

Statement of Senator Carl Levin
U.S.-China Economic and Security Review Commission Hearing on
Intellectual Property Rights Issues and Dangers of Counterfeited Goods
Imported Into the United States
June 7, 2006

Thank you for holding this hearing on intellectual property rights issues and the dangers of counterfeited goods imported into the United States. I appreciate the opportunity to testify on the issue of counterfeit auto parts, which is a growing problem with public health, safety as well as economic implications. Product counterfeiting is one of the U.S. auto parts industry's greatest concerns with China – along with currency manipulation and the ongoing U.S., European Union and Canadian WTO case challenging China's auto parts tariffs. So this morning's hearing is both timely and critical.

Today, I'd like to discuss the scope of the auto parts counterfeiting problem; why it matters; and how we can attack it effectively.

Scope of the Problem

Product counterfeiting and piracy has long been associated with knock-off watches and handbags. But counterfeiting has exploded in recent years across many industries to become a serious threat to the competitiveness of the U.S. economy. One of the greatest assets of American businesses is their intellectual property, but when American innovations can quickly be stolen by competitors around the world the vitality of those businesses is at risk. The FBI estimates that counterfeiting costs U.S. businesses \$200 billion to \$250 billion annually, and growing. Counterfeiting money is a serious crime and treated as such. Counterfeiting auto parts should be treated the same way.

China is one of the worst piracy offenders, accounting for 70 percent of all imported counterfeit products seized by U.S. Customs and Border Protection in 2003. It is estimated that counterfeits constitute an alarming 15 percent to 20 percent of all products made in China and account for about 8 percent of China's total GDP.

The U.S. auto parts industry conservatively estimates it loses \$12 billion in annually to counterfeit auto parts: \$9 billion outside the United States and \$3 billion inside the U.S. China is responsible for about 75 percent of those counterfeit auto parts, according to estimates by American automotive suppliers. The auto parts industry estimates millions of counterfeit auto parts enter the U.S. every year and only a fraction of them are ever detected at the border by U.S. enforcement officials.

Virtually every automotive part has turned up in the counterfeit trade, including windshield glass, brake fluid, headlights, taillights, emissions components, structural parts, sheet metal parts, suspension parts, tires, belts, hoses, and alternators. The industry has found enough different fake parts being sold in U.S. stores to construct an entire car.

And the problem is now spreading beyond just auto parts. The theft of intellectual property in China has become so widespread and bold that recently an entire car was copied, manufactured and sold under a different name – sold not as a “Chevy” but a “Chery QQ”. The counterfeiter even had plans to export the knock off to the United States.

Why it Matters

Counterfeiting hurts U.S. manufacturers and the unsuspecting public that buys fake parts in many ways. Here are a few of the biggest problems:

- Counterfeit and pirated automotive parts mean lost revenue and jobs in the United States. The FTC estimates that the auto industry could hire 250,000 additional American workers if the sale of counterfeit parts were eliminated. This is in an industry that has already suffered many layoffs and bankruptcies in recent years.
- American manufacturers have a difficult enough time to get a foothold in the Chinese market: if that market is permeated by counterfeit products American manufacturers should rightly be making, it is that much more difficult.
- Counterfeit parts hurt the legitimate producer’s brand name and reputation here and abroad because these products are substandard.
- The U.S. Immigration and Customs Enforcement (ICE), has noticed connections between counterfeiting and organized crime, gang activity and terrorism. Because it is easier, more lucrative, and carries fewer penalties than drug smuggling, counterfeiting is becoming the activity of choice of criminal groups and even terrorists.
- Fake parts also undermine U.S. safety standards and put customers at risk. For example, components such as brakes have been found that were made of compressed grass and wood.

I brought some examples of counterfeit parts to show you how sophisticated counterfeiters have become in making fake products that look and feel identical to the originals.

