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FULL COMMITTEE HEARING ON THE IMPACT OF INTELLECTUAL PROPERTY ON ENTREPRENEURSHIP AND JOB CREATION

HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES
HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

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FULL COMMITTEE HEARING ON THE IMPACT OF INTELLECTUAL PROPERTY ON ENTREPRENEURSHIP AND JOB CREATION

Wednesday, July 21, 2010

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The Committee met, pursuant to call, at 1:00 p.m., in Room 2360 Rayburn House Office Building, Hon. Nydia Velázquez [chairwoman of the Committee] presiding.

Present: Representatives Velázquez, Moore, Dahlkemper, Lipinski, Graves, Bartlett, Luetkemeyer and Thompson.

Chairwoman VELÁZQUEZ. This hearing is now called to order.

Many of our most successful ventures in America started as a note on a napkin, or a dream by an entrepreneur. When these ideas blossom into new products and services, they create jobs, a critical component of any economic recovery. The success of these new ventures requires a system that effectively protects entrepreneur's ideas from being unfairly copied and stolen. Businesses that develop new products need assurances that the economic value of their innovations will be maintained.

At the same time, we must insure the rules are workable. If they are overly restrictive, companies that help entrepreneurs reach global markets will see their growth curtail. Technological entrepreneurs want to know that innovations like TiVo And Slingbox are not hindered, as we seek to protect content creator's rights.

Because of our entrepreneur's productivity, the United States is an unparalleled global leader when it comes to new ideas. In fact, more than 18 million Americans work in industries with an intellectual property focus. This includes industries where small firms are independent television and movie producers, video game designers, some writers, and manufacturers. Collectively, these and other industries make U.S. intellectual property worth $5.5 trillion operating in hundreds of thousands of small businesses.

Just as the concept of intellectual property touches many economic sectors, preserving it requires diverse approaches. The Administration recently announced plans to bolster protection of American business interests. The private sector has played, and will continue to play, an equally important role in protecting intellectual property. Those efforts will be highlighted today, as we look at the proactive efforts to meet small business needs.

As the Internet continues to evolve, we see a cross section of businesses who can help reserve U.S. ideas. The advent of e-Com-

merce has been a boom to many small businesses. It has also allowed artists and more producers to rapidly disseminate music and video content, while reaching new audiences. But the Internet has also created opportunities for piracy.

To assist U.S. companies in the Internet age, content owners are taking several steps. They are engaging in consumer outreach and education, and, where necessary, taking legal action against infringers. Others are collaborating with video and social networking portals to distribute their product.

In the end, the innovation of entrepreneurs is directly tied with the confidence that their ideas will not be stolen. Today's hearing will examine how the system for protecting intellectual property can spur job growth, and foster innovation. During every previous recession, the creativity of America's entrepreneurs has led us back to prosperity. That will be the same again, today.

I thank all of our witnesses for taking time out of your busy schedule to be here with us to provide your insight into this very important issue. And with that, I yield to the Ranking Member, Mr. Graves, for his opening statement.

[The prepared statement of Chairwoman Velázquez is included in the appendix.]

Mr. GRAVES. Thank you, Madam Chair, and thank you for holding this hearing on intellectual property, and my thanks to the witnesses also for being here. I look forward to hearing your testimony.

On average, intellectual property represents about 70 percent of a business' value, which is a significant increase from the past. However, many small businesses assume or don't understand that intellectual property issues affect them just as much as it does their larger counterparts.

The reality is that small businesses have a significant amount to gain or lose when it comes to intellectual property protection. Intellectual property laws in the United States are designed to protect a company's ideas. And it's typically the most valued asset a company usually has to offer. Whether it's a name, or a logo, or software, videos, new inventions, or literature, laws are in place to protect them. Taking full advantage of U.S. Intellectual Property laws helps small businesses, and gives them a better opportunity to be successful, and create businesses, or create jobs.

Protecting intellectual property is critical to our economy, jobs, and consumers. A violation of Intellectual Property laws directly affects a company's brand, its market share, its bottom line, its ability to export, and creates a number of safety concerns for consumers. It's very easy to see the trickle down effect that this has on an economy. And it's important that the United States maintains an aggressive strategy for protecting these highly valued assets.

U.S. Customs and Border Protection have seen seizures of counterfeited and pirated goods increase over the past few years. And if there's one bad actor, there's usually many more hiding. The Administration needs to take, and must take a hard line approach to fighting intellectual property violations, both domestically, and internationally. The economic consequences are too strong to ig-

nore. And, additionally, engaging the world in a more open trade will bring greater transparency to the seedy underworld of counterfeit goods, and help reduce these threats to our economy, while improving consumer safety.

Again, Madam Chairman, I want to thank you for holding this hearing, and I'm looking forward to our witnesses.

[The prepared statement of Mr. Graves is included in the appendix.]

Chairwoman VELÁZQUEZ. Thank you.

The Chair recognizes the gentlemen from Illinois for a unanimous consent request.

Mr. LIPINSKI. Thank you, Madam Chairwoman. I want to thank you for holding this hearing, and Ranking Member Graves for holding this hearing.

I want to ask unanimous consent to insert an opening statement for the record, look forward to hearing from the witnesses. And I consider South Bend to be part of the Chicago area, since you're going to have Mr. Mansfield here from ABRO Industries with us.

[The prepared statement of Mr. Lipinski is included in the appendix.]

Chairwoman VELÁZQUEZ. Hearing no objections, so ordered.

The gentleman is recognized. No? Okay.

The Chair now will introduce Mr. Robert Holleyman. He is the President and CEO of the Business Software Alliance. Mr. Holleyman has headed the Alliance since 1990, overseeing its BSA operations in more than 85 countries. BSA is the largest software industry trade organization, working with international governments to advance the industry's goal.

The gentleman has five minutes to make his presentation. Welcome.

STATEMENT OF ROBERT HOLLEYMAN

Mr. HOLLEYMAN. Madam Chairwoman, Ranking Member Graves, thank you for inviting the Business Software Alliance to testify.

Small business is an integral part of the success of the software industry. 97 percent of the software firms in this country are small businesses, three-quarters of the software firms in America have fewer than 20 employees, and we believe that the success of these businesses is an integral part of the entrepreneurial spirit, as well as the economic leadership of this country.

America's copyright industries lead the world, and that's a great thing for us to be excited about. And the software industry is, by far, the largest of the copyright industries. Software and related services sector employs more than 2 million Americans at jobs that are twice the national average wage, and the software industry contributes a $37 billion positive trade surplus for the U.S.

All software companies partner, as well, with resellers, integrators, and other software developers, most of which are small businesses. For example, Apple, a BSA member, provides technology and tools for developers, including more than 43,000 partners who have created software for the iPhone and iPad. These developers

are overwhelmingly small businesses and individuals, and have earned more than $1 billion from App Store sales to date.

Symantec, and Microsoft, and other BSA members have partner programs for thousands of small businesses. Microsoft, for example, has 640,000 partners in its network, and about 15,000 of those were here in Washington last week for a partner conference at the Convention Center.

This entire software industry is built on the foundation of intellectual property protection, and that is rooted in our Constitution. But our industry faces a substantial problem from software theft. In the U.S., one in five PC applications installed last year were stolen, and we have the lowest percentage rate of software piracy in the world here in the U.S. Many countries have much higher rates. For example, China has a rate of software piracy of 79 percent.

Now, small developers are particularly threatened by software theft. They often lack the resources to fight infringement, and they have fewer product lines across which to spread the risk. But the economic harm from illegal software use goes far beyond the software industry. And, indeed, this is the untold story.

Most software theft occurs when an otherwise legal business makes illegal copies of software for their workplace. This gives them an unfair cost advantage, because software is a critical tool of production. And these businesses compete unfairly with companies, large and small, across all sectors of the economy that respect the law. So, internationally, while most businesses in high piracy countries like China, steal the software they use to run their companies. The vast majority of their U.S. competitors pay for their software, as they should.

Simply put, overseas producers from high piracy markets compete unfairly with U.S. companies, undermining the sales of U.S. goods, and displacing American jobs.

In conclusion, I would like to congratulate Congress and the Administration on the release of the first Joint Strategic Plan on IP Enforcement. One month ago today, Vice President Biden unveiled this plan with Victoria Espinel, the first ever U.S. IP Enforcement Coordinator. Her office, and the Strategic Plan, itself, were mandated by Congress in the bipartisan Pro IP Act of 2008.

The Plan calls for specific actions, including promoting enforcement of IP overseas, improving coordination among law enforcement resources in this country, and serving as a model for the rest of the world by insuring that government agencies, and federal contractors manage and protect IP assets in the workplace.

I urge this Committee and Congress to insure robust implementation of this plan, particularly as it pertains to small business. U.S. leadership in software depends on the success of small business, and that hinges on effective protection of IP for everyone.

Thank you for the opportunity to testify.

[The prepared statement of Mr. Holleyman is included in the appendix.]

Chairwoman VELÁZQUEZ. Thank you, Mr. Holleyman.

Our next witness is Mr. Rick Carnes. He is the President of the Songwriters Guild of America, located in Nashville, Tennessee. Mr. Carnes is a working songwriter who has co-written number one

songs for Reba McEntire, "I Cannot Even Get The Blues," and Garth Brooks, "Longneck Bottle." The Songwriters Guild was formed as the Songwriters Protective Association in 1931, and promotes the profession of songwriting. Welcome.

STATEMENT OF RICK CARNES

Mr. RICK CARNES. Thank you so much, Chairwoman Velázquez, and Ranking Member Graves for the opportunity to testify on the impact of intellectual property on entrepreneurship and job creation. I would also like to take a moment to thank Fred Cannon of BMI, and Cindi Tripodi of the Copyright Alliance for their assistance in alerting me to this hearing.

My name is Rick Carnes, and I'm President oft he Songwriters Guild of America. The SGA is the nation's oldest and largest organization run exclusively by and for songwriters. I am a professional songwriter living and working in Nashville, Tennessee since 1978. While I've been fortunate enough to have a modicum of success in my career writing number one songs for both Garth Brooks and Reba McEntire, along with songs recorded by Dean Martin, Steve Wariner, Alabama, Pam Tillis, Conway Twitty, among others, I'm constantly reminded of the perilous existence of all of us who have chosen songwriting as a profession.

Critical for this Committee is the fact that professional songwriters are not employees. We are self-employed small business people, and the songs we write produce jobs everywhere you look. Practically everything in this country is sold with music. Examples abound, just turn on the TV and listen to the car commercials. Every restaurant provides music with your meals. Fashion follows music, sporting events have music, technology is tied at the hip to music. The iPad and the iPhone, and practically everything else that starts with an 'i' delivers and plays music. Can anyone deny the resurgence of Apple computers was tied directly to the iPod, and iTunes as a music delivery service? Search engines sell huge amounts of advertising on searches for songs. And music file downloading was and is a major driver in the adoption of broadband Internet service.

Songwriters' jobs are valuable to the economy, and totally green. No smoke stacks or heavy infrastructure costs are needed for song creation. The only resource we depleted is pencil erasers, and the only thing we spill is coffee.

Every single job in the music industry springs from a hit song. Unlike recording artists, songwriters don't make money from live shows, or selling merchandise, because we don't perform. And, frankly, we're not that pretty. We're the folks who sit in a room along with a guitar, and a blank page, and a burning desire to tell our story through music.

As professional songwriters, we make all of our money from copyrights. The income from those copyrights come primarily from two sources, CD sales, and if we're lucky enough to get a single, we get performance money when the song is played on radio or TV. But songwriting as a profession is vanishing.

Songwriters can no longer depend on record sales for a major part of their income in a market where it is estimated that 20 songs are stolen on line for every song that's sold. The music pub-

lishers are not contracting staff songwriters any more. It's too risky to advance money for songs in a market that doesn't protect those songs from theft.

The last music publisher I signed with had 12 professional songwriters on staff in 1998, the year of Napster. By 2008, they had let go of all of their staff writers, including myself and my wife.

We need to establish new business models for digital music delivery that will insure the protection of copyrighted songs, while giving consumers a great experience with music at a fair price. Unfortunately, it is very difficult to establish those business models, when the entrepreneurs we need to fund those ventures have to compete in a marketplace glutted with stolen music.

It is the hope of songwriters everywhere that technological innovation will help find a solution to the problem of music piracy. In that regard, the SGA supports the development of high performance content delivery networks that could give consumers a better, safer experience in accessing music on line. In this way, we might be able to compete with the virus ridden, poor quality, illegal copies of copyrighted songs you so often find on peer-to-peer services.

In closing, let me recount an experience that is happening all too often to me with my discussion with songwriters today. I met a legendary country song writer in a coffee shop last month in Nashville, and he told me he's now selling ammunition at gun shows instead of writing songs. When I asked him if he was ever going to start writing again, he said, and I quote, "Why bother?"There will always be people who are moved by the muse to write the occasional song, but without a way to sell their music and make a living, the professional songwriters that made American music the envy of the world, will pursue other jobs that pay a liveable wage, jobs where their work and their rights are respected, and protected.

In conclusion, Ms. Chairwoman, and members of the Committee, SGA truly appreciates your efforts on behalf of small business people like us. We look forward to working with you to enliven job creation in the music industry through the protection of intellectual property rights, and the encouragement of technological innovation in the delivery of music. SGA and I stand ready to be a part of that effort. Thank you so much.

