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On Behalf of

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Before the

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District of Columbia

Hearing on

“Finding and Fighting Fakes: Reviewing the Strategy Targeting Organized Piracy”

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Mr. Chairman, members of the subcommittee, I am pleased to appear before you this morning to participate in a review of the Strategy Targeting Organized Piracy (the STOP initiative). The National Association of Manufacturers (NAM) commends you, Mr. Chairman, for holding this hearing on the vitally important subject of product counterfeiting and what is being done to stop it.

The NAM is the nation’s largest industrial trade association, representing small and large manufacturers in every industrial sector and in all 50 states, as well as 350 vertical industry associations and state manufacturing organizations. Understandably, therefore, the NAM is very concerned about the growing worldwide scourge of counterfeiting and copyright piracy.

Counterfeit products account for a staggering 5 to 7 percent of world trade -- a volume of almost \$500 billion annually. Counterfeiting not only violates the intellectual property rights of manufacturers, it also puts the safety of consumers at risk. Dangers range from ingestion of fake pharmaceuticals to accidents caused by substandard parts in rather important components such as replacement aircraft parts and automobile brake linings.

China, in particular, engages in unfair trade practices, including wholesale counterfeiting of U.S. products. They have huge factories dedicated to making products

that look exactly like U.S. brand name goods but don't meet the quality standards of the U.S. manufacturer. This is not cute. This is, as NAM President John Engler has said repeatedly, grand larceny on a massive scale. We are pleased that Secretary of Commerce Gutierrez stressed in his recent visit to Beijing that intellectual property abuse is a crime and needs to be treated as such. We applaud that he told the Chinese that, "Intellectual property rights are not up for negotiation. And frankly, the abuse of intellectual property rights is not acceptable."

The NAM met with a Chinese government intellectual property protection delegation earlier this month, when Vice Minister Ma visited Washington principally to discuss plans for the forthcoming meeting of the Joint Commission on Commerce and Trade (JCCT) – a bilateral commission I was privileged to staff for the U.S. side during part of my career at the U.S. Department of Commerce. In the NAM's meeting with the Chinese delegation, it was clear that while China is taking additional steps and is improving its laws, the effectiveness of enforcement in such a large country has a long way to go. While welcoming the steps the Chinese government is taking, the NAM made it plain that from our view, we are running out of time. We must see a sharp increase in enforcement, in criminal charges, and in convictions that put counterfeiters in jail.

Let me stress that counterfeiting is not just a serious problem for big companies. We hear from many of our small manufacturers that they are affected very strongly. Not only do they frequently find their market in China destroyed by Chinese-made fakes, but also their markets around the world can be ruined. The Subcommittee is hearing today from NAM member company Will-Burt on industrial and emergency lighting, and they are scarcely an isolated case. Tomorrow, the House Energy and Commerce Committee's Subcommittee on Commerce, Trade and Consumer Protection will hear from our member Uniweld, a Fort Lauderdale, Florida, manufacturer of manifolds that has found its markets as far away as in Saudi Arabia to be affected by Chinese-made counterfeit products.

### **The NAM's Role**

The National Association of Manufacturers has worked to make this issue a top priority for lawmakers and the Bush Administration. In 2003, the NAM Board of Directors approved a resolution calling for greater industry vigilance against counterfeiting. Responding to increasing member-company complaints about counterfeiting, the NAM formed its Product Counterfeiting Working Group. The membership reads like a Who's Who of industry sectors – including automotive and aerospace; textiles, apparel, and footwear; widely used consumer goods including personal care and toiletries; chemicals and pharmaceuticals; electronics and imaging supplies; distilled spirits, cigarettes and groceries. Most major manufacturing industry segments have a serious global counterfeiting problem.

The NAM has also helped launch the Coalition Against Counterfeiting and Piracy (CACCP), a broad coalition focused on this issue. The NAM shares the leadership in close partnership with the U.S. Chamber of Commerce. We are delighted that such an

experienced individual as the Chamber of Commerce's Brad Huther is the Executive Director for the coalition, and I am pleased to be on the same panel with him today. It is significant to note that this coalition represents the first time that the copyright side and the trademark side – that is, companies most hit by piracy and those most hit by counterfeiting – are working together formally.

