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COUNTERFEITING AND THEFT OF TANGIBLE INTELLECTUAL PROPERTY: CHALLENGES AND SOLUTIONS

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BEFORE THE

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COUNTERFEITING AND THEFT OF TANGIBLE INTELLECTUAL PROPERTY: CHALLENGES AND SOLUTIONS

TUESDAY, MARCH 23, 2004

UNITED STATES SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Committee met, pursuant to notice, at 2:38 p.m., in Room 226, Dirksen Senate Office Building, Hon. Arlen Specter, presiding.

Present: Senators Hatch, Specter, Leahy, and Biden.

Senator SPECTER. Good afternoon, ladies and gentlemen. The hearing of the Committee on the Judiciary will now proceed. Senator Hatch, the Chairman, has asked me to preside. Senator Hatch is recovering from back surgery from last week, but he is on the premises today, but is taking it just a little easier.

The first question I want to address today is one which is on many minds in this room, and that is what happened to me. I was walking down Market Street in Philadelphia, the 200 block, after dinner on Saturday night, and I tripped on a defect in the sidewalk, and customarily there is a reflex action to put your hands out. Well, I did not do that, and the first contact was my nose and the cement. And I am pleased to report that I am fine, although bruised, and the cement is cracked. [Laughter.]

Senator LEAHY. Mr. Chairman, if I might, I am glad you made the explanation because I know that it sometimes gets contentious in the Judiciary Committee, and I did not want anybody thinking, insofar as Senator Specter and I have been friends for more than a quarter of a century, I did not want the wrong impression to be here.

Senator SPECTER. Senator Leahy and I have had no tough moments in the 24 years I have been here. He has been here 6 years longer. Our paths first crossed at a National District Attorneys Association meeting in Philadelphia, when he was the district attorney of Burlington, Vermont, and I was the DA of Philadelphia. In those days, we had important jobs.

That is a laugh line.

[Laughter.]

OPENING STATEMENT OF HON. ARLEN SPECTER, A U.S. SENATOR FROM THE STATE OF PENNSYLVANIA

Senator SPECTER. Today, we are going to proceed with our hearing on intellectual property theft and counterfeiting, a subject of really great importance in the United States today and growing. A

broad range of American industries are affected, including pharmaceuticals, automotive, music, movies, software and virtually every type of consumer product. There are enormous lost corporate revenues and profits, lost tax revenues, lost American jobs in the hundreds of thousands and a genuine threat to public safety from counterfeit drugs, foods, airplane and car parks.

The International Chamber of Commerce estimates that some $350 billion a year in counterfeit goods are sold worldwide. The automobile industry loses $12 billion a year, software another $12 billion, movies $3.5-, and in the music industry between $4- and $5 billion in losses and, globally, 2 in 5 recordings are pirated. There is a real public safety threat, and perhaps surprising to some, there are links to terrorism.

During a House International Relations Committee hearing last summer, the secretary general of Interpol testified that intellectual property crime is "becoming the preferred method of funding for a number of terrorist groups." It has been reported that the captured al Qaeda terrorist training manuals revealed the organization recommends the sale of counterfeit goods as a means to support terrorist operations and reports that Sheikh Omar Abdul Rahman, the blind Egyptian cleric linked to the 1993 World Trade Center bombing, relied upon counterfeiting to fund his operation.

So this is an issue of enormous importance, and we have assembled a very distinguished panel of witnesses from all branches of the Federal Government and then from many branches of the private sector to make an in-depth analysis here to find out what is being done and what the Congress can do further to try to deal with this enormous problem.

I am delighted now to yield to my good friend and colleague, the Ranking Member of this Committee, Senator Pat Leahy.

STATEMENT OF HON. PATRICK J. LEAHY, A U.S. SENATOR FROM THE STATE OF VERMONT

Senator LEAHY. Thank you, Mr. Chairman. I want to thank you and Senator Hatch for agreeing to hold this hearing. Both of you have had a long interest in this type of counterfeiting. We have spent a lot of time in recent years focusing on the many problems of intangible piracy, and that is what it is, piracy, particularly the theft of copyrighted works on the Internet, but I am pleased the Committee will also address the problems of tangible piracy: knockoff goods that violate the rights that are in trademarks, patents and copyrights, and then deprive the owners of the fruits of their efforts and investments, and often present consumers with very shoddy knockoffs.

Several years ago, Senator Hatch joined me in sponsoring the Anticounterfeiting Consumer Protection Act from 1996. That law addressed this problem. It amended a number of our criminal and tariff codes. The law made important changes, particularly by expanding RICO, the Federal antiracketeering law, to cover crimes involving counterfeiting, and copyright and trademark infringement. Even with that, more enforcement is needed in light of these practices that involve the theft of goods based on intellectual property rights.

Then, as now, trafficking in counterfeit goods hurts purchasers, State and Federal Governments, and economies at every single level. Indeed, this form of theft has become a method of choice for organized crime syndicates, as Chairman Specter pointed out, terrorist organizations—they do it for profit, to launder money to fund their criminal activities. I think Mr. Wray would agree, if we were in a closed-door hearing, and we could discuss that at even greater length, as he knows.

Just last year, I joined with Senator Allen in sponsoring an amendment to the foreign operations bill for 2004. It provides $2.5 million to the State Department in order to establish programs that will help developing Nations protect intellectual property rights—theirs and ours. These programs will strengthen intellectual property laws, educate and train law enforcement officers, and they will help our Customs officials to combat trafficking. It is going to give flexibility to the people who actually combat piracy in the field. So, Mr. Wayne, I am going to be very interested in knowing how this is being implemented at the State Department, and what other steps we might take.

We ought to remember that consumers feel the effects of counterfeit goods when they think they are buying a "brand name," spend the money to buy a brand name, and end up with a shoddy imitation instead. We are going to be hearing today from Vanessa Price of Burton Snowboards—back in my home State—who will bring home the kind of damage this does. I am very disturbed by the story she is going to tell, but I am glad she is here. Burton is a small company. Through a lot of work, a lot of trial and error, a lot of innovation, it has become the industry leader in snowboarding equipment and apparel, but you can find knockoff products labeled "Burton" all over the world. And this theft and free-riding on the reputation of such a creative company threatens to undermine the efforts of years of hardworking Vermonters.

I see similar stories all of the time in my office. SB Electronics in Barre, Vermont, has a niche area of capacitors, brilliantly put together, but now they see them reverse engineered, and its customers lost worldwide to inferior copycat models. Vermont Tubbs, a furniture manufacturer in Rutland, has seen its designs copied and then produced offshore with inferior craftsmanship and materials and then reimported to undermine their own sales. Hubbardton Forge in Castleton, Vermont, makes beautiful and very original lamps—again, a niche market—but they are being counterfeited, and then they are sold within the United States, with a lesser quality and at prices that undercut their own.

And some of the stuff being taken is amazing. At trade shows, cameras are prohibited. Well, at one trade show, a competitor—a competitor—hired the night cleaning crew to take pictures of showcased furniture, so then they could make knockoffs.

Of course, in some cases, these counterfeit goods pose a significant public health risk. According to the International AntiCounterfeiting Coalition, counterfeit parts have been discovered in helicopters sold to NATO, in jet engines—think about that the next time you get on a plane—bridge joints, and fasteners in equipment designed to prevent a nuclear meltdown. We all know about the stories of counterfeit pharmaceutical drugs.

What does it cost us? Three hundred and fifty billion dollars a year. That constitutes between 5 and 7 percent of world trade. Again, think about that in this country, when we have a $500-billion trade deficit this year alone. We are the world leader in intellectual property. So, if there are knockoffs, American companies suffer a disproportionate amount. In 2002, the movie industry lost $3.5 billion in pirated videos. To put that in perspective, that is a 60-percent jump from 1997. In a study examining the impact on trademarks, researchers for the International Trademark Association estimated that trademark holders worldwide lost $2 billion in 1995 as a result of this policy.

The Business Software Alliance estimates that pirated software alone cost the U.S. economy 118,000 jobs and $5.7 billion in lost wages in the year 2000. In my little State of Vermont, we lost $15.3 million in retail sales of software in 2002. That is 267 fewer jobs. Of course, it is lost revenues to our State, and that is just from computer software. You can go all the way down.

So think of what we have here—counterfeit and pirated music, software, T-shirts, clothing, fake drugs—and then think also of terrorist organizations using that money. There are thousands of reasons, thousands of reasons to work harder to end the trafficking and counterfeit goods: thousands of jobs lost, consumers harmed, trademarks and patents infringed, businesses threatened, and illegal enterprises enriched.

We all understand drug trafficking, international drug trafficking. We all understand arms trafficking. This is something we better start understanding because it is hurting us at every single level, including our personal and national security.

So, Mr. Chairman, thank you for having this hearing. It is extraordinarily important.

[The prepared statement of Senator Leahy appears as a submission for the record.]

Senator SPECTER. Thank you very much.

We now turn to our distinguished panel. The rule of the Judiciary Committee is 5 minutes on opening statements.

I might comment about recent memorial services for Ambassador Walter Annenberg in Philadelphia. We had a very distinguished array of speakers, including former President Ford, and Secretary of State Colin Powell, and I was there, Governor Rendell, and the limit was 3 minutes of speech. So I want you to understand that 5 minutes is a very generous allocation based on that analogy.

We now turn to our first witness, who is Acting Under Secretary of Commerce for Intellectual Property, Jon Dudas, who has been in this position since early this year. Last week, President Bush announced his intention to nominate Mr. Dudas for the appointment of Under Secretary of Commence for Intellectual Property and Director of the U.S. Patent and Trademark Office.

Before his current responsibilities, he served as council to the Subcommittee on Courts and Intellectual Property for the House Committee on the Judiciary for 6 years. So he is well-versed in Judiciary Committee hearings.

Thank you for joining us, Mr. Dudas, and we look forward to your testimony.

STATEMENT OF JON W. DUDAS, ACTING UNDER SECRETARY OF COMMERCE FOR INTELLECTUAL PROPERTY, AND ACTING DIRECTOR, U.S. PATENT AND TRADEMARK OFFICE, WASHINGTON, D.C.

Mr. DUDAS. Thank you, Mr. Chairman.

Mr. Chairman, Ranking Member Leahy, thank you for the opportunity to discuss the problem of intellectual property theft and the Department of Commerce's role in protecting intellectual property here and abroad. I want to begin by commending you and the Committee for holding today's hearing. Your longstanding commitment to protecting U.S. intellectual property and your consistent support of the United States Patent and Trademark Office are tremendously important.

Secretary Evans is keenly aware of the increasing significance of intellectual property protections for American businesses and innovators and has made combatting counterfeiting and piracy a top priority for the entire Department. As acting Under Secretary of Commerce for Intellectual Property, I am dedicated to marshalling U.S. Government efforts to reduce the toll that IP theft takes on American IP owners and American consumers. Far too many jobs are lost and far too many companies are hurt because of intellectual property theft.

More and more, intellectual property is a key driver of economic growth. For example, the U.S. copyright industry continues to lead the economy in their contributions to job growth, GDP, and exports. Between 1977 and 2001, their share of GDP grew more than twice as fast as the rest of economy. These same companies depend upon their brands and trademarks to compete effectively in the marketplace. Unfortunately, the economic benefits of capitalizing on intellectual property rights have captured the attention of pirates, organized crime, and as you mentioned, in some limited, but increasing, cases, terrorists. The Secretary General of Interpol testified last year, again, that IP crime is becoming the preferred method of funding for a number of terrorist groups.

The illegal duplication of software, music, DVDs and other digitized information and the trafficking in counterfeit products is widespread. In China, an estimated 90 percent of business software, valued at $1.5 billion, is pirated. In Russia, the bulk of video and audiotapes are counterfeit. Because of this piracy, the U.S. software industry has lost billions of dollars in 2002 alone. Global trademark counterfeiting totals about $500 billion a year. Counterfeit automotive parts production alone costs the auto industry $12 billion a year. Commonly prescribed drugs, such as Lipitor and Viagra, are increasingly counterfeited, posing health risks to consumers.

Given these threats, the USPTO and our colleagues in the Department of Commerce are working hard to curb intellectual property crime and strengthen intellectual property enforcement in every corner of the globe. Through our Offices of International Relations and Enforcement, the USPTO works to ensure that American IP owners have sufficient legal tools to fight piracy. We provide technical assistance and training to foreign entities on implementing and enforcing effective intellectual property laws. We also serve as co-chair of the National Intellectual Property Law Enforce-

ment Coordination Council, which coordinates domestic and international intellectual property law enforcement here in the U.S.

The focus of USPTO's efforts are: one, addressing the difficulties Governments face in meeting international intellectual property obligations; and, two, bringing together local authorities to address enforcement issues.

For example, we help countries establish adequate enforcement mechanisms to meet their obligations under the WTO TRIPs Agreement. The TRIPs Agreement sets minimum standards of protection for IP and requires WTO members to provide for effective enforcement of intellectual property rights. In negotiations on Free Trade Agreements, we push for a "TRIPs-Plus" format that expands the minimum standards that are set out in TRIPs.

China, as the Committee is well aware, is a major concern on intellectual property piracy. Last fall, Secretary Evans led a mission to China and highlighted China's lack of intellectual property enforcement. The Secretary met with high-ranking Chinese officials and reiterated that effective IP protection requires that criminal penalties and fines be large enough to serve as a deterrent rather than a mere business expense.

As a follow-up to the Secretary's trip, the USPTO recently led a delegation to China for consultations with senior Chinese officials and U.S. companies operating on the ground in China. A primary focus of this trip was to further the administration's goals of reducing widespread counterfeiting and piracy. Many industries have noted that the Chinese Government, by restricting market access for certain products, is providing free reign for counterfeiters, pirates and criminals to exploit the void created by the lack of legitimate products.

Given these trends, we are continuing to press hard for enhanced steps by the Chinese Government to significantly reduce the extent of intellectual property violations.

Mr. Chairman, Ranking Member Leahy, the demands on the Department of Commerce and the USPTO's expertise in combatting IP piracy have grown dramatically in the last few years. I am hopeful that with the continued support of this Committee, and in partnership with the Congress, we will be able to do even more to provide American businesses and entrepreneurs with the IP protection they need and deserve.

Clearly, in terms of the economy and national security, much is at stake. That is why our dedicated team of experts will continue to work tirelessly to protect American products in every corner of the globe.

Thank you.

[The prepared statement of Mr. Dudas appears as a submission for the record.]

Senator SPECTER. Thank you very much, Mr. Secretary Dudas.

We turn now to the assistant general for the Department's Criminal Justice Division, Christopher Wray. Over the past years, the Division has developed an institute of the joint initiative with the FBI and U.S. Customs to combat piracy and counterfeiting.

Before General Wray was appointed to his current position, he served as U.S. attorney for the Northern District of Georgia and

was the director of a special task force investigating Enron Corporation.

Thank you for coming in today, General Wray, and we look forward to your testimony.

STATEMENT OF CHRISTOPHER A. WRAY, ASSISTANT ATTORNEY GENERAL, CRIMINAL DIVISION, DEPARTMENT OF JUSTICE, WASHINGTON, D.C.

Mr. WRAY. Thank you for inviting me to testify before you today, and this is an extremely important topic, and I commend you, Mr. Chairman and Senator Leahy, for holding this hearing. My full written statement has been submitted to the Committee, so I will just summarize briefly here.

We are, I think it is clear, at a pivotal time in the history of intellectual property rights enforcement. A number of factors have come together to create unprecedented challenges to intellectual property rights holders and to law enforcement. The Internet and technology have made piracy and counterfeiting easier and less expensive than ever before.

At the same time, the quality of the illicit goods is often near perfect. Detecting these illegal operations is more difficult than in the past and is compounded by sporadic and inconsistent enforcement throughout the world. Piracy and counterfeiting are often deemed low-risk, high-reward endeavors that are beginning, not surprisingly, to attract organized crime syndicates throughout the world.

The harm caused by these criminals is real. Businesses cannot survive in an environment where black-market goods are more available and cheaper than legitimate goods. Small businesses, as Senator Leahy noted, are forced to close and bigger businesses must downsize.

Piracy also deprives consumers of their important right to be assured that the products they buy are safe and legitimate. Since the beginning of his tenure, Attorney General Ashcroft has worked to ensure that the Department has the prosecutorial resources necessary to fight intellectual property crime.

With the assistance of Congress, he has expanded the number of Computer Hacking and Intellectual Property Units—what we call our CHIP Units—operating nationwide from just 1 to 13. These specialized units consist of dedicated Federal prosecutors whose primary focus is prosecuting high-tech crimes, including intellectual property crimes. The CHIP Units complement the already existing network of over 200 specially trained Computer and Telecommunications Coordinators—or CTCs—that now serve in every U.S. Attorney's Office across the country. Like the CHIP Units, the CTCs also focus on the prosecution of high-tech crimes, again, including intellectual property crimes.

Working closely with the CHIP Units and the CTC network is our Criminal Division's Computer Crime and Intellectual Property Section, also known as CCIPS. And, again with the support of Congress, the size of CCIPS has increased significantly over the past 2 years, allowing us to substantially enhance our intellectual property enforcement efforts. CCIPS is developing and implementing a focused and aggressive long-term plan to combat intellectual prop-

erty crime. So, working in concert, CCIPS, the CTCs and the CHIP Units create a formidable, multi-pronged approach to prosecuting intellectual property crimes.

As my written testimony highlights, our efforts are having an impact. We have successfully prosecuted piracy and counterfeiting cases that are resulting in significant penalties. Recently, for example, in the Eastern District of Virginia, a man received 70 months in prison and was ordered to pay $1.7 million in restitution for trafficking in high-quality Microsoft products. And last year in South Carolina another defendant was sentenced to 7 years in prison and ordered to pay over $3.4 million in restitution to Nike and Tommy Hilfiger for trafficking in thousands of counterfeit T-shirts and other products and engaging in money laundering.

These are significant prison terms that send the clear message that counterfeiting is no longer a consequence-free enterprise. Such severity is essential, for the damage from intellectual property offenses can go beyond lost sales and cut right at the heart of public health and safety. For example, we have successfully prosecuted a number of individuals for selling counterfeit baby formula, as well as a man in Alabama for selling misbranded pesticides, intended to stop West Nile Virus, to municipalities all across the Southern United States.

Counterfeit products, such as pharmaceuticals, pesticides and food products not only deprive consumers of their right to safe and legitimate products, but they threaten society's most vulnerable members, including our children and those who are ill or injured. We are actively exploring additional ways in which we can increase the use of criminal trademark and counterfeit labeling laws to help protect the health and safety of our citizens.

Our efforts do not stop at our borders, however. Piracy and counterfeiting are global crimes that ignore geographic boundaries. The Department is committed to working with our foreign law enforcement colleagues to improve international IP enforcement. For example, later this month, a Ukrainian man is scheduled to be extradited to the United States from Thailand to face prosecution for his piracy and counterfeiting activities involving the online sale of over $3 million in counterfeit software. The Department is also in the process of seeking the extradition of a man from Australia for his leadership role in an international piracy conspiracy.

We are working closely with law enforcement from around the globe to identify and assist in the prosecution of IP criminals in their native lands, and this will become increasingly important in the years ahead, as we are seeing an increasing emergence, particularly in Asia, of organized crime involvement in IP crime. Organized crime has the resources and distribution methods to operate sophisticated counterfeiting operations. These groups do not hesitate to threaten or injure anyone, ranging from industry representatives to Government officials who attempt to interfere with their illegal operations.

Information from overseas indicates that it is not uncommon for enforcement raids on illicit factories to degenerate into full-blown shootouts. There is no doubt that these worldwide criminal syndicates are formidable foes and that we must be just as formidable in our response to truly attack the problem of hard goods intellec-

tual property piracy. Effective IP enforcement must be global, and we are working daily to set standards in international cooperation.

In closing, I want to reaffirm the Department's commitment to combatting IP crime aggressively, both domestically and overseas. In the prosecutions that we have undertaken, and those that lie ahead, we will continue to send a strong message to those engaged in piracy and counterfeiting that their conduct will not be consequence free.

Thank you, Senator.

[The prepared statement of Mr. Wray appears as a submission for the record.]

Senator SPECTER. Thank you very much, General Wray. Your full statement will be made a part of the record, as will all of the statements.

We now turn to Assistant United States Trade Representative James Mendenhall, who handles the services, investment and intellectual property in the Office of Trade Representative. Prior to his current duties, he served as deputy general counsel to the trade representative and has a very extensive career in private practice, concentrating on international trade law.

Thank you for coming in today, Representative Mendenhall, and we look forward to your testimony.

STATEMENT OF JAMES MENDENHALL, ASSISTANT U.S. TRADE REPRESENTATIVE FOR INTELLECTUAL PROPERTY, OFFICE OF THE U.S. TRADE REPRESENTATIVE, WASHINGTON, D.C.

Mr. MENDENHALL. Thank you, and good afternoon, Mr. Chairman and Senator Biden.

The theft of intellectual property worldwide is an enormous and growing problem. U.S. industry losses due to piracy and counterfeiting are conservatively estimated to be around $200- to $250 billion a year. As a result of this criminal activity, many foreign markets are simply evaporating. In China and Russia, industry estimates that piracy levels in many sectors are close to or exceed 90 percent of the market.

USTR and other agencies are working around the clock to resolve this problem, a problem made complex not only by its sheer scale, but by multiple underlying causes. I will outline four key challenges facing the United States in this area and five tools that we have brought to bear on the issue.

First, pirates and counterfeiters exploit technological advances and employ modern business models to streamline and expand their operations. Sophisticated copying technology is now available off the shelf, and pirates have been quick to put it to illicit use. For example, CD and DVD burners enable pirates to churn out thousands of illegitimate copies of music, software and movies without significant investment in equipment and facilities.

Pirates have also become globalized. If they are shut down in one country, they simply move to the next. They run global production and distribution chains, exporting their illicit goods and displacing legitimate products from markets around the world.

We have begun our counteroffensive on this front, for example, through the development of new enforcement rules in our Trade Agreements, as I will explain later.

Second, the unshackling of markets and economies, such as China and Russia, present tremendous opportunities, but unfortunately not always for the good. Criminal enterprises, including small operators and sophisticated organized crime syndicates, are growing up side-by-side with legitimate business operations. Yet these countries have failed to provide adequate means and incentives to prosecute criminal offenders in all cases or to deter future criminal activity. The solution to this problem runs much deeper than the protection of intellectual property and requires the creation of a legal system and culture built on the rule of law.

A third challenge is the creation of international legal rules to deal with enforcement. Enforcement is perhaps the chief complaint that we hear today from our IP-intensive industries. Yet enforcement obligations, by their nature, are not as black and white as other obligations in that it is difficult to determine, for examine, whether a country has in place effective deterrent remedies to prevent IPR infringement. We have tackled this issue head on in our FTAs, which contain extensive provisions designed to strengthen IPR enforcement.

The final challenge is to rebut the skeptics in other countries who question the value of intellectual property rights. Obviously, the infringement of intellectual property rights has deep adverse impacts on our economy and on our industries, but it is more than that. For example, trademarks are not simply names and symbols, but measures of quality, trustworthiness and the value of a product. IPR protection promotes consumer protection and safety. Trademark infringement can result not only in the counterfeiting of handbags and shoes, but can lure unwary consumers into purchasing defective windshields that shatter on impact. We have all heard the horrible stories, such as counterfeit pharmaceuticals filled with paint or baby shampoo filled with industrial solvents.

IPR protection also promotes development. As long as local artists cannot make a living in their home markets because of rampant piracy, local talent will remain undeveloped. Patent and copyright infringement can cause the flight of investment out of a country, thereby curbing development of a local technological base.

Now, the complexity of this problem calls for a comprehensive, multi-faceted solution, and USTR and other agencies have employed all tools at our disposal to deal with the problem, and we will continue to do so.

First, we require that our Free Trade Agreement partners bring their IPR regimes up to world-class standards. Our FTAs contain provisions dealing with a whole range of IPR, including such issues as curbing the use of equipment used to circumvent anticounterfeiting technology and dealing with sector-specific problems, such as optical disk or broadcast piracy. They also facilitate the bringing of cases and strengthen domestic criminal and civil enforcement measures.

Second, the USTR annually issues the Special 301 Report, which catalogues the IPR problems in dozens of countries around the world and places them in a hierarchy of wrongdoing, ranging from the lowest-ranking of "Watch List" to the ranking reserved for the worst offenders, a "Priority Foreign Country."

As a result of this exercise, countries come forward each year with reforms and reform proposals to avoid elevation on the list. In the most serious cases, countries identified as Priority Foreign Countries can be subjected to a Section 301 investigation and face the possible threat of trade sanctions. We used the threat of trade sanctions in the mid 1990's to win an IPR agreement with China, and we have more recently imposed Section 301 sanctions on the Ukraine.

Third, USTR is the lead agency, working closely with other agencies, in addressing IPR issues multilaterally through the WTO. The initiation of dispute settlement proceedings is the most forceful expression in the WTO of dissatisfaction with a country's IPR protection and can be an effective way to achieve reform. In nearly all cases that USTR has initiated, U.S. concerns were addressed via changes in laws and regulations by the other party. We also regularly review countries' IPR laws and practices through the WTO Trade Policy Review mechanism and in the TRIPs Council.

Fourth, USTR administers the Generalized System of Preferences program and other similar programs which allow us to withhold tariff preferences if a country fails to adequately protect IPR. The "carrot" of preserving tariff preferences is an effective incentive for countries to protect intellectual property rights.

Finally, USTR, the State Department, the Department of Commerce and others have used diplomatic pressure to encourage IPR reform around the world. For example, Ambassador Zoellick has repeatedly emphasized the importance of this issue with the Chinese Government, and Deputy USTR Josette Sheeran Shiner has had multiple visits to China in the past few months alone to deal with this matter. In the coming days, she will return to China to prepare for the U.S.-China Joint Commission on Commerce and Trade meeting next month, where IPR will be high on the agenda.

Dealing with the problem of piracy and counterfeiting requires a comprehensive, intensive and sustained effort. Ambassador Zoellick is strongly committed to continuing to bring all of USTR's weapons to bear on this issue and to maintain the pressure in the coming years. We have made progress, but enormous challenges remain, and I look forward to working with you and your staffs to continue to devise solutions for dealing with this critical matter.

Thank you.

[The prepared statement of Mr. Mendenhall appears as a submission for the record.]

Senator SPECTER. Thank you very much, Mr. Mendenhall.

Our next witness is assistant secretary of State for Economic and Business Affairs, Earl Anthony Wayne. Mr. Wayne has had a distinguished career in international trade and foreign service. He had been first secretary to the embassy in Paris, a very extensive background in Western European Affairs at the National Security Council.

We thank you for joining us, Secretary Wayne, and the floor is yours.

STATEMENT OF EARL ANTHONY WAYNE, ASSISTANT SECRETARY OF STATE FOR ECONOMIC AND BUSINESS AFFAIRS, DEPARTMENT OF STATE, WASHINGTON, D.C.

Mr. WAYNE. Thank you very much, Mr. Chairman, Senator Biden. It is a pleasure to be here to talk about this important set of problems.

In the State Department's Economic and Business Affairs Bureau, we have a mission statement on the wall, and one of the top priorities in that statement reads: "Increase market access for U.S. goods and services, protect intellectual property and promote global information and technology communications."

So I would like to talk a little bit today, complementing my colleagues, on three interrelated activities that we are undertaking to try to put this statement into action, working with our missions around the world. That involves three types of building: building knowledge, building capacity and building will.

By building knowledge, I am talking about the need to increase awareness of intellectual property rights. That starts at home. It starts in the training. When new foreign service officers come in to the Department of State, in their introductory courses, they now learn about pharmaceutical data protection, about optical disk piracy, about counterfeit Levi jeans, about the problems this poses for American businesses. That training now continues for economic and commercial officers, for deputy chiefs of mission, for ambassadors. We have built this in to drive home how important these issues are for America's prosperity.

Of course, an even greater problem is building that understanding overseas, where sometimes the perception is that, "gee, IPR, that only benefits big American companies. It does not really concern us in this country." But we are trying to use all of the diplomatic tools that we have in our tool chest to get the message out, from bilateral meetings, sending foreign journalists to the U.S. to understand the issues better, sending academic experts overseas to talk with people, using digital video conferences to bring people together and to get our ambassadors and economic counselors out on the stump and really explaining this to all sorts of audiences, from academics and officials to students overseas, so they start understanding how important these things are.

Attached to my written testimony, I have included an op-ed that our ambassador to Russia, Sandy Vershbow, wrote last year specifically tailored to the Russian cultural heritage and how a lot of this cultural heritage was being lost, and their artists were not being able to build on this because of the piracy and counterfeiting that was going on and how a lot of the Russian intellect in software and other things just could not be profitable because they had so much piracy and counterfeiting. Those are the kind of things our embassies around the world are doing to build understanding.

The second, key front is building capacity. At home, we are working to use the Internet much more effectively ourselves, to connect with our embassies, and to put embassies in touch with each other when they are facing similar problems around the world. We are bringing officers together to talk about best practices. We are having a conference in Brussels next month, where we are bringing officers from all over Europe, North Africa and the Middle East, so

we can learn together with officials from Washington, what are the best arguments, what are the best practices, how can we be more effective overseas?

Now, the other kind of capacity building is helping developing and transitional economies. That is where the funding that Senator Leahy mentioned earlier is so important as we try to really build the chain that is so key between judges and prosecutors and Customs officials and cops on the street, so really we can fight this problem overseas. We know from our own experiences, one weak link can make that a flawed process, and there are a lot of weak links in these developing economies and transitional economies We are trying to use the means that we have to address that challenge.

We have a number of coordinating efforts to make sure that we work with industry, with other agencies to find the best kind of programs to go forward, to use the funds that we have available for training well. And we very much appreciate the congressionally appropriated money for this, which will be very, very helpful in this effort.

Finally, building will. Often building will is a key part of what we are doing, maybe even the most important part. This is the will in foreign capitals to really take action. As my colleagues have mentioned, we use a lot of different tools in this process—bilateral meetings, for example. The Secretary of State, my boss, the Under Secretary of State, our ambassadors around the world and I are complementing what our colleagues in the U.S. Government are doing on a regular basis. We see this as a very important part of our foreign policy portfolio.

All of the trade negotiations that are going on constitute another tool. USTR is in the lead in that effort, but it is often our missions overseas that are, on a daily and weekly basis, reinforcing that message from USTR and working very closely with them to reach out to try to build the coalitions in those local Governments that really understand why this is in their interests.

And that is similarly true in the 301 process—often very important to get the attention of countries overseas, as we are moving forward, to really address the problems that they have. And, as Jim Mendenhall mentioned, when other methods do not work, we do consider imposing sanctions, using the Special 301, the Generalized System of Preferences or going to the WTO in certain cases.

We do not pretend to have all of the answers to this, Mr. Chairman, but we do know that we need to keep working hard on these three aspects: knowledge, capacity and will. We also know this has to be a team effort. It has to be a team effort within the U.S. Government. It has to be a team effort with industry and, Senators, with you and your colleagues in going forward. When you all pay attention to these issues, when you speak out on your foreign trips and communicate with your foreign colleagues, it does have a big impact. We very much appreciate your attention and interest in this and look forward to working with you.

[The prepared statement of Mr. Wayne appears as a submission for the record.]

Senator SPECTER. Thank you very much, Secretary Wayne.

We are going to now go to questioning of the panel, and we are going to establish a 7-minute limit. We have another panel of 5 dis-

tinguished witnesses, so we are going to be running late, in any event. And we are uncertain as to whether there are going to be votes later this afternoon, but when you get near the 4 o'clock range, you are in jeopardy of votes. And once they start, it is pretty hard to keep people waiting a long time and to come back. So I appreciate your staying within the time limits, generally.

As I hear your testimony, I see a breakdown which I would specify: Actions against Nations, number one; individual violators, number two; organized crime, number three; and terrorists, number four.

General Wray, you have stated an impressive list of prosecutions by the Department of Justice. What is your evaluation of the sufficiency and deterrent quality of those prosecutions? Stated differently, is the message getting across? Do you have sufficient resources to bring enough prosecutions to let the violators, the pirates know that they are subject to tough prosecutions to have a deterrent effect on would-be violators?

Mr. WRAY. Senator, I—Mr. Chairman, I should say—I would think that there—

Senator SPECTER. Senator is okay.

Mr. WRAY. I would answer on a couple of fronts. On the success I think we are having, in terms of getting the message out, we are trying to focus our cases primarily on the biggest organizations, the most sophisticated ones, the ones that we think are having the greatest and most harmful impact.

Senator SPECTER. Are you sending some of them to jail of that size?

Mr. WRAY. We are. We are sending individual defendants to jail. One of the things—

Senator SPECTER. What is the longest sentence you have got?

Mr. WRAY. I think that is—

Senator SPECTER. Pardon me if I get down to nitty-gritties, as a former prosecutor.

Mr. WRAY. The longest one that I know of, off the top of my head, is the 7-year sentence I mentioned in my opening testimony.

Senator SPECTER. A good sentence?

Mr. WRAY. One of the things that we have seen over the last couple of years is increasingly stiff penalties. For example, in fiscal year 2000, I do not think we had a single defendant who went to prison for more than 3 years. Last year, fiscal year 2003, we had I believe at least 10 who went for more than 3 years. So we are starting to see—

Senator SPECTER. Do you sense a deterrent effect from the success you have had on sentencing?

Mr. WRAY. We think we are starting to see the message getting through that we are serious about this and that we are cracking down.

You also mentioned things that we could do to improve enforcement, and I think obviously, as a former prosecutor yourself, you can never have too many good investigators, and we would certainly always appreciate more agent resources to work on it because that would enable us to do more proactive investigations which, as you know, in an organized crime-type of setting enables us to penetrate the organizations in a more effective way.

The other thing that I and all of my colleagues here on the panel are all recognizing is that this is a truly international problem. If you think of it like the weed in your yard, if you just focus on it domestically, all we are really doing is cutting off the blade that is above the soil, and we are not getting down into the roots of it. And by doing it in a multi-agency, international way, we are really trying to get at it everywhere because intellectual property crime in other countries has a direct impact on victims, businesses and consumers here.

Senator SPECTER. General Wray, let me turn to that. With respect to suggestions about sanctions, which Mr. Mendenhall has mentioned, and China as being a major violator, which Mr. Dudas has mentioned, what would you think of the prospect of revoking China's Most Favored Nation status? I did not like that in the first place. I was one of fifteen Senators to vote against that.

Mr. Dudas, you say that China has a lack of piracy enforcement, and it is getting worse. Why not get tough with them and revoke their Most Favored Nation status?

Mr. DUDAS. I think that is something that would have to be thoroughly discussed. I can tell you I think right now the initial step with China is to make clear that there are measurable, deliverable results that the United States must see.

Senator SPECTER. Secretary Evans is a tough guy. What effect did he have when he jaw-boned him?

Mr. DUDAS. I think he has had a fairly dramatic effect. When I went out in the last week, the sense I got, I think, is that the jury is out on what the Chinese will come in and want to discuss, and perhaps what they will deliver at the JCCT.

Senator SPECTER. The jury is out? You are going to have to poll the jury. They are pretty hard to figure, even after they come back.

Mr. DUDAS. I think what we are discussing now is what specifically does China need to show. We have found that the statistics that we see are not improving. The statistics show that our Customs seizures since 1997, 16 percent of seized goods came from mainland China. That has grown to over 66 percent of seized counterfeit goods coming from mainland China.

I think, in the absence of seeing improvement in our statistics, the discussions we had with Chinese Government officials are: you will need to show specific improvement along the following lines.

Senator SPECTER. Mr. Mendenhall, let me turn to you because I have two more questions, and I want to conclude within my time limit. If Most Favored Nation status is not tough enough, what can we do tougher under 301 sanctions to Chinese? Just start there. They are the leading nominee for tough sanctions.

Mr. MENDENHALL. Well, I would like to reiterate the comments that Mr. Dudas has made already. I think there is very little question that we are at that point where getting tough with China is where we ought to be

There are processes that are in train that will hopefully get us to the point where we can make a fully considered decision about what the next steps would be; the next one being the JCCT meeting in mid-April, where we have, as Mr. Dudas explained, provided the Chinese with very concrete steps that we would expect them

to take, concrete measures that we would expect them to take to move forward until that process is working.

Senator SPECTER. What tough sanction, Mr. Mendenhall?

Mr. MENDENHALL. I am sorry?

Senator SPECTER. If they do not comply, what tough sanction?

Mr. MENDENHALL. Well, there are multiple options that would be presented to us. I mean, there is the multilateral option of going to the WTO, if we feel that that is appropriate at that point. There is this Section 301 process available under U.S. law, but that is—

Senator SPECTER. How about closing our markets to them or tariffs like on steel?

Mr. MENDENHALL. Well, there are I think things that we would have to consider that would have to factor into that decisions.

Senator SPECTER. Mr. Mendenhall, let me ask you to supplement your answer in writing because I want to ask Mr. Wayne a question, and I have only got 33 seconds left.

Mr. MENDENHALL. Yes.

Senator SPECTER. Mr. Wayne, as I listen to the four of you—Treasury, Justice, Commerce, State—four potent operations, do your four powerful organizations sit down in a joint cooperating Committee to figure out what they are doing and figure out ways to act in a joint way with all of the power that your four departments have?

You can have the balance of my time on answering.

[Laughter.]

Senator SPECTER. The red light went on when I finished the question.

Mr. WAYNE. Thank you, Mr. Chairman. We do sit down. We sit down regularly, and we sit down to look at it from several different angles.

One, in the Special 301 process, we work very closely together. We are right now in the midst of getting reports from all of our embassies overseas, hearing from industry, hearing from other interested parties, and then we sit down together, and we work through what has the performance been over the past year, what makes the most sense vis-a-vis number of these key actors to really enforce the need for action.

Secondly, we have a Committee that sits down on a monthly basis, at a working level, and looks at the different kind of training programs that are going on, from industry, from the various agencies, and we try to figure out what is working. Where should we put our priorities for the months ahead? Are there a set of trainings that really did produce results? Should we try and do that somewhere else?

And then we have the NIPLECC process, which is led by USPTO and Justice, where we get together at a policy level and look at what is working overall, in our macro approach.

So, in those three examples, and then in a number of other specific examples, especially, if we are considering going forward on the WTO process, I would say we are in really pretty much constant contact and constant discussion about what is working, what is not working, what is the best way to take on some of these ongoing problems.

Senator SPECTER. Thank you, Mr. Wayne.

Senator Leahy?

Senator LEAHY. Well, to follow up a little bit—I wanted to thank you—on what the Chairman said, Mr. Dudas and Mr. Mendenhall, I thought he asked very clear questions about China. I am not quite sure I got a clear answer, so I will be submitting more questions, but China has been ripping us off for years, and we keep saying, "Boy, next year, wow, it is going to be so much better." They have an artificially set currency, which hurts us. A lot of American jobs are going over there, and I happen to be one who strongly believes in as much free trade as possible, if it is fair. I voted for a lot of the things to allow trade with other countries.

And this has gotten beyond the question of "let us have another meeting", and "let us put the highest level in our meetings," and "let us have the highest discussions, and let us consider our options, of which there are many." It is actually time to do something. They have made a laughingstock of us. They steal hundreds of millions, even billions of dollars from us every single year. I do not see where we do anything that is actually going to stop them.

Take a place like Singapore—put a 3-inch graffiti mark on the wall somewhere, and you can go to jail. Steal hundreds of millions of dollars of American intellectual property, and you are probably going to get "businessperson of the year." We really look like saps around the world with what happens.

Mr. Wray, the Department of Justice plays a critical role in the enforcement of intellectual property rights. And of course whatever amount of time you spend on it, there are priorities—and of course in the Department of Justice you have to set priorities—that determines how effective our intellectual property will be. Obviously, if we had somebody who walks into a bank, and stole a billion dollars and made a clean get-away, the Department of Justice would put enormous resources to go after him. We have billions of dollars being stolen all the time.

The AG's Annual Report from 2002 cites 81 investigative matters that resulted in 52 cases filed in regard to trafficking in counterfeit goods. I am going to ask specifically for the record, does the Department have any plans to increase the number of investigative matters? What resources were devoted to counterfeit goods and IP piracy investigations in 2003? I will have those for the record.

But we had a lot of publicized prosecution of the bootleg film of "The Incredible Hulk." Well, big whoop, they could have just waited. That movie sank like a rock at the box office. Within a couple of weeks, they probably could not have given away the copies. But I do not remember a significant prosecution in the intellectual property area over the past 3 years. What would you say are your 10 most significant intellectual property prosecutions in the last 3 years—the 10 most significant intellectual property prosecutions in the last 3 years? I am not saying the last year. I will give you 3 whole years, at 3-and-a-third a year?

Mr. WRAY. I think one of the biggest ones was something called "Operation Buccaneer," which was a large piracy conspiracy that involved search warrants all over the world, has resulted in I think 26 convictions so far, as well as some prosecutions overseas, working in partnership with overseas—

Senator LEAHY. How many of those convictions were here in the United States?

Mr. WRAY. I am sorry?

Senator LEAHY. How many convictions in the United States?

Mr. WRAY. Twenty-six in that operation so far.

Senator LEAHY. What was the nature of the intellectual property being stolen?

Mr. WRAY. I believe it was movies, and CDs, and that sort of thing. I can try to see if I can find the specifics on that.

Senator LEAHY. How many people went to prison?

Mr. WRAY. I believe that a significant number of those 26 have gotten prison sentences. I do not have the specifics for that.

Senator LEAHY. Do you have any idea of how long?

Mr. WRAY. As I mentioned before, the sentences we are seeing are going up more, so, increasingly, for example I think we got a 70-month sentence, which is more than historically we have been getting in those types of cases.

Another sig—

Senator LEAHY. If a bank robber stole $100 million, what would they get for a prison sentence?

Mr. WRAY. If it was armed, he would of course—

Senator LEAHY. No, just—

Mr. WRAY. Just a "note job" kind of thing? With $100-million loss, I would have to look at the sentencing guidelines for $100-million loss, but you would look at the loss table under the sentencing guidelines, and my guess is probably 7, 8, something like that, years.

Senator LEAHY. You have got a black kid in the inner city who sells a couple grams of crack cocaine to his classmate for $40, what do they get?

Mr. WRAY. I am sorry. How much cocaine? I did not—

Senator LEAHY. A couple grams. Five grams. Say five grams, and say they make a $40 profit on it overall between what they paid for it and what they sold it to one of their classmates at school, how long are they going to go to jail?

Mr. WRAY. In excess of 5 years.

Senator LEAHY. Well, you know, we probably have a lot of businesspeople who might say, well, look at those kids and see what we might do, but maybe the person who stole several million dollars' worth of counterfeit goods ought to go—but give me a couple more of your, you have given me one of the most significant prosecutions. You can give the 10 over the 3 years for the record, but give me a couple more.

Mr. WRAY. A couple more would be a case that we recently brought in Alabama involving counterfeit pesticide, in which the defendant sold the pesticide, passing it off as legitimate pesticide to deal with West Nile Virus. So, of course, you had all of these municipalities all over the Southern United States buying this stuff, thinking that they were going to protect their communities with it, and in fact it was not the real stuff. That defendant, I do not have his sentence off the top of my head, but that was another significant case.

Senator LEAHY. You see what I am leading to, and also overseas, if you can address that, because I mentioned my provision to put

$2.5 million to address IP piracy overseas, and I want to make sure that really is a priority of the FBI, which is under your Department.

Mr. WRAY. Our international focus has been primarily on working, forging partnerships with our law enforcement counterparts overseas. So, more and more, we are trying to engage in things like Operation Buccaneer. There is another one called "Operation Safehaven," where we are working with law enforcement partners in other countries to try to make it a coordinated take-down, where they take down some of the people there, we take down some of them here, searches are being executed all over the world. It is an effort to try to get at the entire organization and dismantle it, much the same way we would in situations that you are also familiar with, with drug organizations, major organized organizations, and other contexts, suck as terrorist organizations. The idea is to try to dismantle the organization.

And so working with our international partners on the law enforcement-to-law enforcement relationships, that is kind of where our focus is on that front.

Senator LEAHY. Thank you.

I will submit the other questions for the record, Mr. Chairman.

Senator SPECTER. Thank you very much, Senator Leahy.

Senator Biden?

STATMENT OF HON. JOSEPH R. BIDEN, JR., A U.S. SENATOR FROM THE STATE OF DELAWARE

Senator BIDEN. Thank you, Mr. Chairman, and thank you for holding this hearing.

The three of us, and others, have done an awful lot of work in this area. In speaking for myself, Senator Smith and I started a caucus of now 70 Members of the House and Senate to deal with this issue. The reason I bother to say that is not to say we have done this, it is to acknowledge that we know how difficult this is. This is a very difficult problem.

And some of the answers asked are of above your pay grades to be able to answer, we understand, because there are policy decisions that have to be made. But, Mr. Chairman, I would ask unanimous consent that my statement be placed in the record.

Senator SPECTER. Without objection.

[The prepared statement of Senator Biden appears as a submission for the record.]

Senator BIDEN. We have done this. We have held other hearings. We have written reports. We have made suggestions. But let me get to what I think is one of the core problems here.

In a sense, advances in technology have outrun our enforcement capabilities. It is awful hard to catch up, and I understand that. But if you are willing, and I am not being solicitous when I say this—and I understand if you do not want to take a chance and answer these questions—but what are the tradeoffs that you all have to make on the enforcement side? Let us talk about the Special Trade Representative, the State Department, the Commerce Department.

The truth of the matter is I introduced a bill last year that had a lot of support until I decided to try and make it more difficult,

and all of a sudden I found I had a split between software manufacturers and the industries, and it broke off.

The Chamber of Commerce does not know what they are talking about here, and the AFL–CIO does not know what they are talking about here either because they have real problems internally. There are great splits. The harder you come down on this, the more you are going to make my chemical manufacturers angry, the more you are going to make my—I see the head of the Chamber of Commerce. He cannot give you a straight answer, and I love him, and the reason he cannot is his constituency is split. And if he does not know it, he should come to Delaware, and I will explain to them why they are split.