[The prepared statement of Rick Carnes is included in the appendix.]

Chairwoman VELÁZQUEZ. Thank you, Mr. Carnes.

Our next witness is Mr. Steven Friedman. He is the President of T3 Technologies located in Tampa, Florida. T3 Technologies has provided main frame computer solutions to the small and medium-size business community since 1992. Mr. Friedman is testifying on behalf of Computer and Communications Industry Association, representing companies in the computer, Internet, information technology, and telecommunications industries. Welcome.

STATEMENT OF STEVEN FRIEDMAN

Mr. FRIEDMAN. Thank you, and good afternoon, Chairwoman Velázquez, Ranking Member Graves, and members of the Small Business Committee. First, I want to thank you for allowing me to

tell my story here today. I've been a small business owner for 19 years, and it's a label that I'm very proud to wear.

Let me say, first, that I do not disagree that intellectual property can be of great help to small businesses in commercializing their ideas. However, my recent experiences have proven to me that the current IP system is a bit out of balance, and that our imbalanced Intellectual Property laws actually hinder innovation, disproportionately so for small businesses.

This reality was recognized recently by Justice Stevens in one of his final Supreme Court opinions in Bilski v. Kappos, in which he wrote, and I'm quoting, "Even if a patent is ultimately held invalid, patent holders may be able to use it to threaten litigation, and to bully competitors, especially those that cannot bear the costs of a drawn out, fact- intensive patent litigation. That can take a particular toll on small and upstart businesses."

I, personally, hear a lot of talk about intellectual property and its importance to small business, but from where I sit, IP is really just a complicated regulatory system. This regulation of knowledge and ideas has expanded into many areas of our economy. AS with any regulation, big business figures out the best ways to navigate the system, while the little guys who don't have the high priced legal teams at their disposal get tied up with paperwork and lawsuits, or simply eliminate innovative ideas from their plans in order to avoid such paperwork and lawsuits.

My story is fairly technical and complicated, but the lesson is simple; intellectual property can be as much a danger to small business as it is a benefit. A large firm can use the current Intellectual Property laws to effectively put smaller rivals that threaten its bottom line out of business.

Let me first briefly explain the market I'm in. Until recently, my company built computer systems that were capable of running IBM's mainframe operating system, similar to the way Dell and HP build systems that run Windows. Although some people are unfamiliar with mainframes, or may think them as relics, in reality, they power much of the world that we live in today. They are the computing power behind ATMs, health care records, global stock markets, the Social Security Administration, just to name a few, and 70 percent of the world's government and corporate data is stored on mainframes. It's estimated up to $5 trillion in business assets reside on these systems. My small company sold such mainframe systems to Fortune 500 businesses, the U.S. military, NATO, and a large number of city and county governments.

I employed over 50 people who served nearly 1,000 customers in 28 countries selling our mainframe solutions to former IBM customers who needed lowers power mainframes, because, quite simply, not everyone needs a Ferrari. This was a profitable niche for us, and we quickly became a "go to" company for businesses that needed cost- effective mainframes.

One of the reasons we got into this business was in 1999, IBM had stopped selling these smaller mainframes that we sold. With no competitors left in the field, they simply were able to scale down their larger systems, and charge what we felt were monopoly rents to these smaller users. Seeing this as an opportunity for our little company, we licensed a new technology from a company called

Platform Solutions, a California-based small business, whose product allows less expensive hardware to run IBM's mainframe operating system. As a result, I could compete with IBM by selling much more affordable mainframe machines to my customers.

Thanks to a well-known Department of Justice Consent Decree that lasted for decades, and it compelled IBM to license their mainframe operating system to all comers on reasonable and non-discriminatory terms. This is what permitted a small startup company like Amdahl to innovate and excel in the market in the 1980s and 1990s. The continuation of this practice was a basic assumption in our decision to develop our products.

However, in 2003, IBM was released from this Consent Decree. Almost immediately, they began putting up obstacles to T3 and our customers who wished to license this operating system. This culminated on October 31st, 2006, when IBM publicly announced they would no longer license their patented operating system to any hardware except their own. Imagine, if you will, if Microsoft one day announced that they were building their own PCs, and that Windows would only be sold on those machines.

To make matters worse, they then sued my business partner and I for alleged intellectual property violations. The court process has taken three years, cost millions of dollars, and is still not over. To make matters worse, IBM has since purchased PSI and shelved its technology. And now, almost incredibly, in civil court, IBM hides behind Intellectual Property laws claiming that they permit otherwise forbidden monopolistic behavior, essentially saying that Intellectual Property laws trump Antitrust laws.

Chairwoman VELÁZQUEZ. Time is expired. Can you sum it up?

Mr. FRIEDMAN. Yes. Absolutely.

Chairwoman VELÁZQUEZ. Because votes are happening right now.

Mr. FRIEDMAN. Okay. Although I can afford no cure-alls, I do implore you to think beyond bumper sticker slogans, and think through the whole process, and the unintended consequences of these laws. And I thank you for your time, and look forward to answering any questions.

[The prepared statement of Steven Friedman is included in the appendix.]

Chairwoman VELÁZQUEZ. Okay. The Committee will stand in recess until we finish voting on the House floor. Thank you.

[Recess.]

Chairwoman VELÁZQUEZ. The Committee is called back to order. Sorry for the time that we spent on the House floor.

It is my pleasure to introduce Mr. Peter Carnes, and he is not related to Mr. Rick Carnes. And he is the CEO of Traffax, Incorporated located in Silver Spring, Maryland. Traffax is a startup that measures traffic flows through the use of Bluetooth Wireless signal. Mr. Carnes is testifying on behalf of the Association for Competitive Technology, representing more than 3,000 technology firms.

Welcome.

STATEMENT OF PETER CARNES

Mr. PETER CARNES. Thank you. Chairwoman Velázquez, Ranking Member Graves, and well, there were distinguished members of the Committee here before, but I'm sure that they'll be able to review this by—

Chairwoman VELÁZQUEZ. They will be coming back.

Mr. PETER CARNES. Right. So, my name is Peter Carnes. I'd like to thank you for holding this important hearing on the role that intellectual property plays in driving innovation and creating economic growth. And, most importantly, new jobs.

I am the Chief Executive Office of Traffax, Inc., a transportation monitoring equipment startup in College Park, Maryland. Traffax was a May 2008 winner in the University of Maryland's Maryland Technology Enterprise Institute business plan competition, and we, as you said, design equipment and systems to measure the flow of traffic, both pedestrian and vehicular traffic. We use a technology that detects and monitors electronic signals from end-use electronic devices. The technology is accurate, it's inexpensive to deploy, and it operates while protecting people's privacy, which is a significant improvement, and overcomes some disadvantages found in some existing technologies.

While we are US-based, traffic is a global problem, and Traffax' equipment is also currently being used in Canada, England, Australia, and Brazil. We're many conversations with other European countries. We have a whopping seven employees, and we've managed to extend our reach of our equipment to these particular areas. And the way that we've been able to do that is, obviously, we've been able to attract good partners, but it's the value of our idea, and the ability to solve an apparent problem that has really helped us expand beyond Maryland, and beyond the U.S., into other parts of the world.

In today's global world, innovation serves as the linchpin for creating future jobs, solutions to modern problems, and maintaining technological leadership. When I go to work everyday, I have a very unique opportunity. I have the opportunity to fail, and I do it over, and over, and over until I find a solution. Most people when they go to work, they need success, and they need it all the time, so they cannot push the envelope. In my job, I'm supposed to make sure things change. I'm supposed to focus on problems, and make sure that they get solved. And that's a tremendous benefit, but it is a high-risk way to live your life. And the reason that that works is because that there is the potential for there to be high reward when you solve a real problem, and you find a creative solution.

So, to do that, you've got to integrate IP culture into all stages of your innovation process to be able to protect the work that you do. So, you have to treat IP holistically within your business, you have to view it as copyright, trademark, relationships that you make, and, obviously, patent protections. You have to reward employees that help you create IP.

So, we view IP as America's way forward. And according to the 2007 report by the Information Technology and Innovation Foundation, IT, Information Technology, adds $2 trillion annually to the U.S. economy, and is responsible for nearly all of the pickup in economic growth over the last decade. And when you look at the peo-

ple's day-to-day work, that translates to increases in productivity. That increase in productivity comes from IT. For IT to work, it requires its own fuel, which is intellectual property, or the right to benefit from your idea.

There's, essentially, three roadblocks that I identified for building IP culture, the time it takes the USPTO to process a patent, the uncertainty of IP protection in overseas markets, and the lack of funding options from banks and SBA for companies that create IP. Small technology companies like mine, we do not buy buildings, we do not buy furniture, we do not buy trucks, we often don't even buy computers. We use our money to pay engineers, and software developers, and marketing people, and sales people to create a new idea, create a message, and get it out. And we have a very difficult time with funding unless we can point to IP as something that will help an investor value their return.

So, we would like for you to do the work that you do, and we recognize that it's quite difficult, but we believe that the USPTO needs some help, and they need to be able to use the money that they collect, that we pay them in fees, so we ask you to pass the USPTO budget request. We want you to continue to do what you can to help protect IP globally, both focusing on bad actors, but trying to achieve harmonization with our closer friends, as well. And then whatever work could be done to help the SBA recognize that all small businesses aren't delis, they aren't gas stations, some of them have the same kind of technology problems that IBM, and Google, and Apple, and eBay have. Thank you.

[The prepared statement of Peter Carnes is included in the appendix.]

Chairwoman VELÁZQUEZ. Thank you, Mr. Carnes.

The Chair recognizes the Ranking Member for the purposes of introducing our next witness.

Mr. GRAVES. Thank you, Madam Chairwoman.

Our next witness is Mr. William Mansfield. He's the Director of Intellectual Property at ABRO Industries in South Bend, Indiana. ABRO Industries was founded in 1939, and currently manufactures and distributes industrial, automotive, and consumer products. Mr. Mansfield is testifying on behalf of the Motor & Equipment Manufacturers Association. Welcome.

STATEMENT OF WILLIAM MANSFIELD

Mr. MANSFIELD. Madam Chairwoman, Ranking Member Graves, and other distinguished members of the Small Business Committee, thank you for the opportunity to testify before you today on the impact of intellectual property on entrepreneurship and job creation. My name is William Mansfield, Director of Intellectual Property for ABRO Industries, Incorporated.

I am here representing the Motor & Equipment Manufacturers Association and ABRO. The Motor & Equipment Manufacturers Association, or MEMA, represents nearly 700 companies that manufacture motor vehicle parts for use in the light vehicle and heavy-duty original equipment, and after-market industries. Motor vehicle parts suppliers are the nation's largest manufacturing sector,

directly employing over 685,000 U.S. workers, and contributing to over 3.2 million jobs across the country.

ABRO Industries Incorporated is a small after-market supplier headquartered in South Bend, Indiana. Now, if you never heard of ABRO Industries before, do not feel bad. Virtually, no American has. ABRO operates in a manner once common in America, but which is now almost unheard of. ABRO has a variety of automotive hardware and basic consumer goods, such as radiator fluid, glues, and masking tape, manufactured in America under the ABRO brand name.

We sell those items exclusively overseas, mostly in developing nations. We do not sell any items in the United States. We have spent decades building the ABRO brand name into a reliable identifier of high-quality goods. ABRO greatly values its name, which is registered in multiple categories in over 160 nations.

Because ABRO faces counterfeiters all around the world, I run ABRO's very aggressive Anti-Counterfeiting program, and I fought counterfeiters on six continents. And I'm always looking for a case in Antarctica, as well, on ABRO's behalf.

The magnitude of global counterfeiting is significant. International IP protection is about much more than Hollywood, or luxury goods, though both will always be an important component of the battle. IP protection is also about safety of a wide variety of consumer products, such as pharmaceuticals, and motor vehicle parts.

Counterfeit parts and components for motor vehicles pose a critical problem to the American economy, and the supplier industry. MEMA conservatively estimates that counterfeit goods cost motor vehicle suppliers at least $3 billion in the United States, and $12 billion globally in lost sales. And while protecting intellectual property is important for major multinational corporations, I would argue that IP is extremely critical for small businesses like ABRO, which has only 24 employees, because a single incident could force a company out of business. A giant corporation can recover from a hit to its reputation, a small company does not have this ability. If counterfeiters have managed to undermine their brand name by selling low-quality and/or defective products under that name, they can easily be permanently damaged, or even destroyed.

Now, it is common to blame all counterfeiting on China, and this is, of course, not the case. Counterfeits are also made in India, Russia, and other countries. We at ABRO have been able to work with the Chinese government in enforcing our intellectual property, and they have pursued counterfeiters when our company presented credible evidence of our trademark being violated.

There's a wide range of counterfeit parts and components for vehicles that are manufactured and distributed globally, which may result in catastrophic vehicle systems malfunctions, endangering the car or heavy-duty truck driver operating the vehicle, and all motorists traveling the same road.

