



Intellectual Property:

Making It Personal

By Thomas A. Schatz
and Deborah S. Collier

Citizens Against Government Waste

Citizens Against Government Waste (CAGW) is a private, nonprofit, nonpartisan organization dedicated to educating the American public about waste, mismanagement, and inefficiency in the federal government.

CAGW was founded in 1984 by J. Peter Grace and nationally-syndicated columnist Jack Anderson to build public support for implementation of the Grace Commission recommendations and other waste-cutting proposals. Since its inception, CAGW has been at the forefront of the fight for efficiency, economy, and accountability in government.

CAGW has more than one million members and supporters nationwide. Since 1986, CAGW and its members have helped save taxpayers more than \$1.3 trillion. CAGW publishes special reports, its official newspaper *Government WasteWatch*, and the monthly newsletter *WasteWatcher* to scrutinize government waste and educate citizens on what they can do to stop it. CAGW's publications and experts are featured regularly in television, radio, print, and Internet media.

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Thomas A. Schatz, President
Deborah Collier, Director of Technology and Telecommunications Policy

Citizens Against Government Waste
1301 Pennsylvania Avenue, NW, Suite 1075
Washington, DC 20004
(202) 467-5300
www.cagw.org

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Introduction

Most Americans do not think much about how property rights affect them in their daily lives. If they consider the subject at all, they are likely to be more aware of the monetary value of private property than intellectual property (IP). People will protect their valuables at home and work by locking their doors and installing security systems, and they usually have a good idea of how much their business, home, car, and investments are worth.

But few people realize that nearly every product they use is the result of someone's idea, or IP; nor are they likely to know the value of IP to the economy. And it is even more unlikely that they understand the impact of IP theft on either the creative process or the tens of millions of ordinary Americans who participate in that process.

A Brief History of Intellectual Property Protection

During medieval times guilds, associations, or artisans were granted authority by the government to control the regulation and conduct of various industries.¹ In England, personal property and IP were traditionally viewed as distinct subjects with different origins. Personal or tangible property was viewed as “a creature of common law,” whereas copyrights and other IP were considered “largely a creature of statute.”²

The 1623 Statute of Monopolies provided for the exclusive control over an invention for a period of 14 years to the “true and first inventor.”³ The Statute of Anne in 1710 granted an initial 14-year protection period with a possible 14-year renewal for protection of IP rights.⁴

In the United States, following the Revolutionary War every state had its own patent law, and every state except Delaware had its own copyright law.⁵ The protection and promotion of IP was so important to the Founding Fathers that they included it in the General Welfare Clause, Article 1, Section 8 of the U.S. Constitution:

To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.⁶

Unlike IP, personal property is protected under the Fourth and Fifth Amendments, not in the Constitution itself. During the First Congress, H.R. 43, the Copyright Act of 1790, was enacted and signed into law on May 31, 1790 by President George Washington. As one of the first laws enacted by Congress, the legislation provided copyright protection for books, maps, and charts and established both the U.S. Copyright Office and the U.S. Patent and Trademark Office (PTO). These agencies were tasked with cataloguing, analyzing, and protecting IP rights.

Musical compositions were not mentioned in the text of the act and would not be expressly covered by copyright until the Copyright Act of 1831. However, they were routinely registered under the 1790 Act and categorized as “books.”⁷

Unlike the PTO, there is no “Office of Personal Property” or a “Department of Personal Property.” In fact, Article 5 states that private property can be taken for public use with just compensation. Although the government can exercise eminent domain over private property under such circumstances, it has no similar right to take away IP.

The legal protection of IP has enormous value. It turns intangible assets into exclusive property that can be traded in the marketplace. A March 2012 report by the U.S. Department of Commerce Economics and Statistics Administration and the PTO found that direct employment

in the most IP-intensive industries in the U.S. accounted for 27.1 million jobs in 2010, and indirect activities associated with those industries provided an additional 12.9 million jobs for a total of 40 million jobs, or 27.7 percent of all jobs in the economy.⁸

In a comparative study on the value of IP, economists Kevin A. Hassett and Robert J. Shapiro estimated that “innovation in its various forms accounts for 30-40 percent of the gains in growth and productivity by the American economy during the 20th century.”⁹ The study further found that the value of IP in the U.S. was between \$5 trillion and \$5.5 trillion in 2005.¹⁰ By comparison, in 2010 that value had increased to between \$8.1 trillion and \$9.2 trillion, or the equivalent of 55–62.5 percent of U.S. GDP.¹¹

