

**PROTECTING INTELLECTUAL PROPERTY RIGHTS
IN A GLOBAL ECONOMY: CURRENT TRENDS
AND FUTURE CHALLENGES**

HEARING

BEFORE THE
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,
ORGANIZATION, AND PROCUREMENT
OF THE
COMMITTEE ON OVERSIGHT
AND GOVERNMENT REFORM
HOUSE OF REPRESENTATIVES

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PROTECTING INTELLECTUAL PROPERTY RIGHTS IN A GLOBAL ECONOMY: CURRENT TRENDS AND FUTURE CHALLENGES

WEDNESDAY, DECEMBER 9, 2009

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT,
ORGANIZATION, AND PROCUREMENT,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m. in room 2247, Rayburn House Office Building, Hon. Diane E. Watson (chairwoman of the subcommittee) presiding.

Present: Representatives Watson, Connolly, Cuellar, Speier, Chu, Maloney, Bilbray, and Issa.

Staff present: Bert Hammond, staff director; Valerie Van Buren, clerk; Adam Bordes and Deborah Mack, professional staff; Adam Fromm, minority chief clerk and Member liaison; John Ohly, minority professional staff member; and April Canter, minority staff member.

Ms. WATSON. Good morning. The Subcommittee on Government Management, Organization, and Procurement of the Committee on Oversight and Government Reform will now come to order.

Today's hearing will focus on the Federal Government's role and responsibility in the global protection and enforcement of intellectual property rights. The subcommittee will also seek additional information from administrative witnesses on the strategic objectives of the Obama administration for improving coordination among the stakeholder agencies having IPR protection or enforcement responsibilities.

Without objection, the Chair and ranking minority member will have 5 minutes to make opening statements, followed by opening statements not to exceed 3 minutes by any other Member who seeks recognition.

Without objection, Members and witnesses may have 5 legislative days to submit a written statement or extraneous materials for the record.

I would like to welcome all of you to today's subcommittee hearing on Federal efforts to protect and enforce the intellectual property rights of our Nation's industrial base throughout the domestic and global marketplace.

Before we begin, I would like to apologize for the subcommittee having to postpone our original hearing that was scheduled for November 4th, but our legislative calendar was rather full that week,

as some of you probably will recall. So I welcome our distinguished witnesses, especially those who have had to rearrange their travel or business schedules in order to attend today's rescheduled hearing, and look forward to hearing your testimony.

Intellectual property rights [IPR], is an issue that is near and dear to my heart and the livelihood of many of my constituents. My congressional district, the 33rd, which includes Los Angeles, Culver City, and Hollywood, CA, is home to a number of important entertainment companies, including Sony Studios, the Culver Studios, Capital Records, Raleigh Studios, and Television Studios, and, of course, the American Film Institute.

According to figures compiled by Americans for the Arts, approximately 30,000 people are employed in entertainment-related industries located in my congressional district. More than 18,000 people who work in the congressional district make a living from film, radio, and television, whose profits and future viability are dependent on strong IPR protection and enforcement.

As a fellow member of the California congressional delegation, I know my Ranking Member Bilbray recognizes the vital economic importance of intellectual property to our State's economic health, as well as to the future growth and stability of our Nation and the global economy.

Since the establishment of the World Trade Organization in 1995, America's key IP-related industries have prospered through our domestic comparative advantage in innovation and research, but this advantage has been severely undermined by sharp escalation in IP infringement, such as piracy and counterfeiting, even among our closest and most vital trading partners and strategic allies. This causes great economic harm to innovations and innovators who invest significant capital in the products or creations that have improved our standard of living and increased our knowledge base. While the true amount is unclear, recent estimates of the losses or costs associated with IP infringement for the U.S. domestic industry ranges from \$200 to \$250 billion annually.

The prevalence of such losses extends to all IP-related sectors, including information technology, life sciences, digital content, pharmaceuticals, the defense industry, and the entertainment industry. These losses threaten our Nation's economic growth and global leadership in innovation.

Furthermore, IPR infringement poses significant risk to our national security, consumer welfare, and ability to rely upon an effective legal framework for our domestic industries working abroad. According to the Los Angeles County Economic Development Corp., the cost of global piracy and counterfeiting activities in Los Angeles County in the year 2005 was estimated at \$5.2 billion. Those figures were proportionately shared across all sectors of the IP-driven economy, with motion pictures leading the way at \$2.7 billion, followed by the recording industry, apparel makers, and software developers.

Unless such trends are soon curtailed, the roughly 1 million L.A. County IP-dependent jobs will be placed at a significant risk. The findings in this year's special 301 Report issued by the Office of U.S. Trade Representatives tell us that a combination of technological advances and various market access barriers in key coun-

tries are preventing our companies from protecting their IP-based goods and services.

With that in mind, I would like our witnesses to discuss what they believe are the major factors in the escalation of IPR infringement abroad. Specifically, I want our Government panelists to explain how they believe the newly established intellectual property enforcement coordination office will aid in their development of a stronger framework for managing our inter-agency IPR protection and enforcement responsibilities, both domestically and abroad. Specifically, what new authorities has this office been granted to police our patchwork of agencies charged with combating global IPR infringement.

Furthermore, I would like you to discuss how our trade agreements with other nations, including those issues being negotiated as part of the proposed anti-counterfeiting trade agreement, are reducing the growing incidence of digital-based piracy or the illegal manufacturing of counterfeit drugs and consumer goods for importation.

These activities pose significant threats to our economy, to public health, to national security, and must be countered in order to maintain our position in the global marketplace.

Last, I would like to address an emerging IPR issue with the People's Republic of China and its efforts to restrict our domestic technology industries from participating in their governmentwide procurement programs. And under the Chinese government's newly issued rules, only products that contain Chinese proprietary intellectual property would be eligible for government procurement. This process will, in effect, result in excluding the products of international companies from the government procurement market in China. This is a troubling development that will have major economic consequences for our trade relations if we do not find an amicable resolution.

I am hopeful that our witnesses can educate us on the latest developments with these matters and other recommendations on how we at the subcommittee can be helpful in facilitating a resolution for all parties involved.

I will also ask my ranking member, Mr. Bilbray, for his consideration on how we may be able to work collaboratively on this topic of vital importance to our home State's economy.

Once again, I want to thank our panelists for joining us today and look forward to your testimony.

Are you taking his place, Mr. Issa?

Our distinguished Member, Mr. Issa from San Diego, will take the place of our ranking member, Mr. Bilbray.

Mr. Issa.

Mr. ISSA. Thank you, Madam Chair. I would ask unanimous consent that Mr. Bilbray's entire opening statement be placed in the record.

Ms. WATSON. Without objection.

[The prepared statement of Hon. Brian P. Bilbray follows:]

EDOLPHUS TOWNS, NEW YORK
CHAIRMAN

DARRELL E. ISSA, CALIFORNIA
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House of Representatives
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2157 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6143

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Opening Statement

Brian Bilbray
Ranking Member
Government Management, Organization and Procurement Subcommittee

Hearing on
“Protecting Intellectual Property Rights in a Global Economy: Current Trends and
Future Challenges.”

December 9, 2009

Thank you, Madam Chair.

The protection of intellectual property rights is a very important topic. I thank the Chair for her interest and leadership in examining this issue.

The copyrights, trademarks, and patents of our writers, inventors, designers, engineers, and other creative Americans are among this nation’s most vital resources. It is essential that this work be protected from imitators and counterfeiters. This not only fair to those who create and purchase intellectual property, but it also protects Americans from potentially shoddy and unsafe substitutes, as well.

Intellectual property encompasses a vast array of goods, including music, movies, books, pharmaceuticals, auto parts, handbags, footwear, and apparel—just to name a few. The development and sale of intellectual property contributes an estimated \$5.5 trillion every year to our economy. Industries which produce intellectual property outperform other sectors of our national economy. Adequate protection and enforcement of intellectual property rights is a key condition for securing and nurturing further economic advancement, both here and in developing countries.

The U.S. Constitution gives Congress the responsibility "to promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive right to their respective writings and discoveries." This is a responsibility I take very seriously.

Today's hearing provides an excellent opportunity to hear from government and industry experts about threats to our intellectual property rights in the expanding global marketplace. I look forward to their testimony and a productive discourse about the U.S. government's role and performance in this area.

Because intellectual property theft, by definition, occurs surreptitiously, it is difficult to determine the precise economic damage it causes companies, employees, and governments. But, it is certain that counterfeiting and piracy pose enormous costs. Some estimates suggest that rights holders around the world lose between \$500 billion and \$600 billion in revenue each year. This is equivalent to 5% to 7% of global trade.

According to the Federal Bureau of Investigation and the Department of Homeland Security, companies and individuals in the United States lost between \$200 billion and \$250 billion in 2002 because of intellectual property theft. In addition, the annual assessment by the U.S. Trade Representative of the international commitment to intellectual property rights (known formally as the "Special 301 Report") concluded that lax controls in seventy-seven countries cost American companies lost approximately \$16.1 billion in 2009.

This hurts U.S. business and damages our competitiveness. Therefore, it is important to understand what other countries are doing to stop infringement.

But, this is not only an economic issue. It is also essential that we consider the potential harm to consumers posed by counterfeit goods. When individuals are exposed to faked machine parts, pharmaceuticals, or other items which do not meet stringent standards, health and safety can be endangered.

I am eager to understand more about those countries deemed deficient in their intellectual property laws and enforcement practices, and how the United States and our international partners are working together to improve the global standard.

I appreciate the participation of today's witnesses. From international negotiations and law enforcement to effects on the entertainment industry, each of you represents a unique perspective into the complexity, scale, and impact of this growing issue.

Thank you again, Madam Chair, for holding this very important hearing today. I look forward to hearing from our witnesses.

Mr. ISSA. Thank you, Madam Chair.

Intellectual property contributes \$5.5 trillion—I repeat, \$5.5 trillion—a year to our economy. In fact, we have become the intellectual property giant around the world. We have traded many, many jobs, entry-level jobs in manufacturing of garments and other products, for our development of these high-skill, high-paying jobs, and we have off-loaded many of them to China. So I find it today particularly confusing that China would look at this bargain that has been so favorable to them and begin the process of far exceeding any moratorium or prohibition allowed under the WTO.

We in the U.S. Congress, under the chairwoman and my watch, participated in China ascending to the WTO. They did so not having met all the requirements but with the promise to meet them and to continue in this direction. Intellectual property was, in fact, at the core of the items which China had not lived up to their responsibility but promised to. Over the years, countries such as Russia have been prohibited and stopped from getting into that for good reason. We have seen that China has not gained any respect for intellectual property. In fact, they continue to be the largest customer in Asia for Microsoft products. They simply don't buy them.

Madam Chair, it is very clear that we have to say that China has a right to have such special property as is necessary for its own defense. We, too, maintain a policy that certain technology must be domestic for our national security. Certainly neither one of us would want the ability to put a space-based defense system into space not to be domestically controllable and known. But China very clearly is trying to force partnering with U.S. companies' transfer of technology for purposes of getting a jump start on that next generation of products and services.

So, Madam Chair, I appreciate your viewing something which this committee has a longstanding belief that we not only control the procurement process governmentwide, but we have, by necessity, a requirement to look beyond our borders for free and fair trade and access for our products.

So I look forward to our witnesses and, again, Madam Chair, thank you for holding this important hearing.

I yield back.

Ms. WATSON. Thank you.

Without objection, Members and witnesses may have 5 legislative days to submit a written statement or extraneous materials for the record.

I now yield to Congressman Cuellar for an opening statement.

Mr. CUELLAR. Thank you, Madam Chair. I appreciate this hearing.

I am a big believer in trade agreements, but one of the things that I think, along with my other colleagues, we have to make sure that we protect our intellectual properties. I am interested, as we go through the testimony, to see what we are looking at as we look at the countries of Colombia, of Panama, and, of course, of Korea also. If you all could highlight that also during your testimony, if one of you all could do that. Otherwise, Madam chair, I am ready to listen to the testimony and ask some questions afterwards.

Thank you very much for having this hearing today.

Ms. WATSON. If there are no further opening statements, the subcommittee will now receive testimony from the witnesses before us today.

We will now turn to our first panel. There will be two this morning. It is the policy of the Committee on Oversight and Government Reform to swear in all witnesses before they testify. I would like to ask all of you to please stand and raise your right hands.

[Witnesses sworn.]

Ms. WATSON. Let the record reflect that the witnesses answered in the affirmative.

I will now introduce the panelists. We will first start with Mr. Stanford K. McCoy, who is the Assistant U.S. Trade Representative for the Intellectual Property and Innovation at the Office of U.S. Trade Representative. He serves as the chief policy advisor to the U.S. Trade Representative on the intellectual property and trade issues and serves as the lead U.S. trade negotiator on intellectual property and innovation to the WTO and Trips Council, and as part of the U.S. Free Trade Agreement negotiations.

Next to him is Mr. Robert Stoll, who is the Commissioner of Patents at the U.S. Patent and Trademark Office, where he oversees the administration of all U.S. PTO patent programs. Prior to his current appointment, Mr. Stoll served as Director of Enforcement for U.S. PTO, as well as Dean of Education and Training Programs for external agency stakeholders involved with intellectual property issues.

Mr. Jason Weinstein is the Deputy Assistant Attorney General of the Criminal Division at the U.S. Department of Justice. Before joining the Criminal Division, Mr. Weinstein served as chief of the Violent Crime Section in the U.S. Attorney's Office for the District of Maryland, and as assistant U.S. attorney for the Southern District of New York. Before becoming a Federal prosecutor, Mr. Weinstein served as Special Investigative Counsel in the Justice Department's Office of the Inspector General.

Mr. William Craft is the Acting Deputy Assistant Secretary of the Bureau of Economics, Energy, and Business Affairs at the U.S. Department of State. Prior to this, he was Director of the Office of Multilateral Trade and Agricultural Affairs. He is the lead officer in the State Department for all issues related to the World Trade Organization [WTO], including negotiations including the DOHA Development Round and WTO Accession issues.

Mr. Loren Yager is the Director of International Affairs and Trade at the Government Accountability Office, where he oversees issues associated with intellectual property rights and international trade negotiations.

I ask that each of the witnesses now give a brief summary of their testimony, and to keep this summary under 5 minutes in duration. Your complete written statement will be included in the hearing record.

Before we proceed, I am going to ask Ms. Chu if she would like to make an opening statement.

Ms. CHU. I am just happy to take part in these proceedings and I look forward to hearing what the witnesses have to say.

Ms. WATSON. We are happy to have you.

Mr. McCoy, would you please proceed.

STATEMENTS OF STANFORD K. MCCOY, ASSISTANT U.S. TRADE REPRESENTATIVE FOR INTELLECTUAL PROPERTY AND INNOVATION, OFFICE OF THE U.S. TRADE REPRESENTATIVE; ROBERT L. STOLL, COMMISSIONER FOR PATENTS, U.S. PATENT AND TRADEMARK OFFICE; JASON WEINSTEIN, DEPUTY ASSISTANT ATTORNEY GENERAL, CRIMINAL DIVISION, U.S. DEPARTMENT OF JUSTICE; WILLIAM E. CRAFT, ACTING DEPUTY ASSISTANT SECRETARY, BUREAU OF ECONOMICS, ENERGY, AND BUSINESS AFFAIRS, U.S. DEPARTMENT OF STATE; AND LOREN YAGER, DIRECTOR, INTERNATIONAL AFFAIRS AND TRADE, GOVERNMENT ACCOUNTABILITY OFFICE

STATEMENT OF STANFORD K. MCCOY

Mr. McCoy. Thank you, Madam Chairwoman. Thank you to the ranking member, Mr. Bilbray, and all the members of this subcommittee for the opportunity to join you today and talk a little bit about the mission of the Office of the U.S. Trade Representative in respect to the protection and enforcement of intellectual property rights.

As you said in your opening statement, Madam Chairwoman, one of the factors that makes American exporters and investors competitive across so many sectors of the global economy is the value we add to our products and services through innovation and creativity.

Intellectual property rights and their protection and enforcement are critical to securing that comparative advantage in global trade, and thus to securing the jobs of workers in America's many innovative and creative industries. Providing leadership in the creation and maintenance of the global infrastructure of trade rules to support American exports and investments is a critical part of the work of the Office of the U.S. Trade Representative. It is a job that we carry out in coordination with the other agencies represented here at the table, and in coordination in coming days with the new Intellectual Property Enforcement Coordinator, who has recently been confirmed by the Senate.

We carry out that mission in many ways. One of the best tools we have is one that was handed to us by the U.S. Congress of consistently monitoring our partners' trade practices through the special 301 report. If they know that we are holding a magnifying glass up to their actions, they will be less likely to break the rules, and special 301 is one of our biggest and strongest magnifying glasses. We use it to scour the globe for copycats and counterfeiters and call out countries that provide safe havens for the theft of American intellectual property.

Madam Chairwoman, this year marks the 20th anniversary of the first special 301 report, which was mandated by the U.S. Congress in 1988 and first issued in 1989. The past two decades have brought enormous new challenges in the scope and sophistication of international piracy and counterfeiting. The special 301 process has expanded in scope and breadth to match that challenge. For our most recent report, USTR examined IPR protection and enforcement in 77 countries and listed 46 of them in the report.

Special 301 works because the reports' rankings shine a light on IP protection and enforcement, and also afford an opportunity to give credit where it is due.

The Republic of Korea is a good example of both of those. It was removed from the watch list in 2009, marking the latest in a series of improvements in the Asia Pacific region and around the world that have been encouraged and recognized through the special 301 process created by Congress.

We hope to see that trend continue and spread. It is vital that trading partners such as China, Russia, and other countries on the priority watch list and watch list follow suit. It is also critical that valued trading partners like Canada and Spain step up and confront emerging challenges like Internet piracy.

China still presents significant challenges to the protection and enforcement of intellectual property rights, including the indigenous innovation challenge that was mentioned by you, Madam Chairwoman, and by Mr. Issa in your opening statements. With China we are making use of every available trade tool to achieve progress on IP issues.

Madam Chairwoman, let me say it as plainly as Ambassador Kirk has said it: China must do more to protect U.S. intellectual property rights.

In addition to reporting and engaging bilaterally, USTR is also providing essential leadership through trade agreements to strengthen norms for the enforcement of intellectual property rights. A key USTR initiative in this area is the Anti-Counterfeiting Trade Agreement [ACTA]. In that effort, we are partnering with a group of key trading partners representing about 50 percent of global merchandise trade. When it is finalized, the ACTA will help governments around the world to more effectively combat the proliferation of pirated and counterfeit goods.

With that, Madam Chairwoman, I will close my summary of my remarks and thank you and the members of the committee again for the opportunity to be here today.

[The prepared statement of Mr. McCoy follows:]

**Statement
Stanford K. McCoy
Assistant U.S. Trade Representative for Intellectual Property and Innovation
before the
House Committee on Oversight and Government Reform
Subcommittee on Management, Organization and Procurement**

December 9, 2009

Madam Chairwoman, Ranking Member Bilbray, my name is Stanford K. McCoy, and I am the Assistant United States Trade Representative for Intellectual Property and Innovation. Thank you for providing this opportunity to speak to you today about some of the U.S. Government's work to strengthen protection and enforcement of intellectual property rights (IPR) around the world, the role of the Office of the U.S. Trade Representative (USTR), and some of the key tools of U.S. trade policy, including the "Special 301" process.

The mission of the USTR, broadly stated, is to help Americans grow their farms, build their businesses, and support their families through trade. In 2008, exports generated nearly two trillion dollars in income for American workers, farmers, ranchers, manufacturers, and producers. That's about one in every eight dollars Americans earned last year. Manufacturing exports alone supported six million American jobs. Millions more high-quality jobs depend in part, or entirely, upon trade in services. And jobs supported by exports pay as much as 18 percent above the national average.

One of the factors that makes American exporters and investors competitive across so many sectors of the global economy is the value we add to our products and services through innovation and creativity. That added value comes from the genius of American workers and entrepreneurs in businesses large and small, and it represents a significant comparative advantage for the United States in the global economy. Intellectual property rights are critical to securing that comparative advantage, and thus to securing the jobs of workers in America's innovative and creative industries.

President Obama has laid out an innovation strategy that focuses on critical areas where sensible, balanced government policies can lay the foundation for innovation that leads to quality jobs and shared prosperity. Significantly, part of that innovation strategy is to ensure that intellectual property is protected in foreign markets.

Intellectual property assets may be intangible, but protecting those assets abroad yields tangible benefits. For instance, according to industry reports, copyright-intensive industries, including some in your district Madame Chairwoman, make significant contributions to U.S. employment and GDP. IP protection is also an engine for growing small and medium-sized businesses, many of which depend on intangible assets like inventions and brands to gain a foothold in the marketplace.

Madam Chairwoman, I want to emphasize that the importance of intellectual property protection is by no means a narrow one. Enforcement of intellectual property rights is essential to America's strength in diverse export sectors such as movies, music, software, pharmaceuticals, agricultural chemicals, and medical devices. And an intellectual property system consisting of appropriate and enforceable rights, as well as appropriate limitations and exceptions, is also critical to America's strength across a wide range of other sectors as well, including innovation in the manufacturing sector.

I want to take a minute to paint a picture of what that means for real American businesses and workers. Recently, I traveled to Illinois to meet with employees of Illinois Tool Works Inc., a diversified global manufacturer of advanced industrial technology that serves customers around the world. ITW is headquartered in Glenview. It operates in 52 different countries and employs about 60,000 people. The team at ITW stressed that innovation is at the heart of their business strategy, and IP protection and enforcement is one of the keys to its success. They count on a reliable international infrastructure of sound intellectual property laws, and they depend on effective systems for enforcing those laws.

Providing leadership in the creation and maintenance of the infrastructure of rules to support American exports and investments is a critical part of the work of the Office of the United States Trade Representative. We are doing everything we can to support the jobs that flow from trade and the workers who hold them, and that means stepping up our trade enforcement efforts. President Obama and Ambassador Kirk believe that on a level playing field, Americans can compete in any sector – from manufacturing to services to agriculture. Just enforcing the rules on the books can win our workers and companies the benefits of trading as fully, fairly, and freely as our agreements allow.

Special 301

One of the best ways we guarantee America's trade rights is by consistently monitoring our partners' trade practices. If they know we are holding a magnifying glass up to their actions, they'll be less likely to break the rules.

One of our biggest and strongest magnifying glasses is the one that we use to examine protection and enforcement of intellectual property rights and market access for persons who rely on IP rights. I am referring, of course, to the tool the U.S. Congress created for USTR in the Omnibus Trade and Competitiveness Act of 1988, commonly known as the Special 301 Report.

We use the Special 301 report to scour the globe for copycats and counterfeiters, people who steal America's greatest strength: the intellectual property that flows from the ideas of the American people. Imitation may be the sincerest form of flattery, but as Ambassador Kirk likes to say: "piracy isn't flattery – it's theft."

That theft lets foreign companies market pirated and counterfeit goods that costs U.S. manufacturers, software companies, movie and music producers, and other creative and innovative enterprises billions of dollars, these illegitimate goods also expose US consumers and those around the world to products that can pose threats to public health and safety and damage

the environment. So, we call out countries that provide safe havens for the theft of American intellectual property.

Madam Chairwoman, this year marks the twentieth anniversary of the first Special 301 report, issued in 1989. The occasion presents us with an opportunity to look back and draw lessons from the past 20 years, and also to look ahead.

When Congress enacted the Special 301 provisions in 1988, the international legal infrastructure for the protection of the rights of U.S. creators and innovators was not yet well developed. The World Trade Organization (WTO) Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) did not exist. And significant U.S. trading partners, such as China, Korea and Taiwan, had major gaps in their laws on the books to protect intellectual property rights.

Just as significantly, when Congress enacted the Special 301 provisions in 1988, few of us would have had the foresight to imagine routinely using the internet to buy goods and services, downloading movies and music, putting ringtones on cellphones, building brands and markets around web addresses, or even watching movies on DVD players. Along with the unquestionable benefits of these innovations have come enormous new challenges in the scope and sophistication of copyright piracy, trademark counterfeiting, and other forms of infringement of intellectual property rights. Technology was only one of several factors that contributed to what author Moises Naim has described as an “explosion of illicit trade” – including trade in counterfeit and pirated goods – in the 1990s.

As intellectual property has become more complex and sophisticated and its protection and enforcement problems more prevalent over the past two decades, the Special 301 process has expanded in scope and breadth to match it. In last year’s report for example, USTR examined IPR protection and enforcement in 77 countries, 46 of which were listed in either the Priority Watch List or the Watch List, or were designated for special monitoring pursuant to the statute (section 306 monitoring). The report reviewed current trends in IPR protection and enforcement, including internet and digital piracy; trends in counterfeiting; intellectual property and health policy; implementation of the WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS Agreement); and it included a section listing “notorious markets”, both physical and virtual, that have been associated with illicit trade in counterfeit and pirated merchandise.

How and why does this report work? Every year, USTR obtains information from wide variety of sources, including affected stakeholders, foreign governments, Members of Congress and their staffs, and interagency discussions. These close consultations begin in January and culminate around the end of April. At that time, we publish the report and note which countries are on the Priority Watch List, the Watch List, or other categories, and provide country reports for each country, carefully noting lapses in IPR protection and enforcement.

Special 301 works largely because the report’s rankings shine a light on IP protection and enforcement. In turn, that sends a message to the world, including potential investors, about the trading partner’s level of commitment to IPR protection. Indeed, one of the functions of the

report is to help inform businesses, including small businesses, about shortcomings in foreign IP systems that may make enable counterfeiters to take advantage of U.S. exporters by selling false copies of their product. . Even apart from the threat of trade sanctions, the Special 301 report is a matter of concern for trading partners that value their trade relationship with the United States.

The Special 301 process also affords an opportunity to give credit where it is due. For example, we improve countries' Special 301 standing when they implement important improvements in IPR protection and enforcement.

A good example of both of these situations is the Republic of Korea. As I noted earlier, when the Special 301 report was first created the United States had grave concerns about the IP protection and enforcement in Korea. As the child of a U.S. Air Force officer I spent my high school years in Korea, and I can tell you from personal experience that there was no shortage of pirated audiocassettes, knock-off Nike sneakers, Ralph Lauren shirts, and other trademark and copyright infringing products being sold . Throughout each successive Special 301 report, Korea was always mentioned, usually on the Watch List, and sometimes even on the Priority Watch List. But this April, Ambassador Kirk removed Korea from all lists in the report. His decision not only reflected significant reforms undertaken in the past year. It also reflected the turnaround Korea achieved over many years. Of course, street piracy remains a challenge, joined by newer challenges like Internet piracy. Significantly, however, the Government of Korea has demonstrated a strong commitment to meeting these challenges, which is reflected, for example, in the strong IP chapter that is part of the KORUS FTA and is achieving results in this area. We credit our partners in the Government of Korea for bringing about that change, and urge them to sustain their commitment to adequate and effective protection and enforcement of intellectual property rights.

Korea's actions represent the latest of a series of improvements in the Asia-Pacific region that have been encouraged and recognized through the Special 301 process. For example, we have seen similar turnarounds in Hong Kong, Singapore, and Taiwan. And progress has not been limited to a single region. In Europe, in the Americas, in the Middle East and across Asia, the Special 301 process has played a significant role in fostering positive changes.

Another recent example of success involved cable piracy in the Bahamas. Faced with an impending preference program review and the possibility of being placed on the 301 list again the Bahamas finally enacted and implemented a law that should ensure that American movie and television creators don't have to compete with unauthorized transmissions of their own shows. That law went into effect on October 1. While this is seemingly a small example, in a small market, it illustrates how ensuring respect for intellectual property and implementing trade commitments can actually open markets for U.S. creativity- and innovation-intensive industries around the world.

We hope to see this trend continue and spread. It is vital that trading partners such as China, Russia, and other countries on the Priority Watch List and Watch List meet the objectives set by Congress by providing adequate and effective protection and enforcement for intellectual property, and market access for persons who rely on IPR protection. And it is critical that countries like Canada and Spain step up and confront the challenges of Internet piracy. The

failure to effectively do so has landed those valued trading partners on the Priority Watch List and Watch List, respectively.

Other IP initiatives/tools

Even as we recognize successes, we need to also recognize that these and other markets, most notably China, still present significant challenges to the protection and enforcement of intellectual property rights. China is by far the world's leading exporter of knockoff products, and its domestic markets for IP-intensive products such as software, music, and films have been decimated by inadequate respect for IP rights. Madame Chairwoman, let me say it just as plainly as Ambassador Kirk has done: China must do more to protect U.S. intellectual property rights.

With China, we are making use of every available tool to achieve progress on IP issues. That includes the Special 301 report, but it also includes bilateral dialogues and, when appropriate, WTO dispute settlement.

I want to show you how those tools work together, so let me take a minute to talk about exactly what we're doing and how we're doing it. We begin each year by reviewing China's policies in order to prepare the Special 301 report. And this coming year we will also be conducting a provincial review, to assess progress on IPR issues in several key provinces and independent municipalities of China.

We also use the Joint Commission on Commerce and Trade (the "JCCT"), a long-standing bilateral dialogue, to obtain commitments from the Chinese Government to improve their IPR regime. For instance, in 2006 we obtained commitments that only legitimate software would be used on Government computers. This year's JCCT meeting took place last week, and the Chinese Government made commitments to: impose maximum administrative penalties on Internet infringers and has begun a four month campaign to clamp down on Internet piracy; strengthening protection of copyright-protected academic and medical journals in state run libraries and academic institutions; and committed to work closely with the United States to resolve U.S. concerns about a new Ministry of Culture circular relating to online music distribution that is creating serious problems for the U.S. music industry

Finally, in appropriate cases, where bilateral dialogue has not resolved our concerns, we have taken the further step of filing for dispute settlement before the World Trade Organization (WTO) dispute settlement. So far we have initiated two disputes that relate to our IPR concerns, and have obtained important decisions from the WTO that reaffirm the need for China to respect its WTO commitments.

For example, in March of this year, the WTO ruled that China's denial of copyright protection to works that do not meet China's content review standards was impermissible under the TRIPS Agreement. In addition, the WTO ruled that China's customs rules cannot allow seized counterfeit goods to be publicly auctioned after only removing the infringing trademark. There was a third claim concerning China's thresholds for criminal prosecution and conviction of counterfeiting and piracy on which the United States prevailed on the interpretation of the important legal standards in the Enforcement articles of the TRIPS Agreement, including the

finding that criminal enforcement measures for counterfeiting and piracy must reflect and respond to the realities of the commercial marketplace. However, the panel found that it needed additional evidence before it could determine whether China's criminal thresholds in fact are too high. China has committed to make the necessary changes to their laws to implement the WTO's findings by next March, and we are staying in close touch during this process.

This past August, USTR also won a significant victory in another WTO case I mentioned, although I should note that the Chinese are currently appealing the decision. The WTO found that major Chinese restrictions on the importation and distribution of copyright-intensive products such as theatrical films, DVDs, music, books and journals are inconsistent with China's WTO obligations. The WTO panel called on China to come into compliance with its obligations to allow U.S. companies to import these products into China and to eliminate the discriminatory requirements faced by imported products and their U.S. distributors in China. This case is an important component of our IPR strategy in China: promoting adequate and effective protection and enforcement of IPRs that will get pirated copies off the shelves, and ensuring market access that will put legitimate copies on the shelves in their place. WTO-inconsistent market access restrictions in China fuel the demand for pirate products by create a drought of legitimate ones. In turn, that creates opportunities for pirates to fill the void for Chinese consumers hungry for U.S. movies, music and books.

For countries that are not WTO members, we can use the process of WTO accession to press for needed changes, as we have done with Russia. Specifically, we are pressing Russia for full implementation of a November 2006 bilateral agreement reached in the context of Russia's ongoing WTO accession negotiations. Similarly with Ukraine, we are maximizing the WTO accession process and the pressure of trade sanctions imposed under Special 301 to bring about much needed changes. Those efforts have contributed to significant improvements in IPR protection and enforcement over the course of a few years.

ACTA

In addition to reporting and engaging bilaterally on other countries' deficiencies in enforcing intellectual property rights, USTR is also providing essential leadership to strengthen international norms for the enforcement of IPR. A key USTR initiative in this area, the Anti-Counterfeiting Trade Agreement, or ACTA, aims to strengthen legal frameworks, to bridge the gap between laws on the books and strong enforcement on the ground, and to foster ongoing cooperation among the ACTA participants.

In this effort, we are partnering with a group of key trading partners who together represent more than 50 percent of global merchandise trade. Those partners include Australia, Canada, the European Union and its 27 member states, Japan, Mexico, Morocco, New Zealand, Singapore, South Korea, and Switzerland.

When it is finalized, the ACTA is intended to help governments around the world more effectively combat the proliferation of counterfeit and pirated goods. Doing so will support sustainable global development, protect American consumers, and undermine organized crime.

We have had five negotiating rounds to date. At the latest ACTA negotiations in Seoul, Korea, negotiators from my team joined colleagues from other trading partners in discussing tools to combat internet piracy.

