



As prepared for submission

**U.S. CHAMBER OF COMMERCE VIEWS ON
CHINA'S ENFORCEMENT OF INTELLECTUAL
PROPERTY RIGHTS AND THE DANGERS OF THE
MOVEMENT OF COUNTERFEITED AND PIRATED
GOODS INTO THE UNITED STATES**

Testimony

**Before the US-China Economic and
Security Review Commission**

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On behalf of the US Chamber of Commerce, I am delighted to have this opportunity to offer our organization's views on the importance of intellectual property (IP) protection in China.

As the world's largest business federation representing more than three million members, the U.S. Chamber of Commerce is keenly aware of the threats posed by counterfeiting and piracy to the well-being of American firms and workers. In today's Information Age, intellectual property rights (IPR) constitute the new "gold standard." Strengthening IP protection is essential to achieving economic prosperity in this new era.

A Global Challenge

IPR theft goes by many names: counterfeiting, piracy, knockoffs, imitations.

Copies of brand names and copyright works are taking increasing market share away from lawful businesses in an ever-widening range of industries. In earlier times, the problem was mostly associated with luxury goods; but today, it impacts almost every industry, including both consumer and industrial goods. The list of items targeted by counterfeiters is almost endless, ranging from pharmaceuticals to auto parts, food, beverages, cosmetics, electronic appliances, batteries, and computer peripherals. Copyright piracy meanwhile remains at extreme levels for entertainment and business software, movies, music, and books. And the problem will get worse before it gets better, particularly as more and more illegal business is promoted and conducted through the Internet.

Anecdotal reports from industry further indicate that IPR violations—including those emanating in China—are not just impacting large corporations. Increasingly, counterfeiters are targeting American small and medium-sized enterprises (SMEs) and thereby seriously undermining their ability to compete in global markets. Many SME victims do not have operations in China, and have fewer resources to pursue investigations and legal actions against pirates in China and their middlemen in other countries.

IPR infringement is clearly a world-wide problem, and any solutions require a global perspective. They also require more concerted efforts among business and governments in a number of key countries—including particularly China and the United States.

Hidden Harm

Counterfeiting and piracy are clearly costing American companies billions of dollars annually by stealing away market share and reducing overall demand for legitimate products.

It has been estimated by U.S. Customs and Border Protection that counterfeiting and piracy cost the U.S. economy between \$200-\$250 billion in global sales annually, consequently displacing 750,000 American jobs.

But while this harm by itself is a serious concern, it is essential to consider the other types of damage that are inflicted upon society by counterfeiting and piracy.

The most obvious threats include the risks to public safety and human health. Just last week, nine patients at a hospital in Guangzhou, China died after receiving fake medicines that proved to be toxic. These problems are not limited to China's borders, as there have been increasing reports of fake drugs—including many emanating from China—finding their way to U.S. shores.

In fact, in a highly publicized case, the U.S. Federal Drug Administration recently seized 51 shipments of so-called "generic Tamiflu" that was on its way to U.S. consumers from China. And in another frightening example of how counterfeit pharmaceuticals from China are now affecting average Americans, a licensed pharmacist in Houston, James George, was convicted earlier this month of conspiracy to introduce into the U.S. market counterfeit and misbranded pharmaceutical drugs as well as trafficking in counterfeit drugs from China.

The World Health Organization (WHO) recently estimated that counterfeit drugs account for 10% of all pharmaceuticals sold globally. Incredibly, in some developing countries, the WHO believes that this number is as high as 60%.

Counterfeiting and piracy also deprive governments of enormous tax revenues. In New York City alone, it has been estimated that tax losses caused by counterfeiting exceed US\$1 billion annually. The diversion of legitimate trade denies government at all levels badly-needed revenues. Meanwhile, it is extremely rare to find counterfeiters and copyright pirates paying any taxes whatsoever.

Then there is the impact of fakes on corporate investment and innovation. The U.S. Chamber has found American SME's particularly vulnerable in this regard.

Last but not least is the cost of investigating and prosecuting infringers. Some companies spend millions of dollars annually in tracking down infringers, mostly with results that are far from cost-effective.

And with increasing reports of counterfeiting and piracy, law enforcement agencies are being called upon to do more, often with fewer resources than they had a few years ago. Since government resources are limited, counterfeiting and piracy must compete with other types of crime, presenting local and federal government agencies with extremely difficult choices.