Because if you enforce 301, then there is a backfire. You may very well deal with these guys. You may crack down, but all of a sudden he is going to have all of these guys on his doorstep from the Business Roundtable saying, "Whoa, whoa, whoa, wait a minute. You are talking about this intellectual property stuff. You have got everybody all ginned up. They went ahead, and they imposed sanctions, and now, guess what?" You guys know the rest of the story.

Tell me what the competing interests are. Not good guys/bad, what are the competing interests? The truth of the matter is we have not imposed 301 Sanctions to any degree that it hurt and anybody yelled, "Uncle." Why? There is a good reason. Tell me the reason why. I think there is a good reason. I am being serious. I am not trying to—but explain to the public, so I am not doing it because they do not believe Senators, but they will believe very impressive bureaucrats. And I mean that sincerely, you are an impressive bunch. I give you my word. I mean that sincerely.

What are the reasons, Mr. Mendenhall?

Mr. MENDENHALL. Well, I would like to say actually two things about that.

Senator BIDEN. Do not give me a State Department answer, okay?

[Laughter.]

Mr. MENDENHALL. I will turn to my colleague for that.

There are two things: One, at times the threat of 301 Sanctions has had some impact. It did with China in the mid-1990's.

Senator BIDEN. Well, it can have a lot of impact. Why do you not, in fact, use it?

Mr. MENDENHALL. Right. Well, the domestic reason, of course, is that imposing sanctions also has implications for our own folks. If we block—

Senator BIDEN. Explain that. What do you mean? Give me an example of implications.

Mr. MENDENHALL. If we impose sanctions on or raise tariffs or otherwise block imports, it does have repercussions through the economy for those who need to import their raw materials for production, those who otherwise purchase the goods, sell them in the United States, that type of thing. So there are political tradeoffs that have to be made.

Senator BIDEN. And by the way, I want to make clear, I am not saying they are Democrat-Republican political tradeoffs.

Mr. MENDENHALL. Right.

Senator BIDEN. But there are tradeoffs, there are economic tradeoffs, right?

Mr. MENDENHALL. Yes. There are tradeoffs, yes.

Senator BIDEN. Now, a second question is, I am going to make a statement, and if any one of you disagree with me, do not just disagree. Tell me why you disagree.

I would posit that the reason why we have not moved in the way we should move is, quite frankly, on the scale of economic interest, this is at the lower end of the scale. The tradeoffs that we have to pay for, for imposing sanctions that were legitimately able to be imposed, would exceed the benefit we perceive would come from getting international piracy significantly stunted in its growth.

The short-term and mid-term tradeoffs will be significant for the economy, right? Who are you going to hear from if, in fact, you go ahead and impose 301 Sanctions against China on this issue?

Mr. MENDENHALL. I do not think we can say categorically that the tradeoffs are such that it would necessarily be a bad thing, not result in the results that we want at the end of the day. I think, at this stage of the game, we should not take any options off the table, and we should consider—

Senator BIDEN. With all due respect, then, if they would not, then you are doing a very bad job. You are doing a very bad job. Unless you—Commerce, State and Special Trade Rep—cannot demonstrate that the economic impact to the United States, by imposing what we legitimately could impose on in terms of sanctions for piracy far exceed the cost of the piracy, then you are derelict and irresponsible—flat out, you are derelict and irresponsible.

It has cost us 750,000 jobs. Forget the money, 750,000 jobs. The Chamber and a lot of other people think outsourcing is not such a bad idea, and from an economic model, they may be right, but from the terms of the impact on the economy and people, it is devastating—750,000 jobs.

And let me explain to folks who are listening. It is a real simple reason. When we do not have someone in a factory making that little disk, when we do not have someone reproducing that movie, it is being reproduced overseas, so no one else reproduces it. They are manufacturing jobs, they are high-tech jobs, and we are losing them, and 750,000, according to our estimates, this administration's estimates from the U.S. Customs Service.

So I am supposed to sum up now. Folks, look, we have got to get honest with the American people. There is no question that we are not for using the tools available to us. There may be a good reason why we do not use them all, but let us explain to people. They are smart. They are smart. Tell the truth.

My time is up, and no one can believe I actually stopped within my time. So that is why there is this stunned silence here.

[Laughter.]

Senator SPECTER. Thank you very much, Senator Biden.

Senator BIDEN. Surprised, huh?

Senator SPECTER. Well, that is emphasis which we have come to expect from Senator Biden. He and I ride the train from Washington to Wilmington, where he gets off and I go on to Philadelphia. I have had more time today, equal time. Occasionally, I get

in a word with Senator Biden when we ride the train, but only occasionally. Senator Leahy concurs, I think. [Laughter.]

Well, thank you very much, gentlemen. We are glad to see the Treasury Department, and the Justice Department, and the Trade Representative, and the State Department going after this issue. This Committee is very deeply concerned about it, and we are ready, willing and able to help you further. We like the idea of tough prosecutions and the sanctions as a deterrent.

Speaking for myself, I believe there could be more done on sanctions dealing with China as an example. Secretary Snow was in China, as well as Secretary Evans. Senator Biden was in China as well, and from the reactions that I got when I was with Senator Biden, I have doubts as to the impact and would be looking for something tougher.

So thank you very much. We will continue to work together.

Senator BIDEN. Thanks, guys.

Senator SPECTER. We will now turn to our next panel: Mr. Thomas J. Donohue, Mr. Richard K. Willard, Mr. Brad Buckles, Ms. Vanessa Price, and Mr. Timothy Trainer.

While the panel is being assembled and seated, I will start with the introduction of our first witness, Mr. Thomas J. Donohue, President and CEO of the U.S. Chamber of Commerce, one of the strongest—perhaps the strongest—advocacy group representatives of American business in the country. He has held that position since 1997. For 8 years before, he was group vice president for the Chamber, and prior to that he had worked 13 years as president and CEO of the American Trucking Association, the national organization of that industry.

Mr. Donohue has had a very keen interest in this subject and recently held a long symposium in the Chamber on it, and we welcome him here today to continue the exploration of this important subject and to figure out what more can be done to deal with it.

Thank you for joining us, Mr. Donohue, and we look forward to your testimony.

STATEMENT OF THOMAS J. DONOHUE, PRESIDENT AND CHIEF EXECUTIVE OFFICER, U.S. CHAMBER OF COMMERCE

Mr. DONOHUE. Thank you, Mr. Chairman and Members of the Committee. I am glad Senator Biden is here. Maybe we can carry on with his discussion.

First, Mr. Chairman, let me thank you for participating in our program, where we kicked off the Chamber's massive long-term effort on intellectual property and counterfeiting issues here and around the world. Your interest, I would say accelerated interest after your participation in that event, has had a lot to do with bringing us here today, and we very much appreciate your efforts.

For the members of the panel, Senators, let me say that the Chamber's program has got three parts to it:

First, we are going to mass a large educational effort to explain to people what is at stake here, what is being lost and, by the way, how many of our fellow citizens are helping—inadvertently, perhaps—helping the counterfeiters.

Second, we are going to spend a good deal of time on cross-industry domestic coalition building to protect our supply chain. What

that means, we have got to bring the people together on these issues in a way that does the type of research, the top economic analysis and answers the very question that Senator Biden asked.

And, finally, we are launching a whole series of international issues to go where the problem is, some of it being overseas, some of it being here, and to create a tremendous amount of pressure, including, by the way, notwithstanding the Senator's point, a willingness on our part to play serious hardball. I am not sure, Mr. Chairman, that I would join your view of saying that we ought to get rid of our relationship with China, but I would suggest a number of ways in the discussion that we might use our relationship with China and the rules-based organization to light a fire under them. Action not talk.

But I do appreciate the opportunity to come up here and to say in very simple terms that the American people do not understand this problem. Some of our own family will go out and buy a knockoff watch or go out and buy a purse, and they do not think much about that, but you need to understand that this is, if we wanted to go into the criminal business together, this would be a great crime to get involved with because the sanctions and the costs are very light and the opportunities to make a ton of money are there, but folks have to understand this is a well-financed effort. These are groups of people, criminal in nature, large investment capabilities. Do you know what it costs to buy a truckload of disks to steal? You need a million dollars. So there is a lot of money in here.

And the other thing we have to educate our fellow citizens on, that this is a very sophisticated issue that is hurting us in pharmaceuticals, automobile parts, airplane parts, components for technology. This is a serious matter with many risks.

I have heard—and I am not going to repeat what some of the people said here—but we are talking about a three-quarter of a trillion dollar problem, and we are talking about, as Senator Biden indicated, a lot of lost jobs.

On the other hand, by the way, if the panel would allow it during the discussion, we are bringing far more jobs into this country, on in-sourcing and other ways to be discussed at another time, than we are losing on outsourcing. Outsourcing and in-sourcing we have discussed, but criminal activity that is costing us three-quarters of a million jobs, and it is taking three-quarters of a trillion dollars out of the taxpaying systems in our countries is a dumb idea.

What we need to do is—and I appreciate the point you made to the fellows and the representatives of the Government agencies—we have got to make this an expensive crime to get involved in. This is not a victimless-type crime. There are people being hurt on this all of the time. One of the major pharmaceutical companies had to recall all of their drugs on cholesterol because there were some phony drugs. So these are the kinds of issues that we need to get involved in.

Mr. Chairman, the time always runs very, very quickly on these clocks. I simply want to say that we are going to invest a lot of money, over a long period of time, to go out and dramatically increase the communication on this issue and understanding, to interrupt supply chains that we think are fraudulent and protect

supply chains that are not, and to push domestically and internationally to make this an expensive crime to get involved in.

May I end with just one sentence, sir? The Chamber of Commerce of the United States, we have gotten pretty good at forcing American business into a coalition of interests, and there are some times we do not, so on behalf of the whole business community, we are not going to listen to the complaints of some. I think we have demonstrated our willingness to lead on this deal, not follow.

Thank you very much.

[The prepared statement of Mr. Donohue appears as a submission for the record.]

Senator SPECTER. Thank you very much, Mr. Donohue.

We turn now to Mr. Richard Willard, senior vice president and general counsel of The Gillette Company, chairs the Product Counterfeiting Working Group of the National Association of Manufacturers. For 5 years, between 1983 and 1988, he served as assistant attorney general in the Department of Justice Civil Division.

Thank you for being with us today, Mr. Willard, and we look forward to your testimony.

STATEMENT OF RICHARD K. WILLARD, SENIOR VICE PRESIDENT AND SENIOR COUNSEL, THE GILLETTE COMPANY, BOSTON, MASSACHUSETTS

Mr. WILLARD. Thank you, Mr. Chairman and Members of the Committee. It is a pleasure for me to be here today to talk about this important issue to my company. I am also here on behalf of the Grocery Manufacturers of America, a trade association representing a lot of consumer product companies as well.

Our company, Gillette, we manufacture and market a broad range of products, not just the famous Gillette shaving products, but also Duracell batteries, Oral-B toothbrushes, and a number of other lines of products.

We also participate and work with the U.S. Chamber of Commerce and the International AntiCounterfeiting Coalition, both of which are represented here today as witnesses.

I would like to make my brief time for my spoken remarks to make a few quick points:

First of all, counterfeiting is not a problem limited to luxury goods. In fact, that is a tiny fraction of it. I have here in front of me two packages of what appear to be Duracell batteries. The one on the right I can tell you a lot about. I know where it was manufactured, I know what is in it, I know how long it will last. The one on my left is counterfeit. It was one of one million counterfeit batteries we seized in a single seizure in China, recently.

Senator BIDEN. One million.

Mr. WILLARD. One million at one time. Other than that, I cannot tell you much about it. I do not know what is in it. I suspect it will last maybe a tenth as long as the real Duracell battery, but that is about it.

The danger to consumers, of course, is that they can unknowingly buy counterfeit products that will underperform. More seriously, as testimony has already brought out, they can buy counterfeit products that are actually dangerous to their health and safety.

I would like to turn briefly to what I think this Committee should look into doing.

First of all, we need to close some loopholes in U.S. laws. We need to outlaw trafficking in counterfeit labels and packaging in the U.S. and overturn the recent decision of the Tenth Circuit in the Giles case, which said it was not a crime to traffic in counterfeit labels unless they were actually attached to a counterfeit product. That is a loophole that the counterfeiters know how to exploit here and in China in our experience, where they simply bifurcate the counterfeiting process, and thus insulate the manufacturing and the more expensive equipment from any liability because it only becomes a counterfeit when the label is put on it.

We also need to make, under our U.S law, mandatory the seizure and destruction of machinery used to make counterfeit products and labels.

If we can make these changes in U.S. domestic law, then we can leverage that through Free Trade Agreements to make other countries make these changes in their law. USTR understandably takes the position it will not negotiate requirements in FTAs that would require a change in domestic U.S. law, and so we cannot get other countries to make these changes in their laws unless we first make them in our own laws if we want to impose that requirement under Free Trade Agreements.

And then, finally, my last suggestion is that our Government needs to be explicit in its pressure on China, not just to say we want you to do something, but to tell them what to do. And the one thing they could do that would make a big difference is to implement an enforcement program at the point of export. They should be examining cargos, as they are shipped out of China, to discover counterfeit goods and, at that point, to seize the goods, destroy them and prosecute the people who are exporting the goods. There is no such enforcement program in existence now.

And so it is really not such a matter of just telling China we want you to do something, it is a matter of telling them what to do and giving them the assistance, law enforcement training and other resources to help them do the job effectively.

We have been doing business in China for a number of years. It is a very valuable market for our company, and we do not want to antagonize the Chinese Government. What we ought to do is help them develop an effective enforcement policy, and I believe the top leadership in China recognizes that counterfeiting is bad for their country as well as for others. What they do not have is the competence to implement an effective enforcement program, and I think we can help them develop that.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Willard appears as a submission for the record.]

Senator SPECTER. Thank you very much, Mr. Willard.

Our next witness is Mr. Brad Buckles, executive vice president for Antipiracy at the Recording Industry Association of America. He formerly worked as Director of the Bureau of Alcohol, Tobacco, Firearms and Explosives.

We thank you for being here today, Mr. Buckles, and the floor is yours.

STATEMENT OF BRAD BUCKLES, EXECUTIVE VICE PRESIDENT FOR ANTIPIRACY, RECORDING INDUSTRY ASSOCIATION OF AMERICA, WASHINGTON, D.C.

Mr. BUCKLES. Thank you, Mr. Chairman, Senator Leahy, Senator Biden, for holding this hearing on the devastating effects of counterfeiting and theft of tangible intellectual property.

The Recording Industry Association of America is a trade association that represents the U.S. recording industry, and our members create, manufacture and distribute approximately 90 percent of all of the legitimate sound recordings sold in the United States. One of the primary missions of our trade association is to protect the intellectual property of our members from theft.

Intellectual property is our country's number one export and comprises more than 5 percent of the U.S. gross domestic product over the last few years. And our creative and artistic genius in America is what fuels the intellectual property industries, and it is one of our most precious commodities. Yet everyday in our country intellectual property is stolen here in the United States and around the world through the sale of pirate and counterfeit copies of music, movies and software. We cannot permit criminals to openly steal this country's greatest assets.

Piracy is not a private offense against those businesses that produce intellectual property. In the case of the industry I represent, piracy and counterfeiting hurts everyone, those who make music and those who love it, in diminishing the incentive for others to invest in the creation of that music. Moreover, like other underground businesses, pirate sales also deprive Governments of tax revenues. Intellectual property pirates do not invest in recorded music, they steal it. They do not pay taxes. Like drug dealers, they launder their proceeds to hide their profits.

The counterfeiting of music is almost as old as the recording industry itself, but with the advent of the compact disk, the nature of piracy was radically altered by providing a pirate producer with the opportunity to produce near-perfect qualities of a recording. There is now massive manufacturing and international trafficking in illegal CDs and DVDs. The recent proliferation of inexpensive, recordable optic disks—or CD–Rs—combined with readily available CD burning capability has only served to compound the problem.

Our partners in the International Federation of Phonographic Industries—the IFPI—report that worldwide music pirate sales approach 2 billion units annually, with an estimated value of $4- to $5 billion. Globally, the IFPI estimates that two in five recordings are pirate or counterfeit copies.

This new manufacturing capacity clearly exceeds the amount of legitimate demand and creates a business environment right for exploitation by criminals. The physical production of a pirate CD costs as little as 35 cents. Given that the pirate producer has none of the overhead associated with the creating of the intellectual content on the disk, the profit margin is enormous.

To address this problem, the music industry, the IFPI, the RIAA, and other industry associations around the world have established Antipiracy Units to work with law enforcement agencies to combat music theft. The IFPI's unit specifically targets organized criminals who operate in transnational piracy schemes. They have found evi-

dence of organized criminal involvement that is incontrovertible and examples are given in my written testimony.

In the U.S., we have also seen that as music piracy has become more lucrative, the organizations that produce, distribute and sell counterfeit and pirate music have become more complex and more sophisticated. The most extreme form of organized crime affecting our society is terrorism, and the clandestine nature of terrorist organizations requires large sums of money to maintain their operation, and the high profit margins on intellectual property have been particularly attractive.

Law enforcement officials have called for more careful attention to this problem. Taking a leadership role, Interpol General Secretary Ron Noble has pledged the full support of Interpol in addressing what he describes as the intensive involvement of organized crime and terrorist groups in intellectual property crimes.

The music industry is committed to confronting the organized groups that now threaten the very survival of our business, and no other business invests so much energy or capital, and no industry has such a wide range of professionals and investigative resources dedicated to this problem around the world.

I look forward to working with the Committee on these important issues, and thank you again for your attention to these matters.

[The prepared statement of Mr. Buckles appears as a submission for the record.]

Senator SPECTER. Thank you, Mr. Buckles.

Our next witness is Ms. Vanessa Price, intellectual property specialist of Burton Snowboards Corporation, based on Vermont.

Thank you for making the trip down, Ms. Price. I had occasion to be in Burlington recently. Our younger son is a second-year medical student. Senator Leahy is a Vermonter. I commented to him that I thought the 5-degree-below-zero weather was brisk and refreshing, and came back to Philadelphia, where it was 24 and a heat wave. So it must be nice for you to be down South today.

The floor is yours, Ms. Price.

Senator LEAHY. Senator Specter did not mention that he was there in May.

[Laughter.]

STATEMENT OF VANESSA PRICE, INTELLECTUAL PROPERTY SPECIALIST, BURTON SNOWBOARDS, BURLINGTON, VERMONT

Ms. PRICE. It is a pleasure to come down here today. It feels like summer compared to what we have had in Vermont.

Thank you, Mr. Chairman, Senator Leahy, for inviting me to come down and speak today.

Despite vigorous measures to protect our intellectual property through trademark and patent registrations, Burton has seen significant counterfeiting recently, and we expect that counterfeiting will increase dramatically as our brand continues to grow. As a smaller company, Burton is deeply concerned about the rise in theft of our IP since we do not have the resources that it takes to combat or offset the effects of large-scale counterfeiting.

I would like to also tell you a little bit about Burton. The Burton name has become synonymous with snowboarding. We were found-

ed in 1977, and we are a Vermont-based company that employs 350 people in Vermont and 160 people at offices in Japan and Austria. The board sports industry credits Burton Snowboards with the founding and popularization of snowboarding as a legitimate sport. Snowboarding is growing rapidly worldwide. Snow Sports Industries of America, our trade group, estimates that participation in snowboarding has increased 300 percent since 1998.

Burton has seized this opportunity to grow its brand and has expanded to include Gravis Footwear, Analog casual apparel, Anon Optics, and R.E.D. Protective Gear. However, this growth in popularity is not without a significant downside. Our industry has gone through considerable consolidation in recent years. Most of the snowboarding manufacturers are seasoned competitors at this point. Competition is keen and profits are shrinking, even as the sport grows in popularity.

Unfair competition from counterfeiters significantly compounds the problems of seasonality and severe sensitivity to economic downturns that our industry already faces. Virtually none of the companies that manufacture ski and snowboard equipment are large enough to have the resources or tools necessary to fight counterfeiting, leaving a growing portion of what should be domestic revenue going to foreign counterfeiters. We could not even guesstimate the amount of tax revenue that the U.S. Treasury loses to these unrealized gains.

Burton has taken all available and appropriate steps to register our trademarks both in the U.S. and internationally. Currently, we maintain more than 60 trademark registrations in the U.S. alone. We have also taken the additional steps of registering our trademarks with Customs officials in the U.S., Chile, Argentina, Brazil, Hong Kong, China, as well as several other countries. Unfortunately, filing with Customs has offered us very scant protection. Burton also holds patents worldwide relating to our snowboard technology, including boots, bindings, snowdecks, and snowboards. So we have really availed ourselves of all possible protection. However, despite the measures that we have taken, we see growing evidence that our brand is suffering from counterfeiting and illegitimate sales.

Burton has noticed growing problems with small-scale counterfeiting in the U.S. Typically, this involves the manufacture and sale of fake stickers, accessories and clothing on Internet auction sites, specifically eBay. We can find these goods almost any day of the week continuously. All the time, if you check eBay, you can find Burton. eBay affords us the opportunity to get these auctions taken off of their site, but again, after they are off the site, we really do not know where the goods go. We do not know who is making them. We have no way of really going after them, small scale or large scale. This might not appear to be a big problem for us, but we manufacture limited editions of certain things, and when they show up on eBay in a large quantity, it just causes our brand to lose commercial appeal really.

Burton right now is in the process of expanding from one-season business, moving beyond snowboarding into the apparel business, expanding our sales of T-shirts, fleeces, sweatshirts and accessories. As this aspect of our business grows, we see significant

counterfeiting. Relative to our boards, bindings, our engineering technology, these items are easier to counterfeit and sell worldwide. Typically, we see them showing up in markets in Asia, China, Taiwan, et cetera. We see them all over the place.

This is not unique to Burton. This is a problem that is pervasive in the board sports industry.

My time is up, but that is mostly it.

Thank you.

[The prepared statement of Ms. Price appears as a submission for the record.]

Senator SPECTER. Thank you very much, Ms. Price.

Our final witness on the panel is Mr. Timothy Trainer, president of the International AntiCounterfeiting Coalition, a group which concentrates on protection of industry from counterfeiting and piracy. Mr. Trainer has been an order with Arder & Hadden and worked at the U.S. Patent and Trademark Office.

We look forward to your testimony, Mr. Trainer.

STATEMENT OF TIMOTHY P. TRAINER, PRESIDENT, INTERNATIONAL ANTICOUNTERFEITING COALITION, INC., WASHINGTON, D.C.

Mr. TRAINER. Thank you, Mr. Chairman and Senator Leahy. On behalf of the IACC and its members, I thank the Committee for the opportunity to address the issue of product counterfeiting and piracy that generates revenues for criminals and impacts our National economic security, consumer safety and economic health of the companies that develop, make and distribute products that incorporate intellectual property assets. Our members represent a cross-section of industries from autos and medicines to toys and entertainment.

Due to time constraints, I will summarize my full written submission.

The IACC, respectfully, requests that the Committee and Congress consider implementing the following package of recommendations to combat counterfeiting and piracy:

Strengthen the Federal criminal statute against trafficking in counterfeit goods;

Encourage Federal law enforcement agencies to increase investigations and prosecutions of manufacturers, distributors and others involved in the trafficking of counterfeit goods;

Increase vigilance at the U.S. border regardless of the products involved;

Impose higher IP enforcement standards on trading partners;

And support Interpol's effort to combat international trafficking in counterfeit goods.

The last three IACC Special 301 submissions to the U.S. Trade Representative have identified nearly 40 countries that have woefully inadequate and ineffective systems against product counterfeiting and piracy. The products targeted by counterfeiters in the global market are, at times, shocking because of the reckless disregard counterfeiters have for consumers in their effort to profit off of famous trademark goods.

There are no industries exempt from counterfeiting and no country spared. Although consumers may generally be aware of the

counterfeit watches, handbags, shirts, hats and sunglasses offered at flea markets and on big city streets, they are not well aware of the fact that the global counterfeiting industry has moved into pharmaceuticals, auto parts, toys, batteries, extension cords, cosmetics, beverages, body lotions, home electrical appliances, tools, pesticides and vision wear.

This sample list underscores the products that are now counterfeited here and around the world. Highlighting a few examples, one auto industry member found 7,000 sets of counterfeit brake pads in China intended for export to Egypt. Another auto industry member reported raids resulting in the seizure of thousands of counterfeit windshields and several thousand suspension control arms valued at nearly $4 million.

Another member, whose certification mark is relied upon as a mark of safety, reported that U.S. Customs seized 91 shipments of counterfeits bearing its mark in fiscal year 2003. These seizures included air compressors valued at $1.5 million that had counterfeit ground fault circuit interrupters, a $700,000 seizure of counterfeit extension cords, power strips and hair trimmers that, in turn, led to an additional $7-million seizure of counterfeit extension cords and power strips, and there are examples here on the table. In addition to the Customs seizures, another million-dollar seizure of Chinese-made counterfeit portable and hand tools was made by police in Southern California.

In Australia, an investigation led to the discovery of massive counterfeit operations of Chinese-made counterfeit batteries and razors. Three containers heading to different ports—Dubai, Oman, and Los Angeles—were seized having counterfeit goods valued at $1.5 million. Australian authorities also seized two shipments of counterfeit shampoo from China bearing the trademark of a famous brand.

In 2003, counterfeit vodka in the U.K. caused hospitalization and induced coma for consumers who unknowingly purchased the counterfeit vodka containing dangerous levels of methanol.

Turning to counterfeit batteries for a moment, a boy playing with a toy that had a counterfeit battery suffered facial injuries from an exploding battery, and a man suffered injuries to a hand when his remote control exploded from the use of a counterfeit battery, both incidents in Malaysia. Nokia found that counterfeit batteries used in connection with their cell phones were exploding as reports of such incidents were widespread—from Vietnam to the Netherlands.

Russia's chief trade inspector noted that for certain categories of consumer items, 30 to 50 percent of the market consists of counterfeits. These product lines include alcohol, juices, butter, vegetable oil, canned foods, tea, coffee and cosmetics.

Domestically, in addition to the auto parts, substandard and counterfeit heavy-duty truck replacement parts are also getting into the U.S. aftermarket in significant numbers, and the problem is likely to get worse, according to the industry.

In the power tool industry, counterfeits pose risks due to the substandard parts and their failure to stand up to the type of use that genuine-tested products can withstand. In one case involving civil and criminal judicial proceedings, the focus was on theft of trade

secrets and the sale of counterfeit fiber optics products and lighting.

Product counterfeiting affects all industries and all countries. The volume of seized goods is a clear indication of large-scale manufacturing and a sophisticated distribution sales network. Thus, the challenge of global counterfeiting is one that must be fought with the cooperation of our trading partners and relevant intergovernmental organizations. The recommendations that we have proposed are only a few of the many things that need to be done.

In conclusion, we cannot treat any type of counterfeiting as a victimless crime or we risk attracting criminal elements to this type of "easy money" activity. The present situation begs the question: Where does the money go? We have yet to learn exactly where the money goes, but do we dare to take the risk that some of the funds land in the hands or accounts of individuals or groups that will do the unthinkable?

A multi-pronged effort is needed to take more aggressive enforcement actions, implement a broad strategic plan to target sources, educate consumers and train Government officials and business leaders in ways to make IP enforcement more effective.

Thank you very much, and I am happy to answer any questions you may have.

[The prepared statement of Mr. Trainer appears as a submission for the record.]

Senator SPECTER. Thank you, Mr. Trainer.

Without objection, Chairman Hatch's statement will be made a part of the record.

Mr. Donohue, when you say you would not want to end our relationship with China, I certainly think that is a correct—I think we could not end our relationship with China if we wanted to. They are the oncoming superpower. And we talk about China because they seem to threaten us the most. They were trying to influence our 1996 presidential election. They take a librarian from Dickinson College and do not relent until there is pressure in a Sense of the Senate Resolution. And we try to structure what we think are civilized, but tough, sanctions. What would you suggest as to how we deal with China?

Mr. DONOHUE. Well, China has 1.3 billion people. We have a lot of companies—and by the way the Congress would encourage this—that would like over time to be able to sell those people things.

We compete with the EU, whose economy is probably going to be 20-percent greater than ours after their enlargement, and so our work with the Chinese have to be twofold, one is engagement, and inducement and correction, and the other is economic advance for both countries and the positive benefit of keeping China in a rules-based system, and we ought to use that rules-based system.

We also must understand that the central Government in China is making a lot of progress on this. The provinces run by very strong Governments are a little more liberal, as you know. But as you know, Senator, from your participation in our program, we intend to let the American people and everybody around the world know what is being talked about here, what the cost is, what it is doing to our country.

We intend to interdict the supply chain and the logistics chain with a lot of action to make it more difficult for them to do what they want to do, and that requires the help of our Government. But we very much intend to put a lot of pressure on China—not only China—China, Russia, Brazil, Korea, India to play by the rules.

And you raised a lot of issues with the first panel, and I do not know why anybody would get excited about all of the things we talk about in terms of intellectual property and counterfeiting theft because nobody goes to jail. I mean, there are a few good examples here, and domestically that is a lot easier, but my view is, if you make enough noise, if you put enough pressure on our own Government and on Governments overseas, if you put enough pressure on American business that it is going to become more difficult, more expensive, more embarrassing, and much less attractive to have anything to do with this counterfeiting issue.

Senator Biden was kind enough to come down and say a word before he left. As you know, the Chamber works very hard to have a consensus within our members, but there are no group of members that are going to get us off this issue. We have made a 5-year, very significant commitment to go out there and ring this bell until people hear it.

And my issue, in dealing with the Chinese, is constructive engagement and very, very tough enforcement. Do not ask me if I want to do a 301 because that has all kinds of other implications. There are lots of ways to ring their bell in the domestic and in the international market, and we are prepared to do it.

Senator SPECTER. Well, when you talk about enforcement, both Mr. Willard and Mr. Buckles have talked about Interpol. Mr. Willard, when you have asked that the loopholes be tightened, our staffs will be in touch with your office to get the specifics. That is something that, speaking for myself—and I believe I would have co-sponsors—we would be glad to do.

But when you talk about, as you articulated it, inspect, seize, destroy and prosecute, that is a pretty good quartet. How about it, Mr. Willard, Mr. Buckles, both of you, might Interpol be used? They are investigative, and fact-finding and pooling agencies, but what would you think of some effort at international prosecution? Too ambitious, Mr. Buckles? ATF would probably like to do that.

Mr. BUCKLES. Right. Well, we are making some significant inroads to prosecutions around the world, working with representatives of Interpol.

Senator SPECTER. But will China prosecute?

Mr. BUCKLES. Well, we have in selective locations. We were successful in Hong Kong, for example, in having laws changed in Hong Kong that resulted in a change of—

Senator SPECTER. A pretty sophisticated part of China. How about the rest of China?

Mr. BUCKLES. Well, there are still problems in the rest of China, there is not any question.

Senator SPECTER. Mr. Willard, how about it, could we use Interpol to take an aggressive lead there?

Mr. WILLARD. Well, Senator, I think that the most promising avenue would be to get the Chinese Government itself, perhaps in cooperation with the United States, to implement an enforcement

program at the point of export. That is kind of a choke point, and there is no enforcement there now.

We do get a fair amount of enforcement inside China. Every week that goes by, our company conducts raids on factories that are making counterfeit products. We do get seizures. We get prosecutions. We have even had people sentenced to prison in China for counterfeiting our products.

What the Chinese Government does not do is conduct a program of surveillance at the point of export. So, if they had agents on the docks in Shanghai and other key ports who would go through cargos before they leave the country and seize the counterfeit products, we think that would make a big dent in the problem, and that is something that is not happening at all right now. I do not think that requires Interpol; it just requires a commitment—a financial commitment—as well as expertise on the part of the Chinese Government.

Senator SPECTER. Ms. Price, you have outlined what you have done to try to investigate infringements on your property, have you taken those facts to prosecutors and gotten any results?

Ms. PRICE. No, we have not. We have not taken those facts to prosecutors, not in terms of—

Senator SPECTER. You might do that. You have articulated quite a long list of investigative actions you have undertaken.

Ms. PRICE. On our counterfeiting side, we have not taken very much to prosecution. However, on our patent infringement side, we have had substantial litigation in terms of—

Senator SPECTER. Thank you.

Mr. Trainer, I think I have time to ask a question before my red light goes on.

How about the Patent Office, could we deny entrepreneurs from other countries access to our Patent Office as a sanction to make them enforce and respect our property rights?

Mr. TRAINER. Well, I think there may be a problem just because people who are applying for a patent, if they fit within the framework of the legal requirements to obtain a patent, we would need to have some other mechanism as a penalty with our trading partners.

So, under the current scheme, we probably could not without additional legislation.

Senator SPECTER. We could change the law.

[Laughter.]

Senator SPECTER. We have been joined by our distinguished Chairman, Senator Hatch.

First, Senator Hatch, I think there is an interest in knowing how your back is. And with an operation last week, how could he be on the bench here so early?

Senator LEAHY. I do not know why you are not back home resting.

Chairman HATCH. Well, I have been trying to rest, but it is tough to get over two back operations in 6 months. So I am a little bit behind the curve right now. But do you mind if I ask just one question?

Senator SPECTER. No, take all of the time you want.

Chairman HATCH. First of all, I want to thank the distinguished Senator from Pennsylvania and my friend from Vermont for holding this hearing. It is a very, very important hearing, as you all know. These are some of the most interesting aspects to me as well. So I am grateful to all of you for being here and to the prior panel for being here as well.

Let me just ask you a question, Mr. Willard, because it is a question that I am very concerned about, and that is the health and safety implications of various product counterfeiting. The health and safety ramifications are very profound, and yet most of the information that is presented seems anecdotal, at least to me.

Now, are there efforts being made to quantify the impact of product counterfeiting on health and safety, to the best of your knowledge, or anybody else on the panel who would are to answer that as well.

Mr. WILLARD. As I understand it, Members of Congress tried to get the Department of Commerce to do a more rigorous study of this problem a couple of years ago, and they have failed to set aside the money to do so. And you are right, most of the evidence we have is anecdotal or involves numbers that are based on estimates rather than rigorous statistically valid market sampling and analysis, That is expensive to do, but we certainly think it would be appropriate for Congress to designate money and try to get that kind of study done by the Commerce Department or some other appropriate agency.

Chairman HATCH. I think we ought to try and work on that because that is important.

Does anybody else care to comment?

Mr. DONOHUE. Well, Senator, you know when you see the smoke, we might have a new pope, and when you find brake pads made out of sawdust, when you find one of the major pharmaceutical companies in this country having to call back their cholesterol drugs, when you find airplane parts that have been made in ways that will not stand the tension and the wear and tear, when you find, as Mr. Willard talked about, batteries that blow up, I mean, wow, that is anecdotal. If you find one, you can believe there are 10 or 100 or 1,000 or 10,000.

What we are going to try and do is to get people to understand that this is going on, where it is going on and what it is costing people, physically, economically and personally. I think what we need to do is follow the anecdotes, and that is what we are going to try and do.

One of the things Senator Specter mentioned about using Interpol and others, you know, I ask one question. I visit all around the world, and people, you know, the leaders of countries say, "Now, we are working on this, Mr. Donohue."

I say, "Good. Let me just ask you what court in your country do I take my complaint to?"

Well, when they do not have one or when the one that they have is not as open as you might find in Hong Kong, then you have to ask the second question, "Okay. I accept that, but to what power do we go to try and get some pressure put on this issue?"

Anyway, I appreciate the question, and what we are going to do is try and find out some more of the answer.

Chairman HATCH. I want to thank my friend from Vermont, again, for allowing me to interrupt him. I had not thought about that, and I apologize to you.

Could I ask just one more question of Mr. Donohue?

Opponents of intellectual property protection have begun arguing in the international arena that strong intellectual property protections will impose American capitalism and American culture upon other Nations. Now, I find such arguments disingenuous at best. I believe that Nations who respect intellectual property rights will expand their domestic economies, tax bases, industries and native cultural institutions far beyond, and far more effectively, than if they allow untaxable black markets, if you will, in pirated goods—American goods, in particular—to flourish.

Now, can the Chamber help to coordinate, with our intellectual property owners, to make sure that our Government policy owners or policymakers are apprised of the "success stories" of other Governments that have expanded their own economies, fought corruption, and built their own domestic industries by cracking down on intellectual property theft?

That might be an area where—

Mr. DONOHUE. Thank you, Senator. Before you came in, I thanked Senator Specter for coming down to the kickoff of our major, long-term effort on addressing these issues. And part of what we are attempting to do is to join with other countries and to highlight, to intercept and to make very, very difficult a culture that allows and condones this type of behavior. And, by the way, there are Nations, some of which have been mentioned here and others who have not, where it is a cultural issue. I mean, it is entrepreneurial. We saw how they made it down the street, so we will come over here, we will make it, and we can—and some of them, by the way, one of the problems with some of the counterfeiting, it is damn good, but everybody is being cut out of the system. And I want to assure you—

Senator LEAHY. It is, also, if I might, it is very, very good because they have not had to do any of the development work—

Mr. DONOHUE. Absolutely.

Senator LEAHY. —do any of the other things—

Mr. DONOHUE. They do not have any of the liability coverage, but when I say it is "good," I know in one instance they had to bring the people from Microsoft all the way from Washington to tell which one was which.

But, Senator, I want to assure you that one of the things we are going to do is push that, and, quite frankly, I do not care what your culture is. If you are stealing American products, and American technology, and American profits, and American taxes, then you have got a problem. Good luck.

Chairman HATCH. I agree with you. I think the Chamber can help us in this regard, and of course we want to do everything we possibly can. I have been all over the world and encouraged people to not steal intellectual property, and in particular the Chinese, just to mention one country, in particular, and I have had mixed results.

I have had everyone say they will, but mixed results with regard to follow-through.

Mr. DONOHUE. Well, we will try and make the noise as loud as we can to see if we can get a little more response, and we will look for your help.

Chairman HATCH. Thank you.

Mr. DONOHUE. Of course, Senator Specter is raring to go, and I am sure Senator Leahy is as well. There are some things you can do to help here, and I think we need to start at home. We need to go after, as our friends from the music industry and others indicated, we can send a very loud message by doing the domestic thing right. There have been a few people who have gone to jail, but this is a slap on a wrist and a civil fine, usually. We need to get this real ugly. And then when we can demonstrate what we are doing at home, it is going to be a lot easier for us to be tough abroad.

Chairman HATCH. Well, thank you.

I thank my colleagues.

Senator SPECTER. Senator Leahy?

Senator LEAHY. Thank you, too, Chairman Hatch. It is good to see you back. We have all been worried about you, but Senator Specter assured us all here earlier that you are up and about. You are tougher than the rest of us. And I will explain later to you about Mr. Donohue's white smoke and the pope. I am the one expert on this panel.

[Laughter.]

Mr. DONOHUE. It is the same way they do it in Utah.

Chairman HATCH. Yes, I am fully aware.

Senator LEAHY. I will fill you in more.

I did want to say that when Pope John Paul was installed, shortly after his installation, President Carter—I was down at the White House—and he was saying he had sent every Italian American in the Congress over for that.

I said, "Wait a minute. What about me? You did not send me," realizing my mother was first-generation Italian American.

He got very apologetic, and he said, "Do not worry. Next pope you go."

I said, "Great. They are usually there for 20, 30 years." Unfortunately, in that case, 3 weeks later there was another pope, and he kept his word.

Mr. Donohue, I do not want to go into too much of this, but you made a very good point earlier. You said there are a lot of things we can do. I mean, you cannot just take automatic unilateral action against China, using that as an example, and I agree with you. I have been over to China many times in the negotiations on everything from arms control to economic matters. It becomes a long and careful dance.

But you also said the Chamber is willing to take some very tough steps. I wish you might answer, for the record, to the extent you can, what some of those steps might be. I would be very interested in hearing from you or to me privately, if you would prefer.

Mr. DONOHUE. Well, I will make some public comments, and then perhaps we might have a chat one time about some other things we would like to do.

First of all, as I said, I think if we start at home with people that are counterfeiting and bringing counterfeit goods into the country, knowingly, I think we send a very loud message.

Second, I think the gentlemen that were on the first panel have to continue to be encouraged to use the tools of Government, which we will encourage them to do, in a thoughtful and a unified way to send a loud message around the world. And one of the ways you do that is by making examples of people that you can catch and prosecute, highlight, and you know—

Senator LEAHY. I agree with all of those things, and I have stated all of those myself, but I want to know some specific actions that we can take if we still face basically a stonewall in a lot of the Chinese counterfeiting, which still is a very, very significant part of what we face.

I am going to have to ask—only because I want to go to some of the others—I am going to have to ask you to answer that—

Mr. DONOHUE. I will answer it in one sentence.

Senator LEAHY. Go ahead.

Mr. DONOHUE. I would like to use all of the persuasive and pressure tactics we could before we go to 301, but this thing is getting so big, it is going up about a quarter of a billion dollars every year, if we do not put some stop on this, we are going to be talking about some very draconian action.

Senator LEAHY. Would that include 301, eventually, if nothing else works?

Mr. DONOHUE. If nothing else works, we are not going to have a choice. This is going to be more expensive than the issue we debate all the time, which is on the cost of the Nation's legal system.

Senator LEAHY. Thank you.

Now, Mr. Buckles, you have had 30 years of public service, and I commend you for it, at the Bureau of Alcohol, Tobacco and Firearms. I am going to give you some questions, which I will submit to you for the record, regarding the resources that we have here. And I would be interested in getting your responses back. They will be part of the record, but I am particularly interested in that.

Mr. Willard, just before we started—we did not have time to really go much into it—I talked about a speech I gave at Georgetown this morning, Georgetown Law School, about radio frequency identification, RFIDs. That is these tiny, tiny computer chips—I mean, they are tiny. They are smaller than the end of that pen—they can store information, and they respond to radio signals. We can use them in identifying, tracking and authenticating goods.

Gillette has actually used them in marketing at WalMart, where if somebody picks up an item that has got one of those, it triggers a camera that goes to a person that is usually watching at a place 700 or 800 miles away.

Could this be something that could also be used in piracy? I mean, the more of these you use, and you are getting them down to the price of 2 or 3 cents apiece. Is this something that could be used in piracy?

Mr. WILLARD. It certainly could, Senator. That is something we have identified as one of the strategic benefits of the RFID chip when it is used on consumer products.

Just to make it clear what our company's approach is in this area, is initially to use it at the case and pallet level in the supply chain between the manufacturer and the stores for inventory management and that sort of thing. Before it is implemented on a wide-scale basis at the consumer level, we are strongly committed to making sure consumer privacy is protected in the way it is done. But this could help to overcome the problem that we have heard about, which is that counterfeiters are getting so good it is hard to recognize what is real and what is fake. These chips could do that for you and greatly enhance enforcement capability.

Senator LEAHY. I am thinking of things that Mr. Trainer talked about, some of the problems with brake pads, things like that. When I am going to pay for what I think is, if I am buying a brake pad for my car, I am going to pay for something which I assume the manufacturer recommends. It is high quality. If I hit those brakes, I want it to stop.

I would think, Mr. Trainer, that sometimes mechanics might have difficulty, following what Mr. Willard has said, is this fake or is this real; is that not true?

Mr. TRAINER. Well, I think with the kind of technology you are talking about, the question really becomes can a counterfeiter still make these types of products and somehow get it into some type of a retail outlet so that he bypasses the authorized distribution channels?

Of course, that is always going to be possible. So it really becomes this issue of companies, and their suppliers and manufacturers really pressing their distribution channels so that people are actually looking and being forced really to buy authentic merchandise.

Senator LEAHY. Ms. Price, in your testimony, I remember one time getting on a plane, I believe it was in Chicago, and Jake Burton was getting on there, and he was showing me a new ski boot for snowboarding. It is somewhat different gear than they are from skiing. He spent a lot of time and a lot of effort to design it and make it the best, and the safest and so forth.

He and I were sitting back in coach. He said, "You see that guy that just got up in First Class? He is one of the ones that goes to China and rips off, just copies mine. He does not have to pay any development. He does not have to do any of the work. He does not have to do any of the trial and error. He can afford to fly First Class. I am the one that is actually creating the jobs here in America. I am the one doing all of the work." He said, "Pat, I am glad to see we are back here together."

Let me show you one thing. This, I am told—I just happen to have this knockoff of one of your jackets. If that is in a store, look at it as you walk in, that would look like one of yours, would it not?

Ms. PRICE. It would look like one of ours. Just because I work for the company, I know it is not. But if I was a consumer, either that fleece or I have several others, and many more in my office, these are not actual Burton fleeces, not designs we use, but they have been made, and made very well, and our name has been put on them. So it is very confusing.

Senator LEAHY. But you had to bring—I mean, I have been in the factory. I see your designers go in there, and they might spend

a couple days trying one design. No, it does not look right. Try another design. It does not look right. They bring people in, and they test, and they throw things away. They finally get something that really works, they spent a lot of time doing it.

Ms. PRICE. Oh, yes, absolutely.

Senator LEAHY. My youngest son snowboards. We also go paragliding together. Mr. Donohue, see there is hope that you may end up getting a Republican seat in Vermont after all if I keep doing this, and sky diving and things like that with him.

[Laughter.]

Senator LEAHY. But he likes the Burton things, and this is not a paid ad for you, but he just happens to like it, and he looks for that brand, partly for safety, but he assumes, when he picks it up, that is what he is getting.

I had a couple of other questions that you actually answered before, so I am not going to ask more. But I just want to say thank you for coming down. But I would also point out—and this goes to what Senator Specter quite appropriately asked—you are a very small company. Gillette is a very large company and will have a significant Legal Department to go after counterfeiters. It does not mean you are going to get them all or anything else. But I suspect that their Legal Department is probably bigger than the whole headquarters of Burton. And it is not just Burton, but there are a whole lot of other people that make something unique. They may be a cottage industry, but their uniqueness becomes cachet in that industry, and they are hard-pressed.

I would assume, to the extent that you can get some of these Government agencies that talked before to help you in going after counterfeiters, you are a lot better off; is that correct?

Ms. PRICE. Absolutely.