Trademark or brand infringement is the most immediate problem faced by many motor vehicle suppliers. Pirates also copy trade dress or the unique appearance of product packaging. Often they do not make perfect copies, instead making the packaging confusingly similar. To demonstrate, I have three cans of spray paint, a

genuine ABRO product, and products labeled AMBRO and ARVO. This example shows how hard it can be for the average consumer to distinguish between an authentic and a counterfeit good.

MEMA supports the recent Intellectual Property Enforcement Coordinator's Joint Strategic Plan, which is the first ever plan to include a roadmap on how to address challenges of counterfeiting, and piracy of American IP. Additional resources are necessary to fully implement the plan, which will improve our nation's ability to combat counterfeiting and piracy.

Our country must promote and defend a robust international system of IP laws and norms, while strengthening cooperation with like- minded countries, and key trading partners to promote shared IP protection. Congress should authorize additional resources for CBP and ICE to enforce intellectual property laws at our borders, and support comprehensive robust anti- counterfeiting trade agreements.

Finally, Congress should consider expanding the IP Attache program. These contacts have generally assisted my company in understanding local anti-counterfeiting procedures, gaining access to key foreign government personnel, and obtaining the necessary resources to fight counterfeiting in other nations.

Madam Chairwoman, thank you again for the opportunity to testify today.

[The prepared statement of William Mansfield is included in the appendix.]

Chairwoman VELÁZQUEZ. Thank you, Mr. Mansfield.

If I may, I would like to address my first question to Mr. Holleyman.

Two years ago, your Association released a study on the impact of piracy. Can you tell the Committee since that study was released, how effective your industry has been in addressing the problem of piracy in software industry? And how does this issue post obstacle for small firms?

Mr. HOLLEYMAN. Thank you for that question. Each year we work with ITC, which is one of the leading technology research firms to try to quantify the impact of piracy, not just on U.S. companies, or not just on our members, but globally.

Over the past two years, we've seen two trends happen. One is that the overall global rates as a percentage of piracy are going up, and that is because large markets like China, Brazil, the BRIC markets, who have higher rates of piracy on average than the global average, they're becoming so important in terms of sales of PCs, that the sales of legal software are lagging behind, that they're driving overall global rates up.

At the same time, because of the progress in many countries, and also, candidly, because of the economic environment last year, the dollar loss due to piracy has stayed sort of roughly the same over the last couple of years. But it's about $51 billion a year lost due to piracy, and when I'm sort of challenged, how could that possibly be the case? Well, that's the commercial value of pirated software estimated to have been put into use. And if you look at the fact that the packaged software industry is a $300 billion a year indus-

try, it's not a surprise to see that there could be as much as $51 billion in pirated value with the marketplace.

Chairwoman VELÁZQUEZ. Thank you.

Mr. Friedman, I recognize that litigation can have a crippling effect on small businesses. It also creates the prospect of unknown costs. How are your business decisions, including those on R&D spending and hiring impacted by this uncertainty?

Mr. FRIEDMAN. Certainly, what has happened to us in the last few years has put us on guard to be a little more wary than we might ordinarily have been in terms of our hiring and our R&D. We are also, however, extremely aware and cognizant of the importance of IP, especially in the technology field. And for a small company, as others here today have testified, it's a critical path to success to gain that intellectual property.

Our issue with it really is only how larger companies utilize IP to the detriment of smaller companies. But for ourselves, we feel it's a critical component to future success for small companies.

Chairwoman VELÁZQUEZ. Thank you.

Mr. Carnes, the music industry supports thousands of small businesses, from production-related activities. These includes firms ranging from marketing, to video production, to small recording studios. Can you discuss the direct and indirect effects of piracy on the industries that you deal with?

Mr. RICK CARNES. Well, as a songwriter, in my testimony I said all I produce is copyright. That's the only thing that I get paid on. But that copyright, like that hit song, is the thing that drives the entire business. I mean, if you get a hit song, you run into the studio and you demo it. Well, you immediately give jobs to studio musicians, to recording engineers, to the studio owners who are small business people. And then it goes to the record label. If they decide to record it, then they rerecord it. They make a master recording, so now you have more studio musicians, you have bigger recording studios. The budgets continue to increase. And then once it gets to the radio, then you have all the marketing people that go out and market the record. And then, of course, you have all the retail people that sell the record. And it continues up the chain. Then you have the advertising people that use the song for the purpose of selling other goods. And every one of these things adds—the value is all added on top of one copyright.

Absent that hit song, that whole process, it all starts with a song. Absent the song, it stops right there. If you don't have a hit song, that's it.

Chairwoman VELÁZQUEZ. Thanks.

Mr. Peter Carnes, the process of managing and protecting one's trademarks, patent rights, or copyrights can be very complex. And, in many cases, small firms do not know where to start, and maybe end up taking no action. So, can you talk to us about what proactive measures should a small business take to manage their intellectual property rights?

Mr. PETER CARNES. Yes, ma'am. Thank you.

First of all, I'd like to say that the USPTO actually does a very good job with regard to outreach, and trying to explain their process. It's not their job to tell you about the importance of IP, but

it is their job to explain to you how their process works. And I do think that they generally do a good job trying to do that.

I think that if you're in the technology business, you have some sense of make it once, and sell it many times. And once you overcome that original hurdle of an idea, then, typically, what happens is that you set aside some of your funding to engage with an attorney that practices Intellectual Property law. And often your investors will require you to do that.

So, I think that that system is actually pretty well, works pretty well as far as information goes. I think the problems with IP are not the information about how that it works, but the understanding of the timeliness and the effort that it will take.

One area that is a big issue, though, is your patent, if you are issued a patent in the U.S., it protects you in the U.S., so you must go out and seek protection in every market that you think is relevant to your technology. So, anything that could happen to help with harmonization would help you, especially as a small business, to only have to learn kind of the rules, the general rules instead of learning the specific rules for each place.

Chairwoman VELÁZQUEZ. Thank you.

Mr. Mansfield, you mentioned in your testimony that ABRO, that most Americans haven't heard about ABRO, because you don't sell any of the items here. Why is that?

Mr. MANSFIELD. Well, first, Madam Chairwoman, I'd like to echo Mr. Carnes' comment. I think the USPTO does an amazing job in outreach.

Chairwoman VELÁZQUEZ. That's good to hear.

Mr. MANSFIELD. And they're often not recognized for that, but they do very good work there.

ABRO's history has been about selling where "Made in America" has a strong competitive advantage. And in developing nations around the world, "Made in America" really means something, no matter if they're angry at us, they're mad at us, our political structure, anything, they trust our products, especially non-electronic consumer goods. So, we have just built up in a small niche where "Made in America" can really have an impact, especially after 30 years of consistently providing American-level quality non-electronic consumer goods.

Chairwoman VELÁZQUEZ. Okay. And just since you sell your products overseas, can you tell us what obstacles do you face when you do business in countries with limited protections of IP?

Mr. MANSFIELD. It certainly is true that the counterfeiters target countries where the protections are hard to get, or hard to enforce. They're pretty much any country now, especially with the Madrid Protocol, you can get trademarks, you can get the registration. But that is not the end of the fight, that's just the beginning.

In most countries, especially developing countries, you have to invest significantly and work to make sure your brand is protected there. In my work, I spend about 100 days a year on the road internationally physically going to the countries, meeting the key people, and learning what works there. And too often, Western brand owners assume that what works here, will work everywhere. There's always a way to protect intellectual property in every coun-

try. It's just not always our way. And you have to spend the time to learn the local way.

Chairwoman VELÁZQUEZ. Thank you.

Mr. Graves.

Mr. GRAVES. Thank you, Madam Chair.

My question is for each of you, and it's about trade agreements. And my curiosity is, when it comes to enforcement of intellectual property rights, how do—the trade agreements, at least the ones that we've passed recently, do they the protections you need? Do they go far enough? Just, in general, just I'd be very curious about that. Mr. Holleyman.

Mr. HOLLEYMAN. Sure, I'll start. I think that the trade agreements have been a huge factor behind the growth of the software industry, both the multilateral ones by WTO, including Intellectual Property provisions, but many of the Free Trade agreements have been quite specific in recent years in addressing the issue of software, insuring that governments were using only legal software, and trying to take steps to drive private sector use. So, they're important, and we think that IP components need to be a part of every trade agreement.

Mr. GRAVES. Mr. Carnes.

Mr. RICK CARNES. Well, certainly, when we harmonize treaties, like WIPO, and things like that, that helps, because you get—when you have some countries that have limited copyright protection, and other countries like the United States now has Life Plus 70, gets to be a problem, so it has positively impacted us, that we're harmonizing some of the laws.

Mr. GRAVES. Mr. Friedman.

Mr. FRIEDMAN. I will admit that I am not very well versed in the trade agreements. I can say that, historically, about one-third of our business has been overseas, primarily in Europe. The only restriction that we had was in our early days shipping some technology, or not shipping some technology to the former Soviet Union into Russia. So, I'm sorry, but I can't be too much help on this question, I don't think.

Mr. GRAVES. Mr. Carnes.

Mr. PETER CARNES. Yes, thank you. I, in general, feel very positive about the trade agreements, and the progress that has been made in that area. And I think that as a government, you tend to think about it at a macro level. As an individual, I tend to think about it as a micro level. And at the micro level, what I see happening in some of these countries is that the protection of IP is entering into the narrative. And I think in many parts of the world, and I've had the opportunity to visit China about 25 times, and I think that part of what we need to do is continue to focus on these things at the macro level to make sure that it enters into individual narrative, because in some parts of the world, I think their view of your rights around intellectual property are just fundamentally different than the U.S. right. So, I think that the focus of our government on these issues encourages discussion down at the working level. Thank you.

Mr. GRAVES. Mr. Mansfield.

Mr. MANSFIELD. I would once again agree with Mr. Carnes, who I've never met before today, but, apparently, we're very much in agreement.

I think the more America is involved with other countries in these trade agreements, the better Americans are able to function in those structures, and the more respect is given to intellectual property rights.

I would love to take this as a chance to, again—the IP Attache program, which currently exists, I think we have eight of them in our embassies, if that was expanded, I think we would have better protection, especially better protection for small businesses, who could then call upon that person as a local expert in the structure that they are now dealing with.

Mr. GRAVES. Thank you, Madam Chair.

Mr. LUETKEMEYER. Thank you, gentlemen, for being here today. I've got a couple of questions with regards to—I was talking with one of my Small Business people last week, and he was kind of frustrated with the process, to the point where he said—I asked him if he had his process patent, and he said, "No." He said, "One of the things that concerns me is the fact when you put the patent out there, it allows everybody to see what you just did, and all they have to do is tweak it just a little bit, so that they can go out and have their own patent on your own product."

Do you see something like that as a problem with your own particular areas of interest, any of you?

Mr. PETER CARNES. Yes. Obviously, that is a consideration that everybody has. Essentially, the patent process, you have—after 18 months, your patent is published at some point, and people can read it. And I think that you have to think about from the perspective of what is the patent system about. It is really about trying to drive innovation. So, if people are able to read your patent, and develop a significant leap forward, then the world needs that leap forward.

The big issue is whether people can just read your patent, and go out and copy your work. And the truth is, the time between when the patent is published, and when the patent is released, during that time you cannot do anything to discourage a potential competitor.

It used to be the time that you had published your patent, and your patent was issued was the time that you established your market leadership. And you traveled down the learning curve to get better at your technology before somebody else did. And right now, with the huge gap of time between when the patent is published, and when they're issued, you don't have that time to earn that market leadership anymore.

Mr. MANSFIELD. I'd also like to comment, if I could, sir.

Mr. LUETKEMEYER. Yes.

Mr. MANSFIELD. They have another option. Trade secrets exist specifically for that sort of concern. Coca Cola never published or patented its recipe, and it jealously guarded it, kept it secret, and it hasn't been duplicated. But going public is kind of part of the tradeoff of getting the protected period under a patent system.

Mr. LUETKEMEYER. Do you believe that existing laws are enforced adequately, both here in this country, and abroad, or are there problems in one place, or the other?

Mr. MANSFIELD. ABRO doesn't actually have any patents. I'm just-

Mr. LUETKEMEYER. Intellectual property either way.

Mr. MANSFIELD. I think it is getting better. It's far from perfect, but more and more there are tools that you can work with to protect your own intellectual property. So, by and large, I think we're improving yearly.

Mr. HOLLEYMAN. Congressman, I'll add to that. I certainly took heart from Mr. Mansfield's comments about the progress that his company has been making in markets like China. I have been working intellectual property issues there for almost two decades, and I do think that there is a level of understanding that, ultimately, intellectual property protection will be important to China. I think it's a question of when, and where will that be exercised. We work very closely with the Copyright Office in China, and their enforcement authorities, who are, by all accounts in my meetings, very diligent, hardworking, committed public citizens. But there are less than 20 people at the Central government in China working on copyright protection industries, and trademark industries for the whole of China. So, it's not a question of the ability or interest of certain people to do their jobs, but it's a question of a priority that's been placed.

So, in our case, where we have digital piracy largely within businesses, including state-owned enterprises, finding an effective remedy for enforcement, we're still a long way from that. And there are many other countries like that.

Mr. LUETKEMEYER. Okay, very quickly, my time is about to run out. I've got one question I would like each of you to answer very quickly, if you would.