On top of all this is the link between IPR theft, terrorism, and organized crime. National and intergovernmental agencies such as INTERPOL have observed that counterfeiting and copyright piracy are now among the preferred sources of income for terrorists and organized criminal networks, both in the U.S. and abroad.

The U.S. Chamber: Making a Difference

The scope and scale of harm caused by the rising tide of IPR theft has motivated the U.S. Chamber to embark on a wide range of initiatives to deal with the problem—initiatives that are intended to make a real difference.

The U.S. Chamber is aggressively implementing a three-part IPR strategy.

First, we are educating businesses, media, and lawmakers on the growing threats posed by counterfeiting and piracy in the United States.

As part of our efforts, the U.S. Chamber established the Coalition against Counterfeiting and Piracy (CACP) with the National Association of Manufacturers (NAM) to coordinate the efforts of the business community to stop counterfeiting and piracy. CACP is committed to increasing the understanding of the negative impact of counterfeiting and piracy by working with Congress and the administration to drive government-wide efforts to address this threat.

Second, we are securing the supply chain by toughening existing laws and increasing detection and enforcement efforts.

The Chamber is creating a framework to strengthen links between federal, state, and municipal enforcement officials such as Department of Justice prosecutors, Customs and Border Protection agents, the FBI, police, state prosecutors and district attorneys, and INTERPOL. We have hired investigators to assist law enforcement officials by detecting and investigating trafficking, particularly with respect to goods that impact health and safety.

The Chamber is also working with Congress to strengthen U.S. IPR laws, thereby closing loopholes in existing legislation and ensuring that resources expended by both industry and government enforcement agencies are more effective, as well as cost-effective. Most recently, the Chamber helped to secure congressional support for the Stop Counterfeiting in Manufactured Goods Act, which was signed into law by the President on March 16, 2006. This legislation closes loopholes that previously allowed counterfeiters to avoid prosecution entirely by importing products and infringing labels separately. It also strengthens the ability of the government and IP owners to seize the illegal proceeds of counterfeiters and copyright pirates—thereby hurting them where it counts most—their wallets.

Third, we are engaging internationally in China, Brazil, India, Russia, and Korea to strengthen global IP protection and enforcement by working with key stakeholders on policy advocacy and education, capacity building, data collection, coalition development, and consumer awareness campaigns.

CHINA: An Opportunity and Challenge

Our bilateral relationship with the People's Republic of China (PRC) is of immense and increasing importance to both the U.S. and Chinese economies and business communities. U.S.-China trade has boomed in recent years, and the trend is only growing. The United States ranked second among China's global trading partners in 2005, and China was again the 3rd largest trading partner for the United States. U.S. exports to China have grown by 150% since 2000, making China the United States' fourth largest export market in 2005, compared to the fifth largest in 2004.

Exports of U.S.-made goods have clearly been increasing. For example, from 2004 to 2005, exports of U.S. aerospace products and components increased by 115%, electrical equipment exports increased by 13%, and optics and medical equipment exports increased by more than 15%. These statistics underscore the opportunities that China offers to U.S. exporters, to

investors, and, more broadly, to U.S. economic development—particularly in high-technology sectors.

China's growing middle class is also an engine for the sale of American-made consumer goods. McKinsey estimates that the number of middle-class households in China will jump to 105 million in 2009, up from just 36 million in 2004. In 2025, middle-class Chinese will likely constitute one of the largest consumer markets in the world, spending about RMB 20 trillion (US\$2.5 trillion at today's exchange rate) or almost as much as all Japanese households currently spend. China's urban population has demonstrated a liking for imported goods and American brands. As consumer spending increases and China's tariffs decrease, exports from the U.S. will certainly rise, as will sales of goods incorporating American technology.

Notwithstanding the importance today and future promise to American business of the commercial relationship, the Chamber recognizes the escalating concerns in many quarters over the growth and direction of China trade...the ballooning bilateral trade deficit, rising competition from Chinese-made imports, consternation over China's currency practices, and clearly inadequate enforcement of American IPR.

Let me be perfectly clear. The Chamber believes China has failed to adequately enforce its own laws against counterfeiting and copyright piracy, thereby putting into question China's compliance with its obligations under the World Trade Organization (WTO) and various other bilateral agreements and accords. We believe not only that enforcement is lax, but that relevant laws, regulations, and policies relating to IPR enforcement are ambiguous and contain too many loopholes—all of which need to be addressed as soon as possible.