Senator LEAHY. And I am not suggesting, Mr. Willard, that your company should not either. They should be helping all of you.

Thank you very much. I thank all of you.

Senator SPECTER. Thank you very much, Mr. Donohue, Mr. Willard, Mr. Buckles, Ms. Price, and Mr. Trainer.

I think that the exploration of the two panels has been very informative, and we intend to follow up in a number of particulars. I will be introducing the legislation that Mr. Willard looks at the loopholes, as he has articulated them. We will keep a relationship with China, but we may have to go to 301, maybe not to revoke Most Favored Nation status, but they will hear about the hearing today. They monitor our proceedings very, very closely. When we put in a little resolution about our—

Senator LEAHY. You may have a call from the Chinese Ambassador by the time you get back to your office.

Mr. DONOHUE. I hear from him all of the time.

[Laughter.]

Senator SPECTER. When we put in a little resolution about the Dickinson librarian, I got a call from the Chinese Ambassador to the United States, and we got him out. A little appropriate pressure goes a long way.

Without objection, we will put in the statement by Senator Cornyn, and that concludes the hearing.

Thank you all very much.

[Whereupon, at 4:42 p.m., the Committee was adjourned.]
[Questions and answers and submissions for the record follow.]

QUESTIONS AND ANSWERS

Senator Leahy
Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions
March 23, 2004
Additional Questions

Mr. Brad Buckles

1. Do you believe the problem of tangible piracy is the result of too few resources for law enforcement or too few legal avenues to punish intellectual property thieves?

   The growth in tangible music piracy, both domestically and internationally, can be attributed to significant advances in technology (i.e., high-speed, high-capacity CD burners) as well as the low cost, low risk, high return nature of piracy when compared to other criminal endeavors. Increased law enforcement resources to CHIP's units as well as federal and international enforcement entities, more vigorous enforcement of existing laws, and changes to laws (such as the PIRATE Act and the ENFORCE Act) are all needed to help address this growing problem. We also applaud the Justice Department's recent formation of an Intellectual Property Task Force designed to look at ways the department can strengthen and improve its efforts to combat theft of intellectual property. Because of the expanding geographical scope and sophistication of the organized criminal enterprises behind the piracy problem, cooperation among local, state, federal and international law enforcement entities will continue to be important.

2. You noted in your testimony on March 23 that forty per cent of music recordings worldwide are pirated. This is astounding. You also note that the decision to produce counterfeit records is a very pragmatic one for many pirates. It is, as you say, a low cost, high reward crime. In addition, you note that pirates vary their business models to reflect changes in the enforcement polices of the countries in which they work. Has there been a successful effort to change the economics of piracy, to make these sophisticated criminals find another line of work?

   There clearly is no silver bullet answer to solving the problem of physical piracy; however, there are several things that can be done that would help change the risk/reward calculation for pirates. These include, among other things, increased asset forfeiture, lower criminal thresholds, increased sentencing guidelines, as well as easier and more definite loss calculations. In other contexts, these tools have provided law enforcement with greater flexibility and authority to crack down on the epicenter of criminal enterprises as opposed to continually dealing with the problem further downstream. It will come as no surprise that attacking these criminal enterprises higher "up the ladder" (i.e. acting against manufacturers and distributors as opposed to low-level street vendors) not only increases our deterrent impact, but is also a much more efficient use of our limited resources.

3. You also noted the connection between Intellectual Property crimes and the financing of terrorist organizations. Is it your opinion that going after piracy syndicates is a useful avenue to disrupt or infiltrate the terrorist groups themselves?

   Yes, I definitely believe enforcement against piracy syndicates can be a useful instrument against terrorist groups because of the legal and technological circumstances described above. Sustaining a terrorist organization and funding terrorist's activities requires money, and law enforcement around the world has found that these organizations frequently turn to illegal funding sources. DEA has demonstrated that terrorists use drug trade to raise funds for their activities. U.S. State Department officials have testified before the Congress that terrorists groups are increasingly involved in piracy and other financial crimes. Interpol has provided congressional authority along the same lines. Criminal trafficking in contraband cigarettes

here in the United States was also found to be a source of funding to Hezbollah terrorist in the Middle East. There is every reason to believe that the enormous profit potential found in music piracy activity here in the United States is just as inviting as it has been elsewhere in the world and in connection with other contraband commodities. Dismantling such pirate operations may provide valuable opportunities to disrupt their source of money which is critical to almost any organized crime endeavor.

4. Many people think of piracy as hurting primarily artists whose songs have already earned millions of dollars. Do you have any estimate of the number of job losses that the music industry has suffered as a result of piracy, and whether these job losses are primarily among the artists, or among technicians, store clerks, and others who help produce and distribute music?

Although there is no definitive source of job loss figures and store closings according to recent press reports in Billboard and Rolling Stone magazines, over 1,000 record stores have closed nationwide over the last several years and all five of the major record labels have cut their staff by at least 1,000 workers over the last year alone due to the piracy problems:

- "Sony Music's chief outlined a long-awaited restructuring at the No. 3 music company that will streamline management, cut costs and eliminate an initial 1,000 jobs in response to a continuing slump in CD sales, CNNfn confirmed Friday." (CNNFn.com, March 28, 2003)
- "EMI Group Plc on Wednesday became the latest big music company to slash costs to cope with an ailing market, cutting 1,500 jobs, or 20 percent of its work force, trimming its roster of artists by a fifth. . ." (Reuters, April 1, 2004)
- "Universal Music, the world's largest record company, is shedding 1,350 jobs as it responds to volatile sales and illegal downloading across the industry." (Financial Times, October 16, 2003)
- "Warner Music Group is to lay off one fifth of its 5,000 global workforce and consolidate the business divisions of its Elektra and Atlantic Group labels." (BBC News, March 2, 2004)
- "In an effort to return BMG to the black, Chairman Schmidt-Holtz cut 1,500 jobs, or about 20% of the company's work force . . ." (DotComNews, March 10, 2003)

UNITED STATES PATENT AND TRADEMARK OFFICE

UNDER SECRETARY OF COMMERCE FOR INTELLECTUAL PROPERTY AND
DIRECTOR OF THE UNITED STATES PATENT AND TRADEMARK OFFICE

APR 27 2004

The Honorable Orrin G. Hatch
Chairman, Committee on the Judiciary
United States Senate
Washington, DC 20510

Attention: Mr. Barr Huefner

Dear Mr. Chairman:

Thank you for the opportunity to testify on behalf of the United States Patent and Trademark Office (USPTO) at the Judiciary Committee hearing on "Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions" on March 23, 2004.

In response to your request, attached are our responses to the written questions submitted by Committee members.

We appreciate your support for the USPTO's operations and your continuing efforts to promote effective protection of intellectual property.

Sincerely,

JON W. DUDAS
Acting Under Secretary and Acting Director

Enclosure

P.O. Box 1450, Alexandria, Virginia 22313–1450 - WWW.USPTO.GOV

Questions Submitted by Sen. Patrick Leahy

Hearing before the Committee on the Judiciary
"Counterfeiting and Theft of Tangible Intellectual Property:
Challenges and Solutions"
March 23, 2004

Questions and Responses:

1. As the Patent and Trademark Office takes these steps to modernize its examination procedures, are there particular steps that you can take to enhance the enforceability of the resulting patents?

   Modernizing examination procedures, strengthening quality and improving timeliness will raise the confidence level in patents and trademarks and discourage infringement. Because intellectual property laws are national in scope, U.S. rights holders must rely on enforcement programs of other governments to protect their interests abroad.

   While no process change in the U.S. can bestow enforceability outside the United States, the USPTO's 21st Century Strategic Plan and accompanying fee restructuring proposal enhances enforceability of intellectual property worldwide by setting the standard. On a multilateral and bilateral basis, the USPTO continues to lead by example. With many developed and developing nations modeling their offices after the USPTO, what we do in the United States has a real effect on enforceability internationally.

   In addition, the USPTO plays an active role in monitoring how foreign governments implement their intellectual property protection obligations and, when needed or requested, provides assistance in implementing an intellectual property protection and enforcement scheme.

   Within the last 18 months, the USPTO has implemented several initiatives that will improve the quality of issued patents. These initiatives are part of the 21st Century Strategic Plan, and are part of a three-step process -- to improve the examiner's knowledge and skills, to improve management oversight of the examiner's work, and to improve the completeness of the prosecution history of the application.

   As part of the Plan, the USPTO has implemented a certification exam for junior examiners, which contains questions covering sections of patent laws along with questions directed to the practice and procedures of examination. The exam must

be successfully completed before independent authority is granted to the examiner. Senior and Primary examiners will undergo a recertification of their knowledge and skills every three years. In addition, these examiners will be required to attend continual legal training. In technical areas with identified deficiencies, senior staff is reviewing allowances before a final patentability decision is reached. The Office of Patent Quality Assurance has been expanded, and more applications are receiving an independent review both during prosecution and after allowance.

The prosecution (or file wrapper) record of applications is also being enhanced. Previously, the prosecution record for some patents failed to clearly indicate why the examiner had chosen to allow the application. Procedures are now in place to enhance the prosecution record by requiring the examiner to state specifically the reason why a rejection was withdrawn at any time during the prosecution before the Office.

2. At the hearing on March 23, Mr. Willard testified that one of the problems inherent in tangible piracy is that we do not know the full extent of the problem or how it is affecting different sectors of the economy. As Acting Director of the PTO, you are also Acting Under Secretary of Commerce for Intellectual Property. Does the Department of Commerce or the PTO have plans to undertake the piracy study that we have authorized and to which Mr. Willard referred?

While the Fiscal Year 2004 budgets for the Department of Commerce and the USPTO do not include specific funding for a formal study of intellectual property piracy, the USPTO will continue to closely work with other Federal agencies, IP policy organizations, trade associations and other interested parties in developing assessments of the impact of piracy. In particular, we intend to reach out to chief executives in the business community to discuss compilation of verifiable data on the extent and impact of piracy. Having such detailed information will help us to better tailor and focus our enforcement and training-related efforts.

3. One of the themes we have heard repeated again and again is the problem of counterfeit goods coming out of China. I understand that piracy there is a major problem for a wide range of industries, and that the Chinese government's enforcement efforts are part of the problem. In your view are there steps we can be taking to encourage China to

be a better global citizen, and more vigorously enforce Intellectual Property rights?

Yes. We are actively encouraging China to implement its intellectual property obligations. A current focus has been on the Joint Committee on Commerce and Trade (JCCT), chaired jointly this year by Secretary Evans and Ambassador Zoellick. Their Chinese counterpart is Vice Premier Wu Yi. The session completed on April 21, 2004, has resulted in China presenting an action plan designed to address the piracy and counterfeiting of American ideas and innovations. According to the USTR fact sheet on the plan, China has committed to:

- Significantly reduce IPR infringement levels.
- Increase penalties for IPR violations by taking the following actions by the end of 2004:
  - -- Subject a greater range of IPR violations to criminal investigation and criminal penalties.
  - -- Apply criminal sanctions to the import, export, storage and distribution of pirated and counterfeit products.
  - -- Apply criminal sanctions to on-line piracy.
- Crack down on violators by:
  - -- Conducting nationwide enforcement actions against piracy and counterfeiting – stopping the production, sale and trade of infringing products, and punishing violators.
  - -- Increasing customs enforcement action against the import and export of infringing products and making it easier for rights-holders to secure effective enforcement at the border.
- Improve protection of electronic data by:
  - -- Ratifying and implementing the World Intellectual Property Organization (WIPO) Internet Treaties as soon as possible.
  - -- Extending an existing ban on the use of pirated software in central government and provincial agencies to include local governments.
- Launch a national campaign to educate its citizens about the importance of IPR protection (campaign started on April 6). The campaign will include press events, seminars and outreach through television and print media.
- Establish an intellectual property rights working group under the JCCT. Under this working group, U.S. and Chinese trade, judicial and law enforcement authorities will consult and cooperate on the full range of issues described in China's IPR action plan.

The Department of Commerce and the USTR, among other Federal agencies, will carefully monitor the implementation of these commitments.

Senate Judiciary Committee
April 27, 2004
Supplementary Hearing Questions

Secretary of Commerce Don Evans is keenly aware of the increasing significance of intellectual property protection for American businesses and innovators and has made combating counterfeiting and piracy a top priority for the entire Department. Under the direction of Secretary Evans, the USPTO has been working extensively to reduce piracy and counterfeit activity in China.

Last fall, Secretary Evans led a mission to China and highlighted China's lack of IPR enforcement. The Secretary met with high-ranking Chinese officials and reiterated a continuing concern; that effective IPR protection requires that criminal penalties for stolen intellectual property theft and fines are large enough to be a deterrent rather than a business expense. Secretary Evans believes in the strong enforcement of our trade laws and is taking new and proactive measures to strengthen the enforcement and compliance of our trade agreements. He has tasked Commerce agencies, such as the USPTO and the new Office of Investigations and Compliance under Commerce's International Trade Administration, to coordinate their efforts to vigorously pursue allegations of IPR violations wherever they occur, especially in China.

4. You stated in your testimony that part of your efforts include "bringing together local authorities to address enforcement issues." What success have you had in bringing together these local authorities?

The USPTO's Office of Enforcement routinely brings together local authorities to discuss and coordinate intellectual property rights enforcement. For example, the Office of Enforcement develops and administers training and technical assistance programs which are offered around the world, and through which best practices for enforcing IPR in particular countries or regions are identified and disseminated. In addition, through its participation in international bodies such as the World Intellectual Property Organization (WIPO) and Asia Pacific Economic Cooperation forum, the Office of Enforcement works with enforcement authorities from other countries and regions to develop strong international IPR enforcement standards and encourage vigorous IPR enforcement.

The following is a recent, but by no means exhaustive, sampling of the types of programs the Office of Enforcement has hosted:

October 2002, Hanoi and Ho Chi Minh City, Vietnam. Workshop brought together more than 50 local law enforcement officers, judges, prosecutors, and customs officials to discuss various practical, hands-on IPR enforcement issues. Participants rated the workshop as helpful to their local efforts at raising public awareness of need for stronger IP protection and enforcement.

January 2004, Muscat, Oman. Workshop brought together more than 50 local law enforcement officers, judges, prosecutors, and customs officials to discuss various practical, hands-on IPR enforcement issues within the GCC region. Participants rated the workshop as helpful to their local efforts at raising awareness within local government and the public of need for stronger IP protection and enforcement.

February 2004, Georgetown, Guyana. Workshop brought approximately 30 local IP officials, prosecutors, judges, customs officials, and other government officials together with industry representatives and rights holders to discuss need for stronger IP legislation and practical issues concerning IPR enforcement efforts and activities in Guyana. Participants rated the workshop as helpful to their local efforts at raising awareness within local government and the public of need for stronger IP protection and enforcement.

February 2004, Paramaribo, Suriname. Workshop brought approximately 40 local IP officials, prosecutors, judges, customs officials, and other government officials together with various industry representatives and rights holders to discuss need for stronger IP legislation and practical issues concerning IPR enforcement efforts and activities in Suriname. Participants rated the workshop as helpful to their local efforts at raising awareness within local government and the public of need for stronger IP protection and enforcement.

Questions Submitted by Senator Patrick Leahy
Hearing before the Committee on the Judiciary
"Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions"

Follow-up Questions for Mr. James Mendenhall

1. **I know that the US Trade Representative's office has been busy negotiating a number of free trade agreements in recent months, and expects to continue to do so. I also understand that the intellectual property provisions of those agreements require a lot of attention and effort from Congress. What problems do you face in trying to persuade other countries to respect US intellectual property rights? Does the US have a consistent position of respecting other countries' IP in the same ways that we expect to be treated?**

Response 1:
Yes, the United States does respect other countries' intellectual property in the same ways that we expect to be treated. The problems that we face in persuading other countries to respect U.S. intellectual property vary by country. One of the most common problems is in obtaining effective enforcement. Enforcement problems manifest themselves in many different ways; some examples include: insufficient closures of factories engaged in counterfeiting and piracy, inadequate prosecution of infringers in criminal and/or civil courts, judicial delays for IP cases, issuance of penalties that fail to have a deterrent effect, lack of seizure and destruction of infringing goods, and insufficient raids against distributors and vendors. Besides enforcement problems, we also face problems in some countries in ensuring that their laws meet their international obligations under the Agreement on Trade-Related Intellectual Property Rights (TRIPS Agreement). We address each of these problems on a case-by-case basis with each country, bringing to bear the various available tools that I outlined in my testimony.

2. **In his testimony before the Committee on March 23, Mr. Willard proposes changing our laws to require seizure and destruction of counterfeiting equipment, in addition to seizure of the offending goods. He states that our trade negotiators should have such laws in place so that they could demand them of our trading partners overseas. Do you agree that such a provision is necessary to effective IP enforcement globally?**

Response 2:
What is necessary for effective IP enforcement varies by country depending on its domestic circumstances. In certain instances, we feel that requirements for the seizure and destruction of counterfeiting equipment would be beneficial. Regarding whether US laws should be changed, this matter is currently under review by the Department of Justice in consultation with the Congress.

3. We have all seen frighteningly large numbers - in terms of retail revenue lost, jobs foreclosed, and taxes unpaid - associated with counterfeiting and piracy. Can you quantify the harm that these crimes have on our economy? Among the problems that you face on negotiating trade agreements, and in promoting US industries on the world stage, how would you rank IP piracy?

Response 3:
We certainly share your concern over the reported losses due to counterfeiting and piracy. Although it is difficult to quantify the actual harm on our overall economy, the losses resulting from such crimes have a negative impact on a significant and growing sector. For example, the latest data available show that the U.S. copyright industries accounted for 5.24% of U.S. GDP or $535.1 billion in 2001. With a total of $88.97 billion in foreign sales and exports reported in 2001 - a 9.4% gain from the previous year - the copyright industries' foreign sales continue to be larger than several other leading industry sectors, including automobiles and auto parts, aircraft and agriculture. Between 1977 and 2001 employment in the copyright industries more than doubled to 4.7 million workers (3.5% of total U.S. employment) and grew nearly three times as fast as the annual employment growth rate of the economy as a whole (5.0% vs. 1.5%).

Given the significance and size of our IP-related industries, ensuring adequate and effective protection for U.S. intellectual property rights in foreign markets continues to be a top priority for this Administration. Provisions to strengthen the protection and enforcement of intellectual property rights that combat IP piracy are a key objective in all our trade agreement negotiations. IP piracy and lack of effective enforcement are serious concerns, and we are committed to pursuing the highest achievable standards for intellectual property protection and enforcement in all of our future FTAs.

4. In your testimony you stated that to solve the problem of IP enforcement overseas, we need to create legal systems and cultures built on the rule of law. What steps have we taken, and what can we take in the future to encourage these legal systems?

Response 4:
We have been actively engaged in helping to create legal systems built on the rule of law bilaterally and regionally through IP-related provisions in our FTAs, and multilaterally through the WTO TRIPS Agreement and other such fora as APEC. In addition, we have worked bilaterally with several countries in providing technical assistance and expertise.

With regard to the future, the successful conclusion of FTAs with trading partners such as Thailand and the Andean countries will help create effective legal systems in countries and regions where we have had serious piracy and enforcement problems in the past. In addition, we can work through the interagency process to utilize various tools we have such as the Special 301 process, preference programs and diplomatic leverage to encourage the rule of law. As I noted in my testimony, we also need to improve public awareness in foreign countries about the economic benefits of a vibrant IP sector and the need for effective legal systems to promote and protect the development of IP-related industries. Possible avenues to achieve this goal could include working with foreign governments and public diplomacy programs through our embassies.

Questions Submitted by Senator Patrick Leahy
Hearing before the Committee on the Judiciary
"Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions"

Follow-up Questions for Vanessa Price:

In your testimony on March 23, you mentioned that a small company such as Burton does not have the resources to fight counterfeiting on a large scale. Do you believe that there are steps the U.S. government can take to better protect Burton's work products from counterfeiters?

Resources available to U.S. companies are known to be largely ineffective. Beyond trademark registration and filing with Customs officials, there are very few options. Suits in foreign countries alleging unfair competition are expensive, time consuming, and unsuccessful. Moreover, insurance policies do not cover a company such as Burton against losses due to IP theft.

In our experience with counterfeiters, the most pressing issue is timing. When counterfeit goods surface in the U.S. or Asia, they are there and gone in a matter of days or hours. There is never enough time to track the source of the goods and to prosecute the counterfeiters. Therefore, the individuals who profit most from counterfeiting are rarely caught or punished. The most serious threat they face is a confiscation of their fake goods. What are sorely needed are effective laws and vigorous enforcement mechanisms. Customs, police, other law enforcement agencies, and judicial systems need to be held accountable for the enforcement of anti-counterfeiting laws. Counterfeiting needs to be truly considered "theft." Additionally, the United States should provide technical and monetary assistance to developing nations to improve their anti-counterfeiting efforts.

I understand that many counterfeit goods are offered for sale on the Internet, especially on auction sites. Has Burton had trouble with this kind of distribution of knock-off goods? What steps could the government take to help curtail the use of online auctions sites for the sale of counterfeit goods?

The ease and anonymity of worldwide electronic and internet sales have given counterfeiters and gray marketers unprecedented access to markets and marketplaces. Their contraband is now even harder to trace. Burton has noticed growing problems with small-scale counterfeiting in the U.S. Typically, this involves the manufacture and sale of fake Burton, Gravis, and Analog stickers, accessories, and clothing on Internet auction sites, specifically eBay. Unauthorized Burton branded goods can be found on eBay almost continuously. While eBay affords intellectual property owners the right to request the removal of counterfeit items from auction, Burton Snowboards does not have the resources to pursue every instance of counterfeiting on eBay. eBay surveillance on this

scale would necessitate additional employees. Additionally, while the goods have been removed from eBay, they are still in the marketplace.

Small-scale counterfeiting may not appear to be a significant problem. However, Burton manufactures limited editions of specific stickers and products. These items stand to lose their consumer appeal when they routinely show up in large quantities on eBay.

I am particularly concerned about individuals using products they believe to be safe and effective when they are in fact endangering their well being with inferior products. You mentioned in your testimony that sub par products put the public at risk – I am wondering if you would tell the Committee more about this problem.

Counterfeiters care little about the quality of the products they sell under our good name. In turn, counterfeit products that fail to adhere to our high safety standards put the public at risk, and inevitably damage our industry and our brand. Almost by definition counterfeiters go into business only to make a quick profit, having no accountability for the safety of the wares they sell. Burton invests heavily in research and development on our Hardgoods to ensure production and sale of top-quality products. Counterfeiters not only steal our good name from us, but they deceive the buying public who believe they are obtaining genuine products that are safe and of high quality. Additionally, Burton takes all available measures to produce equipment according to high safety standards, and we stand behind the quality of our product. Counterfeiters undermine the investments we make in the development and implementation of new safety features.

While counterfeiting of our Hardgoods (snowboards, boots, and bindings) has not been substantial to date (due to cost of production), we have noticed a growing problem with counterfeiting and factory leaks as we expand our business operations. For example, in the weeks since my Senate testimony, I discovered a shipment of counterfeit Burton snowboard boots for sale through a discount sports outfit in Maine. After examining the poor quality of the counterfeit boots, we determined that anyone using the boots for snowboarding risks injury due to a lack of reinforcement and support in the product's construction. These cheap fakes were produced in China. Most fakes are produced offshore where safety standards are non-existent or ignored. Of course, this foreign production takes more jobs away from U.S. workers, goes untaxed, and further increases the trade imbalance as well.

April 12, 2004

The Honorable
Orrin G. Hatch
United States Senate
U.S. Senate Judiciary Committee
224 Dirkesn Senate Office Building
Washington, D.C. 20510

Dear Senator Hatch:

I appreciated the opportunity to testify before the Committee on March 23, 2004, on the issue of "Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions".

I have received your April 5, 2004 letter that includes additional questions as follow-up to the hearing and provide responses in this letter and through the accompanying attachments. The questions are reproduced below with their respective responses.

1. You mention in your testimony that auto parts such as brake pads have been counterfeited. The prospect of vehicles traveling at high speeds or airlines flying at high altitude experiencing mechanical failure is certainly frightening. How difficult is it to recognize these parts as counterfeit and stop them from being used with what I imagine could be catastrophic consequences?

Identifying counterfeit auto parts is complicated for several reasons. First, today's counterfeiters have access to modern technology and they can reproduce parts packaging to look practically identical to the authentic packaging. Thus, products entering any country/port pose significant challenges to customs officials responsible for inspection. Absent industry training, intelligence information and the ability to have side-by-side comparisons, it is extremely difficult to detect counterfeit parts. Second, the outward appearance of the parts themselves are made to look either exactly like the authentic part to the point that differences are overlooked except for a very well trained inspector. Third, often, the authentic part does not have the protected trademark/logo on the part itself, i.e., may not be part of the mold and thereby not present once the part is removed from the packaging.

International AntiCounterfeiting Coalition, Inc., 1725 K Street, N.W., Suite 1101, Washington, D.C. 20006
Telephone 202-223-6667 • Facsimile 202-223-6668 • www.iacc.org

Combined, these factors pose significant challenges to the industry in attempting to protect themselves and consumers from counterfeits entering the stream of commerce. Moreover, the challenge is global for the companies because all major auto manufacturers offer their products in numerous markets around the world. As a result, their enforcement efforts are global because the risks posed by counterfeits are global. Auto manufacturers are involved in an anti-counterfeiting effort encompasses every part of the globe. Because of the threat of counterfeits, they have established cooperative efforts in some of the most challenging places around the world in an effort to combat the manufacture, distribution and sale of counterfeit auto parts and related products such as lubricants.

2. Among the Recommendations of the IACC is that the government strengthen the federal criminal statute against trafficking in counterfeit goods. Do you have specific recommendations for how this might be done?

Please see the attached proposal to amend 18 U.S.C § 2320 "Trafficking in Counterfeit Goods or Services".

I hope that the above responses and the attachments have adequately responded to your questions. If, however, you have additional questions, please do not hesitate to contact me.

Respectfully,

SIGNED

Timothy P. Trainer
President
Email: ttrainer@iacc.org

Attachments

INTERNATIONAL ANTICOUNTERFEITING COALITION (IACC)

Section 2320 of Tile 18 of the United States Code criminalizes intentional trafficking in goods or services that bear a counterfeit trademark. In its current form, section 2320 restricts criminal prosecutions for trademark counterfeiting to those cases where the spurious mark is used in connection with goods or services that are *identical* to those listed in the certificate of registration for the mark being counterfeited.

Based on the current law, a savvy counterfeiter can avoid criminal prosecution in one of two ways. First, the counterfeiter can evade liability by merely examining the trademark registration (a public record) and placing the counterfeit mark on goods not specifically listed in the registration (i.e., non-identical goods). A second method often employed by sophisticated counterfeiters is to sell counterfeit versions of the marks themselves in the form of "patch sets" or medallions, that can later be attached to generic merchandise and give the appearance of a genuine product. The second scheme is best illustrated by the case of *United States v Giles,* 213 F.3d 1247 (10th Cir. 2000)(see attached summary of *Giles* case).

Section 2320, as currently worded, does not adequately serve the enforcement needs of trademark owners and has failed to keep pace with the underhanded practices of sophisticated counterfeiters and needs to be amended.

Proposed Amendments to 18 U.S.C. § 2320

In response to these problems and as part of its continuing efforts to strengthen IP protection in general, the International AntiCounterfeiting Coalition (IACC) offers the attached draft proposal for amending section 2320. The proposed amendments, if signed into law, will serve to:

- inform counterfeiters that Congress intends section 2320 to prohibit trafficking in counterfeit labels/patches/medallions that are unattached to any goods. In this sense, trademark owners would only be obtaining protection that is already afforded to copyright owners under 18 U.S.C. § 2318. *See § 2320(e)(1)(C) of attached redline version of § 2320 (providing an alternative definition for the term counterfeit mark).*

- provide greater protection for "famous marks" by removing the burdensome requirement that the spurious mark be used in connection with goods or services identical to those for which the genuine mark is already registered. *See 18 U.S.C. § 2320(e)(1)(D) of attached redline version of § 2320 (also providing an alternative definition for the term counterfeit mark).* It is important to note that many state criminal trademark counterfeiting statutes provide the benefits of criminal prosecution irrespective of the goods offered in connection with the sale of a counterfeit mark.

- provide mandatory destruction, forfeiture and restitution provisions similar to those already afforded to copyright owners. *See §§ 2320(b)(1)-(3) of the attached redline version of § 2320.*

Contact Information

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§ 2320. Trafficking in counterfeit goods or services

(a) Whoever intentionally traffics or attempts to traffic in goods or services and knowingly uses a counterfeit mark on or in connection with such goods or services or intentionally traffics or attempts to traffic in counterfeit marks, as that term is defined in section 2320(e), shall, if an individual, be fined not more than $ 2,000,000 or imprisoned not more than 10 years, or both, and, if a person other than an individual, be fined not more than $ 5,000,000. In the case of an offense by a person under this section that occurs after that person is convicted of another offense under this section, the person convicted, if an individual, shall be fined not more than $ 5,000,000 or imprisoned not more than 20 years, or both, and if other than an individual, shall be fined not more than $15,000,000.

(b)(1) Upon a determination by a preponderance of the evidence that any articles in the possession of a defendant in a prosecution under this section bear or are counterfeit marks, the court shall order the forfeiture and destruction of such articles, regardless of the criminal culpability of the defendant.

(2) The court, in imposing a sentence upon a person convicted of a violation of this section, or upon a person who pleads guilty or nolo contendre to a violation of this section, shall order, in addition to any other sentence imposed, that the person forfeit to the United States - -

(A) any property constituting or derived from, any proceeds the person obtained, directly or indirectly, as the result of such violation; and

(B) any of the person's property used, or intended to be used, in any manner or part, to commit, facilitate, aid or abet the commission of such violation, if the court in its discretion so determines, taking into account the nature, scope, and proportionality of the use of the property in the offense.

(3) When a person/defendant is convicted of a violation of this section, or pleads guilty or nolo contendre to a violation of this section, the court, pursuant to 18 U.S.C. §§ 3556, 3663A(c)(1)(A)(ii) and 3664, shall order the person/defendant to pay restitution to the owner of the mark and any other victim of the offense.

(4) The word/term "victim" as used in subsection (a)(3) shall have the same meaning given that word/term in 18 U.S.C. § 3663A(a)(2).

(c) All defenses, affirmative defenses, and limitations on remedies that would be applicable in an action under the Lanham Act shall be applicable in a prosecution under this section. In a prosecution under this section, the defendant shall have the burden of proof, by a preponderance of the evidence, of any such affirmative defense.

(d) (1) During preparation of the presentence report pursuant to Rule 32(c) of the Federal Rules of Criminal Procedure, victims of the offense shall be permitted to submit, and the probation officer shall receive, a victim impact statement that identifies the victim of the offense and the extent and scope of the injury and loss suffered by the victim, including the estimated economic impact of the offense on that victim.

(2) Persons permitted to submit victim impact statements shall include--

(A) producers and sellers of legitimate goods or services affected by conduct involved in the offense;

(B) holders of intellectual property rights in such goods or services; and
(C) the legal representatives of such producers, sellers, and holders.

(e) For the purposes of this section--
(1) the term "counterfeit mark" means—

(A) a spurious mark--
(i) that is used in connection with trafficking in goods or services;
(ii) that is identical with, or substantially indistinguishable from, a mark registered for those goods or services on the principal register in the United States Patent and Trademark Office and in use, whether or not the defendant knew such mark was so registered; and
(iii) the use of which is likely to cause confusion, to cause mistake, or to deceive; or

(B) a spurious designation that is identical with, or substantially indistinguishable from, a designation as to which the remedies of the Lanham Act are made available by reason of section 220506 of title 36; or

(C) a spurious mark –
(i) that is identical with, or substantially indistinguishable from, a mark registered on the principal register in the United States Patent and Trademark Office and in use, whether or not the defendant knew such mark was so registered; and
(ii) that is applied to or consists of a label, patch, sticker, wrapper, badge, emblem, medallion, charm, box, container, can, case, hangtag, documentation or packaging of any type or nature that is designed to be affixed to, distributed with, consist of or otherwise accompany the goods or services; or

(D) a spurious mark –
(i) that is used in connection with the trafficking of goods or services; and
(ii) that is identical with, or substantially indistinguishable from a famous mark, that is registered on the principal register in the United States Patent and Trademark Office and in use, regardless of the goods or services or class(es) of goods or services for which the famous mark is registered, and regardless of whether or not the defendant knew such mark was so registered and famous;

but such term does not include any mark or designation used in connection with goods or services of which the manufacturer or producer was, at the time of the manufacture or production in question authorized to use the mark or designation for the type of goods or services so manufactured or produced, by the holder of the right to use such mark or designation;

(2) the term "traffic" means transport, transfer, or otherwise dispose of, to another, as consideration for anything of value, or make or obtain control of with intent so to transport, transfer, or dispose of;
(3) the term "Lanham Act" means the Act entitled "An Act to provide for the registration and protection of trademarks used in commerce, to carry out the provisions of certain international conventions, and for other purposes", approved July 5, 1946 (15 U.S.C. 1051 et seq.);

(4) In determining whether a particular mark is a "famous mark" the court may consider information, data, testimony, documentation regarding factors such as, but not limited to:

(A) the degree of inherent or acquired distinctiveness of the mark;

(B) the duration and extent of use of the mark;

(C) the duration and extent of advertising and publicity of the mark;

(D) the geographical extent of the trading area in which the mark is used;

(E) the channels of trade in which the mark is used;

(F) the degree of general public recognition of the mark;

(G) the nature and extent of use of the same or similar marks by third parties;

(H) survey evidence; and

(I) the record of successful criminal, civil or administrative enforcement of rights in the mark, in particular, the extent to which the mark has been recognized as being famous by federal or state courts or administrative authorities;

(5) In order to qualify as a famous mark, the mark must be registered on the principal register of the United States Patent and Trademark Office;

(6) The United States shall bear both the burden of proof and persuasion with respect to the determination of whether a particular mark is a famous mark. Evidence, in the form of a certified copy of a published court or administrative opinion, of a prior determination, on the merits, by a federal or state court or administrative authority, holding that a particular mark is a famous mark, (regardless of whether the proceedings leading to the determination were civil, criminal or administrative in nature), shall create a rebuttable presumption that the mark in question is a famous mark;

(7) A defendant may not be prosecuted under this section where the defendant owns, or is the agent or employee of a legal entity that owns, a valid and subsisting United States federal registration for a mark that is registered on the principal register of the United States Patent and Trademark Office for a mark that, if not for the valid and subsisting federal registration, would otherwise qualify as a counterfeit mark as that term is defined in this subsection.

(f)

(1) Beginning with the first year after the date of enactment of this subsection [enacted July 2, 1996], the Attorney General shall include in the report of the Attorney General to Congress on the business of the Department of Justice prepared pursuant to section 522 of title 28, an accounting, on a district by district basis, of the following with respect to all actions taken by the Department of Justice that involve trafficking in counterfeit labels for phonorecords, copies of computer programs or computer program documentation or packaging, copies of motion pictures or other audiovisual works (as defined in section 2318 of this title), criminal infringement of copyrights (as defined in section 2319 of this title), unauthorized fixation of and trafficking in sound recordings and music videos of live musical performances (as defined in section 2319A of this title), or trafficking in goods or services bearing counterfeit marks (as defined in section 2320 of this title):

(A) The number of open investigations.

(B) The number of cases referred by the United States Customs Service.

(C) The number of cases referred by other agencies or sources.

(D) The number and outcome, including settlements, sentences, recoveries, and penalties, of all prosecutions brought under sections 2318, 2319, 2319A, and 2320 of this title.

(2) (A) The report under paragraph (1), with respect to criminal infringement of copyright,

shall include the following:

(i) The number of infringement cases in these categories: audiovisual (videos and films); audio (sound recordings); literary works (books and musical compositions); computer programs; video games; and, others.

(ii) The number of online infringement cases.

(iii) The number and dollar amounts of fines assessed in specific categories of dollar amounts. These categories shall be: no fines ordered; fines under $ 500; fines from $ 500 to $ 1,000; fines from $ 1,000 to $ 5,000; fines from $ 5,000 to $ 10,000; and fines over $ 10,000.

(iv) The total amount of restitution ordered in all copyright infringement cases.

(B) In this paragraph, the term "online infringement cases" as used in paragraph (2) means those cases where the infringer--

(i) advertised or publicized the infringing work on the Internet; or

(ii) made the infringing work available on the Internet for download, reproduction, performance, or distribution by other persons.

(C) The information required under subparagraph (A) shall be submitted in the report required in fiscal year 2005 and thereafter.

Appeals Court Decision Harms Trademark Owners

United States v. Giles, 213 F.3d 1247 (10th Cir. 2000)

Trademark owners face a tougher time combating counterfeiters in the wake of an appeals court decision that held trafficking in counterfeit trademarks not attached to goods (i.e., trafficking in labels, patches, medallions, etc.) does not violate the federal trademark counterfeiting law (18 U.S.C. § 2320).

Facts/Background

The defendant, Donald R. Giles, owns a business in Atlanta, Georgia called "Fabulous Fakes," which specializes in the sale of "designer look-alikes" such as handbags, belts, watches and other accessories. The defendant also sells certain items in bulk on the wholesale market. The wholesale items at issue in this case consisted of "patch sets" bearing the logo/trademark of Dooney & Bourke, a manufacturer of high quality handbags, luggage and accessories. The "patch set" consisted of a leather patch and gold medallion, (both bearing the Dooney & Bourke logo/trademark), and a leather strap used to attach the medallion to a purse or piece of luggage. Once the patch set is applied to a generic purse or piece of luggage, the article will appear to have been made by Dooney & Bourke.

In June 1994, the FBI, using an informant, conducted a sting operation to catch Giles in the act of selling the patch sets. The operation was successful and in July 1994, Gile's Fabulous Fakes company shipped 1,000 Dooney & Bourke patch sets from its Atlanta facility to an FBI informant in Oklahoma. The patch sets were seized by the FBI and Giles was indicted for trafficking in counterfeit goods in violation of 18 U.S.C. § 2320. After his motions to dismiss the indictment were denied, Giles was subsequently convicted by a jury in the United States District Court for the Western District of Oklahoma. Giles appealed to the United States Court of Appeals for the Tenth Circuit, which ultimately vacated the conviction.

Elements of Criminal Counterfeiting

To obtain a conviction under 18 U.S.C. § 2320, the government must prove that the defendant: (1) trafficked or attempted to traffic in goods or services; (2) did so intentionally; (3) used a counterfeit mark on or in connection with such goods or services; and (4) knew the mark was counterfeit.

Elements one and three above proved to be troublesome for government prosecutors, specifically with regards to whether the "patch sets" at issue were "goods" within the meaning of 18 U.S.C. § 2320. Giles argument was that he could not be convicted because the language of 2320 requires that a defendant both traffic in goods and knowingly use a counterfeit mark on those goods (essentially referring to elements one and three above). Giles argued that an individual who merely traffics in only the counterfeit marks themselves (i.e., labels, patches, medallions, etc, that are not attached to any goods) does not violate the express terms of 18 U.S.C. § 2320.

Issues

Whether the patch sets at issue, (which essentially consist of nothing more than a reproduction of the mark itself), constitute "goods" under the provisions of 18 U.S.C. § 2320.

Whether an individual who traffics in trademarks which are not attached to any goods or services violates 18 U.S.C. § 2320.

Reversal of Conviction By Tenth Circuit

The Tenth Circuit reversed Gile's conviction for three reasons, all three of which present criminal enforcement problems for trademark owners.

First, the Court determined that the "patch sets" at issue did not constitute "goods" for purposes of the statute. The Court concluded that "goods" were intended to be viewed as separate and distinct from the marks they carry.[1] See United States v. Giles, 213 F.3d 1247, 1249 (10th Cir. 2000)(referring to 18 U.S.C. § 2320(e)(1) which defines, in part, a counterfeit mark as a "spurious mark that is *used in connection with goods*").

Second, the Court determined/recognized that § 2320 does not separately prohibit trafficking in counterfeit labels, patches, medallions, etc. which are unconnected from the goods:

> In order for the government to prevail the statute must prohibit trafficking in counterfeit labels such as the patch sets. Section 2320 does not contain such a prohibition. Another criminal provision makes it illegal to traffic in counterfeit labels for specific products such as records, computer programs, and motion pictures. *See* 18 U.S.C. § 2318. Mr. Giles persuasively argues that if Congress had intended to outlaw trafficking in labels for other goods, it would have done so in this or another provision of the criminal code.
>
> We have little case law to guide us in determining whether 18 U.S.C. § 2320, the criminal statute we are dealing with here, should be applied to trafficking in labels. Because the statute does not so provide, we are persuaded that section 2320 does not forbid the mere act of trafficking in counterfeit labels which are unconnected to any goods.

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[1] Clearly, whether defendants, in similar factual scenarios, can be convicted of criminal trademark counterfeiting depends on how the term "goods" is defined for purposes of 18 U.S.C. § 2320. Under the current wording of section 2320, the best argument a prosecutor can put forward is that because the patch sets are sold separately they qualify as "goods." See Giles, 213 F.3d at 1249 ("The government would have [the Court] adopt the following syllogism: because the patch sets were sold for a price, they are merchandise; merchandise by definition is goods; therefore, the patch sets qualify as goods under section 2320, and Mr. Giles can be held criminally liable for trafficking in them."). The Court rejected this reasoning. Thus, trademark owners seek and need a stronger statutory based argument to help protect them from the likes of Mr. Giles. This, of course, would be in addition to the logic and inherent notions of fair play and justice that already permeate their current position that "Giles-like" activity should be considered criminal in nature.

Id. at 1251 (footnotes omitted). As is evident from the above passage, copyright holders are already given similar protection (and perhaps even greater protection if S. 2395 becomes law). Trademark holders simply seek equal/similar protection from counterfeiters who continue to unlawfully trade on the hard earned brand equity, goodwill and reputation of trademark owners.

Third, the Court noted that a criminal conviction under section 2320 can only be had where a spurious mark is used in connection with goods or services for the which the genuine mark is already registered and in use. See id. at 1251; 18 U.S.C. § 2320(e)(1)(A)(ii)("'counterfeit mark' means a spurious mark . . . that is identical with, or substantially indistinguishable from, a mark registered for those goods or services on the principal register in the United States Patent and Trademark Office . . ."). In the instant case, Dooney & Bourke did not have a separate trademark registration for leather patches, labels or medallions. As such, the Court held that criminal liability could not attach to Giles activity.

In closing the Court noted the need to clearly define criminal conduct and stated:

> We cannot say with confidence that Mr. Giles was adequately informed that the conduct in which he engaged could be a federal crime, or that section 2320 was intended to cover his conduct. In any event, we must give him the benefit of the doubt. We hold that the allegations in the indictment failed to state an offense under section 2320.

Id. at 1253.

Proposed Amendments to 18 U.S.C. § 2320

In response to this case and in its continuing efforts to strengthen IP protection in general, the International AntiCounterfeiting Coalition (IACC) respectfully offers the attached draft proposal for amending section 2320. The proposed amendments, if signed into law, will serve to adequately inform Mr. Giles, and others like him, that Congress intends section 2320 to cover, among other things, trafficking in counterfeit labels that are unattached to any goods. *See § 2320(e)(1)(C) of attached redline version of § 2320.*

The proposed amendments will also provide greater protection for "famous marks" by removing the burdensome requirement that the spurious mark be used in connection with goods or services for which the genuine mark is already registered. *See 18 U.S.C. § 2320(e)(1)(D) of attached redline version of § 2320.*

The other proposed amendments to § 2320 include mandatory destruction, forfeiture and restitution provisions. *See §§ 2320(b)(1)-(3) of the attached redline version of § 2320.*

Darren E. Pogoda
International AntiCounterfeiting Coalition, Inc. (IACC)
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"THE IDENTICAL GOODS DOCTRINE" OF 18 U.S.C. § 2320: A SERIOUS ENFORCEMENT OBSTACLE FOR OWNERS OF FAMOUS TRADEMARKS

"A man is not to sell his own goods under the pretence that they are the goods of another man . . ." -- *Perry v. Truefitt,* 6 Beav. 66, 73; 49 E.R. 749 (Ch.)(1842).

Over the course of the past two decades, trademark owners have witnessed an explosion in the size and scope of trademark counterfeiting operations, in both the domestic and international arenas. In today's global economy and with easy and widespread access to technological advances such as computers, copiers and scanners, there are virtually no product lines, corporations or consumers that escape the reach of determined counterfeiters. Never before has it been so easy to duplicate products, labels, packaging, documentation, authentication devices and symbols/marks/logos with such speed, accuracy and relative anonymity. In addition, the enormous profit potential and the relatively low risk of prosecution have made trademark counterfeiting an attractive enterprise for highly sophisticated and organized criminal syndicates. In the battle against the onslaught of knockoff products, the federal criminal trademark counterfeiting statute[1] has stood as the most potent arrow in the trademark owner's quiver. Unfortunately, for trademark owners, some savvy counterfeiters have recently begun conducting their operations in a manner that allows them (the counterfeiters) to fall just outside the reach of the federal trademark counterfeiting statute. Along these lines, this article will attempt to examine how reliance on the "identical goods doctrine" of 18 U.S.C. § 2320 serves to severely hamper meaningful enforcement efforts against individuals who apply counterfeit versions of (famous) trademarks to goods not specifically listed in the certificate of registration (i.e., non-identical goods) and/or sell counterfeit versions of the actual marks themselves in the form of patches, medallions or labels that can later be attached to generic goods to give the appearance of a genuine product.

A. 18 U.S.C. § 2320 and the "Identical Goods Doctrine"

In 1984, in response to an increasing tide of commercial trademark counterfeiting and in response to concerns that the Lanham Act was not providing sufficient civil protection against counterfeiters, Congress passed the Federal Trademark Counterfeiting Act ("The Act").[2] The

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[1] *See* 18 U.S.C. § 2320.

[2] Congress's intent in passing the Act is evident in the legislative history accompanying the Act. *See* S. Rep. No. 98-526 (1984), *reprinted in* 1984 U.S.C.C.A.N. 3627.

