wish to join the World Trade Organization, but they must negotiate their way in. Our government has the ability to veto Russia's WTO accession. In addition, the Congress must approve PNTR—permanent normal trade relations—with Russia as a part of this process. I urge you and the US Administration, not to approve Russia's accession to the WTO—nor PNTR—until Russia has adequate addressed its massive runaway piracy. Otherwise our leverage to effect change there is lost.

The US Government must press China and Russia harder to strengthen its anti-piracy enforcement regime. The current systems in these countries do not work. Unless the US uses each and every option available to it, we will continue to face the same situation we do today for the foreseeable future—overwhelmingly pirate markets and lost opportunities for legitimate US companies.

Thank you.

Statement of Al Lubrano
President, Technical Materials, Inc.
and
President, Rhode Island Manufacturers Association

On Behalf of
The National Association of Manufacturers

Before
The House Small Business
Rural Enterprises, Agriculture and Technology Subcommittee
and
Tax, Finance and Exports Subcommittee

"Does China Enact Barriers to Fair Trade?"

May 27, 2005

Good afternoon Mr. Chairman and members of the Committee. Thank you for giving me the opportunity to participate in this panel. My name is Al Lubrano, and I am president of Technical Materials Inc., a small manufacturer of engineered materials systems primarily for the electronics industries. In addition to other markets we serve, we are also part of the auto industry supply chain and sell to many of the major auto manufacturers' biggest suppliers. We are located in Lincoln, Rhode Island. I am also the President of the Rhode Island Manufacturers Association which represents over two hundred companies in our state. I am pleased to testify today on behalf of the National Association of Manufacturers (NAM) at this hearing regarding our trading relationship with China and barriers to fair trade that might be enacted by China.

The National Association of Manufacturers is the nation's largest industry trade association, representing small and large manufacturers in every industrial sector and in all 50 states. As member of the NAM's China Policy Subcommittee, I participated in the development of our 2005 China Trade Agenda that included vigorous participation from both small and large NAM member companies. The fact that we developed a separate China policy is an indication of its importance to NAM members. The entire agenda is available at www.nam.org/trade.

No other trade subject comes close to commanding the attention that China is getting from NAM companies. China is simultaneously the greatest concern of many of our import-competing members and the fastest-growing global market for many companies that operate internationally and for exporters large and small. The fastest growing economy in the world, China has emerged within a short span of two decades as a strong international competitor in a wide range of manufactured products and a key market for U.S manufactured exports.

More recently, China has also gained prominence as a huge consumer of industrial raw materials, with demand so large that it has significantly boosted world prices of important inputs such as steel and copper scrap, iron ore and coke used in steel production. It is not surprising then, that U.S. manufacturers pay close attention to China's trade and economic policies, and how they affect not only bilateral trade and investment, but the entire global marketplace.

Trade generally, and with China specifically, has to be put in the context of a recovery in many sectors of the U.S. manufacturing economy over the past 18 months. But, despite this recovery, a number of manufacturing sectors that have borne the brunt of China's emergence as an industrial power have continued to lose revenue and jobs. Thus the China challenge not only continues to be at the center of the NAM's trade agenda, but also is central to how U.S. manufacturing defines its own future.

There is no doubt that China exerts the largest bilateral trade effect on manufacturing. In 2004, we had a trade deficit in manufactured goods of $490 billion. Two-thirds of that total is with Asia and 34%, or $166 billion, is with China. (See Chart 1 attached.) By way of comparison, $166 billion is six and one half times larger than our deficit with Mexico and three and a half times larger than our entire NAFTA deficit, even though our two-way trade with China is one-third as large as our two-way trade with NAFTA.

The surge in Chinese imports has been a serious problem in many sectors and anecdotal evidence indicates that there are underlying factors that we cannot afford to ignore. In addition, Chinese production has exerted a downward pressure on prices at a time when costs are rising. Companies cannot pass on those costs because of the so-called "China price."

The NAM seeks a positive and balanced trading relationship with China that reflects market forces as closely as possible. China as a participant in the global market is a fact of life. At some point, China will become the world's second largest economy. We as American manufacturers must take advantage of the opportunities offered by the large, emerging market in China, as well as be adaptive and innovative to maintain our competitiveness globally.

In this vein, it is important to note that while the rapidly-rising trade imbalance with China is a growing factor affecting U.S. manufacturing production and employment, it is not the only factor. Domestic costs like health care and litigation costs, slowly-recovering U.S. exports, dollar overvaluation with other Asian currencies and regulatory pressures are also at work. Problems with China should not be used as an excuse for not tackling the other problems. Nonetheless, the China currency situation, subsidization and other factors feeding our deficit with China must be addressed.

China's emergence as a leading world economy has meant significant new opportunities for many NAM members, including increased export and investment. However, these opportunities are not fully realized by all NAM members. These companies see prices of Chinese products so low that it is difficult for them to see how they can compete. Others see their customers moving to China and cannot find new ones to replace them.

I have seen this in my own company. As I said, we are a small manufacturer of engineered materials systems with about 200 employees in Lincoln, Rhode Island. As a result of fierce Chinese competition, fueled partially by the undervalued yuan and possible other unfair trade practices, I have seen many of our customers lose their business because their customers' customers have sought refuge in one of two strategies: either outright moving production to China or forcing purchasing from lower-cost Chinese manufacturers. Some of our customers tell us that their customers will only pay the "Chinese price."

On the other hand, we are not without distinct advantages in U.S. production. Right now, we are selling high technology precious-metal-plated material systems to stamping companies in China that are unable to procure the high-quality product they need from a Chinese or other regional supplier and therefore are buying from us. Our technology and innovation have kept us ahead of the game with some of our customers, but it is not going to be enough if we don't address the problems in our trade with China and soon.

The NAM believes that trade must be market-based, without government interference. In China, we are seeing problems with currency undervaluation, the possible wide spread subsidization of industry and the failure to implement its responsibilities under the WTO to protect intellectual property and prevent product counterfeiting and piracy.

Along these lines, the NAM is looking for ways to address these issues, working within established trade rules and our WTO and other international commitments. It is essential that we have a rules-based system that is adhered to and enforced.

Pressing for a Revaluation of the Undervalued Yuan

China devalued its currency by about 30 percent in 1994 and has maintained that value for the last eleven years -- despite a huge increase in production capability, productivity, quality, production range, foreign direct investment inflows and other factors that would normally be expected to cause a currency to appreciate. Economists estimate that the yuan is undervalued by as much as 40 percent. This undervaluation effectively taxes U.S. exports and enables artificially cheap imports from China, fueling the growing bilateral trade deficit.

Would a considerably stronger Chinese yuan have beneficial effects? Many NAM member companies have indicated that a 20 percent or more price shift would change the competitive situation dramatically. Others say their problems go beyond that. Some commentators state that Chinese wages are so low that no amount of appreciation would make a difference. Labor costs, however, are only one factor in the production process. In fact, production worker wages and benefits are only 11 percent of the cost of U.S. manufactured goods, on average. An exchange rate reflecting market forces would shift the competitive equation so that some Chinese industries would remain extremely competitive, while others would find their artificial advantage diluted. U.S exports would also grow more rapidly, helping to bring about a more sustainable trade position.

In 2004, the bilateral trade deficit with China was about $160 billion, the largest with any country and, at growth rates of the last few years, will almost triple in five years. The latest data show the deficit growing even more rapidly. Data for the first quarter of 2005 indicate a 40% increase in the U.S. deficit with China over the same period in 2004. If this rate of growth continues, our trade deficit with China could reach an astonishing $225 billion for the full year. (See Chart 2 attached.) Furthermore, the undervalued yuan makes foreign investment in productive capacity in China cheaper and more attractive, thus artificially encouraging the movement of investment to China.

The degree of upward pressure that the yuan would feel is amply indicated in the amount of reserves that the Chinese government has to accumulate to maintain its artificial peg. Reserves grew a remarkable $200 billion last year – to a total accumulation of $660 billion, or 40 percent of China's entire annual output of goods and services. That is an enormous amount to have in Treasury securities earning a couple of percentage points when China could be using those funds internally to build up its economic infrastructure and stimulate domestic-led growth. In turn, this could be expected to stimulate the purchase of U.S.-made goods by Chinese businesses and consumers.

Yet China has no choice but to continue this huge reserve buildup so long as it insists on maintaining a sharply undervalued currency. This practice also exacerbates our trade deficit because, while we buy from China, to a great degree, instead of using that money to buy our goods and services, China is buying our Treasury bills in order to keep its currency cheap and its exports under-priced.

It should be noted that, while a currency peg *per se* does not contravene International Monetary Fund (IMF) requirements, IMF Article IV proscribes "manipulation of exchange rates to gain unfair competitive advantage over other members - and this includes protracted large-scale intervention in one direction in the exchange market." With foreign currency reserves of $660 billion, China's action is clearly incompatible with the intent of IMF Article IV. It is also in violation of its obligations in the WTO to avoid frustrating trade liberalization through exchange rate action and to avoid subsidization of exports or impairment of trade benefits.

It is important to note that there has been a significant change in the Administration's tone and message to the Chinese government on their currency practices. Recently, Secretary Snow and other Treasury officials began indicating that China had made sufficient progress in reforms to its financial and banking sectors to allow them to make a move toward currency flexibility now. In the Treasury Department's semiannual report delivered to Congress last week, they stated that "China is now ready and should move without delay in a manner and magnitude that is sufficiently reflective of underlying market conditions." In Secretary Snow's remarks and in the report, China has been put on notice that "If current trends continue without substantial alteration, China's policies will likely meet the statute's technical requirements for designation."

While the NAM had been calling on Treasury to cite China for currency manipulation in this last report and expressed its disappointment that this did not happen, this was by far the strongest Treasury Report language on China yet and, as NAM President John Engler said, "This [the Treasury Report] marks the end of a period of quiet diplomacy and technical assistance. The language is about as hard-hitting as it can be without actually citing China." We are encouraged that China has been put on notice that the horizon is not limitless and that the timeframe is short for them to take positive steps to adjust the value of the yuan to more closely align to market fundamentals.

In this regard, we would also like to recognize several additional important point made by Secretary Snow, one that the NAM has been making for some time: that any step taken by China in this regard must be a significant one, one in Secretary Snow's words that would "get their currency into alignment with underlying market forces."

A slight shift in the peg or a marginal widening of the band will not be sufficient to make any meaningful difference. It will not do anything to address the problems created on either side of the trading relationship by China's currency peg. It won't translate into a more realistic price for Chinese imports into the United States or in global markets and it won't provide sufficient change in the currency to stem the flow of speculative funds or "hot money" into China – in fact it may only increase it, as has been cautioned by Morris Goldstein and Nick Lardy of the Institute for International Economics – and it won't make much progress toward the goal of a market-determined currency that will give China the necessary tools to engage in meaningful monetary policy.

The other important point made by Secretary Snow is the detrimental effect China's currency policy is having on its Asian neighbors. He said that "China's rigid currency regime has become highly distortionary. Concerns of competitiveness also constrain neighboring economies in their adoption of more flexible exchange policies." The NAM has long held the view that eliminating the severely undervalued yuan is essential to creating more balanced and sustainable trade flows. A revaluation of the yuan to reflect underlying economic fundamentals would create more favorable conditions within Asia, enabling other countries to free their currencies to better reflect market conditions. These multiple currency misalignments artificially depress U.S. exports to a substantial portion of the world and reduce the competitiveness of U.S.-based manufacturing in the U.S. market.

The Chinese currency is the key, not just because of the huge bilateral imbalance, but also because other Asian countries are looking over their shoulders at Chinese competition and are reluctant to allow their currencies to move up against China's. China could take several actions immediately, including un-pegging the yuan from the dollar and relating it instead to a basket of major trading partner currencies, establishing a large band around its current rate, and moving its peg upward.

The NAM also welcomes the appointment of Treasury Special Envoy to China Olin Wethington as a measure that reinforces the Administration's determination to press the Chinese to act on their currency. Building on the excellent work by his predecessor and first envoy to China, Ambassador Paul Speltz, the NAM is looking forward to working as closely with Mr. Wethington.

The NAM urges the Administration to work with China and other countries to resolve this problem and thus avoid the dangers that misaligned exchange rates pose to the United States, China, Asia and the global financial system. We also believe the Treasury Department should urge the International Monetary Fund to exercise its surveillance authority over exchange rates. We hope that these efforts will result in positive action but, if they do not, the IMF should be prepared to cite China under Article IV if progress is not made in consultations.

Last month, the introduction of Schumer-Graham legislation in the Senate, which the NAM opposed, indicated the level of frustration with the Chinese failure to take steps to bring their currency closer to its market value. I should note that the NAM opposed the amendment not because we do not believe this is an issue of critical importance. In fact, we were the first organization to raise this issue and we continue to make it a top priority, but any action taken must be done within WTO rules.

Protectionism must be avoided. We cannot reverse the open trading system that has been such a source of growth for the United States and the rest of the world, and risk a downward cycle of global trade deterioration. We must pursue approaches relying on market mechanisms and take actions consistent with the rules-based trade system.

Applying Countervailing Duty Laws to China

There is no question that the Chinese currency is seriously undervalued and is having a major effect on U.S. bilateral trade and on the trade of other nations as well. However, the undervalued currency is not the only concern with China, and I would like to address some of the other issues as well.

As President of the Rhode Island Manufacturers Association (RIMA), I hear from a number of Rhode Island companies that when they try to bid for a contract against Chinese manufacturers of the same product, the Chinese price is below their cost of raw materials. This raises concerns that China's industries may benefit from a wide array of government policies that, in effect, result in subsidies. These include: government bank lending to enterprises without creditworthiness, export-based tax incentives, and the discriminatory application of tax rates and rebates.

The subsidization of manufacturing by the Chinese government extends beyond what might be considered normal bounds to even include the acquisition of raw materials. A fellow NAM member in the copper industry tells us that exports of copper and brass scrap to China have increased about 50% a year for several years, driven in large part by a special subsidy of 30% of the VAT tax applied by the Chinese government to imports of scrap. This subsidy is given to the scrap consumer to invest in upgrading facilities. This subsidy amounts to about 7 cents a pound of the copper content in a market where the successful bidder may be determined by a margin of a quarter cent.

The WTO Subsidies and Countervailing Measures (SCM) agreement allows countervailing import duties to offset such subsidies. In fact, China's WTO accession agreement specifically outlines the process for assessing subsidies in China. A good deal of time was spent by former USTR Barshefsky negotiating this language.

In Beijing in September 2003, former Commerce Secretary Evans said, "There is simply no valid economic justification for many of the loans currently being extended to unprofitable businesses in China. Non-performing loans to state-run companies are a form of government subsidy." However, since 1984, the Commerce Department has not applied countervailing duties against imports from non-market economy countries such as China.

In developing NAM's 2005 Trade and China Agendas, what emerged as very important to many of our members, especially small companies, is the need for greater focus on trade enforcement. Many companies said that, while they supported trade liberalization and recognized the general benefits, they did not see the follow-up in enforcing agreements that were negotiated. The policy that does not permit the application of countervailing duties to non-market economies, an action that is entirely consistent within the WTO generally and with regard to China's WTO accession agreement specifically, is a glaring example of this lack of enforcement.

The NAM supports reversal of the Commerce Department's 1984 decision in light of the SCM Agreement and the terms of China's accession to the WTO, and supports legislation that was introduced in the House by Congressmen English and Davis (H.R.1216) and in the Senate by Senators Collins and Bayh (S.593). We hope that members of the subcommittees will look favorably on this legislation.

With regard to the bill introduced by Congressmen Hunter and Ryan (H.R. 1498) that would make currency a countervailable subsidy, the NAM is currently working this through our policy process and we have not yet taken a position on the legislation.

Ending Product Counterfeiting and Copyright Piracy

Next to the exchange rate, the most serious problem NAM members have with China is its failure to curb intellectual property theft – particularly copyright piracy and product counterfeiting. I have close personal experience with this problem. A company with whom we do business, one of the leaders in the production of very high tech equipment, whose president is a close colleague of mine told me a couple of years ago that they were moving a portion of their production to China and that we should make the same move, that "we had to be there."

When I talked with him a year later about the project, he told me that they were still finishing construction on their plant in China when another, identical plant was put up only one-half mile away by a Chinese company that began producing his product. He told me, "Thank God you didn't go there."

China has become the world's epicenter of counterfeiting, costing U.S. companies billions of dollars and thousands of legitimate jobs, and threatening consumer health and safety. Because of this, our members have pressed us to do more, and the NAM, with the U.S. Chamber of Commerce currently co-chairs the Coalition Against Counterfeiting and Piracy (CACP).

Despite bilateral and multilateral agreements with China to protect intellectual property rights, China's record of enforcement has been inadequate and seriously flawed. China has been taking positive steps; the laws are better, and there at least is a higher degree of official attention to the enforcement of those laws at the central government level. But it is enforcement that counts and China seriously fails in that regard. It is each WTO member's obligation to provide effective protection for intellectual property.

In spite of these official efforts, it is the general view that product and trademark counterfeiting and copyright piracy is not getting better, but worse. An inability or unwillingness to protect intellectual property strikes at the core of American competitiveness. If the products of our innovation and research and development are stolen, there will be little we can do to maintain our industrial base.

The NAM, in its submission to the USTR on the Special 301 out-of-cycle review of China, recommended that the Administration designate China a Priority Foreign Country and commence development of a WTO case, ideally in conjunction with the EU, Canada, Japan and countries whose companies are also suffering from what NAM President John Engler calls China's "grand larceny on a massive scale."

We need to see the law enforced, with counterfeiters thrown in jail and the volume of counterfeiting significantly reduced. It is time to deal decisively with this problem and we welcome the amount of attention this problem is receiving from the Administration. USTR is engaging China on multiple levels and is giving IPR high priority at the upcoming Joint Commission on Commerce and Trade (JCCT) meeting with China this summer.

Addressing Standards and Regulatory Market Access Barriers

In foreign markets around the world, standards and technical regulations as well as procedures established for conformity assessment have emerged as increasingly important market access barriers for U.S. manufacturers. In China we have seen disturbing developments that standards and technical requirements are being deliberately used to limit market access of foreign products and give Chinese producers unfair advantage. And these concerns need more attention.