Given the enormous harm that is being inflicted, the U.S. Chamber feels strongly that China must do significantly more to comply fully with both the spirit and the letter of its World Trade Organization (WTO) commitments to respect IPR.

Scope of the IP Problem

Upon joining the WTO over four years ago, China agreed to fully comply immediately upon its accession with the provisions of the Agreement on the Trade-Related Aspects of Intellectual Property Rights—the so-called “TRIPS Agreement”. While a number of legislative changes and enforcement campaigns have been introduced since 2001, it is clear to most in U.S. industry that the level of infringement in the market has not improved significantly and that enforcement measures introduced by the government have been inadequate. China is generally obligated under the TRIPS Agreement to provide access to enforcement of foreign IPR which is “effective” and creates “deterrence”. Yet China continues to fall short in adhering to these obligations as well as some IP undertakings set out in accords reached during the Joint Commission on Commerce and Trade (JCCT) meetings held in 2004 and 2005.

According to the American Chamber of Commerce in China (AmCham) 2006 annual survey of its members, China's enforcement of IPR deteriorated or failed to improve over the last year. According to the survey, 41% of U.S. companies said that counterfeits of their products increased in 2005. Other industry surveys similarly suggest that counterfeiting has likewise worsened or remained the same for the vast majority of companies polled and that exports of Chinese-made fakes pose a serious business challenge in markets outside the PRC.

Alarming, counterfeits of many of the more widely-used pharmaceuticals in China are said to occupy 30% or more of the market.

There is now little doubt, based on hard data from government and industry, that China is the single largest source of counterfeit and pirated products exported worldwide. The U.S. Department of Homeland Security estimates that from 2004 to 2005, China's share of total IPR infringing product seized at the U.S. border increased from 63 to 69 percent. China's share of border seizures is more than ten times greater than that of any other U.S. trading partner.

Meanwhile, losses in China for U.S.-based copyright industries in 2005 were estimated by the International Intellectual Property Alliance (IIPA) to amount to about \$2.69 billion—thereby imposing a severe drain on the U.S. economy. IIPA and its member associations estimate that the market share of pirated movies, music, and business and entertainment software continues to hover around 90%, much as it has for years. And this is notwithstanding the remarkable increase in buying-power of Chinese consumers and their demonstrated preference for American copyright works.

As suggested above, the lack of more adequate protection for American copyright works stems in part from loopholes in Chinese laws and regulations. But government policies are clearly tilted against greater resource allocation for copyright enforcement—particularly criminal enforcement.

Adding insult to injury, the Chinese government continues to maintain severe market access restrictions on entertainment industries, generally—barriers which are more severe than for virtually any other sector of the U.S. economy. These limits on market access significantly hamper the fight against piracy inside China by depriving American copyright owners of a more solid presence in the market, including distributors, licensees, and other allies within local industry that might help in combating piracy.

The use of the Internet in China is growing dramatically and is now estimated at over 111 million users. Consequently, copyright piracy through the Internet is quickly becoming a grave threat—one which reminds us that losses in American jobs and business revenues will only be higher in years to come if the problem is not addressed more effectively. Relevant Chinese authorities recently conducted a very tardy and non-transparent consultation process with foreign industry in bringing forward China's new Internet Law. Although U.S. industry is still assessing the new Law, it appears to contain many flaws and loopholes that pirates could exploit.

But the news is not entirely negative. According to the Business Software Alliance, China's software piracy rate last year declined four percentage points—from 90 percent in 2004 to 86 percent in 2005. At the same time, the estimated market value of the pirated software in use in China increased from \$3.6 billion in 2004 to at \$3.9 billion in 2005, due to increased sales of computer hardware. Thus, while the respect for copyright in software is increasing somewhat, the actual losses being suffered by American industry remain among the highest in the world.

As the U.S. Chamber stated in its fall 2005 report on China's WTO implementation record, effective enforcement of IPR, in particular criminal enforcement, will require the national government in China to look carefully at the flaws and loopholes in their laws. Of equal, if not greater importance, is the need for substantially stronger commitments from provincial,

municipal, and county-level governments to increase proactive intervention, enforcement resources, and the political priority accorded to IPR protection, as well as to deal more resolutely with protectionism.