In 2010, the value of IP comprised approximately 80 percent of a company’s total assets based on the Standard & Poor’s 500 Index.¹² This compares to the 1975 value of intangible assets comprising only 17 percent as IP, with the remaining 83 percent found in physical and financial assets.¹³

Internationally, some governments have been developing policies that threaten IP. The creative process will suffer as a result of such policies, because individuals and companies will not be willing to spend as much time or money on new IP if they believe the fruits of their labor will be taken away without sufficient – or any – compensation.

In a 2007 CAGW report entitled “Property Rights in the 21st Century: Don’t Steal This Paper or My Ideas,” one of this report’s co-authors examined four “myths and reality” surrounding the definition and use of IP. These premises hold true today.

Four Intellectual Property Myths

1. Myth: The price of information and ideas should be zero because products should be priced at marginal cost.

Reality: Economists reject marginal cost pricing because such policies destroy investment.

2. Myth: Intellectual property rights result in information and ideas being “locked down” by their owners.

Reality: The creators of art, books, movies, and inventions want their creations to reach as many people as possible, so long as they are compensated.

3. Myth: Intellectual property rights are monopolies that give their owners too much economic power.

Reality: Patents or copyrights support competition by encouraging inventors and creators to enter new markets; IP gives its owners no more economic power than any other asset.

4. Myth: Intellectual property rights benefit big firms at the expense of “the little guy.”

Reality: Patents are often the best protection that a small inventor has against large firms; copyright benefits creative ventures of many sizes, from solo musicians to big studios.

Strong protection of IP provides real benefits. Consider the following American inventions and whether they would have come about in a climate of weak IP protection:

- The telegraph in 1835¹⁴
- The phonograph in 1877¹⁵
- The light bulb in 1880¹⁶
- Air conditioning in 1902¹⁷
- The television in 1927¹⁸
- The point contact transistor in 1947-1948¹⁹
- Marshmallow Peeps in 1952²⁰
- Magnetic tape cartridges in 1964²¹
- The cell phone in 1973²²
- The microprocessor in 1973²³

The value of these and future inventions relies on strong IP protection. This report will review copyright, trademark, and patent issues, as well as ongoing threats to IP protections from piracy, counterfeiting, and illegal sharing online.

Many individuals who buy a fake Gucci bag on the corner or illegally download a TV show, movie, or music, share the view of Hana Beshera, one of the founders of NinjaVideo, who served 16 months in prison for violating copyright laws. Even after she got out of jail, Beshera still believed that “the movie business is so large that skimming a little off the top doesn’t hurt anybody.”²⁴ IP theft is wrong at every level; its impact affects everyone associated with the creative process. Indeed, with more than 40 million Americans directly or indirectly working in an IP-related industry, one of the victims of IP theft might well be personally known to the perpetrator.

The importance of protecting IP rights cannot be overemphasized. The right to retain legal possession of, and benefit financially from, IP is constantly being threatened. The intent of this publication is to help educate the public about the value and importance of IP, the impact on individuals and the economy from the theft of IP, and how IP helps innovation flourish and economies around the world thrive.

Chapter 1 – The Changing Face of Piracy

“Pirate” conjures up swashbuckling raiders capturing merchant ships plying their trade on the open seas. These individuals were infamous: Barbarossa, Black Bart, Blackbeard, Captain Kidd, and of course, the Dread Pirate Roberts.

Their victims were not as well-known and often elicited little sympathy, particularly if they were considered to be wealthy or otherwise elite.

Today’s pirates operate in the hidden sea of the Internet behind seemingly innocuous websites and hack into computer systems to capture trade secrets in order to produce counterfeit goods or make available stolen copyrighted material. They are mostly anonymous: unknown individuals, organized criminals, and terrorists. On the other hand, some are well-known: China, India, Russia, and Kim Dotcom.

Their victims are not so faceless. They are the creators, designers and innovators of products and services used by billions of people every day. They are the local furniture maker and wedding dress designer; they are also Ethan Allen and Vera Wang. They are the songwriter trying to share new music and the budding moviemaker with an HD video camera; they are also Bob Dylan and Disney.