China has been active in promoting standards in a number of information technology areas, for example, wireless encryption standards (WAPI), radio frequency identification tagging (RFID), Internet protocols and its own microprocessors. This indicates that the Chinese government has a longer-term plan to encourage the use of Chinese products and technology, particularly in high-technology sectors where the U.S. has competitive advantages, by gaining wide acceptance of domestically-developed standards.

U.S. manufacturers also face other market-access problems resulting from technical and regulatory requirements established by government authorities, and from costly and burdensome conformity assessment procedures. The process for approving new chemical products, for examples, is slow and unpredictable. Duplicate testing to meet overlapping technical requirements are common in a wide range of products, including medical equipment, personal care products, mobile phones and consumer electronic products.

We also hear frequent complaints about the application of requirements for a "China Compulsory Certification" (CCC) mark on 130 categories of products, such as appliances, electric motors and machinery, and information technology equipment. Only Chinese companies are authorized to certify conformity to the standards, and inspection of foreign factories is required. U.S. testing companies, such as Underwriters Laboratories and Intertek, cannot provide these services in China. The CCC process is costly, time-consuming and complicated, particularly for small manufacturers and producers of components.

As part of its WTO obligations, China has become a party to the WTO Technical Barriers to Trade (TBT) Agreement, which establishes disciplines aimed at preventing countries from using standards and technical requirements as trade barriers. The U.S. Government needs to work with the business community to ensure that China lives up to both the letter and spirit of this agreement and its commitments to open the Chinese market to foreign products and companies. We are concerned that China is not doing enough to meet is obligations in this area.

Enhancing Export Promotion to China

In looking for positive ways to alleviate this imbalance, promoting the more rapid growth of U.S. exports to China certainly should be emphasized. The NAM believes there is substantial potential for Chinese economic growth to lead to a corresponding growth in the U.S. manufacturing economy. But that potential is far from realization. Of the $560 billion of goods China imported in 2004, only 8 percent were from the United States, including agricultural products. In contrast, the European Union (EU) and Japan have been significantly more successful selling into the Chinese market. (See Chart 3 attached.)

Many manufacturers are taking advantage of China's rapid economic growth to sell more of their products there. In fact, for some member companies, China is their most important foreign market for increasing export sales. However, China remains a difficult place to do business and small and medium-sized companies, even those successful in other foreign markets, often have difficulty entering the Chinese market and developing profitable business relationships.

To help U.S. manufacturers reach their export potential in China, a new and greatly expanded export promotion initiative is needed. Current U.S. Government export promotion programs offer useful assistance but are not on the scale needed to make a sufficient difference in overall export trends. The U.S. Government and private sector must work together to launch a more ambitious program that provides more on-the-ground assistance in China and more trade outreach to potential U.S. exporters. A complete outline of NAM recommendations for this program can be found in the 2005 NAM China Trade Agenda which can be found at: www.nam.org/trade. Our goal should be to achieve at least one-third growth in our exports to China each year. This would triple our exports in four years and quadruple them in five. To implement a program of this scale, the NAM will seek to obtain a doubling of the Commerce Department's China-specific trade promotion budget for FY2006.

Conclusion

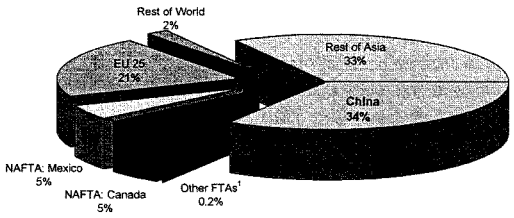
Mr. Chairman, I want to reiterate that the NAM wants a healthy, vibrant trade relationship with China that provides benefits to both our countries. During its three years of WTO membership, China has made progress in opening markets and adhering to international rules, but the benefits of the relationship still remain heavily one-sided in China's favor. Manufacturers continue to face an unlevel playing field that limits U.S. exports to China and gives Chinese products unfair advantages in the United States.

The issues I have outlined today are having a serious and negative effect on manufacturing in this country. We do not have a decade to solve these problems. It is essential that America maintain a strong manufacturing base, while at the same time maintaining a consensus for free trade.

Many U.S. manufacturers can and will deal with the fact of China's low wages and lack of worker benefits through innovation and technology. But as we open markets around the world to U.S. exports, we must also make sure that our trading partners, especially our most significant ones, are living up to their commitments both bilateral and multilateral through the WTO. Trade enforcement must be a priority within the U.S. government in order to ensure that American companies are given a fair chance to compete both at home and in the global marketplace. We look to the Administration and Congress to see to it that China plays by the rules and the system works.

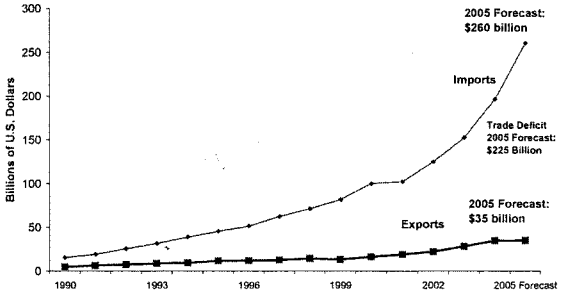
Thank you, Mr. Chairman.

Chart 1: U.S. Manufacturing Trade Deficit, 2004



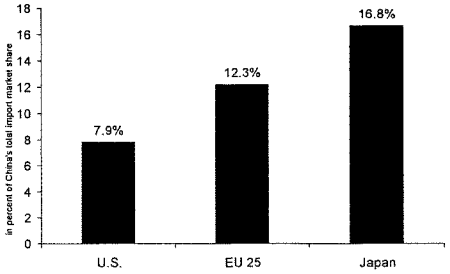
Source: U.S. International Trade Commission and NAM calculations based on NAICs codes 31-33.
1/ Other FTAs include Chile, Israel, Jordan and Singapore

Chart 2: U.S. Trade with China
1990 - 2005 Forecast



Source: Census Bureau , U.S. Department of Commerce

Chart 3: Foreign Share of China's Import Market 2004:
Japan, EU-25 and U.S.



Source: World Trade Atlas

Presentation to the House Committee on Small Business

May 26th, 2005

The Rape of American Manufacturing

In an article published in the Washington Times, Arnold Beichman – a Hoover Institution research fellow – made the following statement:

" The huge Communist Chinese mainland, government and people, is guilty of committing grand larceny on a scale only comparable in contemporary history to the expropriation of private property during the Nazi and Bolshevik revolutions"

If one has any doubts about the veracity of Mr. Beichman's statement, one only needs to educate themselves in the details of the drama that is playing itself out on your watch. Our relatively small company of 350 employees, the Thomas G. Faria Corporation, is one of the vast multitude of US manufacturers whose products are being copied with impunity by the Chinese. We produce engine-monitoring instrumentation including such products as tachometers, speedometers, fuel, volt, and engine temperature gauges for a wide variety of end products and customers. The level of technology incorporated in these devices ranges from relatively simple to quite sophisticated. During our history we have supplied such well-known companies as Ford, Chrysler, Caterpillar, and Harley Davidson. We are currently the largest supplier of instrumentation to the marine industry and the sole supplier of every instrument panel installed in 100% of the Humvees now serving in IRAQ and around the world.

The marine industry is represented here in Washington by the NMMA, the National Marine Manufacturer's Association that represents over 1500 corporations and businesses. I sit on their Board of Directors. The marine industry supplies the products that provide a boating experience to over 72 million Americans annually on the thirteen to fourteen million boats that are registered in the United States. This industry also contributes over thirty billion dollars a year to the nation's economy as well as over seven billion dollars in wages. It is twice the size of the cruise ship industry. While my company services multiple marketplaces, I cite these facts about the marine industry because it was one of the large US marine conglomerates that was approached by the Chinese with an offer to sell identical counterfeits of our

products at approximately one third of our average sales price. In addition, this is an industry that is rife with opportunity for the counterfeiters to steal more American jobs and technology.

The sad fact is that there is almost no area of American manufacturing that is not exposed to Chinese theft and up until now there is little to nothing that is being done about it by our government. In fact, our government in an indirect way has reinforced this unethical behavior by supporting the admission of this country of minimal business ethics to the WTO. A little over 50 years ago, manufacturing provided 42 % of the jobs in the United States. Today, that number is closing in on 10% and it is dropping. A significant driver of this statistic is the number of jobs that have been lost to counterfeiting of American products. The supervisor of my shipping department once worked for an American company that was founded in 1847. Not so many years ago the company employed 2000 people. In the 1980's, the Pacific Rim began a systematic program of copying their catalogs and products. Today the company is no longer in existence.

I know there are some among us who have countered that this is not a problem because we are replacing these manufacturing jobs with service jobs. What I don't understand is how a $22 an hour job on average can be equated to an $8 an hour job at WalMart – our nations largest retailer. WalMart by the way, if it were a nation, would be China's 6th largest trading partner.

There is more at issue here than just economics, there is a real threat to public safety. The counterfeit gauge that is shown in exhibit #1, which is now in the possession of the Secretary of Commerce's office, is not accurate. I assume that we all would be appalled if we found out that a half dozen troops in a Hummvee were shot and killed because their engine failed at a time of crises due to inaccurate instruments in the vehicle that failed to warn them of an impending engine failure at a most inopportune time. I trust that perhaps one or more of you might own a boat. If you do, you might be sensitive to the prospect of coming through a dangerous breakwater only to have your engine run out of fuel due to an inaccurate fuel gauge.

Over a year ago a company just down the road from us, Pfizer Inc., received a complaint from one of its Lipitor customers that in her recent prescription the pills tasted strange. After laboratory analysis it was determined that the pills were counterfeited. This revelation led to the removal of over sixteen

million doses of the drug from pharmacy shelves around the country. Virtually any popular medication is a target. If any of you take a prescription drug you are a potential victim. I have attached a copy of a publication by the National Association of Boards of Pharmacy (exhibit # 2) that lists drugs susceptible to counterfeiting. I would encourage you to read it.

The scope of the unethical activities of these pirates appears to be limitless. In addition to copying other company's products, they are aggressive in taking steps within their governmental infrastructure to steal trademark's, avoid establishment of a legal presence, engage in activities to disallow patents and even use the threat of violence to protect their ill gotten market position selling counterfeit products in countries around the world. I had one of our sales representatives had his own life, as well as his family's lives, threatened if we interfered with the sales of counterfeits of our products in Columbia.

The Chinese Government has disallowed Pfizer's patent for Viagra. One of the requirements's for gaining trademark registration in China is that you must have a "well know mark". China recently determined that "Toyota" was not a well-known mark. An individual named Ma Zhongbo in China is attempting to register out trademark as we sit here (see exhibit # 3). Some might question why the Chinese government seems to be complacent, or often illogical, in their determinations. Perhaps some of the reason for this lies in the fact that the government has a vested interest in the economic gain to be realized through unethical behavior. A business associate of mine who has been in the plant that is counterfeiting our product indicated to me that the Managing Director of the factory is the head of the local Chinese Communist Party and the facility is government owned. I have been told that this is not an unusual set of circumstances and is more the rule than the exception. Given these facts I am not surprised that enforcement is difficult to obtain and punishment is tokenism at best. After all, given the facts, are we not asking the government to actually punish itself given the relationship it has with many of these counterfeiters? When was the last time you asked your child, after committing an improper act, to punish himself or herself and be repentant and they actually did so. Have we really become that naive?

About 5 months ago I testified before the US China Commission. My recommendations to the Commission included the initiation of a case before

the WTO based upon the failure of China to meet the requirements of WTO member economies. Those requirements include laws for the protection of intellectual property and the enforcement and imposition of penalties for noncompliance. These requirements have not been met.
In a report released on March 25th of this year, the Commission has in fact recommended that disputes be filed by the United States in the WTO against China and that a 25% across the board tariff be established on Chinese produced products sold in this country. It is encouraging that a government entity is actually stepping up to the plate with a firm, concise, recommendation to take action.

I am not an economist or a necessarily astute student of international political equations. However, as with many issues in life and as a businessperson, I see a problem with retaliatory actions taken by us that could result in a number of counteractions by the Chinese. We are all painfully aware of the huge budgetary deficits and national debt that exists. A painful reality is that last year China held the position of the second largest foreign holder of US Treasury notes, second only to Japan. In addition, China had a net increase in US holdings for the year whereas Japan, the largest foreign holder, had a net decrease in holdings. Recently, a comment by South Korea that they might shift some of their investment to the EURO sent our stock market into an immediate tailspin. The panic subsided only after a clarification of South Korea's position was issued. What would happen if the second largest foreign holder of our national debt decided to do move away from the dollar? Seems like a serious dilemma to me.

In any event, the situation facing US manufacturers such as us is daunting. We are faced with competition whose labor costs them an average of 65 cents an hour, far less regulatory complexity and a cooperative governmental alliance. We cannot stop competition. However, we are faced with unfair competition from an international player who doesn't play by the rules – at least not the WTO's rules or their own government's. Ironically, they often do play by the rules of law in the US, which often favor their rights over our own citizen's. At times our own government appears to be disengaged in any firm resolve to address this problem.

A quote that I have used before but keeps ringing in my ears is a statement by the former Chairman of the Sony Corporation, Akio Morita. In a speech to a group of high level business executives he said:

" A world power that loses its manufacturing capacity will cease to be a world power"

I hope that his prophecy does not become an epitaph for the tombstone of American manufacturing.

Testimony

presented to the

Joint Subcommittees

of the Small Business Committee

by

Thomas Stallings

on behalf of the National Cotton Council of America

Does China Enact Barriers to Fair Trade?

May 26, 2005

Mr. Chairman, thank you and the members of the sub-committees for inviting me to discuss trade with China. I especially appreciate the assistance provided by Mr. Barrow and his staff. My name is Thomas Stallings. I am a cotton producer and the owner of Funston Gin Company and Funston Warehouse in southwest Georgia. I serve as a member of the Board of Directors of the National Cotton Council of America.

The National Cotton Council is the central organization of the United States cotton industry. Its members include producers, ginners, cottonseed handlers, merchants, cooperatives, warehousemen and textile manufacturers. While a majority of the industry is concentrated in 17 cotton-producing states, stretching from the Carolinas to California, the downstream manufacturers of cotton apparel and home furnishings are located in virtually every state.

The industry and its suppliers, together with the cotton product manufacturers, account for more than 440,000 jobs in the U.S. [U.S. Census of Agriculture]. Annual cotton production is valued at more than $4 billion at the farm gate, the point at which the producer sells [Economic Services, NCC]. In addition to the cotton fiber, cottonseed products are used for livestock feed, and cottonseed oil is used for food products ranging from margarine to salad dressing. While cotton's farm-gate value is significant, a more meaningful measure of cotton's value to the U.S. economy is its retail value. Taken collectively, the annual business revenue generated by cotton and its products in the U.S. economy is estimated to be in excess of $120 billion [Retail Values of U.S. Agricultural Commodities, NCC].

For 2004, Georgia ranked 5th in total cotton production with 1.8 million bales produced, or roughly 8% of the total U.S. crop. The annual farm-gate value of the Georgia crop is estimated to be roughly $430 million. The economic contribution of the cotton industry in Georgia is even more significant when accounting for businesses in cotton's processing distribution, and utilization chain. Cotton in Georgia supports almost 54,000 jobs and generates $6 billion in business revenue.

The subject of this hearing is whether China enacts barriers to fair trade. I will offer the perspectives of the cotton industry on doing business with China, which is a fairly unique perspective.

There are few international trading relationships more complicated or dynamic than that of U.S. cotton and China. The U.S. cotton industry is exporting an ever-increasing amount of cotton fiber to China. At the same time, our long-standing customer, the U.S. textile industry, continues to erode financially in the face of competition from textile imports. China is the most competitive textile and apparel manufacturer in the world.

A few numbers demonstrate the dynamic nature of this trading relationship:

- In 1998, China imposed a quota on cotton imports and imported 359,000 bales of cotton from the world. In 2002, China announced the first tariff-rate quota allocation in keeping with its WTO accession agreement. In that marketing year, China imported 3.1 million bales of cotton from the world and 234,000 bales from the United States.
- We are still recording sales for the 2004 marketing year. So far, China has about 3 million bales in commitments from the U.S. and is expected to import up to 8 million bales from all sources. It also produced a record 29 million bales of cotton in marketing year 2004 and exported almost $55 billion dollars of total textile and apparel products in calendar year 2004, an increase of 50% since 2002. Current USDA projections show China importing 15 million bales for the 2005 marketing year – an increase of 7 million bales over 2004.
- This growth should be taken in context with the demise of the U.S. textile industry. In the 1998 crop year, the U.S. still maintained double-digit mill use of cotton. In that year, the U.S. and China combined to register 29 million bales of mill use. As we enter 2005, a scant 7 years removed from 1998, it is projected that China alone will spin about 41 million bales of cotton in its mills – 12 million bales over the combined total of the U.S. and China in 1998. Meanwhile, U.S. mill use has fallen to around 6 million bales a year, 40% below the rates that existed throughout the 1990s. I know that this committee is very familiar with the economic situation confronting the U.S. textile industry and the need for appropriate measures to ensure its survival.

The numbers I have recited show very clearly that the United States has a new, very important customer, China. The U.S. cotton industry is currently exporting substantial quantities of cotton to China, and China must continue as an important customer. With its rate of increase in cotton production, cotton mill use and cotton purchasing, China is the dominant force in world cotton. I have attached to my testimony an analysis of China cotton production taken from the Economic Outlook report developed by the Economic Services department of the National Cotton Council in January of this year for further background in this area.

The numbers also demonstrate the incredible ability of China to ship textiles and apparel to the United States, underscoring the importance of the timely use of China textile safeguards.

The short answer to the question -- does China enact barriers to fair trade -- is yes, China does have barriers to fair trade. The cotton industry is also concerned with China's currency policy, the use of tax rebates to encourage exports, and the subsidized or forgiven loans provided to its domestic textile industry. In fairness, however, it is important to consider the steps China has taken to open its markets and the extent to which China's trade rules are still evolving. Despite these improvements, there are still many concerns with specific unfair trade practices. I commend this committee for focusing on these issues.

Market Access – Implementation of the Tariff Rate Quota

After being shut out of the China market in 1998, the U.S. cotton industry welcomed the WTO accession agreement and China's commitment to establish a tariff rate quota of over 3 million bales. While China announced that quota fairly promptly in February 2002, the National Cotton Council raised serious concerns with the way in which the People's Republic of China was implementing its commitments. Our primary objection has been China's allocation of a significant portion of the cotton TRQ to the "processing trade." By allocating quota to the processing trade, China is requiring that apparel made from that cotton be re-exported. Essentially, the processing trade category is not true market access as required by the terms of the U.S. - China WTO accession agreement.