In keeping with the Administration's goals on transparency, we are looking at new approaches to keep the public well informed about our progress in these negotiations, and to ensure that they have meaningful opportunities to give input into the negotiating process. We won endorsement of the importance of meaningful public input from all of the participants at the Seoul Round in of the ACTA negotiations in November. We will continue working with our ACTA negotiating partners to meet these objectives. Our goal is to complete the negotiations next year, and once finished, it is our hope that more countries will aspire to join this leadership agreement, and we will thereby encourage greater respect and enforcement of IPR globally.

* * *

In closing, Madam Chairwoman, I would like to reiterate why Ambassador Kirk and his team at USTR go through these efforts – in other words, why ensuring intellectual property rights are protected and enforced is important to us and the economy. Whether it's airplanes or movies, software or state-of-the-art manufacturing equipment, one of our key comparative advantages in the global marketplace is the ability of our large and small enterprises and their workers to occupy the leading edge of the market. It is our innovation and creativity that keeps us there, and the ability to secure the fruits of that innovation and creativity that helps to secure our place in the global economy.

Ms. WATSON. I thank you, Mr. McCoy.
Mr. Stoll, you may proceed.

STATEMENT OF ROBERT L. STOLL

Mr. STOLL. Thank you, Madam Chairwoman Watson and members of the subcommittee. I am pleased to be here to discuss the efforts of the Department of Commerce and the U.S. PTO in promoting the protection of intellectual property rights in a global economy.

Innovation and creativity are essential ingredients of our Nation's prosperity. Appropriate protection of that innovation and creativity domestically and internationally is necessary to stimulate job growth and promote our economic well-being. That is why safeguarding these important assets is a top priority for all of us at this table and throughout the Obama administration. It is truly a team effort among our agencies to help fight piracy and counterfeiting within and outside our borders.

The Department of Commerce plays an important role in encouraging innovation and strengthening the Nation's ability to compete in the global marketplace. The U.S. PTO's statute directs us to advise the President through the Secretary of Commerce in intellectual property issues and to advise other Federal departments and agencies on matters of intellectual property policy in the United States and in intellectual property protection in other countries.

To this end, we are actively involved with the development of overall U.S. Government IP policy. We work to develop unified standards for international IP, provide policy guidance on domestic IP issues, and work with other agencies to procure strong IP provisions in free trade and other international agreements. We also provide training, education, and capacity building programs designed to foster respect for IP and encourage the development of strong IP enforcement regimes by U.S. trading partners.

Madam Chair, my written statement contains more details of a wide range of our efforts. In my limited time here, I would like to highlight some of our programs and initiatives.

The U.S. PTO coordinates, organizes, and participates in intellectual property rights training, trade capacity building, and technical assistance. We are especially proud of our Global Intellectual Property Academy [GIPA]. Since its creation in 2005, the U.S. PTO has provided in its 20,000 square foot training facility in Alexandria, VA, high-level capacity building programs and technical assistance training to foreign judges, prosecutors, Customs officials, IP enforcement personnel, as well as officials from copyright, trademark, and patent offices from around the world. Those individuals come to the United States to learn, discuss, and strategize about global intellectual property rights protection and enforcement.

Our program goals include fostering a better understanding of international intellectual property obligations and norms, exposing participants to the U.S. model of protecting and enforcing intellectual property rights, and promoting discussion of intellectual property issues in a friendly and supportive environment.

The Academy provides both multi-lateral programs and country-specific programs as needed. We further envision programs dedicated to specific legal issues or technologies as the Academy contin-

ues to develop. The U.S. PTO's programs reached an average of 4,000 individuals in over 100 countries annually.

In partnership with the Department of Commerce's United States and Foreign Commercial Service and the Department of State, U.S. PTO intellectual property experts are sent out to strengthen global intellectual property protection and enforcement overseas in selected high-profile countries where U.S. IP challenges are greatest.

The IP experts support, as part of the overseas intellectual property rights attache program, U.S. embassies and consulates on IPR issues, including devising strategies to stop counterfeiting and piracy and supporting U.S. Government efforts to improve the protection and enforcement of IPR. They also advocate U.S. intellectual property policies, coordinate training on IPR matters, and assist U.S. businesses that rely on IPR protection abroad.

The U.S. PTO has offered free programs and materials to help small- and medium-sized businesses improve their understanding of intellectual property, increase the value of intellectual property in their businesses to protect against counterfeits and piracies and of their intellectual property through our public awareness campaign.

An important effort is the intellectual property awareness campaign [IPAC], IP basics program, offered nationwide by U.S. PTO since 2005 to over 1,000 small- and medium-sized businesses. These programs include presentations by our attorney advisors that cover the entire range of intellectual property.

With that, Madam Chairman, I would like to conclude my remarks. Thank you.

[The prepared statement of Mr. Stoll follows:]

STATEMENT OF

ROBERT L. STOLL

**COMMISSIONER FOR PATENTS
UNITED STATES PATENT AND TRADEMARK OFFICE**

BEFORE THE

**Subcommittee on Government Management, Organization, and Procurement
Committee on Oversight and Government Reform
United States House of Representatives**

**“Protecting Intellectual Property Rights in a Global Economy:
Current Trends and Future Challenges”**

December 9, 2009

Our Shared Vision

Madame Chairwoman, Ranking Member Bilbray, and Members of the Subcommittee:

Thank you for this opportunity to discuss the role of the Department of Commerce (Commerce) in protecting U.S. intellectual property (IP) rights in a global economy. Protecting IP rights is one of Secretary Locke’s and the Department’s highest priorities, and for good reason.

Innovation and creativity are vital to this nation’s prosperity and job growth. Our inventors and artists need well-tailored, robust protection of their creations on a worldwide basis – not only so they can enjoy the fruits of their labors but, just as important, so their creations can fuel the enterprises that generate good-paying jobs and continue to enhance productivity. In the global economy, innovation and creativity are our clear competitive advantages. Across the U.S. Government, we must safeguard these national assets.

Of course, there is no more important time to focus on these issues. President Obama and Secretary Locke know there is no scenario for our economic recovery that is not driven by innovation and creativity. Looking out over the long term, our inventors need global protection for their creations if we are to address some of the grand challenges society faces. We have long known that research into and development of new medicines is a costly, high-risk undertaking. If we are to have any hope of providing ever-improving

levels of healthcare while containing costs, it will be with new innovations. Overcoming our energy and climate challenges will be impossible without widespread dissemination of new technology. And our workers of the future – our children and students – will have to be educated in the ways of innovation and creation if they and their children are to enjoy prosperity. Protecting present-day innovation and creation is essential to assuring our economic success in the global marketplace.

The U.S. Commerce Department is Proud to Play a Central Role in Protecting IP

Among the Nation’s Founders’ many enduring legacies is their respect for and values of intellectual property rights by providing for patents and copyrights in Article I, Section 8 of the Constitution -- “to promote the Progress of Science and useful Arts.” Like other parts of the Constitution, the idea of promoting progress by rewarding the creation of intellectual property has become a nearly global aspiration. Over the decades, Congress, federal courts, and the Executive Branch have done a great deal to develop the Nation’s intellectual property system, and in the process, we have established benchmarks for other nations seeking to emulate our success. Many of our national intellectual property rules are reflected in international treaties and agreements.

Today’s world is infinitely more complex than 18th century society. Even where specific intellectual property rights are recognized, we face differing views on stakeholders’ responsibilities in protecting and exercising these rights. The awareness of the importance of IP is not universal and in today’s interconnected electronic age, preventing IP theft faces many challenges. Products can move across the globe at the speed of light and factories can be quickly adapted to replicate commercially successful goods.

Working with Congress, the courts and our sister agencies, the Commerce Department plays multiple roles in the national effort to address this complex set of issues. In broad strokes, we:

- Grant certain intellectual property rights on behalf of the U.S. Government;
- Provide Administration leadership in developing policy that supports statutory and case law;
- Advocate for the establishment of global intellectual property norms;
- Support national and international IP enforcement efforts, advocating protection for product or category-specific U.S. interests; and
- Work to build up capacity in other nations so that they can have more effective intellectual property regimes for their own benefit and the benefit of global commerce.

These activities are mutually reinforcing. Coordinating them across the U.S. Government and with our international partners can be a challenge, but Commerce is committed to working tirelessly on this effort.

Policy-Advice

The U.S. Patent and Trademark Office's (USPTO) role in establishing patents and trademark rights is fundamental to our intellectual property system. By law, the office is "responsible for the granting and issuing of patents and the registration of trademarks" (see 35 USC § 2(a)(1)). The role complements the Copyright Office's registration of creative works, and the courts' protection of trade dress and trade secrets under the common law.

Giving life to this law – applying it in specific instances and evolving it to keep up with advances in technology – requires sound policy-making. Here, Congress has charged different parts of the Commerce Department with complementary missions:

- Congress has tasked the USPTO, through the Secretary of Commerce, with advising the President on intellectual property policy matters in the United States and internationally through the Office of the Under Secretary for Intellectual Property.
- Commerce provides policy guidance and advisory and technical assistance, consistent with Administration policies, on domestic IP issues to Members of Congress and staff, officials of government agencies and other IP stakeholders.
- And as the Internet has become a leading global platform for economic growth and social progress, the role of Commerce's National Telecommunications and Information Administration (NTIA) also comes into play. By statute, NTIA is the President's "principal adviser on telecommunications policies pertaining to the Nation's economic and technological advancement." Since the emergence of the Internet on the commercial scene, NTIA has played a leading role in shaping Internet policy in areas such as Internet domain names, technology innovation, privacy, and security. In these areas, NTIA and PTO have worked together to shape an intellectual property policy that balances strong intellectual property protection with flexibility to allow innovative new applications and services to flourish."

Of course, we perform these policy advice functions in collaboration with other U.S. government stakeholders. They include entities within the Executive Office of the President, including the Office of Science and Technology Policy, trade negotiators at USTR and others, as well as the Copyright Office, our diplomatic corps at the State Department, customs officials at the Department of Homeland Security (DHS), including law enforcement officers at U.S. Immigration and Customs (ICE)'s National Intellectual Property Rights Coordination Center (IPR Center), the Department of Justice and, increasingly, the Federal Communications Commission.

Establishing a Global, Balanced Rule-of-Law for Protecting Intellectual Property

Increasingly, our trading partners around the world also rely on innovative and creative works to drive economic growth. But respect for the intellectual property embedded in

such works is hardly uniform. With the increased significance of intellectual work-product worldwide, there is a parallel upsurge in unauthorized use of intellectual property, counterfeiting and piracy that actively undermines America's innovation-driven economy, the competitiveness of our companies, and the livelihoods of our workers. Counterfeiting and piracy are a threat to our health, safety and national security. Counterfeiting and piracy have annually cost us hundreds of thousands of jobs and billions of dollars. The U.S. Chamber of Commerce estimates that over 18 million American's are employed by IP intensive industries. According to a 2007 study, \$58 billion was lost to the U.S. economy in total output from piracy of motion pictures, music and sound recordings, and business and entertainment software (not even the entire copyright industry)¹. Small businesses are particularly at risk because they often lack the expertise to engage in self-help. Combating piracy and counterfeiting are therefore top priorities.

Here, an essential, foundational step is to promote worldwide adoption of reasonable legal norms concerning the recognition and protection of IP. In parallel, we continue to work with Congress and the courts to improve the state of U.S. law.

Right now, we are actively engaged with Congress to enact patent reform legislation that fairly balances the interest of innovators across all industries and technologies. We are seeking legislative changes that will simplify the patent process, reduce legal costs, improve fairness and make significant progress toward a more harmonized international patent system. As global trade continues to climb, greater harmonization of patent law will lead to greater efficiency, predictability, and reliability for U.S. innovators.

As the President's statutory adviser on intellectual property policy, Commerce and the USPTO have been actively involved in developing the U.S. government's legal position on important court cases. In *Bilski v. Kappos*, which was argued in the Supreme Court, in November of this year, the United States argued that the USPTO appropriately denied patent claims for a business method patent involving a method for hedging risk. In the Google Books matter, Commerce worked closely with the Department of Justice and other government agencies to craft a court filing explaining the many benefits of a settlement that would give consumers easy access to vast numbers of out-of-print works, while articulating a series of concerns about details of the proposed settlement. Likewise, Commerce has helped in developing U.S. litigation positions in other cases involving the USPTO's rulemaking authority, the appropriate standard for considering allegations of collusive conduct in the context of reverse payments from brand name manufacturers to prospective generic competitors in the Hatch-Waxman context, among other important intellectual property matters.

In the international realm, we work closely with the USTR and other agencies to establish, on a bilateral and multilateral basis, workable treaty commitments and trade agreements. For example, Commerce worked with the USTR on matters concerning the IP chapter for several free trade agreements (FTAs) during FY 2008, most notably

¹ Steven. E. Siwek, *The True Cost of Copyright Industry Piracy to the U.S. Economy*, commissioned by the Institute for Policy Innovation.

negotiation of the IP chapter of the U.S.-Malaysia FTA, Costa Rica's implementation of the Dominican Republic-Central America-United States FTA, Peru's implementation of the U.S.-Peru Trade Promotion Agreement, as well as implementation of the U.S.-Chile FTA. Commerce also contributed to the development of the United States' World Trade Organization dispute settlement case against China relating to deficiencies in its IPR enforcement regime. USPTO co-chairs the IPR Working Group in the U.S.-China Joint Commission on Commerce and Trade (JCCT), our ongoing trade dialogue with China.

Commerce also works with the Department of Justice to develop proportionate, deterrent penalties for commercial scale counterfeiting and piracy in regions around the world. In addition, the USPTO maintains an active leadership role in the area of patent harmonization and continues to advocate for harmonization in the so-called Group B+ process, which includes Japan, Canada, Australia, and countries from Europe. Harmonization of administrative procedures is also an important goal of the USPTO in its Trilateral Offices consultations with the European Patent Office and the Japan Patent Office. The Group was convened in an attempt to accelerate progress on substantive patent law harmonization talks that were not moving in the World Intellectual Property Organization.

Protection Abroad

The Department helps provide American intellectual property owners with knowledge and legal tools to fight piracy and counterfeiting both at home and abroad, and assist them in their enforcement efforts overseas. We provide foreign countries with technical assistance on effective enforcement of intellectual property rights.

Within Commerce's International Trade Administration (ITA), we run the Market Access and Compliance (MAC) program. MAC's mission is to develop strategies to overcome market access obstacles faced by U.S. businesses. MAC monitors foreign country implementation of multilateral and bilateral trade-related agreements, and identifies various market access and other issues, including ones related to intellectual property rights. Upon identification of an IPR-related trade issue, a team of experts comprised of country, industry, and issue experts is assembled to coordinate ITA's efforts to successfully resolve the issue. This work is then closely coordinated with the USTR and the Department of State as well as other relevant agencies such as USPTO, the Copyright Office, the Department of Justice, and the Department of Homeland Security.

The USPTO's Attaché Program was formally instituted in 2006 for the benefit of U.S. economic and political interests abroad to promote the value and importance of strong intellectual property protection and enforcement in selected, high-profile countries where U.S. IP challenges are greatest. In partnership with Commerce's more broadly scoped Foreign Commercial Service (FCS) and the Department of State, the intellectual property Attachés are sent out to strengthen global intellectual property protection and enforcement overseas. The IPR experts support U.S. embassies and consulates on IPR issues, including devising strategies to stop counterfeiting and piracy, and supporting

U.S. Government efforts to improve the protection and enforcement of IPR. The Attachés also advocate U.S. intellectual property policies, coordinate training on IPR matters, and assist U.S. businesses that rely on IPR protection abroad. These Attachés serve at posts in Brazil, Russia, India, China, Thailand, and the U.S. Missions in Geneva.

FCS officers working worldwide advocate for the interests of U.S. companies on IPR issues to appropriate foreign government officials in coordination with their Commerce counterparts and State Department colleagues. FCS officers worked closely with ITA's Office of Intellectual Property Rights (OIPR), State, and USTR during the drafting of the Special 301 Report on IP rights protection. FCS officers also deliver demarches, arrange for U.S. Ambassadors to visit Ministries, and work with embassy officials to promote IPR protection. FCS officers and International Trade Specialists at U.S. Export Assistance Centers across the United States also assist U.S. companies to develop IPR protection strategies.

Commerce has put special emphasis on assisting small and medium sized enterprises (SMEs) in protecting their intellectual property both in the United States and abroad. ITA and USPTO, working in conjunction with other agencies, have undertaken numerous activities to assist SMEs. The focal point of much of this effort has been the StopFakes.gov website managed by ITA. The site allows businesses to file complaints about IPR-related trade problems, which are answered within 10 days by a trade specialist from OIPR. On the website, SMEs can find country toolkits that contain detailed information on protecting IPR in key markets around the world including Brazil, Brunei, China, Egypt, European Union, India, Malaysia, Mexico, Paraguay, Peru, Russia, Taiwan, Thailand, and Vietnam. The USPTO and ITA are currently working to expand the program to include toolkits for other trading partners. ITA, USPTO, and the Small Business Administration also worked together to develop an online training program for SMEs to learn how to evaluate, protect, and enforce their IPR. Commerce has established the 1-866-999-HALT hotline answered by USPTO IPR experts to help businesses secure and enforce their IPR worldwide. This has been followed-up with the recent posting of a USPTO attorney to the IPR Center to assist with the coordination of domestic and international investigative training and enforcement capacity building efforts.

To strengthen coordination and strategic planning against counterfeiting and infringement, the Prioritizing Resources and Organization for Intellectual Property Act of 2008, established the position of Intellectual Property Enforcement Coordinator. By statute the Intellectual Property Enforcement Coordinator (which sits in the Office of Management and Budget) will coordinate and assist in the development and implementation of the Joint Strategic Plan against counterfeiting and infringement, facilitate the issuance of policy guidance to assure coordination of intellectual property enforcement policy, and chair an interagency intellectual property enforcement advisory committee. Commerce looks forward to working closely with the Intellectual Property Enforcement Coordinator to improve the efficiency and effectiveness of the Federal Government's enforcement efforts against counterfeiting and infringement.

Training and Capacity Building

Since 2005, the USPTO Global Intellectual Property Academy (GIPA) has provided high-level intellectual property rights training, capacity building programs and technical assistance training to foreign judges, prosecutors, customs officials, IP enforcement personnel, as well as officials from copyright, trademark and patent offices from around the world. Those individuals come to the United States to learn, discuss and strategize about global IPR protection and enforcement. The program's goals include fostering a better understanding of international intellectual property obligations and norms, exposing participants to the U.S. model of protecting and enforcing intellectual property rights, and promoting discussion of intellectual property issues in a friendly and supportive environment. The Academy provides both multilateral programs and country-specific programs as needed. USPTO further envisions programs dedicated to specific legal issues or technologies as the Academy continues to develop. GIPA also delivers training to other stakeholders, including small business owners, U.S. Government officials, and the general public.

With the establishment of GIPA, the USPTO also implemented the International Examiners-in-Residence (IEIR) program for patent examiners from foreign countries. The first one lasted eight months and ended in January 2008. It included examiners from China, India, Egypt, Brazil, Philippines, and Mexico. In the current program, there are eight examiners here from South Korea, China, Saudi Arabia, and Germany for a six-month program finishing the end of December, 2009. The group of five Korean examiners will stay with USPTO up to May 2010 to work on additional projects. These programs are provided free of charge and permit patent examiners from foreign countries to sit in lectures side-by-side with newly hired United States' examiners to learn examination practice and procedure. The current program is aimed at increased understanding of U.S. practice in order to facilitate work sharing efforts with other countries.

In addition, for several years now the USPTO has held enforcement workshops in coordination with, for example, the World Intellectual Property Organization, the Department of Justice, the IPR Center, U.S. Immigrations and Customs Enforcement, and U.S. Customs and Border Protection, providing training for foreign enforcement and intellectual property officials from developing countries on implementation of the TRIPS Agreement (WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights) enforcement provisions, problem-solving exercises involving civil, criminal and border issues, and discussions with rights holders on challenges in obtaining effective enforcement.

Furthermore, the USPTO has a group of in-house experts on China with extensive knowledge of IP legal regimes in China. The USPTO's China Team has actively participated since 2005 in China Road Shows to various cities in the United States as part of an outreach effort to talk to small- and medium-sized businesses about how to protect and enforce their IP in China. Often, these small- and medium-sized businesses lack the

resources and expertise available to larger corporations. These events are open to any business, including those that already are doing business in or with China and those that currently have no business with China but may not understand the risk to their intellectual property from IP theft from China. The China events have, in the past, been conducted in several cities around the country including, for example, Fresno, Oakland, Chicago, Baltimore, Detroit, Atlanta, Kansas City, Manchester, and Pittsburgh, each tailored to the particular needs of the host city's business community. The USPTO has reached out to both government and non-government stakeholders to help publicize the conferences and campaign. Some of the organizations that we have worked with to promote awareness of the conferences and of the issue of IP theft are: The IPR Center, Small Business Administration, Minority Business Development Centers, U.S. Export Assistance Centers, U.S. Customs and Border Protection, U.S. Immigration and Customs Enforcement, American Intellectual Property Law Association, Intellectual Property Owners Association, U.S. Chamber of Commerce, National Association of Manufacturers, Service Core of Retired Executives, National Federation of Independent Business, United Inventors Association, North Carolina Secretary of State's office, federal, state, and local law enforcement officials.

In 2009, USPTO decided to expand the China Road Shows to include issues related to India. In 2010, USPTO will host a China-India Road Show at the USPTO headquarters in Alexandria, Virginia.

The General Counsel's Office in Commerce also supports efforts to improve IP protection -- and rule-of-law more generally -- via the Commercial Law Development Program (CLDP). As part of its capacity building, CLDP assists developing countries with the reform of their IP law, to improve the efficiency and transparency of their IP administration, to increase the strength of local IP enforcement, and to expand public awareness. From Ukraine to South Africa and Pakistan to the Philippines, CLDP has provided a wealth of technical assistance for the training and coordination of judges, IP officials, customs officials, food and drug officials and standards officials, whose knowledge and capacity are key to the improved protection of IP in those countries and regions. This fall, Commerce hosted the 13th U.S.-China Legal Exchange. USPTO officials were joined by a Chinese delegation in Los Angeles, Chicago, and New York to discuss China's new patent law. The discussions highlighted the improvements, as well as the shortcomings, of China's efforts in these areas and provided U.S. businesses, practitioners, and academics an opportunity to give input to Chinese officials.

Finally, through various international frameworks, the USPTO strongly advocates cooperation and collaboration with intellectual property offices as a means of addressing global workload and patent application examination backlog issues, reducing the duplication of work among intellectual property offices, and improving the quality of patent examination. Since 1983, the Trilateral Offices-- the USPTO, the European Patent Office, and the Japan Patent Office-- have been meeting to discuss cooperation in the areas of automation and sharing of patent-related information. Most recently, the Trilateral Offices have focused on creating new efficiencies in the global patent system. As a result, work-sharing arrangements have been introduced and implemented that allow

for accelerated and improved processing of a patent application once an initial office makes a determination of patentable subject matter. To address these issues on a larger scale, the five largest patent offices - the USPTO, the European Patent Office, the Japan Patent Office, the Korean Intellectual Property Office, and the State Intellectual Property Office of China - have been meeting since 2007 to develop a strategy for increasing patent quality and maximizing efficiencies. Known as the IP5, this group recognizes that maximizing work-sharing is critical to sustaining the global patent system and is working on technical projects to support and maximize work-sharing.

Closing Thoughts

Madame Chair, the Department of Commerce and all within the Obama Administration recognize the importance of intellectual property protection both domestically and globally. As you can see, we are deploying our resources with a multi-prong, holistic strategy. We do so because, clearly, much is at stake. We look forward to working with the new office of Intellectual Property Enforcement Coordinator and with other agencies, and we will continue to work tirelessly, with all stakeholders, to combat piracy and counterfeiting around the globe in order to protect American innovation, creativity and jobs.

Thank you for this opportunity. This concludes my statement. I would be happy to answer any questions you may have.

Ms. WATSON. Thank you, Mr. Stoll.
Mr. Weinstein, you may proceed.

STATEMENT OF JASON WEINSTEIN

Mr. WEINSTEIN. Good morning. I want to thank you, Chairwoman Watson, and the ranking member and members of the subcommittee for the opportunity to appear before you today.

Attorney General Holder has made intellectual property protection a top priority, and the Department of Justice is fully committed to aggressive, effective criminal enforcement efforts to protect our Nation's IP stakeholders and the American public. The Department has worked with our law enforcement partners to develop a strong enforcement program that combines aggressive investigation and prosecution of IP crimes with law enforcement training and victim outreach. However, because we understand that in the global economy a successful criminal enforcement program requires a strong international component, we also work in partnership with our foreign law enforcement counterparts whenever possible, which has resulted in great successes.

For example, in January of this year Kevin Xu was sentenced to 78 months in prison for conspiring with others in China to traffic in counterfeit cancer drugs and other pharmaceuticals. Many of these counterfeits were lacking active ingredients or contained unidentified impurities, and drugs with lot numbers identical to the counterfeits were detected in the legitimate supply chain in London, which promoted a massive recall in the U.K.

Just this past September the department obtained its 64th felony conviction arising from Operation Fastlink, which targeted multinational organized criminal networks. In the underlying investigation, which was one of the largest international law enforcement actions ever taken against online piracy, the FBI worked with foreign law enforcement to conduct over 120 simultaneous search warrants in 27 States and a dozen foreign countries.

These are just two examples of the many, many successful international enforcement efforts that we have participated in, and we are proud of all of them, and they all demonstrate the value of strong relationships with international and foreign law enforcement.

The cornerstone of the Department's international efforts is the Intellectual Property Law Enforcement Coordinator [IPLC], program. With the help of the State Department, we have deployed two experienced Federal prosecutors to serve as IPLECs, one in southeast Asia and one in eastern Europe, to provide training and operational assistance in those regions.

Working with the IPLC for Asia, the Department also spearheaded the formation of the Intellectual Property Crimes Enforcement Network [IPCEM], which has helped to strengthen communication channels and promote the informal exchange of evidence among member nations in Asia.

In addition, the Department through the Criminal Division co-chairs the Intellectual Property Criminal Enforcement Working Group, which is part of the U.S.-China joint liaison group for law enforcement cooperation. The working group has fostered an open dialog on criminal IP enforcement, has increased information and

evidence sharing, and has resulted in a number of successful joint operations between the United States and China, including Operation Summer Solstice, which targeted a criminal organization believed to be responsible for the distribution of over \$2 billion worth of pirated and counterfeit software. Summer Solstice was the largest ever joint criminal enforcement operation between the FBI and law enforcement in China.

More generally, the Department has placed great emphasis on efforts to strengthen enforcement capacity overseas, from Europe to Asia to Africa to South America to Mexico. In fact, over the past 5 years, working on partnership with some of the agencies represented here on this panel with me, DOJ attorneys have provided training and education on IP enforcement to over 10,000 prosecutors, investigators, and judicial officers from over 100 countries.

Because IP crime has increasingly become the province of international organized crime, we are working to identify and to address links between organized crime and intellectual property. The Department has already taken a number of significant steps to incorporate IP into its existing organized crime strategy, as directed by the PRO-IP Act.

To succeed in the missions that I have outlined, we work closely with all of our partner law enforcement agencies, including through the National Intellectual Property Rights Coordination Center. Our ability to increase the number and scope of our IP investigations has also been bolstered more recently by the addition of 31 dedicated FBI special agents to investigating IP crime, and we appreciate Congress' decision to fund those positions.

Finally, the Department works extensively on IP issues with other agencies in the Federal Government, including those represented here today, and with the industries most affected by IP crime, and we also look forward to working very closely with Victoria Espinel, who was confirmed just last week as the new IP Enforcement Coordinator, and with our partner agencies on the newly formed or to-be-formed IPEC Advisory Committee.

Again I thank you for the opportunity to share with you the high priority that the Attorney General places on criminal enforcement of IP rights and the work that we do every day at the Department of Justice to combat intellectual property crime both here and abroad.

I would be happy to take your questions.

[The prepared statement of Mr. Weinstein follows:]



Department of Justice

STATEMENT OF

JASON M. WEINSTEIN
DEPUTY ASSISTANT ATTORNEY GENERAL
CRIMINAL DIVISION
UNITED STATES DEPARTMENT OF JUSTICE

BEFORE THE

UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT, ORGANIZATION, AND
PROCUREMENT

HEARING ENTITLED

“PROTECTING INTELLECTUAL PROPERTY RIGHTS IN A GLOBAL ECONOMY:
CURRENT TRENDS AND FUTURE CHALLENGES”

PRESENTED

DECEMBER 9, 2009

Good morning Chairwoman Watson, Ranking Member Bilbray, and Members of the Subcommittee. Thank you for the opportunity to appear before you today to discuss the critical subject of protecting intellectual property rights in a global economy. I am pleased to share with the Subcommittee the Department of Justice's role in and commitment to combating intellectual property crime both at home and abroad.

I. Importance of Intellectual Property Protection

As this Subcommittee is well aware, enforcing U.S. laws that protect intellectual property rights continues to be essential to safeguarding confidence in our economy, creating economic growth, and ensuring integrity, fairness, and competitiveness in the global marketplace.

Intellectual property rights are playing an increasingly significant role in the global marketplace, largely because industries that rely heavily on intellectual property protections represent some of the fastest-growing sectors of the U.S. economy – sectors that also account for an increasingly large share of U.S. exports. As an example, protecting intellectual property is critical to much of America's creative and high-tech industries, from the motion picture production facilities of Culver City, in Chairwoman Watson's district [California 33rd], which rely on copyright laws to protect their work, to the many biotech firms in North County San Diego, in Ranking Member Bilbray's district [California 50th], whose inventions are protected by patents.

Beyond these industries, the importance of intellectual property protection is further illustrated by trade secret laws, which provide a strong deterrent to corporate espionage and other forms of misappropriation in all kinds of businesses, both large and small. Similarly, trademark laws help companies – whether they produce the latest high-tech gadgetry or products that have been sold consistently for decades – protect their investment in their brand and the quality and innovation that brand represents.

But intellectual property protection is not simply important for businesses and the nation's overall economic health – it is also vital to consumers. Effective enforcement of trademarks, for example, helps to protect the public by ensuring that products are what they say they are – that consumers are not given false information about the goods and services they buy. Such protections allow the market to reward makers of quality products and to hold manufacturers accountable when products are inferior – or worse, unsafe.

In the increasingly globalized economy, intellectual property accounts for a growing share of the value of world trade, and protecting intellectual property has become a significant global issue. Thanks to advances in technologies, including the increasing accessibility of the internet as well as improvements in manufacturing, transportation, and shipping, digital content can be distributed to a worldwide market almost instantaneously, and even small businesses have unprecedented opportunities to market and distribute their goods and services around the world.

Unfortunately, the success and profitability of this worldwide trade in intellectual property has also attracted criminals who seek to illegally exploit and misappropriate the intellectual property of others. The same technologies that have engendered rapid growth in the

legitimate economy also allow violators of intellectual property laws to operate global criminal enterprises. Criminals have developed equally sophisticated and diverse methods of committing every type of intellectual property offense imaginable including: widespread online piracy of music, movies, video games, business software, and other copyrighted works; well-funded corporate espionage; increased sales of counterfeit luxury goods, clothing, and electronics, both on street corners and through internet auction sites; and, perhaps of greatest concern, increased international trade in counterfeit pharmaceuticals and other goods that pose a substantial risk to the health and safety of American consumers.

It is well recognized that the intellectual capital of this country is among our greatest resources. American products are highly sought after throughout the world. When criminals illegally exploit American creativity and innovation for their own profit, they do so at the expense of the livelihood and reputation of businesses both large and small. As I am sure others here today will testify to in great length, the harms to the economy and risks to public health and safety posed by intellectual property offenses are significant. Businesses cannot be expected to thrive in the face of daily insidious black market criminal activities that undermine their success. Attorney General Holder has made criminal enforcement of intellectual property rights a top priority, and the Department is fully committed to combating intellectual property crime by working with our partners throughout the U.S. Government, around the globe, and in the private sector, to improve the effectiveness of criminal enforcement efforts for all stakeholders and the American public.

The focus of my remarks today is the role the Department plays in protecting intellectual property rights, particularly internationally, and our efforts to coordinate with other federal agencies to ensure that intellectual property, in its many forms, is effectively and aggressively protected.

II. Role of the Department of Justice

As the agency responsible for enforcing this nation's criminal laws, the Department's unique role in intellectual property protection is the investigation and prosecution of criminal intellectual property offenses, including those involving copyrighted works, trademarks, and trade secrets.

The Department, through the Federal Bureau of Investigation (FBI), the United States Attorney's Offices (USAOs), the Criminal Division, including its Computer Crime and Intellectual Property Section (CCIPS), and other components, along with our other law enforcement partners, including U.S. Immigration and Customs Enforcement (ICE), has developed a robust criminal enforcement network that aggressively investigates and prosecutes intellectual property crimes. The Department has detailed its overall criminal enforcement efforts over the past six years in the Department's report to Congress pursuant to the Prioritizing Resources and Organization for Intellectual Property (PRO IP) Act of 2008, transmitted on October 13. The report contains a detailed account of the Department's activities, some of which I would like to highlight today, particularly those relating to international enforcement efforts and interagency coordination.