In 1996, Congress enacted the Anticounterfeiting Consumer Protection Act of 1996 ("The ACPA"). The ACPA, among other things, substantially increased the potential penalties for criminal trademark counterfeiting. *See* Pub. L. No. 104-153, 110 Stat. 1386 (July 2, 1996).

Act was codified at 18 U.S.C. § 2320 ("Section 2320") and criminalizes intentional trafficking in goods or services that bear a counterfeit mark.

Section 2320 requires the government to establish four elements beyond a reasonable doubt in order to obtain a criminal trademark counterfeiting conviction:

(1) the defendant trafficked or attempted to traffic in goods or services;
(2) such trafficking, or an attempt thereof, was intentional;
(3) the defendant used a "counterfeit mark" (as defined in 2320(e)) on or in connection with such goods or services; and
(4) the defendant knew that the mark was counterfeit.[3]

As stated above, the third element necessary for conviction under section 2320 is that the defendant use a "counterfeit mark" in connection with the trafficked goods or services. It is this element that incorporates what is referred to as the "identical goods doctrine." For criminal prosecution purposes only, section 2320(e) provides a five part definition of the term "counterfeit mark":

(a) a spurious mark[4]
(b) used in connection with the trafficking of goods or services
(c) that is identical with or substantially indistinguishable from
(d) a mark registered on the principal register in the U.S. Patent & Trademark Office for those goods or services that are being trafficked by the counterfeiter/defendant (this is the "identical goods doctrine") and
(e) is likely to cause confusion or to deceive.[5]

Section 32(1) of the Lanham Act (15 U.S.C. § 1114(1)) serves as the basis for civil counterfeiting claims. Section 32(d) of the Lanham Act (15 U.S.C. § 1116(d)) provides for the seizure of counterfeit goods upon ex parte applications to the court. Section 35(b) of the Lanham Act (15 U.S.C. § 1117(b)) provides for treble damages and reasonable attorney's fees for cases of intentional counterfeiting.

[3] An analysis of each element is beyond the scope of this article. For an analytical overview of the elements of the crime of trademark counterfeiting see David J. Goldstone & Peter J. Toren, *Article: The Criminalization of Trademark Counterfeiting,* 31 Conn. L. Rev. 1 (1998). For a more general overview of the history of intellectual property crimes in the United States see Michael Coblenz, *Intellectual Property Crimes,* 9 Alb. L.J. Sci. & Tech. 235 (1999)(including an analysis of the elements of 18 U.S.C. § 2320).

[4] The statute does not provide a definition of what is meant by the term "spurious mark." The legislative history is similarly lacking in guidance and only states the term spurious means "not genuine or authentic." *See* 130 Cong. Rec. 31, 675 (1984)(Joint Statement on Trademark Counterfeiting Legislation). One commentator notes that the term spurious essentially refers to "whether the counterfeiter's use of the mark was authorized by the trademark owner." *See* David J. Goldstone & Peter J. Toren, *Article: The Criminalization of Trademark Counterfeiting,* 31 Conn. L. Rev. 1, 26-27 (1998); *United States v. Petrosian,* 126 F.3d 1232, 1234 (9th Cir. 1997)(defining a spurious mark as one that is "false or unauthentic")(citing Webster's Third New International Dictionary 2212 (1961) and the Joint Statement on Trademark Counterfeiting Legislation, 130 Cong. Rec. 31673, 31675 (1984)).

[5] The Lanham Act, for civil lawsuit purposes, defines the term "counterfeit" as merely "a spurious mark which is identical with, or substantially indistinguishable from, a registered mark." *See* 15 U.S.C. § 1127. For purposes of obtaining an ex parte civil seizure order see 15 U.S.C. § 1116(d)(1)(B)(providing a definition of counterfeit mark for purposes of obtaining such an order). *See also Playboy Enterprises, Inc. v. Universal Tel-A-*

Accordingly, the statute restricts criminal prosecutions for counterfeiting to only those cases where the spurious mark was used in connection with goods or services *identical* to those listed in the certificate of registration for the mark being counterfeited. This limitation is an important distinction from civil claims under section 1114 of the Lanham Act, where protection of trademarks is not limited to the specific goods listed on a registration certificate. In civil cases, courts adhere to the "related goods" doctrine and apply a likelihood of confusion standard, thus potentially extending protection for trademarks beyond the specific goods listed in the registration. The Senate-House Joint Explanatory Statement accompanying the passage of the 1984 Act provided the following example to help illustrate the real world limitations imposed by the identical goods doctrine:

> [A] plaintiff with a Federal registration for use of the mark "Hopscotch" on typewriters might have a Lanham Act remedy against a defendant who used that mark to identify typing paper, even though the plaintiff had not registered that mark for use in connection with typing paper. Under [section 2320], however, the use of the mark "Hopscotch" on typing paper would not count as the use of a "counterfeit mark."[6]

Of course, civil remedies remain at least a theoretical option in this type of scenario. As explained further below, however, civil remedies have generally proven themselves to be wholly ineffective in terms of stopping or deterring career counterfeiters. It is this genuine lack of civil remedies when combined with the strict limits imposed by the identical goods doctrine that serves to significantly limit enforcement efforts against the more sophisticated members of the counterfeiting underworld.

B. Enforcement Problems Created by the Identical Goods Doctrine

1. Two Primary Schemes Employed By Sophisticated Counterfeiters

Based on the current law, a savvy counterfeiter can avoid criminal prosecution in one of two ways. First, the counterfeiter can evade liability by merely examining the trademark registration (a public record) and placing the counterfeit mark on goods not specifically listed in the registration (i.e., non-identical goods). A second "trick"/method often employed by sophisticated counterfeiters is to sell counterfeit versions of the marks themselves in the form of "patch sets" or medallions that can later be attached to generic merchandise and give the

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Talk, Inc., 1998 U.S. Dist. LEXIS 8231, 48 U.S.P.Q.2d 1779 (E.D. Pa. June 1, 1998)(discussing the interplay between these two definitions in civil counterfeiting cases); *Playboy Enterprises, Inc. v. Universal Tel-A-Talk, Inc.*, 1998 U.S. Dist. LEXIS 17282 (E.D. Pa. November 2, 1998)(same); *Council of Better Business Bureaus, Inc. v. Better Business Bureau of St. Louis, Inc.*, 197 F. Supp. 2d 1197 (E.D. Mo. 2002)(same).

[6] *See* 130 Cong. Rec. H12076 (October 10, 1984)(Joint Statement on Trademark Counterfeiting Legislation). *But see United States v. Petrosian*, 126 F.3d 1232, 1234 (9th Cir. 1997)("The definition of the term 'counterfeit mark' in the Lanham Act is nearly identical to the definition in section 2320, suggesting that Congress intended to criminalize all of the conduct for which an individual may be civilly liable").

appearance of a genuine product. The second scheme is best illustrated by the case of *United States v. Giles,* 213 F.3d 1247 (10th Cir. 2000).

In the *Giles* case, the defendant owned a business called "Fabulous Fakes" from which he sold certain items in bulk on the wholesale market. The wholesale items at issue in this case consisted of "patch sets" bearing the logo/trademark of Dooney & Bourke, a manufacturer of high quality handbags, luggage and accessories. The "patch set" consisted of a leather patch and gold medallion, (both bearing the Dooney & Bourke logo/trademark), and a leather strap used to attach the medallion to a purse or piece of luggage. Once the patch set is applied to a generic purse or piece of luggage, the article will appear to have been made by Dooney & Bourke. Giles was convicted of trademark counterfeiting, but on appeal argued that he could not be convicted because the language of 2320 requires that a defendant both traffic in goods and knowingly use a counterfeit mark on those goods. Giles argued that an individual who merely traffics in the counterfeit marks themselves, (i.e., in the form of labels, patches, medallions, etc. that are not attached to any goods), does not violate the express terms of 18 U.S.C. § 2320. The United States Court of Appeals for the Tenth Circuit agreed with Giles's analysis and set aside his conviction.

The Tenth Circuit reversed the conviction for three reasons. First, the Court determined that the "patch sets" at issue did not constitute "goods" for purposes of the statute. The Court concluded that "goods" were intended to be viewed as separate and distinct from the marks they carry.[7] Second, the Court determined that section 2320 does not separately prohibit trafficking in counterfeit labels, patches, medallions, etc. which are unconnected from the goods.[8] Third, the Court noted that a criminal conviction under section 2320 could only be had where a spurious mark is used in connection with goods or services for which the genuine mark is already registered and in use.[9] In the *Giles* case, Dooney & Bourke did not have a separate trademark registration for leather patches, labels or medallions nor did they sell such items separately. As such, the Court held that criminal liability could not attach to the defendant's activity. In closing, the Court noted the need to clearly define the scope of criminal conduct intended to be covered by a particular statute.[10]

For purposes of grammatical convenience, counterfeiters who engage in either of the two primary schemes referenced above will be referred to collectively as "creative counterfeiters."

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[7] *See United States v. Giles,* 213 F.3d 1247, 1249 (10th Cir. 2000)(referring to 18 U.S.C. § 2320(e)(1) which defines, in part, a counterfeit mark as a "spurious mark that is *used in connection with goods*").

[8] *Id.* at 1251 ("In order for the government to prevail the statute must prohibit trafficking in counterfeit labels such as the patch sets. Section 2320 does not contain such a prohibition. Another criminal provision makes it illegal to traffic in counterfeit labels for specific products such as records, computer programs, and motion pictures. *See* 18 U.S.C. § 2318.").

[9] *See id.* at 1251.

[10] *Id.* at 1253. The *Giles* Court, in a footnote, noted that "trafficking in counterfeit labels could expose a defendant to liability as an aider and abetter in the substantive offense." *See id.* at 1251 n.6 (citing 18 U.S.C. § 2). In *Giles,* the government did not make this argument and therefore the Court did not rule on the issue. For a recent case that distinguishes *Giles* on this issue see *United States v. Guerra*, 293 F.3d 1279 (11th Cir. 2002).

Over the years, as their operations have become more sophisticated, creative counterfeiters have successfully exploited these loopholes in the enforcement scheme and continue to use them to unfairly capitalize on the good will and hard earned reputations of legitimate trademark owners, especially owners of famous marks.

2. Civil Remedies are not a Viable Option

Some practitioners/critics will, of course, point to the availability of civil remedies as one means of combating creative counterfeiters. Potential civil remedies include a traditional infringement or civil counterfeiting claim under 15 U.S.C. § 1114 or, assuming the counterfeiter exploits a famous mark, a dilution claim pursuant to 15 U.S.C. § 1125(c). Any "argument" that civil remedies are a viable option, however, is flawed in three respects. First, it assumes a successful case of confusion or dilution can necessarily be made. Second, it ignores the fact that even the wealthiest trademark owners simply cannot afford to discover, investigate and sue everyone involved in counterfeiting operations. Indeed, pursuing even a mere fraction of those engaged in such illegal operations would require the expenditure of significant financial resources easily measured in the millions of dollars. Finally, the argument is usually offered without recognition or discussion of the practical limits of civil enforcement against creative criminal counterfeiters. As evidenced below, the practical realities of how creative counterfeiters typically operate preclude the possibility of successful civil enforcement.

Modern day counterfeiting networks are highly sophisticated and organized and often transitory in nature. They are well aware of nuances in the application of the law and know how to exploit them to evade even the most aggressive enforcement efforts. Trademark owners, i.e., legitimate brand owners, are simply not dealing with the traditional trademark infringement case involving a quasi-legitimate company/defendant that conducts business above ground and over the table and whose assets are genuine and attachable. While it may not have the resources to pursue civil remedies in all traditional infringement cases, the trademark owner at least has the incentive to do so. Unfortunately, creative counterfeiters, even when discovered, provide no such incentive.

Additionally, manufacturers and distributors of counterfeit goods are often transient individuals or illegal immigrant peddlers; others routinely assume fictitious identities. Upon notice of a lawsuit, counterfeiters can move merchandise, hide assets and equipment, switch manufacturing locations, destroy evidence, or simply disappear without a paper trail. Just finding an identifiable defendant against whom to initiate legal proceedings can prove quite troublesome. To complicate matters further, many defendants, assuming one can be found, are often judgment proof. They operate primarily as cash enterprises, lease manufacturing equipment from third parties and generally do not maintain reliable paperwork or business records upon which a court could ascertain the true extent of damages. The counterfeit goods, assuming they are even found and seized, may be the most valuable asset recovered. Unfortunately, many counterfeiters, even if successfully sued and ultimately forced to pay damages, regard civil sanctions as merely the cost of doing business and their operations continue unimpeded.[11] Finally, documented links between counterfeiting and organized crime[12]

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[11] *See* S. Rep. No. 98-526, at 5 (1984), *reprinted in* 1984 U.S.C.C.A.N. 3627, 3631 which noted:

and/or terrorist organizations[13] leave many trademark owners wary of aggressively pursuing at least some counterfeiters. It is this lack of genuine civil enforcement alternatives that is often

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> Although the Lanham Act provides for civil penalties for all forms of trademark infringement, including intentional trafficking in known counterfeits, penalties under that Act have been too small, and too infrequently imposed, to deter counterfeiting significantly. Indeed, many counterfeiters view potential civil penalties simply as a cost of doing their illegal business - a cost they can well afford, given the enormous profits to be made by capitalizing on the reputations, development costs, and advertising efforts of honest manufacturers at little expense to themselves.

See id. The Department of Justice's own prosecution guidelines for intellectual property crimes also recognize the limits of civil enforcement. A copy of the relevant portions of these guidelines can be found at: http://www.usdoj.gov/criminal/cybercrime/ipmanual/06ipma.htm (see sections VI.A.1.c. and VI.A.3).

[12] With respect to organized crime, trademark counterfeiting is a predicate offense under the federal RICO statute. *See* 18 U.S.C. § 1961. The federal money laundering statutes similarly include trademark counterfeiting among the list of crimes that constitute the type of "specified unlawful activity" necessary for conviction under these statutes. *See* 18 U.S.C. §§ 1956-57; Michael Coblenz, *Intellectual Property Crimes,* 9 Alb. L.J. Sci. & Tech. 235, 298-306 (1999)(discussing the RICO statute and its relations to cases involving patterns of intellectual property theft); George W. Abbott, Jr. and Lee S. Sporn, Trademark Counterfeiting § 1.03[B] (2002)(discussing the links between organized crime and counterfeiting). *See also* Erika Martinez & Marsha Kranes, *Knockoffs Knocked Out,* New York Post, May 10, 2001 (discussing the seizure of a stash of fake goods valued at over $125 million in a building that contained secret tunnels, vaults, and trapdoors); Josh White, *Pa. Man Admits Internet Conspiracy,* Washington Post, February 28, 2002, at B2 (discussing the 46 month prison sentence of a man who lead an international piracy ring -- known by the name "DrinkorDie" -- responsible for distributing software, games and movies; the group consisted of over 60 members from numerous countries); *Warez Leader Sentenced to 46 Months,* Department of Justice Press Release, May 17, 2002, available at http://www.cybercrime.gov/sankusSent.htm (discussing same); *Member of "DrinkorDie" Warez Group Sentenced to 41 Months,* Department of Justice Press Release, July 2, 2002, available at http://www.cybercrime.gov/ob/Pattanay.htm (discussing the sentencing of another member of the "DrinkorDie" conspiracy); William Glaberson, *6 Are Charged With Selling Millions of Counterfeit Marlboros,* The New York Times, February 21, 2003, at B3 (discussing charges against six men for importing over 35 million counterfeit cigarettes into New Jersey ports over a two year period); John Marzulli, *Fake Marlboro Men Busted in Smuggling Ring,* Daily News (New York), February 21, 2003, at 37 (same); *Importers of 35 Million Counterfeit Marlboro Cigarettes from China and Distributors on Indian Reservation Charged with Smuggling and Trafficking in Counterfeit Goods,* Department of Justice Press Release, February 20, 2003, *available at* http://www.usdoj.gov/usao/nye/pr/2003feb20.htm (same and noting that some of the defendants were also charged with trafficking in counterfeit batteries). *See also* IACC Facts on Fakes Document, *available at* http://www.iacc.org/teampublish/uploads/factsupdated.pdf (providing more examples of links between organized crime and counterfeiting).

[13] For example, "Operation Green Quest" -- a multi-agency task force established by the Treasury Department and aimed at identifying, targeting and dismantling the terrorist financial infrastructure – has specifically recognized counterfeit merchandise schemes as a source of terrorist funding. *See* Dean Boyd, *Operation Green Quest Targets Terrorist Finances,* U.S. Customs Today, November 2001, *available at* http://www.customs.ustreas.gov/xp/CustomsToday/2001/November/custoday_quest.xml. To view a government brochure explaining Operation Green Quest see http://www.ustreas.gov/rewards/pdfs/Green_Quest_Brochure.pdf. *See also Feds Track Counterfeit Goods Sales,* The Associated Press, *available at* http://abcnews.go.com/wire/US/ap20021024_151.html (October 24, 2002)(noting that counterfeit operations in Paraguay tri-border region may have been used to raise money to support terrorist operations and groups); Larry Rother, *South America Region Under Watch for Signs of Terrorists,* The New York Times, December 15, 2002, at 32 (same); *Patterns of Global Terrorism 2001,* U.S. Department of State, May 21, 2002 (Latin America section), *available at* http://www.state.gov/s/ct/rls/pgtrpt/2001/html/10246.htm (noting that the presence pirated goods have long been associated with this region and also noting the recent influx of terrorist organizations); *Patterns of Global Terrorism 2000,* U.S. Department of State, April 30, 2001, *available at*

fatal to a trademark owner's efforts to meaningfully confront the counterfeiting epidemic that exists today. The situation obviously worsens when the counterfeiters cannot be prosecuted criminally.

3. Restrictive Identification/Description Rules of USPTO Add to the Problem

It should also be noted that the identification of goods system employed by the United States Patent & Trademark Office (USPTO) serves to exacerbate the creative counterfeiting problem by requiring very specific identifications in applications. It is a basic tenet of American trademark law that a person or business entity cannot obtain a trademark registration without first identifying the goods or services that will be used in connection with the mark. Few lawmakers it seems, however, appreciate the impact the current identification scheme has with respect to ultimately enforcing the rights that accompany a valid trademark registration.[14]

Comprehensive identification guidelines detailing USPTO policy are contained in Chapter 1400 of the Trademark Manual of Examining Procedure.[15] Based on a reading of this

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http://www.state.gov/s/ct/rls/pgtrpt/2000/2437.htm (noting the arrest of Ali Khalil Mehri, a fund raiser for Hezbollah and large distributor of pirate CDs)(full text of the 2000 report is available at http://www.state.gov/s/ct/rls/pgtrpt/2000/); Jeffrey Goldberg, *In the Party of God; Hezbollah Sets Up Operations in South America and the United States,* The New Yorker, October 28, 2002, at 75 (also noting the case of Ali Khalil Mehri); Kathleen Millar, *Financing Terror,* U.S. Customs Service Monthly Newsletter, November 2002, available at http://www.customs.gov/xp/CustomsToday/2002/November/interpol.xml (noting that illegal scams like counterfeiting help benefit groups like Al Qaeda, Hamas, Hezbollah and the Irish Republican Army); John Mintz & Douglas Farah, *Small Scams Probed for Terror Ties,* Washington Post, August 12, 2002, at A1(reporting that a t-shirt counterfeiting operation that generated millions of dollars was run by the followers of Sheik Omar Abdel Rahman – a blind cleric who was sentenced to 240 years in prison for plotting to bomb New York City landmarks); James Nurton, *Why Counterfeiting is Not So Harmless,* Managing Intellectual Property, September 2002, at 43 (reporting that a raid of a souvenir shop in mid-town Manhattan led to the seizure of a suitcase full of counterfeit watches and the discovery of flight manuals for Boeing 767s, some containing handwritten notes in Arabic); *Al-Qa'idah Trading in Fake Branded Goods,* BBC International Monitoring Reports, September 11, 2002, *available in* LEXIS, News and Business Library, News Group File (reporting on seizure of a shipment of fake goods by Danish authorities with suspected ties to Al Qaeda); *Festive Fakes Helping Al-Qaida,* Daily Post (Liverpool), December 13, 2002, at 11; Lenore Taylor, *Big Business Targets Terrorist Pirates,* Australian Financial Review, January 29, 2003, at 9; John von Radowitz, *Fake Internet Goods 'Linked to Terrorists',* Press Association, June 25, 2002 (stating that recovered Al Qaida training manuals revealed that the organization recommends the sale of fake goods as one means to raise funds); Willy Stern, *Why Counterfeit Goods May Kill,* Business Week, September 2, 1996, at 6 (reporting that the FBI investigated the link between the sale of counterfeit goods in New York City and the terrorist who planned the 1993 World Trade Center bombing); IACC Facts on Fakes Document, *available at* http://www.iacc.org/teampublish/uploads/factsupdated.pdf (providing additional examples).

[14] Indeed, scholarly literature on the subject of goods identification and/or classification is almost nonexistent. Two such articles include: Daniel L. Skoler, *Trademark Identification - - Much Ado About Something?,* 76 Trademark Rep. 224 (1986) and Jessie N. Marshall, *Classification of Services Under the International(Nice) Agreement,* 82 Trademark Rep. 94 (1992).

[15] Section 1402 details accepted USPTO practices and policies concerning the classification and identification of goods and services. As one commentator stated, the provisions of the T.M.E.P. "interweave case law, policy rationale, and specific instructions on evaluation, preparation and modifications of acceptable ID's." *See* Daniel L. Skoler, *Trademark Identification - - Much Ado About Something?,* 76 Trademark Rep. 224, 233 (1986). The Manual was recently updated and a new third edition of the publication was released in January of 2002. In the prior edition, the identification and classification rules were discussed in sections 804 and 1401. Foreign

text, a few general rules emerge with respect to drafting acceptable identifications. First, "the identification of goods or services must be specific, definite, clear and concise."[16] Next, the identification should employ common or ordinary names and terminology that would be understood by the average person among the general population. Third, highly technical or esoteric verbiage that may require in-depth knowledge of a particular industry should be avoided.[17] Finally, when drafting identifications, specific as opposed to overly inclusive/indefinite terms are preferred. For instance, the linking terms "namely" and "consisting of" are preferred when drafting an identification that may require greater particularity.

Obviously, the high level of specificity required by the USPTO prevents trademark owners from using broader descriptions that could increase the scope of protection (especially in the criminal arena where enforcement is limited to those goods specifically listed in the registration). It is not unheard of for section 2320 defendants to argue for dismissal because they were not selling counterfeit purses (the item listed in the registration), but instead were selling "satchels" or "tote bags." Counterfeiters should not be allowed to avoid prosecution based on highly technical semantic distinctions and/or because, when indicted, they suddenly decide to use synonyms to describe their unauthorized products. Such arguments border on the absurd.

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applications based on section 44 of the Lanham Act (15 U.S.C. § 1126) must comply with the same specificity and identification standards that govern domestic applications. This is true even if the foreign registration upon which the United States application is based contains an overly broad identification. *See* T.M.E.P. § 1402.01(b).

The identification scheme and rules should not be confused with the notion of classification (i.e., classifying goods and services) and the *Nice Agreement Concerning the International Classification of Goods and Services for the Purposes of Registration of Marks*. The Nice Classification however was only developed to *classify* goods and services, as opposed to *identifying* those specific goods and services that will be used in connection with the trademark and that will ultimately be listed on the registration. Indeed, Article 2(1) clearly states that "the Classification shall not bind the . . . . [member States] in respect of either the evaluation of the extent of the protection afforded to any given mark or the recognition of service marks."

The Nice Classification was officially adopted by the United States as its system of classification on September 1, 1973. *See* T.M.E.P. § 1401.02(b)(citing 911 TMOG 210 (June 26, 1973)). The text of the classification is contained in both the Code of Federal Regulations and the Trademark Manual of Examining Procedure. *See* 37 C.F.R. § 6.1; T.M.E.P. § 1401.02(a). The international classification applies, for all statutory purposes, to all applications filed on or after September 1, 1973, and to registrations issued on the basis of such applications. The full text of this agreement can be found at: http://www.wipo.int/classifications/fulltext/nice/ennnic.htm. More general information about the agreement can be found at: http://www.wipo.org/classifications/en/nice/about/nice.html

[16] *See* T.M.E.P. § 1402.01.

[17] *See* T.M.E.P. § 1402.01. As one former Assistant Commissioner described it in a particular case:

> [A]n identification of goods should be brief, clear and concise; it should identify the goods by their common, ordinary name so that the average person would recognize what they are; and it should not be written in technical high-sounding verbiage.

See California Spray-Chemical Corp. v. Osmose Wood Preserving Co. of America, Inc., 102 USPQ 321, 322 (Comr. 1954).

C. Serious Harm Caused by this Problem Lacks an Effective Remedy

Given this analysis, it is easy to see how, under the present enforcement scheme, the law leaves trademark owners without an effective remedy. As noted above, civil enforcement is, for a variety of reasons, generally unavailable and ineffective. Furthermore, creative counterfeiters can avoid criminal prosecutions by simply using the mark on goods not listed in the registration (i.e., non-identical goods) or by engaging in "Giles-like" activity.[18] It is important to remember that counterfeiters are nothing more than keen criminal opportunists who will continue to exploit these loopholes until the threat of prosecution causes them to cease their activities. While their actions may allow them to sidestep the true intent of the law, this does not mean the actions of creative counterfeiters should be legitimized or accepted. To wit, if creative counterfeiters truly believed their operations were legitimate and fair, then they would file an application for the same exact trademark, just for use in connection with non-identical goods and/or patch sets. To do so, however, would force creative counterfeiters to reveal their true identities and could also subject them to opposition proceedings before the Trademark Trial and Appeal Board.[19]

The fact that legitimate trademark owners may choose not to produce and offer the different goods sold by creative counterfeiters does not mean trademark owners and consumers are left unharmed. The ills of counterfeiting are well documented and wide ranging. First, counterfeiters destroy the important benefits of brand equity. The selling power of any mark depends upon the uniqueness or singularity of the mark. The unauthorized use of the mark by counterfeiters on a wide array of products, even non-competing products, slowly destroys a mark's distinctive character, commercial appeal and overall value. Next, a trademark owner's reputation is further tarnished when they are inevitably blamed for the inferior quality of the fake merchandise that often poses a real threat to the public health and safety.[20] Finally, consumers

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[18] *See supra* Part B.1, nn.7-10 and accompanying text (discussing the case of *United States v. Giles,* 213 F.3d 1247 (10th Cir. 2000)).

[19] *See* 15 U.S.C. § 1063 and 37 C.F.R. §§ 2.101–2.107 (regulations governing trademark opposition proceedings).

[20] *See* George W. Abbott, Jr. and Lee S. Sporn, Trademark Counterfeiting § 1.03[C] (2001); 1984 U.S.C.C.A.N. 3627, 3630-31 (1984)(S. Rep. No. 98-526)(acknowledging that the "damage done by counterfeiting often goes beyond economic injury" and providing examples). Pharmaceutical products, alcohol, aircraft parts, and infant formula are just a few of the counterfeit products that pose real dangers to unsuspecting consumers. *See* Ridgely Ochs, *Sounding Alarm on Counterfeit Drugs,* New York Newsday, June 12, 2002, at 6 (discussing recent charges by New York District Attorney relating to the importation and sale of counterfeit Viagra; some of the fake pills were smuggled into the United States in stereo speakers and stuffed toys); *Fighting the Fakers*, The Engineer, April 26, 2002, at 16 (noting that in 2001, illicit vodka, killed 60 people in Estonia and also noting that the World Health Organization estimates that counterfeit drugs account for ten percent of all pharmaceuticals); *China's Killer Headache: Fake Pharmaceuticals,* Washington Post, August 30, 2002 (according to the Shenzhen Evening News -- a government owned newspaper -- approximately 192,000 people died in China in 2001 because of fake drugs); Douglas Pasternak, *Knockoffs on the Pharmacy Shelf, Counterfeit Drugs are Coming to America,* U.S. News & World Report at 26 (June 11, 2001)(reporting that, according to the WHO, 16% of counterfeit drugs contain the wrong ingredients, 17% contain incorrect amounts of the proper ingredients and 60% have no active ingredients whatsoever); Thanassis Cambanis, *Fancy Labels, Cheap Vodka Don't Mix,* The Boston Globe, May 2, 2002, at B1 (reporting on a 2002 federal indictment in which U.S. Customs officials seized 59,000 bottles of counterfeit vodka in a Massachusetts warehouse; the counterfeit vodka was imported from a former Soviet republic). The FAA

and society as a whole are also injured as a result of the actions of counterfeiters, (even those consumers who knowingly purchase fake goods), as the proceeds from counterfeit sales are often funneled to organized crime syndicates and even terrorist groups.[21]

D. Still in Search of a Solution

It should be evident at this point that the current criminal counterfeiting statute does not adequately serve the needs of trademark owners. The current statute and overall enforcement scheme has failed to keep pace with the slick and underhanded practices of creative counterfeiters.[22] Due to the proven inadequacy of civil remedies, there exists a need for criminal protection against the actions of creative counterfeiters. Recognizing the need to effectively deal with those individuals who operate at the edge of established trademark law is far from a novel concept. One commentator recognized this problem over seventy-five years ago when he aptly noted:

> Trademark pirates are growing more subtle and refined. They proceed circumspectly, by suggestion and approximation, rather than by direct and exact duplication of their victims' wares and marks. The history of important trademark litigation within recent years shows that the use of similar marks on *non*-competing goods is perhaps the *normal* rather than the exceptional case of infringement.[23]

Apparently, not much has changed since the early days of the twentieth century. This being the case, now might be an appropriate time for governments and policy makers to be more flexible and start thinking about criminal enforcement outside the strict categories of goods and services for which the mark is registered. Expanding the scope of the criminal statute (18 U.S.C. § 2320) to incorporate penalties for creative counterfeiters will help to further the Act's central policy of protecting trademark holders' rights.[24] Perhaps the fear of criminal prosecution and

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estimates that 2% of the $26 million airline parts installed each year are counterfeit (that equals 520,000 parts). *See* Billy Stern, *Warning! Bogus Parts Have Turned Up in Commercial Jets. Where's the FAA?,* Business Week, June 10, 1996, at 90; *Fugitive Who Sold Counterfeit Baby Formula Convicted of Federal Criminal Charges,* Department of Justice (Press Release)(August 9, 2002), *available at* http://www.cybercrime/gov/mostafaConvict.htm; IACC Facts on Fakes Document, *available at* http://www.iacc.org/teampublish/uploads/factsupdated.pdf (providing more examples).

[21] *See supra* notes 12-13 and accompanying text.

[22] *See* Frank I. Schechter, *The Rational Basis of Trademark Protection*, 40 Harv. L. Rev. 813, 813 (1927) (recognizing that theories of trademark protection must "reflect a consciousness of the need for breadth and liberality in coping with the progressive ingenuity of commercial depravity").

[23] *See* Frank I. Schechter, *The Rational Basis of Trademark Protection*, 40 Harv. L. Rev. 813, 825 (1927).

[24] *See United States v. Hon,* 904 F.2d 803, 806 (2d Cir. 1990). The *Hon* Court provided the following analysis regarding the central purposes of the Act:

> Congress was concerned not only that "trademark counterfeiting . . . defrauds purchasers, who pay for brand-name quality and take home only a fake," but also that "counterfeiters [can earn] enormous profits . . . by capitalizing on the reputations, development costs, and advertising

stiff penalties will serve to deter at least some creative counterfeiters. To that end, Congress should recognize the importance of modifying section 2320 to include protection against creative counterfeiters and focus its efforts on enacting legislation that will close the two "loopholes" identified in this paper.[25]

E. Proposed Amendments

1. Protection Against "Giles-Like" Activity (Patch Sets, Labels, Etc.)

In order to better protect famous trademark owners, the statute must, at the very least, be amended to prohibit trafficking in counterfeit labels/patches/medallions/etc. Currently, section 2320 does not prohibit such activity.[26] This amendment would serve to adequately inform Mr. Giles, and other creative counterfeiters like him, that Congress intends section 2320 to cover trafficking in counterfeit labels. In this sense, trademark owners would only be obtaining protection that is already afforded to copyright owners under 18 U.S.C. § 2318. Section 2318 prohibits trafficking in counterfeit labels affixed to or designed to be affixed to phonorecords, copies of computer programs, documentation or packaging for computer programs, or copies of motion pictures or other audiovisual works.[27] To achieve this parity among intellectual property

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efforts of honest manufacturers at little expense to themselves." *S.Rep. No.* 98-526, *supra*, at 4-5, *reprinted in* 1984 U.S.C.CA.N. at 3630-31.

> Courts have widely agreed that 18 U.S.C. § 2320 is "'not just designed for the protection of consumers. [It is] likewise fashioned for the protection of trademarks themselves and for the prevention of the cheapening and dilution of the genuine product.'"
>
> In the Lanham Act context, we have stated, "the trademark laws are designed not only to prevent consumer confusion but also to protect 'the synonymous right of a trademark owner to control his product's reputation.'"
>
> Thus an interpretation of section 2320's confusion requirement to include the non-purchasing public advances the important purpose underlying the trademark laws of protecting the trademark owner's investment in the quality of the mark and his product's reputation, one that is independent of the goal of preventing consumer deception.

Id. (citations omitted).

[25] *See supra* Part B.1.

[26] *See supra* Part B.1, nn. 7-10 and accompanying text (discussing the case of *United States v. Giles,* 213 F.3d 1247 (10th Cir. 2000)).

[27] *See* 18 U.S.C. § 2318(a), which reads as follows:

> (a) Whoever . . . knowingly traffics in a counterfeit label affixed or designed to be affixed to a phonorecord, or a copy of a computer program or documentation or packaging for a computer program, or a copy of a motion picture or other audiovisual work, and whoever, in any of the circumstances described in subsection (c) of this section, knowingly traffics in counterfeit documentation or packaging for a computer program, shall be fined under this title or imprisoned for not more than five years or both.

Id. See also see Michael Coblenz, *Intellectual Property Crimes,* 9 Alb. L.J. Sci. & Tech. 235, 262-66

owners, the necessary legislative draftsmanship would involve amending the definition of the term "counterfeit mark" (at section 2320(e)) to include labels, patches, medallions, etc. that consist of nothing more than a reproduction of the mark itself. One way of addressing this problem would be to amend section 2320(e)(1) by adding a third means by which prosecutors could satisfy the definition of the term counterfeit mark (there are currently two definitions, codified at sections 2320(e)(1)(A) and 2320(e)(1)(B)).[28] The third alternative for defining the term counterfeit mark could be codified as section 2320(e)(1)(C) and could read as follows:

> (C) a spurious mark –
> (i) that is identical with or substantially indistinguishable from a mark registered on the principal register in the United States Patent and Trademark Office and in use, whether or not the defendant knew such mark was so registered; and
> (ii) that is applied to or consists of a label, patch, wrapper, badge, emblem, medallion, charm, box, container, can, case, hangtag, documentation or packaging of any type or nature that is designed to be affixed to, distributed with, consist of or otherwise accompany the goods or services.

Another option would be to add a companion section to title 18 (e.g., 18 U.S.C. § 2320A) that addresses the issues of patch sets separately.

(1999)(providing an analysis of the history and purpose behind section 2318); 4 M. Nimmer & D. Nimmer, *Nimmer on Copyrights,* § 15.05[B] at 15-40 & n.55 (2002)(discussing the scope, history and purpose of section 2318).

On April 30, 2002, legislation introduced in the United States Senate sought to expand the list of offenses under section 2318 to include trafficking in "illicit authentication features" (i.e., holograms, codes, watermarks and other authentication features) and also provide civil remedies for copyright owners injured by a violation of section 2318. *See* S. 2395, 107th Cong., 2d Sess. (2002). To date, the proposed legislation has not been reintroduced in the 108th Congress.

See also Florida Man Sentenced for Selling Counterfeit Software Labels on Auction Web Sites, Department of Justice Press Release, available at <http://www.cybercrime.gov/mitchellSent.htm> (visited February 19, 2003)(United States Department of Justice Press Release concerning a recent conviction under 18 U.S.C. § 2318).

[28] *See* 18 U.S.C. § 2320(e)(1)(A)-(B), which read as follows:

(e) For the purposes of this section—
(1) the term "counterfeit mark" means—
(A) a spurious mark—
(i) that is used in connection with trafficking in goods or services;
(ii) that is identical with, or substantially indistinguishable from, a mark registered for those goods or services on the principal register in the United States Patent and Trademark Office and in use, whether or not the defendant knew such mark was so registered; and
(iii) the use of which is likely to cause confusion, to cause mistake, or to deceive; or
(B) a spurious designation that is identical with, or substantially indistinguishable from, a designation as to which the remedies of the Lanham Act are made available by reason of section 220506 of title 36;
but such term does not include any mark or designation used in connection with goods or services of which the manufacturer or producer was, at the time of the manufacture or production in question authorized to use the mark or designation for the type of goods or services so manufactured or produced, by the holder of the right to use such mark or designation;

2. Protection Against Use of Famous Marks on Non-identical Goods

Congress should also amend the statute to provide greater protection for "famous marks" by removing the burdensome requirement that the spurious mark be used in connection with identical goods or services for which the genuine mark is already registered. In practical terms, protection would only need to be extended to cover famous marks that are used on non-identical goods because famous marks are generally the only marks subject to wide scale criminal counterfeiting. Once again, this added protection could be provided by amending the current definition of counterfeit mark at section 2320(e)(1). This fourth alternative for defining the term counterfeit mark could be codified as section 2320(e)(1)(D) and might read as follows:

> (D) a spurious mark –
> (i) that is used in connection with the trafficking of goods or services; and
> (ii) that is identical with, or substantially indistinguishable from a famous mark that is registered on the principal register in the United States Patent and Trademark Office and in use, regardless of the goods or services or class(es) of goods or services for which the famous mark is registered, and regardless of whether or not the defendant knew such mark was so registered and famous.

In determining whether a mark was famous the court could consider data, testimony, documentation and other evidence pertaining to factors similar to those listed in 15 U.S.C. § 1125(c)(1)(A)-(G).[29] One additional factor the court could consider would be the record of successful enforcement of rights in the mark, in particular, the extent to which the mark has been

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[29] Section 1125(c) reads, in relevant part, as follows:

(c) Remedies for dilution of famous marks.

(1) The owner of a famous mark shall be entitled, subject to the principles of equity and upon such terms as the court deems reasonable, to an injunction against another person's commercial use in commerce of a mark or trade name, if such use begins after the mark has become famous and causes dilution of the distinctive quality of the mark, and to obtain such other relief as is provided in this subsection. In determining whether a mark is distinctive and famous, a court may consider factors such as, but not limited to—

(A) the degree of inherent or acquired distinctiveness of the mark;
(B) the duration and extent of use of the mark in connection with the goods or services with which the mark is used;
(C) the duration and extent of advertising and publicity of the mark;
(D) the geographical extent of the trading area in which the mark is used;
(E) the channels of trade for the goods or services with which the mark is used;
(F) the degree of recognition of the mark in the trading areas and channels of trade used by the marks' owner and the person against whom the injunction is sought;
(G) the nature and extent of use of the same or similar marks by third parties; and
(H) whether the mark was registered under the Act of March 3, 1881, or the Act of February 20, 1905, or on the principal register.

recognized as famous by courts or administrative authorities. A finding of fame by another adjudicatory body could act as a rebuttable presumption of fame in criminal cases.

Although some may view amending the federal statute in this respect as controversial, the amended statute, if enacted, would certainly not be unique in terms of providing trademark owners with increased criminal protection. A majority of the states have enacted their own criminal trademark counterfeiting statutes and many of these statutes do not restrict prosecutions to only those cases involving goods specifically identified in a state or federal registration.[30] These states include: Arizona,[31] the District of Columbia,[32] Hawaii,[33] Illinois,[34] Louisiana,[35] Maryland,[36] Massachusetts,[37] Michigan,[38] Minnesota,[39] Missouri,[40] New Jersey,[41] Oklahoma,[42] and Pennsylvania.[43] For example, the statute from the District of Columbia defines the term "counterfeit mark" as "any unauthorized reproduction or copy of intellectual property" or "intellectual property affixed to any item knowingly sold . . . without the authority of the owner of the intellectual property." The term "intellectual property", in turn, is defined as "any trademark, service mark, trade name, label, term, [etc.] . . . adopted or used by a person to identify such person's goods or services[.]"[44] In its criminal counterfeiting statute, the state of Minnesota defines the term "counterfeit mark" as "any unauthorized reproduction or copy of intellectual property" or "intellectual property affixed to any item without the authority of the owner of the intellectual property."[45] The term "intellectual property" is defined simply as "any

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30 *See* George W. Abbott, Jr. and Lee S. Sporn, Trademark Counterfeiting § 4, app. 4-2 (2001)(providing citations to and analyses of the state criminal trademark counterfeiting statutes).

31 *See* Ariz. Rev. Stat. § 44-1453 (2002).

32 *See* D.C. Code Ann. §§ 22-901 & 22-902 (2002).

33 *See* Haw. Rev. Stat. § 708-875 (2002).

34 *See* Illinois Compiled Stat. Ann. §§ 1040/1 -- 1040/9 (2002).

35 *See* La. Rev. Stat. Ann. § 229 (2002).

36 *See* Md. Crim. Law Code Ann. § 8-611 (2002)(formerly Article 27, § 48A).

37 *See* Mass. Gen. Laws Ann. Ch. 266, § 147 (2002).

38 *See* Mich. Comp. Laws § 750.263 (2002).

39 *See* Minn. Stat. § 609.895 (2002).

40 *See* Mo. Rev. Stat. § 570.103 (2001).

41 *See* N.J. Stat. Ann. § 2C:21-32 (2002).

42 *See* 21 Okla. Stat. §§ 1990.1 & 1990.2 (2003).

43 *See* Pa. Cons. Stat. § 4119 (2002).

44 *See* D.C. Code Ann. §§ 22-901(1) (2002).

45 *See* Minn. Stat. § 609.895(b)(1)-(2).

trademark, service mark, or trade name."[46] Thus, in these states, trademark owners are provided with the benefits of criminal protection irrespective of the goods or services offered in connection with the use of a counterfeit mark.

The concept of protecting famous or well-known marks, irrespective of the goods or services for which a mark is used or registered, has also been endorsed at the international and/or multilateral level. In 1999, the World Intellectual Property Organization (WIPO) and the Assembly of the Paris Union for the Protection of Industrial Property jointly adopted the Joint Recommendation Concerning Provisions on the Protection of Well-Known Marks ("Joint Recommendation").[47] The provisions of the Joint Recommendation were adopted to serve as guidelines to help Member States of WIPO and the Paris Convention when enacting measures relating to the protection of well-known marks. Article 4(1)(b) of the Joint Recommendation lists those scenarios where protection for well known marks could be provided irrespective of the goods or services used in connection with the counterfeit mark.[48] Specifically, it provides that, irrespective of the goods or services for which the conflicting counterfeit mark is used or registered, the counterfeit mark shall be deemed to be in conflict with a well-known mark when one of three conditions is satisfied:

> (i) the use of [the counterfeit] mark would indicate a connection between the goods and/or services for which the [counterfeit] mark is used, is the subject of an application for registration, or is registered, and the owner of the well-known mark, and would be likely to damage his interests;[49] [or]

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[46] *See* Minn. Stat. § 609.895(d).

[47] *See* http://www.wipo.org/about-ip/en/development_iplaw/pub833.htm.

[48] Instead of using the term "counterfeit", the text of the Joint Recommendation actually employs the rather cumbersome phrase "where the [conflicting] mark, or an essential part thereof, constitutes a reproduction, an imitation, a translation or a transliteration of a well-known mark[.]" *See Joint Recommendation,* Art. 4(1)(b). Although not explicit, this language would certainly seem to cover those cases where the conflicting mark is identical to or substantially indistinguishable from the well-known mark, and not merely infringing or confusingly similar.

[49] The International Bureau of WIPO prepared explanatory notes to accompany the Joint Recommendation. Although the explanatory notes were not adopted by the Assemblies of WIPO or the Paris Union, and are not part of the official provisions of the Joint Recommendation, they nevertheless provide helpful guidance when analyzing the scope of activities that could be prohibited under the terms of Article 4(1)(b)(i)-(iii). With respect to Article 4(1)(b)(i), the explanatory notes state:

> *Item (i).* Under this item, a connection between a well-known mark and a third party's goods or services may be indicated, for example, if the impression is created that the owner of the well-known mark is involved in the production of those goods, or the offering of those services, or that such production or offering was licensed or sponsored by him. The interests of the owner of the well-known mark could be damaged if the goods and/or services with which the connection is established have a down-market image, thereby reflecting negatively on the goodwill of the well-known mark.

See Explanatory Notes to the Joint Recommendation Concerning Provisions on the Protection of Well-Known Marks ("Explanatory Notes"), Note 4.3, *available at*

(ii) the use of that mark is likely to impair or dilute in an unfair manner the distinctive character of the well-known mark;[50] [or]

(iii) the use of that mark would take unfair advantage of the distinctive character of the well-known mark.[51]

The third condition contained in the Joint Recommendation would certainly seem broad enough to allow Member States to prohibit the activities of creative counterfeiters because they (the activities of creative counterfeiters) amount to nothing more than a "free ride on the goodwill of the well-known mark[.]"[52] The Explanatory Note accompanying the third condition provides ample support for this proposition.[53]

3. Related Amendments

The statute should also be amended to include mandatory forfeiture, destruction and restitution provisions. The present statute is severely lacking in this respect and only provides that "the United States may obtain an order for the destruction of such articles."[54]

<http://www.wipo.org/aboutip/en/development_iplaw/pub833.htm.>

50 The explanatory notes for the second condition provide:

> *Item (ii).* This item would apply, for example, if the use of a conflicting mark is likely to impair or dilute in an unfair manner the unique position of a well-known mark in the market. A further example of dilution is where the conflicting mark is used on goods or services that are of an inferior quality or of an immoral or obscene nature. The meaning of the words "in an unfair manner" implies that third-party use of a well-known mark which is not contrary to honest commercial practice (e.g., reference to a well-known mark for review or parody) does not constitute dilution.