As a result of our concerns, the U.S. Trade Representative's Office and USDA's Foreign Agricultural Service (FAS) conducted numerous discussions with China officials in an attempt to get China to modify its implementation of the tariff rate quota (TRQ) for cotton. In 2003 China announced revisions to its regulations that simplified the process and improved matters, but did not eliminate the processing trade distinction.

However, other events in U.S. - China cotton fiber trade have overtaken implementation issues. China has grown to be the largest importer of U.S. cotton in the world; it has increased its import quota above WTO requirements; and it is expected to continue to purchase imports well in excess of its WTO commitments. This level of trade with China is beneficial to the U.S. cotton industry and relieves the immediacy regarding changes in China's tariff rate quota implementation.

Despite this beneficial trade, the United States and the U.S. cotton industry must remain vigilant and continue to push for reform in the TRQ system. Should internal pressures to purchase foreign cotton subside within China, this private/processing trade distinction could once again become a significant barrier to U.S. exports.

Recently, China has announced a variable tariff it intends to impose on imports of cotton over its tariff rate quota. This tariff will reportedly vary depending on the price of cotton, with a smaller tariff applicable if cotton prices are higher. This type of mechanism reminds us of the variable levy system that existed under Europe's common agricultural policy and is a concern. While it is true that China has discretion on the amount of tariff it may impose on imports above its TRQ, that discretion is not unlimited. We are still trying to determine exactly how this new tariff will be implemented, whether it will be implemented in a non-discriminatory fashion, and whether it will effectively amount to price support to China's cotton producers.

Finally, I should note that specific terms of implementation are not the only means by which China can influence imports. The government of China can still exert a significant amount of influence over the availability of credit to importers. By tightening up on credit, China can (and has) quickly caused imports to subside.

Ability to Enter into Contracts

Initially, there was significant confusion within the U.S. cotton sector concerning the ability of any specific cotton textile mill in China to enter into a contract directly and on their own behalf with a foreign merchant. The accession agreement called for a phase-in of the legal ability of companies to enter into business contracts, but the status of that phase-in and the legal status of individual companies was not very clear.

Overall, however, cotton merchants report that China has expanded the ability of mills to contract and appears to be moving forward with this aspect of their commitments. However, those mills are

new to doing business this way. They have a steep learning curve and don't always appreciate the sanctity of their contractual commitments. When the price moves against a mill in China holding a sales contract, U.S. merchants have reported that some mills are unwilling to carry out their contractual commitment. Enforcement of the commitment, then, becomes a serious issue.

Quality Issues

As our cotton exports to China have grown, China's mills have begun to raise quality issues with U.S. cotton. These complaints stem from a number of factors.

First, cotton produced in China is hand-picked and ginned using much older technologies. The result is a different bale of cotton. U.S. cotton has different characteristics as it is machine-harvested and ginned in modern gins, the result of higher implicit labor and capital costs in the U.S.

As a result of these differences, some U.S. merchants believe Chinese mills often over-penalize U.S. qualities. They seem to have more trouble spinning U.S. cotton than do mills in other parts of the world. We don't think this is because U.S. cotton is of inferior quality, but simply because of differences in the fiber.

Further, all cotton in China, whether produced domestically or imported is still classed manually, which can produce inconsistencies.

In 2003 the China Fiber Inspection Bureau (CFIB) announced an ambitious plan to transform the current manual classification system to an instrument based system. The plan is to be completed in 5 years beginning in August 2005. The plan proposed use of High Volume Instrument (HVI) inspection on all Chinese cotton bales with primary emphasis on use of rapid instrumentation testing similar to that used by the U.S. Many details are yet to be resolved but it is a step in the right direction. It is in the best interest of the U.S. if China adopts standards and testing protocols consistent with those we currently use.

Reliable standards are essential for orderly export and marketing of U.S. cotton. Experts from USDA's Agricultural Marketing Service (AMS), FAS, and Agricultural Research Service (ARS) have partnered with Cotton Incorporated and the National Cotton Council to provide technical advice, consultation and assistance to the CFIB. This collaborative effort helps to ensure China grading standards, protocols and parameters are based on sound engineering, scientific and statistical principles consistent with US. In 2004 the U.S. was host to two CFIB technical delegations; furthermore the U.S. team met with the CIFB in Beijing to further the technical collaboration. Additional discussions are planned for later this year with a follow up visit of CFIB technologists to the U.S. The delegation will spend up to one week in intensive technical discussions with the USDA's AMS, ARS and industry.

Evolving Terms of Trade

Contract disputes are the unfortunate result of new market participants, inconsistent quality classification systems, and volatile markets. U.S. cotton merchants report that there is a critical need in China for an improvement of the rules that govern the terms of trade. Quality complaints are not handled equitably. Contract sanctity is not readily enforced and negative price movements can cause significant cancellations of contracts.

We believe that in order to quickly improve enforceability of contracts, solve quality differences, and improve other critical components of the terms of trade, China should look to internationally recognized bodies that have developed terms of trade over an extended period of time and use their experience. These organizations, such as the International Cotton Association (formerly the

Liverpool Cotton Association) could help China revise its outdated and one-sided purchase contracts and help reform rules governing the settlement of contractual disputes.

Interestingly, the National Cotton Council recently hosted an intern from the China Cotton Association to assist their understanding of our business systems and our terms of trade. The National Cotton Council intends to send an intern to China this year to work with the China Cotton Association in an effort to continue this exchange of information.

China Textile Safeguards

The China WTO Accession Agreement contained a textile-specific safeguard mechanism that authorizes WTO members to impose import limits on specific categories of textiles and apparel if imports from China disrupt or threaten to disrupt the orderly development of trade. The right to implement safeguards under this provision is shared by all WTO members. Avoiding disruptive shifts in trade patterns is in the interests of all parties.

The Administration's recent actions regarding textile specific safeguards have been extremely important to the U.S. textile industry.

The temporary textile safeguard mechanism is an appropriate response to disruption that can be caused by significant surges in imports. However, the imposition of safeguards has become controversial with lawsuits trying to prevent the Administration from implementing this provision and with China threatening retaliation of one kind or another should safeguards be imposed.

The efforts by the Administration to make the safeguard process consistent and transparent are commendable. Once a safeguard petition is filed, all interested parties have a chance to file comments and express their views.

The real problem with the mechanism has been timeliness of data. With a four month delay before import data became official, import surges could swamp a particular category of products before a safeguard petition could even get underway – and that process would take another 100 days or so. These anticipated delays are one of the reasons the U.S. textile industry filed safeguard petitions in late 2004. Its concerns proved valid as imports from China in several textile and apparel categories were more than 1,000 percent above the previous year's levels.

In March the United States implemented a significantly improved import monitoring system, which makes import data available much quicker than was possible under the conventional system. This improved monitoring system quickly showed the import surges the textile industry had predicted. The Committee for the Implementation of Textile Agreements acted appropriately to start an investigation and ultimately impose safeguards on six categories of imports. The new monitoring process, together with a willingness to self-initiate safeguard procedures in appropriate categories, provides a means by which appropriate action can be taken before major market disruption occurs. I have attached to my testimony a summary of the status of textile safeguard actions that have been taken by the U.S.

Conclusion

China's ever-increasing mill use of cotton is driving its demand well beyond its current TRQ. While the end of the global apparel quota system in January of 2005 opened up the world market for China's apparel producers, the huge export numbers enjoyed by China bring a host of additional challenges for China and the world. In response, importing countries make use of the temporary safeguard provisions available to their textile industries; third-country apparel producers hustle to secure advantageous trade deals with their important markets fearing they will be swept aside by the

China apparel juggernaut; and China worries about its economy overheating and must deal with the contradictory goals of low-priced cotton for its mills and higher prices for its producers.

China is the dominant factor in the world cotton and textile markets. It is imperative that the U.S. cotton industry continue to cultivate China as a good customer of our fiber. It is just as critical that we hold China to its agreements and ensure that as its economy grows and merges into the world economy our manufacturing base does not become a casualty.

I am certain that this will happen and, despite the bumps in the road, I am convinced our economic relationship with China will normalize.

ATTACHMENT A – TESTIMONY OF TOM STALLINGS

Excerpt from National Cotton Council Annual Economic Report – 2005

China Cotton Production

The People's Republic of China continues to be the dominant factor driving the world cotton market. China remains the world's largest cotton producer with an estimated 2004 crop of 29.00 million bales. This year's crop is roughly 6.70 million bales higher than last season's crop mainly due to much improved weather conditions throughout the growing season. Other factors include an increase in planted acres for the 2004 crop year. USDA's latest estimates indicate an 11.50% increase over 2003, putting acreage at the highest level since 1992.

Xinjiang remains the dominant cotton-producing province followed by Hebei and Shandong. Among the leading cotton-producing provinces, Hebei has the highest growth rate, in terms of planted acres, at about 30.0%, followed by Shandong (19.0%). In the Yangtze River Reaches, except Anhui, where very low yields last year prompted farmers to reduce rather than increase planted area, others are to increase with the highest being Jiangsu at 23.6%. In the Northwest, the growth in planted acres averaged roughly 8.6%.

Improved production practices also played a role in China's increased production. Seedling transplanting was used on 95.0% of the planted area and the use of plastic film as a cover reached 44.0%. In Xinjiang's state-run Production and Construction Corp (PCC) farms, high planting density, standardized varieties planted on a relatively large scale, together with improved irrigation systems, have reduced water waste and ensured stable yields. Non-PCC farms, however, produced lower yields, mainly due to poor field management practices. Regarding seed variety, transgenic Bt cotton planting continued to expand in China, however, it remains difficult to predict the real area share of Bt varieties. Although only officially approved for planting in four provinces, Bt varieties are, in fact, grown much more widely. As a result, estimates for Bt cotton acreage vary from as low as 22.4% to over 70.0%.

In general, the Chinese government took a flexible policy approach toward cotton production and encouraged production based on the Ministry of Agriculture's (MOA) Regional Plan for Agriculture Products announced in February 2003. The plan identified three major cotton regions with the greatest growth potential and designated them as primary cotton producing regions. They are: 1.) the Yellow Basin; 2.) the Yangtze River basin; and 3.) the Northwest region, including Xinjiang. By 2007, China hopes to reach the following objectives. First, in the Yellow River Basin, China officials would like to expand the cotton planting area to 30.00 million mu (roughly 5 million acres) and production to reach 2.10 million metric tons (MMT) (over 9.50 million bales). This area is targeted to be the main production base for cotton which produces yarns of 40 counts.

For the Yangtze River Valley, officials plan to expand plantings up to 15.00 million mu (2.50 million acres) and production up to 1.20 MMT (5.50 million bales). This area is targeted to be the main production base for cotton which produces yarns of 50 counts and over and of 20 counts and under. Finally, in the Northwestern Area, planting area is projected to reach 12.00 million mu (1.90 million acres) with production goals of 1.20 MMT (5.50 million bales). The area is targeted to be the main production base for cotton which produces yarns of 32 counts. Given the limited land availability, in the short term, cotton area is most likely to be relatively stable and remain in line

with MOA's Regional Planning.

Lower cotton prices should lower Chinese acreage in 2005. Grain supplies have tightened over the past few years in China so there will be continued efforts by government officials to ensure adequate grain acreage. As a result, Chinese production is expected to fall to roughly 27.24 million bales in 2005.

ATTACHMENT B – TESTIMONY OF TOM STALLINGS

Textile Specific Safeguards

As the United States has liberalized trade in textiles and apparel with China, there have been significant surges in imports that have justified the imposition of temporary safeguards. The Department of Commerce has imposed safeguards on several specific textile categories and is considering the imposition of safeguards on other categories. The safeguards are temporary, limited in time and in scope, and cover only specific categories of products. The safeguard authority only runs through the end of 2008.

When imposed, safeguards do not stop growth in apparel exports to the U.S. market; they allow for 7.5% increases in the restricted items. The 7.5% growth is measured against the amount entered during the first 12 months of the most recent 14 months preceding the request for consultations. Allowable growth of 7.5% in products subject to safeguards is about twice the recent growth rate for the U.S. retail market for textile products and is on top of the growth that has already occurred. Imports in other categories can grow without limits.

The Committee for the Implementation of Textile Agreements (CITA), an interagency committee, is responsible for evaluating use of the safeguards in the U.S. market.

China is the world's largest and most capable textile manufacturing nation, and is therefore highly valued as a trading partner by both buyers and sellers. For the same reasons, it's no surprise that China is also seen by many as a threat to established trading patterns. Safeguards are a way to ease the transition toward a completely open market for textiles and apparel. As the world's largest market for textile products, the U.S. is already a huge importer of Chinese textiles. The U.S. will undoubtedly continue to increase its purchases of Chinese textile and apparel, as safeguards, to date, have only been imposed on a few categories.

Safeguard Use to Date

In 2003, in response to petitions filed by the U.S. textile industry, the U.S. implemented safeguards on three categories of products: knit fabric, cotton and man-made fiber brassieres, and cotton and man-made dressing gowns. The safeguards were in place for the period December 24, 2003 through December 23, 2004. In June 2004, CITA received a petition seeking safeguards on sock imports from China and ultimately imposed safeguards on sock imports from China through October 28, 2005.

Beginning in the fall of 2004, a coalition of U.S. textile interests filed 12 safeguard petitions alleging that the removal of quotas in January 2005 would trigger a massive surge in imports from China threatening market disruption. The petitions covered cotton trousers, man-made trousers, wool trousers, cotton knit shirts, synthetic fiber knit shirts, cotton and synthetic fiber woven shirts, cotton and synthetic fiber underwear, combed cotton yarn, and other synthetic filament fabric. Renewal petitions were also filed for the three categories covered by previous safeguard petitions.

CITA accepted most of the petitions for investigation and was expected to make a final decision regarding import relief in January or February of this year. However, in early January, the Court of International Trade imposed a preliminary injunction halting CITA's further consideration of the petitions. The ruling was made at the request of the U.S. Association of Importers of Textiles and Apparel, a trade group representing U.S. retailers. The trade group filed a lawsuit seeking to block the safeguard filings in December 2004.

While the injunction was still in place, CITA, on April 4, 2005, self-initiated textile safeguard proceedings in six product categories to determine whether they were contributing to U.S. market disruption. CITA found both market disruption and a threat of market disruption and imposed safeguards. These safeguards cover Cotton Knit Shirts and Blouses, Cotton Trousers, and Cotton and Manmade Fiber Underwear. According to the U.S. government's data, cotton knit shirt imports were up 1,277 percent during the first quarter of 2005 compared with the same period in 2004; for cotton trousers the increase was 1,573 percent; and for underwear, 307 percent.

On April 6, 2005, a coalition of U.S. textile interests filed safeguard petitions with CITA on several additional textile and apparel categories. The categories are as follows:

- Cotton and Manmade Fiber Shirts, Not Knit (categories 340 & 640)
- Cotton and Manmade Fiber Sweaters (categories 345, 645, & 646)
- Cotton and Manmade Fiber Brassieres (categories 349 & 649)
- Cotton and Manmade Fiber Dressing Gowns (categories 350 & 650)
- Other Synthetic Filament Fabric (category 620)
- Manmade Fiber Knit Shirts (categories 638 & 639)
- Manmade Fiber Trousers (categories 647 & 648)

Then, on April 27, a federal Court of Appeals stayed the preliminary injunction and CITA was allowed to continue its investigation of the petitions filed in late 2004. Since that date, CITA announced a positive determination in four of those cases. The other cases remain under investigation.

One of the keys to CITA's self-initiation of safeguards in 2005 was the implementation of a significantly improved import monitoring system, which makes import data available much quicker than was possible under the conventional system. This improved monitoring system, together with self-initiation of safeguard procedures by CITA, provides a means by which appropriate action can be taken before major market disruption occurs. I have attached to my testimony a table summarizing the status of textile safeguard actions that have been taken by the U.S. as of May 23, 2005.