III. International Enforcement Efforts

Combating counterfeiting, piracy, and other intellectual property crimes effectively requires a strong domestic enforcement effort, but we cannot hope to make progress in that fight unless we also look beyond our borders to develop a forceful and effective international enforcement program. The Department has worked to expand its international enforcement efforts, employing a multi-faceted approach. The Department and our investigative partners work closely with our foreign law enforcement counterparts to (1) increase international intellectual property prosecutions that disrupt foreign manufacturers and trans-border shipments of pirated and counterfeit products, and (2) dismantle international organized criminal syndicates engaged in intellectual property crime. The Department has achieved notable successes in these areas, a sample of which I would like to highlight here.

A. Prosecutions involving international piracy and trafficking in counterfeit goods

The Department has had a number of significant successes investigating and prosecuting individuals involved in international piracy and trafficking in counterfeit goods.

- Most recently, in January 2009, Kevin Xu, 36, was sentenced in the Southern District of New York to 78 months in prison for conspiring with others in China to traffic in counterfeit cancer drugs and other pharmaceuticals, including Tamiflu, Plavix, Zyprexa, Aricept, and Casodex. Many of these counterfeits were lacking in active ingredients or contained unidentified impurities. Drugs with lot numbers identical to these counterfeits were detected in the legitimate supply chain in London, prompting a massive recall in the UK.
- In 2008, the Department secured the extradition from Thailand and later conviction of Randy Gonzales, a citizen of the Republic of the Philippines, who was sentenced in the Southern District of Texas to 20 months in prison for his role in importing into the United States and distributing more than three-quarters of a million dollars' worth of counterfeit pharmaceuticals. Gonzales was the first foreign national to be extradited to the United States on charges related to counterfeit pharmaceuticals.
- Also in 2008, the Department obtained the conviction of Iyad Dogmash, a Jordanian national, for importing through the Middle East hundreds of thousands of dollars' worth of counterfeit Viagra tablets, intended for distribution in the United States. Dogmash was sentenced to 48 months in prison.

B. International Online Copyright Piracy Networks

The Department has also achieved unprecedented success in prosecuting large-scale, online piracy and counterfeiting organizations whose crimes seriously damage the marketplace for legitimate goods and services. For example:

- Earlier this year, the Department obtained its 60th felony conviction arising from Operation Fastlink, one of the largest international law enforcement actions ever taken against online piracy. Operation Fastlink targeted multinational organized criminal networks engaged in large-scale software piracy. In the underlying investigation, the FBI worked with foreign law enforcement to conduct over 120 simultaneous search warrants in 27 states and a dozen foreign countries.
- In September 2009, Edward Mohan, II, 46, of Baltimore, Maryland, pleaded guilty in the Eastern District of Virginia to conspiracy to commit criminal copyright infringement for his role in the internet piracy group known as Rabid Neurosis, or “RNS,” which operated from at least 1999 to 2007. RNS gained notoriety for releasing pirated copies of popular albums on the internet before they were commercially released, and the group prided itself on being untouchable by law enforcement.
- In late 2008, Barry E. Gitarts, 25, of Brooklyn, New York, was sentenced to 18 months in prison for his role in operating a server used by the internet music piracy group, Apocalypse Production Crew (APC). Gitarts was the 15th APC member to be convicted of conspiracy to commit criminal copyright infringement.

C. Traditional Organized Criminal Networks

Because intellectual property crime is perceived as a low-risk criminal enterprise with the potential for high profit margins, it is not surprising that the sale of counterfeit and pirated goods is also becoming an attractive revenue source for traditional organized crime groups. This is a serious concern, particularly in Asia, but also in other parts of the world, including countries in the former Soviet Union and the Tri-border region of South America. Organized crime syndicates have the ability and the resources to manufacture and move massive amounts of counterfeit products around the globe.

In the PRO IP Act of 2008, Congress directed the Department’s Criminal Division to work with the FBI and the Department of Homeland Security (DHS) to develop and implement a plan to address links between organized crime and intellectual property crime. Although there has not yet been additional funding provided for this initiative, the Department has nevertheless taken a number of steps to implement the provision and to incorporate intellectual property into its existing International Organized Crime (IOC) Strategy.

For example, the Department has detailed an experienced CCIPS attorney to serve as Counsel to the International Organized Crime Intelligence and Operations Center (IOC-2). Working through senior staff of the IOC-2, CCIPS, the Criminal Division’s Organized Crime and Racketeering Section (OCRS), the FBI, DHS, and other federal agencies are coordinating their efforts and working to ensure that critical IP-related intelligence and case information will be contributed to the IOC-2 data pool and analyzed for links to international organized crime. The Department also is working with member agencies to ensure that IOC-2 is adequately staffed by representatives familiar with intellectual property offenses. Once the IOC-2 is fully operational and incorporates data sources related to intellectual property offenses, the

Department will be able to better identify organized crime cases that involve intellectual property offenses.

D. IP Law Enforcement Coordinators (IPLCs) in Europe and Asia

Building strong and lasting law enforcement relationships with our foreign counterparts is an essential component of effective international criminal intellectual property enforcement. The cornerstone of the Department's effort to strengthen international law enforcement relationships is the Intellectual Property Law Enforcement Coordinator (IPLC) program. Under this program, with the help of the State Department, the Department has deployed two experienced federal prosecutors to serve as IPLCs in Bangkok, Thailand for Southeast Asia and Sofia, Bulgaria for Eastern Europe.

The IPLCs provide training and assistance on intellectual property cases to prosecutors and investigators in their respective regions. The IPLCs' ability to provide targeted instruction on specific enforcement issues is yielding concrete results, including improvements in the number and quality of cases brought in each region. Their presence has also created more opportunities to share evidence informally between countries.

For example, in addition to participating in over 50 regional training programs in the past four years, the IPLC for Asia was integral to obtaining the extradition of Randy Gonzales in the counterfeit pharmaceutical prosecution I mentioned earlier.

The IPLC for Eastern Europe, who has also participated in numerous training programs, has worked directly with small groups of prosecutors and investigators on specific issues. Recently, the Eastern European IPLC worked closely to train Ukrainian prosecutors on how to build a criminal case against a major online piracy site in that country. Although the Ukrainian authorities lacked access to the sort of computer and forensic technology we take for granted, with technical training from the IPLC they were able to take down the online piracy site using an outdated personal computer and a dial-up internet connection.

E. IP Criminal Enforcement Network (IPCEN) in Asia

Working with the IPLC in Bangkok, Thailand, the Department has also spearheaded the creation of an Intellectual Property Crimes Enforcement Network (IPCEN) for Asia in 2007. The IPCEN brings together law enforcement officials from 14 Asian economies to provide a forum for the exchange of successful investigative and prosecutive strategies in combating piracy and counterfeiting crimes. The IPCEN helps strengthen communication channels and promote the informal exchange of evidence, with the ultimate goal of promoting coordinated, multinational prosecutions of the most serious offenders.

F. U.S.-China Joint Liaison Group for Law Enforcement Cooperation

China has been a significant source of counterfeit and pirated products imported into the United States and presents an especially great challenge to U.S. law enforcement. The Department, therefore, has prioritized developing strong working relationships with Chinese law

enforcement officials. For example, since 2006, the Department's Criminal Division and the Chinese Ministry of Public Security (MPS) have co-chaired the Intellectual Property Criminal Enforcement Working Group (IPCEWG) of the U.S.-China Joint Liaison Group for Law Enforcement Cooperation (JLG), which has resulted in an open dialogue on intellectual property enforcement, the sharing of information on selected investigations, and a number of successful joint intellectual property operations.

For example, the IPCEWG provided the platform that supported U.S. and Chinese law enforcement cooperation in Operation Summer Solstice, the largest-ever joint criminal enforcement operation between the FBI and MPS against international criminal groups that manufacture and distribute counterfeit software. As a result of Operation Summer Solstice, in 2007, Chinese law enforcement arrested 25 individuals, dismantled multiple manufacturing locations, and seized over \$7 million in assets and more than \$500 million worth of counterfeit software. To date, China has convicted 11 Summer Solstice defendants, sentencing them each to prison terms of one-and-a-half to six-and-a-half years. According to industry sources, this organized criminal syndicate was responsible for manufacturing and distributing more than \$2 billion worth of pirated software.

G. Training

The Department has also participated in a substantial number of training programs in the United States and abroad to increase awareness of criminal intellectual property issues and techniques for effective enforcement. In many countries, even those with adequate intellectual property laws and criminal procedures, criminal intellectual property enforcement is weak because the police and prosecutors lack sufficient training on obtaining evidence or developing effective criminal investigations and prosecutions in intellectual property cases. Over the past five years, Department attorneys have provided training and education on intellectual property enforcement to over 10,000 prosecutors, police, judicial officers, and other government officials from over 100 countries.

Some of these training programs are brief, while others require multiple training events extending over several years. I would like to touch on just a few of our more recent and significant efforts in Mexico, South Africa, and India.

In 2008, the Department organized several intensive training programs in the Mexican ports of Vera Cruz, Manzanillo, and Mazatlan, working with DHS and the State Department, the World Customs Organization, and various branches of the Mexican government. The courses focused on targeting and risk analysis at the border, criminal investigative techniques, inter-agency networking and cooperation, and the need for stronger sentences. After the Vera Cruz training, Mexican law enforcement conducted nine major seizures of infringing products, seven of which were criminally investigated by local prosecutorial authorities. Before the training, there had never been a seizure or criminal referral at the Vera Cruz port for intellectual property violations. Likewise, after the training program in Manzanillo, government officials pledged to support future capacity building to combat intellectual property crime and to increase the number of intellectual property seizures and referrals at the local port.

In July 2008, the Department, working with the State Department, provided the first-ever training program in South Africa on computer forensic skills particular to intellectual property cases. Bringing 20 pre-configured laptop computers from the United States, the training team was able to provide hands-on training on investigating and seizing computers, securing and analyzing electronic evidence, conducting off- and online investigations using computers, and presenting electronic evidence in court. To increase in-country enforcement capacity, the program also trained instructors from lead agencies in intellectual property enforcement. These newly-trained instructors are now able to provide additional training to other prosecutors and investigators in country. Finally, to increase the level of expertise in the South African judiciary on intellectual property cases, the Department organized a judicial workshop in Johannesburg for more than 200 magistrates from around the country.

India is another country important to U.S. intellectual property interests, with its rapidly expanding information economy and many ties to U.S. corporations through manufacturing agreements, joint ventures, and production facilities. India is experiencing substantial domestic growth as a producer of intellectual property in the entertainment, medical, and software fields. To help ensure that systems to protect intellectual property keep pace with economic and business trends, the Department has worked closely with representatives of the judiciary and the private sector in India, as well as police, prosecutors, and other government officials, to address substantial delays and inefficiencies in the Indian court system that impose significant obstacles to effective enforcement of intellectual property rights in India. Among other things, the Department's Criminal Division has worked with Indian judicial officials to increase efficiency in adjudicating criminal intellectual property cases through plea bargaining, which Indian law first authorized in 2006. Over the past few years, CCIPS has held training programs in India and the United States that demonstrated how plea bargaining can lead to the more efficient administration of justice while also protecting the rights and interests of criminal defendants, crime victims, and the public. The Criminal Division also worked with Indian court authorities to implement a "fast track" court option in Delhi and Bangalore for criminal intellectual property cases and other appropriate offenses that are intended to resolve such cases by plea or trial within six months. Although the "fast track" courts in both cities have resolved a number of intellectual property criminal cases, these court systems are still in the process of reorganization, including the transfer of all criminal intellectual property cases to designated judges.

In addition, the Department has assisted in the creation of mediation centers in these two cities, both of which are major business centers with rapidly-developing technology and intellectual property-based business communities. The Department organized intensive mediation training sessions by U.S. federal judges and other experts. Within 18 months of creating this program, the Bangalore Mediation Center alone has settled nearly 3,000 disputes. The Criminal Division will continue to work with Indian enforcement authorities and representatives of rights holders and other affected groups during the coming year, helping to develop further the expertise necessary for effective investigation, prosecution, and resolution of criminal intellectual property violations.

IV. Coordination with Domestic Law Enforcement Partners

Through the Criminal Division's Computer Crime and Intellectual Property Section and a dedicated network of over 230 Computer Hacking and Intellectual Property (CHIP) coordinators and AUSAs nationwide, the Department works in close cooperation with all of our partner law enforcement agencies on intellectual property cases. The complexity of investigations and prosecutions involving intellectual property crime requires early engagement and coordination between investigators and prosecutors. This collaborative approach has resulted in a number of successful multi-district and multi-national investigations and prosecutions, several of which I highlighted earlier.

The Department also works closely with our law enforcement partners through the National Intellectual Property Rights Coordination Center (IPR Center). The IPR Center consists of investigators and analysts from participating agencies, including ICE, U.S. Customs and Border Protection (CBP), the FBI, the Food and Drug Administration (FDA), and the U.S. Postal Inspection Service, who work together to combat counterfeiting and piracy. The IPR Center de-conflicts investigative leads, coordinates investigations, and provides outreach and training. The Criminal Division's Computer Crime and Intellectual Property Section currently has two attorneys working closely with the IPR Center and expects that attorney support to increase as the Center increases its operational capacity. In addition, the Department also coordinates, when appropriate, with other law enforcement partners, including INTERPOL and state and local authorities.

The Department's ability to undertake coordinated law enforcement actions has been bolstered by the 31 additional FBI Special Agents funded by Congress in 2009 who will be dedicated solely to investigating intellectual property crime. The Criminal Division, the FBI, and the Executive Office for U.S. Attorneys worked together to determine the appropriate placement of these agents. The FBI has placed nearly all 31 agents, including 26 agents in field offices located near CHIP Units and the remaining 5 agents (to include a Unit Chief and two Supervisory Special Agents) at the IPR Center. These Special Agents will help to generate more investigations and better prosecutions of both domestic and international intellectual property crime.

V. Coordination with Other U.S. Agencies

The Department also works extensively on intellectual property issues with other agencies in the federal government, including the Departments of State and Commerce, the U.S. Patent and Trademark Office (USPTO), and the U.S. Trade Representative (USTR). For example, the Department frequently coordinates with USPTO and State in organizing intellectual property training programs overseas. We coordinate with USTR through its Special 301 process, in which USTR examines IPR protection and enforcement in various countries, as well as by contributing to negotiations on portions of international treaties involving intellectual property that affect criminal enforcement interests, such as parts of Free Trade Agreements and the developing Anti-Counterfeiting Trade Agreement.

Another example is the Department's past role as co-chair of the National Intellectual Property Law Enforcement Coordination Council (NIPLECC). NIPLECC was a forum for coordination among federal agencies involved in various aspects of intellectual property policy, including USPTO, DHS and USTR.

The PRO IP Act, enacted last October, replaced NIPLECC with a newly-created Intellectual Property Enforcement Coordinator (IPEC) in the Office of Management and Budget (OMB) and an Advisory Committee comprised of a broad range of federal agencies including the Department's Criminal Division and the FBI; the Department of Commerce, including USPTO; the Department of State, including U.S. Agency for International Development and the Bureau of International Narcotics Law Enforcement; ICE and CBP; the FDA; and the Department of Agriculture. The IPEC will chair the Advisory Committee and work with its members to develop a strategic plan that enhances intellectual property enforcement here and abroad.

VI. Conclusion

I would like to thank the Subcommittee for the opportunity to share with you, and the American people, the high priority the Attorney General places on criminal enforcement of intellectual property rights and the work we do to combat intellectual property crime both here and abroad. We recognize that each of the federal components testifying here today play a distinct and vital role in the protection of intellectual property, and we look forward to continuing to work with them toward our common goal of maintaining a robust system for intellectual property protection that, in the words of our Founding Fathers, "promotes the progress of science and the useful arts," and that fosters creativity and innovation and protects consumers.

This concludes my remarks. I would be pleased to answer questions from you and other members of the Subcommittee.

Ms. WATSON. Thank you, Mr. Weinstein.
Now you may proceed, Mr. Craft.

STATEMENT OF WILLIAM E. CRAFT

Mr. CRAFT. Thank you, chairwoman and committee members. It is a pleasure to be here today to testify on the State Department's role in protecting intellectual property rights in today's global economy.

We welcome the committee's interest in this issue and look forward to continuing to work with you to achieve our mutual goal of ensuring that U.S. intellectual property rights are fully respected everywhere in the world. As President Obama has said, innovation is the key to good new jobs for the 21st century.

Since intellectual property rights encourage and reward innovation, protecting American intellectual property abroad is one of the State Department's top economic policy priorities. We work closely with other U.S. Government agencies, the private sector, and foreign governments to achieve that goal.

Within the State Department, our efforts are led by the Office of Intellectual Property Enforcement, part of the Trade Policy and Programs Deputate that I head. That office now has a staff of 12 people. As you are aware, Congress created this office in 2005 to strengthen State Department efforts to combat counterfeiting and piracy.

IPE promotes enforcement of U.S. IP rights overseas, represents the State Department in inter-agency IPR policy discussions, and participates actively in bilateral and multilateral negotiations to improve enforcement of IP rights.

State implements IPR enforcement training and technical assistance programs for which the Congress has given us \$4 million in 2009. In calendar year 2009, we used that money to train over 1,500 customs, police, and judicial officials from more than 20 countries, including the Ukraine, Mexico, Russia, Vietnam, and Nigeria.

State also conducts public outreach to foreign audiences on the importance of IP to host country economies, innovators, and creators, and trains our embassy officers overseas around the world on IP enforcement.

Intellectual property enforcement is integrated into the work of other State Department bureaus and offices. For example, we work closely with our Bureau of International Organizations and with other agencies to strengthen the World Intellectual Property Organization and to ensure that other U.N. agencies support good IP policy. Our regional bureaus, U.S. embassies, and consulates are on the front lines of protecting U.S. IP rights in particular countries, responding to complaints raised by U.S. companies and vigorously pressing foreign governments to combat piracy and counterfeiting.

There is a Foreign Service officer assigned to work on intellectual property protection in every U.S. embassy overseas.

Madam Chairwoman, as you have noted, piracy and counterfeiting are still enormous problems, but we are making some headway. There are more examples in my written testimony, but let me just cite two examples of areas where we think we have made a positive impact.

On the enforcement side, the U.S. Government and the private sector have been working actively with Mexico to encourage them to increase enforcement of their laws, and working on information provided by the U.S. industry, the Mexican Attorney General's office recently arrested a number of individuals for camcording in movie theaters, thereby dismantling one of Mexico's major camcording rings.

In terms of the winning hearts and minds side on public outreach, an excellent example is the way that our embassy in Bosnia helped to develop an IPR school campaign with a curriculum and comic books printed in the three local languages, supported by appearances by the U.S. Ambassador and several Bosnian movie and music stars.

Let me just note, Madam Chairwoman, that the State Department concurs with the recent GAO report's recommendations on improving coordination between our embassies and our intellectual property attaches overseas, and we have sent a cable to relevant posts instructing them to implement the recommendations of the GAO. We are getting responses from the posts and we are reviewing those now.

As Mr. Stoll and the others have noted, we know very well and very favorably Ms. Espinel and we look forward to working with her as she tries to raise the image and profile of protecting intellectual property as she takes on her new role. We look forward to working very closely with her.

Finally, let me thank you and the committee for your interest in this very important issue and to assure you that we look forward to working with you to strengthen our efforts to protect intellectual property.

Thank you very much.

[The prepared statement of Mr. Craft follows:]

Testimony of William E. Craft
Acting Deputy Assistant Secretary for Trade Policy and Programs in the
Bureau of Economic, Energy, and Business Affairs
U.S. Department of State

Before the House Committee on Oversight and Government Reform,
Subcommittee on Government Management, Organization, and Procurement

Washington, DC

December 9, 2009

“Protecting Intellectual Property Rights in a Global Economy: Current
Trends and Future Challenges”

Chairwoman Watson, Ranking Member Bilbray, honorable committee members, it is a pleasure to be here today to testify on the State Department’s role in protecting intellectual property rights in today’s global economy. We welcome the Committee’s interest in this issue and look forward to continuing to work with

you to achieve our mutual goal of ensuring that U.S. intellectual property rights are fully respected everywhere in the world.

President Obama has made it clear that innovation is “the key to good, new jobs for the 21st century.” Intellectual property rights are an important tool for encouraging and rewarding innovation. The Administration’s “Strategy for American Innovation” notes that “Intellectual property is to the digital age what physical goods were to the industrial age. We must ensure that intellectual property is protected in foreign markets and promote greater cooperation on international standards that allow our technologies to compete everywhere.” Protecting American intellectual property (IP) abroad is one of the State Department’s top economic policy priorities and we work closely with other U.S. government agencies, the private sector and foreign governments to achieve that goal.

Within the State Department our efforts are led by the Office of International Intellectual Property Enforcement (IPE), part of the Trade Policy and Programs Deputate that I head. As you are aware, Congress created this office in the FY2005 omnibus budget, to help ramp up State Department efforts to combat counterfeiting and piracy. As its name implies, IPE focuses on promoting enforcement of U.S. IP rights overseas. It also represents the State Department in interagency IPR policy discussions, such as the Special 301 process led by USTR,

and participates actively in bilateral and multilateral negotiations to improve enforcement of IP rights, such as the Anti-Counterfeiting Trade Agreement (ACTA). IPE collaborates with the Bureau for International Narcotics and Law Enforcement Affairs (INL) to implement IPR enforcement training and technical assistance programs for foreign enforcement officials in developing countries. IPE also conducts public outreach to foreign audiences on the importance of IP and training for State Department officers involved in IPR enforcement.

Intellectual property rights enforcement is integrated into the work of other State Department bureaus and offices. IPE works with our Bureau of International Organizations on strengthening the World Intellectual Property Organization (WIPO) and ensuring that the actions of other UN agencies are consistent with good IP policy. Our regional bureaus, U.S. Embassies and Consulates are on the front line of protecting U.S. IP rights in particular countries: responding to complaints raised by U.S. companies and vigorously pressing foreign governments to combat piracy and counterfeiting.

IPE works closely with our Bureau of Oceans, Environment and Science (OES), which promotes innovation and scientific cooperation. OES is working with the U.S. Patent and Trademark Office (USPTO) in the Intergovernmental Committee under the World Intellectual Property Organization (WIPO) on the discussions there regarding IP and traditional knowledge, genetic resources, and

traditional cultural expressions. OES also leads the U.S. delegations to the ad-hoc working group in the Convention on Biological Diversity that is negotiating an international regime for access and benefit sharing of genetic resources. The outcome of those negotiations could have significant implications for patent applicants seeking protection for inventions that involve genetic material in contracting countries.

The State Department International IPR Enforcement Training Program

In 2004, Congress urged that funds for international law enforcement assistance be set aside in order to fill a perceived gap in government-to-government foreign law enforcement training and technical assistance to combat IPR crime. Criminal enforcement capacity training is essential if we are to confront increasingly sophisticated transnational organized crime groups that have moved into the lucrative IPR crime space. Due to the cross-cutting nature of the IPR crime threat and its impact on trade, growth, and innovation, INL and IPE work in partnership to develop priorities for using the INL funds for IPR criminal enforcement training and technical assistance. Funding for IPR crime training and technical assistance has increased ten-fold since 2003, from \$400,000 in FY03 to \$4 million in FY09. Including the recently approved FY09 programs, since 2004 the State Department has dedicated a total of \$18.5 million for seventy nine

training and technical assistance initiatives designed to build the enforcement capacity of our foreign partners to fight IP crime. For example, in calendar year 2009 alone, State Department funds went to support 18 training events for over 1,500 customs, police and judicial officials from more than 21 developing countries, including Ukraine, Mexico, Russia, Vietnam and Nigeria.

Training is delivered by USG inter-agency teams composed of enforcement officials from DOJ, PTO and DHS, with team composition tailored to the training task. Priorities for funding are developed with input from USG enforcement agencies, U.S. Missions, information from the Special 301 process, and input from U.S. rights holders. As a party to the WTO TRIPS Agreement, the U.S. places particular emphasis on helping developing nations build their enforcement capacity. We also work closely with a number of multilateral organizations such as the Association of Southeast Asian Nations (ASEAN), the Asia-Pacific Economic Cooperation forum (APEC), and the Organization of American States (OAS) to implement training aimed at enhancing multilateral cooperation against increasingly borderless crime groups.

Public-Private Partnership

The State Department develops priorities for IPR enforcement training in close consultation with U.S. rights holders, both through the submissions regularly received from IP rights holders as part of the Special 301 process and also through their participation in the regular meetings of the State Department's Training Coordination Group (TCG). The criminal enforcement training focus in the State Department program is designed to complement private sector training initiatives by focusing on the one kind of training private rights holders cannot deliver: government-to-government criminal enforcement assistance. This strong focus on criminal IPR enforcement is welcomed by industry due to the rise of transnational crime group involvement in IP crime, a phenomena that requires a strong law enforcement response.

Rights holder input helps inform the design of our training programs. For example, in Indonesia U.S. rights holders suggested that the assistance of USG advisors might be the optimal way to facilitate the Government of Indonesia's continued momentum on enforcing its new optical disc piracy regulations. In Eastern Europe, where copyright piracy, including on the Internet, and trademark counterfeiting continues to skyrocket, rights holders supported continuing USG involvement to help coordinate a regional response to transnational crime groups. In Mexico, a ramped-up U.S. capacity building program is acting on the advice of rights holders by focusing enforcement training at ports of entry and other venues

outside the capital. And in Sub-Saharan Africa we have responded to NGO and rights holders concerns about counterfeit pharmaceuticals and other consumer goods that negatively impact public health and human safety by expanding training and technical assistance focused on anti-counterfeiting.

Long-term Focus and Flexibility in IPR Programming

Our IPR capacity-building in developing countries incorporates flexible, multi-year approaches and builds on lessons-learned. Examples include programs in Paraguay, where we funded and developed a multi-year program to build new Paraguayan enforcement units and capabilities that had not existed, and Southeast Asia, where we have developed a multi-year strategy to build regional capacity in advance of the expected ASEAN customs union. In sub-Saharan Africa, we have been increasing assistance every year based on a long-term plan to assist countries in working together through regional entities like the East African Community, South African Customs Union and ECOWAS to combat region-wide issues like counterfeit pharmaceuticals.

Interagency Coordination

The State Department works closely with interagency colleagues to ensure that our projects complement the IP training efforts of other USG agencies –

combining resources when most effective, multiplying the impact of our training through collaboration, and avoiding redundancy. Currently, the USPTO provides funding every year for IPR training for foreign government officials. In addition, USAID provides IPR training through trade capacity building focused on WTO TRIPS implementation, and has funded the work of the Commercial Law Development Program at the Department of Commerce on training for judges and prosecutors. We consult with all of these agencies when planning our training program.

The IPR Training Coordination Group

The State Department Intellectual Property Rights Training Coordination Group (TCG) co-chaired by State's INL and EEB Bureaus is comprised of U.S. government agencies and private stake holders (both industry and NGO) that provide IPR-related international training, technical assistance and informational programs. Participating USG agencies include the Departments of Commerce, Justice and Homeland Security, as well as the Patent and Trademark Office, the Copyright Office of the Library of Congress, U.S. Immigration and Customs Enforcement (ICE) IPR Center, the Federal Bureau of Investigation, the U.S. Agency for International Development, and the Office of the U.S. Trade Representative. The TCG provides an informal opportunity for participants to share information on IPR assistance plans and programs and to discuss lessons

learned and best practices. This information assists participants in setting priorities and in coordinating with each other on the content and delivery of assistance. The State Department International IPR Enforcement Training Program benefits from input from the TCG and announces its annual priorities at TCG meetings.

Many of the training programs offered help developing countries implement their obligations under the WTO TRIPS Agreement. As a party to TRIPS, the United States provides training and technical assistance to developing and least developed members of the WTO.

Public Diplomacy Resources and Outreach Coordination

In addition to our enforcement training efforts, the State Department continues to respond to the need for increased coordination in and emphasis on intellectual property rights outreach to key public audiences overseas. On World IP Day in spring 2007, IPE took the interagency lead on public outreach overseas, kicking off a strategic IPR public diplomacy initiative. In the first year of this initiative, IPE produced and distributed government-wide talking points and fact sheets, and created and packaged new resources for public awareness overseas. The campaign progressed with release of public fact sheets addressing topics important to specific regions, through digital video conferences with foreign government and private sector officials and through foreign press trips to the

United States. Building upon this in 2008, IPE obtained State Department public diplomacy funds, which we awarded to Embassies for strategic IPR outreach in several countries in Africa, Southeast Asia, the Balkans, and South America. For example, in Vietnam, State public diplomacy funds paid for a new IPR enforcement guide for merchant retailers and re-publication of WIPO's outreach materials. In Mauritius, we helped fund a public advertising campaign and radio program.

Finally, IPE continues to foster partnerships on international IPR outreach by facilitating coordination within the State Department and among U.S. agencies, nongovernmental actors, foreign governments, and international organizations such as the World Intellectual Property Organization (WIPO). Through our IPR public diplomacy work, and our collaborative efforts, we continue to encourage developing countries to integrate intellectual property into their economic development planning.

Multilateral Cooperation and Leveraging other Donor Resources

U.S. and State Department IPR training and assistance programs are also designed to complement and promote collaboration with other donor training and technical assistance efforts. For example, the ASEAN - USPTO-managed training

program was designed specifically to complement the European Union ECAP II program of assistance to the ASEAN nations.

International IPR Enforcement Training and Outreach – Lessons Learned

The lessons learned from the past six years of IPR enforcement training and outreach programming are incorporated into our new programs. We've learned the value of going local – some of our most successful programs created IPR investigative units and IPR advisors that have remained in-country over time. We also work to build strong partnerships - both with the governments and with private sector. Our experience has underscored the importance of integrating our training and outreach efforts with other actions being undertaken by other agencies, governments or international organizations – our efforts are more successful if they are not disconnected. We've also learned to leverage other resources – from other USG agencies, host governments, private sector and partner nations – to maximize the training impact and engage a broad array of supporters to the effort.

Embassy Officers' IPR Regional Trainings

IPE also works to ensure that our Embassy officers around the world are well-trained on the latest IPR issues. Since 2004, IPE has organized seven overseas IPR officers training conferences and participated in many more, in

regions around the world, incorporating private sector and government trainers and with a focus on the technical IPR issues and problems facing that particular region. Two more such conferences are planned for 2010. These training sessions result in increased IPR technical knowledge as well as more awareness of IPR-related diplomatic tools that our officers can use in their host countries.

Some Success Stories

Below are some examples of how the State Department's IPR training programs -- for both host government officials and U.S. embassy officers -- and its public outreach initiatives complement each other to promote respect for intellectual property rights.

- Our October 2008 European region officer training conference spurred several participants to initiate major IPR conferences and programs in eight different host countries. For example, our Embassy in Bosnia leveraged its strategic outreach country public diplomacy funds to partner with the private sector and WIPO on a Balkan-region elementary school outreach campaign. Later awarded top marks at a regional marketing and public relations festival in Slovenia, the campaign kicked off on World Intellectual Property Day this year and featured: the development of an IPR curriculum; publication and distribution of WIPO's IPR comic books translated into three local languages; and special guest appearances by the U.S. Ambassador and Bosnian film stars

and recording artists in programs hosted at local schools. Complementing this effort, Embassy Sarajevo worked with the USPTO to organize a regional IPR police and prosecutor training conference in June 2009, which was well attended and received extensive local TV and radio coverage.

- Embassy Kyiv reported in April 2009 that a Ukrainian police officer who had received INL IPR enforcement training at the Embassy in December 2008 was responsible for investigating and shutting down a significant Ukrainian pirate internet website that was receiving 20,000 hits per day and distributing over 7,000 illegal music and movie files. The Embassy has noted that strong collaboration with the Department of Justice IP Law Enforcement Coordinator stationed in Eastern Europe has helped Embassy Kyiv engage in intensive U.S.-Ukraine IPR training and consultations over the past few years.
- Embassy Nicosia organized an IPR seminar in Northern Cyprus in April 2009 that covered a wide range of issues, including organized crime, internet piracy, counterfeit products, as well as both U.S. and EU perspectives on IPR enforcement. Our Ambassador to Cyprus spoke at the event emphasizing the importance of the protection of intellectual property rights in attracting investment and supporting economic development.
- Embassy Athens worked with the USPTO to develop a roundtable discussion in February 2009 with 35 Greek judges on the enforcement of copyright law. A

U.S. judge was brought over to speak and the event included an Ambassador-hosted reception in honor of the Greek judges, our guests, and the Hellenic Copyright Organization, which co-organized the event.