See Explanatory Notes, Note 4.4 *available at* <http://www.wipo.org/aboutip/en/development_iplaw/pub833.htm.>

51 The explanatory notes for the third condition provide:

> *Item (iii).* The case referred to in this item differs from the cases covered by items (i) and (ii) in that no wrong connection concerning the real source of the goods and/or services is indicated (as in item (i)), and the value of the well-known mark has not diminished in the eyes of the public (as in item (ii)), but rather the use in question would, for example, amount to a free ride on the goodwill of the well-known mark for the person who uses a conflicting mark. The reference to "unfair advantage" in this item is intended to give Member States flexibility in the application of this criterion. For example, reference to a well-known mark for commercially justifiable reasons, such as the sale of spare parts, is not unfair and should, thus, be allowed.

See Explanatory Notes, Note 4.5, *available at* <http://www.wipo.org/aboutip/en/development_iplaw/pub833.htm.>

52 *See id.*

53 *See id. See also supra* n.49 (explaining the origin, purpose and authority of the Explanatory Notes).

54 *See* 18 U.S.C. § 2320(b).

An amended section 2320(b) would provide for mandatory forfeiture and destruction of articles found in the possession of the defendant that are determined to be counterfeit, regardless of the criminal culpability of the defendant. Restitution provisions similar to those found in the Economic Espionage Act[55] could also be added. Amending the statute to include mandatory forfeiture and destruction would provide trademark owners with a potent enforcement weapon already available to copyright owners under the terms of 17 U.S.C. § 506(b).[56]

E. Conclusion

The fame and familiarity of well known marks will continue to make them targets of sophisticated counterfeiting schemes that slowly erode the value of the targeted mark and, as detailed herein, hurt the general public as well. The best deterrent to counterfeiting is strong criminal legislation that includes prison sentences and deprives the counterfeiters of the merchandise, profits and other property that allows them to continue operations unimpeded. Unless the statute is amended to lessen the impact of the identical goods doctrine and provide for mandatory forfeiture and destruction, honest trademarks owners will continue to be exploited by the activities of creative counterfeiters.

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[55] *See* 18 U.S.C. §§ 1831 – 1839 (making the theft of trade secrets subject to federal criminal penalties). The forfeiture provisions are codified at 18 U.S.C. § 1834 and read, in relevant part, as follows:

> (a) The court, in imposing sentence on a person for a violation of this chapter shall order, in addition to any other sentence imposed, that the person forfeit to the United States--
> (1) any property constituting, or derived from, any proceeds the person obtained, directly or indirectly, as the result of such violation; and
>
> (2) any of the person's property used, or intended to be used, in any manner or part, to commit or facilitate the commission of such violation, if the court in its discretion so determines, taking into consideration the nature, scope, and proportionality of the use of the property in the offense.

See 18 U.S.C. § 1834(a)(1)-(2).

[56] *See* 17 U.S.C. § 506(b), which reads as follows:

> (b) Forfeiture and destruction. When any person is convicted of any violation of subsection (a), the court in its judgment of conviction shall, in addition to the penalty therein prescribed, order the forfeiture and destruction or other disposition of all infringing copies or phonorecords and all implements, devices, or equipment used in the manufacture of such infringing copies or phonorecords.

Id. See also 17 U.S.C. § 509 (further detailing forfeiture and destruction requirements for criminal copyright violations); 18 U.S.C. § 2318(d) (ordering the destruction and forfeiture of all counterfeit labels and all articles to which counterfeit labels have been affixed or which were intended to have had such labels affixed); 19 C.F.R. § 133.52(b)(providing that "[a]rticles forfeited for violations of copyright laws shall be destroyed").

Questions for the Record Submitted to
Assistant Secretary of State E. Anthony Wayne by
Senator Patrick Leahy (#1)
Senate Committee on the Judiciary
March 23, 2004

Question:

1) Last year, as part of the Commerce-Justice-State Appropriations bill, I co-sponsored a provision that gave $2.5 million to the State Department to begin programs to address IP piracy overseas. What has the State Department done thus far to initiate such programs? How will you measure the success of those efforts? What further steps should we take to promote such initiatives?

Answer:

The State Department, our embassies and other Federal agencies whose programs will be funded out of the $2.5 million soft earmark you co-sponsored, are enthused about the opportunity to bring resources of this magnitude to bear on the issue of intellectual property enforcement. The State Department is taking very seriously the job of deciding how that money will be spent.

The money will be allocated out of the budget of State's Bureau of International Narcotics and Law Enforcement Affairs (INL), consistent with priorities derived from the annual Special 301 Report, discussions in the State-chaired interagency/industry Training Coordination Group (TCG), and

law enforcement information. Following passage of the FY 2004 budget, INL worked with the Bureau of Economic and Business Affairs (EB) to solicit proposals from agencies and embassies, and ideas from industry groups that participate in the TCG. INL and EB have spent the past several weeks reviewing over 90 proposals totaling $7.5 million in requested funding, with the goal of choosing those that will have the greatest impact on the most significant problems in priority countries and regions. The State Department will soon begin consulting interested parties, including the Appropriations Committee, on final recommendations, and will begin obligating the funds following these consultations.

The State Department will ensure that a written assessment of program effectiveness will be made a part of the responsibility of all U.S. government agencies and U.S. Missions that are tasked with carrying out projects. We will use these assessments, as well as feedback from other US government agencies, private industry, host governments, NGOs and other sources, to help us measure the success of this effort. In designing our project proposals, we have solicited suggestions on best training and technical practices from our overseas missions, industry and USG

intellectual property agencies to ensure we provide the most effective assistance.

The State Department believes that training, under the right circumstances, can help a struggling government to do the right thing on IP, and so we welcome Congress' interest and support of the Administration's efforts on behalf of U.S. IP owners.

However, training programs cannot substitute for political will or human and other resources, or overcome problems associated with underpaid law enforcement officials, corruption, etc. In addition, the United States - and our taxpayers' money - cannot solve the global IP problem alone. We are reemphasizing efforts to coordinate with the EU, Japan and other countries whose industries and citizens are suffering at the hands of counterfeiters and pirates. Through the EU accession process, many formerly problematic countries are required to meet European mandatory standards that will have a positive effect on the IP climate. Japan has finally awakened to the threat that China and other Asian sources of pirated and counterfeit products pose to its IP industries, and has begun exerting greater bilateral pressure on those governments. Some countries, such as Jordan,

have understood what there is to gain through strong IP laws, and are voluntarily creating environments that welcome foreign investment in IP-based industries. Many, many others refuse to follow, despite their international obligations. We are faced with a very complicated problem for which there are no fast or easy solutions.

The State Department will continue to work with other agencies, Congress and industry to expand and improve anti-piracy efforts and to give the issue high priority in our foreign policy agenda.

Questions for the Record Submitted to
Assistant Secretary of State E. Anthony Wayne by
Senator Patrick Leahy (#2)
Senate Committee on the Judiciary
March 23, 2004

Question:

2) Is the State Department able to quantify the amount of IP piracy that takes place overseas, especially in non-OECD countries? What impact does such piracy have on our country's relationships with those countries?

Answer:

The State Department is not able to quantify accurately the amount of IP piracy that takes place overseas because we do not have access to the information needed to make such an assessment. We and other agencies that deal with IP issues generally rely on market estimates provided by industry groups and enforcement statistics provided by U.S. and foreign law enforcement agencies.

When a country's IP piracy rate reaches a level where it becomes a significant problem in the estimation of industry and U.S. government agencies, we make that issue part of our bilateral relations agenda. This means we raise the issue more often and at more senior levels in meetings; we devote more public diplomacy resources to increasing awareness of the

problem; and we seek to make that country a higher priority in our allocation of IP training funds. Good examples of this are China, Russia and Pakistan, where IP issues are now at the top of the agenda and are regularly raised with their governments by our ambassadors and senior State Department officials in Washington. This additional diplomatic pressure can be extremely important in convincing unwilling governments to take needed steps in the IP area.

Questions for the Record Submitted to
Assistant Secretary of State E. Anthony Wayne by
Senator Patrick Leahy (#3)
Senate Committee on the Judiciary
March 23, 2004

Question:

3) In your testimony, you noted that there are already tools in place to provide trade sanctions for countries that continue to refuse to respect Intellectual Property laws. But you note that these devices are not favored. You also note that Ukraine has suffered sanctions but you do not mention whether China has been the subject of any such measures. What specific measures have we taken against China as a result of their leniency toward pirates, and is there some sanction program we could institute that would be more useful than the ones we have now? Are there any other tools that the State Department would find useful in addressing IP piracy?

Answer:

The United States briefly imposed Special 301 trade sanctions on China in 1995 as a result of unresolved intellectual property concerns. These sanctions were lifted almost immediately after imposition because China signed a bilateral IPR agreement with the United States. The United States has continued to monitor China's performance under this agreement and has applied pressure through other fora, such as our Embassy and the Joint Commission on Commerce and Trade, to seek better results in the IP area.

It appears that the additional political and diplomatic pressure placed on China is getting Beijing's attention. In the just completed Joint Commission on Commerce and Trade (JCCT), China committed to significantly reduce IP infringement levels by: 1) increasing penalties for IP violations by the end of 2004; 2) cracking down on violators by increasing customs enforcement and conducting nation-wide enforcement actions against piracy and counterfeiting; 3) increasing penalties for IP violations; 4) improving protection of electronic data by ratifying the WIPO Internet treaties as soon as possible; and 5) extending the ban on use of pirated software to include local governments. They have also agreed to establish an intellectual property rights working group under the JCCT to consult and cooperate on the full range of issues described in China's IP action plan. We will continue to follow China's progress in implementing these commitments.

There remains a wide divergence of views, including among U.S. industry groups, as to whether imposing sanctions on China will make matters better, or worse. Another factor that needs to be taken into account is China's status as a WTO member and how any proposed sanctions would fit into that framework. Given these factors, as well as the recent movement

shown by Beijing in the JCCT, it is not clear that there is currently a need to institute a new sanction program.

As far as tools needed to fight piracy, fully-staffed and trained embassies and State Department offices, equipped with modern technology, are our best resources in addressing IP issues. Our requests to Congress will continue to reflect the level of funding we believe is needed to carry out these efforts.

Questions for the Record Submitted to
Assistant Secretary of State E. Anthony Wayne by
Senator Patrick Leahy (#4)
Senate Committee on the Judiciary
March 23, 2004

Question:

4) You also noted in your testimony that USTR is "working very closely with them to reach out and try to build the coalitions" to combat international Intellectual Property piracy. What specific steps have you taken to build such coalitions?

Answer:

Building coalitions to combat IP piracy is part of the everyday work that goes on in our overseas missions, particularly in those countries where piracy is a major problem. These efforts typically focus on working closely with host-country industry, artists, and media -- as well as government policy and enforcement officials -- to make the case that protection of intellectual property rights is in everyone's interest. To support these ongoing activities, the State Department launched in February 2004 an initiative to give our overseas missions better tools and information to use in building these coalitions. This includes briefing and public diplomacy materials sent to the field, and regional conferences to discuss IP topics and ways to address them. Some recent examples of coalition building efforts overseas include:

-- The U.S. Embassy in Beijing, China has now held two annual IPR Roundtables, hosted by the Ambassador, to bring together U.S. and Chinese government and business representatives to build support for increased IP enforcement efforts.

-- The U.S. Embassy in Portugal, in collaboration with the National Science Foundation and the Portuguese Luso-American Foundation, brought together researchers, businesspeople and U.S. and Portuguese government officials in 2003 to discuss issues such as the importance of IP protection to innovation and business development.

-- In 2003, our Embassy in Mexico, in cooperation with Mexico's Judicial Training Institute and the Mexican Attorney General's Office, helped organize IPR enforcement seminars, reaching over 800 Mexican judges, to increase their awareness of legal IP issues.

-- Many Embassies, such as our Mission in Poland, have worked to establish IP Committees within the local American Chamber of Commerce to serve as a forum for business and government officials to discuss IP priorities.

-- The U.S. Embassy in Korea has worked with the Korean Education Ministry to make university presidents aware of the rampant textbook piracy taking place on university campuses.

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April 16, 2004

Mr. Barr Huefner
Senate Judiciary Committee
224 Dirksen Senate Office Building
Washington, DC 20510

Dear Mr. Huefner:

I am enclosing below responses to the questions posed to Richard K. Willard at his testimony on March 23, 2004.

Question #1

In your testimony on March 23, you noted the need for the Department of Commerce to complete a study on counterfeiting. In examining this issue, I too have found that the lack of comprehensive may be hindering our understanding of this problem. Beyond the overall "size" of the problem, what type of information do you believe the Department of Commerce might be able to provide that is not currently obtainable by industry?

Answer

Understanding and measuring the impact of counterfeiting, especially product counterfeiting, must be accomplished to enable America to determine the level of adequate counter measures required to win this important economic battle. Reliable and reproducible data from a health, safety, and environmental statistics are needed to ensure complete coverage of the issue.

Job losses, tax losses, as well as estimates concerning financial support funneled to organized crime and terrorism should be generated in order to focus appropriate levels of resources against the counterfeit threat and to gauge progress. A study of this breadth and magnitude is within the appropriate province of the Commerce Department, but it is well beyond the capability of any particular private industry segments or group of segments.

Reliable and consistent definitions of the various forms of counterfeiting as well as key metrics must also be developed. Calculations of many of these data reside with customs, enforcement authorities and health authorities. Consistent definitions and metrics will spread the development of key performance indictators against which policy and resource decisions would be well grounded.

Question #2

Radio frequency identification is a burgeoning tracking technology that involves the use of tiny computer chips that can store information and respond to radio signals. The chips can be attached to physical objects and will be a useful tool in identifying, tracking and authenticating goods, which would undoubtedly assist in thwarting piracy. In fact, the FDA recently issued a report encouraging the use of RFID to prevent drug counterfeiting. Your March 23 testimony, you testified that piracy prevention is one of the "strategic benefits of the RFID chip when it is used on consumer products." You also testified that, while Gillette's plan is to initially use RFID in the "case and pallet level," Gillette is "strongly committed to making sure that consumer privacy is protected" before RFID "is implemented on a wide-scale basis at the consumer level." Has Gillette developed any policies, principles or guidelines on how it will protect consumer privacy in its use of RFID, and if so, please detail those? If not, will Gillette establish protections for consumer privacy before any use at the individual product level, e, g., in trials and tests that fall short of "wide-scale" use, but still impact individual consumers, and if so, please specify those protections?

Answer

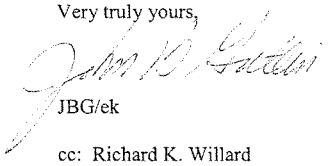
While our focus is on the pallet and case application of the RFID (currently known as "EPC"), we recognize the importance of addressing public interest in the use of the EPC at an item level. To that end, we were a founding signatory to new industry guidelines governing the use of the technology.

These guidelines, which will be effective January, 2005, mandate that consumers should be notified if a product contains an EPC tag - typically in the form of an easily recognizable logo or identifier on the packaging. Consumers should also have the option to deactivate the tag after they have purchased the product.

Companies involved in the testing and development of this new 21st Century barcode are also committed to a program of education designed to ensure consumers understand the uses and benefits associated with the EPC. The guidelines are posted on www.epcglobalinc.com

We appreciate the interest of the Senate Judiciary Committee in this vitally important matter and look forward to working with you to craft effective solutions.

Very truly yours,



JBG/ek

cc: Richard K. Willard
Senator Orin G. Hatch

U.S. Department of Justice

Office of Legislative Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

December 9, 2004

The Honorable Orrin G. Hatch
Chairman
Committee on the Judiciary
United States Senate
Washington, DC 20510

Dear Mr. Chairman:

Please find enclosed responses to the questions you submitted to Assistant Attorney General Christopher Wray, arising from his March 23, 2004, appearance before the Committee.

Please do not hesitate to call upon us if we may be of additional assistance. The Office of Management and Budget has advised us that from the perspective of the Administration's program, there is no objection to the submission of this letter.

Sincerely,

William E. Moschella
Assistant Attorney General

Enclosure

Response to Questions Submitted by Senator Patrick Leahy
Hearing before the Committee on the Judiciary
March 23, 2004
"Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions"

Follow-up Questions for the Honorable Christopher Wray

1) **I notice that the Attorney General's Annual Report from 2002 cites 81 investigative matters which resulted in 52 cases filed with regard to trafficking in counterfeit goods and services, a violation of 18 U.S.C. 2320. Given the massive problem posed by counterfeit goods, does the Department have any plans to increase the number of investigative matters relating to Intellectual Property? What resources were devoted to counterfeit goods and IP piracy investigations in 2003? What resources are being devoted this year?**

The Department, working with the FBI, will continue to work diligently to increase the number and quality of criminal IP investigations in the future.

As noted in my testimony, Attorney General Ashcroft has moved to ensure that adequate resources are available to prosecute intellectual property crimes. Over the past few years the Department has significantly increased the size of the Criminal Division's Computer Crime and Intellectual Property Section ("CCIPS"). With the strong support of Congress, the Department has expanded the number of Computer Hacking and Intellectual Property ("CHIP") Units in the United States Attorney's Offices. In October, the Attorney General announced the creation of five additional CHIP Units to supplement the network of 13 CHIP Units he established in 2001.

The past few years have marked a significant evolution in how we use the resources available to us to prosecute IP crime. We are focusing on highly structured criminal organizations that distribute massive amounts of pirated products throughout the world. Although these multi-jurisdictional and international investigations take more time and require more resources, they strike at the heart of the illegal warez community and significantly impact the illegal piracy community worldwide. Moreover, the sentences imposed in these types of cases have been significantly longer than in prior cases, producing an important deterrent effect. For example, in FY 2000, no one convicted of the IP offenses reported to Congress pursuant to 18 U.S.C. § 2320(f) received a sentence in excess of three years. Last fiscal year, however, there were ten such sentences imposed.

The Department's Criminal Division was authorized 22 positions, 13 attorneys, 22 full time equivalents and $3,058,000 to combat IP crime in FY 2003. For FY 2004, the authorized level is 22 positions, 13 attorneys, 22 full time equivalents, and $3,529,000.

The Civil Division devoted between one and two full time equivalents to enforcement of government IP rights which amounted to an annual cost of about $140,000 to $250,000 during FY2003 and FY2004. The Executive Office of United States Attorneys estimates that the United States Attorney's Office spends approximately $1 million per year on prosecuting IP cases in terms of employee salaries alone. The FBI estimates that it spent $9,764,000 in FY 2003 and $8,722,000 in FY 2004 on its Intellectual Property Rights program.

2) **What were your 10 most significant intellectual property prosecutions in the last year?**

Over the past few years, the Department has investigated and prosecuted significant cases in all areas of criminal intellectual property law. Because of the wide and varied impact each case brings to the overall enforcement effort, it is difficult to single out the 10 most significant cases. Nevertheless, we have identified the following significant cases representing all facets of criminal intellectual property crime, including trademark violations, copyright violations, and theft of trade secrets.

Operation Digital Gridlock (multiple districts): On August 25, 2004, the Department of Justice announced the first federal enforcement action taken against criminal copyright piracy on peer-to-peer networks. Federal agents executed six search warrants at five residences and one Internet service provider in Texas, New York, and Wisconsin, as part of an investigation into the illegal distribution of copyrighted movies, software, games, and music over peer-to-peer networks. Agents seized computers, software, and computer-related equipment in the searches. These search warrants are the result of Operation Digital Gridlock, a joint investigation conducted by the FBI, the Office of the U.S. Attorney for the District of Columbia, and the Justice Department's Computer Crime and Intellectual Property Section. This operation targeted illegal theft of copyrighted materials over five Direct Connect peer-to-peer networks that belonged to a group known as The Underground Network. According to unsealed search warrant affidavits, these networks required users to share a minimum of one to 100 gigabytes of computer files with other users on the network. Upon becoming a member of one of these peer-to-peer networks, each user could then download shared files from the hard drives of all other members on the network. To understand the volume that represents, just one gigabyte of information holds 250 songs. Virtually every kind of software, game, movie, and music was available for illegal downloading and distribution on these networks, from computer games and music that would cost as much as $18 to $35 dollars if purchased legitimately, to specialized software that has a retail cost in excess of $1000. Some works were available even before they could be purchased legitimately by the public, such as movies that had not yet been distributed in theaters or on DVD. The investigation in this case is ongoing.

Operation Fastlink (multiple districts): On April 21, 2004, CCIPS and the FBI led the largest international enforcement effort ever undertaken against online piracy. Operation Fastlink involved the simultaneous execution of more than 120 searches in a 24-hour period in the United States and ten foreign countries: Belgium, Denmark, France, Germany, Hungary, Israel, the Netherlands, Singapore, Sweden, and Great Britain and Northern Ireland. Over 100 individuals believed to be engaged in online piracy have been identified, many of them high-level members or leaders of online piracy release groups that specialize in distributing high-quality pirated movies, music, games and software over the Internet. More than 200 computers were seized worldwide, including over 30 computer servers that functioned as storage and distribution hubs for many of the online piracy groups targeted by this Operation. Shortly after April 21st, Spain took action against targets in that country, bringing the total number of nations involved in Operation Fastlink to 12. The level of international cooperation in Fastlink is unprecedented, and this enforcement effort, coupled with the prosecutions that will follow, sends a clear message that the Department will identify, investigate, and prosecute individuals and groups engaged in piracy regardless of their geographic location.

United States v. Barbot (E.D. Va.): In December 2003, defendant Ben John Barbot of Richmond, Virginia, pled guilty to trafficking in counterfeit goods and copyright infringement. In March 2004, Barbot was sentenced to 70 months in prison, one of the longer sentences imposed for these types of crimes, and was ordered to pay $1.7 million in restitution. Barbot distributed well over $7 million worth of counterfeit Microsoft software products through multiple Internet-based stores he created. The software products he distributed were extremely high-quality counterfeits that had been produced and imported from rogue production plants in Asia.

United States v. Breen (N.D. Ca.): On February 10, 2004, Breen was sentenced to 50 months in prison for his leadership role in Razor 1911, the oldest online piracy group dedicated to game piracy. Breen pled guilty to criminal copyright infringement and to defrauding Cisco Systems out of hundreds of thousands of dollars worth of hardware. The defendant's 50-month sentence is the longest sentence imposed to date as a result of Operation Buccaneer, an undercover investigation by the then-U.S. Customs Service (now U.S. Bureau of Immigration and Customs Enforcement), CCIPS, and the U.S. Attorney's Office for the Eastern District of Virginia, which targeted more than 40 individuals worldwide. To date, Operation Buccaneer has resulted in 38 convictions, with 30 in the United States. Prior to Operation Fastlink, Operation Buccaneer was the largest international online copyright piracy investigation. In addition to targeting the leadership of Razor 1911, Operation Buccaneer also dismantled the software piracy group known as DrinkOrDie, and netted members from a broad cross-section of other online piracy groups such as RiSC, RiSCiSO, Request To Send ("RTS"), WeLoveWarez ("WLW"), and POPZ.

United States v. Farmer (D.S.C.): In May 2003, a Columbia, South Carolina man was sentenced to seven years in prison and ordered to pay $3.5 million in restitution for trafficking in counterfeit clothing and other goods as well as engaging in money laundering. The defendant was ordered to pay $3.4 million in restitution to Nike and $110,000 to Tommy Hilfiger.

United States v. Sprague (C.D. Ca.): In April 2004, an Illinois man pled guilty to federal copyright infringement charges for reproducing and distributing more than 200 Academy Award "screeners." Sprague, who is being prosecuted under the NET Act, obtained movies such as "Master and Commander: The Far Side of the World" and "House of Sand and Fog" from a member of the Academy of Motion Picture Arts and Sciences. Sprague took the screeners in VHS tape format, digitized the films and produced illegal DVDs that were distributed to a variety of persons. Investigation of Internet postings of certain feature films revealed a new digital watermark technology embedded in the screeners which helped trace them back to the Academy member, who implicated Sprague. Sprague has engaged in this conduct for over twenty years. He is currently awaiting sentencing.

United States v. Vysochanskyy, a/k/a Kovalchuk (N.D. Ca.): On April 7, 2004, a 20-count indictment was returned by a federal grand jury in San Jose against a 26-year-old Ukranian defendant, charging him with multiple counterfeiting, money laundering, and credit card offenses arising from his Internet-based distribution of millions of dollars worth of pirated computer software and his use of an international network of intermediaries to launder the proceeds of the counterfeit sales. The defendant allegedly distributed unauthorized copies of software from Microsoft, Adobe, Autodesk, Borland, Macromedia, and others. The indictment follows the defendant's recent extradition to the United States from Thailand, where he was originally arrested in May 2003.

United States v. Gonzalez (E.D.N.Y.): In June 2003, the defendant pled guilty to distributing a copy of the motion picture "The Hulk" on the Internet, prior to its theatrical release. After obtaining a "work-print" of the movie, the defendant uploaded a digitized copy of the work-print to an Internet website chat room hosted in the Netherlands and frequented by numerous movie enthusiasts who gather there to post and trade copies of pirated movies. By uploading the movie, Gonzalez made it available to any chat room visitor, who could in turn distribute the movie across the Internet. Due to the hard work of federal prosecutors and agents, this plea was obtained just days after "The Hulk" opened in theaters around the country. The defendant, who was prosecuted under the NET Act, was ultimately sentenced to 3 years of probation, 6 months of home confinement as a condition thereof, and payment of a $2,000 fine and $5,000 in restitution.

United States v. Whitehead (C.D. Ca.): In September 2003, the U.S. obtained the first-ever jury trial conviction under the Digital Millennium Copyright Act in Los Angeles,

when a federal jury convicted the defendant of selling hardware used to illegally receive DirectTV satellite programming. Whitehead and sixteen co-conspirators were indicted on various related charges in February 2003 as part of an FBI investigation known as "Operation Decrypt." Thus far, ten defendants have been sentenced to terms of imprisonment of up to 60 months. Whitehead is currently awaiting sentencing.

United States v. Murphy (N.D. Ala.): In January 2003, an Alabama man pled guilty to twenty-eight counts of counterfeiting and pesticide misbranding charges. The defendant sold mislabeled and adulterated pesticides needed to control mosquitoes and West Nile virus to municipalities and private businesses in a number of southern and mid-western states. The defendant falsely identified the brand name of the pesticide, the manufacturer, and the active ingredients. On April 21, 2004, Murphy was sentenced to 41 months in prison and ordered to pay $45,000 in restitution.

3) **It appears that much of the counterfeit materials we are seeing in the United States is coming from overseas. What would you say are your 10 most significant seizures at our borders in the last year of counterfeit goods? How do you coordinate with Customs and others entities to improve enforcement and seizures of counterfeit materials?**

The Department works very closely with investigatory agencies, including the Bureau of Immigration and Customs Enforcement and the Federal Bureau of Investigation. Significantly, given the breadth and complexity of many of our cases, we often become involved in case development during the investigatory stage and work closely with the agents throughout the case. We meet regularly with high-level officials in the FBI Cyber Division to coordinate our law enforcement activities, and we have worked successfully with the ICE Cyber Crime Center on criminal investigations and prosecutions.

In addition to investigatory agencies, the Department works with other government agencies in a variety of contexts to address IP enforcement issues, including border control. For example, the Department's Criminal Division and the United States Patent and Trademark Office co-chair the National Intellectual Property Law Enforcement Coordinating Council ("NIPLECC"), an interagency forum for discussion and coordination of efforts among the various federal agencies with a stake in IP enforcement. Additional members include the State Department, the Office of the United States Trade Representative, the Department of Commerce, and the Bureau of Immigration and Customs Enforcement. The United States Copyright Office is an Advisor to NIPLECC.

Additionally, the Department participates in the State Department's IP Training Coordination Group, which serves as a central point for the coordination of international intellectual property training. The Department has also participated in the annual Special 301 Process, conducted by the Office of the United States Trade Representative. During the Special 301 process, federal agencies, including the Department, review information provided by industry, United States embassies, United States trading partners, and the

National Trade Estimates report to determine the adequacy and effectiveness of intellectual property protection in approximately 85 countries. The Department and other agencies participate in the deliberative meetings, and the Department has been able both to provide information and to learn much about trends in global theft from the process. The Department is also involved in the negotiation of free trade agreements by providing assistance to the Office of the United States Trade Representative on criminal IP enforcement issues.

In addition, on October 4, 2004, the Attorney General along with Commerce Secretary Donald L. Evans, USTR Ambassador Robert Zoellick, and Homeland Security Under Secretary Asa Hutchinson announced the Strategy Targeting Organized Piracy (STOP!) Initiative, which has been developed over the last year. STOP! is a joint interagency initiative designed to bolster the government's efforts to combat global piracy and counterfeiting by further cracking down on criminal enterprises within the United States and at U.S. borders, empowering the private sector to enforce their rights, and developing a strong international coalition of countries dedicated to combating IP crime.

The Department is an active participant in these and other efforts to share information and coordinate efforts among the different United States agencies charged with overseeing intellectual property enforcement in its various forms. We respectfully refer you to the Bureau of Immigration and Customs Enforcement to address issues exclusive to border seizures.

4) **Last year, as part of the Commerce-Justice-State Appropriations bill, I cosponsored a provision that provided $2.5 million to address IP piracy overseas. Is piracy a priority for the Department and the FBI? What have the Department done and what has the FBI done in connection with international investigations of counterfeit goods and IP piracy since 2001?**

Combating intellectual property crime is a priority for the Department. Over the past few years, we have made international prosecutions an area of emphasis within our anti-piracy program. Increasingly, many of our cases are intertwined with international piracy groups that operate outside our borders. To effectively dismantle such piracy groups, we need to work closely with law enforcement in other countries. In recognition of this challenge, the Department has significantly broadened its approach in recent years and has made the international dimensions of IP enforcement an increasingly high priority.

It is also important to recognize here, as I explained in my written testimony, aspects of physical piracy and Internet piracy are often intertwined such that discussing one without the other does not fully encompass the scope of the problem. The software, games, movies and music released by warez groups on the Internet can end up as the content used to create infringing hard goods. Thus, we have spent significant resources targeting high-level and prolific online piracy, which is almost always international in dimension.

Operation Fastlink, which I described in response to Question 2, is a prime example of the Department's international enforcement efforts. Operation Fastlink involved the simultaneous execution of searches in the United States and ten foreign countries on April 21, 2004, as well as additional action by a twelfth country shortly thereafter. Operation Fastlink is the largest global enforcement action ever undertaken against online piracy. CCIPS co-led the coordination effort with the FBI's Cyber Crime Section. Investigators and prosecutors developed evidence and information to build cases against targets located around the world. In the months leading up to the April 2004 takedown, CCIPS attorneys and FBI case agents traveled to Europe and met with each country involved to provide background training on the operation of online piracy organizations and law enforcement techniques used to identify, investigate, apprehend, and prosecute them. In the months leading up to the April 2004 enforcement action, CCIPS served as a primary point of contact for questions arising overseas about the investigation. As the investigation continues and charges are filed, CCIPS will continue to fully support the prosecutions occurring overseas in addition to prosecuting targets domestically. Efforts such as Operation Fastlink are extremely resource and time intensive, taking several years to resolve. However, they are one of our most effective tools in international intellectual property enforcement.

Operation Fastlink builds upon the success of a previous effort known as Operation Buccaneer, which I also discussed in response to Question 2. Operation Buccaneer marked a turning point in online IP criminal enforcement efforts. At the time of the takedown, on December 11, 2001, Operation Buccaneer was the largest criminal enforcement action involving Internet software piracy and the first such effort to reach across international borders. During the course of the Operation, the Department made formal requests for assistance from foreign law enforcement authorities in the United Kingdom, Norway, Sweden, Finland and Australia. Foreign law enforcement worked closely with us to exchange information leading to the successful prosecution of numerous defendants here and abroad. For example, last summer, Finland, building upon evidence provided by the United States, successfully prosecuted four Finnish defendants for their role in an international piracy organization. Similarly, the United Kingdom has to date convicted four targets, with an additional two currently on trial in London. In connection with this case, CCIPS attorneys and officials from what was then the United States Customs Service traveled to England to assist in the investigation and forensic analysis of evidence. The Department is also in contact with Swedish officials and will continue to assist them in their prosecutions. To date, Operation Buccaneer has resulted in 38 convictions worldwide.

In March 2003, as part of Operation Buccaneer, the United States indicted in the Eastern District of Virginia a prominent leader from the worldwide piracy group DrinkOrDie. The United States sought to extradite the defendant from Australia where he resides. In early July 2004, the Australian Federal Court granted the request for extradition, reversing a lower court decision by an Australian magistrate judge finding the defendant

ineligible for extradition. The defendant has appealed the decision and is in Australian custody pending the outcome of the appeal.

In a separate case, the Department was recently successful in extraditing a Ukrainian man from Thailand for his role in the Internet-based distribution of millions of dollars of pirated computer software and money laundering. The defendant, who was returned to the United States in March, was indicted on April 7, 2004, on 20 counts of counterfeiting, money laundering, and credit card fraud in the Northern District of California.

In March 2004, the FBI participated in an Intellectual Property Rights training conference in Warsaw and Krakaw, Poland, to educate the Polish police, prosecutors, and judges. On August 4, 2004, Polish investigators removed two warez servers and arrested six individuals for the piracy of music and movies. Polish prosecutors requested the FBI's assistance in locating servers, computers, and subjects in the United States. The FBI has also provided international training of foreign law enforcement in Singapore, Canada, England, Poland, and Romania.

As these examples indicate, the Department is committed to international prosecution of IP crimes. We must respond internationally because piracy is a global crime. In this regard, we hope to lead by example and to support foreign prosecutions to the fullest extent possible. Our primary focus is to encourage prosecution in the defendant's home country but, as the above examples illustrate, we will not hesitate to seek extradition when necessary. Developing international investigations and prosecutions is a lengthy and resource-intensive process, but we are steadily building the international law enforcement relationships that are necessary to create stronger international enforcement.

5) **The inability to enforce United States law outside our borders is obviously a major problem. What steps is the Department currently taking to encourage better enforcement of our Intellectual Property rights overseas?**

Because of the global nature of piracy, failure to respond on an international scale is not a viable option. The most significant effort we are making to improve overseas enforcement, as discussed in response to Question 4, is to identify targets wherever they are located and work with our foreign counterparts to prosecute them. In this regard, we hope to lead by example and to support these prosecutions to the fullest extent possible.

Although prosecution is our priority, our efforts are not limited to case-related assistance. The Department has concentrated its international efforts on boosting the visibility of, and resources allocated to, criminal IP enforcement worldwide. For example, in addition to the efforts described in response to Questions 3 and 4, we have encouraged our foreign counterparts to create specialized units devoted to investigating and prosecuting IP crime. We have also participated in numerous training courses sponsored by the federal government and industry, both in the United States and overseas, and especially in targeted countries where IP crime is prevalent. The Department focuses its resources on

those nations that have a significant piracy problem related to the sufficiency of their enforcement efforts. Doing so allows us to use our limited resources in the most efficient, effective manner. Much of the funding for these international training efforts is typically provided by sources outside the Department, such as the State Department INL or the United States Patent and Trademark Office. As a result, we continually work to prioritize those nations that are in most need of law enforcement assistance so that our resources can be utilized effectively.

Department attorneys have also traveled to specific countries to work directly with our law enforcement counterparts. For example, in July 2003, CCIPS attorneys traveled to Brazil for two weeks to meet with prosecutors, police, and legislators in Brasilia, Sao Paulo, and Rio de Janeiro about increasing effective IP enforcement in Brazil, as well as increasing cooperation between the United States and Brazil on IP enforcement matters. Brazil is a critical country in terms of IP enforcement, not just in South America but globally as well.

Similarly, CCIPS attorneys spent 2 ½ weeks in China in October 2003, meeting with numerous Chinese law enforcement officials in four cities -- Beijing, Shanghai, Guangzhou, and Hong Kong -- to discuss ways of improving mutual assistance in cross-border intellectual property cases. The CCIPS attorneys were also the featured presenters at a conference attended by over 300 Chinese prosecutors, judges, and police on the criminal enforcement of intellectual property rights. The conference, which was the first of its kind with Chinese law enforcement, was held for two days in each of three cities -- Beijing, Shanghai, and Guangzhou -- and consisted of candid discussions of China's IP problems, as well as ways to address those problems and improve China's overall IP enforcement regime.

On April 12, 2004, CCIPS attorneys returned from Poland, where they met with high-level prosecutors and investigators to discuss ways to improve cooperation and coordination on international IP enforcement efforts. Along with colleagues from the United States Patent and Trademark Office, the FBI, and the federal judiciary, CCIPS attorneys provided comprehensive IP enforcement training to almost 200 Polish judges, prosecutors, and investigators responsible for IP enforcement.

In addition, we frequently meet with representatives from around the globe that are interested in learning more about our criminal IP enforcement system. In the past eighteen months, for example, we have met with representatives from countries such as Algeria, Antigua, the Balkan countries, Bulgaria, Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, Italy, Japan, Jordan, Korea, Macao, Malaysia, Mexico, Nicaragua, Nigeria, Panama, Paraguay, Philippines, Romania, Singapore, Taiwan, Thailand, Venezuela, and Vietnam to discuss criminal IP cases and provide related training.

In addition, in FY 2004, the Criminal Division's Office of Overseas Prosecutorial Development, Assistance and Training ("OPDAT") provided technical assistance and training programs to law enforcement counterparts in Russia, Egypt, and Southern African countries to enhance their ability to protect intellectual property rights. On April 6-7, 2004, OPDAT conducted the first of four regional programs in Russia targeting police, prosecutors, and judges who historically have failed to ensure that IP violators were punished by meaningful criminal sanctions. The program emphasized the need for the formation of regional IP task forces or specialized units to investigate and prosecute IP crime, and identified contributions that private industry can make to assist law enforcement's efforts.

OPDAT, in conjunction with CCIPS, is also in the process of developing a training DVD that will expand our reach significantly by allowing greater numbers of foreign prosecutors and investigators to receive training to combat piracy. The DVD will focus primarily on copyright and trademark infringement and will touch on all aspects of the distribution chain from production to sale of pirated optical discs.

Finally, it is important to note that both the interagency STOP! initiative and the Department's Intellectual Property Task Force have focused on ways to improve enforcement of our intellectual property rights overseas. The recommendations of the Intellectual Property Task Force include seven recommendations to increase cooperation with foreign countries regarding intellectual property enforcement. Among those recommendations is the deployment of federal prosecutors and investigators with intellectual property expertise to Hong Kong and Budapest, Hungary, to coordinate intellectual property enforcement efforts in those regions.

6. **This Committee and the Senate as a whole have taken strong steps to protect our children from pornography, and we will continue to do everything possible to combat child pornography. As a former prosecutor, I want to see that law enforcement has effective tools for the identification and prosecution of the individuals who make, use, and traffic in this material. I am concerned that the Department might not be using those tools sufficiently.**

(a) In 1999, Congress created a "duty to report" requirement mandating that Internet Service Providers register with a Cyber Tip Line to be used to report child pornography transmitted through an ISP. Although only a tiny percentage of ISPs have signed up for this tip line and despite the fact that this requirement is more than four years old, the Department informed me in December of 2003 that no regulations have been issued under this requirement. Why have final regulations taken more than four years to be implemented, and when will rules be issued?

The Department respectfully refers you to its response to your question number 4 posed to Deputy Assistant Attorney General John Malcolm following the United States Senate Judiciary Committee hearing regarding "Pornography, Technology and Process: Problems

and Solutions on Peer-to-Peer Networks" on September 9, 2003, as well as the Department's response to your letter dated October 10, 2003, to the Attorney General, and the Department's response to your letter dated March 8, 2004, to the Attorney General.

As indicated in those responses, the Attorney General is authorized to designate the law enforcement agencies to which reports may be forwarded by the National Center for Missing and Exploited Children ("NCMEC"), but the statute does not authorize implementing regulations to impose duties on internet service providers ("ISPs"). See 42 U.S.C. § 13032(b)(2). Accordingly, the statute does not provide for regulations that would require that ISPs report suspected violations in specific ways. The vast majority of large ISPs with whom the Department has consulted have indicated a desire to implement reporting in the manner most useful to NCMEC and the law enforcement community. The Department has been working with NCMEC, the FBI, the Department of Homeland Security's Bureau of Immigration and Customs Enforcement, the United States Secret Service, the United States Postal Inspection Service, and the major ISPs to achieve consensus on a reporting protocol. This is a time-consuming process, particularly because of the technical constraints of both the individual ISPs and NCMEC that necessarily dictate the limits of any reporting protocol. The Attorney General published the initial designation of four law enforcement agencies to which NCMEC should forward reports on November 4, 2003. See 28 C.F.R. 81.11 et seq. As the Department consults with NCMEC and ISPs, we are hopeful that the ISPs will adopt a comprehensive set of guidelines and standards for ISPs' reports to NCMEC, which would obviate any need to address the issue through statutory amendment and mandatory regulations. The Department appreciates the support of the ISPs in this endeavor.

(b) In October of 2003, I wrote to the Attorney General again to ask whether under existing law, the Department believed peer-to-peer networks would be required to register with the Cyber Tip Line. Five months have passed without a response. Does the Department believe that this "duty to report" requirement applies to peer-to-peer networks.

The Department responded to your October 10, 2003, letter on April 8, 2004. A copy of that response is attached. In addition, the Department addressed this question in its response to your question number 3 posed to Deputy Assistant Attorney General John Malcolm following the United States Senate Judiciary Committee hearing on September 9, 2003, regarding "Pornography, Technology and Process: Problems and Solutions on Peer-to-Peer Networks," as well as in its response to your letter dated March 8, 2004, to the Attorney General.

As indicated in those responses, the term "network" in the P2P context generally does not connote a central authority with oversight over file sharing transactions, but rather a series of individual computers exchanging files with one another at any given moment. With respect to the manufacturers and distributors of software that allows this file exchange, it

is unclear whether those manufacturers and distributors have any specific knowledge of, involvement in, or control over this activity. They likely do not provide electronic communications services or remote computing services, and, therefore, do not fall within the mandate of 42 U.S.C. § 13032. Moreover, even if P2P software were technologically capable of allowing its manufacturers to monitor the activities of their users, and even if the manufacturers qualified as providers of electronic communications services or remote computing services, 42 U.S.C. § 13032(e) specifically states that providers have no duty to monitor the content of their users' communications.

The "networks" in the P2P context generally consist of individual citizens exchanging files. As a result, those individuals also do not fall within the mandatory reporting statute. Citizens do voluntarily report the presence of child pornography on the Internet to the National Center for Missing and Exploited Children's Cyber Tipline.

(c) I am concerned that the ability of Congress to address the issue of child pornography is being hampered by the Justice Department's unwillingness or inability to respond to questions in a timely manner. I am not the only Senator to have complained of long delays in receiving responses from this Justice Department. What steps is the Department taking to remedy this serious problem?

The Department apologizes for any delay in responding to your inquiries and appreciates your frustration. In addition to your multiple letters on these topics, the Department received multiple letters from other Senators on these identical issues and therefore sought to develop a coordinated response. In addition, after responses were prepared, it became necessary to update the responses with new information, all of which resulted in unacceptable delays in forwarding a response to you. Please be assured that the Department is fully willing and able to respond to your inquiries, and that any delay was inadvertent and purely administrative.

7) **In your testimony you stated that you are "working closely with law enforcement around the globe to identify and assist in the prosecution of IP criminals." You also state that the "Department is committed to working with our foreign law enforcement colleagues." What steps have you taken to improve international cooperation in IP enforcement?**

My responses to Questions 3, 4 and 5 address the steps we have been taking to foster greater international law enforcement cooperation in IP enforcement.

8) **On March 31, the Attorney General announced the establishment of a task force in the Department of Justice to examine and improve the Department's efforts to combat the theft of Intellectual Property.**

(a) Why was the development of an intellectual property task force not mentioned in your testimony?

The Attorney General announced the creation of the Task Force on March 31, 2004. The members of the Task Force were formally announced on April 21, 2004. The Task Force held its inaugural meeting on May 18, 2004. At the time of the Committee's March 23, 2004, hearing, many aspects of the Task Force – including its establishment, the scope of its mission, and its composition – were still the subject of considered deliberations within the Department. It thus would have been premature for me to have incorporated discussion of a task force not yet announced by the Attorney General into my testimony.

(b) When was the task force first conceived?

I do not know the date that the Task Force was first conceived.

(c) What led the Department to conclude that such a task force was necessary?

Intellectual property is well recognized as a vital element of this nation's economy. It is also a prime target of criminals all across the globe who seek to profit by stealing the hard work of the American creative community. Further, intellectual property crime can threaten the public health and safety of our citizens. The Task Force was established in recognition of the important function of the Department in intellectual property rights enforcement.

(d) What coordination has the Department undertaken with other agencies playing roles in international intellectual property enforcement?

My response to Question 3 describes the Department's coordination efforts with other agencies. It is also important to note that the Department's Intellectual Property Task Force is part of the interagency STOP! initiative.

(e) How will the task force coordinate its future efforts with those agencies?

As stated above, the Task Force is part of the interagency STOP! initiative. It will continue to consult with other relevant government agencies as needed; however, no operational coordination will be necessary beyond that in which Department of Justice components already engage in the course of their regular activities.

(f) How will the task force be staffed? How many attorneys will be assigned to it? What qualifications will they have? What level of seniority will those attorneys have?

In addition to myself, the Task Force is comprised of the following senior departmental officials:

David Israelite, Deputy Chief of Staff and Counselor to the Attorney General;

Daniel J. Bryant, Assistant Attorney General for Legal Policy;
Peter D. Keisler, Assistant Attorney General for the Civil Division;
R. Hewitt Pate, Assistant Attorney General for the Antitrust Division;
William Moschella, Assistant Attorney General for Legislative Affairs;
Paul Clement, Principal Deputy Solicitor General;
Laura Parsky, Deputy Assistant Attorney General in the Criminal Division;
Brian Boyle, Principal Deputy Assistant Attorney General in the Office of the Associate Attorney General;
Valerie Caprioni, General Counsel for the Federal Bureau of Investigation;
Debra W. Yang, United States Attorney for the Central District of California; and
Kevin V. Ryan, United States Attorney for the Northern District of California

Each of these individuals has and will continue to contribute invaluable expertise and insight to achieving the Task Force's goal of improving the Department's overall approach to intellectual property rights enforcement. Additionally, the Task Force has drawn heavily upon the knowledge and experience of existing intellectual property prosecutors and investigators within the Department.

