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An ICC initiative
BASCAP
Business Action to Stop
Counterfeiting and Piracy

September 9, 2010

Ms. Victoria Espinel
United States Intellectual Property Enforcement Coordinator
Office of Management and Budget
725 17th Street, NW
Washington, D.C. 20503

Dear Ms. Espinel,

We write to you today concerning a study¹, soon to be published in the *British Journal of Criminology*, which suggests that police resources should not be used for criminal anti-counterfeiting enforcement. Having had an opportunity to review the paper, it is our opinion that Professor Wall's and Professor Large's basic assumption – that the counterfeiting of luxury fashion goods is significantly different from the counterfeiting of other types of goods, most notably “safety critical” goods – is fundamentally flawed. By extension, their suggestion that the entire burden of enforcement against counterfeiting in the luxury fashion goods sector should fall upon the manufacturers of legitimate luxury goods is, likewise, without basis. The adoption of such a policy would present a grave threat, not only to the economic vitality of legitimate manufacturers, but also to national economies and to end-consumers around the world.

Regrettably, the authors' conclusions are likely to perpetuate the general public's perception of counterfeiting as a largely victimless crime. For the reasons set forth in this letter, the

¹ Wall, D.S. and Large, J. (2010), “Jailhouse Frocks: Locating the public interest in policing counterfeit luxury fashion goods.” *British Journal of Criminology*, 50(6) (forthcoming).

undersigned organizations strongly dispute the authors' conclusions. Further, we urge you to continue your strong support for criminal enforcement, where authorized and appropriate under US law; and to continue your efforts to raise public perception about the full range of harms that result from the global trade in counterfeit goods.

The authors first identify three distinct groups of victims – consumers, who may be exposed to health and safety risks, or who may be fraudulently induced to buy a low-quality good at a premium price; legitimate brand owners whose business may be negatively impacted; and indirect victims, harmed by the loss of tax revenue to the government or other environmental effects. They then turn to what they characterize as the “orthodox anti-counterfeiting arguments”, outlining the economic, cultural and societal harms usually cited as potential harms related to counterfeiting, while seeking to distinguish the market for luxury goods from other types of goods, real and counterfeit. Central to their argument is the idea that the sale of counterfeit luxury items saturates the market with a particular item, driving consumers of legitimate luxury goods to purchase ever new designs from high-end manufacturers. This would suggest that counterfeit luxury goods keep pace with, or lag only slightly behind the current season's designs. However, this argument ignores the fact that counterfeit goods seen in the market are frequently “classic” designs rather than seasonal ones. Such goods are incapable of the authors' theorized “speeding up the turnover of the fashion cycle”, but simply serve to dilute the value of the brand, and destroy the cache of exclusivity that consumers of counterfeit goods are said to be seeking with their purchase.

Similarly, Professors Wall and Large raise, and quickly discount a variety of other traditional harms implicated by the sale of counterfeits.

With regard to consumer deception, it's stated that consumers “rationally weigh up the look, style and feel of the object, as well as the retail setting and its price.” Where the consumer willingly purchases items that they know to be counterfeit, and deception is not a consideration, the harm is said to be lessened. The authors note elsewhere in their paper however that consumers are more frequently purchasing counterfeits online – offering no opportunity to examine the goods prior to purchase – and further notes the trend of improvement in the quality of copies, which increases the likelihood that counterfeiters will be able to deceive consumers and pass off lower quality goods at or near the price of their legitimate counterparts. As the US Government has already noted, the increasing presence of professionally-designed “rogue websites”, which give the appearance of being legitimate online retailers, further increases the possibility of consumer deception in the online environment.

The authors largely ignore the potential for negative impacts related to consumer health and safety when dealing with counterfeit luxury goods – likely due to their primary determination that counterfeit luxury goods are a class separate and apart from “safety critical” counterfeit goods such as pharmaceuticals and airplane parts. They do note in passing that there are “possibly some potential health and safety issues if the materials used to make the goods were not safely manufactured.” Such an acknowledgement is hardly sufficient when one considers that the goods at issue are produced, distributed and sold outside of the regulated supply chain. This omission is more troubling in light of mounting evidence that counterfeiters increasingly manufacture their goods using materials and processes prohibited by laws and regulations governing the legitimate industry.

Another notable omission – especially given their underlying premise that public monies should not be expended on policing counterfeit trade – is the social cost of crime. Even small increases in the crime rate can impose very high costs for society This is a well-documented area of

research², for example in Mexico the social cost of crime as a proportion of GDP for Mexico City and the suburban area is 3.6%, which includes the cost of lives lost (homicide) and government expenditure on crime prevention. In the UK³, the economic and social cost of crime for the period 1999-2000 for England and Wales was estimated by the Home Office to be approximately €80 billion.