### **The STOP Program**

The NAM heartily supports the Bush Administration's interagency STOP initiative – the Strategy Targeting Organized Piracy. The NAM Anti-Counterfeiting Working Group I mentioned above met repeatedly with senior Administration officials to discuss counterfeiting, including several meetings with Deputy U. S. Trade Representative Josette Shiner to discuss how government and industry might work together more closely to combat counterfeiting and piracy. Many of these ideas are reflected in the STOP program.

All of industry has a vital interest in the ongoing success of the STOP initiative. Indeed, Governor Engler made his first public appearance on behalf of the NAM as the incoming president at the October 4 STOP press conference to underscore our support for the initiative. The NAM applauds the increased attention in the Administration to the problem of counterfeiting and piracy that is manifested in the STOP initiative. We appreciate the increased efforts that Commerce (PTO, ITA and others), USTR, State and Homeland Security/Customs and Border Protection have made in increasing cooperation and coordination among themselves and in focusing on what steps can be taken to reduce counterfeiting and piracy.

Let me turn to the components of the STOP initiative for some specific observations. But before doing so, I want to state that the NAM is pleased with the quick start on implementing STOP, and in some ways the U.S. government is out ahead of U.S. business. American business needs to put more time and effort into documenting intellectual property violations so that the U.S. government has the depth and breadth of evidence it needs to make a convincing case to foreign governments and law enforcement officials.

The STOP initiative contains five key elements aimed at addressing counterfeiting and piracy on a global scale. I am going to focus, however, on STOP's application to China because Chinese counterfeiting is the most serious challenge to U.S. manufacturers. The NAM views Chinese counterfeiting as having three major dimensions: 1) the internal problem of counterfeiting within China; 2) the export of counterfeit goods from China to third countries; and 3) the export of counterfeit goods from China to the United States. The STOP program deals principally with the latter two of these. I would like to discuss several aspects of the program.

**Stopping trade in fakes at America's borders** -- This is a very important aspect of the initiative, one which the U.S. government has the most ability to control. The program has resulted in the use of new techniques and technologies to target shipments

that are more likely to contain counterfeit goods, and also includes new efforts to reach out to intellectual property right holders to improve the communication and an ability to ascertain whether shipments are genuine.

In the view of the NAM, this effort has brought about an improvement in the rate of intercepting counterfeit goods, and also provides the opportunity to experiment with new ways of further improving the success rate. Limited customs resources and the need to keep trade flow limit the number of containers that are opened at our borders. Technology, however, can help us better target suspect shipments and track down those trading in counterfeit products.

The NAM would like to work for a central computerized registry that would enable customs officers to be able to ascertain automatically whether individual shipments are authorized. While this will take some time to achieve, we believe it is a goal worthy of seeking. The problems are likely to be more serious on the private sector side as we look for feasible methods that do not slow international trade or pose too large a cost burden.

The NAM, both directly, and with the CACP, has had initial explorations of some possibilities with Customs and Border Protection (CBP), and we welcome CBP's willingness to explore options. The NAM sees great promise in the application of anti-terrorist methods to profiling and catching counterfeit and pirate shipments, another element of the STOP initiative. We understand that CBP faces numerous challenges and needs some level of stability in their pilot project before being able to accept outside industry data, but we are very eager to get going. Essentially, we are seeking to discover what discrete data elements, in what format, companies can submit to CBP so as to increase their ability to profile suspicious shipments and shippers.

**No Trade in Fakes Program** -- This initiative, to encourage companies to take steps to ensure their supply chains are free of counterfeit or pirated goods, was a challenge to industry to examine present controls and procedures. The NAM recognized early on that industry was going to have to take more responsibility for detecting and removing fakes from the stream of commerce, not leaving the whole matter to law enforcement. In 2003, the NAM Board of Directors adopted a resolution calling on member companies to exercise greater vigilance in this regard.