- In Vietnam, IPE worked with our Embassy officials, USPTO, Vietnam's Ministry of Trade, the private sector and WIPO to implement a two-part outreach initiative using PD funds. This included publication of a new IPR enforcement guide for merchant retailers and re-publication of WIPO's outreach materials previously translated by the Viet Government.
- In Mauritius, our Embassy officials, using PD funds, partnered with the Mauritius Society of Authors (MASA) and with Microsoft to conduct a multi-phase IPR outreach program featuring a public advertising campaign, a nationally-publicized radio program, and educational outreach to students and small and medium sized enterprises. Notably, Microsoft signed a MOU with MASA, in the context of this initiative, to help MASA in its fight against piracy.
- Following concerted efforts by the USG and the private sector, the Mexican Attorney General's office, working from information provided by the industry, arrested four individuals for camcording in a movie theatre, thereby dismantling one of Mexico's four major known camcording rings. While this action was undertaken within Mexico's existing legal framework, the USG also continues

to urge Mexico to pass legislation criminalizing camcording in movie theaters in order to enhance its efforts further to combat illegal camcording.

- In March 2009, the U.S. Embassy in Santiago and the U.S. Patent and Trademark Office (USPTO) organized a seminar to strengthen Chile's IPR enforcement. More than 200 Chilean police officers, prosecutors and customs officers attended the seminar. Experts from the USPTO, Immigration and Customs Enforcement (ICE) IPR Center, Customs and Border Protection and FBI discussed topics ranging from effective customs controls to the influence of organized crime in IPR violations. U.S. Ambassador Paul Simons delivered a speech promoting U.S.-Chilean cooperation on IPR issues and Chile's National Prosecutor, Sabas Chahuan, spoke and highlighted the importance of combating IPR violations. As a direct result of the training, within three weeks Chilean authorities seized more than 2,000 counterfeit Apple products.

GAO Report “Intellectual Property: Enhanced Planning by U.S. Personnel Overseas Could Strengthen Efforts”

The State Department concurred with the recent GAO report's recommendation that U.S. posts with USPTO IP attaches develop annual IP interagency work plans that set objectives. We strongly support the importance of interagency coordination and of leveraging scarce resources to achieve a greater

impact on IPR enforcement. We have sent a cable to relevant posts, instructing them to assess how IP is currently addressed in mission work plans and to consider how the suggestions in the GAO report and the recommendation for Executive Action can be effectively applied and we are reviewing posts' responses. Some of our posts are already working to improve interagency coordination and implement the GAO's recommendation. For example, the newly arrived IPR attaché in Beijing is in the process of gathering information from all relevant agencies in our mission and plans to present a draft strategic plan at the next meeting of the mission's IPR task force for interagency discussion. The attaché in Moscow established an "IPR Team" when she arrived at post in 2007, which now includes representatives from the Economic Section, Law Enforcement Section, Public Affairs, the Environmental Science and Technology Section, Department of Justice, Department of Homeland Security and USAID. The team meets quarterly and develops an IPR Strategic Plan, as well as developing an annual calendar of IPR training programs and events.

Conclusion

As we plan for the future, we are stressing some new approaches. We will further enhance coordination within the State Department and with other agencies both to increase the impact of our programs and to reduce costs, by identifying

opportunities where IPR training can be combined with other training. For example, we are organizing an IPR component in training being offered to economic officers in the Western hemisphere in early 2010. We also recognize the need for greater attention to institution-building and coordination among law enforcement entities (customs, prosecutors, judges) in our target countries, and will look for ways to structure our training programs to promote such coordination. The threat of expanding transnational crime groups continues to remind us that in today's global economy, we cannot limit ourselves to country-based approaches. Where appropriate, we will take more regional approaches. For example, commonalities in IP infringement problems in South America might make this area particularly appropriate for a regional problem-solving approach, which we hope to explore with relevant governments over the next year. Finally, we need to put a greater emphasis on a collaborative approach that stresses not only legal obligations, but the mutual benefits of respecting and enforcing IP rights. Increasingly, developing country industries, from textile designers in Africa to research-based pharmaceutical companies in India and Brazil, have their own IP rights to defend. By using public diplomacy approaches, we will be better able to develop our common interest in promoting the creation and use of intellectual property to foster innovation and economic development.

Again, I thank you for your interest in this very important issue and look forward to your guidance on how we can strengthen our efforts to protect IP.

Ms. WATSON. Thank you, Mr. Craft.
Now you may proceed, Mr. Yager.

STATEMENT OF LOREN YAGER

Mr. YAGER. Thank you. Good morning, Madam Chairwoman, Ranking Member Bilbray, and members of the subcommittee. Thank you for the opportunity to appear before the subcommittee to discuss our work on U.S. efforts to protect intellectual property rights. We appreciate the opportunity to continue our contributions to the record that this committee has established on IP protection.

This hearing is timely, as Congress recently overhauled the U.S. structure for IP protection. The PRO-IP Act created a new structure, and the Senate recently confirmed the coordinator to chair the Advisory Committee.

In my statement today I will address two topics on IP protection and enforcement that are relevant to that structure. First let me talk about the lessons learned from past efforts to coordinate IP protection and enforcement, and second I will make a few observations on the efforts of the Patent and Trademark Office intellectual property attaches in key countries around the world.

Let me start with a few observations from our prior work. The PRO-IP Act of 2008 enacted several changes that addressed weaknesses we found in the prior IP coordinating structure. That structure was initiated under two different authorities and lacked clear leadership and permanence, hampering the effectiveness and long-term viability of such coordination.

In a GAO report undertaken for this committee in 2004, we reported that this council had not undertaken any independent activities since it was created. Congress subsequently made enhancements in 2004 to strengthen its role but we reported that it continued to have leadership challenges.

In contrast, the Presidential initiative called STOP had a positive image among the agencies and the private sector, and from its beginning was characterized by a high level of coordination and visibility. However, as a Presidential initiative it lacked permanence, since its influence was tied to a single administration.

While its impact will depend upon its implementation, the PRO-IP Act of 2008 enacted several changes that addressed weaknesses in that prior structure. For example, the act places leadership in the Executive Office of the President, a status similar to STOP. In addition, the PRO-IP Act specifically requires the new agency to prepare a strategic plan that builds in mechanisms for accountability and for oversight. The PRO-IP Act requires the council to submit the strategic plan to committees of the Congress to improve accountability.

Let me now turn to another important issue, and that is the placement of the PTO IP attaches abroad. An additional theme of the PRO-IP act is the emphasis on strengthening the capacity of U.S. agencies abroad to protect and enforce IP rights. In a report we released in September of this year, we found that the IP attaches could be an asset to U.S. firms and to other U.S. agencies who needed assistance in matters related to IP enforcement. These IP attaches provided this assistance by adopting a number of practices.

First, the attaches served as effective focal points. Prior to the creation of the IP attache position, State economic officers had primary responsibility for IP, but IP attaches are full time in the issue, and they also impart their subject matter expertise, which enhances their effectiveness as focal points.

Second, they established IP working groups. Several agency officials at the posts we visited in China, Thailand, and India said that the working groups provided several benefits, such as increasing coordination on training and on other activities.

Third, the attaches leverage resources through joint activities. For example, the IP attaches helped the Foreign and Commercial Service efforts to assist firms by providing advice on how to avoid IP problems and answering IP-related questions.

While our observations on PTO's attaches abroad are largely positive. Our prior work has also demonstrated that the long-term success of overseas operations requires careful attention to human capital planning. In particular, we have observed that other agencies attempting to establish a presence abroad had to make specific efforts to ensure that they could recruit and retain sufficient personnel with both the technical as well as the cultural expertise that is essential in those posts. These considerations may be important as the Congress and the PTO make decisions about the scale and the performance of this program.

Madam Chairwoman, Ranking Member Bilbray, thank you for the opportunity to appear before this subcommittee to summarize our work. I will be happy to answer any questions that you or other Members have.

[The prepared statement of Mr. Yager follows:]

United States Government Accountability Office

GAO

Testimony

Before the Subcommittee on Government
Management, Organization, and Procurement,
Committee on Oversight and Government
Reform, House of Representatives

For Release on Delivery
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**INTELLECTUAL
PROPERTY**

**Enhancements to
Coordinating U.S.
Enforcement Efforts**

Statement of Loren Yager, Director
International Affairs and Trade



Madam Chairwoman and Members of the Subcommittee:

Thank you for the opportunity to appear again before the Committee to discuss our work on U.S. efforts to protect intellectual property (IP) rights. We appreciate the opportunity to contribute to the record that this Committee has established on IP protection. As you know, IP is an important component of the U.S. economy. U.S. government efforts to protect and enforce IP rights domestically and overseas are crucial to safeguarding innovation and preventing significant losses to U.S. industry and IP rights owners as well as addressing health and safety risks resulting from the trade in counterfeit and pirated goods.

This hearing is timely, as Congress recently overhauled the U.S. structure for coordinating IP protection. The Prioritizing Resources and Organization for Intellectual Property Act of 2008 (PRO-IP Act) created a new interagency IP enforcement advisory committee and authorized the President to appoint an Intellectual Property Enforcement Coordinator (IPEC) position within the Executive Office of the President to chair the new committee.¹ In September 2009, the President submitted his nomination to the Senate for confirmation and, on December 3, 2009, the Senate confirmed Victoria Espinel as the first IPEC.

In my statement today, I will address two topics on IP protection and enforcement in anticipation of some of the challenges ahead in implementing the PRO-IP Act: (1) lessons learned from past efforts to coordinate IP protection and enforcement and (2) observations on a recent initiative to place IP attachés overseas to promote and protect IP rights, based on our field work at four posts in three case study countries.

My remarks are based on a variety of assignments that GAO has conducted over the past 3 years on the international and domestic efforts undertaken by U.S. agencies to coordinate their efforts to address IP theft and piracy issues.² Most recently, we conducted field work in March 2009 at four

¹PL 110-403, Title III.

²GAO, *Intellectual Property: Enhanced Planning by U.S. Personnel Overseas Could Strengthen Efforts*, GAO-09-863 (Washington, D.C.: Sept. 30, 2009); GAO, *Overseas U.S. Government Personnel Involved In Efforts to Protect and Enforce Intellectual Property Rights*, GAO-09-402R (Washington, D.C.: Feb. 26, 2009); GAO, *Intellectual Property: Federal Enforcement Has Generally Increased, but Assessing Performance Could Strengthen Law Enforcement Efforts*, GAO-08-157 (Washington, D.C.: Mar. 11, 2008); GAO, *Intellectual Property: Strategy Targeting Organized Piracy (STOP) Requires Changes for Long-term Success*, GAO-07-74 (Washington D.C.: Nov. 8, 2006).

posts in three countries: Beijing and Guangzhou, China; New Delhi, India; and Bangkok, Thailand. We have made several recommendations over the course of our work, with which the recipient agencies generally agreed. We conducted our work in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provided a reasonable basis for our findings and conclusions based on our audit objectives.

Background

The PRO-IP Act of 2008 eliminates the old structure for coordinating IP efforts and creates a new interagency advisory committee composed of eight federal entities. The responsibility of the IPEC, among other things, is to lead the committee in the development of a joint strategic plan to reduce counterfeiting and other types of IP infringement, and to assist in the implementation of the joint strategic plan when requested by the advisory committee members.

As we have reported in our prior work on IP protection, multiple federal agencies undertake a wide range of activities that fall under three categories: policy initiatives, training and technical assistance, and law enforcement.

- U.S. international trade policy initiatives to increase IP protection and enforcement are primarily led by the Office of the U.S. Trade Representative (USTR), in coordination with the Departments of State and Commerce, U.S. Patent and Trademark Office (USPTO), and Copyright Office, among other agencies.
- Key training and technical assistance activities are undertaken by the Departments of Commerce, Homeland Security, Justice, and State; the Federal Bureau of Investigation (FBI); USPTO; and the Copyright Office.
- A smaller number of agencies and their entities are involved in investigating IP violations and enforcing U.S. IP laws. Working in an environment where counterterrorism is the central priority, the Department of Justice, including the FBI, and the Department of Homeland Security take actions that include engaging in multicountry investigations and seizures of goods that violate IP rights. The Food and Drug Administration (FDA) also investigates IP violations for FDA-regulated products as part of its mission to assure consumer safety.

In many cases, IP enforcement is generally a small part of the agencies' much broader missions; however, federal agencies are placing new emphasis on IP protection and enforcement. In particular, USPTO recently established eight IP attaché positions overseas that have IP protection and enforcement as their primary mission.³ The IP attachés work on a range of IP activities in coordination with other federal agencies, U.S. industry, and foreign counterparts.

U.S. IP Coordinating Structure and Strategy Lacked Strong Leadership and Permanence

The PRO-IP Act of 2008 enacted several changes that address weaknesses that we described with the prior IP coordinating structure. The prior structure was initiated under two different authorities and lacked clear leadership and permanence, hampering its effectiveness and long-term viability. In 1999, Congress created the National Intellectual Property Law Enforcement Coordination Council (NIPLECC) as a mechanism to coordinate U.S. efforts in the United States and overseas. In 2004, the Bush Administration announced the Strategy Targeting Organized Piracy (STOP), which included a similar group of U.S. agencies under a Presidential Initiative.

In our reporting, we described how NIPLECC had struggled to define its purpose and retained an image of inactivity within the private sector.⁴ In a report undertaken for this Committee in 2004, we noted that NIPLECC had little discernible impact and had not undertaken any independent activities since it was created, according to interviews with agency officials and its own reports. Congress subsequently made enhancements to NIPLECC in

³USPTO's first IP attaché was posted in Beijing, China, in 2004. During 2006 and 2007, USPTO added a second attaché position in Beijing and an attaché position in Guangzhou, China, and expanded the program to five other countries: Egypt, Thailand, Russia, Brazil, and India. Since then, the Egypt position has been eliminated and a new position in Doha, Qatar, is in the planning stages.

⁴GAO, *Intellectual Property: U.S. Efforts Have Contributed to Strengthened Laws Overseas, but Challenges Remain*, GAO-04-912 (Washington, D.C.: Sept. 8, 2004); and GAO-07-74.

December 2004 to strengthen its role,⁶ but we reported to this Committee in 2006 that it continued to have leadership problems.

In contrast, the presidential initiative called STOP had a positive image compared to NIPLECC, but lacked permanence, since there was no assurance that its authority and influence would continue in successive administrations. Unlike NIPLECC, STOP from its beginning was characterized by a high level of active coordination and visibility. Many agency officials said that STOP has increased attention to IP issues within their agencies and the private sector, as well as abroad, and attributed that to the fact that STOP came out of the White House, thereby lending it more authority and influence.

STOP was also a first step toward an integrated strategy to protect and enforce U.S. IP rights. However, we found that STOP's potential as a national strategy was limited because it did not fully address important characteristics of an effective strategy. For example, its performance measures lacked targets to assess how well the activities were being implemented. In addition, the strategy lacked a risk management framework and a discussion of current or future costs—important elements to effectively balance the threats from counterfeit products with the resources available. Although STOP identified organizational roles and responsibilities with respect to individual agencies' STOP activities, it did not specify who would provide oversight and accountability among the agencies carrying out the strategy.

While its impact will depend on its implementation, the PRO-IP Act of 2008 enacted several changes that address weaknesses we found in the prior coordinating structure. For example, the PRO-IP Act specifically requires the new interagency advisory committee to prepare a joint strategic plan that addresses key elements of an effective national strategic plan, building in mechanisms for accountability and oversight. Also, the PRO-IP Act requires the IPEC to submit the joint strategic plan to Committees of Congress every third year after the development of the first strategic plan.

⁶In December 2004, Congress augmented NIPLECC's capabilities in the Consolidated Appropriations Act of 2005. The act called for NIPLECC to (1) establish policies, objectives, and priorities concerning international IP protection and enforcement; (2) promulgate a strategy for protecting American IP overseas; and (3) coordinate and oversee implementation of the policies, objectives, and priorities and overall strategy for protecting American IP overseas by agencies with IP responsibilities. The act appropriated funds for NIPLECC's expenses. It also created the position of the Coordinator for International Intellectual Property Enforcement, also known as the "IP Coordinator," to head NIPLECC.

In contrast, STOP, a presidential initiative, has not been updated since September 2007, affirming doubts about its long-term viability. In addition, the PRO-IP Act places leadership in the Executive Office of the President—a status similar to that of STOP—in contrast with NIPLECC, whose leadership resided within the Department of Commerce. In September 2009, the administration announced that the IPEC would be located within the Office of Management and Budget. The PRO-IP Act repeals NIPLECC upon confirmation of the IPEC by the Senate. Currently, there is no IP Coordinator or NIPLECC staff. In addition, the most recent NIPLECC annual report was published in January 2008.⁶

Facing Significant Challenges Overseas, USPTO IP Attachés Have Adopted Practices to Enhance Collaboration

An additional theme of the PRO-IP Act is the emphasis on federal efforts to strengthen the capacity of foreign governments to protect and enforce IP rights. In September 2009, we reported that the USPTO IP attachés were generally effective in collaborating with other agencies at the four posts we visited, primarily by adopting practices, such as acting as effective focal points, establishing working groups and leveraging resources through joint activities.⁷ At one post, the IP attaché had worked with other agencies to develop a joint work plan for the post.

U.S. government officials in our three case study countries face a range of challenges in their efforts to promote the protection and enforcement of IP rights. The U.S. government has identified weak enforcement as a key IP issue in the three case study countries; however, weaknesses also persist in their IP laws and regulations. The U.S. government describes enforcement of existing IP laws and regulations and adjudication of suspected infringements as limited and inconsistent, and penalties are not typically sufficient to serve as an effective deterrent. Several factors contribute to this limited and inconsistent enforcement, including flawed enforcement procedures; a lack of technical skills and knowledge of IP among police, prosecutors, and judges; a lack of resources dedicated to IP enforcement efforts; and the absence of broad-based domestic support for strong IP enforcement.

⁶In fiscal year 2009, NIPLECC received an appropriation of \$1 million under the Department of Commerce USPTO budget. The Department of Commerce stated that no budget request was made for fiscal year 2010.

⁷See GAO-09-863.

We found that the USPTO IP attachés have adopted several practices that enhanced collaboration on federal IP efforts overseas, such as

- **Acting as effective focal points:** Agreement on agency roles and responsibilities of the IP attachés, particularly vis-à-vis the State economic section and post leadership, while challenging, was achieved in most posts. Prior to the creation of the IP attaché position at the four posts, State economic officers had primary responsibility for IP; now, they are the most involved in IP issues after the IP attachés. IP attachés also imparted their subject matter expertise, which enhanced their effectiveness as focal points. In addition, IP attachés have the advantage of working full time on IP, influencing agency officials at the posts to increase attention to IP issues despite other competing demands. Several agency officials from all four posts said that they had multiple responsibilities required by their broad portfolios, and some officials in some posts said they spent relatively little time on IP.
- **Establishing IP working groups:** The IP attachés played a key role in creating inter-agency IP working groups at the embassies in New Delhi and Beijing soon after their arrival. Several agency officials at these posts said that the working groups provided several benefits, such as increasing awareness of IP issues and trends, exchanging information on respective IP activities, and increasing coordination on training and other activities. The importance of the IP working group and the role of the attaché in Beijing was demonstrated when the working group became inactive after the attaché left the post in August 2008 and the position became vacant. Two agency officials at the post said that, without these meetings, there was less focus on IP at the post and that it was more difficult to ensure that the embassy spoke with one voice on IP.
- **Leveraging resources through joint activities:** The IP attachés complemented the efforts of other agencies to enhance IP protection and enforcement at all four posts by leveraging resources through joint IP activities. For example, the IP attachés helped the Department of Commerce's Foreign Commercial Service efforts to assist and encourage individuals to do business in the country by providing advice on how to avoid IP problems and answering IP-related questions.

Economic officers in two posts provided several examples of IP attachés' expertise enhancing the officers' relationship with host country officials. For instance, the economic officer in New Delhi said that the IP attaché had used his expertise to build rapport with the host government on IP issues and complement the economic officer's diplomacy with details on

potential solutions. A public affairs officer in Guangzhou said that the IP attaché had met with stakeholders such as academics, students, and industry groups on IP that provided the public affairs officer new contacts for his work.

- **Developing joint strategies:** The IP attaché in New Delhi led an effort to develop a joint strategy in the form of an interagency IP work plan. The plan established specific IP objectives and helped agencies at the working level identify and implement IP activities that address the key issues identified by the United States. For example, the work plan listed the implementation of an optical disk law and a meaningful system for protecting undisclosed data against unfair commercial use as key goals. In addition, the plan identified day-to-day activities, such as meetings that the post intended to hold with various Indian ministries, outreach it planned to perform with the private sector, IP training it planned to provide, and data it planned to collect to bolster the U.S. position on certain IP issues.⁸ In general, we found that other existing post-level guidance was too high-level and did not guide agencies' day-to-day efforts to reach IP goals.

Joint strategies can help agencies maintain focus on IP given numerous competing issues and periodic changes in key IP personnel at the posts. Some agency officials noted that the long-term nature of many IP efforts—such as implementing optical disk laws, developing public outreach to convince consumers of the importance of IP rights, or building the relationships with foreign law enforcement officials necessary to conduct joint IP investigations—require sustained and focused attention over time. In the absence of such sustained attention, the impacts of U.S. efforts can be diminished. For instance, one official noted that he had observed a cycle in which the post would exert pressure on the host country's police to more aggressively enforce IP laws, and enforcement would increase; however, after a time, pressure would ease and previous enforcement levels would return. In our 2009 report, we recommended that the Secretary of State direct post leadership to work with USPTO IP attachés in countries with such attachés to develop annual IP interagency post work plans with input from relevant agencies. The Department of State and USPTO agreed with our recommendation.

⁸As the plan had been in place for a relatively short period of time when we conducted our field work in New Delhi, in March 2009, the IP Working Group had not yet assessed progress that had been made.

While our observations on USPTO's IP attachés overseas are largely positive, our prior work has also demonstrated that the long-term success of operations abroad requires attention to human capital planning. In particular, we observed that other agencies attempting to establish a presence abroad had to make additional efforts to ensure that they could recruit and retain sufficient personnel with the technical and cultural expertise that is important in those posts. These considerations may be important as USPTO makes decisions about the scale and permanence of this program.

Concluding Observations

Madam Chairwoman, thank you for the opportunity to appear before the Committee to summarize our work on IP protection. GAO has performed a number of studies on both domestic and international efforts to protect IP since my last testimony on this subject before this Committee in 2004. As I have noted in my statement, we believe that the PRO-IP Act enacted last year has taken a number of positive steps to clarify the structure of IP agency coordination, and Congress has also tasked the coordinator to provide information we believe will be useful in oversight of U.S. agency efforts. Our most recent report also suggests that efforts such as those of the USPTO to place specialist attachés abroad has had a positive impact in the posts we visited because of their expertise and focus on this issue. Notwithstanding these positive developments, our work suggests that IP enforcement will continue to be a daunting task and that the U.S. agencies still need to demonstrate that they can collaborate effectively over the long term to help address these challenges.

GAO Contacts and Staff Acknowledgments

Should you have any questions about this testimony, please contact Loren Yager at (202) 512-4347, or yagerl@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Individuals who made key contributions to this statement include Christine Broderick (Assistant Director), Jeremy Latimer, Catherine Gelb, Nina Pfeiffer, and Ryan Vaughan.

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Ms. WATSON. Thank you so much, Mr. Yager.

We will now move to our question period and proceed under the 5-minute rule. Before that, I would like to welcome Congresswoman Carolyn Maloney to our committee. Thank you for coming and sitting in with us today.

I want to delve a little deeper into what is happening, Mr. McCoy, and particularly this week, in China. We know that the government is developing regulations regarding what are being called, as you mentioned, national indigenous innovation products. My understanding is that these regulations would, in essence, create preferences for Chinese vendors and eliminate U.S. information technology and intercommunication industries from China's government procurement and acquisition markets. This proposal obviously raises multiple issues surrounding compliance with international trade laws, as well as our bilateral agreements with the Chinese government.

Can you address how the Obama administration, including the USTR, has been proactive with this issue? It is very troubling to us, so let us know.

Mr. MCCOY. Madam Chairwoman, this is indeed a serious concern that you have identified, this indigenous innovation preference issue. Certainly it is in the interest of both the U.S. Government and the Chinese government to promote innovation. There are appropriate ways to do that, and there are inappropriate ways to do that. Let's be clear: innovation is no excuse for discrimination. We are very alert to these industry concerns about China's indigenous innovation policies in a wide range of areas, including the recent announcements out of China on a procurement preference list.

We are in the process of expressing our serious concerns. The inter-agency team in the U.S. Government has sprung into action. Ambassador Huntsman has received instructions and he and his team are in the process of raising our questions with all of the appropriate counterparts in the Chinese government. I can assure you we will stay fully engaged and continue to follow this closely.

Ms. WATSON. There has been mention that we have attaches and we have FBI and so on in our overseas embassies, and so I am really pleased to hear that you are working through the Ambassadors. I have been there, and we really need to have close scrutiny and interchange back with our administration as to how we are progressing.

The 2009 special 301 report that was mentioned highlighted the increased incidence of Internet piracy among U.S. trading partners. Some countries such as France and Britain have pursued legislation that would cutoff Internet access for users who repeatedly are caught engaging in integral peer-to-peer file sharing. Any of you that would like to address this particular question, please feel free to do so. Do you believe that this is a potential legislative remedy to our own significant peer-to-peer file sharing problem? We will start with you, Mr. Stoll.

Mr. STOLL. Thank you, Madam Chairman.

I am not sure that type of activity would be something that the United States would want to follow. I think that there is an intent to try to take care of the issues related to piracy in many manners, but I am not sure that removing access—I think in France it is a

three strikes you are out program. I am not sure that would be palatable here in the United States.

I think that taking many other actions to be able to reduce piracy in the United States is an important interest in all of the agencies represented here, but I am not sure that is the right direction to go in.

Ms. WATSON. Mr. Weinstein.

Mr. WEINSTEIN. I would agree with that, Madam Chairwoman. As a general matter, it is my view that the technology is not the problem, it is the way in which the technology is being used that creates the problem, and I think this is no exception.

In terms of criminal enforcement, we are increasingly concerned—we have been for some time and we continue to be concerned it—online piracy. It is perhaps the greatest emphasis of our computer crime and IP section. In pursuing online piracy, we work closely with industry, with the Motion Picture Association of America, with the Business Software Alliance, with the Entertainment Software Association to help identify emerging trends and to identify and prosecute the most serious online copyright thieves.

We have had great successes over the last few years and are continuing to prosecuting wares groups—that is, online organized groups that are engaging in piracy of software and music—focusing on the first suppliers, on the primary distributors of those materials online.

We have more recently engaged in fairly aggressive investigative operations against peer-to-peer networks, particularly those using BitTorrent software. We had an operation that we called the Elite, which resulted in eight convictions, including the first ever conviction at trial of a high-ranking administrator of a P2P Web site that was distributing massive amounts of infringing copyrighted works—software, video games, music, movies, the whole works—and who got a substantial sentence.

We are also trying to get the problem at the source. Oftentimes the multi-million dollar online piracy scheme begins with a camcorder, someone who is taping a movie, for example, in a movie theater, and so we have aggressively worked in partnership with the MPA and other interested partners to identify appropriate targets for camcording cases and recently convicted, late last year, convicted a gentleman named Michael Logan here in D.C. who was viewed as perhaps the most prolific camcorder on the east coast.

So we are trying to get to the problem at all ends, both once they are on an infringing site and even at the origin at the camcording level.

I would also say that since this problem is increasingly an international one, our international work engagement with foreign partners is increasingly important in this area, perhaps more than any other, and the IPLEC program that I mentioned is a key component of that strategy.

The fact that these sites are often posted on servers that are located overseas presents some investigative challenges, but they are challenges that we are working very closely with our foreign partners to overcome. The fact that a person commits this kind of crime from what he thinks is the privacy of an apartment or an office somewhere in eastern Europe, for example, or Asia is not the safe

haven that it used to be. We are working very hard with our foreign partners, not only to aggressively enforce criminal laws and to take down the organizations and individuals engaging in this conduct, but we are also working to increase their capacity so that we can reduce the number of safe haven countries throughout the world for people who engage in this kind of behavior.

Criminals, particularly criminal organizations, that engage in this type of online piracy, particularly from overseas or using overseas servers and other assets, should make no mistake about our resolve to find them and locate them and our increasing capacity to do that.

Ms. WATSON. Thank you. My time is up, so I would like to go to our most distinguished ranking member, Mr. Bilbray, for 5 minutes.

Mr. BILBRAY. Thank you, Madam Chair. I apologize for my tardiness, gentlemen.

Mr. Stoll, you said that the American people, you didn't think the American system had the stomach to do the three strikes like the British and the French. First of all, it kind of gets me nervous when we figure we don't have the intestinal fortitude of the French, but that's a different issue.

You want to elaborate on why we don't have the stomach for it?

Mr. STOLL. I am not sure I didn't—maybe I shouldn't have said don't have the stomach. I don't think that would be the direction we would go, because their access for informational purposes would be removed completely, as well. So we have a balancing act of interests here. I think there are many mechanisms where we are able to take care of the problem related to piracy, but I am not sure that it would probably be in the interests of our society to block access for other purposes of information exchange, education, of Internet access. So I think that's what I am trying to say.

I think that there are mechanisms that are in place. We work with MPAA, with RIAA. There are many different things to do. I am not sure just about blocking access would be something that we would want to do.

Mr. BILBRAY. I apologize. I am not as well versed as obviously I should be. When you say blocking access, are they talking about a national ban?

Mr. STOLL. Yes.

Mr. BILBRAY. The British are talking about a national ban?

Mr. STOLL. That's what my understanding is. I believe that is correct.

Mr. BILBRAY. OK. Gentlemen, let me be a little blunt. I think the perception out there—and I would ask you to either verify it or refute it—is that when it comes to intellectual piracy, China is the Somalia of the intellectual world. Is that fair to say?

Mr. YAGER. If I could just make a couple of comments on that, Ranking Member Bilbray, certainly China has some unique features that make it a special problem. One, it is an enormous exporter. It has the capability to export a wide range of goods and services, many of which have some level of intellectual property.

Second, China is also a major market. It has become an increasingly large market, not just for U.S. goods, but for goods from other places around the world.

So this is one of the few places around the world where you have both this enormous export capacity as well as a large internal market, so U.S. firms are understandably interested in serving that market, as well as gaining protection from the kinds of exports that China does produce, both shipping here as well as to third countries.

Mr. BILBRAY. So what you are telling me is China is at that critical location right along the major shipping lanes of intellectual property, which indicates that sounds a lot like Somalia to me.

Mr. YAGER. They certainly have a unique position. Whether it is in the south, the manufacturing center of the world, where they are able to produce in mass quantities and at relatively high quality, and using intellectual property in some cases that is not owned by those firms. It does have a unique position.

Mr. BILBRAY. Are you a diplomat? You sure sound like it. Go ahead, sir.

Mr. WEINSTEIN. I am not a diplomat, either, but I have never been accused of being a diplomat, but I do think it is worth pointing out, Congressman, that sometimes some of the countries that present the greatest challenges for IP crimes generally also are the most engaged in terms of trying to address their weaknesses, so it is certainly no—there really is no secret and there can't be any dispute that China is a source of a very large quantity of infringing goods, both hard goods and electronic goods.

But we have enjoyed a very productive and increasingly so working relationship with Chinese law enforcement, and I think the FBI and ICE and Chinese law enforcement officials, working with our prosecutors, have made great strides over the last few years. So at least from a law enforcement perspective I think China is working hard to try to address the challenges that even it identifies within its borders.

One of the areas in which I think we have been effective in other parts of Asia, particularly in southeast Asia and in eastern Europe through the IPLEC program that I mentioned, we have a prosecutor who works on a day-to-day basis not only to do joint operations with law enforcement in those countries or those regions where we have IP problems, but also to build their capacity to investigate and prosecute their own cases. That is a program that we very much would like to see expanded, and it is our long-term goal to expand, and China would be probably first on the list of places on the globe where we think more engagement, at least at the law enforcement level, would be productive for everyone.

Mr. BILBRAY. Well, China probably has the best capabilities of doing enforcement of anybody in the world. I mean, they probably have one of the tightest-knit enforcement capabilities that anybody has ever seen on the face of the earth, so their argument for not being able to crack down really is not germane to this issue.

The question that I have, though, is with at least the huge reputation of being the pirating capital, doesn't that give indications to other countries that, look, if you are big enough, if you are rich enough, if you intimidate the rest of the world you can get away with a lot of this, or maybe it is the other way that, Look what's going on in China. Why don't we try it in Monterrey, Mexico, or why don't we try it in Singapore. Well, Singapore is kind of a tight,

little community, so you might have that problem, too. But questions about how that gives a potential for other parts of the world to expand into the pirating aspect.

Mr. MCCOY. I could speak to that, Mr. Ranking Member, if I could. I think it is important to bear in mind that China, in addition to being the world's leading exporter of knock-off products, is also really suffering in terms of its domestic market the consequences of really decimating markets for software, music, films, and other IP-intensive products because of inadequate respect for IPR, so there is a lesson there to other trading partners, as well, not to go down this path, and we have seen in the Asia Pacific region and around the world other trading partners such as the Republic of Korea, such as Hong Kong, Taiwan, Singapore, take a different path and really look toward growing respect for IP rights as an important part of their economic growth story, and we would hope that other trading partners around the world follow that example.