Here are connecting rods for a Ford car, one genuine and one counterfeit. These are steel structural parts that connect the front end of the car to the body. While the products may look identical, including the Ford logo cast into the fake product, the quality and strength of the steel in Ford’s product is much higher and the machining of the grooves, or “teeth” in the circular ring is much better. If those grooves wear down too quickly with use, the front end of the car could wobble and become unstable. This in turn will put stress on the arm, increasing wear, metal fatigue, and risking failure [in a collision or even normal use.] In short, this is a safety-related item, and the fake product presents a hazard to an unsuspecting driver.

I also have a genuine Ford spark plug wire set and a counterfeit set. Again, although these parts and their packaging may look identical to the untrained eye, the counterfeit part uses substandard gauge wire, substandard insulation, and substandard connectors, which can lead to overheating and fire.

With counterfeit auto parts, the concern goes way beyond the monetary losses like those suffered by a company when a handbag is copied or a high end watch counterfeited. When the connecting rod on your car is fake or your brakes are made of compressed grass and wood, your life and the lives of your loved ones are at risk.

What to do about it

To date there has been a lack of willingness to initiate criminal cases against auto parts counterfeiters because it was not viewed as a serious enough problem by the Department of Justice. Ten thousand sets of counterfeit automobile brakes isn't viewed the same way as a drug case but string the counterfeits together and it adds up to \$12 billion lost to industry each year. The increasing risk to the health of our economy, loss of jobs, the safety of unsuspecting consumers makes changing that perception a vital national priority. The bottom line is that counterfeiting is a serious and growing crime, and the Justice Department should be doing more to fight it.

To date industry knows of only one prosecution for auto parts counterfeiting. The Department of Justice told us they were unaware of any pending case.

The WTO TRIPS Agreement China signed requires member countries to have an effective intellectual property rights (IPR) enforcement mechanism. China may have IPR laws that appear reasonable on the books, but it is not enforcing them. USTR warned China it was considering bringing a case in the WTO against China for failing to enforce its IPR laws, but nothing has materialized to date.

USTR is a paper tiger, I'm afraid. On April 29, 2005, the USTR placed China on the Special 301 Priority Watch List because of its failure to improve protections for U.S. intellectual property rights there. Yet China continues to fail to do so. There China sits while our government dawdles. We need to stop merely putting China on lists and start taking more effective action. We need an enforcement office to pursue trade cases against countries that fail to meet commitments to reduce IPR infringement levels.

Because of the lack of government leadership, the auto industry has had to do too much of the policing itself and at great expense. The automotive industry through its trade associations is working to educate its suppliers and distributors and to train employees purchasing parts on how to detect counterfeit products. U.S. parts companies know they are on the front line.

So to coordinate its efforts, the U.S. auto parts industry created the Coalition Against Counterfeiting and Piracy (CACP). CACP's detection and Enforcement task force issued a report last fall on ways to improve detection and enforcement of counterfeiting and piracy. I want to mention four of their proposals that involve government action. The first is to deploy Intellectual Property Rights staff at foreign embassies. The second is for the government to share information about intellectual property violators so companies can avoid becoming victims of known offenders. The third is to address the needs of small and medium-sized enterprises,

which are particularly vulnerable. And the fourth is to raise standards at foreign trade shows. I urge the Commission take a serious look at these proposals and to encourage their implementation.

I ask that the report and its recommendations be included in the hearing record.

We need strong and fast prosecution of auto parts counterfeiters. If the government won't act against currency manipulation by our trading partners as they should, if it won't force open export markets for U.S. products blocked by tariff and non-tariff barriers and aggressively enforce U.S. trade laws as they should, the least it can do is enforce our anti-counterfeiting laws.

Counterfeiting auto parts is a booming industry, and allowing it to continue unabated would have huge consequences for our country. Counterfeiting presents a grave threat to our automakers, auto parts makers, to our economy and also to the safety and security of all Americans. China is a particularly grave offender, and its violations must be addressed immediately. The U.S.-China Economic and Security Review Commission is uniquely positioned to give this issue the weight it deserves, and I hope you will do so. Thank you for the opportunity to testify before you today.