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UNITED STATES SENTENCING COMMISSION

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My name is John Bliss and I am President of the International AntiCounterfeiting Coalition (IACC). The IACC is a non-profit trade association comprised of more than 170 members, representing corporations, business trade associations and professional firms whose livelihoods depend on the protection of intellectual property rights. Our members are drawn from a cross-section of U.S. industry including auto, apparel, luxury goods, pharmaceuticals, food, computer software, entertainment, and others. Consumers who use the products of our manufacturing members expect these products to be safe and to be of high quality. Unfortunately counterfeiters too often undermine the expectations of consumers by stealing the names and reputations of legitimate manufacturers to sell inferior products for quick profits.

On behalf of the IACC, let me express my gratitude for being afforded this opportunity to testify and offer comments on how Sec. 2B5.3 (Criminal Infringement of Copyright or Trademark) should be amended to best effectuate congressional directives set forth in P.L. 105-147, the No Electronic Theft Act (NET).

The IACC and its members maintain that the only way to effectively deter counterfeiting is to assure that counterfeiters receive jail time for their actions. Stringent criminal penalties are necessary because the nature of counterfeiting as an illicit underground operation does not lend itself to civil enforcement. As a cash business, damages are difficult to prove in counterfeiting cases, and counterfeiters treat monetary damage awards and fines as merely the cost-of-doing-business. The only real deterrent to counterfeiting is the imposition of criminal penalties that result in actual jail time served of one year or more.

Scope of Counterfeiting

In 1982, counterfeiting cost the U.S. an estimated \$5.5 billion. Today, the problem has become an epidemic, generating losses of over \$200 billion. This explosive growth has been accompanied by a migration in the availability of counterfeits from traditional locations like city streets, flea markets, swap meets, and sports stadiums to suburbs, strip-malls, and the shelves of legitimate retail stores.

Of particular concern to the IACC is the increasing availability of fakes that present health and safety risks. Three recent examples underscore this point.

(1) Procter & Gamble, maker of Head & Shoulders shampoo, was forced to take the extraordinary but appropriate step of placing half-page advertisements in at least 27 national newspapers informing the general public that counterfeit Head & Shoulders was available in retail stores. A chief concern of the manufacturer was the fact that the fakes may have contained bacteria, risking infection in users with weakened immune systems.

(2) Counterfeit-labeled infant formula recently found its way onto shelves in Safeway and Pak n' Save grocery stores in 16 states. According to

press reports, the fake baby formula caused rashes and seizures in many of the babies who were given it, prompting concerned parents to notify the legitimate manufacturer.

(3), Counterfeit-labeled confectionery food was seized during a raid in Boston. Illegally labeled as a product of Borden Eagle Brand, the so-called "Almond Bark" butterscotch candy had been stored in unsanitary conditions. Fortunately, while the counterfeit product was awaiting distribution, investigators located the fake food, and confiscated the product.

Another concern is organized crime's growing involvement in product counterfeiting. Attracted by the high profits and low risks generated by counterfeiting and piracy, these notorious organizations operate vast distribution networks to transport fake goods and support other criminal activity. For example, in three recent raids conducted in Los Angeles, law enforcement seized counterfeit Microsoft software and other material with a potential retail value in excess of \$10.5 million. Implicated in this activity were three Chinese organized crime groups known as triads. Los Angeles Sheriff's deputies seized counterfeit software, manuals and holograms and were surprised when they stumbled upon four pounds of plastic explosives, two pounds of TNT, shotguns, handguns, and silencers.

Organized crime has also used counterfeiting to further drug trafficking operations. In a recent New Jersey case, police seized \$400,000 worth of counterfeit handbags. During the raid, law enforcement officials used a trained police dog to discover that heroin had been stitched into the linings of the counterfeit designer bags. Contraband used to transport contraband.

Finally, the sale of counterfeit goods adversely impacts the economy. New York City alone loses over \$400 million a year in lost sales and excise taxes. The U.S. Customs Service estimates that hundreds of thousands of Americans lose their jobs every year due to counterfeiting, and the automobile industry says that they could hire 210,000 additional workers if auto parts counterfeiting could be eliminated. And small legitimate retailers and entrepreneurs suffer as they are forced to compete with companies and retailers selling illegal low-cost fakes.