Mr. BILBRAY. Thank you, Madam Chair. I would be very interested to know how they handle Windows 7, which was really a blatant piracy action that was going on in China.

Ms. WATSON. Thank you.

We will now proceed with questioning. Mr. Cuellar of Texas.

Mr. CUELLAR. Thank you very much, Madam Chair.

Mr. Weinstein, let me ask you, what are we doing to—let me start off with the Republic of Mexico, a big NAFTA country along with Canada. What are we doing to work with them internationally, because I saw your report where you talk about domestically and the coordination that we have here, but what are we doing to work with, let's say, the Republic of Mexico, because now, as in our drug cartels are now involved, the ones in Mexico are involved in—they are going into legitimate areas now, what we call legitimate businesses. I just want to see what we are doing to work with the Mexican government.

Mr. WEINSTEIN. Congressman, one of the things that we have been doing recently with Mexico is working with their officials at the border. One of the things that we do generally when we engage internationally—bilaterally, that is—is try to identify what the particular weakness is in the enforcement regime of particular countries, and it does vary by region and it certainly varies by country. Sometimes the problem is a lack of political will. Sometimes the problem is the political will is there but there is corruption. And sometimes it is a lack of coordination among agencies that would be responsible for various aspects of IP enforcement. Sometimes it is a combination of the three.

In Mexico, at least on the ports, in the ports, what we identified as a significant weakness was a lack of coordination among agencies that would be responsible for port security, and so one of the things that we did was work aggressively at three of the largest ports in Mexico, including Monterrey and Vera Cruz, to improve the level of coordination to teach the inspectors and the other people responsible for the security of the port how to do targeted inspections, how to identify potentially infringing goods.

In at least two of the ports, if I recall correctly, there had never been—or at least one of them, if not two—there had never been a

seizure of infringing goods prior to our training and our engagement with them, and in the period following that, the technical assistance we provided, there were seizures through the roof at those ports and those ports became much more effective at trying to identify infringing goods as they are moving across the border.

That is one area in which we have engaged in Mexico. It is not the only one, but it is one of the most prominent recently.

Mr. CUELLAR. When working with our domestic partners, and different law enforcement, I know that I have heard from the U.S. Chamber and other folks saying that we have so many threats to our country that when it comes to counterfeiting and this type of piracy that our resources are not put there. Is there anything else we can do to help our businesses, to protect them from this economic loss? Whoever else wants to add to that.

Mr. WEINSTEIN. I will jump in. I will lead off briefly and then turn it over to my colleagues.

One of the things that we have done with our partners at FBI and ICE to try to improve the level of coordination and to improve our ability to be responsive to IP stakeholders is to invest a lot of time and resources in the IP Rights Coordination Center, which is located in Crystal City. It is operated principally by ICE, but it has partnership from a number of different agencies, FBI and other law enforcement agencies that have some interest in IP enforcement.

It is intended to do a number of things. No. 1, it provides for a pooling of intelligence from all these different agencies so that they can share intelligence and share information and make their investigations more coordinated and more effective. It is also a deconfliction center, and it is also meant to be one-stop shopping for an industry. We had an industry meeting there on Monday, a lunch with representatives of 29 different IP stakeholder companies or organizations, and one of the things we emphasized to them is that not only can they make referrals directly to the Justice Department, but they can make referrals to the IP Rights Coordination Center. It is meant to be a place where they can share information themselves, they can make referrals, and they can get law enforcement to respond as quickly as possible.

Mr. CUELLAR. I appreciate that. I think that one-stop center so they know who to call instead of being bounced from one place to the other place, so I appreciate that. I appreciate the work that you all do.

Mr. Yager.

Mr. YAGER. Yes. One point I'd like to make. I think your question raises a very important issue, and that is in some cases what we find is these are criminal networks that operating, for example, on the border, so they may not just be involved in intellectual property crimes. There could also be money laundering, there could be illegal arms sales, there could be illegal drugs that are being traded by the same criminal networks. So I think it is important to focus not just on China but also look, for example, at the southern border to determine whether products are being brought in by those same criminal networks that are also taking advantage of the border to make other transactions, either guns moving south or illegal drugs moving north.

Mr. CUELLAR. Right. Again, from what we hear—I live in Laredo, a border town, and we hear that those criminal organizations are starting to look at different ways of making money, so we appreciate it, so whatever you all can do to protection it.

Last question for Mr. McCoy.

Mr. McCoy, our Ambassador Ron Kirk—I will close up with this—are we doing everything possible? I am a big supporter, was a big supporter of CAFTA, big supporter of Colombia, big supporter of Panama, South Korea, and hopefully we will have those agreements this coming year, but are we doing everything possible under those negotiations to make sure that we protect the intellectual property rights of our stakeholders?

Mr. MCCOY. I believe we are, Congressman. Ambassador Kirk has said repeatedly that ensuring strong IP protection is one of the top priorities for the President's trade agenda. It is something that we are working to move forward, both through the implementation of free trade agreements that are already out there, close monitoring and enforcement to make sure that those agreements are properly implemented, our trading partners deliver on their promises, going forward as we look toward new trade agreements, as we look to getting the trade agreements that are out there into force. We will continue that emphasis on proper implementation of IP provisions, and with efforts like the Anti-Counterfeiting Trade Agreement and the special 301 report we can continue to drive home that point.

Mr. CUELLAR. Thank you all. Thank you, Madam Chair.

Ms. WATSON. Thank you very much. You are welcome.

Ms. Chu of California.

Ms. CHU. Thank you, Madam Chair.

Well, this is for any of the panelists. The GAO has identified continued weakness in Global intellectual property protections and enforcement mechanisms, and specifically cites one challenge being the ineffective coordination of agency stakeholders charged with protection and enforcement responsibilities. From what I understand, there are eight agencies with overlapping protection and enforcement responsibilities, and from what I can tell there is not one single agency that leads the charge.

I know that there was legislation that created the Intellectual Property Enforcement Coordinator, and this is one step forward, but that person has not yet been put into place as of now.

What specific steps would you like to see the coordinator take in tackling these issues?

Mr. YAGER. Ms. Chu, I think there are three points that we would make.

We think that the legislation does address some of the prior weaknesses. I think a couple things that we would recommend is that the new group follows the guidance regarding the key elements of the national strategy so that the IP coordinator can create that strategy and ensure that all parts are working together. That would include not just the law enforcement but also the policy level working together.

The balance would also include working both at the firm level as well as at the industry and at the country level.

Finally, I think a point that was made earlier, to the extent possible utilize alliances with IP owners abroad, because in many cases the leverage that the United States has can be limited, but when you also team up with some of the IP owners abroad there could be greater success. So I think there are a couple of general points that we make in our prior statements about how this person or this new group could be effective.

Mr. MCCOY. Let me add from the perspective of USTR, Congresswoman, that I know that as of yesterday Victoria Espinel, the IP Enforcement Coordinator, has just started work. I know she was burning the midnight oil last night on her first day at work, because she talked with me a little bit about how we can work together, so at USTR we are looking very much forward to teaming with her.

We already work intensely with the other agencies here through inter-agency coordination of trade policy under the rubric of the trade policy staff committee mechanism that has been set out by Congress as a vehicle to coordinate, including on intellectual property trade policy.

So we work very closely with the other agencies of the U.S. Government, and we are looking forward to further enhancing that cooperative relationship under the guidance of the IP Enforcement Coordinator.

Ms. CHU. Very good. Then, Mr. Weinstein, the World Health Organization estimates that 50 percent of drugs worldwide are counterfeit, which translates into approximately \$38 billion in loss of legitimate U.S. corporate sales each year due to the sale of these counterfeit drugs. This statistic raises great concerns for me, because these are life-threatening type of issues, and there are huge ramifications to consumers who unknowingly purchase these counterfeit drugs and put themselves at risk.

What methods are the Department of Justice implementing to address this problem?

Mr. WEINSTEIN. Congresswoman, it is of great concern to us, as well, and one of the ways in which we have tried to use our limited resources, prosecutory resources, is to focus on intellectual property violations that are a threat to the public health and safety, and I can't think of one more serious than the one you just mentioned.

We have prosecuted a number of cases, going back several years now and continuing through the present, involving people who have produced counterfeit drugs of all types. Cancer drugs is the one case I mentioned in my oral statement. There are a number of others involving Viagra and other types of medications that are mentioned in my written testimony.

What is striking about these cases is that they are international in scope, just as the online piracy cases are. In fact, in November of last year a citizen of the Republic of the Philippines was charged here and was convicted and sentenced for participating in a conspiracy to import Viagra and Cialis, and I believe other types of medication, as well, and was the first person—he was extradited from Thailand. He was the first person ever extradited to the United States on a counterfeit pharmaceutical charge. We hope he will not be the last.

So in that area as well as the online piracy area we were talking about earlier we are not stopping at the borders and we are trying to find people who engage in this conduct, wherever they are, whether they are in China or here.

Speaking of China, one of the biggest cases involving counterfeit products—it is not a pharmaceutical, but it is a counterfeit product that affects health and safety—involved a national Guinea and a U.S. citizen in the Bronx who were conspiring to import counterfeit tubes of toothpaste from China that not only didn't contain fluoride, but also contained microorganisms and in some cases contained diethylene glycol, which is an ingredient in hydraulic and brake fluid. The co-conspirators brought in almost 83,000 tubes of this toothpaste, which had a retail value of just under \$117,000. And we managed to get the importers here in the United States, and they got significant sentences.

So this is an area that continues to be of concern to us. I would say, other than online piracy and counterfeiting that involves online auctionsites and direct sales sites, the public health and safety continues to be the area where we try to put our greatest emphasis.

Ms. CHU. Thank you. I see my time is up.

Ms. WATSON. Thank you.

We will now proceed to Mr. Connolly of Virginia.

Mr. CONNOLLY. Thank you, Madam Chairwoman.

Let me pick up, if I may, where Ms. Chu left off, Mr. Weinstein. We acknowledge that not only human pharmacological agents but veterinarian pharmacological agents are a problem, as well, coming into the United States. I know the Department of Justice was involved for many years in trying to prosecute folks who were wilfully violating our laws and introducing pirated antibiotics and other substances to Forest Grove into our livestock and feed chain here in the United States.

There are just lots of examples, intellectual property examples involving software, involving music and movies and all the technologies associated with them over the years. It wasn't that long ago you could go to Etawon and Seoul or you could go to neighborhoods in Taipei or Hong Kong and blatantly get knock-offs or infringed items at a discount.

If enforcement is everything it should be and the estimate is accurate that we are losing about a quarter of a billion dollars a year because of intellectual property infringements of one sort or another, the best estimate I have seen, in terms of border agent seizures of pirated materials, the value is something south of \$300 million. In other words, about 1 percent of the estimated cost of the total infringements.

Doesn't that suggest that, while you are not expecting everything to come through our borders, but 1 percent sounds pretty low in terms of our success rate at interdicting these materials or agents coming into our country?

Mr. WEINSTEIN. Congressman, I wasn't smart enough to check your math and I don't have figures myself on the amount of infringing goods, hard goods, that is, that are seized at the border, but I will tell you as a general matter, whether you are talking about goods coming in across borders or you are talking about

goods that are coming here electronically, the problem is far greater than the resources that law enforcement has available, either investigative or prosecutive resources, and I think the problem grows as more and more piracy is committed through online means.

I am an optimist by nature, but I am also particularly optimistic because I think the people who we have conducting these investigations, leading these prosecutions, are the best trained in the world and work very hard to keep pace with and, indeed, to be one step ahead of the people that we are investigating. And so I think that we have terrific people doing it; we just don't have enough of them. And the problem is of a magnitude that is far greater than our resources allow.

Having said that, I think that one of the things that demonstrates is the need for us to be able to turn ourselves into force multipliers, and that is to expand capacity overseas so that our overseas partners can engage in aggressive enforcement actions within their own borders.

I will give you just one example that I think is fairly illustrative. The IPLEC that I mentioned in eastern Europe—you are going to begin I am getting paid by every time I mention IPLEC—but our IPLEC in eastern Europe worked with law enforcement of the Ukraine, which was trying to take down a major piracy site that was operating in the Ukraine and they didn't know how to conduct an investigation of that type, and the IPLEC worked with them.

Their technology was quite outdated. They had an outdated personal computer and they had a dial-up Internet connection. And using an outdated personal computer with a dial-up Internet connection, following the guidance given to them by the one prosecutor we have over there, an investigator in the Ukraine took down the entire site.

So by engaging in trainings like that and in teaching people overseas how to make these cases, themselves, not only do we have bigger, splashier, more high-impact law enforcement operations here, but we can multiply the number of people who are able to be prosecuted in the countries in which they are operating.

Mr. CONNOLLY. Right. Thank you. That's helpful.

With respect to enforcement there are sort of two broad aspects to this. One has to do with capability on the ground, ours and our counterparts; the other has to do, though, with political will. I would like the panel to address that.

Candidly, we know that in some cases, including trading partners and allies of the United States, are not seized with this mission. How severe are we prepared to be, and historically how severe have we ever been in impressing upon an ally or a trading partner, or even somebody who is neither of those categories, that we mean business and we are prepared to exact a price if they don't, in fact, change their behavior from the top?

Mr. MCCOY. I can speak to that, Congressman. I think that we need to have a strategy that proceeds on two fronts. One is to be very frank and, when appropriate, very critical of our trading partners who don't step up to the challenge. And the other front is to work in tandem with our trading partners through leadership and partnership to really get at this problem better, because on the one hand we have to be honest enough to call it out when the problem

is bad; on the other hand, we cannot solve this global problem alone. We have to have international leadership and partnership and be working with our trading partners.

Sometimes we have to be capable of walking and chewing gum, of doing both of those things at the same time with the same trading partners.

There have certainly been occasions in the past when we have gone all the way to the extent of trade sanctions with trading partners who refuse to protect U.S. intellectual property. The most recent occasion was Ukraine. All of the tools of the trade arsenal are available to make progress where it is appropriate, and we are continuing to use all the tools at our disposal.

Mr. CONNOLLY. Madam Chairwoman, my time is up. By the way, I would ask for unanimous consent that my opening statement be entered into the record.

Ms. WATSON. Without objection.

Mr. CONNOLLY. I just want to observe before you call on Mr. Murphy that I thank Mr. McCoy for his answer.

Inferentially, one could conclude from your answer some criticism of past performance on our part in terms of our consistency in strict enforcement and so conveying to other countries in the international community.

Thank you.

Ms. WATSON. Thank you.

Mr. Murphy from Connecticut.

Mr. MURPHY. Thank you, Madam Chair.

I want to continue to pursue the line of questioning from Mr. Connolly and other members of the committee regarding our current approach to, I guess, supply side enforcement when it comes to pirated content on the Internet.

I was a little discouraged to hear your critique of demand side's restrictions, because I wonder about the efficacy of a strategy that effectively tries to play whack-a-mole around the world. We are talking about one guy with a computer that can move his computer, can move his location, can move the site of his hosting entity from city to city, from country to country. I guess I don't doubt your resolve, but as we look at the trend line over the last several years the amount of pirated content and the number of sites that are selling them are going in only one direction.

So I guess I will ask this: what tools do you need that you don't have now to try to pursue this supply side enforcement policy, and how worried should I or any of us be about the ability of the people who are perpetuating these sites to just simply move to a different place or to take up residence under a different business entity, given the fact that it is so easy to just put up a new site and take one down the minute that they sniff that law enforcement is on to them?

Mr. WEINSTEIN. First, Congressman, I am not suggesting that enforcement should only be supply side or demand side. I think that, given limited Federal resources, we can have the greatest impact by pursuing the supply side, by getting the people who doing exactly what you just described, who are actually the first providers of the online content that is then downloaded by people throughout the world.

You can get the person who is downloading it and making a few infringing copies, but you haven't actually made an impact unless you take down the person who is obtaining it, putting it online, and making it available.

To your question what do we need, I would say that the greatest investment of resources that we have made is in this IPLEC program, because with the cost of putting one prosecutor in a foreign region or foreign country, that person can have an impact on enforcement operations, both trans-national enforcement operations and enforcement operations in the countries and regions in which he is operating that go far beyond what that one prosecutor could do working on even a very full caseload here in the United States.

So it is not an inexpensive program by any means. The cost of putting a person and his family overseas for an extended period of time is not small, but we view it as a sound investment in our ability to have a greater impact on the enforcement side not only here but throughout the world.

In terms of how concerned you should be that someone has the capacity to basically pick up and move their operations, I would say there is reason to be concerned about it, but by no means are those methods of evading detection or evading capture foolproof; in fact, quite the contrary.

As we have improved our relationships with our foreign partners, as we have increased our ability to share evidence and to share intelligence and to share information more quickly than we ever have before, the person who picks up a server and moves it overseas or moves it from one country to another country overseas is much more vulnerable than he ever has been before. That is why Attorney General Holder—I said that this was a high priority for him. Attorney General Holder actually initiated the Department's first major IP initiative when he was the Deputy Attorney General back in 1999, and one of the principles of that initiative that we continue to build on today is the need to engage with our foreign partners so that we can not only have effective law enforcement against people who are operating in their countries, but so that they can be more effective in their own countries.

So I think that our determination to get people wherever they are and to find their servers and to find their assets, wherever they are in the world, has never been greater, and our capacity to do it has never been greater.

Mr. MURPHY. So let me ask this: how do I square that with data showing that the amount of pirated content is greater than ever? So how do I square your enforcement capacity being greater than ever with the amount of pirated content continuing to grow?

Mr. WEINSTEIN. Unfortunately, I don't think that they are inconsistent at all. I think, as I mentioned to Congressman Connolly, I think the problem is of a magnitude that is far greater than the resources that are currently available to address it. So we try to address it as intelligently and strategically as we can, both in terms of identifying what targets we should pursue in our own enforcement operations, and, as I said, in terms of trying to improve the ability of our international partners. But it is largely a resource problem.

I think the strategies we have are effective. I think the people we have doing it are outstanding. But there are not enough of them. So I think it is a resource issue.

Mr. MURPHY. Thank you, Madam Chair.

Ms. WATSON. Thank you so much.

Now we will call on our distinguished Member from California, Ms. Jackie Speier.

Ms. SPEIER. Thank you, Madam Chairman.

I guess this is a question for Mr. Weinstein. There is an alarming number of reported instances where information technology goods are counterfeited abroad to sell here in America. Can you speak in general terms of those nations that pose the greatest threat to our information technology vendor supply chain for counterfeiting and national security matters?

Mr. WEINSTEIN. Congresswoman, I don't think I can speak, even in the most general terms, to the countries that pose the greatest threat from a national security point of view, but I would be happy to discuss that with the folks in our national security division and get back to you with a more detailed answer after the hearing.

What I can say is that the regions that are the greatest concern to us right now I think are China, obviously, as we discussed earlier, South America, and parts of Africa. And we have tried to devote resources in terms of training and technical assistance to law enforcement in South Africa, for example, in Brazil, in India, and in other parts of southeast Asia, and again in China, to try to address that as practically as we can. But I think that the regions that we are the most concerned about in terms of not just online piracy but all types of policy would be South America and Africa and China.

And, as I mentioned earlier, I think those areas that present the greatest challenge often also present the greatest opportunity, and some of the law enforcement officials in those countries tend to be the ones who are the most fully engaged with us and are just as aware as we are of the extent to which the problem flows through or arises from the region that they are operating in. So the fact that there is a great deal of piracy that involves those countries is not in any way an indictment of the law enforcement officials in those countries' commitment to address it; in fact, oftentimes, as I said, those tend to be our most committed partners.

Ms. SPEIER. All right.

Mr. Yager, thank you for your work on the GAO reports, and I guess the ones that predated it that created the genesis of the new legislation. The one area that you keep coming back to is the area of just human capital and not necessarily committing enough human capital planning. I guess you are speaking of the operations abroad. Could you elaborate on that some more and tell us, if you haven't already, what more we need to do.

Mr. YAGER. GAO has done a number of reports, as you know, on human capital planning. We have done some for the State Department. More generally, we have done some for USAID. But in this context I think one of the things that we learned when we traveled last summer to visit some of the key locations where intellectual property crimes are rampant is that having someone in that post who is full-time on that job, full-time on IP, someone who under-

stood some of the technical issues related to intellectual property protection, even understanding some of the laws in those host countries, and having the ability to understand the culture, we thought that those three particular assets were extremely important.

And where you have that combination, we found, in our discussions with the private sector, that the private sector felt very well served, and they felt that the U.S. officials could be helpful to them in making contact, solving problems, in some cases before they became a serious problem, and in some cases solving problems after it got to the point where they needed to address it with the host government.

So we certainly found great support for some of the kinds of people that were put abroad recently by the Patent and Trademark Office, but I think one of the other points that we make—and I make this in my written statement—is that you need the ability to continue to send that set of people with those skills over there, and agencies that haven't long had a foreign presence may not be that deep in terms of having people with the cultural expertise as well as the technical expertise. So that's one of the cautions that we made in the report that we recently released.

Ms. SPEIER. So you looked at four different countries?

Mr. YAGER. That's right. We went to three countries, four posts. China, because of the importance of the Guangzhou area, has an IP attache in that consulate because it is such a larger producer of goods for the world.

Ms. SPEIER. So where else do we need to have individuals outposted that we don't presently?

Mr. YAGER. Of course, it depends on the size of the program. We know that some places in central Europe are a significant problem. We know that South America has some, I think what USTR calls notorious trading areas. There are certainly other places in southeast Asia where you could probably benefit from having additional personnel. But, again, if the personnel don't have that unusual combination of expertise, they will not be as effective as the people who were first put in those posts.

Ms. SPEIER. But it would seem to me—I see my time has expired—that should be a high priority for us if we are really going to address this issue long-term, so it might behoove us to identify those other countries and make sure that there are individuals with those skills outposted, if you could provide that to us and the committee.

Thank you, Madam Chair.

Ms. WATSON. Thank you so much.

I would like to thank this panel for your testimony. Now you will be excused so we can bring up the second panel. Thank you so very, very much.

We are now going to proceed to the second and final panel. We will try to get you out of here by noon, and so we have to watch our own timing, the committee, but now that we have narrowed down to just three of us, I think we can do that.

It is the policy of the Committee on Oversight and Government Reform to swear in all witnesses before they testify. I would like to ask all of you to please stand and raise your right hands.

[Witnesses sworn.]

Ms. WATSON. Let the record reflect that the witnesses answered in the affirmative.

I will now take a moment to introduce our prestigious and distinguished panelists.

I would first like to start with Mr. Dan Glickman, who serves as the chairman and CEO of the Motion Picture Association of America. Prior to becoming the leading voice for the motion picture industry, and some of my congressional district's most prominent employers, Mr. Glickman proudly served as a Member of Congress from the 4th congressional district of Kansas for 18 years, as well as the Secretary of Agriculture in the Clinton administration.

In addition to his current position with MPAA, he serves on the boards of the American Film Institute, the Chicago Mercantile Exchange, communities and schools, and the Center for U.S. Global Engagement. He is also a member of the Genocide Prevention Task Force, which is chaired by Secretaries Madeleine Albright and Bill Cohen, and a member of the Council on Foreign Relations, and a member of the Academy of Motion Pictures, Arts, and Sciences.

Mr. Robert W. Holleyman is the president and chief executive officer of the Business Software Alliance. He is widely known for his work on policy related issues affecting the technology industry, including intellectual property laws, cyber security, international trade, and electronic commerce. Before joining BSA, he spent 8 years serving as counsel in the U.S. Senate, and was an attorney with a leading law firm in Houston, TX.

Mr. Brian Toohey is the senior vice president for international affairs at the Pharmaceutical Research and Manufacturers of America [PHARMA]. And prior to joining PHARMA, Mr. Toohey served in multiple Government affairs roles in the medical device and telecommunications industry. Before entering the private sector, he served as both a desk officer and Deputy Director in the Equipment Officers of the U.S. Department of Commerce.

Finally, Mr. Frank Vargo is the vice president for international affairs at the National Association of Manufacturers. He serves as its lead lobbyist and spokesman on issues of trade, currency, and other issues related to global markets and access. And prior to joining them, Mr. Vargo had a three decade trade policy career at the U.S. Department of Commerce.

Without objection, before proceeding to testimony from our panelists, I would like to submit a statement for the record on behalf of the Coalition of Music Ministries representatives that include performing artists, publishers, song writers, composers, and record labels. What is telling to me from their testimony is how critical IPR protection and enforcement is to industry stakeholders across the entertainment spectrum, including independent artists and major recording studios, alike. I am proud to have the music industry as a major constituent in our California's 33rd Congressional District and welcome the many cultural and economic contributions they provide to our Nation.

As I travel abroad and introduce myself as representing Los Angeles, CA, and Culver City, and I get nice nods, but when I say Hollywood, big smiles. So our industry reaches every corner of the

globe and pretty much represents who we are. At least we try to put forth the movies that represent the true beliefs of America.

So I ask that each of the witnesses now give a brief summary of their testimony, and to keep this summary under 5 minutes in duration if possible. Your complete written statements will be included in the hearing record.

Mr. Glickman, I would like to start with you. Welcome.

STATEMENTS OF DAN GLICKMAN, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, MOTION PICTURE ASSOCIATION OF AMERICA, INC.; ROBERT W. HOLLEYMAN II, PRESIDENT AND CHIEF EXECUTIVE OFFICER, BUSINESS SOFTWARE ALLIANCE; BRIAN TOOHEY, SENIOR VICE PRESIDENT FOR INTERNATIONAL AFFAIRS, PHARMACEUTICAL RESEARCH AND MANUFACTURERS OF AMERICA; AND FRANK VARGO, VICE PRESIDENT, INTERNATIONAL ECONOMIC AFFAIRS, NATIONAL ASSOCIATION OF MANUFACTURERS

STATEMENT OF DAN GLICKMAN

Mr. GLICKMAN. Thank you, Madam Chairwoman. Thank you very much for your leadership on film and entertainment issues. It is a great honor for me, after spending 18 years in the House of Representatives, to come back here and to be in the greatest deliberative—

Ms. WATSON. Does it feel like home?

Mr. GLICKMAN. It feels like home, and also it makes me yearn to come back, although I have no intention of going down that road. But I would say that you all have the greatest jobs in the world, and you realize it more when you are out, in terms of the impact that you have on people's lives.

Ms. WATSON. Well, I understand you will be leaving soon. What are you going to pursue, if I can get into your private business?

Mr. GLICKMAN. We will talk privately about that afterward.

Ms. WATSON. All right.

Mr. GLICKMAN. And not for a while, so I will still be around.

First of all, let me say that the intellectual property industries represented by those of us here are so critically important to the country. In the case of motion pictures, directly and indirectly we employ about 2.5 million people in this country. We are one of the few industries that has a positive balance of payment surplus with every single country in the world we do business with.

The movies and television shows are produced in all 50 States now, employment in all 50 States. And if you talk about a symbol of America, entertainment is probably as profound and powerful symbol of everything to do with our great country. So this is a really important industry and important issue for us, as well. These jobs are good jobs, high-paying jobs, and important to the country, as well.

By the way, over half of our revenues are derived from outside the United States. So what happens in the rest of the world, these trade issues are life or death for us, because people do love our product.

So what are the things? I was listening to the work of the Government officials—and, by the way, they have done a very good job.

USTR, Justice, the other agencies here, I must say both in the Bush administration and in the Obama administration have picked up these issues and the importance of intellectual property right protection. They can always do more. We talk about that. I am going to talk about some additional suggestions.

The first thing is we now have a coordinator—and we talked about that—under the PRO-IP bill. We have an IP coordinator. This is very important. There is somebody that is accountable, that we can focus on, that we can go to, and can help lead and marshal resources and enforcement policy throughout the U.S. Government. The question now is to make sure that she and her organization realize the full potential of this position by funding its remaining elements in the PRO-IP bill, the agents, the enforcement authorities that are provided in that bill.

It is also important that the nomination for Deputy U.S. Trade Representative for IP be confirmed. Her name is Miriam Sapiro. She is a critical senior level official in the U.S. Inter-Agency Team. That position has not been confirmed yet. That's very important to get that done.

We have talked about the special 301 process. This is a critical tool which identifies deficiencies in foreign markets and served as the administration's overall road map. Just to give you some idea, I was over in Spain recently. Spain has very serious problems involving Internet piracy. President Obama met with the president of Spain, Mr. Zapatero, raised the issue of Internet piracy. Spain is on the special 301 list and is hot because of that government-to-government coordination and impact. It has highlighted their hopeful desire to fix some of the problems that we have here.

We have something called the general system of preferences [GSP], program, which is intended to offer trade benefits to developing countries, while at the same time protecting U.S. interests. However, too frequently there is a disconnect between special 301, which are the countries on our watch list, and trade preference programs, with some of the most egregious offenders of U.S. intellectual property rights receiving preferential access to the U.S. market, despite their longstanding failure to effectively protect U.S. creativity.

So in my view our foreign policy needs to be more coordinated and cohesive in this particular resolve. Linking special 301 and trade preference program eligibility would provide the United States a powerful enforcement tool.

We have a variety of trade agreements, free trade agreements. There are three pending right now: Columbia, Korea, and Panama. We want to work with you and your colleagues to see the three pending FTAs implemented so that we can benefit from the negotiated IPR obligations of our trading partners. They all involve IPR. In the case of Korea, there are very significant improvements in their enforcement of intellectual property as a result of these trade agreements, and it is something that we think is important to us.

While not a free trade agreement, the U.S. motion picture industry has a keen interest in the anti-counterfeiting trade agreement [ACTA], which is in particular dealing with issues of Internet pi-

racy. And I would echo the comments that have been made about having more IPR attaches overseas in our industries.

Above all, I guess my point in all of this is that this is a big, dynamic, important industry for America. It is very much a face of the soft power of America, our entertainment world. Having you all engaged in this, having an enforcement team and a trade team in our U.S. Government engaged in this, we can make real progress in dealing with what Mr. Bilbray calls the problems of China, which just keep going and going and going, although there is some hope for some improvement there. But the fact of the matter is we have made progress in other places in the world, and we appreciate your interest in this issue.

[The prepared statement of Mr. Glickman follows:]

Testimony of
Dan Glickman
Chairman and CEO
Motion Picture Association of America

Before the Subcommittee on Government Management, Organization, and Procurement
Committee on Oversight Reform
December 9, 2009

Mrs. Chairwoman, Members of the Committee, thank you for convening this hearing today and inviting me to participate.

No issue is as important to the member companies of the Motion Picture Association of America¹ than the protection of intellectual property. Intellectual property – the ideas and creativity behind every image on the screen – is the lifeblood of our industry. Intellectual property and its protection, both at home and overseas, is critical to our nation’s economic strength. The American film and television production industry – which is just one part of the overall American creative community – results in millions of jobs created each year in states all across this nation. Our industry is bolstered by over a hundred thousand small businesses, entrepreneurs and start-ups from nearly every state. Protecting intellectual property preserves these jobs, creates new production-related employment opportunities, and results in consumers having more choices in how they view entertainment.

The US motion picture and television industry is one of the few US industries that consistently generates, even in these difficult economic times, a positive balance of trade, bringing dollars back home and creating good high-paying jobs in the US. International

¹ The Motion Picture Association of America and its international counterpart, the Motion Picture Association (MPA) serve as the voice and advocate of the American motion picture, home video and television industries, domestically through the MPAA and internationally through the MPA. MPAA members are Paramount Pictures Corporation, Sony Pictures Entertainment Inc., Twentieth Century Fox Film Corporation, Universal City Studios LLP, Walt Disney Studios Motion Pictures, and Warner Bros. Entertainment Inc.

markets are vital to the continued success of our industry; over half of our members' revenues are derived from outside of the United States. These accomplishments have not come easily. Our industry faces the relentless challenge of the theft of its creative content, a challenge extracting an increasingly unbearable cost.

MPAA views coordination among the stakeholder agencies with IPR protection and enforcement responsibilities as critical to the effective enforcement of US intellectual property rights. This is why MPAA heartily supports the PRO-IP Act (Prioritizing Resources and Organization for Intellectual Property Act of 2007), which passed last fall with broad bipartisan support. This legislation recognizes the importance of intellectual property to our nation's economic future and, under the leadership of Victoria Espinel as this nation's first Intellectual Property Enforcement Coordinator, should improve interagency coordination. I've had the pleasure of working with Ms. Espinel. She is well-qualified and I am fully confident that she will provide the leadership necessary to harness US resources, both human and financial, to more efficiently and effectively protect intellectual property at home and abroad. It is now imperative that Congress works quickly to realize the full potential of PRO-IP by funding its remaining elements.

It is also important that Miriam Sapiro's nomination for Deputy US Trade Representative move forward expeditiously. The Deputy US Trade Representative is a critical senior level official in the US interagency team for protecting and enforcing US intellectual property rights abroad and her absence is a notable void in interagency process.

