

# **Fighting Counterfeiting in Asia**

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## **Introduction**

"Counterfeiting in China has reached a crisis point"

This is a common view heard from many western executives and government representatives. The problem for many appears to be getting worse as the quality of counterfeits improves every year and counterfeits are found in more and more overseas markets. The view applies not just to China but to other countries such as Indonesia, Vietnam and the Phillipines.

The problems with intellectual property infringement are, however, not just an issue for governments. Many western companies have done little to protect their intellectual property rights in Asia making them vulnerable to having their products copied. In addition, as a senior official of the Chinese Public Security Bureau pointed out at a conference jointly sponsored by the World Customs Organisation and Interpol, it is often foreigners who supply the machines to make counterfeits and it is foreigners who buy the counterfeits that are produced.

There are, nevertheless, improvements that could and should be made in China and other Asian countries intellectual property laws and practices. There are also improvements that can be made by a great majority of Western companies in their policies and procedures for tackling counterfeiting in China.

This article focuses on four areas.

First, in order to put the article in context the current counterfeiting situations in Asia and the way in which counterfeiters operate to manufacture and sell infringing products is reviewed. Second, the article reviews "best practices" right holders can adopt to defend their rights. Finally, how Western companies need to change their own practices so as to effectively protect their IP in China is considered.

## **The current counterfeiting situation in Asia**

For the purpose of this article counterfeits are defined as:

- (a) Complete counterfeits. These are fakes, products that look identical and are packaged in an identical manner, packaged with the same trademarks and the same getup.
- (b) Look-alikes. These are not identical copies, but are packaged with a similar trademark or a similar getup to confuse consumers.
- (c) Products which mis-use of trademarks. These refer to those products that are not products which the trademark owner produces, but use identical similar trademarks.

Anti-counterfeit actions should be aimed at preventing all the above 3 types of counterfeits both on the domestic market and in the export market. Complete counterfeits, generally, are the greatest threat to a business by directly threatening sales. However, look-alikes and products which mis-use trademarks also have potential to damage a right holder by diluting their brand.

## **How counterfeiters operate**

Counterfeiters worldwide operate in increasingly sophisticated ways that are designed to avoid detection and minimise the risk of detection by rights holders and law enforcement bodies. Even if detected, their methods of doing business are designed to minimise penalties that may be imposed. Key ways in which this is done are:

### Corporate practices

Front companies or front men are used to register companies that produce counterfeits. This makes it difficult to identify the true players behind a counterfeit operation and make them liable for their infringing acts.

Further, company production and sales records do not record that counterfeits are being produced and sold; rather model numbers and code words are used. Even if these are obtained as part of an investigation or raid action, they can be difficult to use unless the meaning of the model numbers and code words can be explained satisfactorily to a court.

### Production processes

Like all good modern businesses, in order to reduce "carrying costs" and the risk of seizure, counterfeiters utilise "Just in time production" and do not generally keep stock. They only produce according to orders, making it difficult to have large volumes of counterfeit products seized. If stock is kept, it is generally kept separate from manufacturing facilities in a secret location which is leased in the name of a front company and is difficult to link to the counterfeiter. The locations can often only be found after in depth investigation.

More sophisticated counterfeiters will not produce products themselves. Instead, they use separate sub-contractors to make different parts of the counterfeit goods which are then assembled by a further sub-contractor.

### Sales and Distribution

In order to avoid detection by investigators, counterfeiters will refuse to deal with potential customers who do not make a substantial purchase and will not provide samples. This can make it difficult and expensive to confirm if counterfeiting activities are occurring. Generally to mount any type of civil or criminal case, it is necessary to have a sample of the product to prove that it is counterfeit.

Even if an order is accepted, the main players behind counterfeiting often never themselves take delivery of counterfeit products. Products are instead shipped directly from sub-contractors to freight forwarders who ship products. Payment for counterfeits is arranged to be made to entities separate to the production and sales companies. This can make it difficult to tie the counterfeiter directly to seized products making criminal prosecution difficult.

Finally, sophisticated counterfeiters will often mix counterfeit with genuine products in an effort to avoid criminal prosecution. The counterfeiter will purchase genuine products on the grey market and mix genuine and counterfeit product, making criminal prosecution more difficult because most criminal justice systems provide a defence of innocence to defendants. Any person found in possession of mixed products can simply claim that they have been duped.

## **Best practices for rights holders**

The most successful rights holders in combating counterfeiting are companies that proactively manage their anti counterfeiting program. This includes:

1. designing products in such a way that they are difficult to counterfeit, and if copied are easier to take action through the counterfeit supply chain;
2. actively managing trademark portfolios so that registrations are obtained will in advance of the release of products;
3. proactively managing anti-counterfeiting investigations and programs and not being reactive to reports of counterfeiting.

#### Product design

Products should be designed so that they are not easily copied. This can involve introducing more complex and hard to copy parts. This can increase costs of production but also increase them for a counterfeiter who wants to copy products.

In order to take action throughout the supply chain, many companies in China are embedding trademarks on all key parts of their products and packaging. This means that suppliers of parts can be potentially liable for counterfeiting and raises the stakes for any action.

