

**Statement of Senator Orrin G. Hatch  
to the  
United States-China Economic Security Review Commission  
Regarding  
China's Enforcement of Intellectual Property Rights and Counterfeit Goods  
June 8, 2006**

Thank you Chairman Wortzel and Member of the Commission for your kind invitation to speak here today.

I believe the Commission's mandate of reviewing the national security implications of the trade and economic ties between the United States and the People's Republic of China is a vital one and the research that the Commission publishes has been an invaluable resource to Congress as we debate these timely issues.

However, any discussion of our nation's economic relationship with China must be viewed in the context of our overall trade situation.

In 2005, the United States' trade deficit widened to a record \$726 billion, increasing to 5.8 percent of the Gross Domestic Product from 5.3 percent in 2004, and 4.5 percent in 2003.

Many economists now describe the trade deficit as unsustainable. For example, C. Fred Bergsten, Director of the Institute for International Economics, has pointed out "the United States must now attract almost \$7 billion of capital from the rest of the world every day to finance our current account deficit and our own foreign investment outflows."

One of the greatest components of our deficit is the trade imbalance with China. Last year, it totaled \$201.6 billion, an increase of 24.5 percent from the previous year.

As Chairman of the Subcommittee on Intellectual Property, what alarms me most is that this is far from being a case where American industries are being beaten on a level playing field. In fact, the theft of Intellectual Property in China is rampant.

It is astounding to learn that, according to industry group estimates, the United States lost \$2.3 billion in 2005 due to copyright infringement. They also report that nine out of 10 optical discs and 17 out every 20 sound records sold in China today have been pirated.

The Congressional Research Service estimates "counterfeits constitute between 15 to 20 percent of all products made in China and this sum amounts to eight percent of China's gross domestic product".

These pirated goods are not only depriving American producers of profits in the Chinese market. China, as Russia, continues to export pirated products to other nations, further increasing America's trade imbalance. Many of the countries where pirated goods are sold enjoy large trade surpluses over the United States, thereby further hurting our economic position.

All of this in an industry where the United States enjoys a decisive advantage over foreign competitors.

It should also not be forgotten that we will rely, in substantial part, upon intellectual property industries, which exported over \$90 billion in goods last year, to close our trade deficit.

This has all taken place despite China's repeated commitments to the United States to reduce significantly piracy rates in China. These promises occurred first during negotiations on Chinese Accession to the World Trade Organization, then in April of 2004, and most recently during the April meeting of the U.S. China Joint Commission on Commerce and Trade or JCCT.

Despite a nation-wide anti-piracy "campaign", industry groups state that little improvement has occurred. These industry groups also point out that similar campaigns have been launched in the past with inadequate results.

Yet, there are tools at hand which China could use. For example, the Chinese government could rigorously enforce their copyright infringement laws under Article 217 and 218 of their Criminal Law. Under these statutes an individual can be incarcerated for up to three years for copyright infringement. However, under current practices individuals are rarely criminally prosecuted and the occasional seizure is seen as the cost of doing business.

China's Criminal Law is still not in compliance with the TRIPS agreement. Moreover, its statutes are insufficient. For example, according to the Recording Industry of America, questions have been raised about what exactly constitutes a crime due to ambiguities in Chinese law as to what constitutes legal harm. Ambiguities such as these make criminal prosecution exceptionally difficult.

The Administration is heeding this call. For example, on February 14, 2006, the Office of the United States Trade Representative issued a report describing the results of its "top-to-bottom" examination of U.S. trade policy toward China and outlined steps that would be taken to ensure China's compliance with its trade commitments. These provisions include the creation of a China Enforcement Task Force at USTR, to be headed by a Chief Counsel for China Trade Enforcement.

However, many of us in the Senate do not believe that this initiative goes far enough. Accordingly, I joined Senator Baucus in sponsoring the Trade Competitiveness Act of 2006. This legislation will create a Chief Enforcement Officer at USTR to investigate and prosecute all trade enforcement cases.

Many in the Senate also look forward to positive developments arising from the recent JCCT. As the Commission knows, the Chinese Government made a number of commitments during this meeting which occurred shortly before President Hu's visit. This included intensifying China's efforts to ensure that their public markets are free of infringing goods. The Chinese also announced that legal action has been taken against 14 factories producing illegal optical disks.

I hope that these commitments are met. Unfortunately, I am skeptical. Remember the JCCT would not have had to devote much of its time to Intellectual Property issues, if the Chinese Government had merely lived up to its obligations after its WTO accession and its other assurances.

I am also pleased that the legal action is being brought against 14 factories that are producing pirated goods. Yet, I wonder how fast other Chinese factories that produce pirated goods will increase their production to meet the difference?

In addition to the economic harms caused by China's failure to meet its international obligations, there appear to be significant safety issues with some of the counterfeit goods being exported by Chinese entities. There is an enormous body of anecdotal evidence indicating that many counterfeit goods – principally medical and electronic goods – pose serious health and safety risks to individuals in our country.

There is evidence that Chinese counterfeiters are exporting everything from counterfeit pharmaceuticals, to batteries, to automobile parts, to low-cost electronic devices.

There have been numerous reports, for example, of deficient automobile brake pads, exploding batteries, and fake – and often ineffective – prescription drugs. These counterfeits pose obvious – and frequently very serious – public health and safety risks to the American people.

Our nation has been slow in bringing claims to the World Trade Organization against China's lack of IP protection. However, the Administration has initiated a special process under WTO rules to obtain detailed information on China's intellectual property rights enforcement efforts. Late last year, China responded by challenging the legal basis for such a request. U.S. officials have stated that failure by China to provide the requested information could lead the United States bringing a trade dispute resolution case against China in the WTO.

Yet, these should only be seen as preliminary steps. We must keep going and we must be aggressive.

In sum, our national security and the future economic health of our nation are being jeopardized by a large trade deficit, a deficit that is increasing in large part due to imports from China. Yet in those industries that rely on intellectual property, where we have a market-based advantage, our products are being pirated.

This cannot stand.

We cannot stop until the Chinese completely cease the piracy of IP products.

Therefore, Mr. Chairman I look forward, as I have in years past, to reading the Commission's report and recommendations that will assist us in rectifying the trade imbalance with China.

Again, thank you for your kind invitation and I apologize that I will not be able to remain for questions due to a heavy schedule.