Constructive Engagement

China needs to continue to hear the consistent, open and honest views of foreign governments on concerns over IPR protection. The Chamber believes IPR should remain one of the top, if not the top, economic and commercial policy concern of developed countries in their bilateral relations with China.

Industry will continue doing its part to support bilateral engagement on IPR. The U.S. Chamber is committed now for the long-haul in promoting constructive engagement with the Chinese government, not only at the national level, but also at the provincial and municipal levels. We know from experience that there are demonstrable benefits to be generated from organizing enforcement training seminars, dialogue with government and other stakeholders, and expert exchanges.

While the challenges appear vast, there is clearly a basis for optimism, as China is now awakening to the need for stronger IPR protection not only to satisfy the needs of foreign investors, but for the development of domestic industry.

Indeed, IPR violations could pose a greater threat to China's own economic development and security than they do to foreign rights holders. This stems, in part, from direct infringements (i.e., Chinese infringing Chinese); this also results from the displacement of domestic sales that occurs when pirates target foreign brands and copyright works. Therefore, it is very much in China's own interest to take significantly bolder measures that crack down on IPR infringements and achieve real reductions in the current levels of counterfeiting and piracy.

Increasing Cooperation and Transparency

In the last year, the U.S. Chamber has observed new levels of openness and cooperation on IPR within the Chinese government authorities as well as an increased commitment among various levels of the government to address IP issues. These are positive signs that should be encouraged in every way possible.

During his visit to the U.S. in April, President Hu Jintao stated that the protection of IPR is "essential" for China's economic development. In February, Vice Premier Wu Yi announced that China would "continue to consolidate IPR enforcement, rigorously clamp down on IPR-infringing activities in accordance with law, ... outline an action plan on IPR protection, and ... subject criminals and infringers to applicable punishments."

These commitments by China's leaders, along with statements made at the March National People's Congress meeting by Supreme People's Court President Xiao Yang and Procurator-General Jia Chunwang about the need to combat piracy, appear to signal an increased commitment by the central government to improve IPR protection and enforcement.

China's leadership, thus, is now saying the right things on a regular basis about IP creation, protection, and enforcement. Discussions on IP matters between U.S. and Chinese government officials and between the US and Chinese private sectors are increasingly robust. The U.S. Chamber believes China's growing interest in developing its own IP is a noteworthy trend; a country is much more likely to protect and enforce the IP rights of US companies once it has its own IP to protect.

In this regard, the U.S. Chamber welcomes the recent judgment by the Beijing No. 1 Intermediate People's Court to uphold the Viagra patent. As China's economy continues to grow and develop into a more knowledge-based economy, businesses, both foreign and domestic, will require a dependable patent system. This decision should help significantly to promote investment by knowledge-based industries, including the pharmaceutical sector.

We are also seeing what we regard as some important process-oriented changes at the central level that could, over time, lead to measurable improvements in enforcement. For example, in the past, the many ministries responsible for IP protection and enforcement in China had little, if any, coordination. Following the establishment in 2004 of a National Working Group for IPR Protection under Vice Premier Wu Yi, there are clearly indications of greater coordination across the Ministry of Commerce (MOFCOM), the Procuratorate, the Ministry of Public Security, the State Administration of Industry and Commerce (SAIC), the National Copyright Administration, and the General Administration of Customs.

However, even as we appreciate the government's increased level of awareness of the importance of IP protection, we are cognizant that China's desire to ascend the value chain and develop an economy based on innovation rather than low-cost manufacturing are driving its new focus on IP.

In this regard, the Chamber is monitoring closely China's post-WTO accession use of industrial policies—including antitrust law, standard setting, and patent reform—to foster the development of strategic sectors and reduce the value of foreign-held IPR. Although this topic is not the focus of today's hearing, we are closely tracking several different draft laws and regulations that could substantially weaken legal protection for U.S. rights' holders, and I would be happy to take any questions on this subject.

Need for Deeper Legal Reforms and Additional Police Resources

The Chamber is working closely with Chinese authorities to outline the existing structural and legal problems as well as successful strategies that can be applied to reduce the level of counterfeiting and piracy.

In our regular meetings with high-level IP officials, we stress the critical need for China to create an enforcement system that effectively deters IP violators and, most importantly, that addresses its continuing over-reliance on administrative enforcement.