#### Trademark management

Effective trademark management is an essential part to avoiding counterfeit and infringement issues in China (and worldwide). Given the slowness of the registration system, it is essential that companies register marks well in advance of use, if at all possible. In order to avoid infringement by Chinese translations of marks, registrations should be obtained for Chinese trademarks and their variants.

#### Investigations and actions

Given the increased in sophistication of the counterfeiters, the companies with the best anti-counterfeiting programs in China have made strong investments in investigations. Investigations are targeted to identify the key players behind counterfeiting activities so that targeted action may be taken against them. One key part of such investigations is not to take immediate raid even when an investigator provides a sighting that counterfeit products are to be shipped. All actions are taken in the context of a strategic plan that should not be focussed on "seizure numbers". To be frank, if a factory is making counterfeits and is about to ship product and that factory is never going to make counterfeits again, then it is not a target. A factory found making counterfeits should be investigated to identify:

- (a) suppliers
- (b) sub-contractors;
- (c) customers;
- (d) ways in which products are being distributed in China and exported

Some time a raid action can help to identify such information, but action must be taken with this goal in mind.

The identification of major infringers and the proper recording of this intelligence must be a co-ordinated effort. Information is entered on a database, indicating the locality of the infringing product, the identity of the suspected infringer and the markets supplied. Details of previous actions taken and other relevant information should also be included. .

It is often quite striking how when information is properly analysed it becomes clear that there are a small number of organised syndicates involved in the counterfeiting of certain products. A number of computer programs have been developed that analyse intelligence in a way which

show links between various factories and counterfeiters and which eventually identify the mastermind behind counterfeiting activities.

## **Changes necessary in western companies' approaches**

### General

As a general comment, it is important to understand the legal systems in Asia. While not perfect, they do function and actions can be taken within the system.

Fundamentally, it is important to register rights for which protection is sought in Asia. There is no room for complaint if there is "infringement" of right which have not been registered.

### IP enforcement

Most international companies' anti-counterfeiting strategies have developed on a piecemeal basis with actions principally aimed at cutting off the source of counterfeit products and keeping counterfeiting under control in main markets. Often different in-house counsel are responsible for actions in different jurisdictions. In some cases, quite junior employees with little experience are left to handle counterfeiting matters unsupervised. Their only guideline appears to be to maximise seizures and minimise cost. This often results in disjointed and uncoordinated actions.

In recent years many companies have focussed their efforts on raiding of factories producing counterfeit products in China. This has had some effect in reducing the availability of counterfeits. Over time however, seizures have decreased and numerous repeat offenders have appeared. As noted above, sub-contractors are used to process orders for large factories making action against the real masterminds behind counterfeiting more difficult. Information obtained from actions in other countries is not shared between different people within an organisation and no detailed analysis of how counterfeiters operate is made. The focus on the volume of seizures can also mean that companies focus on easy targets, such as warehouses, and not factories.

The key to a successful enforcement strategy:

- (e) Do not delegate IP enforcement to junior level employees. It is important work that should be supervised by senior people with experience;
- (f) Invest appropriate resources into anti-counterfeiting, in particular by investing in investigation and identification of main players;
- (g) Once identified, go after main counterfeiters;
- (h) Do not judge success or failure of program on number of goods seized. This is a very raw tool that can be easily manipulated and does not reflect at all if progress is being made in rooting out the key players.

That is not to say that all resources should be expended on going after "big fish". It is necessary to keep the market under control and to discourage new entrants by continuing with other actions. However, resources should also be devoted to longer term in-depth strategies.

### Litigation

Many western companies shy away from civil litigation in China and other countries because the system seems too difficult to deal with. This is defeatist. No one has the right to complain about a system unless they have tried to use it. There are certainly difficulties in using the system, some of which have been discussed above, however, with a well prepared case, it should be possible to win and add to the costs of doing business for the counterfeiter.

## Education

All intellectual property lawyers who practice in Asia, have their war stories of clients coming to discuss intellectual property issues and, in many cases, becoming quite upset about infringement of their rights. The very same people will then ask for directions to the Silk Market in Beijing or Yatai market in Shanghai. Only certain types of products are on sale in these markets: counterfeits. Employees of a company from the top to bottom must appreciate that there is no "good" counterfeiting. Buying counterfeits of any type perpetuates the industry and sends a wrong message to the authorities about companies' commitment to fight counterfeiting. All companies serious about tackling counterfeiting should not tolerate the purchase of counterfeit products, even for personal use.

## **Conclusion**

The following tables sets out key recommendations for change for Western companies to protect their rights in China.

<b>Area</b>	<b>Recommendation</b>
General	Understand the systems. Register rights for which protection is sought in Asia - Do not complain if there is "infringement" of unregistered rights
IP enforcement	Focus enforcement strategy: - Do not delegate IP enforcement to junior level paralegals with no support - Invest appropriate resources into anti-counterfeiting - Go after main counterfeiters - Invest in investigation - Do not judge success or failure of program on number of goods seized
Litigation	Use the civil litigation system - it can be effective
Education	Educate workforce on the enforcement of IP, do not tolerate the purchase of counterfeit products, even for personal use.