TABLE - China Textile Safeguards Status

Group	Category	Description	Date Initiated	Status	Imports From China % Change from Previous Year Jan. - Mar (Official)
First Safeguards Enacted	222	Knit Fabric	July 24, 2003	Expired Dec. 24, 2003	-18%
	349/649	Cotton & MMF Brassieres			40%
	350/650	Cotton & MMF Dressing Gowns			36%
Threat Based Safeguards Filed by Industry	347/348	Cotton Trousers	Oct. 8, 2004	Injunction / Subject to self-initiation	1573%
	647/648	MMF Trousers	Oct. 13, 2004	Injunction / Safeguard Imposed	278%
	638/639	MMF Knit Shirts	Oct. 13, 2004	Injunction / Safeguard Imposed	330%
	340/640	MMF Shirts, Not Knit	Oct. 13, 2004	Injunction / Safeguard Imposed	284%
	338/339	Cotton Knit Shirts	Oct. 13, 2004	Injunction / Subject to self-initiation	1277%
	352/652	Cotton & MMF Underwear	Oct. 15, 2004	Injunction / Subject to self-initiation	307%
	301	Combed Cotton Yarn	Oct. 27, 2004	Injunction / Safeguard Imposed	120%
	620	Other Synthetic Filament Fabric	Nov. 8, 2004	Injunction / Investigation resumed	707%
	447	Wool Trousers	Nov. 12, 2004	Injunction / Investigation resumed	171%
	222	Knit Fabric	Nov. 19, 2004	Injunction / Investigation resumed	-18%
	350/650	Cotton & MMF Dressing Gowns	Nov. 24, 2004	Injunction / Investigation resumed	36%
	349/649	Cotton & MMF Brassieres	Dec. 1, 2004	Injunction / Investigation resumed	40%
Active	332/432 & 632 part	Cotton, Wool, & MMF Socks	June 28, 2004	Effective Oct. 29, 2004 – Oct. 28,2005	95%

Group	Category	Description	Date Initiated	Status	Imports From China % Change from Previous Year Jan. - Mar (Official)
Self-Initiated by CITA	338/339	Cotton Knit Shirts	April 4, 2005	Process Self-Initiated / Safeguards Imposed (Effective May 23, 2005 – Dec. 31, 2005)	1277%
	347/348	Cotton Trousers			1573%
	352/652	Cotton & MMF Underwear			307%
Market Disruption Safeguards (Latest Filed by Industry)	340/640	Cotton & MMF Shirts, Not Knit	April 6, 2005	Action taken based on threat petition	284%
	345/645/646	Cotton & MMF Sweaters		Proceeding	200%
	349/649	Cotton & MMF Brassieres		Proceeding and threat investigation resumed	40%
	350/650	Cotton & MMF Dressing Gowns		Proceeding and threat investigation resumed	36%
	620	Other Synthetic Filament Fabric		Proceeding and threat investigation resumed	707%
	638/639	MMF Knit Shirts		Action taken based on threat petition	330%
	647/648	MMF Trousers		Action taken based on threat petition	278%

1
2
3
4
5
6 DISCUSSION OF INTELLECTUAL PROPERTY THEFT
7 JUNE 12, 2005
8 3:00 O'CLOCK P.M.
9 NASHVILLE, TENNESSEE
10
11
12 Hosted by:
13 Marsha Blackburn
Member of Congress
14 Seventh District, Tennessee
15
16
17
18
19
20
21
22
Prepared by:
23 Carole Kimmel-Briggs, CSR
Briggs & Associates Court Reporting
24 1339 Sydney Terrace
Mt. Juliet, Tennessee 37122
25 615/754-4327

1 (Whereupon, the following discussions
2 were recorded and transcribed as follows:)
3 CONGRESSWOMAN BLACKBURN: I'm Marsha
4 Blackburn, and I want to say thank you to everybody
5 for taking the time to come on this rainy Sunday.
6 I'll tell you, Arlene is just raining on Bonnaroo
7 and MCA Fest, and a little bit of everything. And
8 to BMI, thank you. I thank you all very much for
9 the hospitality. Harry, Paul, we appreciate this
10 tremendously. I just cannot tell you all how much I
11 appreciate your taking the time to come out and talk
12 with us.
13 Bart has worked with us repeatedly on this
14 intellectual property issue. David Bennett is
15 working with us on this. And we know if you line up
16 everything that has an impact on the entertainment
17 industry in Middle Tennessee, the one thing we
18 continue to hear from you all, yes, taxation hurts;
19 yes, regulation hurts; and my goodness, this
20 intellectual property and piracy issue is just
21 killing us.
22 As you all are very well aware, I spent a
23 week in China last year, China and Hong Kong and
24 Vietnam and Australia working on this issue. And
25 we're going to go back in August and work on it a

1 little bit more. And this year I'm going to be
2 travelling with Chairman Manzullo who heads the
3 small business committee in congress. He is the
4 chairman of that. It was so exciting for me. He
5 came in a couple of months ago and did his first
6 visit into Nashville into the music industry, and
7 had the opportunity to go into a studio.
8 And, Bart, as we've so many times talked,
9 the entertainment industry is a small business
10 industry. All of you are all small business owners.
11 And as the chairman said, he has widget factories in
12 his district, and I have songwriters, and I have
13 T.V. program producers, and I have sound engineers,
14 and music publishers. So it's a different type of
15 small business. And I appreciate the attention that
16 he has come to put on this issue as a small business
17 issue.
18 And our hope today is that we will be able
19 to listen to you, gather some good anecdotal
20 evidence, have that as I get ready to go back to
21 China with the chairman to represent you in front of
22 the Chinese government, to say this is what is
23 happening to our people, this is the impact that we
24 are feeling in my community.
25 We've had a couple of hearings in energy

1 and commerce committee this year. One, we had last
2 week, and I had the opportunity to question the
3 under-secretary from commerce. And I questioned the
4 U.S. trade rep on this issue also. And I told them
5 that when you look at our Middle Tennessee economy,
6 you're talking about a tremendous impact. And I
7 told them, I said, our state has a 26-billion-
8 dollar-a-year budget; $14 billion of that budget
9 comes from state-generated revenues; about a billion
10 dollars of that comes out of the entertainment
11 industry. And when they start stealing our
12 intellectual property, it is an impact on our state
13 budget. We know that; we realize that. And we
14 expect the trade office to do some things to help
15 us.
16 Now, we know it's cultural with the
17 Chinese. We know that when you copyright something
18 here, it means it's protected. We know in China and
19 many other communist nations, when you print
20 something there, it means it's public. So we accept
21 that it's cultural, but we also recognize that this
22 is a global economy. And if they want to
23 participate with us in this global economy, we need
24 them to recognize the value of our product which is
25 our intellectual property.

1 So we're going through the proper avenues
2 - working with you all, working with our committees,
3 having our hearings, judiciary committee is engaged
4 in this issue, energy and commerce and the trade
5 subcommittee where I am, we're engaged in this
6 issue. We've already had two hearings. We have one
7 more hearing coming up. The small business
8 committee has become engaged in this issue. They
9 are working with us. And we will have the trip to
10 China in August where we're going to have, Patrick,
11 how many on the trip, how many members?
12 MR. WILSON: About 25 members of congress,
13 the largest --
14 CONGRESSWOMAN BLACKBURN: Twenty-five.
15 MR. WILSON: -- ever.
16 CONGRESSWOMAN BLACKBURN: We will be
17 working to try to find some resolutions and some
18 common ground on the intellectual property theft
19 piracy issues that impact your pocketbook and your
20 ability to earn everyday.
21 You know, another thing that I want to
22 just say thank you, because I have several who have
23 been putting on their tennis shoes and grabbing
24 their guitars and making rounds up at the capitol,
25 and I really appreciate that. And Bart is so

1 diligent to do that.
2 This makes an impact. And as chairman of
3 the songwriters caucus, it makes an impact when you
4 all come in and say, let me explain to you what
5 happens. You know, like having the entertainers, we
6 had Julie Roberts and Steve Azar just two weeks ago.
7 That makes a big impact because it allows the other
8 members maybe who are not as familiar with the
9 intellectual property and what happens in the
10 entertainment industry, it allows them to understand
11 that this is a business issue to us. It is a
12 business issue to us. This is how people choose to
13 make their living.
14 And so I thank you for your commitment to
15 come to D.C. and to very openly and willingly tell
16 your stories and communicate that to the other
17 members.
18 Let's do this: let me introduce to you
19 some of the folks that are going to be here with you
20 today. I'm going to start with Patrick Wilson. He
21 is the legal counsel for the house small business
22 committee and serves as the chief policy adviser to
23 Chairman Manzullo. Congressman Manzullo is out of
24 Illinois, and Mr. Wilson is his chief policy
25 adviser. He advises him on the trade, on the

1 copyright issues. He has already been into China
2 holding meetings with their diplomatic group and
3 their representatives addressing the intellectual
4 property issues. And so he is doing a great job.
5 I'll have to tell you, too, enjoying CMA Music Fest
6 while he is here. I even took him out to the
7 Loveless for brunch this morning. And he was so
8 disciplined, he didn't -- don't put this in the
9 record. He didn't even touch a biscuit. I had two
10 before we ever placed an order. He was so good. I
11 was so impressed.
12 So he is learning what Nashville is all
13 about. Then I drove him through -- David kind of
14 drove him through a neighborhood there and showed
15 him where different people live and work, and it
16 kind of gave him a little bit of the lay of the land
17 before he came on back downtown. So we're thrilled
18 that he has given up his weekend to come and find
19 out a little bit more about you guys and what you
20 do. So we welcome you to Nashville. (applause)
21 Now, somebody that you all have become
22 familiar with, Mike Platt, legislative director for
23 our office in D.C., for my congressional office
24 which is my office, your office. And Mike is the
25 one who is leading the way on all of the

1 intellectual property issues in our office. He
2 works very closely with Fred, with Bart, as we have
3 the groups in and out and back and forth. One of
4 the things I really appreciate about Mike, he was
5 such an important part of our team as I sought to
6 move to energy and commerce committee and be able to
7 represent our enterainment community there on the
8 Telcom issues, intellectual property issues. And he
9 has also become a go-to guy with the Telcom
10 Committee and on the intellectual property issue.
11 And much of that comes from the good education that
12 you all are so willingly sharing with him, the
13 information of how quickly your industry changes.
14 And we thank you for that. So Mike is going to be
15 with us and make a few remarks, kind of give you an
16 update on where some things are.
17 David Bennett who is the executive
18 director of the Tennessee Film Entertainment and
19 Music Commission. I have absolutely loved working
20 with David. When we decided CMA Fest was going on,
21 and we had the opportunity to do this, and we wanted
22 to hear not only from our songwriters, but from our
23 video and our T.V. folks also, I called David, and
24 we started working on this issue in pulling a day
25 together. And he has just been absolutely

1 fantastic.
2 And, of course, I can really brag on David
3 because I used to have the spot that he now has.
4 And I think we both agree it is the best job in
5 Tennessee state government, right?
6 MR. BENNETT: Absolutely.
7 CONGRESSWOMAN BLACKBURN: And, you know,
8 we both owe much of what we have and are and will be
9 to Mr. Harry Warner who is chairman of that board.
10 And I wouldn't let him go, and David won't let him
11 go. So he's kind of stuck in there. He can't get
12 away from us.
13 So with that said, I'm going to just say
14 again, we appreciate you. We hope that we encourage
15 the rest of the world to appreciate you and what you
16 do. I am going to turn the microphone over to Mike
17 Platt. He has some remarks, and then Patrick will
18 have some remarks, and then David Bennett is going
19 to kind of kick us into high gear. Mike.
20 MR. PLATT: Thank's for joining us. My
21 remarks are mainly focused on housekeeping. We have
22 a court reporter here so that Patrick can take this
23 back to the chairman of the small business
24 committee, and they're going to make it part of
25 their official records. So when you share your

1 stories, slowly state your first name and your last
2 name and what your business is so that Carole
3 doesn't miss any of it. And we appreciate you, too.
4 Thank you for being here.
5 As Mrs. Blackburn pointed out, the energy
6 and commerce committee has already held a couple of
7 hearings in the last month over intellectual
8 property theft. Next week, the committee is also
9 going to have a hearing on a counterfeiting, not
10 just in China, but on a global basis. With that, I
11 will turn it over to Patrick Wilson.
12 MR. WILSON: Thank you all, very much, for
13 having me to Nashville, but most especially thank
14 you to Mrs. Blackburn. It is really funny. I think
15 all of you who had a chance to get to know Marsha
16 know that's she's a tireless advocate. You are very
17 lucky to have her in congress because two things
18 that really impress me: one, whenever she went to
19 congress, she was a tireless champion down here in
20 the state house, and she figured out right away that
21 there was something missing in the congress, and
22 that was a voice for this industry, particularly a
23 strong one on the Republican side. She saw that,
24 and she did everything necessary to get on the right
25 exact committee to be that powerful voice. And to

1 move so quickly to make that happen is an amazing,
2 amazing thing.
3 She's proving that she is not an junior
4 member. She is a force to be reckoned with. And
5 when my chairman came here at Marsha's invitation to
6 get to know this industry, he was really moved by
7 being reminded that this is not just a glamerous
8 artist-drive industry with billionaires and gleaming
9 jets; this is a small business industry with people
10 who put their house on the line to start a business.
11 It's all about the roll of the dice on one song that
12 makes the hundreds that you wrote, and that one song
13 may be what you put your kids through college with.
14 Those are stories that he recognized
15 because they're every small business story, whether
16 it's starting the Loveless Cafe and you work those
17 20 hours a day to make a small business a success.
18 You may work for several years with no profit. It
19 just seemed exactly the same to him. And it was
20 Congresswoman Blackburn who said, of course, it's a
21 small business industry. And that's putting the
22 face on an industry that America needs to have to be
23 reminded of why we need to devote all of these
24 resources to it.
25 So when Congresswoman Blackburn invited

1 Mr. Manzullo, the chairman, to come back to
2 Nashville to have a listening session in advance of
3 our trip to China, he said, absolutely, I'll be
4 there. Unfortunately, you know the way everything
5 works. So he came back and said, oh, wow, I'm going
6 to be in Toronto on that day. So, Patrick, you have
7 to go, because whatever Marsha wants, that's what
8 she gets.
9 So that's why I am here, is because Marsha
10 is a tenacious advocate for Nashville. As you can
11 see, she's a great ambassador, but also for this
12 industry. So I just thank her very much for coming
13 here. And more than anything else, I think probably
14 the last thing you need to do is have more
15 politicians, or particularly in any case, more
16 staffers talking. I really want to hear from you,
17 because that's why we're here. I just want to tee
18 this up for you by letting you know the context of
19 why we're here to collect your comments.
20 Chairman Manzullo is entering his seventh
21 year as the head of the U.S./China inter-
22 parliamentary exchange. It's the highest level of
23 government-to-government contact we have with the
24 People's Republic of Chinese. We are now in our
25 round six. In fact, at this moment, a senior

1 delegation of some twenty members of the Chinese
2 parliament are in Chicago, Illinois visiting with
3 lots of business leaders, with intellectual property
4 issues - hearing and seeing what ordinary members of
5 congress like my boss, like Chairman Manzullo, like
6 Congresswoman Blackburn, the issues that they see as
7 elected representatives.
8 This is a foreign concept to them. Oh,
9 wow, you mean you actually have to, like, listen to
10 your constituents? Because these are nonelected
11 parliamentarians. It's a parliament sort of in name
12 only. And it helps us to remind them that we're not
13 just clamoring about these issues; our constituents
14 are demanding that we stop having their pockets
15 picked. And that's why they're out in Chicago.
16 Tomorrow they're going to Milwaukee, Wisconsin.
17 And when we do the reciprocal visit in
18 August, we're going to take the largest delegation
19 of members of congress ever to China in one trip.
20 We'll have that big plane with the United States of
21 America on it. We'll land in Beijing. We'll be
22 received by the president of China. And the good
23 news for you guys is in that group is going to be
24 your tenacious champion, because they will get
25 received at the highest level of, the head of the

1 ministry of commerce which does all regulations on
2 intellectual property, the office of trade and
3 investment, the office of protocols and securities,
4 as it's called, which controls patent, copyright
5 rules and regulations in China.
6 And that delegation will be received at
7 the highest level. And that means something in
8 China. It means in a country obsessed with face and
9 perception, that this is a very, very senior
10 delegation. And like I said, you will be lucky to
11 have a champion in there.
12 So what we're here today to do is to lay
13 out to the administers in the Chinese government the
14 impact that intellectual property theft has on the
15 small businesses that we represent, and
16 particularly, the impact that it has on our trade
17 deficit that we currently suffer from China, because
18 intellectual property is our number one export. So
19 many people forget about that. This is our number
20 one export, and it isn't surprising.
21 I've been at CMA. You want to know the
22 one take-away I have from being in Nashville this
23 weekend is yesterday I saw an Indian country music
24 star, a guy from India who plays and records
25 country. I met a Japanese one. They're all around

1 the world. Country music, this industry, is a
2 global industry. It's so uniquely America, and
3 people in China crave that. You can see that that's
4 going to be a huge emerging market. And if it's
5 stolen from us, we'll never get it back. And the
6 small recording record labels that start out a lot
7 of its music, the songwriters, the producers, you
8 have to think about all of the things that go into
9 the small business aspects.
10 I was talking before today about the
11 manufacture of equipment. This is a specialized
12 industry. The equipment, the sound equipment, all
13 of the things that go into the recording industry,
14 some of these things are one-off machines that
15 companies make here just for the industry. And as
16 this stuff gets stolen, it affects all down the line
17 throughout. And that's something that is of grave
18 concern to Chairman Manzullo. And I hope you know
19 that we are trying to follow Marsha's lead in
20 representing your industry and making sure we're
21 pounding on all of the right doors.
22 MR. BENNETT: Thank you, Patrick. I am
23 really encouraged to see everyone here this
24 afternoon. I thank you for coming out. I have to
25 say hello to our host, Fred Cannon. Again, I want

1 to thank you for your efforts in bringing us here
2 today.
3 MR. CANNON: BMI.
4 MR. BENNETT: BMI, of couse. And I see
5 Paul Coreman up there and the president of our
6 board, Harry Warner. Harry has been on this board
7 as chairman of this Tennessee Film and Entertainment
8 Commission Board for ten years now or more, I guess.
9 Harry, thank you for your service.
10 I see a lot of friends in here from the
11 music community as well as the film and T.V.
12 community. So, again, I appreciate you coming out
13 today. What I would like to do, to begin with,
14 ladies and gentlemen, to kind of stimulate the
15 thought process, I want to give kind of a sketch of
16 the problem. And I want you to reflect on this
17 sketch that I am going to give you, and then try to
18 think of how you can apply it to your personal
19 lives, and how you can apply it to our personal
20 problem here in Nashville, Tennessee with
21 intellectual copyright issues.
22 Let me start by making a definition, if I
23 may. Intellectual property rights are the rights
24 given to persons over the creations of their minds.
25 And they usually give the creator an exclusive right

1 over the use of his or her creation for a certain
2 period of time, and, quite often, that minimum is 50
3 years after the death of the author. So that not
4 only affects you as you write music or as you create
5 screenplays or television scenarios, it also affects
6 your children and grandchildren. So we're talking a
7 legacy issue here, if you will. If they're stealing
8 from us, if anyone is stealing from us in
9 intellectual copyright, they're stealing from our
10 children and our grandchildren also.
11 Quite often, though, the argument about
12 this from the other side, if you will, is, well, you
13 know, the United States wasn't that great about
14 intellectual issues, copyrights, either when their
15 economy was in its infancy. Case in point, Charles
16 Dickens had a heck of a time getting royalties from
17 the United States for his novels in the 1840's. It
18 seems like there is an economic arch for when
19 economies grow from their infancy into maturity.
20 There is a period of copying and reverse
21 engineering, if you will.
22 We've seen it happen many times. We've
23 seen it happen in Russia. We've seen it happen in
24 countries like Malaysia and, of course, now China.
25 So that's an interesting question. Is

1 this problem a momentary issue or is it going to be
2 an issue that we have to deal with for litterally
3 hundreds of years past this time?
4 Henry Bloget who is a former securities
5 analyst wrote an interesting article. And he
6 mentioned in this article that in China, piracy is
7 so entrenched, that even the pirates complain about
8 the other pirates. The storekeepers are selling a
9 DVD for ten yuan, but the shopkeepers, the street
10 vendor down the street, is selling ten DVDs for
11 seven yuan. And then his competition is selling two
12 for one. So they're all complaining about each
13 other on this issues.
14 And it's just not DVDs in China that
15 they're copying and pirating, it's much more broad
16 than that. According to estimates, as much as a
17 third of China's gross domestic product comes from
18 piracy and counterfeiting, a third of their gross
19 domestic product. What we're dealing with here is a
20 societal issue that is so entrenched in this
21 society, it has actually created a version of our
22 middle class there. So we have to figure out a way
23 to alter that to where they can still improve their
24 middle class and improve their economy without
25 stealing from us.