Annually, a broad interagency team considers foreign governments' protection of US intellectual property through the Special 301 process. This critical tool identifies deficiencies in foreign markets and serves as the Administration's overall roadmap for the overseas intellectual property rights agenda each year. We believe it should also guide our work with governments that benefit from our trade preference programs.

The Generalized System of Preference (GSP) program, along with several other trade preference programs, is intended to offer trade benefits to developing countries while at

the same time protecting US economic interests, notably the leverage to seek and secure improvements in IPR legislation and enforcement in beneficiary countries. In some instances, the threat of suspending GSP benefits has motivated recipient countries to take meaningful steps to improve IPR protection. Too frequently, however, there is a disconnect between Special 301 and trade preference programs with some of the most egregious offenders of US intellectual property rights receiving preferential access to the US market despite their long-standing failure to effectively protect US creativity. In my view, our foreign policy should be more cohesive.

Linking Special 301 and trade preference program eligibility would provide the US government a powerful enforcement tool. This could be achieved by requiring, as a condition for continuing to receive benefits, that GSP beneficiaries listed on the Special 301 Priority Watch List develop and implement an action plan, in cooperation with the U.S. government, to address the IPR deficiencies discussed in the 301 report. Throughout the process – from developing the action plan to its implementation – countries would be compelled to consider and address IPR deficiencies.

Another critical tool for improving intellectual property protection and enforcement overseas are trade agreements. The improvements in intellectual property rights enforcement that these agreements have required of our FTA partners are vital to our industry's continuing contribution to America's economic strength. All US FTAs call for protections that exceed the minimal requirements of the WTO's Trade Related Aspects of Intellectual Property Agreement (TRIPS) and USTR has continuously improved the level of protections in these agreements. We are eager to work with you and your colleagues to see the three pending FTAs implemented so that we can benefit from the negotiated IPR obligations of our trading partners. Without implementation, these agreements are simply a series of complex, unfulfilled promises.

While not a Free Trade Agreement, the US motion picture industry – producers, studios and guilds -- has a keen interest in the Anti-Counterfeiting Trade Agreement (ACTA), in particular the provisions to address Internet piracy. We firmly believe that for the ACTA

to address the enforcement challenges our industry confronts today, it MUST include robust protections for intellectual property online. Practical secondary liability regimes for online infringement are essential to motivate stakeholders to cooperate in implementing the reasonable practices that promote legitimate consumer options and make the online marketplace less hospitable for infringers. ACTA parties should refine their secondary liability regimes to reflect current realities and adopt modern, flexible systems where they do not exist.

In all of these efforts, diplomats at our embassies and consulates play a vital role in cultivating political will. To meet the challenges the American IP industries will face in the coming years, we need to expand the corps of intellectual property attachés serving in our embassies.

Having worked with some of the current and former IPR attachés, we can attest to their value in serving as a resource in combating piracy, serving as a focal point for embassy efforts with the host government, and providing advice and guidance on how we can best mobilize our efforts and marshal them in concert with other rights holders. I am sure that increasing the number of attachés and ensuring that they are posted to priority countries will strengthen our world-wide campaign to protect American movies from theft, as well as all US intellectual property.

Throughout my career, I have been engaged in political issues. The protection of intellectual property is different. It is not a partisan issue. Fundamentally, we are talking about advocating for the creative industries; protecting property rights; bolstering small and medium sized enterprises; and, supporting a driver of US global competitiveness and well-paying American jobs. The American creative community and the hard working men and women that produce the movies and television programs that are enjoyed the world over are second to none. The results of their efforts are worth protecting.

I am continually appreciative of your interest in seeking ways to improve the enforcement and protection of US intellectual rights and I look forward to answering any questions you might have for me.

Ms. WATSON. Thank you so much. I was just talking to staff. We are going to plan another hearing where we want you to describe just what plans have been laid out by this administration and the enforcement. That is so important. We were just talking about how we would line up the countries. I think China, No. 1. I mean, they are expert at stealing our intellectual property. Maybe Russia No. 2. And Nigeria, No. 3 in terms of technology.

So anyway, what we are going to do is hold a hearing, probably after the first of the year. I just want to let you know what our plans are.

Mr. Holleyman, you may proceed, please.

STATEMENT OF ROBERT W. HOLLEYMAN II

Mr. HOLLEYMAN. Madam Chairwoman, Mr. Bilbray, I thank you so much for holding this hearing today. The hearing is about protecting intellectual property rights in the global economy, but this hearing is also about jobs, it is about health care, it is about education, it is about the environment, and national economic security.

The software industry is helping to provide specific solutions to each of these national needs. The greatest value of what software is is what software does. I would like to offer for the record examples of several BSA member companies and the type of software that they are providing and developing here in the United States to help us meet these national needs.

Ms. WATSON. Without objection.

Mr. HOLLEYMAN. But we also face a challenge of our own. Theft of intellectual property, both in the United States and overseas, is robbing us of resources that we could invest in more innovative solutions. Let me give you a few facts about this industry.

It is a \$300 billion software and services industry, the largest copyright industry in the United States and globally. Sixty cents of every dollar spent on software worldwide inures to U.S.-based companies, and it is a source of American pride, with over 2 million direct workers and a \$36 billion trade surplus.

But all of these benefits are endangered by software theft. The compelling statistic for today is that software theft reached \$53 billion last year. Most software theft occurs when an otherwise legitimate business makes illegitimate copies of software for its use. When repeated millions of times by businesses and consumers throughout the world, this has a staggering cumulative effect.

Harms of software theft include lost jobs, industry, and tax revenues, but what has been missing from this equation is the way this distorts competition. A company that steals business software has an unfair competitive advantage over an enterprise that pays for it. Both get roughly equal productivity benefits from the software, but only one is bearing the legitimate cost.

Software piracy is a problem around the world. It is particularly acute in many of the fastest growing developing markets that have disproportionately high rates of piracy.

Let me talk about China. Wherever I travel in the United States and around the world, the place I am asked about most frequently is China. In China, only 20 percent of software is paid for. In comparison, in the United States 80 percent is paid for. That means that there are a whole host of Chinese enterprises that are enjoy-

ing an unfair advantage over their U.S. counterparts. This unfair advantage is exacerbated by the new industrial policies that threaten to shut out U.S. companies.

Madam Chairwoman, I want to thank you for your comments in your opening statement, for your questions to the Government witnesses today. Steps by the U.S. Government to ensure that providers of software and other innovative technologies can continue to have access to China as the fastest-growing market in the world are critical.

Companies in six critical sectors, from software, telecommunications, and high energy efficiency products were given a December 10th deadline to apply to get on a list of preferred products the Chinese government will buy. We believe that few, if any, U.S. companies will qualify unless they turn over their IP to a Chinese entity. This could amount to a potentially massive transfer of IP, jobs, and economic power.

Madam Chairwoman, that is a step that is not in our national interest or in the interest of U.S. companies.

China made this announcement just a few weeks ago. It violates a series of commitments. The administration is actively pushing back from this policy, and I urge you and the ranking member to strengthen their hand by expressing your own opposition to China's Ambassador here in Washington. This issue is important not just to the IT industry, but to a wide range of business and governmental interests in the United States and abroad. And, indeed, I could add that it is not even in China's own interest to exclude their ability to obtain the best products from the United States or elsewhere.

In closing, I would ask all of us to begin thinking about intellectual property theft in a different way. The problem is more pervasive, it is more complex, and it is more pernicious than it was just a few years ago.

Quite frankly, I think we need to think of another term other than the word piracy for this to talk about the breadth and scope of the problem. It has national implications, national economic implications.

Thank you for holding this very timely hearing.

[The prepared statement of Mr. Holleyman follows:]

**Testimony of Robert Holleyman
President and CEO
Business Software Alliance**

**Before the Subcommittee on Government Management, Organization, and
Procurement
House Committee on Oversight and Government Reform**

**Hearing on
Protecting Intellectual Property Rights in a Global Economy: Current
Trends and Future Challenges**

December 9, 2009

Good morning. My name is Robert Holleyman. I am the President and CEO of the Business Software Alliance.¹ BSA is an association of the world's leading software and hardware companies. BSA's members create approximately 90% of the office productivity software in use in the U.S. and around the world. We appreciate the opportunity to testify today on issues that are important to our member companies.

BSA commends you, Madam Chairwoman, and Ranking Member Bilbray for holding today's hearing. The theft of intellectual property, commonly known as "piracy," is a matter of great concern to the business software industry. Piracy costs the industry billions of dollars in lost revenues each year. It reduces investment in creativity and innovation. And it harms national economies including our own.

In my testimony, I will give a brief overview of the contributions that the business software industry has made and continues to make to the global economy and to describe how piracy has undermined those contributions. I will next describe the evolving challenges the software industry faces with respect to piracy and explain the steps industry is taking to address these challenges. Finally, I will summarize the lessons that we have learned regarding how best to end piracy both here at home and abroad, including certain steps the government can take to more effectively stem the tide of piracy.

¹ The Business Software Alliance (www.bsa.org) is the foremost organization dedicated to promoting a safe and legal digital world. BSA is the voice of the world's commercial software industry and its hardware partners before governments and in the international marketplace. Its members represent one of the fastest growing industries in the world. BSA programs foster technology innovation through education and policy initiatives that promote copyright protection, cyber security, trade and e-commerce. BSA members include Adobe, Apple, Autodesk, AVG, Bentley Systems, CA, Cadence, Cisco Systems, Corel, CyberLink, Dassault Systèmes SolidWorks Corporation, Dell, Embarcadero, HP, IBM, Intel, Intuit, McAfee, Microsoft, Minitab, Quark, Quest Software, Rosetta Stone, SAP, Siemens, Sybase, Symantec, Synopsys, and The MathWorks.

Software Industry Contributions and the Impact of Piracy

Information technology has changed the world in which we live. It has made us more efficient, more productive and more creative. IT delivers better results in dealing with national priorities such as health care, energy, infrastructure, education, and e-government. Software has been at the heart of this technology revolution. Software drives productivity and innovation in almost every economic sector, helping businesses of all sizes perform better in good times and bad. It makes our lives easier, more connected, and more fun at home.

The software industry has also proven to be a remarkable engine for jobs and economic growth. The software and related services sector employed 1.7 million people in the US in 2007 in jobs that, on average, paid 195% of the national average. This sector contributed more than \$261 billion to US GDP in 2007, making it the largest of the US copyright industries.

This sector has yet to reach its full economic potential. This is due, in large part, to piracy. Just as the software industry is the largest copyright sector, software piracy is the biggest component of the piracy problem that we share with the other copyright industries.

As of 2008, one in every five copies of software in use in *this* country, valued at more than \$9.1 billion, was stolen. Globally, 41 percent, or more than one out of every three copies of software in use – nearly \$53 billion worth – was stolen. There are few industries that could endure theft of its products at this level.

Pirates steal jobs and tax revenues as well as intellectual property. A study conducted for BSA by IDC last year found that lowering software piracy rates stimulates the entire IT sector, creating jobs and increasing economic growth and tax revenues. The study concluded that a global 10-point reduction in PC software piracy over four years would deliver an additional 600,000 new jobs, \$24 billion in tax revenues, and \$141 billion in economic growth. This is not an unattainable goal – China has reduced its piracy rate by ten points since 2004, and Russia has reduced its rate by twelve points since 2006.

Reducing piracy delivers indirect benefits as well. Society benefits from new technological innovations. Consumers benefit from more choices and greater competition. Internet users benefit from new ways of communication and expanded creative content made available online. And national economies benefit from enhanced productivity leading to higher standards of living.

Defining Software Piracy

“Software piracy” generally refers to the reproduction or distribution of copyrighted software programs without the consent of the copyright holder. Piracy of software can take a number of forms, but BSA focuses specifically on two particular types: organizational end-user piracy and Internet piracy.

Organizational end-user piracy

The business software industry's most harmful piracy problem traditionally has involved its primary users – large and small corporate, government and other enterprises – that pirate our members' products by making additional copies of software for their own internal usage without authorization. We commonly refer to this activity as "organizational end-user piracy."

Organizational end-user piracy occurs in many different ways. In what is perhaps the most typical example, a corporate entity will purchase one licensed copy of software, but will install the program on multiple computers. Other forms of end-user piracy include copying disks for installation and distribution, in violation of license terms; taking advantage of upgrade offers without having a legal copy of the version to be upgraded; acquiring academic or other restricted or non-retail software without a license for commercial use; and swapping disks in or outside the workplace. Client-server overuse – when too many employees on a network have access to or are using a central copy of a program at the same time, whether over a local area network (LAN) or via the Internet – is another common form of end-user piracy.

Organizational end-user piracy goes on in enterprises large and small, public and private. These enterprises receive the productivity benefits that the software provides, while foregoing the expense of licensed copies of the software. Not only do they steal from software producers, these enterprises enjoy an unfair commercial advantage over their law-abiding competitors who must make a choice between paying for software or doing without. This unfair commercial advantage operates at an international level as well: On average, enterprises in countries with high rates of software piracy are competing unfairly with enterprises from countries with low rates of software piracy.

In many cases, organizational end-user piracy is attributable to negligence and poor asset management practices. Enterprises can also be victimized by unscrupulous computer manufacturers and dealers who install copies of software onto the internal hard drive of the personal computers they sell without authorization from the copyright holder. In some cases, however, organizational end-user piracy is undertaken willfully, with management fully aware and supportive of the conduct.

Internet piracy

The Internet is an indispensable part of global communication and commerce. It has opened up opportunities for faster, more efficient and more cost-effective distribution of information, products and services across the globe. It has also opened up new forms of social interaction that render geography largely irrelevant. As technology innovators, BSA's members are at the forefront of these developments. Software and software functionality are not only sold and delivered over the Internet, but also comprise a key component of the Internet infrastructure.

Unfortunately, in addition to creating significant social and economic opportunities, the borderless and anonymous character of the Internet makes it an ideal forum to engage in a broad variety of unlawful conduct, including copyright piracy.

The scale of software piracy on the Internet is mind-boggling. In the first half of this year, BSA sent almost 2.4 million takedown notices related to P2P and BitTorrent filesharing. We also requested the removal of almost 103,000 torrent files from just nine of the largest BitTorrent index sites worldwide. These torrent files were being used by nearly 2.9 million individuals to download software with a retail value in excess of \$974 million. And this is only a part of the Internet piracy problem.

In addition to harming right holders, Internet piracy exposes computer users to serious risks. Globally, there is significant evidence to link software piracy with the frequency of malware attacks. This is not surprising, since those who use pirated, unlicensed software are typically unable to access or download essential patches and critical updates that ensure their systems remain as secure as possible. This makes them more susceptible to attack over the long term. Moreover, websites that offer access to pirated software often disseminate malware that infects visitors' computers.

Industry Efforts against Piracy

The Business Software Alliance and its individual members devote significant financial and human resources to preventing piracy worldwide. Our efforts are multi-faceted.

First, we are engaged in extensive educational efforts, designed to increase public understanding of the value of intellectual property and to improve overall awareness of copyright laws, on a global basis.

Second, we work closely with governments to encourage adoption of laws that strengthen copyright protection and promote an environment in which the software and IT industries can flourish.

Finally, where appropriate, BSA undertakes enforcement actions against those involved in the unlawful use, distribution or sale of its members' software. As I have already mentioned, BSA has an active notice-and-takedown program directed at various forms of Internet piracy. BSA also has an extensive program to combat corporate end-user piracy. All over the world BSA legal action on behalf of its members against corporate end-users who are using our members' products without authorization.

Technology plays a role in protecting intellectual property rights as well. These may include technological protection measures applied to copyrighted works, or other approaches such as the use of automated content detection and filtering technologies. BSA supports the voluntary development and use of such technologies. We do not, however, believe that government mandates are useful or appropriate. Technology develops most effectively in response to market forces; government mandates would stifle innovation and retard progress.

The Role of Government

Of course, the government also has an essential role to play. Domestically, the investigation and prosecution of IPR-related offenses, using the legal tools provided by Congress, is a vital complement to our own enforcement efforts. We look to the government to continue to expand its IP law enforcement activities here at home.

Internationally, the software industry looks to the U.S. government to persuade foreign governments to commit to protect and enforce intellectual property rights, and to ensure that these countries meet their commitments.

Domestic

Software piracy in the United States is a serious problem – make no mistake. Even though the piracy rate in the U.S. is the lowest in the world, because the market is so large piracy losses exceed \$9.1 billion annually.

Investigation and prosecution of copyright piracy is an essential part of the solution to this problem. BSA commends the Congress for enacting the PRO-IP Act last year. This law provides legal and organizational tools to combat piracy more effectively in the US. The PRO-IP Act also includes authorizing language for increased DOJ funding for IP enforcement activities. In total, the PRO-IP Act authorizes \$55 million per year for FY 2009-2013 for these purposes. We believe that Congress should fund the initiatives contained in Title IV of the PRO-IP Act fully.

Another key element of the PRO-IP Act was the creation of an IP Enforcement Coordinator (IPEC) within the Executive Office of the President to coordinate the development of a Joint Strategic Plan against counterfeiting and infringement, and to improve coordination and communication among the federal agencies involved in IPR protection and enforcement. We are pleased that President Obama has nominated Victoria Espinel, a highly-qualified candidate to hold this important post. It is our hope that, once confirmed as IPEC, Ms. Espinel can bring greater focus and renewed energy to the federal government's efforts to combat IP crime.

International

Intellectual property, including computer software, is a vital part of international trade. In 2007 the copyright industries generated more than \$125 billion in foreign sales and exports. The US-based software industry alone had a \$36 billion *positive* balance of trade in 2008.

Piracy is the most significant market access barrier faced by our industry in many countries around the world. This is certainly the case in emerging markets such as the BRIC countries (Brazil, Russia, India and China). In China, for example, the PC software piracy rate was 80% last year. Only one in five pieces of software that were put into use was acquired legitimately. This represents a \$6.7 billion loss for our industry.

Viewed in isolation, the piracy rates and losses in China and the other major emerging markets are sufficient cause for concern. But that's only part of the story. One of the facts of life for the software industry is that these markets are our future. PC sales in mature markets like the US, the EU and Japan are projected to grow by only 2% over the next three years. In the BRIC countries, by contrast, PC sales are expected to grow by 43% over the same time frame. PC sales drive PC software sales, so it is to these countries that we look for a growing software market. But only if we can make significant reductions in piracy rates that are running well in excess of 50% in each of them.

The nexus between IP and trade has provided one of the principal levers for moving foreign governments into compliance with international norms for protection and enforcement of IP rights. The U.S. government has had great success in using a variety of tools at its disposal for achieving this goal – principally the negotiation of strong IP provisions in free trade agreements, enforcement of the TRIPs Agreement through WTO dispute settlement procedures, the Special 301 program, and administration of trade preference programs such as GSP. BSA applauds the efforts of the small but dedicated professional staff at USTR, supported by the Departments of State, Commerce and Justice, the USPTO and the US Copyright Office, who have made these trade tools work for the benefit of the US copyright industries.

Nevertheless, there is much still to be done. The US government must continue to use these tools to secure improvements to IPR protection and enforcement overseas. Moreover there is important unfinished business remaining from the last Administration. Three free trade agreements have been concluded with our trading partners, but have not been submitted to Congress for approval. These agreements with South Korea, Colombia and Panama have languished long enough. They should be approved.

Another important piece of unfinished business is the Anti-Counterfeiting Trade Agreement (ACTA). The US and a small group of like-minded governments (Australia, Canada, the European Commission, Japan, Mexico, Morocco, New Zealand, Singapore, South Korea, and Switzerland) launched negotiation of this IPR enforcement-oriented agreement just over two years ago. This June, Ambassador Kirk announced that the Obama Administration would support a resumption of ACTA negotiations, and negotiators have met on several occasions since then. We view this as a very positive sign. BSA fully supports conclusion of a strong ACTA that provides an important framework for international IP enforcement standards building on existing IPR rules. We believe that the US can and should negotiate a strong international agreement that is fully consistent with US law.

Conclusion

Software contributes profoundly to the world in which we live. It allows us to share, to create and to innovate in ways previously unimaginable. Software-driven productivity strengthens national economies, including our own, and makes them more competitive and more prosperous. Unfortunately, piracy prevents the software industry from realizing its full potential. We urge the U.S. Government and other governments worldwide to help us solve this problem. We thank you for the efforts made to date.

Thank you again for the opportunity to testify here today. I look forward to your questions and to continued dialogue on this important topic in the future.

Ms. WATSON. Thank you, Mr. Holleyman.
Mr. Toohey, you can proceed.

STATEMENT OF BRIAN TOOHEY

Mr. TOOHEY. Thank you, Madam Chairwoman, thank you, Mr. Billbray, for the opportunity to be here this morning.

First let me just say I absolutely agree with Secretary Glickman's and Mr. Holleyman's statements about the importance of IP intensive industries. According to the Commerce Department, currently driving over 50 percent of our exports and 40 percent of our growth here in the United States. Very important economic industries.

PHARMA's member companies are innovators devoted to developing medicines that allow patients to live longer, healthier, and more productive lives. PHARMA's membership ranges in size from small startup research firms to corporations that employ tens of thousands of Americans and encompass both pharmaceutical and biotechnology companies.

The research-based pharmaceutical sector is one of the most knowledge-intensive enterprises of the U.S. economy. In 2008, our sector invested over \$65 billion in research and development, and of that amount about 70 percent was invested here in the United States. The pharmaceutical industry supports more than 3 million jobs and directly employs nearly 700,000 Americans.

To foster continued economic growth and deliver breakthroughs, our sector relies on policies that promote and protect pharmaceutical innovation, especially complementary protections of patents and data protections.

Our companies face significant challenges to the discovery, development, and commercialization of new medicines. Adequate protection of intellectual property, both within and outside the United States, is essential for continued advances against challenging and costly diseases. In addition, access to international markets is critical to ensuring that these products reach as many patients as possible.

In that regard, PHARMA members especially appreciate the continuing strong efforts of USTR, State, Commerce, and PTO to promote compliance with international obligations by our trading partners.

PHARMA member companies also undertake significant research, both privately and through public/private partnerships, to develop medicines that disproportionately affect poor countries.

In addition to research in this area, in recent years our industry has donated more than \$9 billion to access the medicines programs, more than the entire foreign aid budget of countries like Canada or the Netherlands, and provided enough health interventions to help 1.7 billion people in the developing world.

Currently, nearly 3,000 medicines are under development, including 300 medicines for rare diseases, 750 for cancers, and 109 to fight HIV/AIDS. A recent Tufts study estimated that the cost of developing a new medicine at over \$1.2 billion a year, and for every approximately 10,000 compounds that enter the R&D pipeline, eventually only one comes to market, and can take as long as 15 years.

Two complementary legal mechanisms, in particular, provide periods of exclusive marketing for new therapies. These mechanisms are essential to attract investment needed to fund the R&D process. First, patents protect inventions made in the course of research and development by giving the innovator the right to prevent the unauthorized use of inventions for a defined period of time. Second, data protection has proven essential. Clinical data represents the investment in conducting the rigorous, lengthy pre-clinical and clinical studies that the FDA requires.

One of our concessions made by the United States in the TRIPS agreement was to provide developing countries with a number of extended transition periods to implement new standards. As of 2005, all but the least-developed countries were required to comply with provisions of TRIPS. Many of these trading partners have benefited tremendously from the openness of our market and the industries that aggressively compete with our own. Yet even now many of these countries have not fully met their TRIPS obligations to provide effective IP protection.

Another important area of concern which was discussed earlier is counterfeit drugs. Weak regulatory and IP enforcement regimes in some countries contribute to this problem, which increase health risks to patients.

In addition to the failure to meet IP obligations, many countries erect barriers to reduce the access of our products. Clearly, these restrictions adversely affect the health of patients in their countries, while they also have potential negative effects on the United States and consumers worldwide.

We believe it is critical for the U.S. Government to take action against measures that prevent fair and equitable market access for our products. PHARMA members believe the special 301 process is a particularly useful trade tool through which these barriers and priority markets can be removed. In addition to special 301, the administration should use all available trade tools, including bilateral and multilateral trade negotiations, to pursue a positive agenda on pharmaceutical trade.

For example, the U.S.-Korea Free Trade Agreement or negotiations included provisions on pharmaceuticals and specific steps to improve the transparency and accountability of the pricing and reimbursement listing process. We urge the administration to build on this success and include similar provisions and agreements with future trading partners.

Thank you again for the opportunity to speak with you today. PHARMA and its member companies believe it is crucial for this subcommittee and the Government, as a whole, to foster incentives for innovation both United States and abroad.

Thank you very much.

[The prepared statement of Mr. Toohey follows:]

Prepared Statement of Brian C. Toohey
Senior Vice President, International Affairs
Pharmaceutical Research and Manufacturers of America

Hearing on "Protecting Intellectual Property Rights in a Global Economy: Current
Trends and Future Challenges"

Before the U.S. House of Representatives Subcommittee on Government
Management, Organization, and Procurement, Committee on Oversight and
Government Reform

December 9, 2009

Chairman Watson, Ranking Member Bilbray, and Members of the Subcommittee:
Good morning.

My name is Brian Toohey and I am the Senior Vice President, International Affairs, of the Pharmaceutical Research and Manufacturers of America (PhRMA). PhRMA's member companies are leading research-based pharmaceutical innovators devoted to developing medicines that allow patients to live longer, healthier, and more productive lives. PhRMA's membership ranges in size from small start-up research firms to multi-national, multi-billion dollar corporations that employ tens of thousands of Americans, and encompass both research-based pharmaceutical and biotechnology companies. The research-based pharmaceutical sector is one of the most knowledge-intensive enterprises in the U.S. economy, and is responsible for 80% of the world's global healthcare biotechnology R&D.¹ In 2008, the pharmaceutical sector invested \$65.2 billion in R&D. The vast majority of their R&D investment —\$50.3 billion —was invested by PhRMA's member companies – an increase of over \$2 billion from 2007. Of that amount, roughly 70%, or \$38 billion, was invested in the U.S.

This sector supports high-quality jobs in the U.S. economy, investing almost ten times more per employee in research and development (R&D) than other manufacturing industries.² A 2006 Congressional Budget Office analysis reported: "The pharmaceutical industry is one of the most research intensive industries in the United States."³ This sector is also the source of high-quality, high-value jobs and economic growth. Analyses showed that the industry supported more than 3 million jobs, and directly employed more than 686,000

¹ Burrill and Company, analysis based on publicly available data, 2009.

² R. Shapiro and N. Pham, *Economic Effects of Intellectual Property-Intensive Manufacturing in the United States*, 2007.

³ Congressional Budget Office, "Research and Development in the Pharmaceutical Industry," October 2006.

Americans in 2006.⁴ The pharmaceutical industry's direct contribution to GDP in 2006 was \$88.5 billion – more than triple the average contribution of other sectors.⁵ As a result, many U.S. states actively compete to attract the pharmaceutical sector. As just one example, North Carolina, the first state to specifically target this sector for economic development, is home to a vibrant and growing pharmaceutical sector that has created more than 118,000 jobs in the state.⁶ The state's governor cited the biotechnology industry “as an essential economic engine that can benefit all North Carolinians.”⁷ These figures highlight the critical importance of the work of U.S. trade negotiators to open foreign markets, encourage the adoption of policies that do not discriminate against foreign-based companies, and promote innovation in the global trading regime. High technology industries such as the innovative pharmaceutical industry are the engine of U.S. growth, and it is more critical than ever that the United States takes a strong stand in favor of the open trading rules that will allow such growth to continue.

To foster continued economic growth and deliver the breakthroughs that will save lives and lower health care costs, our sector relies on public policies that promote and protect pharmaceutical innovation. Patents and data protection are the two mechanisms that have proven essential to allow pharmaceutical companies and their investors to realize the benefits of their significant investments. These complementary mechanisms not only stimulate the early-stage discovery and development of new medicines, but also safeguard the sector's ability to carry out the clinical investigations that are essential for ensuring that those medicines are safe and effective.

⁴ Archstone. *The Biopharmaceutical Sector's Impact on the U.S. Economy: Analysis at the National, State, and Local Levels*. Washington, DC: Archstone Consulting, 2009.

⁵ Archstone. *The Biopharmaceutical Sector's Impact on the U.S. Economy: Analysis at the National, State, and Local Levels*. Washington, DC: Archstone Consulting, 2009.

⁶ Archstone. *The Biopharmaceutical Sector's Impact on the U.S. Economy: Analysis at the National, State, and Local Levels*. Washington, DC: Archstone Consulting, 2009.

⁷ Governor of North Carolina. *New Jobs Across North Carolina: A Strategic Plan for Growing the Economy Through Biotechnology*, 2008.

This sector faces significant challenges to the discovery, development, testing, production, and ability to commercialize new medical treatments. Adequate protection of intellectual property – both within and outside the United States – is an essential economic prerequisite for continued medical advances against the most challenging and costly diseases. In addition, ensuring market access is critical to ensuring that these innovative pharmaceutical products reach as many patients as possible. Unfortunately, in some countries, significant market access barriers undermine the effectiveness and viability of intellectual property protection, and function to limit patient access to innovative products, distort trade, and, ultimately, discourage innovation, both in the United States and around the world.

Bringing new life-saving and life-improving products to people is the central role of our member companies. Because intellectual property is critical to carrying out this mission, PhRMA members particularly appreciate the continuing efforts of the Office of the United States Trade Representative (USTR), the Department of State, and the Department of Commerce, including the U.S. Patent and Trademark Office, to promote compliance with international obligations by this country's trading partners.

Today, I'd like to talk briefly about some of the medical advances from this sector that would not be possible without intellectual property protection. I would also like to talk about the major issues with respect to intellectual property protection for innovative pharmaceuticals abroad. These include inadequate patent protection and enforcement, patent linkage, inappropriate usage of compulsory licenses, and lack of proper data protection.

I. Intellectual Property Rights Are Essential To Pharmaceutical Innovation

Few advances in the last century have been as important to the preservation and enhancement of life as pharmaceutical innovations. According to University of Chicago economists, "[o]ver the last half century, improvements

in health have been as valuable as all other sources of economic growth combined.”⁸ New medicines have significantly reduced the socioeconomic burden of disease in the U.S. and around the world. Examples of the impact of medical advances include:

- Cancer. Since 1980, the life expectancy for cancer patients has increased by about 3 years. It is estimated that new medicines account for 50-60% of the increases in survival rates since 1975.⁹
- Cardiovascular Disease. Death rates for cardiovascular disease fell a dramatic 26.4% between 1999 and 2005, according to a recent report by the American Heart Association.¹⁰
- HIV/AIDS. Since the approval of highly active anti-retroviral treatments in 1995 the annual number of AIDS deaths has dropped by over 70%. Today, patients have a range of treatment options, including different combinations of drugs that often keep them symptom-free for years. Hospitalizations have also decreased between 1996 and 2000 with increasing use of anti-retroviral medicines, despite increases in the number of people infected with HIV/AIDS.¹¹
- Alzheimer’s Disease. Patients taking cholinesterase inhibitors were 2.5 times more likely to progress slowly after two years compared to untreated

⁸ Kenin Murphy, Ph.D., and Robert Topel, Ph.D., *Measuring the Gains from Medical Research: An Economic Approach* (Chicago: The University of Chicago Press, 2003).

⁹ F. Lichtenberg, “The Expanding Pharmaceutical Arsenal in the War on Cancer,” NBER Working Paper 10328, February, 2004.

¹⁰ W. Dunham, “Progress Seen in Heart Disease, Stroke Deaths, However, Obesity Epidemic May Offset Decline in Deaths this Decade,” *Reuters*, 15 December 2008.

¹¹ CDC, National Center for Health Statistics, *Health, United States, 2006 With Chartbook on Trends in the Health of Americans*, 2006.

patients, and after five years they were only 1/5 as likely to be placed in a nursing home.¹²

PhRMA's member companies also undertake research, both privately and through public-private partnerships, to develop or improve medicines for diseases that disproportionately affect poor countries. In 2007, the pharmaceutical sector was the third largest source of global R&D investment in neglected diseases after the National Institutes of Health and the Bill and Melinda Gates Foundation.¹³

These pharmaceutical advances — driven by scientific research and creative genius — would have been impossible without a system of laws that provides the structure, stability, and opportunity for the needed investment.

As mentioned earlier, the U.S. pharmaceutical sector is responsible for 80% of the world's R&D in health care biotechnology, and more than 2,900 compounds were in development or seeking regulatory approval in the U.S. in 2009.¹⁴ The compounds in development include 300 potential medicines for rare diseases such as chronic sarcoidosis (an immune system disorder), Lennox-Gastaut syndrome (a severe form of epilepsy) and cystic fibrosis; 750 potential treatments for cancers, particularly lung cancer and breast cancer; 277 new approaches for heart disease and stroke; and 109 new treatments to fight and prevent HIV/AIDS.¹⁵

¹² O.L. Lopez et al., "Alteration of a Clinically Meaningful Outcome in the Natural History of Alzheimer's Disease by Cholinesterase Inhibition," *Journal of the American Geriatric Society*, 2005.

¹³ The George Institute. G-FINDER: Global Funding of Innovation for Neglected Diseases. 2008.