With everyone now being only a mouse click away from the global marketplace, the Internet has opened up the world to economic opportunity. But the information superhighway is also wide open to criminals, who can now steal virtually what they used to have to take physically. And most of what they want is IP. Essentially, everything that can be touched, smelled, listened to, watched, worn or used can be copied or pirated from the original creator, illustrator, artist and manufacturer.

In order to help reduce such theft, governments around the world need to do everything possible to protect IP. The status of such efforts by the United States’ trading partners has been included in the U.S. Trade Representative’s (USTR) “Special 301 Report” since 1989.²⁵

The 2014 report listed 10 countries on the USTR’s Priority Watch List: Algeria, Argentina, Chile, China, India, Indonesia, Pakistan, Russia, Thailand, and Venezuela. Another 27 trading partners are on the USTR’s Watch List.²⁶

The report highlighted positive steps in IP protection in countries such as Italy, Korea, and the Philippines. These countries were removed from the watch list as a result of their efforts to combat copyright piracy, increase enforcement activities, provide more patent transparency, and adopt international treaties designed to protect the rights of authors, performers, and producers of IP.

Korea’s progress toward protecting IP is notable, since it appeared on the USTR’s first watch list in 1989. According to the 2014 report, Korea is now one of the top patent filers internationally, with state-of-the-art standards for IP rights protection and enforcement.²⁷ Unfortunately, far too many countries have failed to make such progress in protecting IP.

According to the World Intellectual Property Organization’s 2013 IP indicators report, there were more than one million patents granted in 2012 and an estimated 8.66 million patents in force worldwide.²⁸ However, protecting patents, copyrights and trademarks from IP theft remains a problem.

Every time something is designed, created, manufactured and sold in the United States and globally, it has an intrinsic IP value. When that item has a patent, trademark or copyright and is copied or remanufactured without the permission of the inventor, creator, or artist, it is stolen. While most people don’t think about the illegal knockoffs they buy online or on the street corner as stolen goods, these items are not innocuous.

The broad impact of IP theft was described by U.S. Immigration and Customs Enforcement (ICE) Assistant Secretary John Morton, who said it “robs people of their innovation, jobs and tax revenue that funds vital government services, ... IP theft is a crime organized criminals engage in, turning their profits toward other criminal activities, and IP theft creates safety risks for everyone due to the proliferation of substandard goods, including counterfeit pharmaceuticals, aircraft parts or daily consumables like toothpaste.”²⁹

On the other side of this equation, the production and use of IP creates millions of jobs and provides incentives for the development of new technology. According to the Global Intellectual Property Center (GIPC), in 2012 IP was responsible for more than 55 million jobs across the country, including California (7.3 million jobs), Texas (4.6 million jobs), Illinois (2.8 million jobs), New York (2.7 million jobs), Ohio (2.6 million jobs), Pennsylvania (2.5 million jobs), and Florida (2 million jobs).³⁰

On January 29, 2014, GIPC released its second annual IP index, rating IP protection around the world.³¹ GIPC ranked the countries through a point system based on six categories: patents (7 points), copyrights (6 points), trademarks (5 points), trade secrets and market access (2 points), enforcement (6 points), and, membership and ratification of international treaties (4 points).³²

The United States topped the list of countries with the most protection for IP with a score of 28.52 out of 30, closely followed by Great Britain, France, and Singapore. Argentina, Indonesia, Nigeria, Thailand, and Vietnam all had poor GIPC scores; Argentina, Indonesia and Thailand also appear on the USTR’s Priority Watch List, and Vietnam appears on the USTR’s Watch List. Bottoming out on the list for the second year in a row was India, with a ranking of 6.95 out of 30.

It is little wonder that India again had the worst score. On December 29, 2013, *The New York Times* reported on the ongoing struggle that drug manufacturers have protecting their patents in India,³³ which is one of the world’s leading producers of generic pharmaceuticals. Maintaining that patented drugs are too expensive for people in developing countries,³⁴ India has ruled invalid patents protecting exclusive sales of Novartis’ Gleevec, Pfizer’s Sutent and Roche’s Tarceva. The Indian government agreed that Bayer’s Nexavar patent was valid, but overrode the patent anyway because a generic drug company promised to lower the price of the treatment.