1 Peter Goodman in the Washington Post on
2 the 4th of June, so this is a current article, was
3 talking about -- I'm quoting him here. He says, The
4 brazen counterfeiting of goods and stealing of
5 patented ideas is a part of the basic fiber of
6 Chinese business. So, again, we're dealing with an
7 issue that is so entrenched and so basic, we have to
8 make a mental shift, if you will, in the Chinese
9 people.
10 Patrick, you mentioned our trade surplus,
11 the Chinese trade surplus. That is going to be
12 around $200 billion, their trade surplus versus what
13 we're importing into China. That's huge. And I'm
14 not sure that that even includes an estimate on what
15 the pirated goods are.
16 MR. WILSON: It's not included. That's
17 the actual trade gap.
18 MR. BENNETT: The trade gap is $200
19 billion excluded pirated materials. That is
20 incredible. Over the past 23 years, the
21 illegitimate trade worldwide has risen a thousand
22 percent. Annually, in 1987, it was $5.5 billion,
23 was the estimate. It's up to $600 billion today,
24 illegitimate products in piracy, $600 billion. And
25 the U.S. Chamber of Commerce says that pirating

1 costs us $250 billion a year here in the U.S., and
2 the loss of 750,000 jobs. It's an incredible issue
3 given all of these details. And it affects us in
4 music and film and television.
5 We want to talk a lot about the music side
6 of it today because there are publishers in here,
7 and we want to get your view of it, certainly; but
8 if I can just address the movie side of it for a
9 moment. This is an interesting problem, because
10 Star Wars, The Revenge of the Sith, was on the
11 streets there before it premiered here in the U.S.
12 The DVDs were selling in China before it ever even
13 premiered here.
14 And DVD technology has really brought that
15 forward, because when you had to copy VHS, you more
16 or less had to copy VHS in realtime. It's a slow
17 process. But DVDs, like CDs, can be stamped out
18 pretty quickly. And they have this machinery, just
19 like our machinery, worth hundreds of thousands of
20 dollars stamping out this pirated product.
21 But there is an issue here that kind of
22 goes beyond that, and that's the fact that the
23 Chinese government will only allow 20 foreign films
24 a year released in their theaters. Exhibition and
25 distribution is a problem. So I contend, possibly,

1 that if we had a vehicle to exhibit our movie
2 product there, whether it be a good Tennessee
3 company like Regal Theaters which is one of the
4 biggest in the United States and in the world,
5 certainly, if we could position theater chains in
6 that country to start exhibiting our product in an
7 environment that we take it in here -- I mean,
8 personally, I love going to the theater. I know you
9 do, too, because of the sound and the ambiance. It
10 makes that viewing experience great. The Chinese
11 don't get that. So they'll buy their Star Wars
12 movie for a buck, and, of course, they don't have
13 the opportunity to go to the theater and see it. So
14 that's something else that we need to think about as
15 we go along today.
16 All right, I'm interested in your
17 opinions, and I want to hear what you have to say
18 and think about it. And we're just going to start
19 the discussion off. If anybody has an idea, a
20 comment, let's range free and be energetic about
21 this, and see if we can really develop dialogue on
22 the issue.
23 MR. VANDERFER: David, my name is Jerry
24 Vanderfer. I am a professional songwriter here in
25 Nashville. I make my living doing so. First of

1 all, thank you so much for doing this. It's
2 impossible from my perspective to tell how much of
3 my material has been pirated or lifted in any Asian
4 nation, in particular. But I had a personal
5 experience. I was in Beijing a little over four
6 years ago and strolling near the U.S. Embassy, as a
7 matter of fact. And as I'm sure you know, the
8 Chinese people are wonderful, friendly, want to talk
9 to Americans. And I was approached, or maybe we
10 approached each other, by a couple of younger
11 Chinese people we were chatting, fortunately in
12 English. And it was fascinating.
13 Let me regress a minute. Just prior to
14 that encounter, I had gone into a Chinese record
15 store to see what American product was in there out
16 of curiosity. It wasn't anything like the size of
17 Tower, but it was still a record store. I didn't
18 find any America product at all; not only did I not
19 find any of my records, but I didn't find any
20 American product. It was explained to me at that
21 point that that was simply because American product,
22 kind of like your issue about the film, just simply
23 wasn't allowed in that store. So I wrote that off,
24 all right, my records are not in China.
25 Then I am encountered by this individual

1 by the American embassy. And he knew all of the
2 artists that I wrote songs for. And it occurred to
3 me how did that happen. If he can't get the records
4 in the Chinese store, how does he know the artist,
5 Tim McGraw. So it was obvious to me at that point
6 that my livelihood has been affected at the moment.
7 And he loved Tim McGraw, too, by the way. He was a
8 very big fan.
9 The other point I wanted to ask on that
10 issue, and this may seem very naive, Congresswoman
11 Blackburn, but I have been very, very fortunate to
12 go to D.C. a couple of times and play my songs for
13 the politicans, and the congressmen and the
14 senators, and be on the steps of the supreme court
15 in doing so. It does have a positive impact. It's
16 been very moving for me. Why can't we go to China
17 with you? Why can't a couple of us songwriters --
18 it doesn't have to be me -- and go play some songs
19 for these dignitaries and bring it personal to
20 Beijing. You know, three-piece suits have an
21 effect, but this has an effect with our guitar, too.
22 Just a thought I wanted to pass out to you.
23 MR. WILSON: My immediate reaction is
24 that's a great idea. One of the best things about
25 getting outside of Washington is -- I guess I am a

1 conservative Republican, fair warning to everyone.
2 I am not one of those people who thinks that all of
3 the goods ideas are in Washington. That's just my
4 nature, and part of the reason that we're here. The
5 policy reply I would make is a carry-on to what
6 David was saying, is that market access is at least,
7 at least, 50 to 60 percent of the problem of piracy.
8 And it's not just in China. It's India, it's South
9 Korea, it's Malaysia, it's Indonesia. That's the
10 crazy thing.
11 I had a great conversation. I was in
12 China last February of this year, and I was meeting
13 at a very high-level meeting in a big boardroom -
14 not as cool as the one next door, but very much like
15 that with all of the Chinese heads of all the
16 departments on that side and us over here, and I was
17 the leader of the delegation. And I looked across
18 the table at them and I said, you know, this same
19 problem that -- we were talking about movies. I
20 said, you know, there is obviously a massive
21 appetite for American movies in China, right? Oh
22 yes, everyone agrees. The people sitting across
23 from me, the head of the ministry of commerce is a
24 Stanford grad. So, I mean, we're taking this is an
25 American sympathetic Chinese official. And I said,

1 the problem is, they can't buy a legitimate American
2 movie because of the limitation on market access;
3 but it's clear from the millions of pirated movies
4 all over China that there is a massive appetite for
5 this product.
6 They tried to sit there with a straight
7 face across from me and say, well, well, Chinese
8 don't really want American movies. We have
9 excellent Chinese movies. I'm like, yeah, but the
10 ones I see for sale all over China.... And they
11 can't say to me, oh, well, Mr. Wilson, you've only
12 been to Beijing. And I can say, no, I've hiked the
13 Stone Forest and Hunan Providence. I've been -- I
14 went to the first ever rock festival, rock concert,
15 in Quiming in 2001 which was an amazingly early
16 break- through experience for artists,
17 world-recognized artists, primarily Europeans.
18 There weren't any Americans there, there were
19 Chinese language artists in a rock festival setting.
20 I've seen that. There is demand for this product.
21 Tim McGraw is everywhere.
22 If February we went to Chong Ching in
23 China which is western China, the far-out
24 interlands, a big, giant, massive city, but really
25 not a city that most Americans would be able to

1 recognize. I was in a country -- not only did I
2 hear -- a country bar in China; didn't look like a
3 country bar. It was plastic and gleaming with
4 mirror balls and stuff, but there was country music
5 on. They definitely know who it is. Did I go up to
6 the D.J. who was in the big sound box like a New
7 York nightclub and say, hey, where did you download
8 that DVD or whatever? I would have liked to have,
9 but I didn't.
10 But they have it. It's all about market
11 access. And that's the other part of this, is that
12 what we have to hammer on is that they want to buy
13 our products, and they want it to say made in
14 America. That's the amazing thing.
15 MR. KELLY: I'm Casey Kelly. I just
16 wanted to throw a question in here. I can do my
17 whole tap dance, I guess. I'm Casey Kelly. I am a
18 member of American Songwriters Guild and am a
19 songwriter and publisher, et cetera, et cetera, like
20 most of the people in here. I was just wondering as
21 you said that, I wonder, probably fairly naively, if
22 this is not something that is purposefully put in
23 place so that someone who keeps this in place is not
24 making the profit from this sort of stuff. And if
25 that doesn't raise even the stakes a bit as far as

1 this being a government versus government issue.
2 MR. WILSON: It absolutely is. You got to
3 the heart of the matter. I was very cynical at
4 breakfast this morning. Congresswoman Blackburn and
5 I were talking about this issue. And I said, it's
6 about the DVD players. Where are DVD players made?
7 All in China. There is an official Chinese
8 government policy. They want every household in
9 China to have a DVD player, because it's a
10 domestically-produced good. It's the entry way for
11 the middle class. And there is an official
12 government policy in that communist-styled
13 governments can decree, we want every household to
14 have a DVD player. How do you do that? We'll make
15 DVD products, whether it's movies or music, as cheap
16 as possible so every household will have to buy one.
17 It's a violation of the WTO, by the way.
18 The agreement that they have signed up for, this is
19 a violation. Our U.S. trade representative is
20 trying to hammer on that. You know, this is a
21 conspiracy. We lay it out to them, and they're like
22 oh, no, no, no, no, no.
23 MR. BENNETT: Let me add one thing to
24 that, if I may. This Washington Post article that I
25 mentioned earlier, Arthur Graver who is the managing

1 editor of the China Economic Quarterly says this: he
2 says, The goal of the government -- I'm quoting him
3 now, The goal of the government is to create an
4 indigenous technilogical capacity. And the
5 perception is that all of the technology is
6 controlled by the U.S., Europe and Japan. They feel
7 like they need to steal as much as they can for as
8 long as they can until they produce their own
9 technology. They have no incentive whatsoever to
10 enforce, so most of these discussions are not very
11 useful. That's what this gentleman says. Something
12 to think about.
13 Real quick case in point. Two years ago,
14 Cisco Systems -- we all know Cisco -- sued Wah Hay
15 Technologies, a fast growing Chinese competitor,
16 accusing the firm of copying its software code and
17 building it into some of its products. Last summer
18 Wah Hay settled the suit which was widely seen as an
19 admission of wrongdoing, though the company denied
20 it. Only months later, the state-controlled China
21 Development Bank extended a $1.25 billion-dollar-
22 line of credit to Wah Hay as the company aims to
23 expand sales and markets around the globe. The
24 banks approval of that was the line of credit.
25 MR. KELLY: I'll come back. I have

1 another issue.
2 MR. WILSON: It's a good conversation to
3 have. I don't want to make this so formal with the
4 microphones.
5 MR. CANNON: First of all, I love the idea
6 of sending a songwriter. I think that's a great
7 idea. I think Bart and I are going to put our heads
8 together and work on that.
9 Secondly, I think one of the biggest
10 problems that the western countries have is that
11 they have a high price in the Chinese market. And I
12 think you've touched on something that is very, very
13 important that we're missing here, is that our
14 product is very, very expensive to the Chinese
15 people. They can't afford our product. They can
16 afford the pirated copy because it's so cheap. And
17 that makes a big difference because if your CD in
18 China costs 25 bucks, in their mind, if they can buy
19 it for a dollar, guess what? They're never going to
20 buy your product. And that's a big issue.
21 That's why the government doesn't want it
22 to happen, because that means they've got to
23 standardize the price. And also the currency
24 exchange is a big problem now, too, because it's not
25 really the true value of their currency. I just

1 wanted to make that point.
2 MR. WILSON: It's a great point. Again,
3 the question about market access, I love -- my
4 favorite thing to do wherever I travel, and I've
5 been lucky to go to a lot of cool places, is I
6 always go to a grocery store or a regular -- like
7 where I would say most people would shop. I went to
8 a Carrefour store which is the French Wal-Mart.
9 There are Wal-Marts all over China, too. But I
10 happened to go to a Carrefour store. I'm a huge
11 Cole Play fan. It's a great British rock band.
12 Love Cole Play. I went into Carrefour and I bought
13 for 10 U-yuan which is just about a dollar and 25
14 cents an awesome DVD music compilation CD that I'd
15 never seen in the United States. It's a unique
16 product. I don't think it's a BMI group. I think
17 it's Universal.
18 MR. CANNON: It's BMI --
19 MR. WILSON: Oh, of course, it's the same
20 product. I'm sorry. I'm just getting to know the
21 industry. I bought it for a dollar and 25 cents.
22 It had great vidoes stored on there in a format that
23 I could use and great music for a dollar and 25
24 cents.
25 AUDIENCE SPEAKER: How was the quality on

1 it?
2 MR. WILSON: It was perfect. It was a
3 studio-produced legitimate outlet, because that's
4 the entry point. They have to sell it that cheap to
5 get anything. And obviously they're taking a
6 gamble. They're saying, well, we obviously would
7 lose our shirts if we tried to sell DVDs in America
8 for $1.25 at Wal-Mart, but we have to do that in
9 China because if it's $25 for the legit, we'll never
10 get anyone at that rate.
11 But in Carrefour people like -- the
12 Chinese are all about prestige. And there is
13 prestige -- you think of China as the knock-off
14 capitol of the world. I have been to the Louis
15 Vuitton boutique in the middle of downtown Beijing
16 where you can buy zillions of knock-off Louis
17 Vuittons right around the corner. And these
18 beautiful Mercedes limousines pull up and these
19 gorgeous Chinese wives of millionaires strole into
20 Louis Vuitton and buy thousands of dollars of
21 legitimate French LV MG products, and that's so
22 great. They show off that bag. I see women in
23 China with the little bag that comes around the
24 actual purse to show that it's legitimate. So there
25 are ways you can combat that.

1 AUDIENCE SPEAKER: Because their husbands
2 have made pirated products.
3 MR. WILSON: Probably, yes.
4 MR. BENNETT: The question would be then
5 are products worth what the manufacturers say
6 they're worth or are they worth what people are
7 willing to pay for them?
8 CONGRESSWOMAN BLACKBURN: David, may I add
9 just a couple of points on this as we're talking
10 about the pirated merchandise. I did have a couple
11 of record labels that were in my office last week
12 who have been working in China. Of course, we know
13 that some of the artist agencies, CAA now has people
14 on the ground in Beijing. And they are working and
15 looking for outlets and ways that they can integrate
16 themselves into this market.
17 And one of the labels mentioned they had
18 met with Madame Wu and were into conversation there.
19 And had even offered if they could have access into
20 the market, that they would match the price of
21 pirators. Much of what you're talking about with
22 the CD compilation set that you have, just so that
23 they began to place that value, and have them
24 understand they, too, can create an indigenous
25 entertainment industry that will use this

1 technilogical product that they are creating, and
2 then be able to sell not only the true for value
3 CD's from the indigenous industry, but at the same
4 time bring some of the -- an additional or greater
5 sum if we can up the number of CDs allowed, if we
6 can up the number of DVDs allowed into the
7 marketplace. They said this as they seek to address
8 the situation that exists which currently 85 percent
9 of all music sold in China is pirated; 95 percent of
10 all movies sold in China are pirated.
11 And getting convictions, having the
12 Chinese have laws on the books that we can negotiate
13 our trade agreements to and then enforce those laws,
14 that is something that we've got to keep our eye on
15 the ball with. They are increasing their number of
16 rates, but they are not where they need to be with
17 prosecutions and convictions.
18 MR. HERBISON: Patrick, I'm Bart Herbison.
19 I'm the executive director of the Nashville
20 Songwriters Association International. And the
21 committee should know we're very proud of that
22 Nashville in our name, but we do have chapters in
23 105 cities.
24 I want to thank you and the chairman for
25 bringing this proceeding to Nashville today. I

1 think it shows his commitment to the issue. I want
2 to thank David Bennett. We've had a great film
3 office under your leadership because you care. You
4 have a passion for what we do.
5 I want to thank BMI and Paul and Harry. I
6 want our songwriter members to know, this guy right
7 here, BMI cares so much about our issues, that I
8 believe this is the only position in the country
9 where a man is in charge of all 50 state
10 legislatures. Fred monitors good and bad that might
11 happen to us in all 50 state capitols. And I want
12 to give him a hand for a great job. (Applause.)
13 And, finally, thank you to the champion.
14 We've got no greater champion in this industry,
15 songwriters or intellectual property, than
16 Congresswoman Marsha Blackburn. (Applause)
17 Having said all of that, I think the
18 greatest picture we could paint on the urgency for
19 this issue is a fact. And that fact is we've lost
20 more than half of America's professional songwriters
21 over this past decade. There are three reasons for
22 that. The first was the deregulation of radio; and
23 then corporate mergers; but the biggest reason of
24 all is piracy, both on line and real piracy. I
25 can't give you a more startling statistic, that half

1 of this profession does not do it anymore not
2 because they don't want to; the opportunities simply
3 don't exist.
4 A question I have for you and the
5 Congrosswoman is, what is our political strategy for
6 this? Is it all on the diplomatic front now? Are
7 we considering some sort of sanctions? I did notice
8 the other day, I was watching ESPN. The Chinese
9 made sure they got part of Yao Ming's marketing
10 rights. That government kept their intellectual
11 property. That did not sit too well with me. So
12 could you respond to that? What is sort of our
13 political -- how are handling it? Are we going to
14 put pressure on?
15 MR. WILSON: Well, there are two parts of
16 that. I will say absolutely what Congresswoman
17 Blackburn mentioned just now is an important part of
18 the cultural change that's going to go on in China,
19 and that is as the Chinese are making more
20 intellectual property, as their economy develops,
21 they're going to seek more protection. House of
22 Flying Daggers was one of the largest Chinese
23 productions to premier in the west. And it grossed
24 about $70 million in the United States. It's a huge
25 hit. It cost $15 million to make in China. It