While the world has perhaps been slow to realize it, there is no longer any uncertainty about whether organized groups have moved into the IP crimes of trademark counterfeiting and copyright piracy. Not surprisingly, criminal groups are attracted to the money to be made in counterfeiting – especially luxury goods. A recent report from Rand Corporation⁴ presents detailed case studies from around the globe illustrating how criminal groups are using the profits generated from these crimes not only as a means of developing further markets for counterfeit goods, but also as a means of recycling and laundering the proceeds of other unlawful activities.

Professors Wall and Large downplay the widely-accepted view that organized crime and terrorist groups have turned to trafficking in counterfeit goods as a source of revenue. “[T]here still remains too much uncritical reliance on the logic behind the link between counterfeiting and organized crime and not enough reflection upon how it works and whether or not it exists at the present time,” they write. Surprisingly, the authors fail to cite any of a number of widely-publicized cases in the US which clearly demonstrate such links.⁵

Wall and Large overlook the potential for counterfeiting to increase the cost of crime facing society – which in turn exposes society and shoppers to greater crime and also puts an ever increasing upward pressure on the public sector to fight crime. As a result, organised criminal engagement in counterfeiting and piracy has emerged as possibly the most serious consequence of counterfeiting and piracy.

To put this into context, public sector budget officials should take a closer look at expenditures. For example, even taking the most modest assumption that counterfeiting could be responsible for raising the UK crime rate by just 1%, the economic and social cost of crime in the UK would increase by €1.7 billion. This figure captures the cost imposed on the criminal justice system as well as other social costs such as the cost of lives lost (homicides) and the cost of insurance and security to protect against crime. The €1.7 billion in additional cost represents more than 80% of total expenditures on the courts service in the UK and almost 5% of total expenditure on the criminal justice system in the UK.

Perhaps investment in fighting the criminal element behind counterfeiting should be considered not as a cost but as an investment – yielding rich dividends in terms of the safety and well-being

² Villoro, R. and Teruel, G. “The Social Costs of Crime in Mexico City and Suburban areas.” .

³ Brand, S. and Price, R. Home Office Research Study 217, “The economic and social costs of crime.”

⁴ Treverton, G. “Film Piracy, Organized Crime, and Terrorism,” Rand Corporation (2009).

⁵ See, e.g., the November 2009 indictments of Moussa Ali Hamdan and others in the Eastern District of Pennsylvania; < <http://www.justice.gov/usao/pae/News/Pr/2009/nov/hodrojetalrelease.pdf> >, and the 2006 guilty pleas of Imad Majed Hamadeh and Theodore Schenk, in a case involving trafficking in counterfeit goods and the provision of material support to Hezbollah; < <http://www.freerepublic.com/focus/f-news/1666784/posts> >.

of constituencies and freeing government resources for investment in infrastructure, education and other public goods.

Professors Wall and Large ultimately find little support for the allocation of public resources for the criminal enforcement of trademark counterfeiting in the context of luxury fashion goods. That conclusion appears less the result of the authors' research and analysis however, and more a function of their flawed assertion that counterfeit luxury goods are fundamentally different from goods which are more widely-viewed as implicating consumer health and safety. By minimizing the potential health and safety threats posed by apparel, leather goods, footwear, cosmetics and the like; and by down-playing, or arguably ignoring outright, demonstrated links between counterfeiting, organized crime and terrorism, the authors present a picture in which the supposed harms are minimized, eliminated, or perhaps even reversed. It is our sincere hope that neither the US government, nor its counterparts in the EU or elsewhere, will put the professors' theory to the test. Without question, such disengagement by law enforcement would have catastrophic effects.

We would like to commend your ongoing efforts to ensure strong enforcement of intellectual property rights in the United States, and in turn, ensuring the continued vitality of American innovators, and the continued safety of American consumers. Furthermore, we encourage you to move forward with the study on the economic impact of IP-intensive industries to the US economy which you outlined in the recently-published Joint Strategic Plan. We would welcome an opportunity to discuss this matter further.

Respectfully submitted by:

IACC (International AntiCounterfeiting Coalition)

BASCAP (Business Action to Stop Counterfeiting and Piracy)

INTA (International Trademark Association)

GIPC (Global Intellectual Property Center)

Cc:

Robert S. Mueller, III-Director of the Federal Bureau of Investigation (FBI)

John T. Morton -Assistant Secretary of Homeland Security for U.S. Immigration and Customs Enforcement (ICE).