The No Trade in Fakes Program is one that the CACP has taken on behalf of U.S. industry, and the NAM is supporting that initiative within the coalition. Brad Huther, the CACP's Executive Director, has elaborated on this aspect of the STOP initiative in his testimony before the subcommittee. We are encouraged by the leadership within the coalition shown by the grocery and retail industries. The Grocery Manufacturers of America, along with neighboring associations, will be working on new guidelines and best practices document this summer. For its part, the pharmaceutical industry has been working closely with the Food and Drug Administration, which is the first civilian agency to have adopted a policy calling for adoption of Radio Frequency Identification Devices (RFID) in its relevant industry sector. Their initial efforts should provide useful

data and experience on how RFID can be applied more broadly by U.S. manufacturers to strengthen supply chain security. We have a considerable distance to travel, but, again, we appreciate the cooperation the U.S. government has extended thus far.

**International Cooperation** – The NAM views this aspect as especially important. The United States greatly needs more international cooperation in law enforcement and diplomacy, for two reasons that loom very large. The first is the sheer volume of counterfeit and pirate activity around the world. The second is the vast spread across so many countries, and the annual Special 301 report from USTR again confirms that 35-40 countries fail to afford adequate and effective protection to U.S. intellectual property rights.

Far too often, the United States has found itself in the lead in dealing with foreign countries containing large-scale piracy or counterfeiting, without commensurate interest on the part of other countries. Never has this need been so pressing when faced with the reality that a wide swath of the economy in China has not effective IPR enforcement, giving counterfeiters a free hand. If the United States stands alone in taking on this problem, which menaces not just Chinese consumers but consumers around the world, steals honest jobs, and besmirches good names, it cannot make enough progress.

There are several aspects to improving international cooperation. The first, of course, is to have others – particularly the European Union and Japan – raise their voices more loudly with respect to insisting that China increase enforcement of its intellectual property laws and reduce the incidence of counterfeiting and piracy. The NAM is pleased at recent statements and initiatives on the part of the European Union and Japan, but the visibility of their efforts still needs to be elevated so that China gets the message that its major trading partners want action. We still hear Chinese officials saying that the problem cannot be as serious as we make it out to be, for European and Japanese companies just don't see the problem in the same light.

The second is to increase third-country efforts to intercept shipments of counterfeit and pirated goods, both to prevent such goods from entering their own customs territories and to prevent their trans-shipment to the United States or other countries. U.S. Free Trade Agreements (FTA's) contain improved provisions and offer the opportunity of closer cooperation between U.S. and foreign enforcement authorities. I believe, however, that a couple of improvements are needed – improving U.S. law, as I will discuss later in my statement, and improving the attention to foreign trade zones. These zones are outside of the customs territories of countries, and are policed to a much less degree because of that. Such zones probably account for a disproportionate amount of trans-shipment of illegal goods, and we need to come up with better ways of dealing with that.

The third is to elevate the priority of fighting intellectual property theft on the part of multilateral organizations. Here, the NAM is pleased that the Organization for Economic Cooperation and Development (OECD) has overcome internal problems and will be conducting its first extensive analysis of global counterfeiting. We are also

delighted that the recent Asia-Pacific Economic Cooperation (APEC) meeting in Korea resulted in agreement that the nations bordering on the Pacific should increase their efforts to combat counterfeiting and piracy, including establishing guidelines for authorities to inspect, seize and destroy illegally-made goods and the equipment used to make them.

### **Need for Better U.S. Legislation**

That point, Mr. Chairman, the destruction of the machinery used to make counterfeit goods, is an excellent transition to my point on the need for better U.S. legislation, for while existing laws permit the destruction of equipment used to manufacture pirated goods violating copyright laws, they do not permit the destruction of equipment used to manufacture counterfeit goods that violate trademarks. This must be fixed on an urgent basis.

Legislation that would fix this was just passed by the House, in the form of H.R. 32, the "Stop Counterfeiting in Manufactured Goods Act." Sponsored by Representative Joe Knollenberg of Michigan, the bill would strengthen U.S. law by allowing the seizure and destruction of machinery and equipment used by counterfeiters and traffickers in the United States.

