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Review

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Industry insight

Proactive enforcement through information sharing

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In recent years IP crime has reached record levels, prompting governments around the world to take a significantly more serious stand against it. The rise in IP crime and compliance with the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) has spurred many governments to update legislation criminalizing counterfeiting and piracy. Many jurisdictions have gone beyond the requirements set out in TRIPs and increased damages awards, improved procedures to speed up IP cases and strengthened criminal provisions (eg, through longer prison terms and monetary fines). In some jurisdictions, new and innovative approaches to IP enforcement, such as third-party claims and the application of proceeds of crime seizures on counterfeiters, have also been introduced.

Despite these generally positive changes, the global counterfeiting and piracy trade continues to present disappointing trends. According to a November 2009 Organization for Economic Cooperation and Development report, the global trade in counterfeit and pirated goods continues to rise, increasing from \$200 billion in 2005 to approximately \$250 billion in 2007. Of the 19 countries surveyed in 2008, 15 exhibited a clear increase in the volume of counterfeit goods. So while it is easy to applaud positive changes in IP legislation and enforcement, the figures suggest that current methodologies are still insufficient to deter IP infringers.

In the highly lucrative commercial counterfeiting and piracy trade, IP rights strategies must address the issue of

effective deterrence. For instance, a recent study compared the profitability of counterfeiting and piracy to that of the narcotics trade. It found that pirated DVDs are sold on the streets of major cities such as London, Paris and New York for about \$9, a mark-up of more than 1,000% – this is three times the mark-up on Iranian heroin or Colombian cocaine. However, counterfeiters in, for example, France can expect to pay only a fine of approximately \$200,000 and serve a two-year prison sentence, while those convicted of narcotics offences can expect to have at least eight more years tacked on to that jail term and pay about \$9 million more in fines. As long as punishments for IP crimes remain light compared to those involving narcotics, high profit margins for commercial counterfeiting will still glitter like gold on a fake Gucci handbag.

In China, one manufacturer estimates that the repeat offender rate is approximately 90%. This is hardly a shock, considering that the maximum penalty for counterfeiting and piracy in China is merely three years' imprisonment, under the Criminal Procedures Law. (Only in serious situations, such as counterfeit pharmaceuticals that could harm people, is the maximum raised to seven years.)

In India, Section 63 of the Criminal Law provides only for up to three years' imprisonment and fines of up to Rs200,000 for IP infringement cases.

China and India are not the only countries with such issues: blatant disregard for punishment is evident in many other countries and often counterfeiters simply factor in the cost of fines and jail sentences to their business. However, several measures being taken in certain jurisdictions are helping to take the shine off counterfeiting and piracy.

In the East African Community (which comprises Burundi, Kenya, Rwanda, Tanzania and Uganda), estimates put losses to rights holders from counterfeiting at half a billion dollars. The most dangerous aspects of counterfeiting are in the pharmaceutical and food industries, where the majority of goods on the market are counterfeit. However, lawmakers are looking at alternative third-party liability and hope to pass legislation similar to the Bawdy House Act by March of this year. This would call for landlords of commercial properties to be held accountable for how their property is used; lessors of commercial property where counterfeit goods were manufactured would be obliged to terminate the lease(s) of counterfeiters.

While statistics paint an optimistic picture of how various legislative changes are leading to increased numbers of convictions in IP cases, enforcement capabilities still lag behind, meaning that rulings are not always effectively enforced. Strengthening IP rights at the domestic level is one thing, but since many goods are not sold in the country where they are manufactured, enforcement becomes increasingly difficult.

This being the case, what recourse do rights holders have when their rights are infringed? Many are left with little option but to stick to the traditional methods of frequent raids to remove infringing products from the market and inflict as much financial damage on the infringer as possible. Bearing in mind that enforcement does not come cheap, this simply cannot be the primary long-term strategy for addressing the growing trade in counterfeit and pirated goods.

For example, to initiate action in China would cost on average \$2,000; the average cost of a raid and seizure action is \$5,000,

“ Information on infringers can be made effectively available to financial institutions. This brings the battle to the economic frontlines, where there is more fire power available to be used against commercial counterfeiting and piracy ”

while a basic IP litigation could mount to \$25,000. Taking into consideration the volume of infringements in proportion to the cost of legal action, many IP infringements are never addressed due to the expense of enforcement strategies required to bring such cases to fruition.

Innovative use of alternative legislation

For the time being, it is unlikely that rights holders can or will diverge from reactive IP protection strategies, such as raids and legal recourse. However, rights holders can begin to seek innovative and proactive solutions to complement their current strategy with the aim of eventually offsetting these costs. By introducing supplemental solutions to their current methods, rights holders can:

- subsidize or potentially fund enforcement efforts;
- impose effective deterrents or barriers to entry on recurring infringers; and
- address methods that weigh the cost-benefit model of counterfeiting and piracy.

The UK Trading Standards Office is a prime example of how innovative methods have been used to address IP crimes. By successfully implementing the Proceeds of Crime Incentivization Scheme, trading standards offices in England and Wales have utilized the Proceeds of Crime Act 2002 to impose financial pressures on commercial counterfeiters, channelling seized financial assets to offset enforcement costs. From 2007 to 2008 alone, £135.7 million was seized under the act. This approach not only addresses the cost-benefit model of counterfeiting and piracy by seizing illicit proceeds, but also serves as a motivation for law enforcement to target this criminal trade.