With regards to, this is the Small Business Committee, and we're always interested in small business folks. Are the laws that deal with intellectual property, are they too cumbersome for our small businesses to work through, are they about right, do they need to be—are they too easy, they need to be enforced, or more layers need to be in it to help protection, or are we where we need to be, if you wouldn't mind each one commenting on that.

Mr. FRIEDMAN. If I may, thank you.

From our perspective, I think the laws are adequate, but in some cases lack clarity, in the case that—in our story that I talked about earlier. The nexus where intellectual property and antitrust meet, for example, there's lacking a lot of clarity of what has precedence in the case that I talked about this morning. And the situation of unintended consequences, where it actually enabled the monopolist to act in violation, we think, of antitrust laws. And, today, that company now has 100 percent market share in our marketplace.

Mr. HOLLEYMAN. I'll start by saying that for software companies, of which 97 percent of the firms in software in this country are small businesses, and globally, 60 cents of every dollar that's spent on software around the world comes back to a US-based company. I'm often asked when I travel what's the secret? Why does that happen? Why has the U.S. been so successful? And it's really—it's

part three things. One, sort of a culture of entrepreneurship, and risk-taking. Two, a good educational system, but it's no surprise that because we've had very strong intellectual property laws in this country, that is really what's allowed us to build a market here, and expand it internationally. And, to me, that is the secret sauce that's missing in most other countries. So, I think it works well for small business.

Mr. RICK CARNES. As a songwriter, I can say that in terms of interdicting physical counterfeited goods, pirated CDs and hard version, the government has done some good, with the CHIP program, with the FBI, the Intellectual Property Law Enforcement Commission, they're actually discussing this. But, by and large, the government has ignored the 800-pound gorilla in the room, which is intellectual property, songs being stolen on the Internet.

As an individual songwriter, there's no way in the world I can enforce my copyrights on line. I have to take literally hundreds of thousands of infringers into Federal Court, and reduce the case to a court of last resort, probably a quarter of a million dollars per every case. How can I possibly do that, when the people that are stealing my music are, by and large, 14 and 15-year old kids, who really, probably, stole it because they don't have a credit card. So, what do I do?

I mean, if the government doesn't actually come in and help enforce the copyright laws on the Internet, then what we need is to have the government help us with technological solutions that will keep the piracy from happening in the first place.

Mr. LUETKEMEYER. Very good. Thank you. Thank you, Madam Chair.

Chairwoman VELÁZQUEZ. So, Mr. Carnes, do you believe that there is a way to support new distribution methods, while insuring financial compensation to right holders?

Mr. RICK CARNES. I do think that there is a way. What we need to do is make sure that we allow for the development of premium content delivery networks, sort of, for lack of a better—it's a place where you can—like the Kindle from Amazon, you've got a side channel, you can just punch a button, bam, 60 seconds, you get the book that you want, smooth, easy transaction.

What we need are content delivery networks where you can get stutter-free movies, and high definition, fast, perfectly delivered copies. The only trouble is that that has run afoul of the Fifth Rule of Neutrality, which says that you can't discriminate on data on the Internet. Well, this is actually—I'm being discriminated against when you say that I can't take my content, and partner with an ISP to deliver premium content that's faster and better. So, I have a problem with the Fifth Rule of Network Neutrality, because of that.

If we could set up those delivery channels, that would help us give the consumer a better experience than they get on peer-to-peer file sharing.

Chairwoman VELÁZQUEZ. Mr. Holleyman, I know your organization has been supportive of the draft Anti-Counterfeiting Trade Agreement, so can you talk to us about what implications does this draft agreement have for small software companies?

Mr. HOLLEYMAN. Sure, thank you.

We have supported this agreement. There have—

chairwoman VELÁZQUEZ. Especially for those small companies looking to enter the foreign market.

Mr. HOLLEYMAN. Sure. At the heart of this proposed agreement, and it's still in negotiation, so we haven't seen what would be a final text, it would, one, not require any changes to U.S. law. And we have strong, effective intellectual property laws, not perfect, but they can be improved in enforcement, but strong laws. This calls upon our trading partners to increase their standards of protections in ways that will provide, like the U.S., effective tools against counterfeiting and piracy. So, we believe for small software companies, for whom there's a huge opportunity in foreign markets where piracy rates tend to be higher than in the U.S., that this agreement has the potential to really make progress in fighting piracy. Again, it's not final, but we're encouraged by what we've seen today.

Chairwoman VELÁZQUEZ. Do you see any will and desire from foreign countries to support this type of agreement? What will be the kind of benefit for them?

Mr. HOLLEYMAN. Well, I'll say two things. One, I'm encouraged by the fact that this agreement was initiated in the Bush Administration, reviewed very carefully by the Obama Administration before they took it on, so I view it as a distinct sort of across party lines, a real win-win for the U.S. There are a couple of key trading partners working on this together.

I mean, I think, ultimately, the test will be how many other countries when it's final can we get to join it? I mean, the verdict is still out on that. Again, the agreement is not final, but the intent, and the fact that it's shared across two administrations now is very important.

Chairwoman VELÁZQUEZ. Okay. Well, let me take this opportunity to thank all the witnesses. And we will continue to ask the Small Business Committees charged with making sure that the law of unintended consequences are not there when it comes to legislation that will impact small businesses, we will continue to monitor this issue. And I want to take this opportunity, again, to thank you for being here today.

I ask unanimous consent that members will have five days to submit a statement and supporting material for this record. Without objection, so ordered. This hearing is now adjourned. Thank you.

[Whereupon, at 3:06 p.m., the Committee was adjourned.]

NYDIA M. VELAZQUEZ, NEW YORK
CHAIRWOMAN

SAM GRAVES, MISSOURI
RANKING MEMBER

Congress of the United States
U.S. House of Representatives
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STATEMENT
Of the Honorable Nydia M. Velázquez, Chairwoman
United States House of Representatives, Committee on Small Business
Full Committee Hearing: *"The Impact of Intellectual Property on Entrepreneurship and Job Creation"*
Wednesday, July 21, 2010

Many of our most successful ventures in America started as a note on a napkin or a dream by an entrepreneur. When these ideas blossom into new products and services, they create jobs – a critical component of any economic recovery.

The success of these new ventures requires a system that effectively protects entrepreneurs' ideas from being unfairly copied and stolen. Businesses that develop new products need assurances that the economic value of their innovations will be maintained.

At the same time, we must ensure the rules are workable. If they are overly restrictive, companies that help entrepreneurs reach global markets will see their growth curtailed. Technological entrepreneurs want to know that innovations like TiVo and Slingbox are not hindered, as we seek to protect content creators' rights.

Because of our entrepreneurs' creativity, the United States is an unparalleled global leader when it comes to new ideas. In fact, more than 18 million Americans work in industries with an Intellectual Property focus. This includes industries where small firms are independent television and movie producers, video game designers, songwriters and manufacturers. Collectively, these and other industries make U.S. intellectual property worth $5.5 trillion – operating in hundreds of thousands of small businesses.

Just as the concept of intellectual property touches many economic sectors, preserving it requires diverse approaches. The Administration recently announced plans to bolster protection of American business interests. The private sector has played and will continue to play an equally important role in protecting intellectual property. Those efforts will be highlighted today as we look at the proactive efforts to meet small business needs.

As the Internet continues to evolve, we see a cross-section of businesses who can help preserve US ideas. The advent of e-commerce has been a boon to many small businesses. It has also allowed artists and small producers to rapidly disseminate music and video content, while reaching new audiences. But, the Internet has also created opportunities for piracy.

To assist U.S. companies in the Internet age, content owners are taking several steps. They are engaging in consumer outreach and education and, where necessary, taking legal action against infringers. Others are collaborating with video and social-networking portals to distribute their product.

In the end, the innovation of entrepreneurs is directly tied with the confidence that their ideas will not be stolen. Today's hearing will examine how the system for protecting intellectual property can spur job growth and foster innovation. During every previous recession, the creativity of America's entrepreneurs has led us back to prosperity. That will be the same again, today.

Contact: Alexandra Haynes
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Opening Statement for Hearing:
""The Impact of Intellectual Property on Entrepreneurship and Job Creation"
Ranking Member Sam Graves (R-MO)
House Committee on Small Business
United States House of Representatives
Washington, D.C.
July 21, 2010

Good afternoon. Thank you, Madam Chairwoman, for holding this hearing on intellectual property, and my thanks to our witnesses for joining us today - I'm looking forward to hearing from you about what intellectual property means to your business and the economy in general.

On average, intellectual property represents about 70% of a businesses' value, a significant increase from the past. However, many small businesses assume or don't understand that intellectual property issues affect them just as much as their larger counterparts. The reality is that small businesses have a significant amount to gain or lose when it comes to intellectual property protection.

Intellectual Property Laws in the United States are designed to protect a company's ideas. It's typically the most valued asset a company has to offer. Whether it's a name, logo, software, videos, new inventions, or literature - laws are in place to protect them. Taking full advantage of U.S. Intellectual Property Laws helps protect businesses and gives them a better opportunity to be successful and create jobs.

Protecting intellectual property is critical to our economy, jobs, and consumers. A violation of intellectual property laws directly affects a company's brand, market share, bottom line, ability to export, and creates a number of safety concerns for consumers. It's very easy to see the trickle-down effect this has on an economy. It is important that the United States maintains an aggressive strategy to protecting these highly valued assets.

U.S. Customs and Border Protection have seen seizures of counterfeited or pirated goods increase over the years and if there's one bad actor, there is usually many more in hiding. The Administration must take a hard-line approach to fighting intellectual property violations both domestically and internationally. The economic consequences are too strong to ignore. Additionally, engaging the world in more open trade will bring greater transparency to the seedy underworld of counterfeit goods and help reduce these threats to our economy while improving consumer safety.

Again, Madam Chairwoman, I thank you for holding this hearing today and I look forward to our witnesses' testimony.

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Testimony of Robert W. Holleyman, II

President and CEO
Business Software Alliance

Before the Small Business Committee of the
United States House of Representatives

Hearing on
The Impact of Intellectual Property on
Entrepreneurship and Job Creation

July 21, 2010

Madam Chairwoman, Ranking Member Graves, thank you for holding this hearing today and inviting the Business Software Alliance[1] to testify. BSA is an association of the world's leading software and hardware companies. BSA members create approximately 90% of the workplace productivity software in use in the US and around the world.

[1] The Business Software Alliance (www.bsa.org) is the world's foremost advocate for the software industry, working in 80 countries to expand software markets and create conditions for innovation and growth. Governments and industry partners look to BSA for thoughtful approaches to key policy and legal issues, recognizing that software plays a critical role in driving economic and social progress in all nations. BSA's member companies invest billions of dollars a year in local economies, good jobs, and next-generation solutions that will help people around the world be more productive, connected, and secure. BSA members include Adobe, Altium, Apple, Autodesk, AVEVA, AVG, Bentley Systems, CA Technologies, Cadence, Cisco Systems, CNC/Mastercam, Corel, Dassault Systèmes SolidWorks Corporation, Dell, HP, IBM, Intel, Intuit, Kaspersky Lab, McAfee, Microsoft, Minitab, PTC, Progress Software, Quark, Quest Software, Rosetta Stone, Siemens, Sybase, Symantec, Synopsys, and The MathWorks.

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. Our industry is dynamic, innovative, and a powerful engine for job creation and economic growth. It is also critically dependent on intellectual property protection. It is no accident that the software industry was born in this country. America's enthusiasm for technology, combined with its effective and constitutionally-rooted system of IP protection, served as the foundation for US leadership in this field.

Let me provide a little background about the industry: America's copyright industries lead the world, and the US software industry is by far the largest of these copyright industries. The software and related services sector employs almost 2 million people in the US in jobs that pay 195% of the national average. Software exports contribute a $37 billion surplus to our nation's balance of trade.

The software industry is made up of enterprises of all sizes. Most BSA members were small businesses not too long ago – even some that are household names today. In fact only a few BSA members were even in existence when BSA was founded in 1988.

Software companies partner with thousands of resellers, integrators and other software developers, many of which are small businesses. For example, companies like BSA Members Symantec and Microsoft maintain sizable partner programs that provide support for small businesses – businesses like Voice-and-Data Corporation, a sole proprietorship in Hickory, North Carolina that provides data backup and network security services to its small-business clients, and participates in both the Microsoft Partner Network and the Symantec Partner Program. Voice-and-Data is one of literally thousands of companies that take advantage of these programs – Microsoft alone has 640,000 participants in its partner network.

Platform providers like BSA member Apple have programs that provide technical support and tools to literally thousands of independent software developers – developers like Imangi Studios, an iPhone application development shop here in DC that produces a hit game that rose to the number three spot in the iTunes App Store's best-seller list this summer. Imangi consists of a couple who left their day jobs as programmers to pursue their dream of owning their own business. The applications available in the App Store have been created by more than 43,000 developers, many of which are small businesses. These developers have earned more than $1 billion from App Store sales.

The software industry sits at the center of a vibrant IT ecosystem – a virtuous circle that is producing jobs and economic growth, spawning new enterprises, and bringing innovative technologies to consumers. But all of these benefits are endangered by software theft. Because, sadly, more than $51 billion worth of stolen software was installed on PCs around the world last year.