As these examples demonstrate, counterfeiting is no longer small mom-and-pop operations sewing labels on T-shirts. Counterfeiters are sophisticated, organized crime groups that use counterfeiting to fund and support other criminal activities.

Congressional Intent

Faced with evidence regarding the extent of counterfeiting and its harms to society, Congress recently took several steps to increase the level of priority federal law enforcement attaches to intellectual property crimes. First, congress passed P.L. 104-153, the Anticounterfeiting Consumer Protection Act of 1996, (ACPA). The ACPA recognized that "[t]he counterfeiting of trademarked and copyrighted merchandise -- (1) has been connected with organized crime; (2) deprives legitimate trademark and

copyright owners of substantial revenues and consumer goodwill; (3) poses health and safety threats to American consumers; (4) eliminates American jobs; and (5) is a multibillion-dollar drain on the United States economy." The Senate Judiciary commented that its purpose in passing the ACPA was to "make the dangerous crime of counterfeiting a higher priority for law enforcement and to provide those charged with enforcing the laws the tools they need to do the job." (Senate Report-104-177)

The ACPA sought to accomplish congress' goal by making criminal infringement of a copyright and trafficking in goods or services bearing a counterfeit trademark predicate acts under the Racketeer Influenced and Corrupt Organizations (RICO) statute. Consequently, law enforcement may now combat the entire structure of a counterfeiting organization, from those providing the financing to those involved in the manufacture, distribution and sale of the copies. Criminals sentenced under RICO are also subject to enhanced penalties.

Second, Congress passed the NET, which directs the USSC, to:

(1) ...ensure that the applicable guideline range for a defendant convicted of a crime against intellectual property (including offenses set forth at section 506(a) of title 17, United States Code, and sections 2319, 2319A, and 2320 of title 18, United States Code) is **sufficiently stringent to deter such a crime** and to adequately reflect the additional considerations set forth in paragraph (2) of this subsection. [emphasis added]

(2) In implementing paragraph (1), the Sentencing Commission shall ensure that the guidelines provide for consideration of the retail value and quantity of the items with respect to which the crime against intellectual property was committed.

By directing the Commission to create penalties to deter counterfeiting and piracy Congress recognized its need to increase the actual length of sentences awarded for crimes under title 18, sections 2319, 2319A and 2320.

Congress' directives also have the effect of signaling the Commission to make changes in order to meet obligations set by international agreements to which the United States is subject. Specifically, the United States is obligated by membership in the World Trade Organization to provide penalties including, " imprisonment and/or monetary fines sufficient to provide a deterrent."¹ The North American Free Trade

¹ Trade Related Aspects of Intellectual Property Rights (TRIPs) Section, Part III, Section 5, Article 61

Members shall provide for criminal procedures and penalties to be applied at least in cases of willful trademark counterfeiting or copyright piracy on a commercial scale. Remedies available shall include imprisonment and/or monetary fines sufficient to provide a deterrent, consistently with the level of penalties applied for crimes of a corresponding

Agreement also requires participating countries to provide penalties to deter counterfeiting activity.²

It is important to note that in its directive to the Commission, Congress did not make corresponding changes to USC 2320, the underlying statute governing trademark counterfeiting. One explanation for Congress's omission is that it believes that existing penalties under the statute are stringent enough to provide a deterrent, if enforced.

Currently, USC 2320 carries with it penalties for first time offenders of up to \$2,000,000 in fines and/or imprisonment of up to 10 years for individuals, and fines of up to \$5,000,000 for corporations. Subsequent convictions may yield fines of up to \$5,000,000 and/or 20 years imprisonment for individuals and \$15,000,000 for corporations. Compared with its trading partners, these penalty levels rank among the highest in the world.

Unfortunately, under current USSC Guidelines, a counterfeiter convicted of violating USC 2320 would have to be caught with over \$120,000 worth of counterfeit merchandise to receive a minimum sentence of one year in jail. To receive the maximum sentence allowed by USC 2320, the counterfeiter would have to be convicted of trafficking in over \$80,000,000 worth of counterfeit merchandise. One result of these high monetary thresholds is that prosecutors are discouraged from pursuing all but the largest counterfeiting cases, because only then can they obtain meaningful criminal sentences under the sentencing guidelines.