A May 30, 2014 briefing on Capitol Hill, hosted by the Information Technology Innovation Foundation (ITIF) and GIPC, highlighted the issues and challenges that India faces in moving forward on IP protection following the installation of Narendra Modi as the country’s new Prime Minister on May 26, 2014. GIPC Executive Vice President Mark Elliot stated that India’s low rankings on protecting copyrights, patents, IP, trade secrets and market access, trademarks and following international treaties contributed to its low score on the GIPC’s International IP Index. Representative Ami Bera (D-Calif.) suggested that companies would like to invest in India, but need to have knowledge of and predictability in how India engages in the protection of IP.

An April 2014 ITIF report criticized India’s use of “innovation mercantilist measures,” which force companies to abide by rules that offer public procurement of information and communication technology products, compulsory licensing of foreign bio-pharmaceutical IP, and restrictions on market access and direct foreign investments in e-commerce, retail and financial services.³⁵ The report recommended changes to India’s IP laws that could help India achieve improved economic stability and growth.³⁶

Given India’s track record, the path to improved protection of IP rights will not be smooth or easy. Moving forward, the U.S. government should continue to engage with all of its trading partners, including India, to ensure that IP is respected and protected.

IP theft affects many other industries in addition to pharmaceuticals. An August 2007 Institute for Policy Innovation report estimated that millions of illegally downloaded songs have cost the U.S. economy \$12.5 billion, 70,000 lost jobs and \$2 billion in lost wages, as well as \$422 million in tax revenue (\$291 million in personal income tax, and \$131 million in lost corporate income and production taxes).³⁷ In a 2012 report on the impact of Internet piracy on sales and revenues of copyright owners, Dr. Stan J. Liebowitz, Ashbel Smith Professor of Economics at the University of Texas at Dallas stated, “On average, the findings for music are that the entire decline in sales since 1999 is due to piracy, and these values tend to be in the vicinity of 50%-70% when dollars are measured in inflation adjusted units.”³⁸

In addition to the adverse financial consequences caused by counterfeit goods, they can also cause physical harm. On May 13, 2013, an ABC News story about a raid on a Los Angeles store selling counterfeit goods included an interview with Underwriters Laboratories, Inc. (UL) in Northbrook, Illinois. UL experts demonstrated the hazards of counterfeit extension cords that caught fire when in use, and suggested that counterfeit products that are used in everything from toasters to the wall outlets in homes have the potential to also cause damage or injury.

On June 13, 2014, ABC’s “20/20” had a segment on counterfeit goods such as name brand shampoos, soaps, and cosmetics sold at a steep discount, which have little similarity to the original product other than packaging.³⁹ Many of these counterfeits contain carcinogens, heavy metals and other chemicals known to be harmful to humans. The products are sold at various retail establishments nationwide as well as online, and are now in millions of homes across the country.⁴⁰

The U.S. Immigration and Customs Enforcement Homeland Security Investigations (HSI) directorate operates the National Intellectual Property Rights Coordination Center (IPR Center), which includes 17 key federal agencies, Interpol, Europol and the governments of Canada and Mexico. The IPR Center’s mission is to “ensure national security by protecting the public’s health and safety, the U.S. economy, and its war fighters, and to stop predatory and unfair trade practices that threaten the global economy.”⁴¹

IPR Center case studies included Operation Safe Summer, which discovered the importation of counterfeit and faulty airbags; Project Copy Cat, which seized 70 domain names of websites that mimicked real store websites to mislead consumers into purchasing counterfeit goods; Cyber Monday 3, which targeted websites selling counterfeit products during the holiday season; and Project TransAtlantic, a joint effort with Europol that led to the seizure of 182 domain names of websites selling and distributing counterfeit goods.

Counterfeit sports apparel and souvenirs have also been the target of IPR Center activities. Operation Red Zone led to the seizure of 196,333 sports-related items with a retail value of more than \$17.3 million, and Operation Team Player has resulted in the seizure of more than \$37 million in fake sports merchandise as well as 163 websites, along with the arrest of 70 individuals involved in these schemes.⁴²

The IPR Center’s ongoing operations target websites that distribute counterfeit products, pirated movies and television content; both websites and smugglers who sell fake and adulterated drugs; and the importation of counterfeit goods into the Department of Defense (DOD) and federal government supply chain.

The Internet has widely changed the way consumers purchase goods and services, but this process has also opened the door to increased fraud, counterfeiting and theft. Criminals have used the Internet to sell counterfeit drugs, bootlegged videos and songs, counterfeit apparel, and fake trademarked items.