1 grossed $70 million in the United States. Massive
2 intellectual property win for a Chinese company.
3 That had an impact.
4 But the real answer to your question is
5 politically what is happening. Let me just tell you
6 what your government is doing. First of all, if
7 you're going to write down anything today that you
8 walk away with, I will tell you this: go to
9 www.stopfix.gov, g-o-v. It's also stopfix.com, too.
10 Those are registered. It's the unified U.S.
11 government website for everything that the U.S.
12 patent and trademark office is doing, the office of
13 the U.S. trade representative, the office of the
14 department of commerce for intellectual property,
15 and the justice department, including the FBI and
16 others who are charged with protecting America's
17 intellectual property. They created this website,
18 and it is a portal for everybody who is a songwriter
19 that says, hey, I just found out that my CD of the
20 song that I wrote is being sold in Beijing for four
21 cents.
22 There is a whole -- there is a tool kit on
23 there. You can click it and it says, small business
24 IP tool kit. It shows you where to report this to
25 the U.S. government so somebody is making a record

1 of the availability of your products to be sold to
2 the Chinese illegally. That tool kit is there. And
3 that is across the government -- the U.S. government
4 working on this, focused on this. That's internally
5 to get you guys to focus on what is being taken out
6 of your proper.
7 Secondly, there is the international
8 effort that is political. And the good news is, is
9 that there is a broad consensus on this, because,
10 again, we're talking about our number one export.
11 This is not some cute boutique product we're talking
12 about. IP is America's export, period.
13 So the office of the United States high
14 representatives which is a part of the Whitehouse as
15 well as all of the other orgs. of government,
16 including the one that we have here, in the
17 congress, our U.S. China interparliamentary
18 exchange, are all focused on raising this issue
19 everywhere. We're doing it in China.
20 You know, there's piracy that's moving
21 from China. There are Beijing fabs for DVDs that
22 are moving to South Korea because of the pressure.
23 We're making success. We can measure some of the
24 success by, you know, in January of this year, 150
25 of the top recording artists in China, Chinese

1 language stars, had a rock concert, a music
2 festival, in Beijing at the olympic stadium. They
3 stood on this huge banner that said stop piracy.
4 And all of these artists said, you're killing us, we
5 can't make any money selling Chinese language stuff
6 because they're making it in South Korea and sending
7 it to China. We're not making any money at Chinese
8 recording studios.
9 I mean, there are positive steps. The
10 Chinese are doing some things to come into
11 compliance. There are lots of market pressures that
12 are, well, maybe we should do nothing because we
13 want to sell these DVDs. We want to make sure
14 things are cheap. There are countervailing forces
15 at work all the time; but as far as like an overall
16 arching political strategy, that is something that
17 Mrs. Blackburn has been taking the lead in the
18 congress to educate members.
19 This is the hardest thing in the world. I
20 mean, I know that -- I went over to the chairman
21 this year, and sat next to Marsha and saw the
22 industry as it is, not as it appears on CMT
23 television or not as it appears in the glamerous red
24 carpet part that maybe the tiny bit of your industry
25 that gets into an average member of congress' brain

1 about what this is. That is a perception that we're
2 helping to change, and by working with Congresswoman
3 Blackburn and the songwriter's caucus, we're able to
4 change the minds of political leaders about what a
5 grave concern this is.
6 That breaks my heart what you said about
7 we're losing half of our songwriters. I mean, I'm
8 sitting in the belly of the beast here, corporate
9 America of the music industry, and I'll tell you, it
10 concerns me. The mixture of interests. When I sat
11 in a room like this for the motion picture industry,
12 I looked at them and I said, you know, there is a
13 problem. If I were in the motion picture idustry, I
14 would tell China, screw you, we're not giving you
15 any movies. You won't let us have any more than 20
16 - that's it, not one, you're not getting any. Which
17 would be hugely embarrassing to the Chinese.
18 Because they love their Beijing Premier, whether
19 it's Star Wars. They had a premier just like they
20 did in London, and it's cool and it's sexy and it's
21 neat, and everybody wants to be a part of it.
22 I looked at those guys and I said, hey,
23 Sony, tell China to go stuff it. Don't give them
24 any movies. It's not worth that much money to you.
25 They're like, well, actually, unfortunately, we

1 don't just make movies, we have all these other
2 interests that we're negotiating with the Chinese.
3 So we have to kind of be nice to them. It's very
4 complex because these huge companies that are the
5 entertainment have a myriad of interests everywhere.
6 And they're looking out for all of them. And they
7 can't just say stuff it, we're not giving you any
8 movies. They're like, well, actually, we want
9 satellite access.
10 And if you are a distributor and a maker
11 and a retailer, which a lot of these people are, and
12 a broadcaster, which many of these people are all of
13 these things, it makes it very messy to go around
14 pounding tables and demanding things. Which makes
15 it all the more important for your elected leaders
16 to really carry the banner. And we're very excited.
17 One of our own, a good conservative Republican from
18 Ohio, the president has just named our U.S. trade
19 representative, a really good guy, honestly. He
20 knows about IP. He's one of the most text savvy of
21 congress. He's a great guy. And we're really
22 hopeful that Rob Portman at the U.S.C.R. is going to
23 do a lot to help out on this issue.
24 MR. HERBISON: I cannot encourage you
25 enough to follow up on Jerry's suggestion to take a

1 songwriter. Some songs they know in China, but this
2 is the person that actually wrote it. It's so
3 powerful. Where are sanctions in this mix? Are we
4 talking about that? I know there is an existing
5 one.
6 CONGRESSWOMAN BLACKBURN: I'll borrow the
7 microphone from Bart, and just respond on a couple
8 of things. On what we're doing and is there a
9 strategic plan, and are we looking at it as a
10 comprehensive issue, yes. There are -- there is a
11 growing number of us that are doing that. And what
12 we have seen happen over the past 18 months or so
13 with intellectual property is not just an issue that
14 you see covered by judiciary or commerce. We've had
15 hearings in government reform. Small business has
16 become engaged in the issue. We're seeing more and
17 more activity come forward, things we're working on
18 you all with, and ways and means, and the education
19 process that is taking place as those members are
20 moving to understand that it is an issue.
21 And, you know, I think that's one of the
22 biggest hurdles that you have to jump first, is a
23 certain amount of education must take place so
24 people realize what it is. We can define what the
25 problem is, and then define what some possible

1 solutions will be. Well, building that kind of
2 foundation takes a little bit of time. And you all
3 have been tremendously instrumental in that.
4 And now what we are seeing is in the
5 hearing that we had on Thursday in Energy and
6 Commerce where I was questioning the under
7 secretary, we talked about raising these issues with
8 the WTO where we require some of these countries
9 where we have trade agreements, China, looking at
10 Vietnam, looking at Brazil which is a growing hot
11 bed, looking at India, and beginning to require
12 prosecutions.
13 And I've asked that they go back, you
14 know, when they've upped the number of raids, that
15 they be able to detail for us what number of those
16 brought prosecutions, convictions and prosecutions
17 and penalties and what they are. Because the
18 Chinese just want to say we've increased our rates
19 19 percent, we've done 40,000 more raids. Fine.
20 Then what did that merit, and what type penalties
21 are being attached? Because they continue to go
22 back and talk about Golden Sciences Technologies
23 conviction that we got last July. And then they'll
24 continue to come around and they'll say, well, Silk
25 Alley got closed. Well, but they built this big

1 building across the road from Silk Alley.
2 So we want to see what the results are.
3 And that accountability is what Patrick is speaking
4 of. That's a pressure that they have not known.
5 And other nations are watching as we negotiate
6 looking at the Gelan agreement. Then as we're into
7 the Kapta agreement, we are on the front end
8 discussing the intellectual property issue, and have
9 reported back to you all twice on trips into Central
10 America as we've looked at Kapta to be certain that
11 they have something on the books that we negotiate
12 to.
13 And, you know, working, trying to find
14 NGOs. You and I have discussed this, Bart, and the
15 need for NGO. Even though we don't participate in
16 that, it's nice to know that NGOs are there, and
17 they're encouraging these nations so that --
18 MR. HERBISON: You might explain what that
19 is, because this is important.
20 CONGRESSWOMAN BLACKBURN: Right. An NGO
21 is a nongovernmental organization. And I was in
22 Vietnam last year at the luncheon, the American
23 Chamber of Commerce in Vietnam, and sitting next to
24 a young man that was involved in entertainment and
25 pharmaceuticals, and American educated working in Ha

1 Noi. And we were discussing the piracy issue and
2 the fact that there was not an NGO in place to help
3 with the education with many of the developing
4 nations about why we needed these laws on the book.
5 And I recommended that I put him in touch with Bart,
6 which I did, so that there could be a link to how an
7 NGO could work, what the type laws are needed, what
8 the problem is, how we see it, how we see piracy as
9 a problem here.
10 So that type bridge building has got to be
11 there first. We've got to have them participate
12 with laws on the books, and then agreeing to enforce
13 those laws, and being able to include that in the
14 trade negotiations. We're not there. We haven't
15 done all that we should be doing to get us to the
16 point we need to be. We have made tremendous
17 strides. And I think the leadership in the house
18 has gone a long way.
19 It's like Chairman Manzullo upping this on
20 their radar and having this here today. The type
21 field hearings we're doing, they're a first. It's
22 the first time in a long time. Fred, I'll pass it
23 to you.
24 MR. CANNON: That was an excellent report
25 of the status and everything. I would just like to

1 ask -- and maybe Patrick or the Congresswoman --
2 what is happening with the World Intellectual
3 Property Organization? Are they fundamentally
4 active and are they pursuing this in a big way?
5 MR. WILSON: Yeah, this is actually
6 something that's fairly new. The World Intellectual
7 Property Organization is exactly what it is. It is
8 essentially -- most of the G -- 7GA countries have
9 representatives, but for the first time, the Chinese
10 have designated a senior member of the central
11 committee of China to serve as a liaison of this
12 group. And they have, particularly, have a
13 protected effort on IP. And that is something that
14 is very new.
15 And, again, the laws in China are only --
16 they're not even three years old yet. Having actual
17 laws on the books against intellectual piracy left
18 is new. So getting the police to understand that
19 you're doing enforcement, doing measures of how the
20 enforcement is going, knocking on doors and kicking
21 things down and confiscating fabs and all that stuff
22 that goes on, I mean, it's a relatively new thing to
23 China. Of course, we want it immediately because
24 we're seeing this devastating impact. But there
25 have been some successes that we've been able to

1 win.

2 As far as like you were talking about

3 punishments, what tools are available in the tool

4 box, opening WTO complaints. I mean, China is now

5 in the room. They used to be, before WTO admission,

6 they were outside the room. Now they're at least

7 tacitly saying, please hold us to this world

8 standard of what is --

9 AUDIENCE SPEAKER: Are they WICC members?

10 MR. WILSON: They're not. We would like

11 that. It's all incremental. But they have this

12 representative who is the chief person. I can't

13 remember his name, but we actually met with him.

14 MR. BENNETT: Is it true that because they

15 are participating in WTO now, that we cannot

16 sanction them as we did 15 years ago? We have to go

17 through the WTO to --

18 MR. WILSON: It's part of the cost and the

19 benefit of being inside the room, is that everybody

20 agrees to play by the rules. If you want to slap

21 them and treat them as an nonmarket economy, as they

22 still are, but they're a nonmarket economy within

23 the WTO, so we use this world forum as a way to

24 impose sanctions and get concessions and changes and

25 stuff like that. It has its blessings and its

1 curses. Before, when it was a more crude
2 relationship, we could use the power of the congress
3 or the presidential authority and just deem them not
4 in compliance and impose tariffs, restrictions or
5 whatever.
6 But the important thing to remember here,
7 and this is something that maybe we haven't
8 mentioned yet, is that primarily, this is not an
9 issue about intellectual property coming back into
10 the United States. This is something that the
11 government does a really good job of. And we had a
12 lot of piracy here, like on-line piracy, and we've
13 got the Grokster case and all of this other stuff
14 happening; but there isn't a flood of DVDs coming
15 into the United States that are made in China.
16 That's sort of the good news, or whether it's music
17 or whatever. This is a Chinese domestic market.
18 It's an overseas domestic market problem.
19 But the WICO issue for China is they had a
20 meeting in March of this year. The whole
21 organization met in Beijing. And, again, anything
22 that we do that raises the profile of accountability
23 on intellectual property protection is we consider a
24 victory. Whether it's mouth lip servicing, in some
25 respects, yeah, that happens.

1 MR. CANNON: You said that South Korea was
2 pirating Chinese product. Are they a part of the
3 WICO?
4 MR. WILSON: Yeah, they are. South Korea
5 is a unique and different situation. We have a very
6 -- they have a very strained relationship there on
7 intellectual property; but the bigger problem is
8 actually -- just to show you how your piece fits
9 into the overall piece that -- the 8,000 of you that
10 I have to look at all the time, I mean that is
11 stolen intellectual property that is more tangible
12 than intellectual property.
13 If you are a machine maker -- my boss is
14 from Rockford, Illinois which is the machine tool
15 capitol of the world. You build a really complex
16 machine that makes everything in this room, whether
17 it's the dies that casts the pieces of this chair,
18 or the tools that are used to fit the upholstery,
19 those are all made here. And what happens is, is
20 that they're knocked off all over Asia. And they
21 even print the brand name right on there. It would
22 say Montgomery Tool, which is a company based here
23 in -- a tool and die company based here in
24 Tennessee. And then Montgomery Tool would get a
25 call from an American suppylier. And they're, like,

1 I bought your replacement part for this thing and it
2 failed and somebody died. And they're, like, wow,
3 we don't remember selling you that tool. Well, your
4 name is right on the part, and it failed. And
5 they're, like, we didn't make that. Come to find
6 out through a costly bit of litigation, that that
7 was a knock-off part. They just took one of them,
8 copied it and made thousands of them and sold them
9 for a tenth of the price of the original creator of
10 that product. And then they're faced with a
11 liability and a costly lawsuit for a part they
12 didn't even make.
13 So this is a very multi-faceted issue; not
14 just in the IP world, but just all across the board,
15 people steal other people's good ideas, and that's a
16 big problem.
17 MS. SPRINGER: I'm Suzanne Springer. I'm
18 a songwriter and a member NSAR. Two things I've
19 thought of. You mentioned House of Flying Daggers.
20 What was the piracy impact on a Chinese-made movie?
21 I'm curious how did they suffer from that.
22 MR. WILSON: The impact on Chinese-made
23 movies is also the same, because they lose a lot.
24 They get better exhibitition rights, which is a cool
25 thing, because if you're a native Chinese-made

1 movie, you can get in more theaters at one time, you
2 can have greater exposure. But they lost money. I
3 mean, they needed the export market. That's the
4 ironic thing, is there basically would be -- not be
5 a for-profit. Because most of the movie industry
6 was state sponsored, cultural propaganda movies.
7 Independent film making couldn't exist apart from
8 markets, because there is Chinese-language markets
9 all over the world. I mean, there are two-and-a-
10 half million Chinese speakers in North America from
11 China in the U.S. that buy Chinese-language movies,
12 made in China. It's a huge market. So they
13 wouldn't make any money here except for the money
14 that they make as an export product which makes them
15 our best advocate.
16 And so when we go, when we take this
17 delegation in August, we'll meet with them. And
18 this is a new thing, to let the government let
19 independent people meet with representatives from a
20 foreign government to speak in common focus. It's a
21 totally new thing which is why it's so cool, the
22 idea of bringing a songwriter along. That would be
23 interesting.
24 MS. SPRINGER: And also that one -- you
25 mentioned the event with the Chinese artists,

1 recording artists. Was that the first of its kind
2 where they were actually protesting piracy?
3 MR. WILSON: It really wasn't protesting.
4 It was a government-sponsored thing. So I didn't
5 mean to make it sound so earthy and grass roots. It
6 was a government-sponsored excerise. It was carried
7 on national television. They had the biggest stars
8 in China on one stage at one time condemning piracy.
9 You know, we'll take that.
10 MS. SPRINGER: That's really significant.
11 MR. WILSON: I mean, that's why I'm
12 saying, you may have heard maybe in David or my or
13 even in Congresswoman Blackburn's voice a little
14 pessimism about we'll never get any changes. That's
15 not really true. It's incremental slow hammering.
16 I think one of the first questions someone asked me
17 was, what does this really matter, is it important
18 for congress to go, is it important for congress to
19 invite these parliamentarians to come to the United
20 States. And all I would say is that this is the
21 Chinese way, this tiny, relentless, ever-edging,
22 you're going to hear the same message from everyone,
23 it's not going to go away.
24 AUDIENCE SPEAKER: Chinese water torture.
25 MR. WILSON: Absolutely. We're going to

1 talk about it every single time. They need to
2 understand that. And it's the drip, drip, drip,
3 drip, drip that gets these concessions one after
4 another.
5 MS. SPRINGER: Yeah, like Congresswoman
6 Blackburn said, it's an education.
7 MR. WILSON: And that's on our side. What
8 we want to do is make sure every time they meet with
9 somebody, they hear the same message. Like, when we
10 go over there, we always tell the state department
11 we always want to have our members meet with the
12 state department. So every time a Chinese official
13 meets with an American about economic concerns in
14 China, they hear the same thing - market access,
15 intellectual property, we want patent protection.
16 Those are the three things. Those are our talking
17 points. We want to make sure every time a U.S.
18 diplomat meets with them, they hear that. Every
19 time they meet with a different member of congress,
20 they hear the same thing, so that there is no
21 daylight between our priorities about what must
22 happen in order for the economic relationship
23 between China and the U.S. and other countries to
24 develop.
25 MS. SPRINGER: Maybe some Chinese

1 recording artists and American recording artists,
2 because they may not have -- certainly they have the
3 product there, but they might not have the
4 visibility, the actual performance.
5 MR. WILSON: A lot of that has to do with
6 the market access, too. I think -- I forget your
7 name that went to Beijing to the music --
8 MR. VANDERFER: It's Jerry.
9 MR. WILSON: Jerry went to Beijing to the
10 music store. I had the exact same experience. Of
11 course, me being this little amateur fan, I want to
12 go see what is available in retail stores. That's
13 changing. There's more market access, but there's
14 not as much. And that's another issue we always
15 have to hammer them about is getting those artists
16 there. If I worked for the RIAA, which I don't, but
17 there is a guy here for RIAA, if I did, I would be
18 thinking about doing exactly that.
19 We haven't had a big country music tour in
20 China. We haven't had a big event there. But, you
21 know, if CMA asked my opinion, I'd say it would be a
22 great opportunity to get some of your marquis
23 players to go to China, stand next to Chinese
24 artists and say if you want more of what we make
25 which is fun, life-enriching intellectual property,