One IACC member in particular has experienced difficulty in New Jersey and Southern Florida where federal prosecutors either required high monetary and evidentiary thresholds for prosecution, or outright declined to take any counterfeiting cases.³ One of the primary reasons cited for not taking the cases was the low penalties associated with counterfeiting under the Federal Sentencing Guidelines.⁴ These difficulties have a domino effect on federal law enforcement with the Federal Bureau of Investigation and the US Customs Service frequently declining cooperation because they knew federal prosecutors would not take the case.⁵

gravity.

² North American Free Trade Agreement, Part Six, Chapter Seventeen, Article 1717: Criminal Procedures and Penalties

1. Each Party shall provide criminal procedures and penalties to be applied at least in cases of willful trademark counterfeiting or copyright piracy on a commercial scale. Each party shall provide that penalties available include imprisonment or monetary fines, or both, sufficient to provide a deterrent, consistent with the level of penalties applied for crimes of a corresponding gravity.

³ Letter from Alfred T. Checkett, Corporate Security, Calvin Klein Cosmetics, to John Bliss, President, International AntiCounterfeiting Coalition, September 24, 1997.

⁴ Conversation with Alfred T. Checkett, October 1997.

⁵ Ibid. at 3.

Recommendations

Support Move to Toughen Fraud Standards

The IACC supports the Commission's proposal to strengthen fraud-related penalties as they apply to counterfeiting and piracy. Although under the proposed amendments first time offenders would have to be convicted of trafficking in over \$40,000 worth of counterfeit goods before facing a minimum sentence of one year in jail, the adjustments should help to raise the average sentence under 2320 above the one year level.

Counterfeiting better linked to theft

Counterfeiting is typically viewed as a fraud crime against the consumer, a viewpoint reemphasized by the USSC's use of the Fraud loss tables to calculate penalties. Counterfeiting and piracy, however, are more akin to theft. Counterfeiting is the theft of another's reputation and goodwill, along with their marketing and investment resources in order to sell cheap, inferior goods at high profits. Bruce Lehmen, former Assistant Secretary of Commerce, Commissioner of Patents and Trademarks, stated in an interview that, "[t]here is no difference between this economic crime [counterfeiting] and the harm that it has on Americans than literally if somebody walks in and steals money out of your purse, or money out of your wallet or from your credit card. . . .It's taking away from our own ability to make a livelihood and have a workable economy." The Commission should consider linking counterfeiting and piracy crimes to the higher theft penalties, rather than to fraud.

Goal to require minimum penalty of one year imprisonment for most counterfeiters

As previously mentioned, the IACC maintains that the only way to deter counterfeiting activity is to raise criminal penalties and impose jail sentences of at least one year. In those states that have passed new felony statutes and aggressively enforced the new laws, police, consumers and trademark owners have seen a marked drop in the level of counterfeiting activity. Enforcement from the federal level which results in actual jail time served will serve notice to counterfeiters that their nefarious activities will no longer be tolerated in the United States.

Calculating losses

The IACC supports the proposed Department of Justice language to "calculate the 'loss to the copyright or trademark owner' in any reasonable manner." As mentioned above, it is very difficult to calculate damages to a trademark holder from counterfeiting because counterfeiters operate a cash business with a limited "paper trail." Counterfeiting also does not necessarily equate into a one-for-one sales loss, since counterfeit merchandise is often sold at a price point far below the actual retail value of the legitimate product. Congress recognized these difficulties when

considering the ACPA and added a provision to the civil law allowing trademark holders to elect statutory damages on a per-mark basis. In the criminal context, courts should consider all aspects of the crime, the value of the legitimate goods, the value of the fakes, harm to reputation, dilution of the trademark, and other market forces when evaluating the amount of losses.

Conclusion

The passage of ACPA in 1996 marked the most significant changes in counterfeiting and piracy law in over a decade. Unfortunately the gains made under ACPA will be a Pyrrhic victory until the Federal Sentencing Guidelines are amended to be more commensurate with the stringent sentences proscribed by Congress.