One might wonder where the money from all of these stolen goods is going. More often than not, it is being used to fund even more nefarious activities, including the illegal drug trade, slave trade, child labor, organized crime and terrorism.⁴³ In addition, covert activity to steal trade secrets is being supported by nation-states in order to allow their domestic companies to develop their own version of these products to sell at a cheaper price.

For example, on May 19, 2014, the Federal Bureau of Investigation (FBI) placed five Chinese military officers on its most wanted list for cyber-espionage. Included in the charges are “conspiring to commit computer fraud; accessing a computer without authorization for the purpose of commercial advantage and private financial gain; damaging computers through the transmission of code and commands; aggravated identity theft; economic espionage; and theft of trade secrets.”⁴⁴

In making the announcement, U.S. Attorney General Eric Holder stated that “the range of trade secrets and other sensitive business information stolen in this case is significant and demands an aggressive response.”⁴⁵

During a trip in April 2014, to Los Angeles, California, one of this publication’s authors noted that the streets of the garment district were lined with storefronts offering steep discounts on designer clothing and handbags, and other shops offering low prices on various electronic goods. Many of these prices just seemed too good to be true.

This experience called to mind an October 22, 2013 report on ABC’s “Nightline,” which discussed seizures by the FBI and the Los Angeles Police Department of goods brought into the U.S.⁴⁶ Among the highlights of the story was the seizure of 16,000 fake Hermes handbags that had a street value of \$300,000. If these handbags had been genuine, they would have been worth more than \$210 million.

While U.S. government agencies, private-sector companies, trade associations, and nonprofit organizations are engaged in the battle to protect IP, consumer awareness is also a key component of these efforts.⁴⁷ By paying attention to details, consumers can avoid purchasing items that may be counterfeit or fake. If the price appears too good to be true, it probably is. If the product is found in a location where one would not expect to find it, such as a Prada handbag sold at a gas station, the authenticity should be in question. If the seller is not authorized to sell the item, it is probably counterfeit. If the packaging is of poor quality or torn, or contains misspelled words or other printing errors, the product is probably stolen.

Consumers shopping online should make certain that websites are authentic by checking the fine print on product descriptions, reading the FAQ section, and reviewing the “Contact Us” page. If typographical, grammatical or spelling errors appear, or incomplete information is presented, chances are the website is a fake; they are not selling the real deal and are instead luring consumers in to steal their credit card numbers and other information for more nefarious purposes.

Changes in technology have brought about new methods for pirates to steal from others. Gone are the days of the swashbuckler, replaced by nebulous criminals who use subterfuge to mislead and redirect consumers into purchasing stolen, fake or counterfeit goods. Domestic and international law enforcement agencies are taking steps to stop these thieves, but consumers must also be made aware of the threats posed to the economy and their personal safety when they purchase these products, as well as how that money is being further misused.

Conclusion

IP rights have been paramount since the Republic was established. As James Madison noted in “Federalist Paper 43,” referring to the authority to promote science and the arts by providing exclusive rights to authors’ and inventors’ writings and discoveries (which became Article I, Section 8 of the Constitution):

The utility of this power will scarcely be questioned. The copyright of authors has been solemnly adjudged in Great Britain to be a right of common law. The right to useful inventions seems with equal reason to belong to inventors. The public good fully coincides in both cases with the claims of individuals. The States cannot separately make effectual provision for either of the cases, and most of them have anticipated the decision of this point by laws passed at the instance of Congress.³¹⁶

The Founding Fathers understood that by protecting the individual rights of artists, authors, entrepreneurs, innovators, and inventors, they were promoting the greater public welfare. These fundamental privileges remain essential to ensure that IP will continue to have a substantial, positive impact on everyone’s life.

Patent holders need strong enforcement of IP laws in the U.S. and by its trading partners. New initiatives to license underutilized patents will increase the availability of hundreds of inventions while reducing the amount of patent litigation. Consumers must have assurances that they are buying safe and effective products that will not cause them harm, and taxpayers need to know that the government is not using fake parts in its weapons systems.

However, there are headwinds to the protection of IP rights. The Internet has spawned a new wave of IP piracy that includes counterfeit drugs being sold on fake pharmaceutical websites and music and videos being illegally downloaded from file sharing or torrent sites. Stealing IP and distributing it without just compensation to its creator has a far-reaching negative impact on the next independent filmmaker, struggling garage band, or young author.