(g) To whom will the staff report, and what will the hierarchy of the task force be?

The purpose of the Task Force has been to consider all aspects of the Department's approach to intellectual property rights enforcement and make recommendations to the Attorney General on how to enhance those efforts. The Task Force has included working groups to address issues relating to criminal law, civil law, international treaties and obligations, legislative and regulatory proposals, and public awareness. The Task Force has operated under the guidance of David Israelite, Deputy Chief of Staff and Counselor to the Attorney General.

(h) Will these staff be relieved of their current responsibilities to any degree, and if so, how will those needs be filled? Will new staff be hired?

The Task Force has not required additional staff, nor do we anticipate that it will.

(i) What resources will be expended on the task force, and where will those resources come from?

The Task Force has not required additional resources, nor do we anticipate that it will.

(j) What docs the task force intend to produce as a result of its work?

As noted in response to Question 6(g), the purpose of the Task Force has been to consider all aspects of the Department's approach to intellectual property rights

enforcement and make recommendations to the Attorney General on how to enhance those efforts. Accordingly, on October 12, 2004, the Attorney General released the Task Force report, listing numerous recommendations. The report is available at: http://www.usdoj.gov/ag/speeches/2004/ip_task_force_report.pdf, and a copy is enclosed for the Committee's convenience.

(k) How long will the task force exist?

No formal termination date has been announced.

(l) What will the task force's role be, if any, in connection with investigations and prosecutions?

The Task Force has not and does not intend to alter the decision making hierarchy with regard to investigations and prosecutions.

(m) On what matters will you, as the Assistant Attorney General of the Criminal Division, be reporting to the staff head of the task force?

I have been and will continue to be involved in all aspects of the work undertaken by the Task Force that relate to the criminal enforcement of our intellectual property laws.

SUBMISSIONS FOR THE RECORD

Statement of Senator Joseph R. Biden, Jr.
Judiciary Committee Hearing on
"Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions"
March 23, 2004

Good afternoon. I would like, first of all, to thank Senator Specter, Chairman Hatch, and Senator Leahy, for organizing today's hearing on this important issue.

In recent years, I have spent a lot of time studying intellectual property piracy and counterfeiting. This issue straddles two of my major interests as a Senator – fighting crime and managing our relations with foreign countries. In February of 2002, in my joint capacity as Chairman of the Subcommittee on Crime and Chairman of the Foreign Relations Committee, I held a hearing entitled, "Theft of American Intellectual Property: Fighting Crime Abroad and At Home," and I issued a report on the status of our fight against this crime.

(continued...)

What I wrote in the report, and what I highlighted at the hearing, is that every day thieves steal millions of dollars of American intellectual property from its rightful owners. It is not only an economic issue, or a matter of diplomacy; it is a crime, pure and simple.

Innovation has been the key to American economic growth throughout our history. The Founding Fathers had the foresight to provide for protection of intellectual property, giving Congress the power to promote the progress of science and useful arts through such tools as copyrights and trademarks.

American innovation and creativity need to be protected by our government no less than our personal property, our homes and our streets.

(continued...)

American intellectual property is an immensely valuable resource. Failing to protect it is equivalent to letting coal be stolen from our mines, or water taken from our rivers. The U.S. Customs Service estimates that counterfeiting costs the U.S. more than $200 billion every year and has resulted in the loss of 750,000 American jobs.

Last October, I joined with Senator Smith and Congressmen Goodlatte and Schiff to found the Congressional International Anti-Piracy Caucus. Our caucus, which now counts 70 Senators and Representatives as members, is striving to draw attention to the international aspects of this problem, and to work with our friends overseas to stem the tide of this crime.

(continued...)

In the few months the caucus has been in existence, we have gotten off to a good start: we released a "watch list" of 5 countries with piracy problems; we wrote to Secretary of Commerce Evans, and Congressmen Thomas and Rangel, to draw their attention to the problem of piracy in China; and we wrote to the governments of each of the watch list countries to encourage action against piracy.

Tomorrow, the Caucus will host a luncheon for visiting Brazilian legislators who have formed a special Investigative Committee on Piracy. This committee has already met with striking success in leading the fight against piracy in their country.

(continued...)

Unfortunately, however, we need not look overseas to find American intellectual property being stolen. We find it happening right here at home as well. That's why, in 2002, I introduced a bill to plug a hole in our federal law that permitted some counterfeiters of authentication features to go unpunished in the United States. Unfortunately, the bill fell prey to a struggle between content providers and Internet service providers, among others, over its contents.

There is reason for optimism this year that these issues may be resolved. Therefore, I am today reintroducing my bill, now known as the Anti-Counterfeiting Act of 2004, and I am hopeful that we can implement this useful tool for stopping the activities of these crooks.

(continued...)

To date, my focus has been on the piracy of copyrighted materials, such as films, music, software and books. However, I am well aware that such problems exist with tangible items such as razors and snowboards, and I look forward to learning more today about this aspect of the issue.

America is a place where we encourage diverse ideas, and with that encouragement we must protect those ideas. They are the source of every concept we conceive, and every product we create - all that is American culture and American know-how.

We must protect these ideas. It will save jobs, improve the economy, and fight crime. And it's the right thing to do.

I would like to thank all of our witnesses for taking the time to join us, and I look forward to hearing their testimony.

(End)

Statement of Brad Buckles
Executive Vice President, Antipiracy
Before the Committee on the Judiciary
United States Senate

March 23, 2004

Thank you Mr. Chairman and Senator Leahy for holding a hearing on the devastating effects of counterfeiting. My name is Brad Buckles and I am the Director of the antipiracy operations at the recoding Industry Association of America. The RIAA's member companies All of the copyright industries which comprise about 5% of our country's gross domestic product and are responsible for a trade surplus, suffer from optical disc counterfeiting. In many cases, counterfeiters use the proceeds from piracy to fund other nefarious activities. More and more, domestically and abroad, the counterfeiting of discs has evolved from small operations to organized syndicates, making it harder for private industry to combat without help from governments worldwide.

The Nature and Extent of Music Piracy

The counterfeiting of music is almost as old as the music industry itself but the advent of the compact disc radically altered the nature of music piracy, providing the pirate producer with the opportunity to produce near perfect copies of any recording. There is massive manufacture and international traffic of illegal CDs and DVDs and the recent proliferation of cheap recordable optical discs has served to create an easy and hard to detect means of mass duplication.

Annual world-wide pirate sales approach 2 billion units; worth an estimated $4 - $5 billion. Globally, 2 in 5 recordings are pirate copies. Total optical disc manufacturing capacity (video / audio CDs, CD-ROMs and DVD) – stands at well over 20 billion units, having quadrupled in the past five years.

Manufacturing capacity massively exceeds legitimate demand. This creates a business environment ripe for exploitation by criminal syndicates. Production costs may be as little as 35¢. Given that the pirate producer has few or none of the overheads associated with genuine production, the profit margin is substantial.

The preferred format for the music pirate varies from country to country and clear regional differences can be seen. Partly in response to successful enforcement actions and partly due to the availability of cheap recordable discs, the preferred choice in the Americas and most of southern Europe, is the CD-R. It is interesting to note that in countries such as Hong Kong, which introduced stringent legislation and active enforcement, the pirates have switched from producing CDs to CD-Rs. The advantages are perhaps obvious; a large investment in machinery and skilled manpower to operate it is avoided. Production can be divided among many sites thus avoiding the risk of

detection. Unskilled and illiterate workers can be used and production can be undertaken close to the point of sale thus again minimizing the risks.

Underlying the continuing spread of music piracy is global overcapacity in the manufacture of all optical discs, i.e. discs carrying all media including music, film and computer software. IFPI estimates that the number of optical disc plants worldwide has increased to 1,000. 2002 saw a geographical shift in capacity within Asia and significant increases in Russia and Eastern Europe. This is a recipe for increasing illegal sales, because the supply of discs is far outstripping legitimate demand.

In Asia, China and Malaysia have seen sharp increases in manufacturing capacity. The movement of plant production facilities from Ukraine contributed to an increase in Russia's production capacity, which rose above 300 million. Poland's excess capacity more than doubled. In all these countries such increases underline the lack of adequate regulation of optical disc manufacturing.

Dealing with the problem of organized piracy

As a direct result of proliferating music piracy IFPI has established an Enforcement Unit specifically to target the organized criminals involved. The strategy adopted was to recruit experienced investigators with a wide range of abilities and to bring in support services in the fields of intelligence analysis and forensics. Currently there are 50 investigators worldwide who obtain evidence and intelligence from many different countries. A further 200 personnel in National Groups investigate domestic music piracy.

The success of the forensic laboratory in linking infringing discs to source factories has resulted in many raids on suspect plants worldwide. This has in turn encouraged several Governments including Malaysia, Poland, Bulgaria and Russia to establish their own forensic programs. Russia alone has over 30 known optical disc plants and pirate discs from 17 of these plants have been found in 25 different countries.

The evidence of organized crime involvement is incontrovertible. Music piracy flourishes in those jurisdictions in which corruption is endemic. Major evasion of tax is inherent to these offenses, causing huge losses in Government revenues. Illegal firearms have often been encountered during raids and in a number of investigations there is evidence that groups are also engaging in the trafficking of drugs. In some developing areas whole economies are being distorted internally leading to loss of revenue and the failure of legitimate domestic enterprise to flourish.

Our industry works in partnership with Interpol and the World Customs Organization. At their General Assembly in Budapest in September 2001, the General Secretary of Interpol, Mr. Ron. Noble, stated that, ***"Interpol recognizes the extensive involvement of organized crime and terrorist groups in intellectual property crimes. There is a real need for facilitation and coordination of international police efforts in combating this criminality, which operates across international borders and has very serious consequences for the public. Working in partnership with customs authorities,***

international agencies and the private sector, Interpol will provide an effective response to this growing threat."

Cases linked to Organized Crime syndicates

The following cases serve to illustrate the links between organized crime and piracy.

□ **February 2003 - Italy**

Mafia boss, Luigi Giuliano, described in a trial the role of organized crime in music and video piracy. Giuliano, La Forcella (Naples downtown) Camorra boss, arrested two years ago, turned State's evidence and provided information on organized crime activities and strategies in Naples in the last two decades. On the 5th of February, in front of the Public Prosecutor Filippo Beatrice, Giuliano stated that the camorra clans earn some "100,000 Euros each week dealing with drugs, extortion and video and music piracy". He described in detail how organized crime manages all the illegal operations in Naples, with different gangs controlling the calls for tenders, the drugs sales, the illegal betting, and the production of counterfeit CDs in different city areas. These "local" gangs keep part of the illegal incomes while other monies are deposited in the Camorra bosses' bank accounts. Giuliano confirmed that the Camorra gang was directly involved in the production and distribution of pirate CDs, not just controlling the area used by organized crime to run illegal activities. Giuliano told the judges that in the early 80's, during a major war between the various gangs in which dozens were killed, the "Cupola", the illegal main board of the criminal alliance, agreed on the distribution of the illegal activities to various gangs. The "pax mafiosa" which followed the agreement allowed the criminal network to increase the business in many areas including the emerging piracy business.

□ **January 2003 – Spain**

A series of 13 raids by the National Police in Madrid led to the arrest of 40 persons involved in the mass duplication of CD-Rs. The suspects many of whom were illegal immigrants from China and who had been brought to Spain by the other members of the gang were found in possession of 346 high speed burners, 168,400 blank CD-Rs, 24,450 recorded CDs, 39,000 DVDs, 10,500 VCDs with films, 515,000 jewel cases, 210,000 inserts and 48,000 Euros in cash. The gang used a number of computer shops and restaurants to launder the money generated by the pirate product.

□ **July 2002 – Mexico**

An investigation led to a police raid that was met with fierce resistance from five juveniles aged under 18. There were 5kg of cocaine in the premises along with 25 CDR burners and 16,000 pirate CDRs. Using juveniles to run CDR and drug trafficking operations is a deliberate ploy by organized crime to protect those behind the syndicate.

□ **October 2001 – Mexico**

Police raided eleven houses, three of which were linked by interconnecting passages and tunnels, which were disguised by false walls. Inside they discovered a massive counterfeiting operation. In total five persons were arrested during searches, which yielded 235 CDR burners, over 1million blank CDRs and 512,000 pirated CDRs together with over 1,000,000 inlay cards. This illegal plant had the potential capacity to produce over 14 million CDRs annually. It is believed, that this crime syndicate have invested the profits from piracy into other activities such as narcotics and prostitution.

Four of the persons arrested were found to be in possession of loaded 9mm pistols. During the searches a car was deliberately crashed into a Police barricade and the driver arrested. This man, an associate of the others had been sent to the address to create a diversion to allow the others to escape. He was found to be in possession of an AK47 assault rifle and has been indicted for attempted murder.

□ **May 2001 – Taiwan**

A raid on residential premises in Kaoshung City, revealed 70,000 suspected pirate discs. Most contained pornographic material but more significantly the search of the premises revealed several illegal firearms. These guns were Italian and German self-loading pistols. Five persons were arrested. As a result of these arrests, further searches were carried out and small quantities of pirate product and further firearms seized. At a third premises an illegal arms factory was discovered running alongside a sophisticated CDR facility. In total 17 rifle barrels, 7 modified handgun barrels, 10 shotgun barrels, 10 cartridge magazines, 50 bullets and other equipment were seized. The main suspect in this case had previous involvement in music piracy

□ **April 2000 – London**

Following an IFPI investigation into the supply of high quality counterfeit CDs linked forensically to Russian plants, a series of raids were carried out in London and four persons arrested. During the search a sophisticated credit card counterfeiting operation was uncovered. The suspects, Russian nationals who had been granted political asylum in Britain, employed members of the Russian community in London, to secretly record details of credit cards when these were tendered for payment in restaurants and hotels. The data obtained was then downloaded onto computers and subsequently written to blank cards, which were then used to purchase high value items from London stores. Forensic examination of the computers revealed that over 30,000 credit card details were recorded. At the suspects addresses 10,000 blank credit cards were found together with stamps for attaching holograms and machinery for printing and embossing the cards. The sale of CDs financed the Credit card operation with a network of couriers smuggling the discs into the UK.

Music Piracy and links to Terrorism

The most extreme form of organized crime affecting society today is that of terrorism.

The clandestine nature of terrorist organizations requires large sums of money to maintain operatives in the field and for the purchase of arms and explosives. Some intelligence has been obtained to indicate that these groups are involved in the fabrication, distribution and sale of counterfeit music and other intellectual property infringing material to raise funds for their operations.

IFPI anti-piracy personnel do not investigate information giving rise to suspicion of terrorist involvement in music piracy. Information encountered has been, and will be, referred to an appropriate government agency.

In the United Kingdom and the Republic of Ireland the investigation of terrorist crimes committed by both sides of the sectarian divide has provided a great deal of intelligence about the operations of those groups. There is no doubt that a significant proportion of their funding stems from the sale of counterfeit product. At a recent Organized Crime seminar hosted by the Police Service of Northern Ireland it was stated by a senior police officer that 93% of persons involved with intellectual property crimes, including music piracy offences, were linked to para-military groups.

□ December 2000 - Ireland

In December 2000 Guarda Officers (Republic of Ireland Police) and Irish Customs officers, investigating the smuggling of diesel fuel between the Republic and Ulster searched a remote farmhouse, where they discovered over 20,000 optical discs suspected to contain infringing material. Whilst still at the premises they were attacked by men dressed in combat clothing and carrying handguns and rifles who stole the discs from them. A subsequent investigation led to the arrests of the gang and the seizure of a huge number of counterfeit music CDs, burning equipment and associated artwork. One of those arrested was a person suspected of being a senior figure in the Provisional IRA during the 1970s and 1980s.

□ September 2000 - Russia

On 20 September 2000 the public relations department of the Federal Security Service (FSB), Moscow announced the elimination of a criminal organization headed by one, Ziyaudi Terloyev. This organization was reported to have been financing illegal rebel formations in Chechnya. Integral to Terloyev's activities was the manufacture of pirate compact discs at a plant in Noginsk, outside Moscow. During the raids this plant was closed and 5,000 pirate discs seized. Explosives, grenades, detonators and ammunition were reported seized at the suspects' residences. It was estimated that this groups average monthly earnings amounted to over $500,000.

□ September 2001- South Africa

During a raid on an address in Durban, in September 2001, counterfeit CDs were seized from a syndicate of Pakistani nationals. A search of the premises also revealed

documentation indicating allegiance to Al Qaeda and Osama Bin Laden. This information was passed to the appropriate authorities in South Africa.

□ **November 2001 - Paraguay**

Several CD-Rs, containing pirate music compilations, recovered by investigators in Paraguay contained inlay cards depicting graphic images of the exploding twin towers of the World Trade Centre, New York, and portraits of Osama Bin Laden. There is a large population of middle - eastern origin in Ciudad del Este, a city notorious in Paraguay for producing pirate products of all descriptions.

□ **November 2001 – Mauritius**

Street hawkers selling counterfeit music products were seen to be selling video CDs containing footage of the twin towers of the World Trade Centre exploding and a message from Bin Laden. These propaganda discs were seized on the orders of the Police Commissioner in Mauritius who feared that they might foment public unrest. The origin of these discs is suspected to be Pakistan. Pakistan has been identified to be a significant manufacturer and exporter of pirate music compact discs.

□ **April 2003 - Philippines**

On 23 April 2003 officers from the Philippine Videogram Regulatory Board (VRB), supported by Police units, took action against street vendors selling pirate discs. During this action in which violent protests were staged a man, linked to the vendors was shot and killed by Police. Subsequently it was established that the dead man was the son of an alleged commander of an MILF unit, a proscribed terrorist organization, operating in Mindanao.

Conclusion

There is no doubt that in many jurisdictions the 'low risk – high reward' environment that characterizes the usual response to music piracy of government and law enforcement agencies encourages exploitation by organized crime groups. The experience of the British in Northern Ireland clearly illustrates that terrorist organizations are alive to the potential of intellectual property crime as a source of funding. The absence of evidence in other jurisdictions cannot be taken to indicate that such crime is not a major source of funding for such groups. The greater probability is that the difficulty in penetrating and investigating their activities, coupled with the fact that piracy thrives in corrupt regimes, allows such groups to engage in piracy unhindered by any authority.

The music industry is absolutely committed to confronting the organized crime groups that now threaten the very survival of our business. No other industry invests so much energy and capital to this; no industry has a team of professionals comparable with the investigative resource that we have constructed. However, this anti-piracy resource is tiny relative to the forces ranged against it. Our investigators have no enforcement

powers to assist them in the investigation of the ruthless sophisticated groups that are realizing huge profits and which readily resort to extreme violence. It is submitted that there are currently few, if any, Governments that appreciate the threat posed by intellectual property crime and that assign commensurate levels of enforcement resources to it.

The music industry resource is capable of disturbing the debris at the edges of this particular stone but the substantial activities beneath continue undisturbed. The crime gangs, and any terrorist groups, engaging in intellectual property crime are fully aware of the relative absence of any effective law enforcement in this arena and, ironically, may be vulnerable because of this. They often fail to adopt the usual tactics that frustrate penetration and detection of their traditional activities. Indeed, intellectual property crime may be the soft underbelly of these pernicious groups.

Statement of Senator John Cornyn

Before the Committee on the Judiciary
United States Senate
on

"Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions"

March 23, 2004

I want to thank the Chairman for scheduling this timely hearing on such an important issue.

I also want to congratulate the Chairman, Ranking Member Leahy and Senator Specter for bringing together such an impressive panel – your testimony is helpful to us and I appreciate each of you being here today.

Property rights have long been a central part of our legal and economic systems. Indeed – intellectual property was deemed so fundamental by our founders as to deserve placement among the powers specifically enumerated to Congress in the Constitution.

Today – the "progress of Science and useful Arts" flourishes as much as ever – representing a significant portion of our economy. For example, the music, film and software industries comprised more than 5 percent of the GDP of the United States, or $535 million.

Even so, the rights of our scientists, inventors, artists and authors are becoming increasingly difficult to protect in the face of changes in the capability and reach of technology.

Theft of intellectual property costs our country billions of dollars every year – and the problem is worldwide. Indeed, one of my staffers – traveling overseas a few months ago – saw a pirated version of the "Lord of the Rings: Return of the King," the recent Oscar winner for best picture, the same week the film was released.

And worse, it is becoming clear that the theft of intellectual property is tied to organized crime. I believe that some of the witnesses here today are testifying to this fact – but this issue is particularly troubling and it is good that we are addressing it here today.

I am particularly pleased that the focus of this hearing is on the theft of tangible intellectual property – as we should not overlook this in the face of online piracy. But the two, unfortunately are inextricably linked. Digital copies of movies, music and other copyrighted materials are being reproduced, packaged and sold by the millions at great cost to our nation's economy.

That is why I introduced, along with Senator Feinstein, the Artists' Rights and Theft Prevention, or "ART" Act in November of last year. That bill, which we expect to bring before the Committee very soon, targets two very serious problems in the on-going fight against piracy.

- First, the use of camcorders in a motion picture exhibition facility to record movies, and

- Second, the use of online file-sharing programs to distribute "pre-release" materials – a particularly egregious form of piracy that undermines the marketing, launch and sale of copyrighted material such as music, software and film and causes significant economic harm to the copyright holders.

I believe that the ART Act is a good start to combating the worst forms of piracy. I look forward to working with the Chairman and members of this committee to move the bill forward and on future legislation to continue to work to protect these important intellectual property rights.

Thank you.

WRITTEN STATEMENT OF THOMAS DONOHUE,

PRESIDENT AND CHIEF EXECUTIVE OFFICER

U.S. CHAMBER OF COMMERCE

BEFORE THE

UNITED STATES SENATE COMMITTEE ON THE JUDICIARY

HEARING ON

"COUNTERFEITING AND THEFT OF TANGIBLE INTELLECTUAL PROPERTY:

CHALLENGES AND SOLUTIONS"

MARCH 23, 2004

Good afternoon Chairman Hatch, Ranking Member Leahy, and members of the full committee. My name is Tom Donohue and I am President and Chief Executive Officer of the U.S. Chamber of Commerce. I would like to thank the Committee for holding this important hearing and I am pleased to have the opportunity to testify on the impact that impact intellectual property crimes have on the business community and on our economy.

The U.S. Chamber of Commerce is the world's largest business federation, representing more than 3 million businesses of every size and in every sector of the economy. Our membership includes nearly 3,000 state and local chambers throughout

the United States and 97 American Chambers of Commerce abroad. This international network of contacts has helped us become intimately familiar with the trends being discussed here. It has also provided us with a worldwide perspective regarding the size and scope of this problem.

As you know, neither counterfeiting nor intellectual property piracy is a new phenomenon. These practices are growing so rapidly they are now having a significant, measurable impact on industry and our economy. The U.S. Chamber and our membership are deeply concerned with the growing global production of, and trade in, counterfeit goods and intellectual property theft and recognize that this crisis is pick-pocketing businesses, stifling innovation, and costing American jobs.

The growth in the trade of illegitimate goods over the past 20 years is astounding. In 1982, it was estimated that the trade in illegitimate goods drained $5.5 billion dollars from the global economy.[1] In 1996, this figure jumped to an estimated $200 billion.[2] The estimates for 2003 range from $450 billion[3] to $500 billion.[4] Various organizations, including Interpol, estimate that the trade in counterfeit and illicit goods ranges between 6-9% of all current world trade with volume sharply rising.[5]

Customs and law enforcement officials worldwide are overwhelmed with the growing tide of fake products. In 2001, the EU seized over 95 million items with an

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[1] George W. Abbot, Jr. and Lee S. Sporn, *Trademark Counterfeiting* SS 1.03 § [A][2] (2002).
[2] S. Rep. No. 104-177, 104th Congress, 1st Session 1-2 (1995); George W. Abbot Jr. and Lee Sporn, *Trademark Counterfeiting* § 1.03 [A][2] (2001).
[3] *"The Economic Impact of Counterfeiting", Organization for Economic Co-operation and Development 1988*
[4] *Automotive Week*, "Manufacturers, MEMA Meet to Address
[5] Motor Magazine, "Counterfeit Parts: A Poor Fit For Your Shop," Tom Nash, January 2004.

approximate retail value of over (U.S.) $2 billion[6], though this represents less than 1% of the worldwide market of counterfeit goods.

No product or category of products can be considered safe from trademark, patent or copyright infringement. Counterfeit products from pharmaceuticals to airplane parts, to sneakers can be found in marketplaces around the world.

Intellectual property crime is one of the fastest growing criminal enterprises worldwide. The primary reason is that intellectual property theft is a low risk, high return crime. According to a recent United States Trade Representative's Special 301 report, the real incentive for criminals to begin counterfeiting and piracy operations is that they can begin illegal operations with little capital investment and even if they are caught and charged with a crime, the penalties in most countries do not offer a sufficient deterrent.[7]

It is also important to note that the trade of these goods is directly linked to the funding of organized crime and terrorist networks. Due to the high profitability of illegitimate goods and lack of enforcement against criminals, as well as the relative ease of manufacturing, this has become a preferred method of raising revenue. For example, according to *U.S. News and World Report,* a counterfeit t-shirt operation funneled money to an Egyptian Sheik to help finance the 1993 World Trade Center attack.[8]

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[6] Statement of Ronald K. Noble (Secretary General, Interpol) before the House Committee on International Relations, *Oversight Hearing on The Links Between Intellectual Property Crime and Terrorist Financing*
[7] Office of the United States Trade Representative, *2003 Special 301 Report*
[8] Motor Magazine, "Counterfeit Parts: A Poor Fit For Your Shop," Tom Nash, January 2004.

Intellectual property crimes drain an estimated $200 - $250 billion from the U.S. economy alone.[9] This obviously harms the businesses that create and hold the copyright on goods being copied and stolen, but by lowering sales revenues, counterfeit goods can also slow the growth of legitimate businesses, depress job growth, reduce federal, state and local tax revenues.

With new job creation at a slowed pace, it is clear that we need to start viewing this as a jobs issue. In 1995, the U.S. Department of Commerce estimated the U.S. automotive industry alone could have hired an additional 210,000 more workers if the trade in counterfeit automotive parts were ended.[10] Another study of software products showed a 10-point reduction in worldwide piracy rates would add up to $400 billion to the global economy, generating 1.5 million jobs and potentially $64 billion in tax dollars.[11]

Those studies show job losses in the automotive and software sectors specifically. It is not known how many job losses can be attributed to intellectual property crimes in other key sectors like apparel and pharmaceuticals, which each lose billions of dollars annually to trade in counterfeit products.

Although this issue begins with our members in the consumer packaged goods, pharmaceutical, automotive, aviation, software, music, and apparel industries, this crisis ultimately impacts the entire U.S. business community.

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[9] Office of the United States Trade Representative, *2003 Special 301 Report*
[10] Detroit News, "Fake Parts Hobble Car Industry," October 2, 2003.
[11] Business Software Alliance, IDC study, *Expanding Global Economies: The Benefits of Reducing Software Piracy,* April 2, 2003

Intellectual property crimes undermine the billions of dollars companies invest each year in not only developing and promoting their brands. This theft deters product development, thus lowering the marketability of new and existing products, and hurting corporate and shareholder profits. In addition, counterfeiting alienates customers who fall victim to faulty counterfeit products, creates liability concerns, and negatively affects distribution of legitimate goods.

Moreover, when fake products fail or cause injury to the consumer, brand owners lose credibility with their consumers, distributors and licensed manufacturers. These factors ultimately reduce consumer confidence, which lead to lost sales and production orders – ultimately resulting in the elimination of jobs.

This issue also matters to small and emerging businesses. Small stores that unknowingly have fake products on their shelves or unknowingly distribute phony goods are at risk of losing consumer trust. Furthermore, small businesses are the primary driver of product and service innovation in the U.S. economy and can be financially devastated when their innovations are immediately copied or reproduced illegally.

When looking for examples of how intellectual property crimes impact small business and job creation, we need to look no further than the software industry. Software piracy accounts for 25% of all software used in the U.S., and 40% used world-wide, approaching figures as high as 90% in some regions. Annual seizures of Microsoft products alone exceeds $1.7 billion. These losses not only directly affect the

companies themselves, but reduce the innovation and job creation activity at suppliers, distributors and retailers, who lose sales and volume due to piracy.

One of the most significant and nefarious impacts of counterfeiting is on consumers. For instance, not only could a consumer purchase a fake and inferior product, but often these products threaten consumer health and safety.

I would like to provide some examples of these problems found in counterfeiting of replacement parts, pharmaceuticals and consumer goods.

- Airline Parts: The dangers to airline passengers caused by using fake, inferior airline parts could be devastating. For instance, in 1989, an airplane belonging to Partnair, a Norwegian charter airline, crashed when its tail assembly fell off because of substandard counterfeit bolts holding it to the rest of the body. Additionally, investigations into the November 2001 crash of an American Airlines flight over New York indicate that it may have been caused by the failure of counterfeit parts.[12]
- Fake pharmaceuticals: Counterfeit drugs can also have severe consequences. Parties could be denied life-saving drugs or could ingest products that could actually harm them.
- Consumer goods: Although sometimes perceived as a victimless crime, counterfeit consumer goods could also cause significant dangers to consumers. For instance, fake software may contain security bugs or other nefarious

[12] *The Economist,* "Imitating Property Is Theft – Counterfeiting," May 17, 2003, U.S. Edition

glitches, where everyday products such as food or shampoo may contain unsafe levels of bacteria or other harmful ingredients.[13]

While consumers, businesses, and government all understand the potential dangers of counterfeit goods, businesses often look at counterfeiting as a 'cost of doing business' and consumers often sees it as a victimless crime. However, given the growing real harms and dangers that these products present, that tide seems to be shifting.

The Chamber believes that additional education and outreach is badly needed and long overdue. The first step to combat the growing tide of intellectual property crimes and their impact on the United States economy is to raise awareness of the issue with key stakeholders. By raising awareness of the implications of intellectual property crimes with lawmakers, the media, and the general public, we can change not only the perception of intellectual property crimes and make the case for greater enforcement efforts but can educate manufacturers, wholesalers, shippers, retailers and others learn how to identify and stop counterfeit products from entering their distribution channels.

It is critical that we recognize intellectual property crimes as a threat to the American economy and a risk to consumers. These are not victimless crimes, but rather real criminal activities with significant personal, economic, and social consequences.

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[13] Henry Gilgoff, *Counterfeit: Rip-Offs of Popular Products Victimize Both Consumers and Manufacturers,* Newsday, August 27, 1995

We also need to take steps to secure the global supply chain. Counterfeiters use a mix of both traditional and more sophisticated means to get their products into legitimate domestic retail markets. By utilizing an organized network of shady middlemen, counterfeiters are able to slip their products into legitimate businesses. Fixing those holes could go a long way toward eliminating illegitimate products.

It is important to remember that the phenomenal growth of counterfeiting is also encouraged by the lack of global enforcement of intellectual property rights. That is not to say there are no existing efforts. We applaud the U.S. Bureau of Customs and Border Protection, Interpol, and USTR who take precautions to defend against the influx of counterfeit goods on a daily basis. The work they do on a day to day basis is greatly helping to protect our nation and consumers from the growing plague of counterfeit products.

However, as counterfeiting networks embrace new technologies to produce and distribute their goods, counterfeit products are becoming more abundant and harder to identify by these agencies. As a result, more counterfeit products are ending up in legitimate retail outlets in the United States.

We need real time connectivity and coordinated information sharing between these departments and the business community on the flow of counterfeit goods into and within the United States. This will not only help us further understand the scope of the issue and its impact on the U.S., but also provide the backdrop for us to develop coordinated proactive solutions to combat these crimes.

We recognize that there are current measures in place to protect intellectual property domestically and abroad. For example, the World Trade Organization has established a commendable legal framework in the Trade Related Aspects of Intellectual Property Rights (TRIPS). But this agreement needs to be enforced. Some key players in the World Trade Organization are countries where intellectual property theft runs rampant, such as those "priority countries" identified in the United States Trade Representative's annual "special 301" report.

In conclusion, the U.S. Chamber of Commerce and our members are actively engaged on this issue. We see it as one of the most important issues facing our economic health and consumer safety. We recognize the importance of an educational campaign to highlight the need to address the issue, and are committed to finding ways to raise the profile of the issue. We look forward to working with Congress, domestic government agencies, and other nations to secure the global supply chain and to build adequate enforcement mechanisms, and to bring a stop to this crisis.

I would like to thank the Committee for focusing on the economic threat intellectual property crimes pose to the business community, to our global economy, and to consumers and I appreciate the opportunity to provide testimony.

STATEMENT OF

JON W. DUDAS

ACTING UNDER SECRETARY OF COMMERCE FOR INTELLECTUAL PROPERTY
AND
ACTING DIRECTOR OF THE UNITED STATES PATENT AND TRADEMARK OFFICE

BEFORE THE

COMMITTEE ON JUDICIARY
UNITED STATES SENATE

MARCH 23, 2004

Introduction

Chairman Hatch, Ranking Member Leahy, and Members of the Committee:

Thank you for this opportunity to appear before you to discuss the problem of counterfeiting and intellectual property theft and the Department of Commerce's role in protecting intellectual property abroad. Secretary Evans is keenly aware of the increasing significance of intellectual property protection for American businesses and innovators and has made combating counterfeiting and piracy a top priority for the entire Department. In addition, as Acting Under Secretary of Commerce for Intellectual Property and Acting Director of the United States Patent and Trademark Office's (USPTO), I am dedicated to marshalling U.S. government efforts to reduce the toll that IP theft takes on American IP owners. To that end, I commend you for holding today's hearing and am very appreciative of the Committee's interest in finding additional ways to protect U.S. intellectual property owners' assets overseas. Your long-standing commitment to these issues, as well as your consistent support of the work of the USPTO, is of tremendous value.

International IP Enforcement Overview

Increasingly, both the United States and our trading partners are relying on intellectual property (IP) to drive economic growth. This is because competitive success in a market economy depends more and more on the IP assets held by an institution -- from the results of the latest research to the brand recognition of a company's trademark. For example, with one of the largest trademark licensing programs in the world, Coca-Cola's brand value exceeded $70 billion in 2003.[1]

According to the International Intellectual Property Alliance, U.S. copyright industries continue to lead the U.S. economy in their contributions to job growth, gross domestic product (GDP), and foreign sales/exports. Between 1977-2001, the U.S. copyright industries' share of the GDP grew more than twice as fast as the rest of the U.S. economy. In 2001, the U.S. copyright industries achieved estimated foreign sales and exports of $89 billion, leading all major industry sectors, including motor vehicles (equipment and parts), aircraft and aircraft parts, and the agricultural sector.[2] These same companies depend upon their brands or trademarks to compete effectively in the marketplace, distinguishing one's products from others used in commerce, and promoting consumer confidence and brand loyalty.

Unfortunately, the economic benefits of capitalizing on intellectual property rights have captured the attention of pirates, organized crime, and -- in some limited but increasing instances -- terrorists. Today, the illegal

[1] "The Global Brand Scorecard 2003," BusinessWeek, August 4, 2003.

[2] "Copyright Industries in the U.S. Economy: The 2002 Report," International Intellectual Property Alliance, April 2002.

duplication of software, music, DVDs, and other digitized information and the trafficking in counterfeit products, from which no industry and no country is exempt, are all too common.

Optical disk piracy in the form of music, business software, videogames, and published materials is a chief concern. In China, U.S. industry estimates that 90 percent of business software, valued at $1.5 billion, is pirated.[3] Worldwide, industry estimates that approximately 40 percent of software programs are pirated. In 2002, *Pravda* reported that the bulk of video and audiotapes produced in Russia were counterfeit. With advances in digital technology, piracy in optical media is increasingly high quality, high volume, and low cost. The problem is compounded by the growth of the Internet and the increase in bandwidth, which makes some of this piracy less dependent on tangible optical media, while at the same time enhancing the impression that piracy is victimless or free.

According to 2001 and 2002 U.S. Customs statistics on seizures based on copyright piracy and trademark counterfeiting, the value of goods seized due to trademark counterfeiting was greater than for copyright piracy. In fact, global trademark counterfeiting totals about $500 billion a year, of which pirated automobile parts account for about $12 billion.[4] Indeed, the U.S. Trade Representative's 2003 Special 301 Report concluded that counterfeiting has become "a massive, sophisticated global business involving the manufacturing and sale of counterfeit versions of everything from soaps, shampoos, razors and batteries to cigarettes, alcoholic beverages and automobile parts, as well as medicines and health care products." The World Health Organization estimates that counterfeit drugs account for ten percent of all pharmaceuticals, and in developing countries the percentage can be as high as 60 percent.[5]

Piracy and counterfeiting come with a high price. For example, according to the Business Software Alliance, in the United States the U.S. software industry lost nearly $2 billion in 2002.[6] The cost of counterfeit and pirated products is not limited to lost revenue and jobs. Consumer health and safety is at stake, too. U.S. Food and Drug Administration counterfeiting investigations have jumped from about five a year in the late 1990s to 22 in 2002.[7] Viagra is known to be a frequent target of counterfeiters, but other commonly prescribed drugs such as Lipitor and Procrit are being targeted as well. Counterfeit drugs may contain too much, too little, or none of a drug's active ingredient. Common everyday household products also are at risk. In December 2003, the Department of Homeland Security's Bureau of Immigration and Customs Enforcement announced seizures of electrical goods and batteries valued at approximately $8 million. Counterfeit batteries can explode in electronic equipment or children's toys. Even product approval marks certifying a product's safety are being counterfeited.

To make matters worse, the global criminal nature of IP piracy is all too real. During a House International Relations Committee hearing last summer, the Secretary General of Interpol noted what we believe is a potential, though yet not significantly realized trend, when he testified that IP crime "is becoming the preferred method of funding for a number of terrorist groups." A customs expert with the European Commission recently stated that al-Qaeda and Hezbollah are among organizations believed to be using counterfeit goods to launder money and fund their activities. Mr. James Moody, former chief of the Federal Bureau of Investigation's Organized Crime/Drug Operations Division, has stated that counterfeiting is likely to become "the crime of the 21st Century."[8]

Given these threats to U.S. economic interests and our national security, the USPTO and our colleagues in the Department of Commerce, particularly the International Trade Administration and the Office of General Counsel, are working hard to curb IP crime and strengthen IP enforcement in every corner of the globe. Indeed, Secretary Evans has been a champion on this issue and has made it a top priority for the entire Department.

Because American IP owners compete in a global marketplace, we need to expand our efforts to promote IP protection internationally. We need to make sure that American IP owners have sufficient legal tools to fight

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[3] http://www.bsa.org/usa/press/newsreleases/New-Economic-Impact-Study-Details-Benefits-of-Strong-Copyright-Protection.cfm
[4] "Chinese Counterfeiters Turn Out Fake Car Parts", Wall Street Journal, March 3, 2004 at p. A.14.
[5] http://www.iacc.org/teampublish/uploads/factsupdated.pdf
[6] http://www.bsa.org/resources/loader.cfm?url=/commonspot/security/getfile.cfm&pageid=1292&hitboxdone=yes
[7] "More Fake Lipitor Prompts Lawsuit from Distributor", Wall Street Journal, Oct. 5, 2003, p. C.9.
[8] http://www.iacc.org/teampublish/uploads/factsupdated.pdf

piracy. We also need to provide technical assistance to foreign entities on drafting and implementing effective IP laws and training on enforcement of IP rights.

Under the American Inventors Protection Act of 1999 (P.L. 106-113), the USPTO is directed to advise the President, through the Secretary of Commerce, and all Federal agencies, on national and international intellectual property policy issues including intellectual property protection in other countries. USPTO is also authorized by the AIPA to provide guidance, conduct programs and studies and otherwise interact with foreign intellectual property offices and international intergovernmental organizations on matters involving the protection of intellectual property.

Through our Offices of International Relations and Enforcement, the USPTO: (1) helps negotiate and works with Congress to implement international IP treaties; (2) provides technical assistance to foreign governments that are looking to develop or improve their IP laws and systems; (3) trains foreign IP officials on IP enforcement; (4) assists in the drafting and revision of IP sections in bilateral investment treaties and trade agreements; (5) advises the Office of the U.S. Trade Representative (USTR) on intellectual property issues in the World Trade Organization; (6) works with USTR and industry on the annual review of IP protection and enforcement under the Special 301 provisions of the Trade Act of 1974; and (7) consults with the Department of Justice and other federal law enforcement entities who are responsible for criminal IP enforcement.

The USPTO also serves as the co-chair of the National Intellectual Property Law Enforcement Coordination Council (NIPLECC), which is tasked with coordinating domestic and international intellectual property law enforcement. NIPLECC was launched in 1999 to ensure the effective and efficient enforcement of intellectual property in the U.S. and worldwide. While NIPLECC's coordination activities may not have a direct impact on corporate stewardship, they ensure that government enforcement efforts are consensus-based and non-duplicative, and therefore are vital to an ensuring fairness and honesty in the use and development of intellectual property.

NIPLECC has developed a comprehensive data base that includes all recent intellectual property law enforcement training provided by the US government and many associations to developing and least developed nations. It is also developing legislative suggestions to improve domestic intellectual property laws related to enforcement. NIPLECC currently operates on whatever funding and resources are provided by individual member agencies. One of the most important NIPLECC initiatives, which is pending due to funding issues, is a public awareness campaign on IP piracy and counterfeiting.

Enforcement Training and Technical Assistance

The USPTO provides intellectual property enforcement training and technical assistance on a truly global basis. These training and assistance programs foster respect for IP, encourage governmental and corporate efforts to combat and deter infringement, and promote honest business practices in the use and development of intellectual property. Our technical assistance and training initiatives were launched to address U.S. statutory and trade obligations to promote IP protection, and to meet increasing numbers of requests for assistance by foreign governments throughout the world. Our efforts have yielded positive results, measured by decreasing levels of intellectual property piracy and stronger legal protections for intellectual property in many countries where we provided training and technical assistance. Still, much works remains.

Today, the focus of our efforts is: (1) addressing the difficulties governments in developing and least developed countries face in meeting international obligations; and (2) bringing together local authorities to address their own enforcement issues.

At the conclusion of the Uruguay Round in 1994, the resulting World Trade Organization's (WTO) Trade-Related Aspects of Intellectual Property Rights Agreement (TRIPs) presented WTO members with new obligations and challenges. The TRIPs Agreement sets minimum standards of protection for the various forms of intellectual property and requires WTO members to provide for "effective enforcement" of intellectual property rights. TRIPs also includes detailed provisions on civil, criminal and border enforcement measures designed to protect the owners of intellectual property rights. Today, developing countries obligations' under

TRIPs have entered into force. Least developed countries have until 2006 to comply with the bulk of the provisions, including the enforcement obligations. As a WTO agreement, TRIPs obligations are subject to the dispute settlement procedures of the WTO.

Over the last several years, the USPTO has assisted countries around the world in establishing adequate enforcement mechanisms to meet their obligations under TRIPs. In bilateral negotiations, we work closely with USTR to obtain more detailed commitments on enforcement and means to deal with infringement using new technology. We provide technical advice through the annual Special 301 process, the GSP review, TRIPs Council review of implementing enforcement legislation, and in the negotiation of free trade agreements (FTAs).

Our approach to the on-going FTA negotiations has been to build upon the TRIPs agreement. In other words, our negotiating position is that these trade agreements should follow a "TRIPs Plus" format by expanding the minimum standards set out in TRIPs. One way of achieving the "TRIPs Plus" goal is by enhancing the enforcement provisions contained in TRIPs and combining them with the enforcement provisions contained in the WIPO "Internet" Treaties – the WPPT and WCT. The 1996 WIPO Copyright Treaty (WCT) and the WIPO Performers and Phonograms Treaty (WPPT) bring copyright law in line with the digital age. The WCT and the WPPT establish important new international norms related to the right to make a work available to the public through interactive media. They also provide for the protection of copyright management information and technological measures used to protect copyrighted works. The FTAs also incorporate provisions from our own Digital Millennium Copyright Act. These include Internet Service Provider (ISP) liability, protection against anti-circumvention devises, and satellite signals.

Regional Concerns

As I am sure the Committee is well aware, one of the areas of greatest concern with respect to IP counterfeiting and piracy is Asia, particularly China. Despite China's membership in the World Trade Organization (WTO) and its requirement to comply with the TRIPs Agreement, inadequate IP enforcement in China is a major problem for U.S. business interests, costing billions of dollars in lost revenue and tens of thousands of U.S. jobs. For example, according to the Business Software Alliance, China accounts for 44 percent of the piracy-related dollar losses to BSA member companies in the Asia/Pacific region.[9] IP enforcement problems are pervasive with piracy and counterfeiting being the most serious and widespread. These problems run the gamut from rampant piracy of movies and business software to counterfeiting of consumer goods, electrical equipment, automotive parts and pharmaceuticals.

China is a leading source of counterfeit automotive parts production, which costs the auto industry $12 billion a year. Most counterfeiting involves parts that need to be replaced frequently, such as oil filters, headlamps, batteries, brake pads, fan belts, windshields and spark plugs. For example, DaimlerChrysler, BMW, Audi, Volvo, Mitsubishi and Toyota report that even though a factory in Guangdong Province has been raided three times in a two and a half year period, it has been allowed to continue making windshields stamped with their brand names for sale in the world market. It is estimated that automotive companies could hire 210,000 more employees if the counterfeit auto parts trade is eradicated.[10] According to the World Health Organization, China also is a major source of counterfeit and substandard medicines.