¹⁴ PhRMA. PhRMA Annual Member Survey, Washington, DC, 2009; Adis R&D Insight Database, Wolters Kluwer Health, accessed 13 February 2009. Burrill and Company analysis based on publicly available data, 2009.

¹⁵ Pharmaceutical Research and Manufacturers of America, "Medicines in Development for HIV/AIDS," December 2008, <http://www.phrma.org/files/New%20Meds%20for%20HIV-AIDS%20report.pdf> (accessed 12 January 2009).

In addition, researchers in the innovative pharmaceutical industry are taking full advantage of new insights in genomics (the study of collections of genes and their role in the body and disease), proteomics (the study of the structure and function of proteins), and biomarkers (molecular, biological or physical characteristics that can help identify risk for disease, make a diagnosis, or guide treatment) to develop new treatments and make the most effective use of existing treatments. As just one example, biomarker research has allowed scientists to map proteins in tumors at the sub-cellular level, an important step in the development of personalized and more effective cancer treatments.

Like innovators across the spectrum of American industries, pharmaceutical companies rely on patents to protect their inventions and provide the opportunity to recover their research investments. But patents are particularly important to pharmaceutical innovation given the research-intensive nature of this sector and the substantial investment required to discover and develop products that meet FDA approval requirements. Without patent protection, potential investors would see little prospect of a sufficient return on investment to offset the accompanying financial risk.¹⁶ It is estimated that without patent protection, 65 percent of pharmaceutical products would never have been brought to market, while the average across all other industries was a mere 8 percent.¹⁷ It is well-established that patents are significantly more important for pharmaceutical firms than for other sectors of industry, in part due to the very high costs and lengthy time required to develop and bring to market new pharmaceutical products.¹⁸

¹⁶ Barfield, C., and Calfee, J. *Biotechnology and the Patent System: Balancing Innovation and Property Rights*. AEI Press, 2007.

¹⁷ Edwin Mansfield, *Patents and Innovation: An Empirical Study*, *Management Science* (February 1986) at 173-181.

¹⁸ Henry Grabowski, *Patents, Innovation and Access to New Pharmaceuticals*, 5 *JOURNAL OF INT'L ECONOMIC LAW* 849-60 (2002).

Several trends underscore the tremendous costs and, importantly, the commercial uncertainty associated with innovation in the pharmaceutical sector that drive the need for effective intellectual property protection:

- In 1960, the average time to develop a new medicine was approximately eight years. By 2007, that figure had increased to between 10 and 15 years.¹⁹ At the same time, costs to bring new discoveries from laboratory to bedside have increased dramatically. A recent study from the Tufts University Center for the Study of Drug Development estimates the average cost of developing a new medicine (including the cost of capital) at more than \$1.2 billion, in 2005 dollars.²⁰
- A typical commercial product results from making and screening *thousands* of promising, but ultimately failed molecules – products that never make it to market. For every 5,000-10,000 compounds that enter the R&D pipeline, only 250 reach the pre-clinical stage, and of those, only five progress to clinical study in humans, and only one receives regulatory approval.²¹ The following figure illustrates this challenging path.
- Clinical trials have become more complex and more costly to perform. Clinical trials today are longer, have more participants (who are difficult to recruit and retain), and involve more demanding and complex trial design and clinical protocols, including more procedures per patient and difficult-to-measure clinical endpoints.²²

¹⁹ *Id.*; Joseph A. DiMasi, *New Drug Development in the U.S. 1963-1999*, 69 *Clinical Pharmacology & Therapeutics* 286, 292 (2001).

²⁰ J. DiMasi and H. Grabowski, "The Cost of Biopharmaceutical R&D: Is Biotech Different?," *Managerial and Decision Economics*, 2007.

²¹ PhRMA, *Drug Discovery and Development: Understanding the R&D Process* (2007), available at http://www.innovation.org/drug_discovery/objects/pdf/RD_Brochure.pdf.

²² Tufts Center for the Study of Drug Development, "Growing Protocol Design Complexity Stresses Investigators, Volunteers," *Impact Report*, 2008.

- The regulatory environment for pharmaceutical products has grown increasingly complex over the past decade. Significant new requirements are continually introduced. For example, two years ago, enhanced post-market surveillance requirements were enacted,²³ in turn increasing the capital investment necessary to launch many products.
- Increasingly, pharmaceutical innovators face the challenges of developing therapies for some of the most complex diseases for which there are currently no effective treatments.²⁴

In light of these complexities, it is not surprising that only two in 10 approved medicines ever produce revenues sufficient to recoup the average cost of drug development.²⁵

As the factors discussed above illustrate, research and development for new pharmaceuticals is unpredictable, requires immense investments of human and financial capital, and can take up to 15 years of effort before a product is actually approved. Yet, once a pharmaceutical product has been developed, often it can easily be copied and produced.

Because the costs and technical challenges required to copy new drug products are trivial compared to the resources required to develop them, legal mechanisms have proven necessary to sustain a competitive market for innovation in the pharmaceutical sector. These mechanisms defer the time after which a new pharmaceutical product is introduced into the marketplace that a copy of the pharmaceutical product can be made and sold. These mechanisms, which provide a limited period of exclusivity in the marketplace for innovators, allow innovator companies the opportunity to make a return on their substantial

²³ See generally Food and Drug Administration Amendments Act of 2007, Pub. L. No. 110-85.

²⁴ Tufts University Center for the Study of Drug Development, *Growing Protocol Design Complexity Stresses Investigators, Volunteers*, Tufts Impact Report (Jan./Feb. 2008), available at http://csdd.tufts.edu/_documents/www/Doc_309_65_893.pdf.

²⁵ Vernon, J., Golec, JH., and DiMasi, J. Health Economics Letters: Drug Development Costs When Financial Risk Is Measured Using The Fama-French Three-Factor Model. Health Economics; June 2009. www.interscience.wiley.com.

investments (which in turn fosters future R&D investment) and provide legal certainty for all concerned.

Two complementary legal mechanisms in particular provide for periods of exclusive marketing of new therapies. These mechanisms are essential to attract the investment needed to fund the long, uncertain, and costly drug development process. First, patents protect inventions made in the course of research and development of a new medicine by giving the innovator the right to prevent the unauthorized use of the inventions for a defined term. The rights conveyed by a patent correspond to the invention – for example, a new drug molecule, a particular drug delivery system, new uses of a drug to treat different diseases, or a way the drug can be made. Thus, for example, depending on the nature of the patented invention, a patent may have a limited capacity to prevent the unauthorized copying of a new drug product. A patent provides proportionate, but not necessarily absolute, protection against copying.

Second, data protection (also known as data exclusivity), has proven essential. Data protection functions by deferring the date on which a generic pharmaceutical manufacturer can rely on the clinical data produced by the innovator to support approval of a new medicine. Such data often represents the investment of more than a billion dollars in conducting the rigorous and lengthy preclinical and clinical testing that FDA requires – and which is indeed essential to establishing whether a new pharmaceutical in fact is a safe and effective therapy for patients.^(add cite for this) Generic drug applicants do not perform and submit full clinical trials on their products, but rather must only demonstrate that their drug is the same and that it is bioequivalent (that is, it is absorbed to the same rate and extent as the innovator in healthy volunteers) to the innovative drug. The generic drug applicant relies on the innovator's data as the basis that its product is safe and effective. Data protection prevents the unfair commercial use of clinical data that would result if a generic manufacturer were entitled to rely on the data as soon as a new product was approved. Data protection is not a patent extension. Rather, it runs independently from the date of approval of the

innovator drug, and thus usually runs concurrently with patent protection (which begins to run when the patent application is filed).

Governments have an obligation to provide for enforcement of patents. This enforcement can be implemented in many ways. For pharmaceuticals, government regulatory agencies are involved in review of products that can infringe patents. Through a patent linkage mechanism whereby the regulatory authority does not grant approvals for products known to infringe patents, governments can avoid having a government agency (i.e., the regulatory approval authority) foster infringement of patents. This rule of law concept is particularly important in countries in which the ability to enforce a patent in court is inadequate.

II. Importance of Effective Intellectual Property Protection by U.S. Trading Partners

During the Uruguay Round negotiations that produced the World Trade Organization (WTO), the United States made significant progress toward more consistent and effective global intellectual property (IP) protection standards. The result of this effort was the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), which requires all WTO Members, including the United States and most of its trading partners, to establish functional intellectual property systems. Under the TRIPS Agreement, intellectual property owners must be given rights promptly, must gain certain minimum assurances of the characteristics of the rights, and must have recourse to effective means for enforcing those rights.

One of the concessions made by the United States in the TRIPS Agreement was to provide developing countries with a number of extended transition periods to implement new standards. During the first transition period, which concluded on January 1, 2005, all but the least developed countries were required to comply with the provisions of the TRIPS Agreement. Many of these trading partners have benefited tremendously from the trade liberalizations of the

Uruguay Round in other areas outside the TRIPS Agreement. These countries are also home to industries that aggressively compete with U.S. industries – particularly in the pharmaceutical sector. Yet even now, many developing countries have not fully met their TRIPS obligations to provide effective intellectual property protection for pharmaceutical technology.

Especially troubling is the failure of almost all the developing countries to establish measures in their countries that implement effectively their obligations under TRIPS to prevent unfair commercial use of pharmaceutical test data (i.e., provide data protection). PhRMA member companies believe it is now time to refocus government efforts on steps that will ensure a full implementation of TRIPS, including its provisions concerning protection of clinical test data.

Another important area of concern is counterfeit drugs. Weak regulatory and IP enforcement regimes in some countries contribute to this problem, which increases health risks to patients, particularly those in poor populations. PhRMA believes this problem may increase in significance, and that the assistance of the United States throughout the Special 301 process and through other fora will be essential to ensuring delivery of safe medicines to patients.

III. Market Access Barriers

Many of the countries in which the pharmaceutical sector attempts to do business erect barriers to reduce the access of our products into their markets. Clearly, these reductions in market access adversely affect the health of patients in those countries, but they also have potential negative effects on our industry in the United States and consumers worldwide. That is, these reductions could translate into lost revenues that, in turn, could translate into loss of employment and decreases in the R&D investment critical for continued medical advances. We applaud the U.S. Government for its success in eliminating certain trade-distorting practices in intellectual property systems worldwide with respect to pharmaceutical products. The problems we face from market access barriers grow each year, in part because of this success. When it is not possible to

eliminate our products from markets through sub-standard intellectual property laws, officials in many countries seek alternatives such as imposing market access barriers.

We believe that it is critical for the U.S. Government to take action against measures that deny fair and equitable market access to our products. PhRMA members believe that the Special 301 review process can be a particularly useful trade tool through which these barriers in priority markets can be removed.

A. Types of Market Access Barriers

Market access barriers for pharmaceutical products are not generally found in traditional forms such as quotas or tariffs. Rather, they often materialize as direct government price controls or the discriminatory administration of national health insurance schemes that dominate markets for pharmaceuticals. In respect to the latter in particular, pharmaceutical suppliers cannot market a product to most of the population until the insurance or reimbursement authority approves its use and its price. Consequently, reimbursement officials can erect barriers to access either unintentionally through poor administration or intentionally through protectionist measures.

There are four general types of market access barriers our industry faces. Any or all may be present in a single country. Often, several types work together to effectively deny market access for our companies' products.

First, many government price control and national insurance programs lack transparency and fairness in product approval and price setting processes. While most countries afford manufacturers or sellers some right of participation in pricing or reimbursement decisions, there are significant disparities in the openness and accessibility of the decision-making process. In many countries (such as China, Brazil, and India) governments obtain information from manufacturers or sellers that forms part of the basis for a pricing or reimbursement decision, but the decision-making process itself is largely

conducted in a non-transparent manner. In addition, a lack of reasoned explanations for final determinations and an unwillingness of administrative bodies and courts to scrutinize administrative decisions often prevents stakeholders from challenging adverse decisions.

Another key transparency concern relates to the frequent failure of decision-making bodies to provide rights of participation to all key stakeholders. For example, many governments (including those in highly developed countries such as Australia, France, and Italy) afford patients little or no opportunity to participate in reimbursement decisions, even though these stakeholders often have information that is essential to a fair decision.

In this vein, the recently concluded U.S.-Korea Free Trade Agreement (FTA) sets an important precedent by building on the transparency and due process provisions addressing pharmaceutical pricing and reimbursement systems included in prior agreements. Under the terms of the FTA, Korea must revise its system to provide, among other things, greater rights of participation to stakeholders, issue full explanations for administrative decisions, and establish an independent review mechanism. These FTA provisions should be adopted in other countries that place pricing and reimbursement constraints on pharmaceuticals.

Second, many government price control and national insurance programs are used to unnecessarily delay marketing approval of innovative pharmaceuticals. In many countries, national health insurance schemes dominate markets for pharmaceuticals. As a consequence, a pharmaceutical effectively cannot be marketed in a country until national authorities have determined its reimbursement price. The government entities responsible for pricing and reimbursement in most countries tend to be highly opaque bureaucracies, and the process of obtaining a government-approved price can be lengthy. These delays may be used by governments to delay market entry for other purposes.

For example, governments may use the fact that each day of delay reduces the effective patent life for a new drug (i.e., the time between initial sale of the product in a country and expiration of the patent) as leverage to negotiate lower prices with innovator companies. In fact, some delays may be so lengthy that the patent term could expire by the time marketing approval is granted, thereby depriving the innovator of the benefit of its patent rights altogether. Delays may also be favored to avoid costs associated with offering new treatments, or to reduce competition with existing products offered by local generic companies. Moreover, it is not uncommon for some foreign governments to close reimbursement lists entirely to innovative pharmaceuticals. These processes all operate to delay market access (and to diminish the effective patent life) for many innovative new drug products.

Third, many government price control and national insurance programs routinely establish unreasonable prices. Policies creating market access barriers can also result in market distortion that makes the cost of generic pharmaceuticals – often produced primarily by domestic companies – quite high. (add cite for this point – perhaps OECD report in fn 26 covers it) Many foreign generics markets are characterized by a lack of true market competition, which tends to raise prices of those pharmaceuticals above what they would be in a free market. Indeed, many foreign systems actually mandate high prices for generics products, requiring that they be reimbursed at rates as high as 70% or even 90% of the price of original branded products. (same) In the United States, where there is vigorous price competition in the generics market, prices of generic pharmaceuticals tend to be much lower. In a letter to Congress that accompanied the 2004 Department of Commerce Study, the Secretaries of Commerce and Health and Human Services asserted that “[i]n fact, U.S. consumers would pay, on average, 50 percent more for their generic medications if they bought them abroad.”²⁶

²⁶ U.S. Department of Commerce, “Price Controls in OECD Countries,” (2004)

Fourth, many government price control and national insurance programs wish to favor local suppliers over innovative, multinational enterprises. Local interests – such as generic producers, wholesalers and pharmacists – generally occupy a politically-favored position within these systems and have significant sway in the policy decisions of the domestic health system.

These are some of the primary market access barriers faced by PhRMA member companies. We provided details of these and other barriers on a country-to-country basis in our submission earlier this year during the Special 301 Review. The submission can be found at www.phrma.org.

B. U.S. Government Engagement on Market Access Barriers

The Special 301 statute authorizes the USTR to identify foreign countries that deny fair and equitable market access to U.S. persons that rely upon intellectual property protection. PhRMA looks to Congress, the Administration, and USTR specifically, to take action by continuing to develop an effective strategy to address these practices. Such actions would be consistent with Congressional directives found in the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 and the Trade Promotion Authority Act of 2002. PhRMA believes that the Administration should use the Special 301 process to advance a multi-front strategy. First, as recognized in USTR's 2008 Special 301 Report, bilateral consultations should be pursued to promote sustainable innovation by addressing market access barriers abroad.²⁷ The market access barriers maintained in even developed countries undermine intellectual property rights, deny patients access to the most innovative medicines, and undermine sustainable innovation.

²⁷ The 2008 Report stated that:

The United States also is seeking to establish or continue dialogues with OECD and other countries to address concerns and encourage a common understanding between developed countries on questions related to innovation in the pharmaceutical sector. The United States already has had such dialogues with Japan and Germany, and is seeking to establish ones with other countries. It also has established a dialogue on pharmaceutical issues with China.

Second, the Administration should continue its use of bilateral and multilateral trade negotiations to pursue a positive agenda on pharmaceutical market access issues. For example, the outcome of the U.S. – Korea FTA negotiations benefited from a two-way discussion on Korea’s complex and discriminatory listing system. The outcome was a negotiated text that included provisions on pharmaceuticals and specific steps to improve the transparency and accountability of the pricing and reimbursement listing process. We urge the Administration to build on this success and include similar provisions in agreements with future trading partners.

We look forward to working with you to continue our efforts in securing adequate and effective market access for U.S.-based innovative pharmaceutical companies.

IV. Summary of Selected Countries and Issues

Next, I would like to highlight some priority issues by country that we and our member companies would welcome the opportunity to work collaboratively with you in addressing.

Brazil: PhRMA’s member companies operating in Brazil remain concerned by the Government of Brazil’s failure to make progress on several important patent and data protection issues. Many of these concerns have been raised in prior years with little apparent impact, including:

- the practice of Brazil’s health regulatory agency (ANVISA) of improperly intervening in the patent examination process, whereby they frequently defer action or block patent grants;
- the lack of clarity, transparency and judicial review of actions taken pursuant to the decree that authorizes the Minister of Health to issue compulsory licenses;

- continued concerns regarding the “patent backlog” contributing to unreasonable delays in the granting of patents to deserving inventions despite some efforts by the patent office (INPI) to improve its operations;
- government price control mechanisms that discourage innovation while not addressing the stated goal of improving access to medicines; and
- the often antagonistic positions advanced by Brazil in numerous multilateral *fora* that would, if successful, undermine the international patent system and thereby diminish incentives for critical R&D worldwide.

India: PhRMA and its member companies remain concerned about deteriorating intellectual property protection standards and significant market access barriers in India. India still has not implemented data protection provisions for pharmaceutical test data, as required by TRIPS. The standards for patentability in India need to be amended to conform to India’s obligations under the TRIPS Agreement as well as prevailing international practice. In addition, the backlog of patent applications awaiting examination and the patent pendency are of growing concern. Also, India is an increasingly significant source of counterfeit pharmaceutical products and is believed to be a major channel for the export of counterfeits to consumers worldwide. Finally, PhRMA members are concerned about proposals to increase the scope of India’s government price control system in a manner that would discriminate against imported products.

China: PhRMA and its member companies operating in the People’s Republic of China remain concerned over inadequate intellectual property protections, including a lack of effective data protection and poor enforcement against counterfeit pharmaceuticals. Likewise, PhRMA is concerned about several market access barriers, including: (1) an inadequate government pricing

policy for innovative products; (2) an absence of update of drug reimbursement list for over four years; and (3) a lengthy requirement for clinical trial applications.

Philippines: PhRMA and its member companies operating in the Philippines are increasingly concerned about the deterioration of the intellectual property protection environment and the failure of the Philippine Government to address PhRMA's long-standing issues. PhRMA members' most pressing concerns relate to the implementation of the Universally Accessible Cheaper and Quality Medicines Act of 2008 ("the Act"). PhRMA's concerns were not considered or addressed by the Government during the drafting of the Act and its implementing rules and regulations. As a consequence, the Act and its implementing rules and regulations contain several provisions that undermine the ability to obtain adequate intellectual property protection in the Philippines and are inconsistent with the Philippines' obligations under the TRIPS Agreement. In addition, PhRMA's member companies continue to face numerous issues related to patent linkage, parallel importation, data protection, counterfeit drug enforcement, and regulation of drug prices.

Thailand: PhRMA and its member companies operating in Thailand are very concerned that no progress has been made in addressing the issues PhRMA has previously raised, particularly the inappropriate use of compulsory licenses in Thailand, and the fear that the Government is seeking to further reduce protections of intellectual property rights. Despite previous assurances by the Thai Government that a constructive healthcare dialogue between PhRMA's member companies and Thailand Government officials would occur, numerous good faith attempts by member companies to start this process have been rebuffed. PhRMA's member companies continue to have major concerns related to counterfeit medicines, patent linkage, the lack of data protection, delays in the grant of patents, and inappropriate government procurement policies.

Russia: As Russia prepares to develop its own innovative pharmaceutical industry, major market access barriers remain for the U.S. pharmaceutical sector. Russia still does not provide pharmaceutical data protection, despite commitments to the U.S. Government to implement such protection by May 2007. Moreover, non-transparent market conditions are compounded by new signals that some Russian officials want to use healthcare reform to promote discriminatory policies that further impair market access for PhRMA member companies. Although Russia made significant commitments in the 2006 U.S.-Russia WTO Accession bilateral on intellectual property rights (IPR), the Russian Government has not taken steps to fulfill these commitments.

* * *

Thank you again for the chance to speak with you today. PhRMA and its member companies believe it is crucial for this Subcommittee and other policymakers to support policies that foster incentives for innovation both in the U.S. and abroad. We welcome your interest in this issue, and look forward to working with members of the Subcommittee and others in Congress as you address these and other important policy issues relating to innovation and access to medicines.

Ms. WATSON. Thank you, Mr. Toohey.
Mr. Vargo.

STATEMENT OF FRANK VARGO

Mr. VARGO. Thank you, Madam Chairwoman and Mr. Bilbray.

The NAM is all about manufacturing in America. We are still the world's largest manufacturer. We make, believe it or not, one out of every \$5 of everything made and manufactured in the whole world.

But we are under a lot of challenges and a lot of threats, and the most serious truly is the threat to the protection of intellectual property. The United States is never going to be the world's low-cost producer, nor would we want to be. We want to be the high-tech producer, the high-value-added producer, but we have to have protection of patents, trademarks, copyrights, and those are under real, real threat right now through what I call the three Cs: counterfeiting, compulsory licensing, and China. Let me just say a few words about each.

The administration has and the previous administration have done a good job in increasing enforcement and trying to intercept counterfeited goods. More resources are going on. Having Victoria Espinel, who everybody in the trade community knows and thinks is just a fantastic choice, is very, very helpful. But there has been a major step backward that nobody has mentioned as yet, and I do want to focus on, because it may require legislation. When I first heard of this I couldn't believe it.

What Customs officials do when they suspect a counterfeit shipment is, logically, contact the trademark holder or the patent holder and send photographs or descriptions and say is this your product. Well, the Customs and Border Protection legal office recently sent a notification to Customs agents saying you can't do that any more. You cannot custom the rights owners with photos or descriptions of suspected counterfeit products because this could allow facing of liability under the Trade Secrets Act.

Now, to me this is ridiculous, and if there is, indeed, some legal conflict here I hope this subcommittee will look into it, and if we need legislation let's do it. This can undo all the good. You know, if a Customs official is prohibited from contacting, say, the Square D Co., which makes excellent circuit breakers, because they suspect that there is a shipment of counterfeit circuit breakers—are these real, did you bring these in—but if they are prohibited from doing that, believe me, the interception of counterfeit goods in the United States is going to come way down. I think this is an extremely serious problem.

Compulsory licensing: the country of Ecuador, for example, is saying now we need U.S. agricultural chemicals, so we are going to just force, we will steal the technology. There are countries talking about global climate change are saying well, you know, if you want us to participate in improving the environment, you have to give us the technology. This technology costs billions and billions to develop, and the even better technologies of the future are going to require more billions. Where does this come from? It comes from the flow of funds by having U.S. companies marketing around the world.

What these countries need to do is not say we want to steal your technology, but what they need to do first is to join in the idea the United States has promoted, that look, there should be an environmental goods and services agreement globally. What sense does it make for countries to put 20 or 40 or 60 percent import duties on clean climate technologies. You know, let's get rid of government interference there and let them take it from there.

Then China. Based on Customs data, we can estimate that 80 percent of the counterfeit goods in the world are made in China. China joined the WTO in 2001 and promised that they would provide an effective deterrent against counterfeiting. An effective deterrent. That means they were going to stop it.

Now 8 years later they haven't done it. They still don't have the laws necessary to criminalize counterfeiting. It is an administrative procedure, you get a slap on the hand, you move across the street, and you are back in business. They have not cracked down on the corruption in the provinces, where frequently you have local leaders in cahoots with the counterfeiters. Enough is enough. This has to be accelerated. China Customs has to start intercepting the export of counterfeit goods.

And then China comes along with the indigenous innovation product accreditation system, saying, you know, we are tired of using American technologies and British technologies and Japanese and others. We want Chinese. And the best way to do that is to take our enormous government procurement market and close it off. So only indigenous Chinese technologies, those developed in China and owned by Chinese, and that were originally registered in China, will be able to participate in the Chinese government market. Well, you know, that is blatant protectionism. That is what the whole world trading system is designed to stop.

Now, on top of that, it was only a couple of months ago that China solemnly promised in the Joint Commission of Commerce and Trade statement, that China will require that products produced in China by foreign enterprises will be treated equally with domestic products. Well, you know, I guess that promise was good only for 3 months.

Anyway, this is a very, very serious challenge. This could be the most serious challenge to U.S. manufacturing ever faced. So I commend you for this hearing. Please stay on top with the NAM will. The best way to solve this, of course, is in a collegial way with the Chinese government, and we certainly hope that works, but one way or another this is unacceptable.

Thank you.

[The prepared statement of Mr. Vargo follows:]



Testimony

of Franklin J. Vargo

Vice President for International Economic Affairs

on behalf of the National Association of Manufacturers

*before the Subcommittee on Government Management, Organization
and Procurement, Committee on Oversight and Government Reform*

The U.S. House of Representatives

*Hearing on "Protecting Intellectual Property Rights in a Global
Economy: Current Trends and Future Challenges"*

December 9, 2009

**MANUFACTURING
MAKES AMERICA STRONG**



**Testimony of
Franklin J. Vargo
Vice President for International Economic Affairs
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Washington, DC**

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Wednesday, December 9, 2009

Introduction

Chairwoman Watson, Ranking Member Bilbray, and distinguished members of the Committee on Oversight and Government Reform’s Subcommittee on Government Management, Organization and Procurement: thank you for inviting me to testify on “Protecting Intellectual Property in a Global Economy: Current Trends and Future Challenges.”

I am the Vice President of International Economic Affairs for the National Association of Manufacturers (NAM), the nation’s largest industrial trade association, representing small and large manufacturers in every industrial sector and in all 50 states. Our membership includes a broad swath of companies, such as medical device manufacturers EXEL International and Moldex Healthcare Products, both in Culver City, California, consumer skin care products producers such as CA Botana and consumer electronics companies like Sony Electronics, both of whom are in San Diego. I am pleased to testify today on behalf of these companies, as well as the rest of our nation’s manufacturers, on a critical issue – that of protecting American consumers from counterfeit and pirated products. The trade in fake products – whether it is medical devices, skin care products, consumer electronics, auto parts, pharmaceuticals, aircraft parts, consumer goods, or machine tools – has had a devastating impact on our economy, manufacturers, workers, and consumers.

My colleagues on today’s panel will agree with me when I say that we all have been in the forefront of pushing for strong U.S. government policies, for aggressive enforcement, for adequate personnel and financial resources, and for strong international cooperation to fight the scourge of piracy and counterfeiting. Hopefully, my colleagues and I can shed some light on how Congress, the Administration and private industry can work together in stopping the trade of counterfeit and pirated products.

IP theft is a job-killer that is stalking the road to economic recovery. While the situation is dire, we are not undone. If our nation is to regain its place of strength in the world economy, we must take affirmative steps now to end this nefarious practice. Remedies are at hand, and if Congress, the Administration and industry can work together, not only can we reverse much of the damage, but we can gain important ground on counterfeiters and pirates both here and abroad. The enactment of the “Prioritizing Resources and Organization for Intellectual Property (PRO-IP) Act” last year, which the NAM supported, is only the beginning. Domestically, the NAM makes the following recommendations:

- Congress and the Administration must continue to establish, empower and fund high-level leadership on IP issues throughout the government – from the recently created Intellectual Property Enforcement Coordinator position within the White House, to every federal agency tasked with the protection of intellectual property. These high-level leaders can then develop an integrated strategic plan to fight counterfeiting and piracy, replete with deliverables, timetables and performance measures.
- To support the strategic IPR plan, Congress and the Administration need to give the Bureau of Customs and Border Protection (CBP) and the Immigration & Customs Enforcement (ICE) Bureau agents at our ports the tools to do their jobs effectively, including increased training, the ability to enforce exclusion orders to stop certain IP-infringing goods from entering the country, and the clear authority to seek meaningful help from rights holders when faced with a suspected counterfeit or pirated product.
- Further, we need to provide dedicated resources to the FBI and Justice Department to empower investigators and prosecutors tasked solely to the job of tackling IP theft. Federal prosecutions for IP-related offenses have increased dramatically in recent years; if we are to continue this trend, we must give them the authority, the tools and the resources to get the job done.

Internationally, the NAM makes the following recommendations:

- Congress and the Administration must continue to support a proactive, aggressive IPR agenda with our important international trading partners from China, India, and Russia to the European Union, Korea, Mexico, and Canada.
- Additionally, Congress and the Administration must ensure that U.S. intellectual property is not arbitrarily traded away at the international negotiating table through compulsory licensing regimes. Under these ‘agreements,’ large industrializing nations can take for a pittance what American companies have toiled to create – all in the name of promoting ‘green technologies’.

- Finally, Congress and the Administration need to work with the Chinese government for meaningful reforms to their IPR enforcement regime. These reforms include lowering the threshold for criminal proceedings in counterfeiting cases, ensuring the destruction of equipment used to produce counterfeit goods after a successful conviction, and ensuring provincial and municipal leaders in China are responsible for IP protection in their own jurisdiction.

Consumers Harmed by Counterfeit Products

Beyond all the economic costs and lost jobs, when counterfeit products – products such as medicines, medical equipment, pet foods, cosmetics, auto and aircraft parts, industrial fasteners, or household appliances – get into the marketplace, the lives of consumers are put at risk.

Disposable medical care product manufacturer EXEL International recounts news stories from earlier this year where over two million counterfeit insulin pens had been introduced into the regular European distribution channels. While it should be noted that these were not EXEL products, it is still a cause of concern for them as every reported incident of counterfeit medical products creates fear and uncertainty over the integrity of *all* medical products, legitimate ones included. Interestingly, these counterfeit insulin pens were distributed from a wholesaler in Malaysia, who in turn claims they derived from Iran, beyond which the supply chain could not be traced.

Our drug-manufacturing members tell us about the threats posed by the aggressive distribution of fake medicines, and the incredible effort being made by the U.S. pharmaceutical industry and its customers, suppliers and other partners to ensure the counterfeit medicines not seep into supply chains in the U.S. or around the world. The World Health Organization (WHO) has estimated that up to 1 percent of medicines available in the developed world are likely to be counterfeit.¹ The figure rises to 10 percent globally and can be as high as 33 percent in some developing countries. Despite the major efforts of the industry, hospitals, pharmacies and other partners, counterfeit medicines are penetrating the legitimate supply chain here in the U.S. And we're not just talking about aspirin and bandages here. These counterfeit products often target very sensitive product areas including cardiovascular and central nervous system medications, chemotherapy medicines, and high-tech medical devices such as endoscopes and defibrillators.

¹ World Health Organization Fact Sheet on Counterfeit Drugs, July 2009, <http://www.who.int/medicines/services/counterfeit/CfeitsFactSheetJuly09.pdf>.

Other examples include counterfeit batteries that look so much like legitimate batteries the only way to tell the difference is with an X-ray machine where you would see that the fake battery is lacking in thermal vents. It may seem like a small oversight, but it is a critical one as thermal vents are integral in avoiding a catastrophic failure of the battery, which could lead to a catastrophic loss of life and property from fire or chemical burn. In the automotive aftermarket for parts and accessories, among the most commonly counterfeited items are brakes, rotors, headlamps, tail lights, oil pumps, windshields, and steering arms, many of which seem to trace their roots back to China.

Manufacturing Jobs Harmed by Counterfeit Products

Not only do counterfeit products steal our nation's most innovative ideas, but they steal high-paying American manufacturing jobs as those fake products displace legitimate ones in the marketplace.

According to the U.S. Department of Commerce, America's IP-intensive industries employ nearly 18 million workers, and account for more than 50 percent of all U.S. exports, representing 40 percent of the country's growth.² U.S. intellectual property is worth between \$5 trillion and \$5.5 trillion – more than the nominal gross domestic product (GDP) of any other country;³ yet the continuing trade in counterfeit products results in the loss of hundreds of thousands of jobs annually.

Counterfeiting is a world-wide problem. In 2008, the Organization for Economic Co-operation and Development (OECD) estimated that the amount of counterfeit goods smuggled across borders amounts to at least \$200 billion per year world-wide.⁴ This number, however, only represent *cross-border* counterfeits, not those produced and sold within the same country, nor does it account for upstream and downstream losses borne by suppliers to and customers of the companies whose legitimate sales are displaced. In total, it is reasonable to estimate that the amount of economic harm inflicted by IP theft easily surpasses a *half-trillion dollars* every year.