The theft of trademarks creates confusion for consumers who believe they are purchasing specific brand name goods, only to find that the items are mislabeled, counterfeit, or even deadly. Some governments have passed laws that essentially strip trademarks from certain goods, in order to support social goals or policies. Other governments enforce antitrust laws or weaken IP laws to allow their domestic businesses to make a profit from the ideas and sweat of others. If more countries develop policies that threaten IP, there will be less incentive to invest in technology, research, and development, and the global economy will suffer.

Despite these barriers to IP rights, there are many countries that understand and promote the importance of IP for economic growth. As Great Britain’s ITV Director of Policy and Regulatory Affairs Magnus Brooke said, “A strong IP regime is an engine of growth, NOT a barrier.”³¹⁷

Keeping this engine running smoothly, using the recommendations and concepts contained in this report and similar sources, will help the global economy continue to grow. In the U.S. alone, IP-related industries provide more than 40 million jobs³¹⁸ and account for between 55 and 62.6 percent of GDP.³¹⁹ Without the innovation propelled by IP, the global economy would be on a slow (or slower, in current circumstances) train going nowhere.

Everyone benefits from IP. If the Founding Fathers had not recognized its importance, the light bulb, the telephone, the cell phone, and the microchip might never have been invented. Strong IP protection is fundamental to keeping the engine of ingenuity on track for generations to come.



Thomas A. Schatz is president of Citizens Against Government Waste (CAGW).

Mr. Schatz is a nationally-recognized spokesperson on government waste and has been interviewed on hundreds of radio talk shows from coast to coast. He is a regularly featured guest on national television news programs and local news broadcasts. Mr. Schatz has testified numerous times on government waste issues before committees of the U.S. Senate and House of Representatives, as well as before state and local legislative and regulatory bodies.

During his 28 years with CAGW, Mr. Schatz has helped make CAGW a “leading government watchdog on fiscally conservative issues, like taxes and earmarks,” according to *National Journal*. CAGW was cited by *The Hill* for its leading role in successfully pushing for the congressional earmark moratorium, which was identified as one of the “top 10 lobbying victories in 2010.” *The Hill* has

named Mr. Schatz as a “top lobbyist” for five consecutive years, from 2010-2014.

His previous books include “End the Income Tax,” co-authored with Jack Anderson in 1997; and “Telecom Unplugged: Ushering in a New Digital Era,” co-authored with Deborah Collier in 2014.

Prior to joining CAGW in 1986, Mr. Schatz spent six years as legislative director for Congressman Hamilton Fish, Jr. and two years practicing law and lobbying.

Mr. Schatz holds a law degree from George Washington University and graduated With Honors from the State University of New York at Binghamton with a bachelor’s degree in political science. He is married to Leslee Behar and has two daughters, Samantha and Alexandra.



Deborah S. Collier is the technology and telecommunications policy director for Citizens Against Government Waste (CAGW). She specializes in information technology (IT) and telecommunications policy, including cloud computing, IT procurement, information security, data privacy, broadband spectrum allocations, network neutrality, cable industry issues, e-commerce, and emerging technologies.

Since joining CAGW in July 2011, Ms. Collier has authored numerous of educational issue briefs; articles and blogs on technology and telecommunications policy, including three reports relating to cloud computing; and a report on the development of government mobile apps. In 2014, Ms. Collier joined with CAGW President Tom Schatz in co-authoring “Telecom Unplugged: Ushering in a New Digital Era.” She

has been a guest on radio and television news programs to discuss Internet taxation and other technology related issues.

Prior to her work at CAGW, Ms. Collier spent 24 years on Capitol Hill working in IT and legislative arenas. She worked for Rep. Clarence Miller (R-Ohio) both as a caseworker and system administrator, and then joined the staff of Rep. Steve Buyer (R-Ind.) as the director of information technology. From 2005 to 2010, she served on the House Committee on Veterans’ Affairs as the Republican Legislative Director. Ms. Collier was a member of the House Systems Administrators Association from 1989 until 2005, and served as the organization’s president from 2002 to 2005.

Ms. Collier holds a Bachelor of Arts (AB) degree in History from Ohio University. She is married to Kimo Collier, and has a son, Christian.

Introduction

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