Last fall, Secretary Evans led a mission to China and highlighted China's lack of IPR enforcement. The Secretary met with high-ranking Chinese officials and reiterated a continuing concern: that effective IPR protection requires that criminal penalties and fines for intellectual property infringement be large enough to be a deterrent rather than a business expense. Secretary Evans believes in the strong enforcement of our trade laws and is taking new and proactive measures to strengthen the enforcement and compliance of our trade agreements. He has tasked Commerce agencies, such as USPTO and the new Office of Investigations and Compliance under Commerce's International Trade Administration, to coordinate their efforts to vigorously pursue allegations of IPR violations wherever they occur, especially in China.

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[9] Eighth Annual BSA Global Software Study, June 2003.
[10] Motor and Equipment Manufacturers Association, September 2003.

Under the direction of Secretary Evans, the USPTO has been working extensively to reduce piracy and counterfeit activity in China. As a follow up to the Secretary's October 2003 trip, I recently led a delegation to China for consultations with senior officials at China's patent and trademark and other intellectual property agencies. Our delegation also met with U.S. companies facing intellectual property issues in China. A primary focus of this trip was to further the Administration's goals of improving the intellectual property environment for U.S. companies doing business in China and, specifically, of addressing widespread counterfeiting and piracy. Many industries have noted that the Chinese government, by restricting market access for certain products, is providing free reign for counterfeiters, pirates and criminals to exploit the void created by the lack of legitimate products. Given these trends, we will continue to press hard for enhanced steps by the Chinese Government to significantly reduce the extent of IP violations.

Trademark counterfeiting and copyright piracy in Russia is a major problem as well. The International Intellectual Property Alliance estimates that 75 percent of the products seized in raids go back into the marketplace to be sold in Russia or abroad.

Organized crime involvement in Russia is such a threat that companies are concerned about the danger in protecting their intellectual property rights. By some accounts, organized crime groups control the duplication and initial distribution of the majority of pirated videos and DVDs. In the 2003 Special 301 Report, the U.S. Government urged Russia to combat organized crime involvement through specialized enforcement units and the enactment of tough criminal penalties. We continue to urge: (1) the closure of plants producing illegal optical discs; (2) increased raids and prosecution of optical disc piracy; and (3) the adoption of an optical media enforcement regime.

The USPTO has been extensively involved to improve the enforcement, especially criminal enforcement, of copyright and other IP rights in Russia. For example, in November 2002, the USPTO cosponsored and participated in a United Nations Economic Commission for Europe (UNECE) seminar in Moscow on intellectual property enforcement in Russia. The seminar was attended by Russian government officials representing the State Duma and the Ministries of Defense, Culture, Education and Science. The USPTO has several proposals pending for technical assistance in Russia in FY 2004, which would build upon these and other programs we have conducted in Russia.

Conclusion

Mr. Chairman, the demands on the Department of Commerce's and USPTO's expertise in the international arena have grown dramatically in the last few years. These demands most assuredly will increase in the next few years, alongside our obligations to meeting our core patent and trademark examination functions.

As we look to the future, however, let me conclude on a positive note. Although by all accounts counterfeiting and piracy appear to be growth industries, there have been some recent successes in attacking the problem. Between 2001 and 2002, according to industry estimates, software piracy in Indonesia decreased from 89 percent to 68 percent. In South Africa, it fell from 63 percent to 36 percent. The Motion Picture Industry has reported a decrease in piracy levels in Qatar from 30 percent in 2001 to 15 percent in 2002. In Bahrain there have been dramatic and systemic improvements in IP protection and enforcement over the past few years. These include the signing of numerous international IP conventions and the virtual elimination of copyright piracy and counterfeiting in retail establishments.

So, there is reason for optimism. I am hopeful that with the continued support and partnership of this Committee, we will be able to do even more to provide American businesses and entrepreneurs with the IP protection they need. Clearly, in terms of the economy and national security, much is at stake. That is why our dedicated team of experts will continue to work tirelessly to protect American products in every corner of the globe.

Thank you very much.

News Release

JUDICIARY COMMITTEE

United States Senate • Senator Orrin Hatch, Chairman

March 23, 2004 Contact: Margarita Tapia, 202/224-5225

Statement of Chairman Orrin G. Hatch
Before the United States Senate Committee on the Judiciary
Hearing on

"COUNTERFEITING AND THEFT OF TANGIBLE INTELLECTUAL PROPERTY: CHALLENGES AND SOLUTIONS"

I would like to thank my distinguished colleague from Pennsylvania, Senator Arlen Specter, for requesting and presiding over this hearing on the critical topic of counterfeiting and the theft of intellectual property rights embodied in tangible goods.

I also want to thank all of our distinguished governmental and private witnesses for appearing today to discuss these increasingly important issues. In particular, I want to thank Tom Donohue and the United States Chamber of Commerce for their leadership in calling for renewed attention to this important threat to the health and safety of our citizens, the growth of our national economy, and the reputations of our American manufacturers.

I believe that education and enforcement are the two key issues in any discussion of intellectual property theft and counterfeiting. These two issues are really two facets of a broader systemic problem that is easy to state, but difficult to solve.

Simply put, intellectual property rights are under siege. Intellectual property theft and counterfeiting are growing problems that are becoming even more difficult to detect and prevent. And these problems will continue to grow until we start taking stronger enforcement actions. Our markets are globalizing and copying technologies are becoming cheaper, better and more readily available. To combat the growing problems of intellectual property theft and counterfeiting, policymakers and intellectual property owners must bring two critical tools to bear: education and enforcement.

Education: Recently, the Chamber of Commerce asserted that American businesses need to pursue a "rebranding" strategy on the issues of intellectual property theft and counterfeiting. I agree with the Chamber that the industries that depend on intellectual property rights need to re-educate the public about the continuing importance of those rights.

I worry that it is easy for policymakers and business executives to underestimate the importance of this educational effort. Users of intellectual property have long educated government policymakers and enforcement officials about the importance of intellectual property rights. As a result, executives and government officials know that copyrights and patents protect incentives to research, create and innovate. Most executives and policymakers know that

trademarks protect not only corporate reputations and revenues, but also the safety of the food that nourishes us, the drugs that heal us, and the products that enrich our lives and homes.

But too many members of the public do not share this understanding of the importance of intellectual property rights. Mainstream news outlets now regularly report claims that copyrights are "tyranny" and that the patent system is "broken." Too many law professors are now teaching that intellectual property rights are antiquated, dysfunctional concepts that impair the creativity and choice that they were meant to empower.

Those who know differently need to start speaking out. It is time for coordinated efforts to educate all Americans about the benefits of intellectual property rights. These efforts must also be proactive: If individual members of the business community wait until their particular rights are threatened directly, the appearance of self-interest may weaken the force of their message. As a result, wise policymakers, inventors, artists, and executives are all speaking out against the theft of intellectual property even when the rights of others are more directly at stake.

For example, I was pleased to see that that HP CEO Carly Fiorina recently spoke out against Internet piracy of copyrighted works. It took real courage for the leader of the computer industry to speak out on that issue. But speaking out was also smart business. Ms. Fiorina recognizes that our technology industries can thrive by providing safe, legal content over the Internet – but only if piracy can be beaten back.

For these reasons, I hope that we will all support the Chamber's efforts to re-educate the public about the importance of all intellectual property rights.

Enforcement: A second critical concern in any effort to combat intellectual property theft and counterfeiting is enforcement. As a legislator, I am committed to helping intellectual property owners develop the tools that they need to protect their rights. But Congress must have input from our enforcement agencies and our industries if it is to assure that enforcement tools are available and effective.

Let me give you an example of how industry can work with Congress to ensure that the law keeps pace with the pirates. In the last Congress, I co-sponsored with Senator Biden S. 2395, the Anticounterfeiting Amendments of 2002.

This bill recognized that our copyright and trademark holders increasingly use sophisticated authentication features to distinguish genuine goods from counterfeit products. But our current laws do not provide rights holders with adequate remedies against third parties who tamper with authentication features or traffic in falsified authentication features. I understand that Senator Biden has reintroduced this legislation, and I look forward to working with all members of this Committee to attempt to address this important issue in this Congress.

# # #

Statement Of Senator Patrick Leahy
Hearing In The Senate Judiciary Committee
"Counterfeiting And Theft Of Tangible Intellectual Property: Challenges And Solutions"
March 23, 2004

I want to thank Senator Specter and Senator Hatch for agreeing to hold this hearing, which will address an issue of tremendous importance to many consumers, workers and businesses in our beleaguered economy. The committee has spent time in recent years focusing on the many problems of intangible piracy, particularly the theft of copyrighted works on the Internet, but I am pleased the committee will also address the problems of tangible piracy: knock-off goods that violate the rights inhering in trademarks, patents and copyrights, which deprive the owners of the fruits of their efforts and investments, and present consumers with shoddy and sometimes dangerous products.

Several years ago, Senator Hatch joined me in sponsoring the "Anticounterfeiting Consumer Protection Act of 1996," which addressed just this type of piracy by amending several sections of our criminal and tariff codes. While that law made important changes, particularly by expanding RICO, the federal antiracketeering law, to cover crimes involving counterfeiting and copyright and trademark infringement, more enforcement is needed in light of these pernicious practices involving the theft of goods based on intellectual property rights. Then, as now, trafficking in counterfeit goods hurts purchasers, State and federal governments, and economies at every level. Indeed, this form of theft has become a method of choice for organized crime syndicates – and more recently terrorist organizations – for profit, and to launder money to fund their criminal activities.

Just last year, I joined with Senator Allen in sponsoring an amendment to the Foreign Operations Bill for 2004, which will provide $2.5 million to the State Department in order to establish programs that will help developing nations protect intellectual property rights. These programs will strengthen local intellectual property laws, educate and train law enforcement officers, and enhance the ability of customs officials to combat trafficking in pirated goods. This measure will give flexibility to the people who are actually combating piracy in the field, so that they can take whatever steps may be appropriate where they are. I hope we can find additional solutions to intellectual property piracy and counterfeiting. I look forward to hearing from Mr. Wayne about how this program is being implemented at the State Department, and what further steps might be useful to law enforcement in combating this form of theft.

Consumers feel the effects of counterfeit goods when they think they are buying a "brand name" product but end up with a shoddy imitation instead. We will be hearing today from Vanessa Price of Burton Snowboards who will bring home the damage this kind of theft creates. Although I am disturbed at the story she has to tell, I thank her for being with us today. Burton is a small company, whose innovation has made it an industry leader in snowboarding equipment and apparel. Unfortunately, knock-off products labeled

"Burton" can be seen around the world. This theft and free-riding on the reputation of such a creative company threatens to undermine the years of effort of many hard-working Vermonters.

Similar stories are becoming all too familiar in my office. SB Electronics in Barre has seen its capacitors reverse engineered and its customers lost to inferior copycat models. Likewise, Vermont Tubbs, a furniture manufacturer in Rutland, has seen its designs copied, produced offshore with inferior craftsmanship and materials, and then reimported to undermine its own sales. Hubbardton Forge in Castelton, Vermont has seen its beautiful and original lamps counterfeited and then sold within the United States at prices – and quality – far below their own.

The means by which illegal knockoff producers will go to copy a design are astounding – all the more for the harm they inflict. At one trade show where cameras were prohibited, a competitor hired the night cleaning crew to take pictures of the showcased furniture.

In some cases, counterfeit goods can pose a significant public health risk. According to the International Anti-Counterfeiting Coalition, counterfeit parts have been discovered in helicopters sold to NATO, in jet engines, bridge joints, and fasteners in equipment designed to prevent nuclear reactor meltdowns. We have all seen news stories about counterfeit pharmaceutical drugs.

The economic impact of tangible piracy in counterfeit goods is estimated to be roughly $350 billion a year and to constitute between 5 percent and 7 percent of worldwide trade. The United States is the world leader in intellectual property. Accordingly, knockoffs of American products account for a disproportionate percentage of that amount. In 2002, the movie industry lost $3.5 billion in pirated videos, a 60 percent jump from 1997. In a study examining the impact of counterfeiting on trademarks, researchers for the International Trademark Association estimated that trademark holders worldwide lost $2 billion in 1995, as a result of trademark infringement and counterfeiting.

In addition to depriving patent, copyright, and trademark holders of the compensation owed to them, the commerce in counterfeit goods robs the U.S. economy of jobs and tax revenue. The Business Software Alliance estimates that pirated software alone cost the U.S. economy 118,000 jobs and $5.7 billion in lost wages in 2000. In Vermont, the State lost $15.3 million in retail sales of software alone in 2002, which translated into 267 fewer jobs and $3.6 million in lost tax revenue. And that is just from computer software. Think of the effects on jobs and on State and local tax revenue.

Another grim aspect of this problem is the link between organized crime and counterfeit goods. We are now learning more about the relationship between terrorism and this form of intellectual property theft, as well. According to the U.S. Customs Service, terrorists have used transnational counterfeiting operations to fund terrorist activities: The sale of counterfeit and pirated music, movies, software, tee-shirts, clothing, and fake drugs "accounts for much of the money the international terrorist network depends on to feed its operations."

There are thousands of reasons to work harder to end the trafficking in counterfeit goods – thousands of jobs lost, consumers harmed, trademarks and patents infringed, businesses threatened, and illegal enterprises enriched. I look forward to hearing from the Administration witnesses about the efforts they have made over the last three years to curtail these effects.

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Testimony of

James Mendenhall

Assistant U.S. Trade Representative

Before the

Committee on the Judiciary

United States Senate

March 23, 2004

Counterfeiting and the Theft of Tangible Intellectual Property Rights: Challenges and Solutions

Good afternoon Mr. Chairman, Senator Leahy and Members of the Committee. Thank you for the opportunity to speak to you today about the challenges and solutions posed by counterfeiting and theft of tangible intellectual property rights (IPR).

The theft of intellectual property worldwide is an enormous and growing problem. As stated in the Administration's Special 301 report last year, U.S. industry losses due to piracy and counterfeiting are estimated to be around $200-250 billion annually. As a result of this criminal activity, many foreign markets are simply evaporating. In China and Russia, industry estimates that piracy levels in many sectors are close to or exceed 90% of the market. Most countries are not quite at that level, and the situation in some countries has actually improved. Yet, while these changes have sometimes been dramatic, the piracy levels in many countries remain unacceptably high.

USTR and other agencies are working around the clock to resolve this problem – a problem made complex not only by its sheer scale but by the multiple underlying causes.

I will outline four key challenges facing the United States in this area. I will then outline five tools that USTR, working with other agencies, has successfully brought to bear on this issue.

Four Challenges

Devising New Solutions for Defeating Modern Pirate and Counterfeit Operations

First, pirates and counterfeiters exploit technological advances and employ modern business models to streamline and expand their operations.

Sophisticated, inexpensive copying technology is now available off the shelf, and pirates have been quick to put it to illicit use. For example, CD- and DVD-burners enable pirates to churn out thousands of illegitimate copies of music, software, and movies without significant investment in equipment and facilities. Similarly, the availability of cheap, high-quality scanners and photocopiers facilitates mass-production of pirated textbooks, journals or other written material.

Pirates have also become globalized. If they are shut down in one country, they simply move to the next. They run global production and distribution chains, exporting their illicit goods and displacing legitimate products from markets around the world.

The evolution of these criminal operations requires new solutions. As I shall explain later, we have led a counter-offensive on this front through the development of

rigorous new rules in our trade agreements and by making use of other tools at our disposal.

Strengthening the Rule of Law

Second, some large developing countries and economies in transition pose their own unique problems. The unshackling of markets and entrepreneurial talent in economies such as China and Russia present tremendous opportunities – unfortunately not always for the good. Criminal enterprises (including small operators and sophisticated organized crime syndicates) are growing up side-by-side with legitimate business operations. Whether through corruption, intimidation or neglect, the legal systems in these countries provide inadequate means and incentives to prosecute criminal offenders in all cases or deter future criminal activity. The solution to this problem runs much deeper than the protection of intellectual property and requires the creation of a legal system and culture built on the rule of law.

Enhancing Effectiveness of International Rules

A third challenge is the creation of international legal rules to address this problem. The TRIPS Agreement was a watershed in the development of international IPR norms, and it has proven to be a tremendous success. While not all WTO Members have implemented their full TRIPS obligations, most have made significant strides.

Perhaps the chief complaint we hear today is not that countries' laws are defective (although that certainly remains a very large problem) but that countries are simply not enforcing their laws. While TRIPS contains provisions on enforcement, these obligations

by their nature are not as black-and-white as other obligations. For example, it is relatively easy to determine whether a country grants patents for a 20-year term. It is much more difficult to determine whether a country has in place effective deterrent remedies to prevent IPR infringement. As I will discuss later, we have tackled this issue head on in our FTAs, which contain extensive provisions designed to strengthen IPR enforcement.

Promoting Awareness of the Benefits of Intellectual Property Protection

The final challenge is to rebut the skeptics in other countries who question the value of IPR protection.

We need to make it clear, for example, that trademarks are not simply names and symbols, but measures of the quality, trustworthiness and value of a product. IPR protection promotes consumer protection and safety. Trademark infringement can result not only in the counterfeiting of handbags and shoes, but can lure unwary consumers into purchasing defective windshields that shatter on impact or automobile brakes that malfunction. Anecdotal evidence of infringement is rife with horrible stories, such as counterfeit pharmaceuticals filled with paint or baby shampoo filled with industrial solvents.

IPR protection also promotes development. Copyright infringement can hinder the development of local cultural industries. As long as local artists can't make a living in their home markets because of rampant piracy, local talent will remain undeveloped. Patent and copyright infringement can cause a flight of investment out of the country, thereby eroding or preventing development of a local technological base.

Five Tools

The complexity of this problem calls for a comprehensive, multi-faceted solution. USTR has employed all tools at its disposal to bring pressure to bear on countries to reform their intellectual property regimes, and we will continue to do so.

Trade Agreements

First, Ambassador Zoellick is pursuing the President's ambitious agenda of free trade negotiations, bilaterally, regionally and multilaterally. In less than two years, we have completed and won Congressional approval of free trade agreements with Chile and Singapore, launched bilateral free trade negotiations with 14 more nations (concluding talks with eight of them), and announced our intention to begin free trade negotiations with six more. At the same time, we are working toward a Free Trade Area of the Americas (FTAA) encompassing 34 countries in the Western Hemisphere. We require that our free trade agreement partners bring their IPR regimes up to world-class standards.

Our FTAs contain the highest level of IPR protection of any international agreements in the world, and they directly address many of the key challenges I discussed earlier. They contain provisions dealing with the whole range of IPR, including such issues as curbing the use of equipment used to circumvent anti-counterfeiting technology and dealing with sector-specific problems such as optical disk or broadcast piracy. They also strengthen enforcement by streamlining procedural rules for bringing copyright and trademark claims, and providing for stronger damages (including statutory damages), expeditious *ex parte* searches to gather evidence, and civil remedies to seize and destroy

infringing goods. They also provide for improved border enforcement to stop imports and exports of pirate and counterfeit goods and stronger criminal enforcement.

Special 301/Section 301

Second, in April of each year, USTR issues the Special 301 report, which catalogues the IPR problems in dozens of countries around the world and places them in a hierarchy of wrong-doing – ranging from the lowest ranking of Watch List to the mid-level Priority Watch List to the ranking reserved for the worst offenders, Priority Foreign Country. A country's ranking in the report sends a message to the world, including potential investors, about a country's commitment to IPR protection. We have used this name-and-shame exercise to great effect, as each year we see countries coming forward with reforms or reform proposals to avoid elevation on the list.

In last year's report, we gave special attention to counterfeiting and piracy, and we have seen results. For example, we elevated Poland to the Priority Watch List, and the Polish Government almost immediately took steps to address several long-standing U.S. industry concerns, including efforts to reduce the amount of pirate and counterfeit goods being sold at the Warsaw Stadium.

In the most serious cases, countries identified as Priority Foreign Countries can be subjected to a Section 301 investigation and face the possible threat of trade sanctions. China is a prime example. In 1995 and 1996, persistent tolerance of piracy led us to threaten $1 billion in trade sanctions, which helped us to win a bilateral IPR agreement in 1995 and further action in 1996. We have also imposed Section 301 sanctions on Ukraine.

WTO

Third, USTR is the lead agency, working closely with other agencies, in addressing IPR issues multilaterally through the WTO.

The initiation of dispute settlement proceedings is the most forceful expression in the WTO of dissatisfaction with a country's IPR protection and can be an effective way to achieve reform. USTR has brought 12 TRIPS-related dispute settlement cases against 11 countries and the EC. Of these 12 cases, two are in consultations, eight were resolved by mutually-agreed solutions between the parties, and two resulted in favorable rulings for the United States. In nearly all these cases, U.S. concerns were addressed via changes in laws or regulations by the other party.

We also regularly review countries' IPR laws and practices through the Trade Policy Review (TPR) Mechanism. Countries recently reviewed include Turkey, Chile and Thailand. In addition, the TRIPS Council regularly reviews implementing legislation, providing a forum for USTR to provide comments on existing and draft legislation and an opportunity for bilateral meetings to discuss specific concerns.

Preference Programs

Fourth, USTR administers the Generalized System of Preferences (GSP) program and other similar programs, which allows us to withhold tariff preferences if a country fails to adequately protect IPR. The "carrot" of preserving GSP benefits is an effective incentive for countries to protect IPR. In fact, the mere filing of a GSP review petition or the initiation of a GSP review has produced positive results. For example, industry

withdrew its petition on Peru after Peru made commitments to improve enforcement. Moldova also enacted stronger enforcement measures after the initiation of a GSP review. Colombia implemented measures to provide data exclusivity and ensure the legitimate use and licensing of software by government agencies in order to qualify for benefits under the Andean Trade Preferences Act.

Diplomatic Leverage

Finally, USTR, the State Department, the Department of Commerce and other agencies have used diplomatic pressure to encourage IPR reform around the world. We spend significant resources traveling the world and meeting with foreign leaders and officials to impress upon governments the importance of committing the political will and resources necessary to deal forcefully with piracy and counterfeiting.

For example, we have made IPR protection and enforcement in China one of the top priorities in our trading relationship. The United States has sent numerous high level delegations to China, and the President himself raised the issue of IPR enforcement with Premier Wen. Ambassador Zoellick has repeatedly emphasized the importance of this issue with the Chinese Government, and Deputy USTR Josette Sheeran Shiner has made multiple visits to China in the past few months alone. In the coming days, she will return to China to prepare for the U.S.-China Joint Commission on Commerce and Trade meeting next month, where IPR will be high on the agenda.

Interventions have also recently taken place at senior or staff levels with Russia, Pakistan, Thailand and other foreign governments.

Conclusion

Dealing with the problem of piracy and counterfeiting requires a comprehensive, intensive and sustained effort. Ambassador Zoellick is strongly committed to continuing to bring all of USTR's weapons to bear on this issue and to maintain the pressure year after year. We have made progress, but enormous challenges remain.

I look forward to working with you and your staffs to continue to devise solutions for dealing with this critical matter.

Thank you.

"Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions"
Senate Judiciary Committee
March 23, 2004

Vanessa Price
Intellectual Property Specialist
Burton Snowboards

My name is Vanessa Price, and I am the Intellectual Property Specialist for the Burton Corporation. It is a pleasure to take part in this hearing on Counterfeiting and Theft of Intellectual Property. Despite vigorous measures to protect our intellectual property through trademark and patent registrations, Burton has seen significant counterfeiting recently. We expect that counterfeiting will increase dramatically as our brand continues to grow. As a smaller company, Burton is deeply concerned about the rise in theft of our intellectual property since we do not have the resources it takes to combat or offset the effects of large-scale counterfeiting.

The Burton name is synonymous with snowboarding. Founded in 1977, the Burton Corporation is a Vermont-based company that employs 350 people in Vermont and 160 people at offices in Japan and Austria. The boardsports industry credits Burton Snowboards with the founding and popularization of snowboarding as a legitimate sport. Additionally, Burton has fueled the growth of snowboarding worldwide through continuous work with, and support of, its Global Team riders and development of successful programs such as Learn-To-Ride (LTR), The Chill Foundation (a not for profit foundation dedicated to providing snowboarding opportunities to underprivileged children), and the US Open Snowboarding Championships.

After twenty-six years in business, Burton remains the industry leader with over 1500 dealers in North America alone. Snowboarding is growing rapidly worldwide. SnowSports Industries of America (the skiing and snowboarding trade group) estimates that participation in Snowboarding has increased 300% since 1998. Burton has seized this opportunity to grow its brand. In recent years, Burton has expanded to include Gravis Footwear, Analog casual apparel, Anon Optics, and R.E.D. Protective Gear. However, this growth and popularity is not without a significant downside. Our industry has gone through considerable consolidation in recent years. Most of the snowboard manufacturers are seasoned competitors. Believe it or not, snowboarding has matured. Competition is keen and profits are shrinking, even as the sport grows in popularity.

Unfair competition from counterfeiters significantly compounds the problems of seasonality and severe sensitivity to economic downturns that our industry already faces. Virtually none of the companies that manufacture ski or snowboarding equipment are large enough to have the resources or tools necessary to fight counterfeiting, leaving a growing portion of what should be domestic revenue going to foreign thieves. We could not even guesstimate the amount of tax revenue that the U.S. Treasure loses to these unrealized gains.

As the Burton brand grows, we face significant challenges to our intellectual property rights. Burton has taken all available and appropriate steps to register our trademarks both in the U.S. and internationally. Currently, we maintain more than 60 trademark registrations in the United States alone. We have taken the additional steps of registering our trademarks with the Customs officials in the U.S., Chile, Argentina, Brazil, Hong Kong, PR China, Taiwan, Japan, and South Korea. Unfortunately, filing with Customs offers very scant protection, especially in recent months, where Customs officers are concerned more and more with national security. Burton also holds patents worldwide relating to our snowboard technology, including snowboard boots, bindings, snowdecks, and snowboards. However, despite these measures, we see growing evidence that our brand is suffering from counterfeiting and illegitimate sales.

Burton has noticed growing problems with small-scale counterfeiting in the U.S. Typically, this involves the manufacture and sale of fake Burton, Gravis, and Analog stickers, accessories, and clothing on Internet auction sites, specifically eBay. Unauthorized Burton branded goods can be found on eBay almost continuously. Fortunately, eBay affords intellectual property owners the right to request the removal of counterfeit items from auction. While eBay will provide a seller's personal contact information, a small corporation such as Burton Snowboards does not have the resources to pursue every instance of counterfeiting on eBay. Small-scale counterfeiting may not appear to be a significant problem. However, Burton manufactures limited editions of specific stickers and products. These items stand to lose their consumer appeal when they routinely show up in large quantities on eBay.

Burton employees have seen a very significant increase in intellectual property theft in Asia. While it is extremely difficult to determine the scale of theft and factory leaks with our current resources, Burton representatives traveling to Asia frequently see unauthorized Burton and Gravis items for sale in shops and markets. Several recent examples include:

- Macau: Several employees traveling noticed legitimate Burton items for sale in a shop. From the location of the shop and the construction of the items, they suspected a leak from a local factory;
- Hong Kong:
    - Our Director of Men's Apparel reports seeing counterfeit Gravis footwear and bags at several stores and markets in Hong Kong;
    - Another employee reports seeing unauthorized Burton products sold in Stanley Market, as far back as 2002;
- Taiwan: On a visit to a factory, several Burton fleeces were found in the showroom. These fleeces were determined to be counterfeit based on their construction and the fact that Burton had never used that factory;
- Thailand:
    - We maintain no distribution in Thailand;
    - While visiting Thailand with his family, Jake Burton Carpenter, our CEO, found vendors selling counterfeit Gravis items in a local night market;

- Counterfeit Gravis bags from Thailand have also surfaced on eBay;
- Counterfeit Gravis bags have been found by employees at night markets in Thailand.

Burton is in the process of expanding from a one-season business by diversifying into the apparel business and expanding sales of t-shirts, fleeces, sweatshirts, and accessories. As this aspect of our business grows in the U.S., Japan, and Europe, we expect to see a significant rise in counterfeiting, especially in Asia. Other companies within the boardsports industry have experienced widespread counterfeiting in Asia with the growth of their brands. Although we protect our brand through trademark registrations in many different countries, we simply do not have additional resources to fight counterfeiting on a large-scale.

Even if resources were available, we know the tools to be largely ineffective. Beyond trademark registration and filing with Customs officials, there are very few options. Suits in foreign countries alleging unfair competition are expensive, time consuming, and ineffective. They certainly are not a deterrent to the thieves. Moreover, insurance policies do not cover a company such as Burton against losses due to IP theft.

While counterfeiting of our Hardgoods (snowboards, boots, and bindings) has not been substantial to date, we anticipate a growing problem with counterfeiting and factory leaks as we expand our business operations. Burton invests heavily in research and development on our Hardgoods to ensure production and sale of top-quality products. Additionally, Burton takes all available measures to produce equipment according to high safety standards; and we stand behind the quality of our product. Counterfeiters care little for the quality of the products they sell under our good name. In turn, counterfeit products that fail to adhere to our high safety standards put the public at risk, and inevitably damage our industry and our brand. They also undermine the investments we make in the development and implementation of new safety features.

Clearly IP theft is a significant and costly problem and there are too few tools available to combat it. The tools that are available are expensive and ineffective. The persons who profit most from counterfeiting are rarely caught or punished. The most serious threat they face is a confiscation of their fake goods. What are sorely needed are effective laws and vigorous enforcement mechanisms. Additionally, the United States should provide technical and monetary assistance to developing nations to improve their anti-counterfeiting efforts.

"COUNTERFEITING AND THEFT OF TANGIBLE INTELLECTUAL PROPERTY: CHALLENGES AND SOLUTIONS"

Written Testimony of

Timothy P. Trainer
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Before the
United States Senate
Committee on the Judiciary

Washington, D.C.
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Mr. Chairman and Members of the Committee, good morning. I am Timothy Trainer, President of the International AntiCounterfeiting Coalition (IACC). On behalf of the IACC, I thank the Committee for the privilege and opportunity to address the very important issue of product counterfeiting and piracy.

The IACC is the largest organization dealing exclusively with issues involving intellectual property (IP) counterfeiting and piracy. The organization has approximately 140 members representing a cross-section of industries, including the automotive, electrical, entertainment, software, apparel, luxury goods, tobacco, personal care, pharmaceutical and office product sectors. The total annual revenues of IACC members exceed US$650 billion.

Today, the global proliferation of product counterfeiting and piracy threatens consumers, governments and companies. Product counterfeiting and piracy is a revenue generating tool of organized crime and threatens national economic security. In addition to the growing organized crime element, counterfeiters act with reckless disregard for consumers. This generation of product counterfeiters does not recognize national borders and counterfeits all types of products.

RECOMMENDATIONS

At the outset, the IACC respectfully requests that this Committee and Congress consider implementing the following package of recommendations to combat the scourge of counterfeiting and piracy that exists:

- Raise the stakes for the individuals involved—the federal criminal statute against trafficking in counterfeit goods should be strengthened;
- Encourage federal law enforcement agencies to cooperatively pursue investigations of counterfeiting to root out and prosecute manufacturers, distributors and others involved in the trafficking of counterfeit goods;
- Increase the level of vigilance at the border regardless of the products involved—counterfeiting and piracy impact national economic security;
- Impose higher intellectual property enforcement standards on trading partners who seek trade preferences to access the world's greatest market;
- Support Interpol's effort to improve cross-border coordination to combat the international trafficking in counterfeit goods; and
- Examine the extent to which organized crime is involved in the international trade of counterfeit and pirated products.

GLOBAL COUNTERFEITING

On February 12, 2004, the IACC identified 27 countries in its Special 301 report that was submitted to the U.S. Trade Representative for inadequate and ineffective protection of intellectual property assets. Only time and resources prevented the IACC from submitting a report that identified more countries. While most consumers and government officials who are not intimately involved in intellectual property theft and

crime may be very familiar with the flea market and street vendor products such as shirts, handbags, sunglasses and other similar items, the expansion of counterfeit activity into products posing public health and safety risks is proliferating. Examples of these products include:

- Pharmaceuticals;
- Auto parts;
- Toys;
- Batteries;
- Extension cords;
- Cosmetics;
- Beverages;
- Body lotions;
- Home electrical appliances;
- Tools;
- Vision wear; and
- Bearings.

This is not an exhaustive list, but underscores the products that are now counterfeited here and around the world and the global nature of this problem.

An IACC member auto company's raid of a Chinese auto parts factory uncovered 7,000 sets of counterfeit brake pads intended for export to Egypt. This single raid represents potential losses of nearly $330,000.[1] Another auto industry member reported raids resulting in the seizure of thousands of counterfeit windshields and several thousand suspension control arms, valued at nearly $4 million dollars. A third auto industry member estimates that 50%-60% of counterfeit parts bearing its trademarks found in the world are made in China.

The auto industry is also confronted by a massive parts counterfeiting problem in India. IACC member auto companies report counterfeit parts make up 20% to 30% of the Indian market. The auto industry as a whole is suffering parts counterfeiting that is reported to be over 35% of the market and valued at roughly $434 million dollars in that country.[2]

While not as mechanically sophisticated as automobiles, the Uganda Manufacturer's Association complains of counterfeit bicycle parts posing risks for citizens of that country.[3]

Another IACC member, whose certification mark is relied upon as a mark of safety, reported that our federal border enforcement authorities seized 91 shipments of

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[1] *Stolen Cars*, Forbes Magazine (February 16, 2004).
[2] *Spurious Automobile Parts Industry Turning 'Organised'*, India Business Insight (December 5, 2003).
[3] *Roadmaster Asks for Tougher Laws On Counterfeit Products*, Africa News (June 12, 2003).

counterfeits bearing its mark in fiscal year 2003. These seizures included a seizure of US$1.5 million in air compressors that had counterfeit ground fault circuit interrupters, $700,000 of counterfeit extension cords, power strips and hair trimmers that, in turn, led to an additional $7 million seizure of counterfeit extension cords and power strips. In addition to the Customs seizures, another $1 million seizure of Chinese made counterfeit portable and hand tools was made by police in southern California.

In Australia, an investigation of two Australian nationals led to the discovery of a massive counterfeit operation of Chinese-made counterfeit batteries and razors. Three containers heading to different ports – Dubai, Oman and Los Angeles – were seized having counterfeit goods valued at $1.5 million.[4] Australian authorities also seized two shipments (50,000 bottles) of counterfeit shampoo from China bearing the trademark of a famous brand.[5]

Counterfeit vodka in the United Kingdom caused hospitalization when the vodka was tested and found to have dangerous levels of methanol.[6] As a result of the detection, authorities issued a description of the bottle and labels that were applied to the bottle to assist potential consumers in identifying the counterfeits. In December 2003, another counterfeit vodka problem arose when a woman went into a coma after consuming counterfeit Kirov brand vodka.[7] It was the second time in 2003 that supplies of counterfeit vodka with high levels of methanol had been found.

Counterfeit batteries have also posed a threat to consumers. A boy playing with a toy that had a counterfeit battery suffered facial injuries from an exploding battery and a man suffered injuries to a hand when his remote control exploded from the use of a counterfeit battery, both incidents in Malaysia.[8] Canadian authorities seized 60,000 counterfeit "Duracell" batteries before the holiday season and warned consumers because of potential hazards if used in toys.[9] Nokia found that counterfeit batteries used in connection with their cell phones were exploding as reports of such incidents were widespread—from Vietnam to the Netherlands.[10]

Russia's chief trade inspector and department head at the Economic Department and Trade Ministry noted that for certain categories of consumer items, 30-50% of the Russian market consists of imitations. These product lines include alcohol, juices, butter, vegetable oil, canned foods, tea, coffee, cosmetics, clothing and footwear.[11] Other sources similarly indicate that up to 50% of the perfume and cosmetics markets are fakes.[12]

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[4] *Counterfeit Gang Foiled,* The Sunday Telegraph (January 4, 2004).
[5] *Shampoo Didn't Wash,* Herald Sun (December 25, 2003).
[6] *Alert Over Danger Vodka,* Aberdeen Evening Express (March 22, 2003).
[7] *Poison Vodka Alert,* Manchester Evening News (December 9, 2003).
[8] *Imitation Battery Warning,* Malay Mail (October 10, 2003).
[9] *Bogus Batteries Pose Safety Threat,* The Vancouver Sun (December 12, 2003).
[10] *Phone Go Boom,* Money (January 2004).
[11] *Beware of Buying Fakes!,* Moscow News (December 3, 2003).
[12] *Survey: 50% of all Perfumery Faked,* Moscow News (December 24, 2003).

DOMESTIC INCIDENTS

As mentioned above, the auto industry is experiencing significant counterfeit auto parts. Substandard and counterfeit heavy-duty truck replacement parts are also getting into the U.S. aftermarket in significant numbers and the problem is likely to get worse according to the industry.[13]

In the power tool industry, a trend that was noticed in Europe is now appearing in the United States. Counterfeit power tools are making their way into the United States and pose risks due to substandard parts and their failure to stand up to the type of use that genuine tested products can withstand. The counterfeit tools are also appearing on the internet for sale. The Power Tool Institute has raised the caution flag on these products.[14]

The United States has enjoyed a safe pharmaceutical distribution system. In recent years, however, the United States has also seen several counterfeit pharmaceutical cases arise, including the Lipitor cases of a year ago. Although the level of counterfeit pharmaceuticals in the U.S. remains far below that of some developing and very poor countries, the cases that have arisen have prompted the Food and Drug Administration to assess the level of risk that is involved for the introduction of counterfeits into the U.S.

U.S. law enforcement authorities are being tested by those who trade in counterfeits. U.S. authorities broke up a ring in Texas that is believed to have imported over 100 million counterfeit cigarettes, mislabeling shipping documents by indicating that they were importing toys or plastic parts.[15]

Recent reports also indicate that product counterfeiting has invaded the pesticide industry. An Alabama man pleaded guilty to a 28-count indictment for selling counterfeit pesticides to several municipalities. The municipalities purchased the pesticides to combat mosquitoes and the West Nile virus.[16] Counterfeit products also pose risks to our environment and pets. Recently, the Environmental Protection Agency (EPA) issued an alert regarding counterfeit pest control products for pets.[17] The EPA indicated that there has been an increase in the influx of counterfeit goods because of product in counterfeit packaging bearing all indications of legitimacy.

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[13] *Counterfeit Parts: Buyer Beware*, Fleet Owner (March 1, 2004).
[14] *Counterfeit Power Tools Appear in United States*, Assembly (February 1, 2004).
[15] *Tobacco-Smuggling Ring Busted*, The Dallas Morning News (January 29, 2004). The international trade in counterfeit cigarettes is extremely challenging to law enforcement around the world. For example, Associated Press Worldstream reported that Austrian authorities charged seven people with smuggling over $19 million worth of counterfeit cigarettes, which were described on shipping documents as kitchen utensils, scooters and suitcases (July 29, 2003) and the Mail on Sunday (London) reported that U.K. Customs arrested ten Polish nationals after 44 million counterfeit cigarettes were discovered in eight containers that had arrived from China in the summer of 2003 (August 3, 2003).
[16] *Man Pleads Guilty in Pesticide Scam*, Birmingham News (January 6, 2004)
[17] *Alert Issued on Phony Anti-Flea Products*, San Diego Union-Tribune (March 6, 2004).

In one case that has involved civil and criminal judicial proceedings, the focus was on the theft of trade secrets and sale of counterfeit fiber optics products and LED lighting.[18]

In the past few years, the IACC has seen an increased level of concern by many industries about the rise in counterfeits. This has prompted several industry associations to reach out to us in order to improve awareness and knowledge about counterfeiting in various industries, including those that manufacture and distribute electrical products, small appliances and personal care products.

Given that we are all aware of the counterfeit goods sold in flea markets and on the streets of major cities, the added knowledge that counterfeiters have moved into auto parts, medicines, home appliances and electrical goods should give us pause to start thinking of the counterfeiting problem as a frontal attack on consumer safety and economic stability.

CHALLENGES/SOLUTIONS

Because no industry sector is immune from attack by counterfeiters and no country is exempt from this type of criminal activity, both corporate and governmental law enforcement resources must be committed to combating IP crime. The volume of goods being seized is a clear indication of large scale manufacturing and a sophisticated distribution and sales network. Thus, the challenge of a global counterfeiting problem is one that must be fought with the cooperation of our trading partners and relevant intergovernmental organizations such as INTERPOL and the World Customs Organization.

IP crime is occurring globally and, thus, poses risks to consumers worldwide and, as a result, U.S. IP owners must invest resources to combat this problem in many countries around the world given that their IP assets are subject to protection and attack in many countries.

Initially, U.S. domestic laws against trafficking in counterfeit goods must be strengthened in order to permit the destruction of counterfeit goods and the authority to take the tools, i.e., the equipment used to make counterfeits, out of the hands of those involved and ensure that they are not available, which may mean destruction. Moreover, courts must see **ALL** counterfeiting, regardless of the type of products involved, as potentially a criminal act that also involves a network and be willing to impose penalties that will deter future counterfeiting. In addition, strong domestic laws will permit U.S. negotiators to try and obtain stronger anti-counterfeiting and anti-piracy provisions in bilateral and international agreements with trading partners, which is needed in the face of the overwhelming tide of counterfeits that U.S. IP owners must combat.

In addition to domestic laws and those agreements in which the U.S. is a Party, the U.S. Government should monitor trade agreements between our trading partners that do not

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[18] *Super Vision International Announces Conspirator in Super Vision Technology Theft Sentenced*, Business Wire (January 2, 2004).

include the U.S. as a Party. In view of the efforts of the U.S. Government to strengthen IP enforcement for U.S. industry, these efforts may be undermined when our trading partners conclude agreements that may facilitate the flow of goods to third countries, decreasing or eliminating inspections upon entry or exit of goods and make the flow of counterfeit and pirate goods easier between third countries where U.S. industry is present and trying to protect their IP assets. Our companies have obtained trademark and patent rights in many countries, but if trading partners fail to incorporate strong IP enforcement provisions with ALL of their trading partners, we run the risk of seeing the protection of U.S. IP assets weakened abroad.

The U.S. Government should also be vigilant regarding free trade zones as these zones are being used to facilitate the trade in counterfeit and pirated products. We request that the U.S. undertake a special effort to ensure that trading partners apply their IP enforcement provisions within free trade zones. We need to underscore the fact that free trade zones are to facilitate legitimate trade, not an area where Governments look the other way when illegal activity is occurring and, in some cases, flourishing.

The current onslaught of global counterfeiting has another "health" aspect to it. This is the health of industry. The current level of global counterfeiting diverts corporate resources away from the business of research and development that leads to new and better products for consumers. Today's level of counterfeiting has reached the point that it now requires government intervention to confront the organized crime elements that are involved around the world. Industry is neither equipped to deal with organized crime nor is it a function for industry to pursue. Because of a reluctance to combat product counterfeiting in the past, we now see it as a real and dangerous threat to consumers and industry.

CONCLUSION

While we have concentrated on counterfeiting that involves goods that have a direct public health and safety aspect, we cannot overlook the fact that treating any type of counterfeiting, whether of handbags, shirts, or watches, as a victimless crime will only attract criminal elements to this type of easy money activity. The present situation begs the question: Where does the money go? We have yet to know exactly where the money goes, but do we dare to take the risk that some of the funds land in the hands or accounts of individuals or groups that will do the unthinkable. A multi-pronged effort is needed to take more aggressive enforcement actions, implement a broad strategic plan to target sources, educate consumers and train government officials and business leaders in ways to make IP enforcement more effective.

Franklin J. Vargo
Vice President
International Economic Policy

March 31, 2004

Honorable Orrin Hatch
Chairman
Honorable Patrick Leahy
Ranking Minority Member
Senate Judiciary Committee
SD-224
Washington, DC 20510

Dear Mr. Chairman and Senator Leahy:

The National Association of Manufacturers (NAM) wishes to submit this statement for the record of the March 23, 2004 hearing on intellectual property theft, to supplement the testimony of Mr. Richard K. Willard, Senior Vice President and General Counsel, The Gillette Company.

Questioning of witnesses appropriately went to the question of the deterrent effect from federal criminal enforcement against piracy and counterfeiting. The witness from the Department of Justice stated the view that, at current criminal enforcement levels, a deterrent effect can start to be seen. There was no suggestion that mere civil actions would deter anyone from entering the lucrative field of product counterfeiting.

More urgent, however, is deterrent effect – or the lack of it – around the world, especially in China. China's civil enforcement is not *de minimis*, yet it lacks any meaningful deterrent effect. This was essentially the major topic of discussion between U.S. industry representatives and the Chinese intellectual property delegation that was in Washington to prepare for the upcoming Cabinet-level meeting of the Joint Commission on Commerce and Trade. At a meeting held at the Patent and Trademark Office on March 18, Chinese authorities cited some very specific statistics, for example, regarding seized pirate compact disks. In addition, some prison sentences are now being administered.

Manifestly, however, current enforcement efforts do not have a deterrent effect and do not shut down illegal enterprises permanently. The televised report on CBS's *Sixty Minutes II*, "The World's Greatest Fakes" (January 28, 2004), goes straight to this phenomenon. What is needed, beyond even seemingly impressive numbers and a small if growing number of prison sentences, is mandatory destruction and seizure not only of articles for sale but also of machine tools and computers (the enclosed NAM presentation at the U.S. Embassy workshop held in Beijing last November 18, which emphasizes this point).

Honorable Orrin Hatch
March 31, 2004
Page Two

The Office of the U.S. Trade Representative, however, finds itself in an awkward situation in this regard. Essentially, it needs to press for tougher enforcement than the United States affords at home. In an almost unbelievable weakness, Section 2320 of the criminal code does not – unlike Section for 2318 for copyright piracy – mandate such seizure and destruction even when a conviction is obtained domestically.

As Mr. Willard noted, the position of USTR not to negotiate for stronger protection abroad than Congress has afforded domestically is reasonable. Otherwise, Congress would have to amend the criminal code as part of ratifying a trade agreement, which could raise a process issue even if the substance were well-founded. I have enclosed the detailed language that the NAM has provided to USTR to fight counterfeiting. The NAM strongly regrets that the opportunity has been missed to incorporate these necessary tougher provisions into the latest round of free-trade agreements.