1 you can't have this culture of theft. And that's a
2 big part of it.
3 MR. WILDER: My name is Turk Wilder. I am
4 a songwriter publisher, same as everybody in the
5 room. The problem is huge that you were talking,
6 the way that there is a culture of threat. And
7 they're even knocking off golf clubs and Levis
8 Jeans, everything you can think of. What can we do
9 as writers, songwriters here in Nashville, to assure
10 that we -- the importance of our concerns don't get
11 shuffled to the bottom of the barrel as they usually
12 do, because we're songwriters, and ours remains an
13 important thing. Because outside of Nashville,
14 songwriters are looked at as the guys that clean the
15 bathrooms. We don't want that to happen here. We
16 want it covered.
17 MR. WILSON: First of all, I just cannot
18 let that go uncorrected. I am a total dork. I'm
19 some crazy lawyer from Washington who has come down
20 here and, gosh, songwriters, I'm like in awe. You
21 actually have real skills. My parents still wonder
22 what I do. No, I do not think that's true. I do
23 not think that songwriters and the product that they
24 create is in low esteem.
25 I mean, you ask any member of congress,

1 Republican, Democrat, in any part of the country,
2 and they will tell you all about their favorite
3 song, who they fell in love with while it happened.
4 And they will tell you that that is an issue, as an
5 economic concern, like what part does it contribute
6 to the economy. That's the eduction process that
7 we're going on, about to remind people that this is
8 our number one export. The product that these
9 people create, those lyrics, the poetry, the insight
10 that they bring to music, that is an important
11 export for us. And that's not about low esteem;
12 it's more about just pure uneducation.
13 When Congresswoman Blackburn brought
14 Chairman Manzullo here, he was on fire about this.
15 He was, like, look how big our coalition is. It's
16 not just these tool and die guys. The tool and die
17 guys think that they're even lower than you guys.
18 They're, like, I don't have sexy songwriters. I
19 just make boring metal tools. There's nothing cool
20 about that. No one is ever going to pay attention
21 that they're ripping off these cool metal-building
22 machines. There's nothing sexy about that. We're
23 going to lose our whole industry before anybody
24 notices.
25 So you're not toiling alone. This is

1 something that everybody who makes things -- and
2 tool and die makers are creative people. They bend
3 and make things to solve problems just like you bend
4 and shape words and phrases. But artistry is in it.
5 MR. KELLY: Songwriters, it's worse. You
6 know why? We don't have any way to make any money
7 with our product at all until it gets protected in
8 this way. We can't -- a tool and die person, they
9 can still make their stuff and go sell it on the
10 street. We can't do it. We've got to have --
11 they're taking -- when these people lift our stuff,
12 they are taking our brains.
13 MS. JACKSON: And this legislative --
14 limited is in congress as it is.
15 MR. WILSON: You've got to tell us your
16 name. This is the first time you've spoken.
17 MS. JACKSON: I'm Betsy Jackson. I'm a
18 singer, songwriter, publisher, also.
19 MR. WILDER: We are the only -- I can't
20 think of another occupation where congress sets the
21 amount of money that we are allowed to make. And
22 for us to get ripped off --
23 MR. HERBISON: We have a maximum wage.
24 MR. WILDER: We have a maximum wage. They
25 set our maximum wage.

1 MR. WILSON: That doesn't sound very
2 Republican at all. I'm not for that at all. How
3 did I get to be for that? That's very uncomfortable
4 for me.
5 CONGRESSWOMAN BLACKBURN: Well, we just
6 keep trying to visit, and Bart comes in and we visit
7 with some of the members and the chairman. And
8 it's, you know, progress has been made.
9 MR. HERBISON: It's ongoing.
10 CONGRESSWOMAN BLACKBURN: Let me say this:
11 Turk, I want to go back to what you were saying.
12 How you view things and how you address a situation
13 that came to be which is really what we find
14 ourselves doing. This is something that came to be
15 through legislation in the '30s, the '40s, the '50s.
16 And so you do now have congress setting a maximum
17 wage. It's in statute, a maximum wage you can earn.
18 And you do have that kind of cram down, if you will,
19 for lack of better word, on your industry.
20 And what Casey is saying is so true. Your
21 thoughts are your stock and trade. And what you
22 write and what you feel and put on that paper, that
23 is your stock and trade. And you want to be able to
24 hold some value to that.
25 Harry and I talked many times over the

1 past 10 years. One of the hardest things we have to
2 do is to convince people that a songwriter's
3 catalogue is probably worth a whole lot more than
4 the physical structure of the building in which that
5 songwriter sits. And have a banker, someone who is
6 in finance, someone who is in venture capital,
7 someone who is in government, understand that,
8 because it's an intangible, and you can't put your
9 hands around it, and you can't see it. You feel it
10 and you hear it. And it's tough. And that is why
11 we appreciate you all thinking out loud with us on
12 this issue.
13 A couple of things I want to say, because
14 the education process and having people understand
15 the issue is at the crux of this. And that is why
16 the songwriters caucus came to be.
17 Another thing is we have watched our
18 nation in the last few years shift from an
19 industrial economy to a knowledge economy. And the
20 basis of that knowledge economy is intellectual
21 property. And whether you are creating
22 pharmaceuticals, designing cars, creating products
23 that are sold that we wear, books that you read that
24 stimulate your thought, music that you listen to
25 that inspires your soul, it rests on a knowledge

1 economy.
2 Now, one of the things that hampers this
3 is that as you look at that knowledge economy, and
4 look back at the industrial economy, the industrial
5 economy is based on something you see and feel and
6 produce, and you can look at that production. We
7 have a legislator here in the state of Tennessee
8 and Bart and I have discussed this, because I've had
9 the conversation with the gentleman time and again
10 over the past few years, how do you have a value to
11 something that you can't touch, that you can't see.
12 And so that is the difference. Part of
13 the problem is in our laws and constructs -- and
14 David and I were just talking about the SIC codes
15 which are the standard industrial codes which are
16 based for an industrial economy. And if you want to
17 capture anything, everything, and all things in the
18 entertainment industry, it would come under
19 copyright. Well, you know, that's kind of tough to
20 capture a lot of what you all do under copyright.
21 Those things have not been updated in years and
22 years and years.
23 So there is so much. Government moves
24 very, very slowly. We have made a lot of progress
25 in the past couple of years, but we've got a long,

1 long way to go. And as long as you all will hang in
2 here with us on this issue and help keep educating
3 and will talk to us so we can listen, I think we'll
4 get there, but it will be a long process.
5 I'm going to pass the microphone back. In
6 a few minutes, I have to slip out. I have a 5:52
7 flight back to D.C. tonight because I have to be
8 there at eight o'clock in the morning for something,
9 but I've got my notes. We have the transcription.
10 And we're going to look forward to having you all
11 there. And I love the idea of the songwriter in
12 China. This is a great idea. Thank you, so much.
13 (applause)
14 MR. BENNETT: If I could add one thing
15 real quick. Betsy, I know you want to go next. And
16 Dr. Ming Wang is with us. Of course, we want to
17 hear your comments. I want to remind you all that
18 Marsha Blackburn has been involved in this issue for
19 10 years now, since 1995, as my predecessor at the
20 Tennessee Film and Entertainment Music Commission.
21 I have files there that you conducted meetings like
22 this 10 years ago.
23 And so as she speaks to the issue of
24 government moving slowly, don't forget for one
25 moment how top of the mind it stayed with her. and

1 as she's gone onto Washington, how she's carried it
2 forward to this position that she has now. One of
3 the problems that she's dealing with in meeting with
4 the Chinese officials, and maybe Dr. Wang can
5 address this also, is the fact that the federal
6 Chinese government can pass a law, but how long does
7 it take to trickle down to the local governments and
8 get their buy in on that law also. The local
9 governments kind of are problematic somewhat. Even
10 if the Chinese government buys into it, the local
11 provinces sometimes have difficulty enforcing it.
12 Betsy, do you want to say something?
13 MS. JACKSON: I was going to support that.
14 That was pretty much what I was going to say. I am
15 Betsy Jackson, singer, songwriter, et cetera.
16 How many -- I mean you say nine out of ten
17 are possibly corrupt. How many of the people really
18 are the corrupt ones? Is it the local governments?
19 Who are the people that are getting the money?
20 And you said education. That really
21 struck me. I didn't know that in China, if it's
22 written down, it's public domain, and here is
23 copywritten. That's education for me.
24 And one of the things that really -- I've
25 taught other people, and is a good way to teach

1 other people is when I was a child, 45's were 99
2 cents. And it's funny, they download a song now,
3 it's 99 cents. It hasn't changed much. The only
4 difference is I had something physical to hold onto.
5 Now kids download it. And one way I tell parents
6 when -- if a kid wants their credit cards to
7 download something, well, do your chores. When I
8 wanted a 45, I'd say, mom, I want -- well, go do
9 your chores, you get the 99 cents, you go to the
10 store and get it. Well, go do your chores, you get
11 my credit card, you download a 45. There is no
12 difference.
13 In fact, I told that to my friend, a
14 preacher, and she talked with the parents, how
15 stealing is not the issue, that you can teach your
16 children the right way to do it. It's just
17 educating the parents. And it's kind of educating
18 the people, now, of the right way to do it.
19 MR. BENNETT: Dr. Wang.
20 DR. WANG: Thank you for the invitation.
21 Sorry I'm late. Driving back from Memphis, we ran
22 into traffic. I appreciate Congresswoman
23 Blackburn's attention and the whole government's
24 attention to this issue. I want to say two points.
25 One, if you look at the global scale, the large

1 scale, China is a representative of east Asian
2 country, and U.S.A. is a representative of western.
3 What is the basic difference of people's mentality
4 as it relates to intellectual property such as
5 music? It's one fundamental difference. Because an
6 old man has to just stick with the way he or she is
7 used to doing things, that's the example of ancient
8 Asian countries. A young man can sets by rules and
9 go by the rules - an example, the United States, the
10 young man. Asian countries are older, and they're
11 used to the way they've been doing it.
12 Modern economy require infrastructure,
13 legal structure. Rules and regulations is foreign
14 to Asian countries, as opposed to the United States.
15 Rules were set relatively early. A young man is
16 comfortable, going to good school, getting good set
17 of rules and go by it.
18 So we have to recognize this fundamental
19 difference in people's mentalities. In China,
20 things that get done by connection, not by a
21 business plan. So we have to recognize that that
22 part of the world is going to come around slower in
23 recognizing the importance of modern infrastructure,
24 rules and regulations and legal guidelines.
25 I go to China frequently. Last year I was

1 there three times, and we'll be going soon to
2 lecture. Economy is explosive, developing, and
3 opportunities are there.
4 So that relates to my second question. If
5 we say United States today, China tomorrow, what
6 lessons can we learn from the United States in the
7 past 10, 15 years in the music industry that may
8 apply to China that can help convince the Chinese
9 officials in your interaction, that what they can
10 watch out and prevent some mistakes, and make modern
11 China make its technology.
12 If you look at from record, you know,
13 turntable to cassette to CD player, now to what I
14 call the future of music, formless, complete
15 formless. There is less, no physical device. You
16 just download it, the 99, and then example. That's
17 the future. So the United States has gone through
18 this technilogical transformation. China is on path
19 to it.
20 And I think technology can play huge role
21 in setting structure right. And so that we at least
22 don't have to rely upon the slow conversion, if you
23 will, of Oriental economy. Just say, okay, in the
24 United States we're going to this formless music
25 now, internet direct download and CD. A physical

1 device will be a thing of the past very soon. And
2 China, you are going to go in that direction also.
3 So let's kind of look at the United States today,
4 China tomorrow.
5 Can we set rules, governing rules,
6 technilogical guidelines anticipating this upcoming
7 formless shape presentation format of music, and
8 anticipate the problems, and maximize the
9 possibility to set those rules as technilogical
10 based; not having to trust on the understanding,
11 because it will be, and I think it's what makes the
12 world interesting, is different mentality. Orient,
13 east, that's the way it is. We're going to devise
14 rules later. West is rules first, and then we
15 behave accordingly. I think that makes the world
16 interesting and dynamic, exciting. We need to
17 recognize the fundamental differences. We need to
18 recognize the United States today is China's
19 tomorrow.
20 Let's learn a lesson from ourselves, how
21 we transform technology, and can we help Chinese
22 devise rules anticipating tomorrow they will go form
23 this music as well. And can government, legal
24 system, set up and anticipate the change. Not so
25 much you have to depend on a slow conversion of an

1 old man, as you know, is usually not successful.
2 Thank you.
3 MR. BENNETT: Dr. Wang, that was a very
4 interesting point you brought up. Of course, many
5 of you know Dr. Wang is a native of China. A very
6 interesting insight and just what we needed in the
7 conversation today, because that brings up a point
8 we may discuss. Is there an opportunity to create
9 technological partnerships with Chinese companies.
10 For example, could we develop a kiosk that we could
11 download our product into that they could then
12 purchase out of this kiosk on to what would be the
13 Chinese equivalent of an I-pod? Is that one way
14 that we can help? Is it a technological leap and
15 not so much a regulation leap? I think that's a
16 very interesting point about how long it takes the
17 old man to get what we're talking about. Andy?
18 MR. VANROON: I'm Andy Vanroon. I sat on
19 a a board of an NGO with David Bennett called Film
20 Nashville, and we have somewhat of a film contingent
21 in this room.
22 I have three sort of little observations.
23 One is, I would be very interested in knowing how
24 the folks in China and India look at how we're --
25 regarding enforcement, how they're looking at our

1 ability to enforce, you know, the issues. They have
2 to be looking at our own inability to try to control
3 the music being stolen in our own country. So that
4 has to be a big issue they're contending with. How
5 do we deal with it in China if we're a new market
6 economy, and you are an old market economy setting
7 the stage for the rest of planet, you can't even
8 control it in your own borders.
9 Secondly, I would say going with what
10 Patrick was saying, and he said something very
11 important things like an hour ago, and that is our
12 number one revenue generating source right now --
13 and Marsha has certainly talked about that -- is the
14 knowledge economy, is IP.
15 To me, a very simple thing to do, you
16 know, following on the Chinese movie model is to go
17 to China -- maybe you're already doing this, but I
18 am just corroborating it -- if you were to go to
19 China and talk with Dr. Wang, as you said, China is
20 the U.S.A. in the future, to me if you went 20 years
21 down the road and said let's analyze all of these
22 areas of intellectual property that you, China, will
23 be doing in 20 years, and let's add up the trillion
24 dollars that that will amount to, and if we,
25 America, and all of the other consumering countries

1 on the planet took all of your intellectual
2 property, you would be losing a trillion dollars a
3 year in 10 years. I think that would be a simple
4 thing to do, to list all of the different IP.
5 The third thing is what David was saying.
6 I was involved a couple of years ago with a company
7 called Cinema Presents. And the idea of the company
8 was in movie theaters around the country -- Regal
9 was actually one of the companies we were working
10 with -- was to literally have a machine in every
11 movie theater where you could literally buy the DVD
12 and the CD.
13 Now, the interesting thing that we talk
14 about with 20 films a year being shown in China, but
15 in reality our biggest box office, the majority of
16 box office receipts every year, are really with the
17 top 10 films coming out of Hollywood. So the top
18 20, you know, are going to do well. If we basically
19 had a mechanism in China on the ground in movie
20 theaters where people went to see these top 20
21 movies, to sell DVDs at their rate using David's
22 idea of being able to burn the DVD there and the CD
23 there, then you could have a practical mechanism to
24 bypass the need for fulfillment and you could simply
25 burn the property right there at the cost that

1 they're buying it for on the streets right there.
2 That's all I have to say. Thank you.
3 MR. WILSON: I thought you made a bunch of
4 good comments. I don't know if you were inviting me
5 to reply to them, but I felt compelled to. I almost
6 said something right in the middle. The first thing
7 is you're absolutely right. I continue to be very
8 impressed with all of you, your understanding of the
9 way the debate goes with the Chinese. Certainly,
10 the Grokster case is a perfect example, and the
11 Chinese will cite that. The commerce department of
12 China, they'll very often say, well, you know, this
13 is obviously a problem we all share. And there is
14 truth to that.
15 I mean, the recording industry has
16 launched a very high profile, a very costly in terms
17 of reputation and public opinion, and also just pure
18 cost to go after amateur pirates in the United
19 States. Perhaps some of your children our pirates.
20 My own boss had to be told. This was just a year
21 ago. I had to tell him about the Morpheus program
22 that his 19-year-old college freshman son had
23 installed on his home computer that he shares as a
24 member of the judiciary committee with hundred's of
25 songs stolen right on his own computer. And he was

1 shocked and saddened and upset about this, but it
2 was an education process.
3 But the difference is between China and
4 the United States, and this is the distinction we
5 have to make, none of these are just pure, like all
6 the angels on one side and all the devils on the
7 other. It isn't that way.
8 The difference is that 95 percent of all
9 of the intellectual property in China is pirated;
10 whereas, in the United States, the marketplace, many
11 in the industry, we have somebody here from IRA that
12 might be able to tell us, but the industry is less
13 than 20 percent of the revenue of the industry, the
14 available IP product, whether it's movies or music
15 or whatever is really pirated. Even if you get a
16 really generous definition to, like, all the
17 downloaded illegal mass music and all of that
18 together, it's a much, much smaller part of the
19 industry which is more typical.
20 You're never going to get rid of piracy.
21 Piracy is as old as commerce, period. It's also
22 going to be with us, whether it's the Barbary
23 pirates off the cost of Lybia at the founding of our
24 country or whatever, there's going to be people who
25 want to take advantage of other people's hard work.