In the US alone, one in five PC applications installed last year were unauthorized and unpaid-for. And we have the lowest software piracy rate in the world. Many countries outside the US have rates well over fifty percent. China, for example, has PC software piracy rate of 79%.

Most software theft occurs when an otherwise legitimate business makes illegitimate copies of software for its use. When repeated millions of times by businesses or consumers throughout the world, this conduct has a staggering cumulative effect.

The massive theft of our products harms software companies, depriving them of revenue that could be invested in new products and new innovation. The impact on the software industry in the US is particularly severe for the simple reason that the US is the dominant player in the global software market. Sixty cents of every dollar spent on software worldwide inures to the benefit of US-based companies.

Small software developers are particularly disadvantaged by software theft. They generally lack the resources to devote to fighting infringement of their products. They also tend to have smaller product portfolios over which to spread the risk of software theft.

But the economic harm due to illegal software use overseas goes well beyond the software industry. This is because software is a critical input of production for businesses across all sectors of the economy. Too often businesses from high-piracy countries like China disobey the law and steal the software they use to run their companies. They avoid a cost that their US competitors – both large and small – must bear. When their products enter the US market, they are competing unfairly with those US producers, undermining sales of US goods and displacing American jobs. This problem is repeated in every country where US businesses – in all economic sectors – compete against companies using stolen software to reduce their costs of doing business.

BSA will soon be releasing a study to quantify the impact of this unfair competition. Preliminary results conservatively estimate that addressing this problem in China alone would add over 25,000 new US software jobs and many times that throughout the rest of the economy.

So how do we address this problem?

One element must be education. BSA devotes significant resources in the US and overseas to train businesses how to manage their software licenses to protect themselves from the legal, technical and financial consequences of using unlicensed software. We have partnered with the Small Business Administration to bring this important information to small businesses around the country. Through this partnership we developed resources for small businesses, including our "Software Strategies for Small Business" guide and our www.smartaboutsoftware.org website. We hope to continue and expand this partnership with the SBA in the future.

Another critical element is enforcement. BSA enforces the IP rights of its member companies in the US and many countries overseas. But we are only one part of the equation. Governments need to do their part in stopping IP theft. This is particularly critical for small software developers that do not have means to enforce their IP rights on their own.

We are encouraged by the Obama Administration's release of a Joint Strategic Plan on IP Enforcement last month to coordinate and strengthen the government's enforcement efforts. The Plan, which was released on June 22 in a joint news conference with Vice President Biden

and the new US IP Enforcement Coordinator, calls for 33 specific actions, including:

- Promoting the use of only legal software by federal contractors;
- Promoting enforcement of IP overseas through trade policy tools;
- Improving communication between the US government and victims of IP theft;
- Improving coordination of federal, state and local law enforcement; and
- Preventing US government purchase of counterfeit products.

We urge the US government to execute on this plan and to provide the responsible agencies with sufficient resources to do so. The government should put particular emphasis on finding ways to help small businesses bridge the gap between the promise of IP rights and the reality of IP enforcement. Greater attention should be paid to ensuring that IP theft doesn't snuff out small software developers before they have the opportunity to become tomorrow's household names.

Thank you for this opportunity to testify.

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TESTIMONY OF RICK CARNES
President, Songwriters Guild of America

Before the
HOUSE COMMITTEE ON SMALL BUSINESS

July 21, 2010

Hearing on the Impact of Intellectual Property on Entrepreneurship and Job Creation

Chairwoman Velázquez and Members of the Committee, thank you for this opportunity to testify regarding the impact of intellectual property on entrepreneurship and job creation. In summary, I believe that the failure to achieve meaningful enforcement of copyright laws on the internet has nearly destroyed the American songwriting profession, which is a crucial driver of job creation in the music industry. Critical for this committee is the following fact: most U.S. songwriters are not employees—we are small business people.

My name is Rick Carnes, and I am President of The Songwriters Guild of America (SGA). SGA is the nation's oldest and largest organization run exclusively by and for songwriters. I am a working songwriter and have lived in Nashville since 1978. While I have been fortunate to have had a modicum of success in my career—including co-writing number one songs for Reba McEntire ("I Can't Even Get the Blues") and Garth Brooks ("Longneck Bottle") along with songs for Steve Wariner, Alabama, Pam Tillis, Conway Twitty, and Dean Martin among others—I am reminded constantly of the perilous existence that all of us who have chosen songwriting as a profession labor under daily.

Songwriters Produce Jobs Everywhere You Look

Practically ***everything*** in this economy is sold with music. Examples abound: just turn on the TV, and listen to the car commercials, or go into a restaurant to eat, and listen to the music. Fashion follows music; sporting events have music; technology is tied at the hip to music. The iPad, the iPhone—and practically everything else that starts with an 'i'—is tied directly to the delivery of songs. Can anyone deny that the resurgence of Apple computers was tied directly to the popularity of the iPod and iTunes as a music delivery service? Every search engine is selling huge amounts of advertising on searches for songs. It was the desire to download massive amounts of music fast that in large part lead to the growth of broadband internet service.

Every Job in the Music Business Springs from a Hit Song

Without hit songs, there would be no music publishing business; no recording studios; no studio musicians; no background singers; no recording engineers; no record labels; no promotion staff; and no artists touring to promote their hits.

I won't try to catalog the large number of jobs that are created by a hit song at radio, nor mention the pervasive use of songs in creating jobs in TV and film. I will point out, however, that American hit songwriters have created more goodwill around the globe than we could possibly account for on a balance sheet. Songwriters drive job creation in the music industry.

All Songwriters Are Self-Employed Small Businessmen and Women

Songwriters primarily make our money from two sources: CD sales and, if we are lucky enough to get a single, airplay money when the song is performed on the radio or TV. Unlike recording artists, we don't make money from live shows or merchandise because we don't perform. We're not that pretty. We just sit in a room alone with a guitar or piano and a blank page and a burning desire to tell a story through music. We don't sell tickets, we create copyrights.

But songwriting jobs are rewarding, valuable to the economy, and totally green. No smokestacks or heavy infrastructure costs are needed for song creation. We only need a guitar or piano, something to write on, lots of determination, luck, and a fearless heart. The only resources we deplete are pencil erasers, and coffee.

Professional Songwriting Jobs have Nearly Vanished

Songwriters used to survive from year to year on album cuts which netted us, on average, about $17 thousand, per million sales. Unfortunately, even that paltry income is gone now because there are very few million-selling records due to online music piracy. It is estimated that for every one song purchased online, 20 are stolen.

Your only chance to make a living as a songwriter anymore is to get a single on the radio and make the airplay money. Since most radio station play-lists today concentrate on around twenty new songs, however, and the rest are recurrent play on old hits, only a very, very small number of professional songwriters are still able to survive writing songs full-time.

We desperately need to establish new digital music delivery business models that will ensure the protection of copyrighted songs while still giving consumers a great experience with music at a fair price. Unfortunately, it is very difficult to establish such a business model when the entreprenuers who would fund the venture have to compete in a marketplace submerged in stolen music.

The Old Songwriting Business Model Has Been Broken by Piracy

The music publishers are not contracting with staff songwriters anymore. It is too risky to advance money for songs in a market that doesn't protect those songs from theft. The last music publisher I wrote for had twelve Nashville songwriters on staff in 1998, but by 2008 they had laid off all their staff writers, including me and my wife.

Absent any help from the Government in protecting music online, our best hope is self-help. The SGA supports the development of content delivery networks that give consumers better, safer access of music online. In this way, we might be able to compete with the virus-ridden, poor-quality illegal copies of copyrighted songs you find so often on Peer-to-Peer services.

The Current Failure to Protect Intellectual Property Hinders Job Creation in the Music Industry

In closing, let me recount an incident that is happening to me all too often in my discussions with my fellow songwriters.

I met a legendary Country songwriter in a coffee shop last month in Nashville and he told me he is now selling ammunition at gun shows instead of writing songs. When I asked him if he was ever going to start writing again he said, "Why bother?"

I couldn't answer that question.

There will always be people who are moved by the muse to write the occasional song. But without immediate and meaningful enforcement of copyright laws on the internet, the Golden Age of professional songwriting is over. The songwriters that made American pop music the envy of the world will pursue jobs that pay a living wage—jobs where their work and their rights are protected.

Conclusion

Ms. Chairwoman and Members of the Committee, SGA truly appreciates your efforts over the years on behalf of the songwriting community. We look forward to working with you to enliven job creation in the music industry through the protection of intellectual property rights. SGA and I stand ready to be a part of that process.

Testimony of Mr. Steven Friedman
President, T3 Technologies, Inc.
Before the House Small Business Committee
"The Impact of Intellectual Property on Entrepreneurship and Job Creation"
July 21, 2010

Good afternoon, Chairwoman Velázquez, Ranking Member Graves and members of the Small Business Committee. First, I want to thank you for allowing me to tell my story today.[1] I have been a small business owner for 19 years and it is a label that I am proud to identify with.

Let me begin by saying that I do not disagree that intellectual property can help small businesses commercialize their ideas. However, my recent experience has proven to me that the current IP system is out of balance and our imbalanced intellectual property laws can actual hinder innovation—disproportionately so for small businesses like mine. This reality was recognized recently by Justice Stevens in one of his final Supreme Court opinions in the *Bilski v. Kappos* case, in which he wrote *"[e]ven if a...patent is ultimately held invalid, patent holders may be able to use it to threaten litigation and to bully competitors, especially those that cannot bear the costs of a drawn out, fact-intensive patent litigation. That can take a particular toll on small and upstart businesses."*

I hear a lot of talk about intellectual property and its importance to small business, but from where I sit IP is a complicated regulatory system. This regulation of knowledge and ideas has expanded into many areas of our economy. As with any other kind of regulation, big business figures out the best ways to navigate the system while the little guys who do not have high priced legal teams at their disposal get tied up with paperwork and lawsuits, or simply eliminate innovative ideas from their plans because of the mere threat of such paperwork and lawsuits.

In fact, a study commissioned by the Small Business Administration showed that large businesses were overrepresented when it comes to utilizing intellectual property.[2]

My story is fairly technical and complicated, but the lesson is simple: intellectual property can be as much a danger to small businesses as it is benefit. A large firm can use the current intellectual property laws to effectively put smaller rivals that threaten its bottom line out of business.

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[1] For a more complete version of T3 Technologies story, visit: http://openmainframe.org/featured-articles/the-t3-technologies-story.html

[2] "Although small firms make up 40 percent of all firms in the database, they make up just 6.5 percent of all the patents in the database. IBM, the largest patenting entity, with 34,700+ patents since 1997, actually has more patents than all of the small firms combined over the same period." (Breitzman, Anthony and Diana Hicks, "An Analysis of Small Business Patents by Industry and Firm Size." Link: www.sba.gov/advo/research/rs335tot.pdf)

First, let me briefly explain the market I am in. Until recently, my company built computer systems that were capable of running IBM's mainframe operating system much like Dell and HP build systems capable of running Windows. Although some people are unfamiliar with mainframes – or even think of them as relics – they power much of the world we live in today. They are the computing power behind ATMs, health-care records, global stock markets, and the Social Security Administration to name a few. Seventy percent of the world's government and corporate data is stored on mainframes and it is estimated that up to $5 trillion in business assets reside on these systems. My small company sold such mainframe systems to Fortune 500 businesses, the U.S. military, NATO and a large number of city and county governments.

I employed over 50 people who served nearly 1,000 customers in 28 countries by selling our mainframe solutions to IBM customers who needed lower power mainframes, because, quite simply, not every mainframe user needs a Ferrari. This was a profitable niche for us and we quickly became the "go to" company for businesses that needed cost-efficient mainframes.

One of the reasons we got into this market was because in 1999, IBM stopped selling low-end mainframes. With no competitors left in the field, they were able to simply scale down larger systems and charge what we felt were monopoly rents to these smaller users. Seeing this as an opportunity for our little company, we licensed a new technology from a company called Platform Solutions (PSI), a California-based small business, whose product allowed less expensive hardware to run IBM's mainframe operating system. As a result, I was able compete with IBM by selling much more affordable mainframe machines to my customers.

Thanks to a well-known DOJ Antitrust Consent Decree, for decades, IBM licensed their mainframe operating system to all comers on reasonable and non-discriminatory terms. This is what permitted a small start-up company like Amdahl to innovate and excel in the market in the 1980s and 1990s. The continuation of this practice was a necessary assumption in my company's decision to develop our products. In 2003, IBM was released from the Consent Decree. Almost immediately IBM began putting up obstacles to T3 and our customers who wished to license their operating system. This culminated on October 31, 2006 when IBM publicly announced they would no longer license their patented operating system to any hardware except their own. Imagine if Microsoft one day announced they were building their own PCs and that Windows would only be sold on those machines! Without the coveted operating system, our hardware was nothing better than an expensive coffee table.

To make matters worse, they then sued my business partner, PSI, for alleged intellectual property violations. They also threatened my customers and me with IP lawsuits. Despite the fact that no court has found me guilty of infringing anyone's intellectual property the threat of litigation has scared almost all of my customers away.

The court process has so far taken over 3 years and cost millions of dollars and is still not over. To make matters worse, IBM purchased PSI and shelved its technology – the technology I relied upon for our products. And now, almost incredibly, in civil court, IBM hides behind intellectual property laws, claiming they permit otherwise forbidden monopolistic behavior—essentially saying that intellectual property laws trump antitrust laws.