Today, only the counterfeited inventory can be seized, and even that is discretionary; machinery used to make the fake goods cannot be seized at all. Additionally, the bill plugs the loophole through which unlabeled counterfeit goods may be brought into the country and the labels then applied later. Put these two weaknesses together, and you have a gaping import hole, under which shoddy no-name merchandise from China or anywhere else, for that matter, can be shipped into the United States, and Customs and Border Patrol has no grounds under IP laws to interfere with the entry.

What makes the weakness of the trademark counterfeiting remedies so odd is that the copyright piracy remedies are so much stronger. Seizure of inventory is mandatory, and seizure of equipment is provided for. We will not be able to make a convincing case to our trading partners that they should take tough action against counterfeiters, including the seizure of equipment used in this illegal practice, if U.S. legislation does not authorize our law enforcement officials and courts to take similar action.

We honestly see no rational reason not to move this legislation as fast as possible. Passing this legislation is a top priority for the NAM. While the Senate Judiciary Committee has jurisdiction over Senate consideration of the Knollenberg bill, the NAM hopes that you, Mr. Chairman, and all members of this subcommittee and the full committee will press for quick Senate adoption of the bill so that we can improve U.S. law and boost the ability to fight fakes. H.R. 32 by no means exhausts our legislative interests, but it will be hard for us to move on to anything else until we get this urgent business taken care of.

## **More Must be Done for Small and Medium-Sized Firms**

I have reserved my discussion of one of the most important aspects of the STOP program for last – because it is the area in which I believe we all need to accelerate our efforts. The STOP program established a “hotline” that for the first time provides a one-stop shop for smaller firms that generally lack the resources to understand their rights and seek redress when their rights are violated. This website is a good beginning, but we all need to work to make it better. Far too few small firms have registered their trademarks in China, for example. Without such registration, they have no rights.

Many of the major multinationals doing business in China, most of them NAM member companies, have banded together as the Quality Brands Protection Committee (QBPC), operating under the China Association of Enterprises with Foreign Investment. For several years, the QBPC has been encouraging prosecutors to bring the most far-reaching and visible cases against offenders and producing criminal convictions. This work is entirely necessary. At the same time, major multinationals have their own legal and enforcement staffs in China and also retain investigators so as to hand over enough evidence to local authorities to instigate seizures and arrests.

But where does this leave small manufacturers that have no personnel in China? All that they know is that fake products “Made in China” are for sale. Typically, even if the products are for sale in China and elsewhere around the world, the small U.S. manufacturer will discover the presence of counterfeits in the stream of commerce in the United States in one of several ways:

- Web site monitoring
- Trade show monitoring
- Customer service calls from those who have unknowingly bought fakes.

A small manufacturer, for example, a company of fewer than 500 employees, which typically has one or two lawyers to handle all legal matters has no way of knowing from where in China the fake products come.

The NAM and the other groups in the CACP will be developing specific ideas for how small companies might better be able to cope with the epidemic of counterfeiting. We believe it would be worthwhile to sit down with the subcommittee staff and with representatives of the Administration to explore some of these ideas. We would like to explore, for example, whether some form of “public defender” for small and mid-size firms might be feasible, or whether the U.S. government can play more of a role in third countries through diplomatic channels when it comes to stopping the sale of fakes. Additionally, there may be some way in which the resources of the government can be used to reduce some of the costs of investigating possible instances of counterfeiting, particularly in China.

Finally, Mr. Chairman, the NAM has suggested to the Chinese government that it would be very useful were the Chinese embassy and Chinese consulates around the United States to provide a means for U.S. companies to better understand how to protect their intellectual property rights in China.

Before concluding my statement, Mr. Chairman, let me be clear that China is not the only problem. Counterfeiting and piracy are occurring in many other countries as well. In Russia, it is estimated that U.S. companies lost over \$1.7 billion in sales to pirated optical discs and over \$7 billion in the last 8 years. The focus in Russia is now on copyright piracy. But manufacturers are also concerned that weak IPR laws and poor enforcement in Russia will lead to rampant counterfeiting of trademarked products down the road, just as has occurred in China. We need to insist on effective IPR protection as a condition for WTO membership.

Thank you, Mr. Chairman.