² *Engines of Growth: Contributions of the U.S. Intellectual Property Industries*, Stephen Siwek, Economists Incorporated, 2005, at http://www.nbcuni.com/About_NBC_Universal/Intellectual_Property/pdf/Engines_of_Growth.pdf.

³ Robert Shapiro and Kevin Hassett, "The Economic Value of Intellectual Property," USA For Innovation Report, October 2005; available at http://www.usaforinnovation.org/news/ip_master.pdf

⁴ The Economic Impact of Counterfeiting and Piracy, OECD, June 2008, <http://www.oecd.org/dataoecd/21/20/40896133.pdf>.

Despite the world-wide impact of counterfeiting and piracy, U.S. manufacturers bear the brunt of the burden. Statistics released by CBP this year show that from FY07 to FY08 the number of IPR seizures increased by 9.7 percent, from 13,657 to 14,992, and the domestic value of the goods CBP seized for IPR violations increased by 38.6 percent to \$272.7 million from \$196.7M in FY 2007.⁵ This is no doubt to some extent attributable to CBP doing a better job identifying and seizing counterfeit goods. But from the reports of our member companies, it primarily reflects the fact that the economic assault on the worldwide marketplace in every sector is simply out of control.

Congress and the Administration's Role

The President's Innovation Strategy explicitly recognizes the importance of IP protection, stating that the U.S. "must ensure that intellectual property is protected in foreign markets and promote greater cooperation on international standards that allow our technologies to compete."⁶ Last year, the PRO-IP Act was signed into law, expanding government's ability to respond to this national crisis with stronger laws, better leadership and dedicated resources. This was an important first step, but the battle is not over. First, we must strengthen law enforcement's ability to identify, detain, prosecute and punish those who would bring illegal counterfeit products onto U.S. shores via our ports. At the same time, we must work with our foreign partners abroad to help them stop the trade in fake products.

In the United States, there are a number of things that Congress can do to help manufacturers. First, effective high-level leadership on IP protection must be established, both at the Agency level and on a government-wide level. To that end, President Obama has named an Intellectual Property Enforcement Coordinator (IPEC), as directed to by the PRO-IP Act. Victoria Espinel, who was the first Assistant United States Trade Representative for Intellectual Property and Innovation, now awaits confirmation by the full Senate. As part of her responsibility as the IPEC, Ms. Espinel will be responsible for creating our nation's anti-counterfeiting policy with the help and coordination of the eight different federal agencies responsible for interdicting and prosecuting these criminals. We are pleased that the Administration has taken this step in selecting Ms. Espinel, and we are looking forward to the benefits of a more coordinated approach to IP enforcement.

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http://www.cbp.gov/linkhandler/cgov/trade/priority_trade/ipr/seizure/fv08_final_stat.ct/fv08_final_stat.pdf

⁶ A Strategy For American Innovation: Driving Towards Sustainable Growth and Quality Jobs (page 15), http://www.whitehouse.gov/assets/documents/sept_20_innovation_whitepaper_final.pdf

Congress' role in IP protection is equally important in combating counterfeit products. Specifically, effective enforcement requires dedicated resources. The PRO-IP Act authorized new IP-dedicated FBI agents and prosecutors, so as to have the undivided attention of key federal law enforcement officers focused not only on the problem, but the solution. To aid in that effort the House this June passed the Commerce, Justice and Science (CJS) Appropriations bill, H.R. 2847, that would increase funding to critical programs authorized by the PRO-IP Act, including an additional \$8 million for new FBI agents to investigate intellectual property (IP) cases, an additional \$2 million for new U.S. Attorneys to prosecute IP crimes, and \$20 million for economic, high-tech and Internet crime prevention grants to state and local law enforcement agencies. In the Senate, however, this critical funding has been stricken from the CJS Appropriations bill. The NAM would like to see this funding restored.

In June, the House passed the Foreign Relations Authorization Act, H.R. 2410, which would create 10 new Intellectual Property Attaches in key embassies around the world, plus the resources to support their efforts. These IP Attaches would aid enforcement efforts abroad, as well as work with their host governments to help reform applicable laws, regulations, practices and agencies to enable them to fulfill their international and bilateral obligations with regards to IP rights. The NAM is supportive of this aspect of the bill, which is now pending in the Senate Foreign Affairs Committee.

Also currently pending in the Senate Finance Committee is the "Customs Facilitation and Trade Act of 2009," S. 1631, which will create a stronger role for the CBP and ICE in protecting U.S. consumers from counterfeit products. This legislation is particularly critical, as CBP and ICE are our nation's first barrier against the flood of counterfeit and pirated product coming in through our nation's ports. Unfortunately, they are overburdened and do not have the rights tools to fight the rising tide of pirated products. S. 1631 will go a long way in strengthening CBP and ICE by establishing leadership with the responsibility to make IP enforcement a priority, increasing IP resources with better training for those in the field, and making statutory changes that will enable more effective enforcement for CBP inspectors and ICE investigators. Overall, the Customs Facilitation and Trade Act is a solid bill. The NAM will continue working with stakeholders in the Senate to strengthen the bill before it goes to the House.

The International Side

The NAM has long supported an aggressive U.S. program to raise international rules and national laws around the world protecting intellectual property rights. But strong international and national laws and regulations are only part of the battle. Strong enforcement is absolutely essential. The NAM strongly supports a proactive, aggressive international approach by the U.S. Government agencies. We also have supported putting intellectual property rights (IPR) issues, including enforcement, high up on the agenda for US government dialogues with a wide range of important international trading partners from China, India, and Russia to the European Union, Korea, Mexico, and Canada.

It is not an overstatement to say that America's international economic competitiveness – and thus our ability to create viable good jobs here at home – depends on strong IPR rules and laws, aggressive enforcement and deterrent penalties, and in-depth international cooperation. Our competitiveness is based on developing and producing top-quality, cutting-edge technologies. And that strategy is all based on IPR, such as patents, copyrights, trademarks, and industrial designs.

One key new area of IPR concern which has emerged over the last year goes to the heart of our Green Technologies manufacturing strategies. In the international negotiations leading up to the Copenhagen Conference on Climate change, a cabal of large rapidly-industrializing nations has insisted that “green technologies” must be exempt from IPR rules and laws. Those nations, led by India and China, have been insisting throughout the preliminary negotiations that green technologies must be subject to a “compulsory licensing” regime so that developing nations can immediately access the latest environmentally friendly industrial technologies without having to comply with standard IPR rules or indeed the rule-of-law more generally.

We at the NAM and others in U.S. industry are well aware of how “compulsory licensing” regimes are often gamed, as evidenced by the abuses against U.S. and other international pharmaceutical manufacturers. We've seen U.S. companies, workers, and regions suffer when countries abuse the compulsory licensing regime. The NAM will continue to urge U.S. negotiators in the Copenhagen process fight aggressively to oppose any compulsory licensing provisions in a Copenhagen agreement or anywhere else. Manufacturers in the United States have invested billions of dollars (and will invest much more) to develop cutting-edge, environmentally-friendly technologies and to create good jobs here at home. We will not sit by idly and let anyone, anywhere steal that technology in the market place, in the back alleys, or at the negotiating table.

As U.S. manufactures lead the way in the research, development and production of cutting edge “green technologies” we must ensure that these innovations are protected internationally. Achieving the kind of breakthroughs that the Administration, Congress and U.S. industry seeks will require billions in investment and will consumer the best minds of our generation. We simply must ensure that a strong and robust IP regime supports these investments.

In the international negotiations leading up to the Copenhagen Conference on Climate change, a group of large rapidly industrializing nations has insisted that “green technologies” should somehow be exempt from well-established rules protecting IP. Those nations, led by India and China have been falsely claiming that the patents on “green technologies” are putting key tools out of the reach of developing nations. This is a dangerous proposition because it distracts us from two key issues. First, it distracts us from the true challenges to deploying clean technologies in most developing countries which are related to infrastructure and adoption of basic improvements. Most of the technologies that would have the biggest impact on developing nations aren't protected by patents and/or have gone off-patent. Second, probably the single biggest deterrent to deploying clean technologies in most nations are large tariffs put in place as protectionist

barriers. When Brazil has a total tariff and non-tariff barrier of 160 percent and China has a 40 percent barrier on clean-coal technologies, our conversation should start there.

Insisting that green technologies must be subject to a “compulsory licensing” regime so that developing nations can simply take the latest environmentally friendly industrial technologies is a short-sighted attempt to take advancements made by U.S. companies that will chill investment and cost jobs.

We applaud statements made by Congress and the Obama Administration regarding the importance of protecting IP in the context of climate change talks. Earlier this year the House adopted by a vote of 432-0 an amendment to the Foreign Relations Authorization Act that emphasizes the importance of intellectual property in the Copenhagen Climate negotiations, and a bipartisan group of 60 Members recently sent a letter to Secretary Clinton reaffirming this point. Likewise, the President’s top negotiator to Copenhagen has testified to Congress about the importance that the Administration places on IP protection.

I want to highlight growing concern about the spread of blatantly unlawful anti-IP attitudes into new countries of concern. The NAM has been a strong supporter of the annual “Special 301” process lead by the Office of the USTR to identify priority IPR problems around the world. We commend USTR and all the other agencies of the U.S. Government which have worked so hard to make the Special 301 process a useful tool that can deliver real results. We look forward to working with USTR, the Administration, the Congress, and other stakeholders to strengthen and sharpen the Special 301 process and make it an even more useful tool for fighting counterfeiting and piracy and protecting U.S. manufacturing, technologies, and jobs.

Today, I also want to highlight one of our latest concerns regarding the virulently anti-IPR policies and politics, most vividly in the diatribes from President Correa himself, in Ecuador. Rapidly deteriorating IPR conditions are far from our only concerns about Ecuador. IPR takes its place in the list along with counter-narcotics cooperation, human rights, democracy, rule-of-law and treatment of international investors in a growing list of concerns about conditions in Ecuador. President Correa’s public threat to revoke well-established IPR protections for local and international companies in the pharmaceutical, agricultural and chemical sectors seem to signal that Ecuador prefers to deal with pirates and counterfeiters, rather than legitimate businesses.

China

We have special concern with regard to China, which has for a number of years been the epicenter of global counterfeiting. China, the number one source country in FY 2008 for counterfeit goods seized, accounted for \$221.6 million or 81 percent of the total domestic value of IPR seizures.⁷ Despite extensive engagement between the U.S. and Chinese governments, and a range of commitments on the part of the Chinese government, there still remains a thriving counterfeit industry in China.

Another member company, CA Botana, gives an example of how counterfeiting in China is aided by its one-sided import laws and their impact on even small U.S. businesses. Any company looking to obtain an export license for personal care products from China must provide a 100 percent formulation of the product – essentially a list of the secret ingredients and their amounts – as well as comply with further requirements that these imported products have 75 percent Chinese content in them. Because of these requirements, companies such as CA Botana are forced to work with Chinese companies who are producing both authorized and unauthorized products (which are also considered as counterfeit). Due to this practice, U.S. businesses are seeing over 20 percent of their sales – both in China and in the U.S. – supplanted by counterfeits. When a full fifth of a manufacturer's sales disappear, so does their ability to maintain their worker base.

The theft of their intellectual property is a big problem for large companies; it is an insurmountable one for small companies that do not have the resources to track down and prosecute counterfeiters. Many small companies choose not to sell their goods to Chinese buyers for fear of having them illegally copied and sold in China and third markets.

Foreign companies are not alone in suffering losses in profits and reputation as a result of product counterfeiting. The NAM believes that there are several things that must be addressed in order for China to bring the problem under control:

- Currently 99 percent of copyright and trademark counterfeiting cases in China are enforced administratively, rather than criminally. In these circumstances, counterfeiters, if convicted, receive fines that represent just a cost of doing business, not a real deterrent. A greater number of cases must be referred for criminal prosecution.
- In addition, in cases when there is a counterfeiting conviction, the equipment used to produce the goods must be destroyed. Under current Chinese practice and law, it is too easy to leave the courtroom and resume business as usual.

⁷ CBP, ICE Release Annual Report on Counterfeit Goods Seized, January 08, 2009, http://www.cbp.gov/xp/cgov/newsroom/news_releases/january_2009/01082009.xml.

- The Chinese central government has made great strides in recognizing the importance of IPR protection and in raising awareness of the issue. However, until provincial and municipal leaders in China are measured and held accountable both by the Government of China and internationally on the degree of IP protection afforded within their jurisdictions, there will continue to be greater emphasis on job creation without regard to enforcement of IP law, and U.S. manufacturers and workers will suffer.

Conclusion

If we allow counterfeiting and piracy to run unabated, the risks to the American economy are obviously very serious. However, if we invest in protecting our nation's consumers, workers and businesses from IP thieves, the rewards will come back to us six-fold. According to a report commissioned by the Coalition Against Counterfeiting and Piracy (CACAP) – which the NAM helped fund – investing in stopping counterfeiting is sound economic policy. Authored by Laura Tyson, former Chair of the National Economic Counsel, the report entitled “An Economic Analysis of the Proposed CACAP Anti-Counterfeiting and Piracy Initiative” concluded that:

- For every dollar invested, federal tax revenues would increase significantly with an intermediate range of \$4.9 to \$5.7;
- Each dollar would increase U.S. economic output approximately between \$64 and \$75;
- The increase in output would result in the creation of between 174,000 and 348,000 new jobs during the third year of the program; and
- State and local governments can expect to receive incremental revenues between \$1.25 billion and \$1.50 billion, in present value terms over three years.

The Report also concludes that by aggressively going after counterfeiters and pirates as laid out by the PRO-IP Act and recommendations included in S. 1631, Congress' efforts could reasonably be expected to reduce losses attributable to piracy and counterfeiting somewhere between five and ten percent over three years.

We are looking forward to working with Congress and the Administration to ensure that all possible efforts, avenues and opportunities to stop counterfeiting and piracy are explored and exhausted, whether it be within our borders, at our ports-of-entry, or with our trading partners abroad. The health and well-being of our consumers, our workers and our manufacturers demand we do it.

The NAM appreciates the opportunity to work with the Committee in developing any plan to combat IP theft and we hope for a continued dialogue regarding ways to strengthen our nation's efforts.

Ms. WATSON. I would like to thank all the witnesses for your very informative testimony.

I would like to raise some questions, first with Mr. Holleyman. I want to continue on this issue that we have been referring to, China's proposed regulation on what is being called the national indigenous innovation products.

Is my understanding correct that these regulations will require your members to partner with or transfer their IPR to Chinese industry in order to qualify for government procurement programs?

Mr. HOLLEYMAN. Madam Chairwoman, that's the perfect question, and this issue is moving so quickly. Fortunately, the U.S. Government team has mobilized very quickly to counter this. But yes, that certainly is the intent of those regulations, that something would have to be completely indigenous to China, which would require the transfer of IP. It is certainly not clear that any of my members could ever—

Ms. WATSON. What type of products?

Mr. HOLLEYMAN. Well, there are six categories: computer applications and devices, communications products, modernized office equipment, software, new energy and equipment, and highly energy efficient products, and the understanding is this will be rolled out across a very broad sector of products, starting with these. And so it is not clear that any U.S. company could qualify or will make the type of concessions that the Chinese are seeking, so this will effectively exclude them from the market and certainly give hard preferences to whatever indigenous innovation occurs.

Ms. WATSON. Are there other proposals still under consideration?

Mr. HOLLEYMAN. Still under consideration. As with all things in China, it is not completely explicit and clear until it is seen, and in this case it moves very quickly, but the business community not only here but in Europe, elsewhere in Asia and Latin America, and governments understand that this could be sweeping in scope, and what we need is this to be rolled back while there are further discussions with the United States, the E.U., and other major trading partners.

Ms. WATSON. Are we still partnering, discussing partnering in terms of the membership of China with the WTO?

Mr. HOLLEYMAN. Well, they have made a commitment that they will join the government procurement agreement as part of the WTO. They did it when they entered the WTO. They have made it in JCC to commitments to the United States and we believe that this action is contrary to the spirit of those commitments. In addition, it will have a dramatic exclusionary effect for companies.

Ms. WATSON. Now, do you think it would be helpful for us here on this subcommittee to assist you in engaging our Federal agencies or China's diplomatic representatives here in Washington on these matters?

Mr. HOLLEYMAN. Absolutely. I think that an outreach by this committee, you as the Chairwoman and Mr. Bilbray, directly to the Chinese Ambassador urging cooperation and trying to hold these off for pending further discussions will be useful.

I know that the issue is now getting the highest level of attention within the U.S. Government. One of our CEOs raised it at the President's job summit last week because not only does this take

away the potential for job growth for American companies and software and other industries in China, but it could cost the loss of jobs that we currently have today if that large market is shut out for further procurements.

Ms. WATSON. Our ranking member, Mr. Bilbray, has questions.

Mr. BILBRAY. Thank you.

Congressman, thank you very much for broaching the issue that there needs to be a nexus between trade agreements and intellectual property. I think, looking at the lack of oversight in trade agreements in the past create a situation like what we have right now with Colombia, and especially Panama, where we have still got that trade agreement hanging out there. And I see why people are skeptical of trade agreements, because they look at the history of not maintaining some level playing field.

And it really does hurt when you have a gray proposal, like we have with Panama, that they want to buy our bulldozers, Mr. Vargo. They want to build a canal with American equipment, and Washington's political structure is holding this up, when boy, I tell you, if there was any agreement that I saw that should be a matter of signing, that was one. But because of the lack of nexus, we are not doing enforcement.

Now, the Korean situation to me is as close to a parallel, could become a parallel, as China as we see on the horizon. The question is: is it just because, as we would say, too big to fail, that China is too big to confront now, that we are confronted with an 80 percent of world pirating coming out of one political agency.

And we can't say that they are not willing to do enforcement. We saw how effective they were with the milk tainting situation. Instead of giving them AIG pay raises, they take people out in the back yard. But you want to clarify exactly how we could be a little tougher on this?

Mr. GLICKMAN. First of all, that's a great question. I mentioned this before. We have this conflict because we have these countries on our special 301 list, and yet the same countries are on our general preference list.

Mr. BILBRAY. Right.

Mr. GLICKMAN. One, for example, is Russia. Eight years ago the U.S. industry submitted a petition to suspend GSP benefits for Russia, which has been on the priority watch list for the last 12 years, which has some of the highest piracy in the world; however, no action has been taken on the petition, and copyright piracy rages in Russia. Ironically, Russia is one of the fastest growing legal markets, as well, for U.S. products. So these are, as you can imagine, very complicated issues.

China, my friend Robert talked a bit about China. We, of course, filed a WTO case against China for basically inadequate intellectual property enforcement. We largely won that case. The Chinese are going to be appealing that case. And I think one of the things that is helping us now more than what we faced in the past is the rest of the world is coming along with us now.

If it were viewed just as the United States versus China, we will probably wait for another 250 years to get really anything done. But if it is the rest of the world involved in this case, if they join with us on the manufacturing sectors, the pharmaceutical sectors,

the automobile sectors, the entertainment sectors, and at agriculture sectors, then I think that we can have some impact.

They are in the WTO now, and one positive sign I see out of China for the first time is a great entrepreneurial class that is building that wants to protect their own intellectual property and see themselves victims of an arbitrary government action in this regard. But it is not easy and there is no simple solution except pressure at all levels, from the public sector and the private sector. It has had some impacts on other parts of the world; it has not yet had dramatic impact in China. There is no question about it.

Mr. BILBRAY. Is the European Union backing us up on this now?

Mr. GLICKMAN. They are beginning to back us up a lot more than they used to be. For example, you know, for a while they let us fight the battles for them, as they often—

Mr. BILBRAY. Europe has gotten into that habit.

Mr. GLICKMAN. But now, I mean, Europe and the United States share many of the same perspectives on manufacturing and intellectual property issues. In the film issue, for example, there is a quota. China will only import 20 foreign films a year under what you call normal revenue sharing agreements. The United States has maybe 13 or 14 of those, and the rest of the world has 6 or 7 of those. Of course, you can find any movie ever made in the history of the world on the streets of China, as well. But the Europeans are beginning to join us on those issues, as well.

By the way, the Europeans are making their own positive movement in the area of piracy. You mentioned both France, U.K., that are moving ahead, particularly in the area of Internet piracy. That is a positive sign, not only for themselves but also how it relates to places like China that we have seen very little movement in the past.

Mr. BILBRAY. Now, let's get back to this, though, this nexus between if you want to be our first class trading partner you have to be responsible to the intellectual property issue. I see this as a major issue. I have scientists that have developed new, you know, genetically altered algae that can produce diesel gasoline and jetco. This is going to be a big deal in the next 20 years. Have we made that nexus? Are we tying those together? Are we welding them together to where you can't play one game here and then expect to play the other game over here?

Mr. GLICKMAN. I think it requires, quite frankly, much greater attention to the inconsistencies that exist in the world trading situation, and for the U.S. Government to be a lot more consistent in its own approach.

I realize there are a lot of political issues here that you have to deal with country-by-country, but the disconnect, just the Russia example I have given you, and there are a lot of others in there where we kind of turn a blind eye on some things for maybe political reasons and our trade agenda suffers. That is something that we really need to move away from.

Mr. BILBRAY. And I worry about it, Madam Chair, that the fact is the big guys get away with murder while the little guys like Panama are waiting in hand with everything we have ever asked from them, but because they are so little we don't want to bother with the negotiations, and I just think it sends a really wrong mes-

sage. I think any parent would never accept the same thing in their family, and I don't think in the international community we should accept it, either.

Thank you very much.

Ms. WATSON. Thank you.

Ms. Chu.

Ms. CHU. Mr. Toohey, California is home to many research institutions from well respected universities to biotech firms. In fact, the State is home to 2,042 biomed companies. In fact, the California biomed industry has grown from ideas first germinated in the State's first universities and has flourished through entrepreneurial commitment and investor financing to create a very strong industry that has led to breakthrough technologies and therapies that have helped patients around the world. These businesses create high-paying jobs and keep more than 270,000 Californians employed. All of this is dependent on patent protection that is strong.

How do the needs of the pharmaceutical industry compare to that of the biotech and research universities? What are the areas where you agree with regard to patent requirement? Where do they diverge?

Mr. TOOHEY. Well, first of all, Congresswoman, I absolutely agree with the importance to California and the leading role that California has played with respect to biomedical innovation and it is a growing engine for the industry and for the world and it needs to be protected.

Patents and data protection and the whole suite of protections available for biomedical innovations are critical. They are critical to universities. They are critical to innovative companies. But we are finding in many cases that these patents are not really respected around the world. I believe we share very much with biomedical universities the same concerns about the protection of patents and the protection of test data protection.

You know, I would appreciate the opportunity perhaps to discuss a little bit more with some colleagues and get a more complete answer back to you about some of the areas and ways we have worked with some of the California biomedical universities. But as I understand it, we very much share the concerns that countries around the world need to enforce patents, need to provide appropriate protection for our clinical data. And in many cases that is not happening. The United States really leads the world in its protection, and we are finding that countries, even developed countries, are not allowing the protection of IP and market access in order for all patients to be able to receive their medicines.

Ms. CHU. Thank you.

Mr. Glickman, many of my constituents work in the film industry, either in set design, editing, or even acting. I know how important a strong and robust film industry is to them, not to mention to the overall U.S. economy. I know the industry is working hard with international governments and the Federal Government here at home to ensure that intellectual property laws are adequately enforced.

Just yesterday your organization was successful in helping to put an end to a notorious illegal Web site that was being operated in China after a 2-year-long Government investigation. This convic-

tion of a Chinese couple is the most recent that you have successfully brought against copyright infringers on mainland China.

What can we learn from other countries? I know we talked a lot about China and how badly they are protecting, but are there examples that are both good and bad of how we can improve our enforcement system here at home?

Mr. GLICKMAN. That's a very good question. First of all, I don't want to say it is 100 percent bad in China. After we filed the WTO case, the Chinese resisted, but there have been some improvements of training of IP judges. There has been some enforcement improvement. I would call it not material yet, but better than it was 5 years ago. But there is a lot of great stuff. So the pressure stays on and what we find is the more the Chinese develop an indigenous film industry of local producers, local actors, local directors, their stuff is getting pirated all over the place in China, just like our stuff is getting pirated. So the more we are all in this together, the better they, as well as us, see the need to protect intellectual property.

You go into these stores, there is a store in Shanghai called the Oscar Club. It is about 95 percent pirated stuff. Most beautiful video store you have ever seen in your life. It is not just American stuff. It has as much Chinese stuff as almost anything else. It has French. It has south Asian. It has everything else. So the more we can get the Chinese creative community involved, the better we are.

But other countries are also taking a very strong lead, particularly in Internet piracy. The French have adopted a system of graduated responses where they try to educate consumers, and then if they can't get them educated then they give the Internet service provider a mandate to take more forceful action. Other countries around the world are following that model.

We in our country, we are working with the Internet service providers very diligently to get them to do the same kind of thing that is permitted under something called the Digital Millennium Copyright Act [DMCA] in which all of this is done. But this is a worldwide battle waged everywhere in the world, but there are two positive things that have happened that I must tell you. One is this used to be a music and movies issue. This is a comprehensive, worldwide manufacturing, software, pharmaceutical, automobile, and everything, and for the first time in the last 4 or 5 years we are all working on this thing as an American issue. It is a gigantic American issue.

Then, in terms of the movie industry, we now have our unions, our guilds, the folks who actually work in the trenches all the time making these movies, as much involved with us—the Directors Guild, the Screen Actors Guild, and others, the Theater—well, all the organizations that are there. So we are finally beginning to get some political clout, both with respect to American industry generally as well as within our own industry.

There is a lot of perception out there that our business is big movie stars and that's it. Of the people, 99.9 percent make less than \$100,000 a year. They work very hard. They support their families. They are the people that Chairwoman Watson, I am sure, that occupies her District by and large.

So with that you try and develop the political clout to be able to show that this is important to our Government as well as governments around the world.

I don't want to make this all the voice of gloom and doom. I think there is a growing political clout to take this on as a very monumentally serious economic issue to this country. I hope we can get your help, which we have, and the help of our U.S. Government representatives to keep the fight going.

Ms. WATSON. I would like to conclude with throwing this question out to all of you, and then specifically being that we are in the kind of financial crisis as a Government that we are in, would your industries that are represented here at the table be willing to contribute financially to our efforts as the Government through a dedicated tax or users fee? So if you have recommendations that have not been mentioned, would you comment on those and let us know how we can pay, how you can help us to be able to bring these recommendations to fruition. Let's start with Mr. Holleyman.

Mr. HOLLEYMAN. Madam Chairwoman, I think the question for us is how do we drive more American jobs through protecting IP here and abroad. I think that companies in BSA are spending tens of millions of dollars a year independently and through organizations like BSA to do this. I think that a tax to cover this could be misused in other markets as a subterfuge for diverting resources into funds that were not focused on IP enforcement.

So I don't think the tax mechanism, certainly in the current climate, is the way to do it. I think it is a will. I think it is getting the new people in place who are now getting in place, and the support of this Congress to ensure that agencies understand this is an issue of American jobs and American innovation.

Mr. VARGO. Madam Chairwoman, American manufacturing is already the most heavily taxed in the world. That's one of the major problems that we face, along with theft of intellectual property. So I would not see this as a way to go ahead. But there is so much more the Government can do, both through coordination and through the trade agreements.

Mr. Bilbray mentioned Panama. He is exactly right. The NAM likes these trade agreements because we have a manufactured goods trade surplus. We think NAFTA, CAFTA, Australia, and the rest together, last year we sold \$21 billion more in manufactured goods than we bought, so we need more of these. The Government can do more to advance these. Every day that the Colombia, Panama, and other agreements languish costs us jobs. It costs us revenues.

Enforcement of trade agreements, this administration is doing a good job with accelerating that.

Ms. WATSON. Mr. Toohey.

Mr. TOOHEY. Well, as has already been stated, innovation is critical to the future of this country, and protecting innovation ought to be a core function of what the U.S. Government does. I think in some cases countries around the world think differently about intellectual property. Intellectual property is the only right contained in the main body of the U.S. Constitution. Article I, Clause VIII, Section VIII, it is the only right. We have it so much in the soul

of our country, which allows us to really lead in innovation, and many countries around the world simply don't share that view.

We as the pharmaceutical industry have worked proactively and in many cases with partnerships with organizations like PTO and the State Department to train judges in Latin America, to train patent examiners in China, to build that capacity. I think it is a cooperation that we need to do more of, and it is the right type of capacity building that we are engaged in. But protecting innovation ought to be a core function of the U.S. Government.

Ms. WATSON. Mr. Bilbray.

Mr. BILBRAY. Yes. I appreciate your bringing that up, because I think that is one thing we don't teach our children or our Members of Congress enough, about the intellectual property issue, that everything that we looked at what happened after 1800 in this country and how we basically moved on and beyond our mother country, which was the industrial base, countries like Germany and Britain had a big head start.

But intellectual property allowed us to evolve. That's where we did get the Carnegies. That's where we did get new processing for creating steel. That's where the railroad systems were totally renovated by the Americans. That's where the automobile was evolved. All of the prosperity that we see in capitalism we have to understand was based on the fact that intellectual property protection, that Government's place in this great economic boom was to protect those intellectual properties so that there was the return for the investment in developing these new concepts.

I think we grossly underestimate that, and I am glad you brought up the fact that before there was the Bill of Rights, before we articulated the rights of individuals to do and speak and possess certain things, the right to possess and protection your intellectual property was in our Constitution before all those other rights were enumerated, and that is an essential thing that we don't articulate enough either in our classrooms or in the halls of Congress.

Thank you very much.

Ms. WATSON. And Mr. Glickman, we are going to give you the final word. Since you represent an industry in my District, we will give you the final word.

Mr. GLICKMAN. I just concur with what my colleagues have said. This is a matter that affects the general economy of the country, so I think that if we go down the road of doing special assessments and special taxes for issues that affect—

Ms. WATSON. Or user fees.

Mr. GLICKMAN. Or even user fees for items that affect the country as a whole, then, you know, you could probably fund the Government just by nothing else but special assessments, special user fees. So I think the question here is resources, but it is also a question of will. It is also a question of commitment.

What is so great about your hearing today is that the message that is being shouted out from you all is that we need to sustain this will to take this problem on, and I can tell you from an industry's perspective we are getting our act together, without question.

Ms. WATSON. I appreciate that.

I just want all of you in the audience to know this is a very critical issue, and this won't be the last hearing, as I mentioned before. We are going to followup. We want to know what is being done in Government. We have a theory of pay-go, and we have a huge debt. China becomes the central focus, Mr. Vargo, as you mentioned among your three Cs, politically. We need their assistance in dealing with North Korea and so on, the largest nation in population on the globe, and so it presents some unique challenges to us.

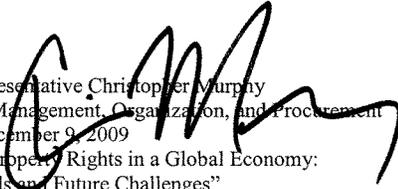
But we are on it. The political will is there. We are going to continue to pursue it until we get some resolutions that are workable.

With that, thank you for your testimony panel two. Thank you for the audience being here. We will adjourn the meeting.

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

[The prepared statement of Hon. Christopher S. Murphy follows:]

Statement by Representative Christopher Murphy
Subcommittee on Government Management, Organization, and Procurement
December 9, 2009
"Protecting Intellectual Property Rights in a Global Economy:
Current Trends and Future Challenges"



Chairman Watson, thank you for holding today's hearing on an issue of critical importance to the viability of our nation's most innovative businesses and job creators. As we work to turn around this economy, it's important that we recognize that part of this turn around will be assisted by protecting the intellectual property and proprietary content of American businesses.

No matter where Members hail from – California to Connecticut, Tennessee to New Hampshire – we represent businesses that are investing billions of dollars in creating the next big breakthrough in their respective industry and can only justify these investments if they have some assurance that the intellectual property derived years of work won't be stolen before they realize some gain from that work. Even more critically, the theft of our nation's intellectual property has the potential to stifle job creation and critically harm some of industries that America has historically lead the world in.

I know that the panels assembled here today can provide great insight on where we are today in our ability to enforce current law and the sufficiency of those laws. I am most interested to understand from both our government and private sector witnesses, what additional tools you believe are necessary to help fight this battle.

Most importantly, I would like to hear about our efforts to crack down on the hosting of pirated content in overseas locations with, in many cases, the complicity of foreign governments. I recently had the opportunity to meet with representatives from Paramount Pictures – and I believe Chairman Watson will appreciate this – regarding the speed at which their most recent release of Star Trek was pirated and sent all over the world via the internet.

According to Paramount, the movie was theatrically released on May 6th domestically and May 8th internationally. On May 8th, the same day it was released, a pirated version of the movie was available on DVD and the internet. They believe the first pirated copy came from Russia followed by copies, within days, from the Philippines, Ukraine, Spain, and Germany. By August, over 5 million illegal downloaded copies of the film had been made. Most of the downloads were made from sites hosted overseas.

This is only one example in the myriad of examples that can be sighted and I look forward to hearing from today's witnesses on how to continue to combat this growing problem. I yield back the balance of my time.