Meanwhile, the threat of patent and copyright litigation prevented other companies from entering the market and providing customers with greater choice and lower prices. As a result, the market is stagnant and there is little innovation compared to the rest of the computer industry. In this case, intellectual property laws have led to IBM having a 100% share of the mainframe hardware market and the mainframe operating system market.

The Constitution says that Congress grants IP rights in order to "promote the Progress of Science and useful Arts." In short, intellectual property's goal is to promote innovation, but in my example, out-of-focus intellectual property laws have been used to stifle small innovative businesses and protect the status quo.

Although I can offer no cure-alls for the current system, I do implore lawmakers to think beyond bumper sticker slogans. The current IP system can have massive unintended consequences and actually be a huge detriment to innovation that disproportionately disfavors small businesses that don't have the resources to play the game.

I thank the Committee for its time and I look forward to answering your questions.

Statement of Peter Carnes

CEO

Traffax Inc.

Testimony before the House Committee on Small Business

"The Impact of Intellectual Property on Entrepreneurship and Job Creation"

July 21, 2010

Chairwoman Velazquez, Ranking Member Graves, and distinguished members of the Committee: My name is Peter Carnes, and I would like to thank you for holding this important hearing on the role intellectual property plays in driving innovation and creating economic growth and, most importantly, new jobs.

I am the chief executive officer of Traffax, Inc., a transportation monitoring equipment startup in College Park, Maryland. A May 2008 winner in the University of Maryland's Maryland Technology Enterprise Institute business plan competition, Inc. designs equipment and systems to measure the flow of traffic, both vehicle and pedestrian, based on technology that detects and monitors electronic signals from consumer electronic devices. The Traffax technology is accurate, inexpensive to deploy, and operates while protecting individual privacy, overcoming some disadvantages found in existing systems. While we are based in the U.S., traffic is a global problem and Traffax equipment is also in use in Canada, England, Australia and Brazil. We have seven employees, plus sales agents domestically and overseas, and have plans to expand further.

We started Traffax to commercialize technology developed at the University of Maryland, in recognition of the fact that ideas—and the realization of those ideas as useful products or services—are a high-value opportunity to drive economic revitalization. As a result, our company's very existence is predicated on ideas. Those ideas were protected through a combination of patents and copyrights, and that intellectual property (IP) created the opportunity to build a business.

In today's global world, innovation serves as a linchpin for creating future jobs, solutions to modern problems, and maintaining technological leadership. The lifeblood of any small, high-technology enterprise is the intellectual property (IP) that it creates. In other words, the short-term viability, the long-term profitability, or the eventual initial public offering or sale of a small company all depend upon its ability to develop, acquire, protect, and apply innovative ideas and concepts.

Lessons Learned: Integrating an IP Culture Into All Stages of the Innovation Process

Entrepreneurs have many motivators but from a financial perspective, there are really only three positive outcomes resulting from starting a company: You build a business and leave it to your kids, you have your company acquired, or you take your company public through an IPO. Most of the time your kids don't want the company, and the number of companies who make it to IPO is infinitesimal compared to the number of companies started. That leaves acquisition, which requires you to have something worth acquiring. For many generations that was land, or inventory, or client lists. But for today's innovative new businesses, oftentimes the only asset of value is intellectual property.

Through decades of startups and consulting, I have seen that companies who manage their IP in a systematic way are often the companies who get funding from VCs more quickly, and have a more successful exit strategy. These companies look at their IP not as just a single idea, but as a package of trademarks, copyrighted software, patents and even the non-disclosure agreements employees sign. They build into employment agreements profit sharing for employees who generate valuable IP, and they manage their contracts with customers to make sure that rights to end products are clearly defined.

Companies who manage their IP holistically also make it less attractive for big companies to free-ride on their ideas, and keep their customers from taking ideas and replicating them in-house.

As innovators, our job is to solve a problem, to change things, to create new possibilities. We have the wonderful opportunity to fail, and with each iteration we learn and improve until we refine the product until it solves the problem - or we hit a dead-end.

So the innovation model is high risk, and the only thing that makes it worth doing is the possibility of high reward. Without IP, it is very difficult to get that reward before competitors crop up to dilute the value of the innovation. Traffax is facing this dilemma today – our competitors now claim to have the same functionality we invented, and in some cases they probably can, all because they have read our patent application.

IP as America's Way Forward

America's technological leadership is not an accident. America's IT giants are built on the back of our robust IP system, and the entire economy is reaping the benefits.

According to a 2007 report by the Information Technology & Innovation Foundation, IT adds $2 trillion dollars annually to the US economy, and "is responsible for nearly all of the pickup in economic growth over the last decade."

IT drives the economy, but it also requires fuel of its own—intellectual property. Most of the leading companies driving IT innovation are less than 30 years old. Small companies like mine work in the hope that we can become one of those companies. Entrepreneurs often risk everything for this possibility – we mortgage our homes, quit our jobs, and generally make our families very nervous. And the people we hire risk quite a lot to become part of this effort as well, often forgoing higher salaries they could be earning in larger, more established companies. IP protection makes it possible for the risks pay off if and when our products become successful.

And the use of IP to drive America forward isn't just about copyrighted software for desktop computers or patents for a Traffax monitor, it's going to be key for deriving the maximum benefit from the next wave of green technology products. Regardless of anyone's opinion on climate change, the success of the Prius, solar roofing tiles and sales of new wind turbines make it clear that there is a market for energy efficient products with a smaller carbon footprint. America is dedicating significant intellectual firepower to inventing these products domestically, but the reality is that the market will be global. Ensuring that American companies are paid for these new inventions becomes critical to the continued development of new products, and the hiring of more researchers, engineers, sales people and marketing teams – all high paying jobs that will help grow the economy.

In the IT industry, there's a concept regarding a product's value chain known as the "smiling curve." It is a U-shaped curve where the highest value of a product is at each

end and the lowest at the bottom dip. According to this model, the majority of a product's value goes to firms that research and develop a product on the one end, and that market and sell the product on the other end. The bottom dip represents the least amount of value, which is the production and assembly of the product.

Successful U.S. companies such as Apple are often innovative creators and marketers of products, but they outsource the production to overseas companies. Doing so maximizes value and allows innovators to reap the highest economic rewards, but they are also exposed to the greatest risk because their ideas are most vulnerable to theft. This is why intellectual property protections and enforcement are so important to IT companies.

Roadblocks to Building a Culture of IP

There are three big roadblocks facing small companies that wish to bring innovative new ideas to market using the IP system: The time it takes the USPTO to process a patent, the uncertainty of IP protection in overseas markets, and the paucity of loan options available because banks and the Small Business Administration (SBA) does not know how to value IP or treat angel investors correctly.

USPTO Delay

Many small, innovative businesses pay some attention to IP – they pour their scarce resources into the front end, but because the process takes so long, they fail to pay to maintain their patents, or give up part of the way through. I have been with several companies that haven't been able to make their IP worth much – not because the IP was worthless, but because they just ran out of steam.

It takes so long to achieve patent protection that it is hard to "stay the course." Right now the patent office publishes a patent application 18 months after filing, but the average wait until the patent is granted is 40 months. Most technology entrepreneurs are doing everything they can to survive for 40 months, much less waiting around to see if they got their patent.

Global devaluation of IP

Piracy reduces your potential world market – companies don't bother to explore expansion into some countries because they know protection is unlikely. Ironically globalization expands available market but can harm your ability to realize its potential. Before the Internet, entrepreneurs often would calculate that we could get into a new market and sell a significant number of units before the technology was copied. We had a chance to establish market leadership in spite of the inability to protect our IP legally. Nowadays the copying begins before our first product hits the shores.

The big problem today with the Internet world is that copyright has been devalued – it is the unfortunate reality of the web culture that says "if its on the web it must be free". Years ago, building a brand often came from the creation of thoughtful analysis or specific information. In today's age of cut and paste, the moment I put my ideas on the web, they are no longer mine at all. Competitors either outright copy the prose, or just re-word the thought and the value of that new idea is diluted. It used to be that when you had an idea, you had some opportunity to travel down the learning curve, and gain the first mover effect. Today, the individual with the most resources can step in and usurp the market, without coming up with the idea. Most small businesses don't have the resources to enforce IP rights, especially on copyright.

Having been in the "pure" software business, I can tell you that selling software only is going to get harder. The speed at which software is copied, and the willingness of overseas users to steal, makes it ever harder to build products that have a multiplier effect (i.e. I write it once and then sell many copies). Instead, software developers are doing more custom software development or work for hire, where they are only paid by the hour – this is a fine way to make a living, but it almost never leads to breakthrough innovation.

The other major focus for software developers is to create software that is only expressed on a particular physical product. At Traffax, our hardware is totally dependent on the software that implements our patented inventions. This is also seen in the medical device field. Great strides are being made on new medical tools by marrying cutting edge

software with hardware. And we even see it in the consumer space; thousands of developers are flocking to the iPhone and other platforms because the security of their software is bounded on just that physical device. Copying is more difficult and of limited value.

SBA Loans and IP valuation

We explored SBA loans at Traffax, but we found that banks have almost no ability, and no interest, in granting loans to companies that have few tangible assets. Innovation companies don't buy buildings, they don't buy furniture, they don't buy trucks, they may not even buy computers. Instead they pay wages for engineers, they hire software developers, they build and destructively test prototypes – none of which is a tangible asset that a bank can attach if you fail.

A further complication of the SBA loan is the practice of holding all owners individually liable for the debt. This means that each person is wholly responsible if other signers cannot help repay the debt. If I have an angel investor who has money (by definition, an angel investor has to have money), he or she may only have 10% ownership of the company, but he or she will end up being 100% liable for the debt. This is a big mismatch between potential reward and level of risk. In practical terms it means that my investors are uninterested in using SBA loans.

Solutions

Give the Patent Office the Budget it Needs

The US patent office continues to suffer under a crushing backlog of patent applications, and new examiners need to be trained in the kinds of technology that will lead the nation forward. Innovative businesses are being held up at the starting line while they wait for more than forty months to find out of their innovative new idea has received a patent. Simply put, stalled applications because of inadequate resources will delay the development of new technologies and the creation of new private sector jobs. One of the best ways to help small IT companies is to give the USPTO the budget it needs to

eradicate the shameful backlog of pending patent applications – there are over a million pending patent applications, 500,000 of which have not even had a preliminary review.

Technology innovation is a virtuous cycle that repays investments exponentially – but it often takes IP protection to get the funding to develop that innovation fully. There is no reason that the USPTO should have budget problems since its entire budget comes from application fees. In times like these, we should be promoting growth, not shackling the information economy with uncertainty and delay.

Help Protect Our IP Globally

It is a truism that we are in a global economy. Free trade in IT is incredibly important to innovative companies. One of the side-effects of globalism is the incredible amount of uncertainty about how much protection we can count on for our IP. It is not just those countries that fail to protect our IP and allow piracy that hurt us throughout the world, but uncertainty about the levels of protection even in those countries generally amenable to IP. Currently, there is a lot of focus on those countries with very little IP protection, and those countries do need to take steps to stop the overt theft of our IP. But there should also be some attention paid to the other countries that generally respect IP, to try to encourage similar IP policies globally. This would not just help innovative U.S. companies, but increased certainty around IP protection would help innovative companies everywhere. And that benefits everyone.

Reform SBA Loan Processes

As the U.S. economy depends less on bricks and mortar, and more on information and technology, the SBA processes and rules need to be modernized to keep up with the times. SBA loans need to be more available to the innovative technology companies that will lead our economy into the future. As I mentioned, current policies impose a disproportionate risk/reward profile on angel investors, who are among the few sources of funding for innovative startup companies. One solution would be to have SBA give non-recourse loans to IT companies; innovative companies like Traffax that do not have securable assets, but will need to invest in salaries to hire programmers and engineers.

Chairwoman Velazquez, Ranking Member Graves, and distinguished members of the Committee, the innovation economy is dependent on small business, and small business is dependent on IP. I hope that the committee will continue to focus the spotlight on the contribution small business makes to the future of the U.S., and the way the government can do a better job to encourage our IP based economy. Thank you for your time and consideration on this important topic.

Testimony of the

Motor & Equipment Manufacturers Association

Before the

United States House of Representatives

Committee on Small Business

"The Impact of Intellectual Property on Entrepreneurship and Job Creation"

21 July 2010

The Motor & Equipment Manufacturers Association (MEMA) represents over 600 companies that manufacture motor vehicle parts for use in the light vehicle and heavy duty original equipment and aftermarket industries. Motor vehicle parts suppliers are the nation's largest manufacturing sector, directly employing over 685,000 U.S. workers and contributing to over 3.2 million jobs across the country. The motor vehicle parts supplier industry is a leader in developing technologies critical to making today's vehicles safer and more fuel efficient and is investing in product development to help meet future consumer demand. Suppliers also manufacture the aftermarket products necessary to repair and maintain over 247 million cars and trucks on the road today.

Collectively, U.S. motor vehicle parts suppliers are a $388 billion industry, comprising three distinct segments: original equipment, heavy duty, and aftermarket parts manufacturers. MEMA's Brand Protection Council leads industry efforts on brand protection and intellectual property issues.