1 They are cheaters in every middle school and high
2 school in America. That's the way it works.
3 The question is it cannot be normative.
4 Not to overstate that too much, but currently in
5 China, as Dr. Wang alluded to, it's normative to use
6 something created by something else with no
7 attribution or payment. It's not normative. It's
8 outside the norm in the United States.
9 The second thing is the value of China's
10 IP in 20 years. China is an amazingly gifted and
11 well-led country. We're thinking about the next
12 quarter, they're thinking about the next quarter
13 century. They are excellent at planning,
14 particularly in such a central-planned economy.
15 They've got the communist legacy in China. And so
16 they've always got these five-year, ten-year,
17 thirty-year plans. In congress we have a much
18 harder time doing it that way.
19 They recognize this is going to happen.
20 There is self interest in this. Why did all of
21 these music stars stand on a platform in Beijing to
22 denounce piracy? Because they know where it's
23 going. House of flying Daggers is a perfect
24 example. You know, it's like, wow, this is
25 important to us. We're Chinese filmmakers.

1 And part of the thing I can tell you that
2 is encouraging is look at Hong Kong. Hong Kong was
3 the wild west of IP only 25 years ago. Now it is
4 completely up to international standards. They have
5 very little piracy there. Excellent rule
6 enforcement. Granted, they have all of the benefits
7 of a British legal culture that is probably superior
8 to our own and excellent judges and enforcement of
9 contract. But it used to be a massively corrupt
10 place 25 or 30 years ago.
11 Now, because of the Hong Kong movie
12 industry which is huge, Jackie Chan, it's huge, it's
13 a massive world-wild market worth millions of
14 dollars. So, of course, IP protection now is huge,
15 too. I think eventually we're going to get there in
16 China because the marketplace is going to grow to
17 the extent that it's going to be in their interest
18 to have it, too. The problem is how many
19 songwriters will we lose while we wait for it to get
20 there? How many small business manufacturers?
21 We are losing a tool machine tool maker --
22 in the United States we have one. This is just a
23 random aside. Cold forming machines are a special
24 kind of manufacturing machine that shapes metal into
25 various simple products, whether it's molding the

1 parts of this chair or whatever. There is only one
2 cold forming machine manufacturer left in the United
3 States. There used to be hundreds. Every town had
4 one.
5 Do you know what cold forming machines
6 make? They make bullets. It's a very important
7 product for any country that expects to protect
8 itself needs to have. We only have one left. It
9 snuck up on us. We're shocked that this industry
10 has left our shores. That's what we want to avoid
11 by our inaction on intellectual property.
12 And I was taking good notes on all of your
13 points that you made. You made a bunch of them.
14 The last one was about movies and theaters and the
15 market access question about film. Mike is -- we
16 work very closely together. He's brought this to
17 our attention so much. Mike is the principal
18 staffer of the songwriters caucus. I work with the
19 movie industry a lot. That's one of the things I
20 have been helping them to redefine themselves more
21 as a small business industry.
22 And this access issue about getting movies
23 in theaters in China is something that we're going
24 to have to solve, because the Chinese want to go to
25 the movies. They want to see these movies not on

1 the tiny screen in their -- I mean, their apartments
2 are smaller, they're cramped, they're not air
3 conditioned, it's not pleasant. It's not like --
4 you guys imagine here in suburban Nashville, the
5 neighborhood where I saw today. It's lovely at a
6 home theater to watch a movie at home on DVD. It's
7 great. You can sit on the floor and have your own
8 popcorn and everyting else. But it's not the same.
9 There is a huge market, there is a huge demand in
10 China for going out to the movies just like there
11 was in the 1920s and '30s as the movie industry grew
12 in America. Going out to the movies was a great
13 occasion for a family to go out and see
14 entertainment in a beautiful air conditioned,
15 environmentally delightful environment to see a
16 movie. And there is demand for that. And until we
17 get Regal or someone else to get some investment in
18 China to be permitted to have more screens, we're
19 going to be at a great disadvantage in incremental
20 changes.
21 MR. LAMB: My name is Kevin Lamb, and I am
22 the vice president of Peer Music here in Nashville.
23 There has been a number of comments made this
24 evening -- references, rather, to bouts of trade
25 issues. Prior to being at Peer Music, I served on

1 the board of directors of the National Music
2 Publishers Association, was on their international
3 committee. And my experiences on there tell me that
4 at least during that time period, anywhere from 40
5 to 60 percent of a music publisher's income is
6 generated outside of the United States.
7 I recall not too long ago at an ASCAP
8 general membership meeting when they posted their
9 figures up on the -- their presentation there, that
10 roughly for every one dollar they paid out to
11 foreign composers and publishers, roughly four
12 dollars was coming in. Harry was kind enough to do
13 some research for me at BMI. And that was pretty
14 much the same case as BMI.
15 So I submit that to you since you're
16 looking for facts, more or less, to say that
17 probably the effect of piracy outside of the United
18 States is going to have a much greater impact on our
19 industry than you realize.
20 Secondly, this is an industry, the song-
21 writing community, is an industry that is an
22 industry that doesn't affect our -- or harmfully
23 affect our environment. We don't cause air
24 pollution, we don't cause water pollution.
25 MR. WILSON: You might cause over

1 population. All of that extra romance from those
2 movies and music.
3 MR. LAMB: But it's a resource in and of
4 itself that the average government recognizes to the
5 extent that they do not tax playrights, recording
6 artists, songwriters, et cetera, on the royalties
7 that are generated because of the not harming the
8 resources, so to speak.
9 And the last thing I want to mention is a
10 bit more on the personal side for me. My oldest
11 daughter wrestles with depression. And during some
12 of her most darkest bouts, if you will, one of her
13 sources of strength was the song I Hope You Dance.
14 I worked for Alabama for nine years and read an
15 awful lot of fan letters that came in. and I know
16 there are songs out there that have kept people from
17 suicide, that have held marriages together, have
18 been inspiration for any number of things. And
19 that, as the commercial says, is priceless. Thank
20 you.
21 MR. WILSON: I think that is an intangible
22 benefit of artistry. I'm one of those crazy liberal
23 supporters of arts and entertainment, because I
24 believe that is something transcendent. And that's
25 why what you do has so much respect from me. That's

1 why I kind of laughed when you said this low appeal.
2 Because somebody like me who doesn't know anything
3 about -- I mean, God bless the people who have to
4 sit next to me in church and hear me sing. I mean,
5 my God, I don't have that skill. And I respect it
6 and admire it so much because it has its impact on
7 me.
8 But something more mundane about what you
9 said is that five percent of the world's consumers
10 for stuff live inside the boundaries of the United
11 States. Think about that. Five percent of the
12 people in the world live here. Everyone else lives
13 somewhere else. If you're not thinking about
14 selling your stuff to all of the rest of the people,
15 it's a pretty big marketplace. And whether it's
16 country music in Sweden or Isreal or China or South
17 Korea or whatever, they want to buy our stuff. We
18 are in a pretty privileged position because we make
19 a lot of really cool things, we make a lot of really
20 cool songs. We have the most ubiquitous cultural
21 impact of anything.
22 I mean, I was bicycling down the road in
23 Lombok, Indonesia in 2003. And not only did I walk
24 past a cafe in the most remote part of the world and
25 see a kid in a Yankee's cap listening to Nirvana in

1 Lombok, Indonesia. Our cultural is powerful and
2 it's in demand, and it's a product we can be proud
3 of, for the most part, because of all of the reasons
4 you said, because of the value that it brings to
5 people's lives.
6 But most of the people who want to buy
7 this don't live here. And we have to be mindful,
8 and your industry is right to be mindful of the
9 global marketplace implications of what you make.
10 DR. WANG: I have one question. I think
11 the question is how to stop piracy. And I am
12 fascinated by the example of Hong Kong - 25 years
13 ago was rampant, today in the west. I can summarize
14 in my mind -- I mean, I am not an accomplished
15 musician, but just logically I am interested in all
16 affairs concerning China and I love music myself.
17 Number one is education, obviously. So we talk
18 about that. So you've got to be to a point where
19 peer pressure is not cool to do that. But that
20 takes its time.
21 Second, waiting for the economy of that
22 country to grow up so that piracy is not as
23 worthwhile doing. That takes time also. Economy
24 growth is process still to control people here, and
25 China will have economy over time, but hopefully, by

1 the time the living standard is high enough, it
2 doesn't make an economic difference to copy music
3 and buying. So the second one you have to wait.
4 So these are the top -- there are three
5 reasons I can see that can stop piracy historically
6 in most countries: education and rising standard of
7 the country. So these two we cannot control. We
8 can always help the first one, education.
9 But the third one, I think, is the key.
10 The third one, in my understanding of looking at
11 Hong Kong as one example why piracy stopped, is
12 because the technology is driven so that the people,
13 like people in this room and musicians of the world,
14 and the business people, realize that, you know,
15 rather than 89 percent of business and be held up to
16 standard principles, you're always fighting a losing
17 battle. We just go down a little bit. You say,
18 okay, rather than I sell one record and have a
19 hundred copies made, make no money off of that, why
20 don't I half the cost of the record I'm selling. So
21 I am not getting nothing, I get something.
22 So along that line, I do believe the
23 future is in technology. The future is in the
24 electronic technology, such as the 99 cents a song,
25 then eventually, especially with the rising economy,

1 the people, you know, that isn't that much
2 difference now. I can get on downline on these,
3 record companies are making the record cheaper, and
4 I try to be more accessible.
5 So in summary, I believe that the top
6 reasons to stop piracy: education, we have to wait
7 for its own course and help; rising standard of the
8 native country. We certainly have to wait for that.
9 We have no control over that. But third, how we can
10 make it at less economic gain, perhaps, so that we
11 at least gain something out of all 101 records
12 rather than just sell one, and they get freebies on
13 all the rest from the copies, but also take
14 advantage of technology, recognize it.
15 We have unprecedented opportunity with
16 electronic technology, buy by 99 cents. And we can
17 actually now design it right with the central
18 planning in China. Tell them, America today is
19 China's tomorrow. Why don't you give us regulations
20 and technology guidelines and technology. So
21 anticipate those things so that the American
22 songwriters can earn. It may not be the full scale
23 of what they should, but if you earn 80, 50 percent,
24 it's still better than earning nothing.
25 MS. JACKSON: I think his first two ideas

1 are great. Songwriters make like a little over
2 eight cents per copy sold. I don't know if you're
3 familiar with the music business or not, but
4 songwriters are the lowest paid. Fifty percent of
5 us have had to drop out of the business in the last
6 10 years. I have to do a side job. I'm a
7 professional writer, and I have to do real estate on
8 the side to make a living. I don't know if you have
9 to take a side job from doing eye work because there
10 are so many eye doctors in the field; but,
11 personally, I take it as a slap in the face to think
12 that I have to take four cents per copy sold.
13 That's just hard for me to think about.
14 And I don't know a lot of -- I don't think
15 -- I don't believe that all Chinese people are doing
16 the downloading. I think it's a few people that
17 make a lot of copies, perhaps. And maybe that's
18 what we need to look into. Maybe somebody here can
19 tell me, is it a lot of people who do it or a few
20 people who make many copies to sell to the masses?
21 MR. HANCON: I'm John Hancon from the
22 Recording Industry Association of America, the RIAA.
23 At least domestically we've found on any given day
24 there is 80 million files being traded of various
25 shapes and sizes which is about five million users.

1 That's our best guess.
2 But just to speak quickly about the
3 domestic issue. A lot of it for us and what we've
4 found is dedication. You know, we have been forced
5 to sue some of our consumers. And the biggest thing
6 we hear back from these parents is, well, we didn't
7 know it was illegal, we didn't know it was illegal
8 to take music off the internet. All of the kids are
9 doing it. And that's sort of been the biggest
10 hurdle is putting a price. Everyone thinks the
11 internet is kind of like the west, everything is
12 free. You can get whatever you want. You can get
13 directions, coupons, you can get whatever. Music
14 should be free, too.
15 So for us it's been a big education issue.
16 Where's your got milk campaign? There isn't one.
17 The problem is, and this is a personal opinion, this
18 is not a company opinion, I think it's almost as if
19 we're fighting ourselves when you put on the T.V.
20 and there is Ms. Elliott with 12 cars in her
21 driveway and Britney Spears with a huge mansion.
22 Yeah, they're millionaires, what do they care if I
23 steal a song or what do they care if I steal and
24 download this movie. It's Tom Cruise. He makes 20
25 million a picture. He's not going to miss my $8.

1 But five million people doing that everyday all day,
2 that's your problem.
3 So for us it's been just this ongoing
4 education issue. We worked with Bart, and had a lot
5 of people come and sit with us on the steps of the
6 supreme court and sort of help hammer this home. So
7 it's, unfortunately, a long road; but I think we're
8 making some good progress.
9 MR. WILSON: I just wanted to add to what
10 you said, the question about how you have a cultural
11 of respect for copyright whether it's in Hong Kong
12 or anywhere else, is that you have to have resolve
13 from public figures. That was the component that I
14 was referring to you, like the three or four things
15 that are necessary to the development, the other
16 things that have to happen. I would have corrected
17 only one thing. What we've seen is public will by
18 the elected officials to be able to say no, this
19 won't happen. And that's what we have been
20 insisting on from the Chinese government. We try to
21 get local provincial governors to sign anti-piracy
22 pledges, that they won't allow it on govenment
23 computers, that they'll have legitimate software.
24 It's that leadership will that is such an important
25 component of protecting it.

1 MS. SPRINGER: How are Chinese writers,
2 composers, compenstated?
3 MR. WILSON: And the problem is I am not
4 that expert. Honestly, I don't know. I'm sorry.
5 MR. DAVIS: I'm J.R. Davis, general
6 partner with Wynnco Film and Video. Thank you for
7 this forum. I just wanted to mention, I'm glad you
8 made it, Dr. Wang, because he actually invited me.
9 I didn't know how to really tell your story.
10 I think it's interesting and important to
11 know that Dr. Wang is a musician and a writer.
12 Bart, you need to sign him up for today, but
13 actually quite an accomplished writer.
14 Also, Dr. Wang in your congressional
15 delegation, I think you were going to be in China at
16 the same time. So you may want to see what is going
17 on. The largest delegation of congress people going
18 over there on this same issue. So I think there
19 might be some good parallels there.
20 I'll tell you, Dr. Wang and I have been
21 working on this sort of independently. I am excited
22 to see what is going on here today. David knows
23 about this, but we've been actually talking with
24 artists and writers as far as going through Dr.
25 Wang's contacts to China. And it's interesting

1 around Music Row, the first thing is, well, we've
2 tried the China thing. There is no way for us to
3 make money and we're not sure we want to go with
4 you. There are a lot of people that are interested,
5 but from rock and roll to pop to country, they've
6 had a hard time finding it.
7 So I think in Nashville we have a great
8 resource and a great insight to the culture here. I
9 will tell you to take advantage of him because he is
10 very accessible and I think he will give us all some
11 insight as to how to address this issue.
12 MR. WILSON: Thank you, very much, for
13 having me here. And so much also thank you to BMI
14 for hosting this event. I know I've been greatly
15 impressed. My thought is it's Sunday afternoon and
16 it's five o'clock, and I think that we will probably
17 just have some concluding remarks.
18 MR. CANNON: I just have one more thing.
19 I'm Fred Cannon from BMI in case you didn't get that
20 before. The one situation I've encountered
21 travelling around the world is that piracy creates
22 an economy, creates a local economy; and therefore,
23 it creates jobs for people locally. And we have
24 Vietnam, now we have South Korea, we have Malaysia,
25 we have all of those wonderful countries like India

1 who are creating these local economies.
2 We also need to address these places now
3 and start educating them now because when these
4 local economies become a prominent economy, they are
5 not going to stop. They are going to grow and grow
6 and grow. So I think we need to address it now as
7 these little local economies start budding, because
8 if we don't, they're going to becopme major
9 economies with major corruptable people along the
10 way. And that's another issue in these economies,
11 as you know, and then it's going to be much harder
12 for us to stop it.
13 MR. WILSON: I'm humbled by your comments
14 because that was the thing I should have said a
15 minute ago in response to your question and also Dr.
16 Wang's point about at what point do these factors
17 come together to inspire protection of intellectual
18 property. It is the emergence of those little jobs.
19 Right now all of the jobs in China, India and
20 Vietnam, is that they do hire people. It's part of
21 the local economy. It's an illegal, elicit economy,
22 but it's jobs. And that matters to every
23 government. It matters to my government, it matters
24 to your government, it matters to all of us. And
25 that is one of the triggers, too, is when the

1 legitimate economy becomes big enough to have a
2 voice of its own in politics, which is exactly what
3 we saw in Hong Kong. All of a sudden when Hong Kong
4 theater was worth millions and millions of dollars a
5 year, all of a sudden the Hong Kong government was,
6 like, we got to be out here protecting our --
7 because they are a powerful voice. They hire and
8 employ lots of people, and those are the caterers,
9 the set finishers, and the make-up artists, and
10 everything that goes into the entertainment industry
11 and the production industry of this IP. Local jobs,
12 we'll say that changing in China as there will be
13 more domestic songwriters, more domestic singers,
14 more domestic movie makers, as that industry grows,
15 the insistence and the local domestic pressure to
16 protect those jobs is going to increase. And that
17 is going to happen over time.
18 MR. BENNETT: I want to thank everybody
19 for being here today and taking time out of your
20 Sunday afternoon in the late spring time to join
21 this forum. What a great intellectual discussion
22 we've had today.
23 I want to thank Patrick Wilson for your
24 insight and your intellect on these issues. Thank
25 you. Mike Platt, thank you for being my part guy in

1 Washington. Thank you, very much. Again, we want
2 to thank Congressman Marsha Blackburn for continuing
3 to spearhead this issue in the congressional halls.
4 She is doing a fantastic job. Thank you, wherever
5 you are right now, Marsha Blackburn.
6 MR. WILSON: Running really fast in the
7 airport.
8 MR. BENNETT: I just want to add in
9 closing, thanks again to BMI for allowing us to have
10 this forum today. Opening up this beautiful
11 building and this great room for us ain't cheap.
12 And we appreciate the investment you made in this
13 gathering today.
14 In closing, I would just like to say that
15 this is an important issue to Governor Bredesen
16 also. Governor Bredesen, as you all know, has been
17 dealing with weighty state governmental issues for
18 the past two-and-a-half years. We can't wait to get
19 all of that behind us so we can go on to addressing
20 problems like this which mean a lot to everyone.
21 But I want to remind everyone about Governor
22 Bredesen. He owns several patents himself. He
23 developed software. This is an issue that is very
24 important to him. So always remember that. You
25 have a voice in that executive there at the state

capitol also.

Again, thank you, everybody. It's been a great time.

(Whereupon, the meeting was concluded.)