Less than one percent of the total copyright and trademark cases handled by administrative enforcement authorities were turned over to the police for prosecution in 2005. To illustrate, out of almost 40,000 cases in 2005, local Administrations for Industry and Commerce (AICs) transferred only 230 cases for criminal investigation.

Criminal convictions of IPR offenders in China in 2005 increased 24%. While this statistic is encouraging, it is woefully insufficient compared to the current needs. Indeed, even if the number of arrests and convictions continue to increase annually by 50%, the number of criminal actions would still remain far too low in relative terms for some time to come.

Boosting criminal enforcement of IP will clearly require dramatically greater resources and training for Chinese police—who are already notoriously under-resourced for IP enforcement. IP owners—particularly SMEs—need Chinese police to be user-friendly. Proactive investigations by Chinese police are particularly needed in cases which are difficult to investigate privately, e.g., cases involving large syndicates and those that operate in the shadows of cyberspace.

Progress in criminal enforcement will also require amendments to judicial interpretations and (we believe) China's Criminal Code itself to create a more credible and effective framework for criminal action against more egregious IPR offenders.

The American government and industry will need to maintain focus on these obvious structural problems in China's IPR enforcement system in ongoing dialogues with the central government. Given the scope and seriousness of the challenge, particularly at the provincial and local levels, China's heightened awareness of the commercial benefits of IP, its discussions with foreign governments and business representatives, and process-oriented changes, alone, will not lead to tangible improvements in the IP environment for U.S. companies.

China's IP Action Plan

In earlier congressional hearings, the Chamber has voiced our concerns over the need for a wide range of legal and policy reforms to boost IPR enforcement, as well as for a comprehensive action plan to ensure proper implementation and coordination of these reforms. In an encouraging sign, on March 8, 2006, the Chinese government issued a new Action Plan on IPR Protection which provides the most comprehensive blueprint ever issued by the Chinese government to promote respect for IPR.

Regrettably, some of the core concerns of American industry are not adequately addressed in the Action Plan. However, the contents of the plan provide a clearer basis for engagement with China over the implementation of promised reforms.

The U.S. Chamber will continue to engage MOFCOM and other enforcement agencies in the Chinese government to remain focused on implementing the Action Plan, and also expanding its scope to cover important problems not addressed therein. We will in particular be focusing priority attention on the following:

- First, the Action Plan indicates the intention to amend all of China's main IP legislation by 2008. However, the plan makes no mention of the intention to amend the IP provisions in China's Criminal Code. The Chamber and others in industry have made clear the need for China to eliminate gaping loopholes in the Criminal Code and provide more detailed provisions for dealing with infringements in the internet era. The Chamber

is therefore working with the US business community to push for a commitment by the National People's Congress to amend the Criminal Code no later than 2008.

- Second, we are pleased that the Plan calls for an impact analysis of the December 2004 Judicial Interpretation (JI) of the Supreme People's Court and Supreme People's Procuratorate, which lowered the numerical thresholds for IPR crimes. As we have stated in the past, the Criminal Code and JI, together, lack clear standards for the calculation of case values. Currently, local police and other authorities use widely divergent methods of valuing fake products—some by reference to the infringer's declared price, normally without evidentiary support. The JI also fails to provide enough non-numerical criteria for criminalization of cases. To illustrate, there are currently no provisions in the JI for criminal enforcement against repeat offenders, or criteria that would facilitate easier prosecution of cases involving underground factories, pharmaceuticals, food, and auto parts.
- Third, the Action Plan refers to new measures to be introduced to facilitate the transfer of administrative cases to the police for criminal investigation. The promotion of criminal transfers was a key commitment of the Chinese government set out in the 2005 JCCT accord. The Chamber has been pleased to note the issuance between January and March of four regulations by the Ministry of Public Security together with other authorities that have a role in criminal transfers (including the Supreme People's Procuratorate, the General Administration of Customs, the State Administration for Industry and Commerce and the National Copyright Administration). Each of the regulations clarify the responsibility, procedures, and deadlines for administrative authorities to evaluate and transfer suspected criminal cases to the Public Security Bureaus (PSBs).