Intellectual property and strong IP protections are critical to the success of motor vehicle parts manufacturers who continually innovate and develop new technologies. Suppliers are responsible for two-thirds of the value of today's vehicles, for nearly 30 percent of the total $16.6 billion automotive research and development investment and provide much of the intellectual capital required for the design, testing and engineering of new parts and systems.

MEMA is represented in this hearing by ABRO Industries, Inc., a small aftermarket supplier headquartered in South Bend, Indiana. If you have never heard of ABRO Industries before, do not feel bad – virtually no Americans have. That is because ABRO operates in a manner once common in America, but which is now almost unheard of. ABRO has a variety of automotive, hardware and basic consumer goods such as radiator fluid, glues and tape manufactured in America under the ABRO® brand name. ABRO then sells those items exclusively overseas, mostly in developing nations. ABRO does do not sell any items in the U.S.

ABRO is able to compete against cheaper foreign competitors for two reasons. The first is that the label "Made in America" has great value in developing nations when it comes to non-electronic consumer goods. The rest of the world has faith in the quality of ABRO's products. Secondly, ABRO has spent decades building its brand name into a reliable identifier of high-quality goods. In fact, ABRO is so popular that in some countries, it has entered the language. For example, in Pakistan masking tape is known as "ABRO tape" (similar to how, in the U.S., invisible tape is known as "Scotch tape").

Because of this, ABRO greatly values its name. Matching ABRO's global product distribution is its global trademark coverage. The name ABRO is registered in multiple categories in over 160 countries. This is necessary because ABRO faces counterfeiters around

the world. To protect the name, ABRO has a very aggressive anti-counterfeiting program and has fought counterfeiters on 6 continents.

The safety and economic implications of counterfeit auto parts will be the focus of today's testimony. Comments will outline the global counterfeit challenges facing the motor vehicle parts industry, give you an idea of the particular counterfeit issues faced by ABRO Industries and then offer some ideas, legislative and otherwise, that would help combat the intellectual property piracy that faces ABRO and other parts manufacturers.

A. Economic Impacts

The magnitude of global counterfeiting is significant. In 2008, an OECD report estimated that industry losses due to counterfeiting and piracy of trademarks, copyrights, patents and design rights were $250 billion. This does not even begin to estimate the value of pirated non-physical goods. In April 2010, the Government Accountability Office reported that counterfeiting and piracy are "expanding" and "a sizeable problem, which affects firms' incentives to innovate."

Pirated luxury goods as well as movies and music are often the first things that come to mind for many people when they think about IP infringement. In many cases, consumers are seeking bargains and are aware that they are purchasing counterfeit or pirated goods. However, international intellectual property protection is about much more than the entertainment or luxury industries of the East and West coasts, though both will always be an important component of the battle. Intellectual property protection is also about the safety of a wide variety of consumer products developed and manufactured all across this country such as pharmaceuticals and motor vehicle parts. IP protection is critical to the health and safety of American families as well as the economic health of these industries and the communities that support them.

Counterfeit parts and components for cars, trucks, buses and commercial vehicles pose a critical problem to the American economy and the supplier industry because of the wide range of counterfeit products manufactured and trafficked worldwide. In the past, MEMA has estimated that counterfeit goods cost motor vehicle suppliers at least $3 billion in the United States and $12 billion globally in lost sales. Please note that the industry believes these numbers are conservative. In fact, Frost and Sullivan estimated in 2006 that the global losses to motor vehicle suppliers due to counterfeiting would be as high as $45 billion in 2011.

While the media tends to focus on the intellectual property struggles of major multinational corporations, IP is an extremely critical issue for small businesses like ABRO, which has only 24 employees, because a single act can destroy a small business. A giant corporation can recover from a hit to its reputation. They have the money to hire top PR firms and to spend whatever is

necessary in terms of advertising in order to repair any damage to their name. A small company, however, does not have this ability. If counterfeiters have managed to undermine their brand name by selling low-quality and/or defective products under that name – they can easily be permanently damaged or even destroyed.

Small companies usually only have one or two pieces of key intellectual property. In ABRO's case, that key piece of IP is the brand name. Other companies may be built entirely on a single patent or copyright. A giant corporation can offset damage to one trademark, patent or copyright with the profits from a thousand others that they own – a small company usually has all its intellectual property eggs in a single basket.

While a major corporation sees intellectual property protection in terms of maximizing profits, for small businesses it is a matter of survival. Either the ABRO name stands as a guarantor of quality or the company goes out of business. There is no fall-back position, no second chances, no Plan B.

It is common to blame all counterfeiting on China. This, of course, is not the case. While the motor vehicle parts manufacturing industry faces problems with counterfeits made in China, it also face problems with counterfeits made in India and Russia and other countries. It is true that most counterfeits do appear to be made in China, but this is more a result of the fact that many legitimate products are also made in China. The counterfeiters have grown along with the manufacturing capabilities in general in China, and it is unfair to blame counterfeits originating from that country as the result of some cultural proclivity – as some commentators have done in the past.

Rather, ABRO has been pleased overall with the efforts of the Chinese government in fighting counterfeiters within their borders. In just this last year, Chinese authorities have raided over 20 major sources for counterfeit ABRO merchandise in China. Over two dozen shipments of counterfeit merchandise have been seized and destroyed by Chinese customs authorities on ABRO's behalf. Finally, ABRO also has seen the conviction for three years on counterfeiting charges of a counterfeiter who embodied the type of villain that companies felt they couldn't touch under the old system – a well-connected and wealthy regional figure.

Since China joined the World Trade Organization in 2001, the government has upgraded intellectual property protections to world standards. In addition, the motor vehicle supplier industry is seeing evidence that enforcement is improving in China. China experienced a history changing shift in the 1990s, and went from a developing nation to a growing economic power-house in the space of just one decade. Not surprisingly, many counterfeiters found a weakness to exploit in this delay between the growth of manufacturing ability and the rise of the legal and enforcement regime necessary to enforce international intellectual property rights.

What companies and the people that established their prejudices regarding China in the 1990s are slow to recognize and credit is that just as China has made dramatic leaps in manufacturing ability in the 1990s, it has made equally dramatic leaps in IP enforcement in this decade. The Chinese system isn't perfect, but it also isn't what it once was. The Chinese authorities deserve significant credit for the dramatic modernization of their enforcement system that they have managed to pull off.

B. Health and Safety Impacts of Counterfeit Motor Vehicle Parts

There is a wide range of counterfeit parts and components for cars, light trucks, buses and commercial vehicles that are manufactured and distributed globally. Many counterfeit products, especially in the automotive parts industry, go undetected and are purchased unintentionally. Because trademark and brand infringement are so convincing, many times consumers or installers of these components may not be able to recognize or distinguish the genuine part from the counterfeit part. In many instances, the part manufacturer becomes aware of counterfeit products when responding to warranty claims of a failed product.

Counterfeit motor vehicle parts may fail to meet U.S. Federal Motor Vehicle Safety Standards (FMVSS) or other industry-accepted safety standards; likewise, these parts may be produced with dangerous, inferior materials and have a shorter-than-average service life. Thus, the use of these counterfeit vehicle parts – such as brakes, brake pads, brake fluid, tires, belts, and automotive lighting which look identical to genuine, brand name parts – may result in sudden, catastrophic engine failure, brake failure, or other system malfunction, endangering the car or heavy duty truck driver operating the vehicle and all motorists traveling the same roads with these vehicles.

Trademark or brand infringement is the most immediate problem faced by many motor vehicle suppliers. It is the most direct and easiest method for pirates to get their counterfeit goods into the market. Stolen trademarks give instant market credibility to pirated goods.

Another method used by pirates is to copy trade dress or the unique appearance of product packaging. Usually the pirates do not make perfect copies, instead making the packaging confusingly similar, to allow them to disingenuously claim that they are not infringing. The average consumer cannot always distinguish the two packages and erroneously concludes that the counterfeit package is also an authentic product. The pirate preys on the market recognition of the trade dress owner. Further, the infringed trademark owner may be faced with honoring warranty claims for pirate products or risk loss of customer confidence and loyalty. This is an added and unanticipated cost of doing business.

C. Other Industry Experience Regarding Counterfeit Parts

Counterfeit issues are wide-spread in the motor vehicle parts industry, including with two other MEMA members, Bendix Commercial Vehicle Systems, LLC, headquartered in Elyria, Ohio and the Gates Corporation, headquartered in Denver, Colorado.

Bendix manufactures active vehicle safety systems and braking systems for commercial vehicles which includes, but is not limited to, semi trucks, fire engines, ambulances, vocational vehicles and passenger buses. Due to the wide scope of products they design and manufacture, Bendix frequently encounters multiple counterfeit products – many of which are safety critical – not only for operation of the commercial vehicle on which these components are installed, but also for those who share the highways with these vehicles. Of particular note are two recent reported cases involving air dryers for buses. Air dryers are a critical component for vehicle braking systems. In the first situation, a school bus equipped with what was thought to be a replacement genuine Bendix air dryer was causing a loss of air pressure and erratic operation of the vehicle, placing the safety of the students riding the bus in jeopardy.

The second incident involved a transit bus driver traveling through the streets of a major southeastern U.S. city. While en-route, dropping off and picking up passengers, a sudden, loud sound reverberated through the inside of the bus. The sound originated from something that actually shot through the floor of the bus, ripping up the floorboard, damaging the body, and forcing the vehicle to come to a complete stop. Fortunately, neither the driver nor any passengers were injured. But extensive repairs were needed, and the bus required a tow from the road.

Maintenance technicians determined that a knockoff air dryer installed on the bus had malfunctioned, causing the part to tear through the vehicle floor and create the loud noise. An ineffective dryer design and construction caused the retaining ring that held the canister to split in the middle and fail. The failure propelled the canister off the dryer with enough force to drive it through the floor of a bus. The desiccant in the cartridge had broken down into powder and was injected throughout the braking system, contaminating the system and contributing to the potential for future failures of downstream parts. The dryer and cartridge – which had just been installed a few months before – was not a genuine Bendix product.

Gates is a major manufacturer of a range of belts used in motor vehicles. Gates has faced a number of cases worldwide of counterfeit belts. Timing belts allow the internal components of the engine to operate with proper timing; namely, the valves and pistons. A counterfeit timing belt may wear and fail prematurely causing serious cost, health, and safety ramifications for consumers. Gates has tested pirated timing belts and has found they have a significantly shorter life when compared to genuine product. Unexpected and premature failure of a timing belt would be highly problematic to a motorist since it would result in the destruction of the engine

for all practical purposes. Consequently, a broken timing belt could strand a motorist and cost several thousand dollars to repair the damaged engine.

D. Existing and Potential Solutions

MEMA supported and applauded the passage of the Prioritizing Resources and Organization for Intellectual Property (PRO-IP) Act in 2008. The PRO-IP Act strengthens the nation's trademark and copyright laws and increases domestic enforcement efforts to protect intellectual property. It provides new resources for the Federal Bureau of Investigation (FBI) and the Department of Justice (DOJ) for enforcement and prosecution efforts. It also creates the Intellectual Property Enforcement Coordinator (IPEC) within the Executive Office of the President tasked with coordinating the various federal agencies working to enforce our intellectual property laws.

Implementation of this legislation is critically important. The federal government has begun carrying out the requirements of this legislation. Funding has been provided for the FBI and DOJ to hire new Special Agents and new U.S. Attorneys solely focused on intellectual property crimes. Victoria Espinel has been appointed as IPEC and she recently released the Joint Strategic Plan required in PRO-IP.

The Joint Strategic Plan is the first ever plan with multi-agency support and input to include a roadmap on how to address the multi-billion dollar challenge of counterfeiting and piracy of American intellectual property. MEMA applauds the release of this plan, its focus on the robust enforcement of IP rights worldwide, and the goal of enhancing US advocacy on IP issues in multiple international forums. If the plan is fully implemented, our nation's ability to combat counterfeiting and piracy will be greatly improved. The goals included within the Strategic Plan are important, and to be met, additional resources will be necessary. To release the plan, the IPEC relied on detailees from other federal agencies and does not have any permanent staff. Congress should consider providing additional funding and resources for this office.

Our country must promote and defend a robust international system of IP laws and norms while strengthening cooperation with like-minded countries and key trading partners to promote shared IP protection. Customs reauthorization legislation, pending before the Senate Finance Committee, includes authorization for additional resources at Customs and Border Protection and Immigration and Customs Enforcement to enforce intellectual property laws at our borders. Additionally, the Administration is working to conclude an ambitious and comprehensive Anti-Counterfeiting Trade Agreement (ACTA) before the end of this year. Such an agreement should include robust provisions to confront IP theft worldwide. This will help protect American jobs, stimulate the economy, and encourage innovation. We firmly believe an agreement that includes

robust provisions to confront IP theft in both the physical and online environments will help protect American jobs and stimulate the economy. MEMA is supportive of both of these efforts.