Anti-money laundering regulations

Another alternative method to address IP crimes is the use of anti-money laundering (AML) regulations. The global standard in AML regulations recommended by the Financial Action Taskforce (FATF) has (since 2001) included commercial counterfeiting and piracy among 36 predicate crimes. This means that commercial counterfeiting and piracy constitute a defined area of crime that financial institutions are required to identify proactively and guard against.

It remains relatively unknown outside AML circles that commercial counterfeiting and piracy are a major typology in AML regulations. Besides the obvious understanding that profits from commercial counterfeiting and piracy are considered to be criminal proceeds, the trade in counterfeit and pirated goods is also used to launder illicit finances. Trade-based money laundering remains one of the oldest and most popular methods of laundering illicit proceeds. Techniques include:

- over or under-invoicing for goods and services;
- multiple invoicing for goods and services;
- over and under-shipments for goods and services; and
- falsely describing goods and services.

A particularly worrying trend is the invoicing of counterfeit and pirated goods on par value as their genuine counterparts. In this typology, the invoice would be of a far greater value than the par value of the goods traded. This method is even more useful for laundering criminal proceeds for individuals involved in commercial counterfeiting on an international level. In a case study published by the FATF, criminal groups involved in commercial counterfeiting have been

known to adopt the trade-based money laundering method. Additionally, using this technique, these criminal groups have been able to establish a greater appearance of legitimacy, thus reducing the risk of detection. Considering the extremely large volume of international trade, and that only a minor fraction of shipments are ever inspected by customs officials, trade-based money laundering continues to be effective and popular.

Proactive enforcement

AML legislation is actually highly compatible with IP issues. Besides the fact that AML regulations are far better established over a much longer period of time, the AML model provides farther-reaching enforcement capabilities that target financial benefits, which is the root motivation for commercial counterfeiting and piracy.

A particular cornerstone of compliance in AML regulations are know-your-customer regimes. Essentially, these enable financial institutions actively to screen their client relationships against a database such as World-Check, identifying high-risk persons and entities associated with the 36 predicate crimes outlined by FATF recommendations and other closely related criminal activities. Financial institutions maintain perpetual cycles where account-opening clients and pre-existing clients are screened for associations with terrorism and crimes such as fraud, organized crime, narcotics trafficking, arms smuggling, war crimes, corruption and IP crimes.

Under AML regulations and practices, financial institutions will decline to establish relationships with an individual or entity that is identified as high risk. In situations where risk association is

Trade-based money laundering of counterfeit goods



identified with existing relations, financial institutions must file a suspicious activity report with the local financial regulator. In most countries, financial regulation falls within the jurisdiction of either the national law enforcement or judicial body. In the United Kingdom, for example, suspicious activity reports are filed and submitted to the Serious and Organized Crime Agency. In these cases the financial regulators will initiate an investigation. Today virtually every financial institution in the world has installed a know-your-customer regime within its internal compliance system.

If AML regulatory activities such as these are used against IP crimes, it could effectively deny IP infringers access to the global financial system, thus diminishing their capacity to conduct international trade. Further, without access to the global financial system, it will become extremely difficult for IP infringers to reap the financial benefits.

Information is the critical issue in this strategy; after all, financial institutions are not investigators. This means that financial institutions can act only on information made available to them. Most know-your-customer regimes depend on commercial database vendors to provide them with the information to help them know whom they are doing business with. To utilize AML regulations effectively on IP issues, rights holders must look beyond traditional partnerships and seek arrangements where information on infringers can be made effectively available to financial institutions. This brings the battle to the economic frontlines, where there is more fire power available to be used against commercial counterfeiting and piracy.

More strategies are being developed for rights holders to share intelligence with law

enforcement officials to facilitate raids and investigations. On a global level, INTERPOL launched the Database on International Intellectual Property Crime in 2008 precisely to facilitate this information sharing. In addition, programmes such as INTERPOL's OASIS programme provide training for certain regions in criminal intelligence analysis and combating specific areas, such as counterfeit pharmaceuticals. On an industry level, several trade and industry organizations have taken on the role of facilitating information sharing between rights holders.

As communication becomes easier and technology makes the world more accessible, rights holders have come to realize that information sharing with partners is critical in the fight against the global trade in counterfeiting and piracy. Most rights holders have a wealth of information obtained through years of investigation – sometimes this leads to raids and the seizure of goods, but in many cases information is under-utilized. To advantageously leverage this information, pieces of the puzzle must be assembled into highly structured datasets conveniently accessible to all stakeholders. While progress has been made in information sharing between rights holders, to date there is no globally established governmental policy for information sharing between rights holders and financial institutions. However, over 4,500 financial institutions, including 49 of the world's top 50 banks, already utilize a system established by World-Check that is also used by law enforcement agencies and customs authorities around the world. World-Check is in a unique position to bridge the gap between holders of information on IP crimes and financial institutions. Its well-established, close

relationship with the global financial and law enforcement communities will help it to make a powerful contribution to curbing counterfeiting across all markets and industries.

Key points for the future

Rights holders must continually petition governments to increase IP enforcement actions; this can be achieved only through political lobbying and effective addressing of resource limitations. They must also be prepared to look beyond reactive enforcement strategies and use supplemental deterrence strategies. While reactive enforcement strategies remain the most convincing options in terms of return on investment debates, with no effective deterrence or barriers to entry, such strategies are not a long-term solution.

Instead, enforcement strategies must target the economic motivations of IP infringement. The high profitability and low cost of counterfeiting and piracy are the fundamental drivers for this booming trade. Enforcement strategies simply cannot be effective if economic motivations are not addressed. [WTR](#)

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