While it is yet unclear what impact these regulations will have on contributing to effective deterrence, this action shows a desire by the central government to help overcome institutional barriers to increasing criminal enforcement. That said, the Chamber has noted language in three of these regulations which seems to give discretion to police to reject cases which meet the numerical thresholds for criminalization on the basis that they are "inconsequential" or otherwise do not warrant criminal action. The Chamber will be seeking clarification from relevant authorities on this language, which to date remains undefined. The Chamber also remains concerned as to whether these rules will be implemented in a manner that promotes on-the-spot referrals from administrative to criminal authorities where there is a "reasonable suspicion" that the infringer has committed acts which, upon further investigation, would meet the criminal threshold.

- Fourth, the Chamber was pleased to note plans to issue new regulations that appear intended to strengthen the deterrent impact of administrative enforcement measures, including fines. The Trademark Office of the State Administration for Industry and Commerce has indicated since 2002 plans to issue such regulations, but for reasons which are not entirely clear, they have not yet been issued. Consequently, fines imposed in administrative enforcement cases are normally so low as to constitute a mere cost of doing business for most infringers, let alone a deterrent to further infringement.

The Chamber was also heartened by China's commitment at the April 2006 JCCT to require the pre-loading of legal operation system software on all computers produced or imported into China as well as its issuance of a notice requiring government agencies to purchase computers with pre-

loaded software. If the new notices are effectively implemented, this new requirement could make a significant contribution to curbing software piracy in China.

As the dust settles on the April 2006 JCCT meeting, we hope that additional progress will be forthcoming soon in cracking down on optical disc piracy, creating a software asset management system, and increasing transparency in rule-making and statistical reporting of cases and criminal penalties.

However, even as we note these examples of progress, these steps taken by the Chinese government and judiciary over the last year have achieved very little, if any, reduction in the level of infringement in the market.

As we indicated at the outset, the problem remains as serious today as it was a year ago. Administrative penalties—still the mainstay of the current trademark and copyright enforcement system in China—remain grossly inadequate and in most cases create no deterrent to further infringements. Moreover, serious obstacles still remain in the transfer of most administrative cases to the police.

One such obstacle is the lack of police resources and training to ensure that officials at the local level have the capability to support the regulatory and infrastructure changes in China's IPR enforcement regime. Without the allocation of additional police resources targeted at IP hotspots, China's provincial and local security bureaus will be unable to bring rampant counterfeiting and piracy under control.

U.S. Chamber Action Plan

The U.S. Chamber is supporting the Chinese government in its efforts to extend greater protection to foreign and Chinese IP owners. We have embarked on a targeted program offering on the ground capacity-building efforts in the provinces, fostering public awareness of the importance of IPR protection among the Chinese public, and advising on policy changes to better strengthen the legal framework.

The four main components of the U.S. Chamber action plan include:

- (1) Spearheading high level dialogues with Chinese business and government leaders including here in Washington DC in 2005 with State Administration of Industry and Commerce (SAIC) Vice Minister Li Dongsheng and Guangdong Vice Governor Song, and in San Francisco with Guangdong Governor Huang; in 2006 with State Intellectual Property Office Commissioner Tian Lipu, Vice Minister Ma Xiuhong of MOCOM, National IP Strategy Office Deputy Commissioner Zhang Qin, and other ministries on IPR;
- (2) Engaging local and provincial Chinese leaders on best practices, judicial and administrative training or related educational programs;
- (3) Benchmarking progress with AmCham-China and with provincial authorities in Guangdong province;

- (4) Promoting public awareness in China by implementing a media strategy for re-branding IPR as not a “victimless crime.”

To achieve these goals, the U.S. Chamber is working closely with U.S. and Chinese governments, our corporate members, and counterpart associations, including with the AmCham network in China.

As I noted earlier, the root of China’s IP problem resides in the provinces. It is, therefore, absolutely critical that we cultivate the support of the provincial/local officials, as well as local industry, if IP enforcement is to be addressed in a truly meaningful way.

At the end of June, I will travel to China for our second installment of provincial IP enforcement seminars in Guangdong and Jiangsu—two IP theft hot spots. Together with U.S. government and corporate representatives, we will exchange enforcement best practices and illustrate to provincial and local officials the steps they can take to solve their persistent IP enforcement problems.