A relatively inexpensive method that would help provide businesses with the tools they need to address counterfeiting overseas would be the expansion of the Intellectual Property Attaché position. Currently, less than a dozen U.S. Embassies have an IP Attaché on staff. These contacts have greatly assisted the industry in understanding the local anti-counterfeiting procedures, gaining access to key foreign government personnel and obtaining the necessary resources to fight counterfeiting in other nations. By putting one IP Attaché in each US Embassy we would greatly expand US businesses ability to respond to the production and sale of counterfeit goods overseas. Moreover, these attachés act as spokespeople to their assigned country for the importance of respecting intellectual property rights. Finally, they send a clear message to counterfeiters that the United States takes the IP rights of its citizens very seriously. Especially for smaller businesses with limited resources, IP Attachés greatly help to even the playing field between the legitimate rights holders and the counterfeiters.

E. Conclusion

Protecting intellectual property is of the utmost importance to companies like ABRO as well as MEMA. It has been a priority that has garnered support from the current Administration as well as both sides of the aisle here in Congress. All stakeholders must continue to work together to see that the existing laws are enforced, that IP protections overseas continue to improve and that the necessary resources are being utilized to safeguard the investment made by companies and individuals across all industries and sectors.

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Opening Statement
Rep. Dan Lipinski (D-IL)
House Committee on Small Business
Committee Hearing:
The Impact of Intellectual Property on Entrepreneurship and Job Creation
July 21, 2010

Thank you Chairwoman Velazquez and Ranking Member Graves for holding this important hearing on intellectual property, entrepreneurship, and job creation.

Right now Congress must be focused on job creation. I think that many of us have chosen to be on this committee because we know that most job creation is driven by America's small businesses. Today I'd like to talk about a particular kind of small business, the high-tech startup.

There is something uniquely American about an entrepreneur who is willing to gamble on a brand new innovation, an idea right out of the lab, with no guarantee that a market will exist or that an invention can even be built. Many large companies are unwilling or unable to take those risks, and as a result most technology transfer and commercialization is done by small business. These are the risk-takers, along with venture capitalists, who create the new products, markets, and companies that drive our economy forward.

I chair the Research and Science Education Subcommittee of the Science and Technology committee, where I have been a strong advocate for funding basic research and development. These investments in R&D are the first step in a long road toward new small businesses. We all know how difficult it can be to commercialize a new idea, and I again must compliment Chairwoman Velazquez for her strong leadership in advancing the SBIR / STTR reauthorization last year.

But intellectual property issues can also be a challenge for our small businesses. Adequate protections for IP are crucial for a successful innovation ecosystem, guaranteeing that startups and venture capitalists who spend time and money on tech transfer activities will not see their idea stolen on the victory lap by a company in China.

Our startups can face a hostile IP environment that includes everything from counterfeiters to overzealous lawyers to a patent system that is increasingly inaccessible for small applicants. I applaud the Chairwoman for holding this hearing, and hope it helps us identify sensible measures that strike a balance between protection and innovation, allowing the Intels, Apples, or Googles of the future to grow and thrive here in the United States.

I firmly believe that America's greatest IP threats come from China, which has long been the leading producer of counterfeit clothing, media, and electronics. While the Chinese government has recently set up new administrative guidelines and penalties, they are

nowhere near enough. Even in cases where infringers are found guilty, the fines imposed have been so low that the convicted were still able to earn an ample profit.

During last summer's Olympic Games I remember reading about shops in Shanghai that would simply hang a curtain in front of the counterfeit DVD section of the store in order to present a more positive image to visiting foreigners. I have no doubt those curtains have since come down. And just this week, federal prosecutors and the FBI announced proceedings against Kexue Huang, who is accused of stealing over $100 million worth of trade secrets from the Dow Chemical Company.

It is no wonder that even as the number of infringement cases has gone up in China, the average settlement awarded to victims has remained relatively unchanged and significantly below the average settlement won in American courts. If we want to see our investment in R&D turn into American small businesses instead of Chinese ones, this is something we need to fix.

Innovation is the lifeblood of many small businesses, and we need an IP environment where these companies can succeed. I look forward to hearing what the witnesses have to say on these issues, and to learning what steps they recommend we take to improve IP laws and regulations for America's small businesses.

Thank you.

July 21, 2010

Chairwoman Nydia M. Velázquez
House Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515

Ranking Member Sam Graves
House Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515

Dear Chairwoman Velázquez and Ranking Member Graves:

The Copyright Alliance applauds you for conducting today's hearing on "The Impact of Intellectual Property on Entrepreneurship and Job Creation" and welcomes the Committee's focus on the importance of intellectual property on job creation.

A recent study by economist Stephen E. Siwek, sponsored by the International Intellectual Property Alliance, demonstrated convincingly that intellectual property is a major contributor to real U.S. economic growth and GDP. The comprehensive study conducted using the same statistical approach of the World Intellectual Property Organization found that in each year from 2004 to 2007, real annual growth rates from both core and copyright industries were more than twice that of the total U.S. economy. In 2004, 2005, 2006 and 2007, the real annual growth rates achieved by both the core and total copyright industries were more than twice the real growth rates achieved by the U.S. economy as a whole.

This significantly positive contribution by copyright industries to real U.S. growth was demonstrated in 2006-2007, the most recent period with current available data. In that period, core copyright industries contributed 22.74% of the U.S. economy's real growth; for the total copyright industries the contribution was 43.06% of total real U.S. growth. The value added in 2007 by core copyright industries was $889.1 billion, approximately 6.44% of U.S. GDP, with the value added for total copyright industries rising to $1.52 trillion, or 11.05% of GDP.

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The Copyright Alliance is a non-profit, non-partisan educational organization dedicated to the value of copyright as an agent for creativity, jobs and growth. The Alliance membership is comprised of unions, creative guilds, non-profit and for-profit corporations as well as trade associations, and individual artists and creators. We believe that copyright law promotes creativity and job creation and strengthens the U.S. economy. Those who create, render, and publish copyrighted works rely on the copyright law and its enforcement, for their creative and financial success. Without it, these creators would likely cease to exist, or at the very least, cease to produce these important works that are enjoyed by billions of people around the world.

We are committed to promoting the cultural and economic benefits of copyright, providing information and resources on the contributions of copyright, and upholding the contributions of copyright to the fiscal health of this nation and for the good of creators, owners and consumers around the world.

We look forward to working with the Committee as it continues to examine these important issues.

Sincerely,

Patrick Ross
Executive Director
The Copyright Alliance

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Written Statement of Tod Cohen
Vice President and Associate General Counsel, Government Affairs,
eBay Inc.
Before the House Committee on Small Business,
"The Impact of Intellectual Property Entrepreneurship and Job Creation."
July 28, 2010

Thank you Chairwoman Velazquez, Ranking Member Graves, and Members of the Committee for this opportunity to express eBay's view about the need for balanced intellectual property protections to encourage the growth and continued success of small businesses and the Internet platforms on which those businesses flourish.

eBay had its beginnings as a small business fifteen years ago, when the highest percentage of items offered on our site were Beanie Babies. Today, eBay is a Fortune 500 company that is no longer just an auction-style site, but an online marketplace that enables hundreds of millions of buyers to access hundreds of thousands of small business sellers and the staggering variety of items they offer at incredible value around the world.

At a time when the economy remains troubled and when the greatest hope for rapid recovery is tied to our nation's small businesses, I am proud that eBay provides the preeminent breeding ground for small businesses and job creation.

So while eBay itself is actually a big business (with more than $50 billion in transactions enabled annually across our platforms), we can proudly say that we represent the interests of the hundreds of thousands of small businesses that make our company a success. With respect to intellectual property enforcement, we want to ensure that enforcement is balanced and that well-established liability protections in intellectual property law continue and are strengthened as needed.

Balanced Enforcement Means Stopping the Misuse of Intellectual Property Laws

eBay supports and is actively involved in the strong enforcement of intellectual property laws to stop the traffic of pirated and counterfeit goods. Our work on behalf of rightsholders is world class and unmatched in the Internet. Unfortunately, over the last few years, we have seen a clear and consistent increase in the *misuse and overreach of* intellectual property laws by well-established manufacturers to prevent small businesses on our sites from reselling legitimate and authentic goods and shutting down legal third-party supply chains. Not only are small businesses hurt by this anti-competitive use and

misuse of intellectual property laws, but consumers also end up paying unnecessarily higher prices because of this abusive and improper conduct.

There is an alarming trend by companies to control downstream distribution of their products after the goods have been sold and the manufacturers paid. Rights holders continually attempt to circumvent the "First Sale Doctrine," which protects consumers and resellers once they have bought a good protected by IP rights. The First Sale (or "exhaustion") Doctrine applies to copyrighted (17 U.S.C. §109), trademarked, and patented goods. It is rooted in the common law principle that purchasers have the right to alienate freely their own property. .

The First Sale Doctrine is intended to ensure that buyers who purchase legitimate products can resell them in secondary markets. Once an item is sold, the IP rights holder can no longer use intellectual property laws to control downstream distribution of goods. The First Sale Doctrine thus protects consumers' ability to gift, resell, or otherwise freely dispose of any copyrighted, trademarked, or patented item they purchase. Secondary markets, in turn, benefit consumers by giving them an opportunity to obtain such products at lower prices.

Since the inception of the First Sale Doctrine, some manufacturers try to stop legitimate customers rights by structuring or simply claiming that a transaction is a lease or "licensed" use of the product. Some manufacturers claim that by manufacturing and selling the product overseas, they can block further distribution on the theory that no authorized first "sale" ever occurred in the United States. Such conduct undermines the purposes of the First Sale Doctrine and undercuts secondary markets and the jobs that depend upon them while simultaneously harming consumer welfare.

Here are some recent examples of attempts to undermine the First Sale Doctrine:

- A manufacturer of paper towel dispensers has claimed that, because it allegedly leases its trademarked products to customers, listing such products for sale on eBay constitutes *an infringement of its IP rights*. The manufacturer has demanded that under IP laws (not contract law) the item must be taken off our site. The manufacturer is misusing IP law in an effort to restrain trade.

- Manufacturers are also trying to evade the First Sale Doctrine and control distribution by locating plants overseas. In *Costco v. Omega*, the U.S. Court of Appeals for the Ninth Circuit held that *Omega can use copyright law to bl*ock the distribution of legitimately purchased Omega watches by independent sellers in the United States as long as it manufactures and sells such products first abroad and places a tiny logo on those products.

- Software developers use license agreements to prevent the resale of software that has been purchased legitimately. The courts are split as to whether a "shrink wrap" license or EULA or other distribution agreements may be used in this manner. Just as consumers benefit enormously from the ability to buy used

books, they should not be denied the opportunity to buy used software or other digital goods that were legitimately purchased.

IP laws were never intended to bar the resale of lawfully purchased goods in this manner. Allowing IP rights owners to do so is anti-competitive, hamstrings innovation, and hurts U.S. small businesses (including importers) that rely on a robust secondary market in authentic goods for their survival.

Congress should prevent weakening of the long-established First Sale Doctrine. Manufacturers should not be permitted to use IP rights to bar resale of legitimately purchased goods, i.e., the manufacturer has already been paid. Nor should a manufacturer that manufactures overseas and sells a product be able to restrain further trade merely by placing a logo on the good. At a minimum, Congress should clarify that §109 of the Copyright Act, the Lanham Act, and the Patent Act embrace a robust First Sale Doctrine that protects small businesses and preserves free trade of protected works.

Balanced Enforcement Means Maintaining Well-Established Liability Protections

While eBay is a strong supporter of intellectual property enforcement and works tirelessly and successfully with law enforcement and rights owners to stop the traffic of counterfeit or pirated goods on its site, we have also flourished, like other online companies because of limitations and exceptions in intellectual property that were developed and designed to encourage innovation and investment. Liability exemptions that remain crucial for ecommerce include Section 512 of the Digital Millennium Copyright Act (DMCA) and Section 230 of the Communications Decency Act (CDA). These laws were expressly enacted to protect intellectual property rights while enhancing free speech and providing critically needed limitations on the liability of Internet and ecommerce intermediaries. We urge that any examination of any intellectual property enforcement and laws must recognize the importance of these liability protections for all intermediaries, such as eBay, which provide a platform for small businesses to succeed.

Balanced Enforcement Means Ensuring Fair Treatment Overseas

Finally, when our government works with other countries to reduce intellectual property crimes, eBay encourages our government to use those opportunities to advocate for the benefit of U.S. companies and to help guard against the extraterritorial application of excessive European trademark and selective distribution laws to the Internet to the detriment of U.S. exporters. Enforcement of European intellectual property rights for the purpose of suppressing legitimate channels of commerce in order to artificially maintain higher prices harms U.S. exporters and consumers. European luxury goods manufacturers (who manufacture the majority of their goods in lower-cost Asian job markets) have been most aggressive at using European courts to harass and extend global jurisdiction for their trademarks and selective distribution practices by filing lawsuits against U.S. Internet companies. We look to the leadership of this committee, Congress, and others policymakers to protect U.S. companies and businesses against such harms.

Intellectual property enforcement is important for small businesses, eBay, and consumers, but more importantly, *balanced* enforcement will ensure that small businesses, and the venues where those small businesses can succeed online, will flourish and grow. Online small businesses are the economic engine of the 21st century and those small businesses must not be subject to misuse of intellectual property laws by large businesses, the majority of whom are non-US companies.

Thank you, respectfully submitted.

Tod Cohen

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