Our programs this year will also allow us to gauge progress on some of the indicators we discussed with provincial and local authorities last July. We are exploring the possibility of developing a benchmarking initiative with the Guangdong Provincial government to improve transparency, demonstrate progress, and highlight enforcement bottlenecks in the province. The Chamber looks forward to expanding our provincial efforts to Fujian and Zhejiang provinces—two additional “hot spots”—in the fall of this year.

Separately, the U.S. Chamber is working with AmCham China to benchmark China’s problems and progress administrative and criminal enforcement. Our initiative with AmCham aims to measure the effectiveness of enforcement over time by administrative authorities, including administrative fines, confiscations of production equipment, export enforcement, and the success of the government in transferring cases from administrative enforcers to the police for criminal prosecution. And with respect to criminal enforcement, we are also tracking the number of judicial prosecutions, convictions, and jail sentences for IP crimes on a periodic basis.

U.S. Chamber –U.S. Government Collaboration

The U.S. Chamber supports the Administration’s ongoing efforts to address and improve the inadequacy of China’s IP protection and enforcement regime. In particular, we appreciated the Administration’s increased focus in its 2006 Special 301 Report on assessing enforcement progress—or the absence thereof—in China’s provinces.

We also see as essential the Administration’s efforts to foster increased transparency in the way China gathers and presents its IPR enforcement data to the world. In this regard, the U.S. Chamber viewed USTR’s October 2005 formal request that China transparently document its actions under Article 63.3 of the TRIPS Agreement to enforce IPR as a constructive action.

Only through increased transparency will the Chinese authorities be able to document that the IPR climate is improving, and specifically, that regulatory reforms and enforcement efforts are creating a climate of deterrence. We look forward to receiving conclusive data from the Chinese government that confirms a more substantial increase in proactive government investigations

into cases, and substantial increases in case transfers, prosecutions, convictions, and incarcerations of counterfeiters and copyright pirates. U.S. government efforts to address inadequate transparency, the absence of criminal deterrence, and other regulatory and enforcement shortcomings in China's IP regime through the JCCT, other bilateral forums, and multilateral policy mechanisms are complimentary to ongoing private sector work. The U.S. Chamber strongly supports our government's efforts in this regard.

Looking Ahead

In short, we are seeking continued and more rapid progress from China in seven key areas. We hope that China in the near-term will use recent and encouraging advances in the areas of IP process, regulation, and awareness to:

- (a) Demonstrate a significant increase in the number of criminal IPR investigations, prosecutions, convictions and deterrent sentencing;
- (b) Implement administrative IPR enforcement actions that are deterrent;
- (c) Demonstrate specific steps to combat copyright and trade infringing activities, including internet piracy;
- (d) Make public available case rulings and IPR-related statistical data;
- (e) Demonstrate steps Chinese customs authorities are undertaking that are leading to significant declines of exports of infringing products;
- (f) Ensure that China removes administrative and other market access impediments that support illegal infringing activities and prevent the sales of legitimate foreign products; and
- (g) Resolve high profile cases involving infringements of foreign IP owners thus establishing the primacy of the rule of law.

If China were to take such actions, tangible results could be achieved.

In our view, the burden of ensuring a reduction in China's piracy and counterfeiting levels in 2006 will ultimately hinge on the political will of local Chinese authorities as much as the national government. Police investigations into new cases need to be proactive and adequately resourced in order to send a proper message to criminal networks that are increasingly behind the problem.

Full protection under PRC law and enforcement of IPR in China as set forth in China's TRIPS obligations are critical to the interests of foreign and PRC companies in China, as well as to China's public health and safety, the integrity and attractiveness of China's investment regime, and its broader economic development goals. We hope that the PRC government will accelerate IP enforcement in 2006 by further enhancing national leadership and dedicating additional capital and resources. Only through aggressive measures will China's IPR protection and enforcement regime be effective and respected.

China's accession to the WTO afforded it an opportunity to sell increasing quantities of products where it has a comparative advantage to the United States. But by tolerating massive counterfeiting and piracy, China is denying U.S. companies the chance to do the same in China. Moreover, by tolerating the export of such counterfeits, China strips our companies of the opportunity to use their comparative advantage—and thus WTO benefits—in third countries as well.

Ultimately, it is essential that China purchase the foreign IP-based products it is illegally using. That would translate into billions of dollars of sales and exports by U.S. and other foreign companies and more accurately reflect the balance of trade between the U.S. and China.