Bolstering the U.S. negotiating position with respect to enforcement in China and elsewhere, and in negotiating new trade agreements, is even more urgent than improving our own law for domestic enforcement. Thus, in a real sense, the fight against fakes around the world starts with the Judiciary Committees in Congress. The NAM strongly welcomes Senator Specter's expressed intent to introduce legislation and urges you to move this legislation through the Senate this year. No further weakness in the U.S. position relative to foreign governments in turning the tide against counterfeiting is acceptable.

Sincerely,

Franklin J. Vargo
Vice President
International Economic Policy

Enclosures (2)

cc: Senator Specter

Franklin J. Vargo
Vice President
International Economic Policy

September 4, 2003

The Honorable Robert Zoellick
United States Trade Representative
600 17th St., NW
Washington, DC 20506

Dear Ambassador Zoellick:

As the United States proceeds to negotiate new Free Trade Area (FTA) Agreements, the National Association of Manufacturers (NAM), comprising 14,000 companies in every industry segment, wishes to stress the importance of effective measures against product counterfeiting. The International Chamber of Commerce now estimates that counterfeiting comprises seven to nine percent of world trade. In that regard, the NAM welcomes the increased emphasis on product counterfeiting in this year's Special 301 Report.

The NAM recognizes the outstanding work that your office has accomplished in the FTA Agreements with Chile and Singapore, and we congratulate you on congressional approval and presidential signature of those pacts. In particular, the Singapore and Chile texts in most respects set a good standard for provisions against counterfeiting.

Nonetheless, we believe it is necessary to go a little farther and would like to propose that an ideal model text, relative to trademark protection and fighting counterfeiting, consist of a modified Singapore text. We seek specific improvements in three topics. We ask that this improved text be used immediately with respect to negotiations already underway, or about to commence, with Australia, Morocco, the South Africa Customs Union, and Central American countries, as well as all other future negotiations.

We have enclosed specific language with explanatory notes to achieve these ends. David Peyton, director, technology policy, will follow up with Mr. Mendenhall and his staff.

Sincerely,

Enclosure

Manufacturing Makes America Strong
1331 Pennsylvania Avenue, NW • Washington, DC 20004-1790 • (202) 637-3144 • Fax (202) 637-3182 • fvargo@nam.org • www.nam.org

Explanation of Model FTA Provisions on Trademarks and Product Counterfeiting

The NAM sees model anti-counterfeiting text as comprising the Singapore text with the following modifications.

1. Madrid Protocol Ratification

The Singapore FTA provides, "Each Party shall make best efforts to ratify or accede to...the Madrid Agreement..." (Chapter 16.1.2(c)(ii)). The U.S. now has ratified the Protocol itself, as have Australia and Morocco, and the Patent and Trademark Office is well along in implementing the U.S. accession, effective on November 3. Accordingly, it is time to delete "best efforts," such that the new clause reads,

Each Party shall ratify or accede to...The Madrid Agreement....

Given the U.S. experience, we concur in allowing other parties one year to ratify and give effect to Madrid, as in Singapore's Chapter 16.10.1(b).

2. Injury and Deterrence

With respect to civil enforcement, the Singapore and language does not go as far as it should. The language could be greatly improved by replacing "consider" with "rely upon," to preclude the possibility that injury will be calculated on some other basis.

[I]n determining the injury to the right holder, the judicial authorities shall, inter alia, rely upon *the value of the infringed-upon good or service, according to the suggested retail price of the legitimate good or service.* (Singapore Chapter 16.9.8, as amended).

For criminal enforcement, the Singapore text has advisory language that should be strengthened to contain direct instructions on penalties (as does the Chile agreement), worthy of being carried forward in future FTAs:

[E]ach party shall provide...remedies that include imprisonment as well as monetary fines sufficiently high to deter future acts of infringement and present a level of punishment consistent with the gravity of the offense, which shall be applied by the judicial authorities in light of, inter alia, *these criteria.* (Singapore Chapter 16.21(a)(i), as amended)

3. Forfeiture and Destruction

The Singapore agreement represents the strongest language yet achieved by the U.S. on forfeiture and destruction. Nonetheless, it reflects an unjustifiable asymmetry and weakness in current U.S. domestic law. Section 2318 of the criminal code, on copyrights, provides for forfeiture and destruction not only of articles for sale but also for equipment used to produce the pirated articles. Section 2320, on trademarks, goes only to the articles for sale. Without question, machine tools and servers must be seized and disposed of so as to put counterfeiters out of business permanently, perhaps even more so abroad than in the U.S. Rectifying this inadequate provision is one of the key objectives in draft legislation that the NAM is supporting before the House and Senate Judiciary Committees. Given the current unacceptable state of domestic law, the Singapore language reads, at Chapter 16.9.21(a)(iii),

...[I]ts judicial authorities shall, except in exceptional cases, order the forfeiture and destruction of all counterfeit or pirated goods, and, at least with respect to willful copyright or related rights piracy, *materials and implements that have been used in the creation of the infringing goods. Each Party shall further provide that such forfeiture and destruction shall occur without compensation of any kind to the defendant.*

The NAM believes that the highlighted phrase should be removed and anticipates that, by the time any FTA agreement is presented to Congress for approval, the necessary change in the U.S. criminal code already will have been made.

Anti-counterfeiting Issues in China Comments and Suggestions

Michael Shu,Legal Counsel, Gillette China

Representing National Association of Manufacturer(NAM)

Beijing,Nov.18,2004

Anti-counterfeiting Issues in China

About NAM:

The NAM is the largest industrial trade association in the States. We represent 14,000 members (including 10,000 small and mid-sized companies) and 350 member associations serving manufacturers and employees in every industrial sector and all 50 states. Headquartered in Washington, D.C., the NAM has 10 additional offices across the country.

Gillette's Senior VP and General Counsel, Mr. Richard Willard, chairs Product Counterfeiting Working Group.

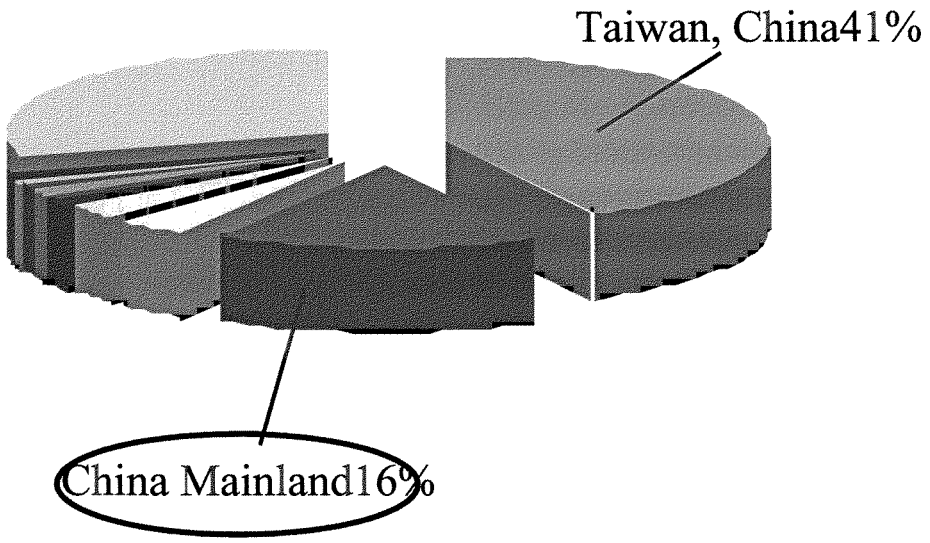
Anti-counterfeiting Issues in China

For Gillette, China remains the country with the highest level of production of counterfeit goods, in our case razors, and batteries. Counterfeited Gillette products were exported to North America, Europe, South America, Africa and FSUs, from China.

When asked, most other NAM member companies also cite China.Our sense agrees with the seizure statistics from the U.S. Customs:Half of goods seized for an intellectual property violation have come from China.

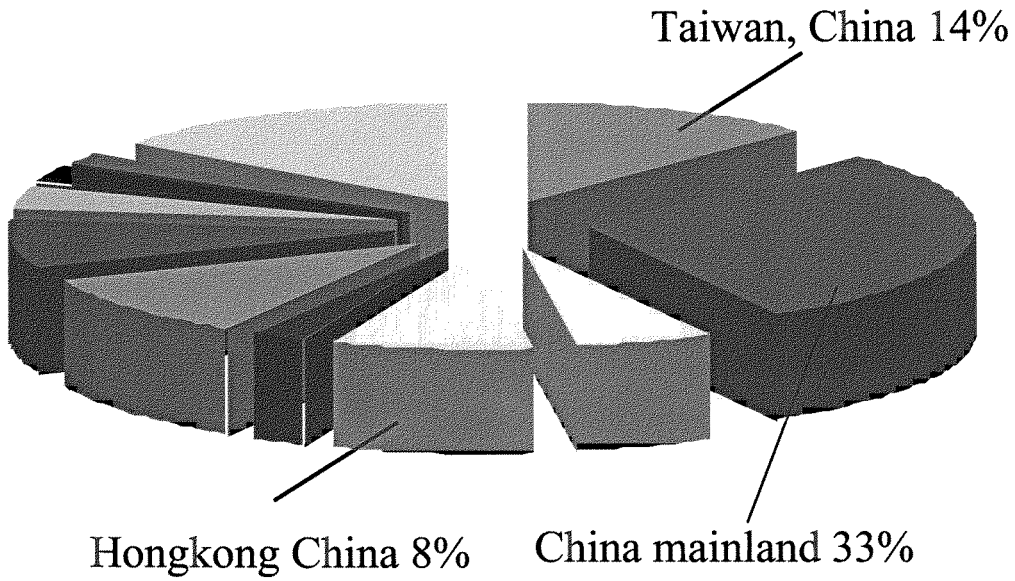
1999 US Customs IPR Seizures

(Source: US Customs website)



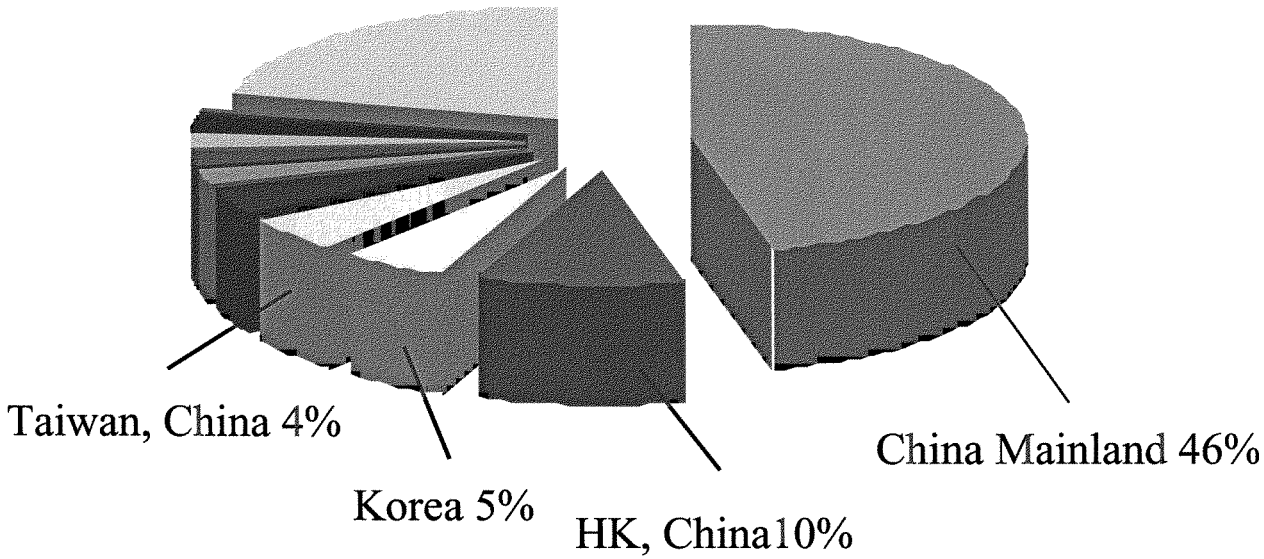
2000 US Customs IPR Seizures

(Source: US Customs website)



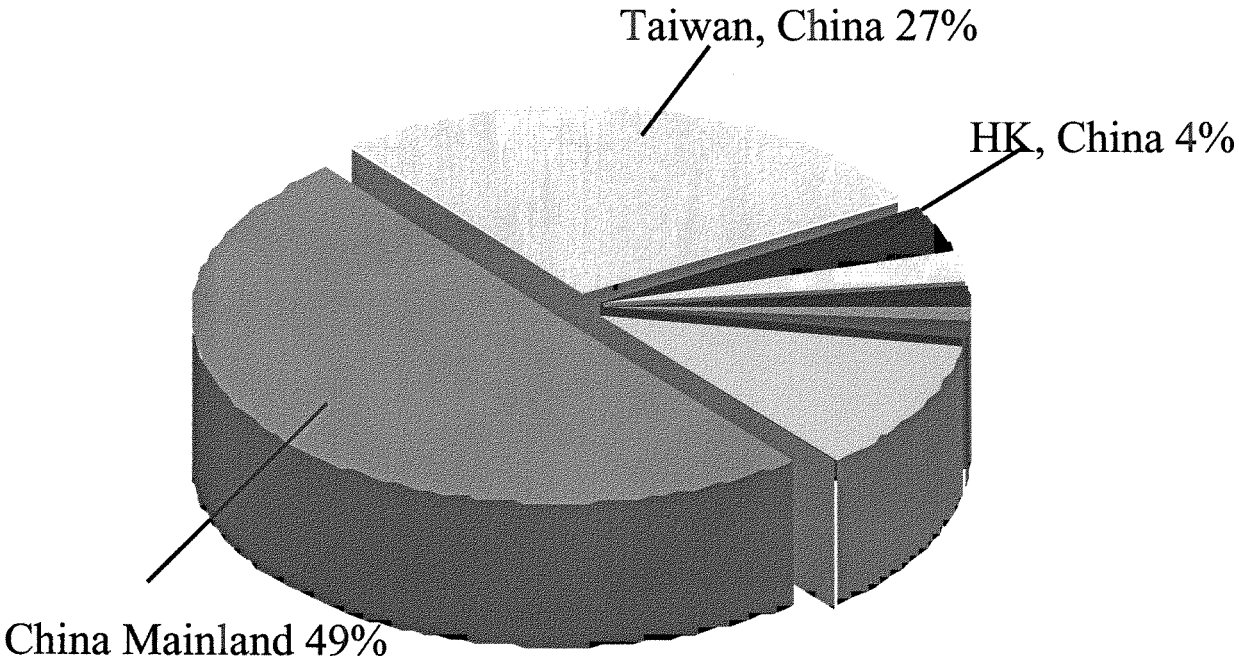
2001 US Customs IPR Seizures

(Source: US Customs website)

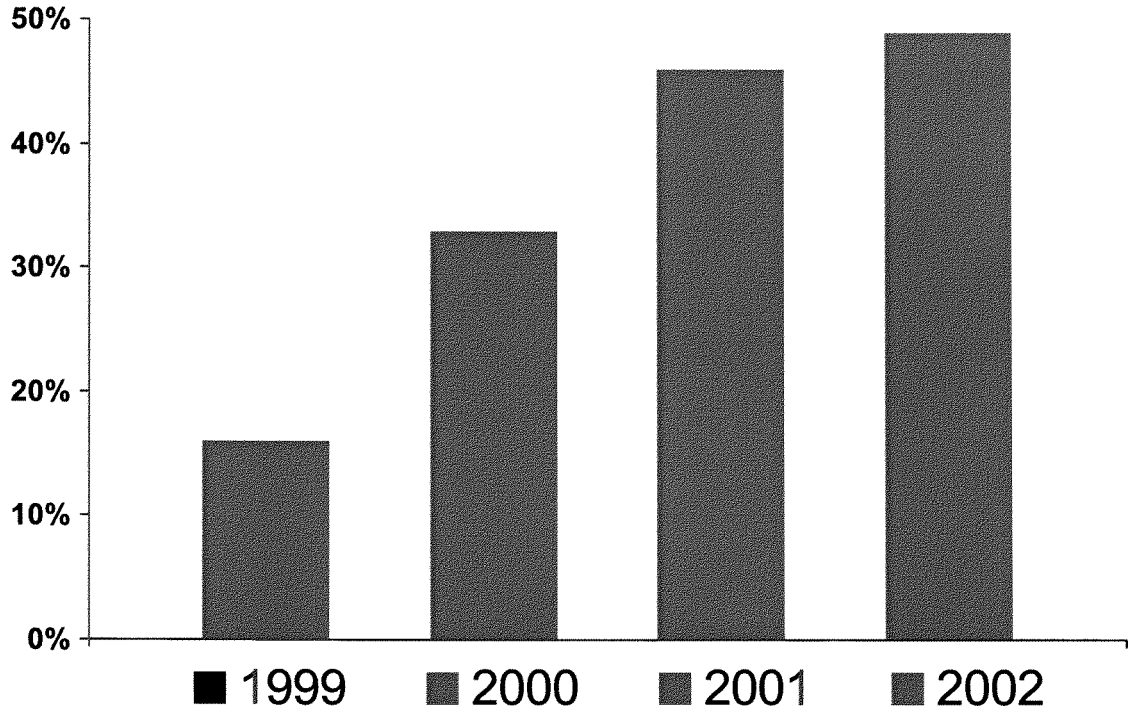


2002 US Customs IPR Seizures

(Source: US Customs website)



The Export of Counterfeits from China Increasing Rapidly
(Exclusive of Taiwan and HK)



Anti-counterfeiting Issues in China

We understand that national authorities face a large problem with enforcing compliance at the local level.

We need to pay more attention to local protectionism. The trend is that counterfeiters are moving toward to China‘s developing areas, where local governments needs more investments to develop local economy and fix employment issue.

The big players, the repeated offenders should be put in jail.

Anti-counterfeiting Issues in China

Gillette once had a case, the counterfeiter continued to manufacture counterfeits, just the next day after the criminal hearing, unfortunately he was just suspended.

We are not expecting miracles and we will help the best we can.

Anti-counterfeiting Issues in China

The goal must be steady annual improvement.

A year from today, we need to be able to say that egregious offenders have been prosecuted and put in prison. Their equipment has been seized **and destroyed** and their businesses closed permanently.

We need to be able to say that more counterfeit product has been seized before leaving the country.

And then we will need to sustain the effort for years.

Anti-counterfeiting Issues in China

We do not mean to suggest that there are no bright spots.

Hong Kong is demonstrating that it is able to serve as reliable portal into China.

Customs, police, and judicial authorities in Hong Kong cooperate effectively.

Anti-counterfeiting Issues in China

We believe that there are good opportunities for improved coordination between Hong Kong and the rest of China.

Furthermore, all enterprises,domestic and foreign-based, would be well served if all China local governments were to implement the measures that have proved effective in Hong Kong.

Anti-counterfeiting Issues in China

Suggestions to US Government:

1. Pay more attention to local protectionism in China;

2. Urge China Customs to transfer IPR infringement cases to police for further investigation and then followed by criminal prosecution.

Anti-counterfeiting Issues in China

At 5 to 7 percent of world trade, counterfeiting has become a serious problem for the world economy.

Consumers are endangered.

The time has come for a coordinated effort to reverse the worsening situation around the world.

With mutual benefit and cooperation, we believe that this goal can be reached.

Testimony by Assistant Secretary of State for Economic and Business Affairs E. Anthony Wayne before the Senate Judiciary Committee March 23, 2004

Mr. Chairman and other distinguished members of the Committee, I want to thank you for giving me the opportunity to talk about the protection of American intellectual property overseas. The State Department appreciates the Committee's efforts to bring more attention to this very important issue.

In the State Department's Bureau of Economic and Business Affairs, we have a Mission Statement that hangs on our office walls in the Bureau. One of the priorities listed in that Statement reads, "Increase market access for U.S. goods and services, protect intellectual property and promote global information technology and communications."

Today, I would like to explain what we are doing, both here in Washington and in our embassies and consulates overseas, to translate this part of our Mission Statement into action.

Importance of Intellectual Property

No one can doubt the increasing importance of intellectual property to the U.S. economy. Studies have indicated that over 50 percent of U.S. exports now depend on some form of intellectual property protection, compared to less then 10 percent fifty years ago. The World Intellectual Property Organization estimates that copyright industries alone contributed $791 million, or 7.75 percent, to the U.S. economy in 2001. The economic contributions provided by patents, trademarks and other forms of intellectual property are more difficult to quantify, but nonetheless just as important as those provided by copyrights.

As the importance of intellectual property rights have grown, so too have the challenges associated with their protection. Estimates of U.S. companies' worldwide losses to counterfeiting and piracy range from $200 to $250 billion per year. Last year's Special 301 Report from USTR named this problem for what it is: a "global scourge."

Part of the challenge today is being driven by new technology: with CD burners, you can now make pirated copies of music and movies on a commercial scale in the back rooms of small residences rather than large factories, making this crime all the more difficult to detect, and stop.

But the new challenges posed by digital technologies should not lead us to ignore the massive and growing problems in tangible piracy and counterfeiting. Trademark theft remains one of the largest and most widely spread of intellectual property crimes. The International AntiCounterfeiting Coalition's 2004 Special 301 submission lists 27 countries as having serious problems in this area, the most ever submitted by the organization. The list of counterfeited products noted in its report range from air compressors and shampoo in China, to cell phones and printer cartridges in Canada. As this problem grows, so too do related concerns about the health and safety of consumers who assume they are getting a genuine, not fake product; and about the involvement of organized crime and other unsavory actors.

The State Department is actively engaged in these issues through our function of protecting U.S. interests overseas. We care about intellectual property because American industry cares about it, because American artists and innovators care about it, and indeed, as evidenced by this hearing today, because the legislative representatives of the American people care about it.

There's another reason that we attach so much importance to this issue. We have a long-term goal of promoting peace and prosperity around the globe. That goal rests on our ability to encourage sound policies that will lead to increasing economic growth. Investment has to be part of this equation, and this is where intellectual property plays such an important role. Respect for patents, copyrights, trademarks and other forms of intellectual property protection is an essential element in any long-term economic growth strategy; not only is it needed to give innovators and artists the incentive they need to take risks with their talent, but it is also needed if countries are going to attract foreign investors and their technology.

The World Intellectual Property Organization has noted that a number of studies show a correlation in developing countries between a healthy intellectual property regime and foreign direct investment. The World Bank's Global Economic Prospects report for 2002 concluded that there are "reasons to believe that enforcement of intellectual property rights has a

positive net impact on growth prospects." The report also found that "across the range of income levels, intellectual property rights are associated with greater trade and foreign direct investment flows, which in turn translate into faster rates of economic growth."

There is a final set of issues that is making the protection of intellectual property an even more critical issue today. Counterfeiting and piracy in most countries around the world is a high margin, low risk activity. Combine that with a weak legal and law enforcement regime, as again we find in many countries, and you have a situation that invites organized crime and other actors to step in. INTERPOL has identified this as a serious and growing risk, and called for intellectual property crimes to be treated more seriously by governments around the globe. So in this sense, we see cracking down on intellectual property theft as part of our response to the new set of national security challenges we face as a nation.

So that's why we think the issue is so important. Now, what can be done about it?

Let me list three inter-related activities that need to be part of any sustained effort to improve intellectual property protection: building knowledge, building capacity and building will. At the outset, I want to underline that the State Department's actions in these three areas are coordinated with and supported by other federal agencies, such as USTR, the Commerce Department, including the Patent and Trademark Office, and industry, here and in our missions overseas. This truly is a team effort.

Building Knowledge

By building knowledge, I am referring to the need to increase awareness of intellectual property issues. At the State Department, each entering class of new Foreign Service officers now receives a briefing on intellectual property issues. They learn about pharmaceutical data protection, optical disk piracy and counterfeit Levi jeans. The world of diplomacy has changed dramatically, and we are adapting to it. This awareness training continues in courses we run for economic and commercial officers, for deputy chiefs of mission and for ambassadors, all designed to drive home to our people how important this issue is.

The greater challenge in the building knowledge area lies overseas. All too often intellectual property is seen as something that benefits only large American multinational corporations, or as something that has no relevance to local interests. Governments may believe that they can't afford the time or effort to protecting intellectual property, given so many other pressing needs.

We need to use every instrument in our diplomatic tool-kit to get the intellectual property message out. This includes activities such as raising the issue in bilateral meetings with government officials, sending foreign journalists to visit the U.S. to understand the issues better, sending U.S. academic experts to countries to give lectures, hosting digital video conferences with foreign counterparts, and having our ambassadors and economic counselors give speeches and write opinion pieces in the local media.

We need to spread the message that protection of intellectual property is good for these countries too, and in doing so build domestic constituencies that will also press for change. The U.S. Ambassador to Russia, Sandy Vershbow, last year wrote an op-ed piece that reminded Russians of their wonderful artistic heritage. He made the point that pirates and counterfeiters are threatening to kill off Russia's once-proud movie, literature and music industries. I have attached a copy of this op-ed to my written statement as an example of the type of work we are doing in the public diplomacy field.

We are also reaching out to non-traditional audiences to get our messages across. My colleagues and I at State often speak to young people both domestically and abroad about what we do in the Department on the economic front, and we use these opportunities to challenge their attitudes on piracy and counterfeiting. We talk to them about the potential to develop their ideas and creativity -- even to be a member of the next big rock group -- and how intellectual property protection is needed to make it all happen.

As another example of this non-traditional approach, one of our embassies will soon hold a reception featuring various members of the local entertainment community, including a singer will put on a short performance. The reception will also include various business and government officials involved in intellectual property protection. The message will be clear to all in attendance -- the future of the entertainers and

their potential to contribute to their country's culture will depend on the officials' ability to protect their work from pirates and counterfeiters.

Building Capacity

The second front in the fight to protect American intellectual property overseas concerns building capacity. And here too our efforts need to have one side that addresses our own needs, and another that addresses the needs of other countries.

On the home front, the State Department is improving the way it trains and equips its officers and embassies to deal with intellectual property issues, to complement the awareness raising programs mentioned earlier. We are using the Internet to link up officers in different posts facing similar problems, and disseminating background papers to help our officers better understand the issues they are handling. For example, just last week we sent a message to all overseas posts explaining why the issue of Geographical Indications, or GIs, is so important to the United States. Under GI proposals made by her European Union, U.S. companies would be forced to abandon names and terms that have long been established in the U.S. market, such as feta or gouda cheese and kalamata olives. In cases where a company is forced to abandon use of the term, it would lose the benefit of the reputation built up in that product, its market access, and the benefit of use of a well-known name. Although the losses are difficult to quantify, our industries are very concerned that they would be substantial.

We have a series of cables on other intellectual property-related topics planned for the remainder of the year.

As a further example, next month we are bringing together economic officers from a number of our embassies in Europe, North Africa and the Middle East to attend a conference on current intellectual property and telecommunications issues. I plan to fly over for this event, which will also include representatives from industry. This will give our mission officers a chance to hear the latest developments and, more importantly, to learn new approaches to intellectual property issues they can take back to their respective countries and put into practice -- for example, how to set up an Embassy Intellectual Property Task Force to focus efforts and improve coordination between policy and enforcement sections, how to use local media more effectively to get our intellectual property message out, or how

to set up a business advisory committee to assist a host government in drafting copyright or patent legislation.

We plan to hold similar conferences in other regions.

While on the topic of our internal capacity, I should also mention that our efforts on the intellectual property front have benefited greatly from the general increase in State Department staffing and modernization of technology brought about by the Diplomatic Readiness Initiative.

We are building up the State Department's capacity to address intellectual property issues because we recognize that one of our greatest assets in this area is our people. We have "boots on the ground" in all the countries where the major intellectual property issues are, so we need to make sure that the Americans and local staff serving in our embassies and consulates have the tools they need to be effective advocates of U.S. intellectual property interests.

In developing and transitional economies, we face a very different kind of capacity issue. Many of the countries where we see rampant piracy and counterfeiting already have laws on the books to prevent it. If the problem is not caused by a lack of political will, which I will get to in a minute, then it may very well have its roots in the lack of adequate domestic legal and law enforcement structures. Strong protection of intellectual property requires the working together of a large number of actors, from intellectual property officials to judges and prosecutors, from customs officials to cops on the street. Weakness in any one link can make the whole effort fail.

And ironically, the biggest losers in such a failure can often be the local artists and innovators whose struggle to get their talents recognized -- whether it be Brazilian musicians or Malaysian software designers -- is defeated by the pirates and counterfeiters.

We are helping to provide and coordinate assistance to these countries to improve their intellectual property regimes, both on a policy and on an enforcement level. The State Department chairs the government-industry IPR Training Coordination Group that, as its name implies, seeks to coordinate and maximize the effectiveness of different agencies and industries' training programs. The group is now looking at issues such as

best practices, and what type of training seems to work best, in order to improve performance.

In addition, the State Department, through the Bureau of International Narcotics and Law Enforcement Affairs, funds its own government-to-government training and technical assistance focused on building law enforcement capacity. Training for police, prosecutors, judges, customs, border and other officials involved in fighting intellectual property crime is provided through our network of International Law Enforcement Academies, bilaterally in country and also by bringing foreign officials to the U.S.

USAID also runs programs that have a broader focus of improving intellectual property regimes, often providing technical assistance with drafting of legislation or training of staff. In 2003, USAID spent $7 million on programs to assist developing countries in meeting their WTO-related intellectual property obligations. Other kinds of programs supported by USAID included assisting the government of Bolivia in combating the sale of pirated audio/video materials, and addressing the intellectual property dimension of promoting the development of agricultural biotechnology in Africa.

Building Will

We now come to the last, and in many cases, the most important aspect of protecting American intellectual property: building up the will to take action. The real test of this comes in our ability to convince foreign governments to take on the pirates and counterfeiters within their borders, and to implement and enforce strong intellectual protection rules. The other two aspects obviously play a role in this: raising knowledge of the issue, and providing needed technical assistance, can make the job easier and build a local constituency that can provide political cover for government actions. But sometimes that is not enough, and we need to take a tougher approach.

We have a number of ways to bring pressure on governments to act. The first tool used is raising the issue in a high-level bilateral meeting. Sometimes, just by making clear that this is an important issue to the United States and that other aspects of the relationship will suffer without progress, we can begin to see movement. The Secretary of State, Under Secretary for Economic, Business and Agricultural Affairs Al Larson, our ambassadors

around the world, and I have all delivered the message on intellectual property rights to our foreign counterparts. We see it as part of our foreign policy portfolio.

Another tool we use is the leverage provided in trade discussions, whether in bilateral or regional free trade agreements, or in a multilateral setting such as the WTO accession process. USTR has the lead on these efforts, but the message often is delivered through our missions overseas.

The Special 301 process, which will culminate next month, is another way to convince countries it is time to take action. Countries do not like seeing their names on a black list, and this threat is sometimes what is needed to prod them to do what they know they have to do. Again, I should note that this is a USTR-led process, but one which we actively support through the information gathered in our overseas missions on local intellectual property conditions.

When all these other efforts fail, then the U.S. can consider imposition of trade sanctions, either through our own programs such as Special 301 or the Generalized System of Preferences (GSP), or through multilateral dispute resolution such as in the WTO. Ukraine has had its GSP preferences withdrawn and a further $75 million in trade sanctions imposed under Section 301 because of its persistent failure to find the will to address serious problems in its intellectual property regime. This is obviously a tool of last resort, but it is one the State Department has supported when it was truly necessary.

Activities in Selected Countries

Having provided that background, I would now like to illustrate the types of actions being taken to address serious intellectual property problems in key countries.

China

- President Bush raised IPR issues with Premier Wen during Premier Wen's December 2003 visit to the United States.

- In November 2003, USTR led a high-level USG delegation to China, which included the State Department, to discuss Chinese implementation of its WTO commitments, including the vital IPR component.

- In November 2003, the U.S. Embassy in Beijing also held its second annual Ambassador's IPR Roundtable, bringing together over one hundred IP industry representatives with U.S. and Chinese government officials, to focus on China's IPR situation. Vice Premier Wu Yi accepted our invitation to deliver the keynote message at the event.

- Following up on this Roundtable, the Embassy compiled, summarized and delivered submissions and recommendations by participating IP associations to the Vice Premier.

- The U.S. Embassy in Beijing has developed a ten-point China IPR Action Plan in conjunction with U.S. industry. This IPR Action Plan identifies deficiencies in China's enforcement of IPR, as well as legislative issues in need of redress by the Chinese Government.

- As a result of coordinated pressure by the U.S. Embassy in Beijing in cooperation with U.S. industry in China, the Chinese Government has designated Vice Premier Wu Yi to head up China's efforts to address IPR concerns. In April of this year, the Administration will again raise our IPR concerns with her at the Joint Commission on Commerce and Trade.

- The USG expends significant resources providing technical training to Chinese judges, prosecutors, customs officials and other officials. The most recent large-scale training took place in October of 2003, when an interagency United States Government IPR experts team traveled to Beijing, Shanghai, and Guangzhou to train hundreds of Chinese Government prosecutors and law enforcement officials in areas such as protection of IP over Internet, procedures for collection of evidence for IPR crimes, and legal standards for opening cases against criminal networks involved in large-scale IPR counterfeiting and piracy.

Russia

- President Bush raised IPR with President Putin at the Camp David Summit in September 2003. As a result of that meeting, IPR was placed on a checklist of items and both government agreed to work more closely on the issue.

- Pressure from the Embassy, in coordination with efforts by other agencies over the growing number of pirated optical discs helped to convince the government to create an IPR Commission headed by the Prime Minister. Contacts indicate that Commission will be retained and headed by Deputy Prime Minister under the new government.

- Ambassador Vershbow and Embassy staff remain in regular contact with Russian officials and industry, pressing for stronger enforcement by Russian law enforcement agencies and passage of a stronger Copyright Law and separate Optical Disc Law.

- The Embassy has developed an IPR training program focused on law enforcement officials and funded through INL. Four seminars will be held in 2004 throughout various regions in Russia

- The State Department will fund an exchange program in 2004 between Russian and U.S. judges focused on civil IPR suits.

- The Embassy is currently developing an international visitor program for Russian officials devoted to "Intellectual Property Rights and New Technology."

Pakistan

- Secretary Powell and Under Secretary Larson were just in Pakistan, and ensured that intellectual property protection was on the agenda for meetings with government officials.

- In July 2003, the U.S. proposed a technically-comprehensive IPR Road Map to Pakistan that sets out goals in a number of areas. We plan to discuss this further at the inaugural trade and investment framework agreement meetings in mid-April.

- In January 2004, after much encouragement from the U.S., the Pakistani Cabinet approved legislation to create the Pakistan Intellectual Property Office (PIPRO). The government expects this legislation to be passed and enacted by Parliament by the middle of this year, or sooner if temporarily enacted by Presidential decree.

- Also in January, the government, with encouragement from our Embassy, launched the Intellectual Property Rights Advisory Committee (IPRAC), which is designed to increase coordination between the public and private sectors and serve as an impetus for reform. IPRAC includes representatives from several U.S. firms and other IPR stakeholders.

- In addition, new trademark regulations will be approved and published soon, and assume force of law. This is another step outlined in the IPR Roadmap.

Brazil

- Despite Brazil's severe problems with intellectual property right (IPR) enforcement, we have seen encouraging signs recently that the Government of Brazil may be looking for ways to improve IPR protection.

- In December 2003, Brazil had its first ever National Anti-Piracy Day, during which several well-known Brazilian recording artists joined political leaders to witness the televised destruction of half a million pirated CDs.

- The Investigative Commission on Piracy of the Brazilian Congress has taken the lead in the past several months in drawing public attention to the problem of the organized criminal activity and tax evasion that underlie many intellectual property crimes.

- The State Department is hosting a visit on March 25 of several members of this Investigative Commission. The congressmen will meet various intellectual property industry groups during their visit and will discuss ways of improving IPR enforcement.

Vietnam

- The Government of Vietnam is making progress in implementing the intellectual property provisions of the 2001 U.S.-Vietnam Bilateral Trade Agreement (BTA).

- As part of a USAID-funded $5 million program to implement the BTA, consultants have been hired to assist in drafting intellectual property legislation and to train intellectual property professionals.

- The U.S. Consulate in Ho Chi Minh City, working with the U.S.-Vietnam Trade Council, has set up Vietnam's first intellectual property law library, and has a program to continue training of library staff.

- The Consulate has also arranged for Ho Chi Minh City's Chief Justice -- before whom all intellectual property cases involving foreign interests are heard -- to receive training in Washington and other U.S. cities.

Mr. Chairman, we do not pretend to have the answer on how to stop growing intellectual property theft around the world, nor to claim that the activities I just mentioned above indicate that things are necessarily getting better. This is a huge global problem, and it will take time to resolve.

One thing we do know, however, is that whatever we do has to address the key aspects of the problem -- knowledge, capacity and will. This must be a team effort, involving numerous federal agencies, the Congress and industry. We must continue to do what we have been doing, attacking the problem from all angles. We look forward to working closely with all the stakeholders in this debate to improve our own performance, and to further America's intellectual property agenda.

As I close, let me urge members of the Committee to remain engaged on these issues, and to raise them with foreign officials, legislators and media in your overseas travel. Believe me when I tell you that foreign governments pay close attention to what you say and do.

Thank you again Mr. Chairman for this opportunity to be here today. I look forward to answering any questions you may have.

Statement of Richard K. Willard
Senior Vice President and General Counsel
The Gillette Company

"Counterfeiting and Theft of Tangible Intellectual Property: Challenges and Solutions"

before the
Committee on the Judiciary
United States Senate

March 23, 2004

Mr. Chairman and Members of the Committee, my name is Richard Willard, and I am the Senior Vice President and General Counsel of The Gillette Company. Gillette is a large, publicly held consumer product company based in Boston. The company manufactures and markets a broad range of products for shaving, personal care, and oral care, as well as alkaline batteries and small household appliances. Our brands include MACH3, Venus, Right Guard, Oral-B, Duracell, and Braun.

Gillette's Chairman and CEO, James M. Kilts, also serves as Chairman of the Board of the Grocery Manufacturers Association (GMA). GMA is the world's largest association of food, beverage, and consumer product companies with combined U.S. sales of more than $460 billion.

I am here today on behalf of Gillette and GMA. In addition, I chair a working group on anti-counterfeiting at the National Association of Manufacturers (NAM). My company also participates in the U.S. Chamber of Commerce and the International Anti-Counterfeiting Coalition, each of which is represented by its own witness at today's hearing

I am delighted to have the opportunity to testify before you on an issue of intense concern to Gillette and to U.S. manufacturers nationwide – the counterfeiting of our products. Today I would like to focus my comments on three problems: the increasing scope and danger of counterfeiting, the legal barriers to punishing offenders here in the United States, and the lack of adequate enforcement abroad.

Counterfeiting is a Devastating Global Problem

Counterfeiting, both domestically and internationally, adversely affects all businesses with successful brands – from automakers to pharmaceutical companies. While corporations that sell well-known, branded products are the obvious and direct victims of counterfeiting, this illicit activity also poses a real threat to the livelihoods and lives of workers and consumers, though many may not realize it.

When the average American thinks about counterfeit goods, he or she may think of phony Rolex watches, fake high-fashion handbags, or cheap knock-offs of designer T-shirts.

The purchasers of these items usually know the products are not originals, so they may readily conclude that buying a fake is no big deal, no harm done. What many consumers do not realize, however, is that this benign and somewhat limited picture of counterfeiting could not be farther from the truth. Counterfeiting is far more pervasive and dangerous than street vendors selling fake luxury items. In fact, only a minute portion of counterfeit goods are luxury items; most product counterfeiting has a far more immediate, and sometimes devastating, impact.

I can illustrate the far-reaching, and very real, effects of counterfeiting with the two small packages of batteries that I am holding. Both are labeled Duracell™. I can tell you a lot about the package in my right hand. I know exactly where and when it was made, its chemical composition, and how well it will perform. I can also tell you how much Gillette and the retailer can expect to make from selling it and how much the government will receive in tax on its sale.

I cannot, however, tell you much about the package in my left hand, because it is a counterfeit. All I can tell you is that the consumer will get a product for half the price that works about one-tenth as well as the real thing, and Gillette, its shareholders and employees, the retailer, and the government will get nothing. And the public stands to lose even more: Consider for a moment the consequences should the counterfeit batteries wind up in firefighters' flashlights and fail during a major rescue operation? The counterfeiter, a criminal, is the only one who stands to gain.

My battery example involves just one package of one product at one company. The magnitude of the problem at Gillette alone is staggering. Our lawyers are working alongside law enforcement agencies worldwide to identify and arrest counterfeiters. Recently in China, over the span of one week, we seized more than 1.5 million fake Gillette products that were destined for France, Russia, South America, the Middle East, and English-speaking nations. In one province, we seized a substantial amount of fake packaging for several of our products. In another, we recovered 100,000 counterfeit razor blades, 400,000 fake disposable razors, more than one million counterfeit Duracell batteries, and 40,000 fake Oral-B toothbrushes. Again, all of this is in just one week, in just two Chinese provinces, and involving just Gillette's products. Imagine how much bigger the problem is for all U.S. manufacturers and for manufacturers around the world.

To put the enormity of the problem in financial terms, the U.S. Customs Service estimates that counterfeiting activity costs the U.S. more than $200 billion annually and has resulted in the loss of 750,000 American jobs. Recently, the FTC stated that eradicating counterfeit auto parts could create 200,000 new jobs in the U.S. auto industry alone. The International Chamber of Commerce estimates that counterfeiting drains more than $350 billion each year from the world's economy – this is 7 to 9 percent of *total* world trade. And each dollar lost to law-abiding, hard-working American citizens and companies winds up lining the pockets of criminals.

Counterfeiting frequently is part of a larger criminal enterprise involving the theft of legitimate goods. Criminals responsible for distributing counterfeit goods are also often the ringleaders of organized retail theft. They have become expert in mixing counterfeit goods with stolen goods to "sanitize" the stolen goods and move them back into the supply chain. They feed

on those buyers or distributors who are willing to turn a blind eye in return for a good deal. Sometimes, the buyer is innocent. We have documented evidence of a U.S. retailer buying back the very stock stolen from it a few weeks earlier. Counterfeit distribution networks also ease the transport of illegal drugs into U.S. markets. Recently, heroin was discovered stitched inside fake Louis Vuitton and Chanel handbags recovered in the Northeast.

The danger of counterfeiting goes beyond mere financial harm and theft. Organized crime and terrorist groups use the sale of counterfeit goods to raise money for illegal activities and violence. The Basque separatist group, ETA, has been linked to the sale of counterfeit clothing and handbags. Paramilitary groups in Northern Ireland have funded terrorist activities through the sale of pirated products, including copies of Disney's The Lion King. Protection rackets in Italy no longer demand just money from retailers; instead, they want shelf space to sell counterfeit goods. Most alarming is that those who aim to terrorize United States citizens look to counterfeiting to help them achieve their deadly goal: Seized Al Qaeda training manuals recommend the sale of fake goods as a financing source for its terrorism.

In addition to aiding those who would intentionally harm us, counterfeiting leads directly to human suffering and death. Every day, thousands of sick people take counterfeit drugs that do nothing for them or, worse, hurt them. In the United States, there are dozens of recent cases involving everything from fake Viagra to phony meningitis vaccine. In China, the government-owned Shenzen Evening News estimates that 192,000 Chinese died in 2001 as a result of taking fake drugs. In a documented case in Nigeria, 100 children died after ingesting antifreeze that had been sold as a popular cough syrup.

We also know that fake automotive and aerospace parts are causing accidents with inevitable tragic consequences. In particular, the FAA has estimated that 2% of all replacement parts used on commercial airliners are fake, putting passengers at risk.

Counterfeiting is not a victimless crime. On the contrary, it causes devastating financial and physical harm to United States companies, employees, investors, consumers, patients, and citizens.

So what can be done? The problem of counterfeiting is complex, but many of the solutions are straightforward. We need stronger laws domestically, and we need cooperation internationally.

Changes in Law are Needed at Home

The first step in combating counterfeiting worldwide is to improve enforcement at home. We need to close some of legal loopholes that allow counterfeiters to escape prosecution, and we need laws that give enforcement agencies better tools to fight counterfeiting.

Current federal criminal law, as interpreted by the courts, allows counterfeiters to escape prosecution for trafficking in stolen goods by simply selling or distributing the counterfeit labels separately from the counterfeit products. This disconnect arises from two statutes, Sections 2318 and 2320 of the federal criminal code. Section 2320 makes it unlawful for anyone intentionally

to traffic in goods or services and knowingly use a counterfeit mark "on or in connection with" those goods. A recent case in the 10th Circuit Court of Appeals, *United States v. Giles*, held that a man could not be prosecuted for shipping fake Dooney & Burke labels to a buyer because the labels, while clearly fake, were not "on or in connection with" any counterfeit goods.

Section 2320 does not match Section 2318, which prohibits general trafficking in counterfeit labels and packaging, but only for albums, computer programs, motion pictures, and other audiovisual works. Congress should fix this problem: It should be illegal to traffic in counterfeit labels and packaging for *any* product.

These loopholes have global implications – international counterfeiters take advantage of them. We are now observing that in China, the assembly line and the packaging line are split as a deliberate strategy to avoid prosecution under current U.S. law. Counterfeiters ship their phony products to the United States without any brand markings, and the products pass through the port with no outward sign of any violation. These goods are then labeled, packaged, and wrapped here domestically, thousands of miles away from the actual point of manufacture. To stem the increase in counterfeited imports, we must be able to prosecute the people who do the labeling and packaging here.

In addition, Congress should expand the tools for law enforcement to combat counterfeiting. Law enforcement officials must have the ability to seize and confiscate not only the counterfeiter's inventory of phony goods, but also the equipment and assets – such as machine tools and computers – used to produce counterfeit products, labels, and packaging. Without this ability, law enforcement officers will be forced to chase the same counterfeiters over and over again. The counterfeiters can simply continue to use their infrastructure to replace seized inventory and resume their trade.

Finally, we suggest that Congress press forward to complete work it began two years ago to initiate a study of counterfeiting by earmarking money for a counterfeiting study. So far, the Department of Commerce has chosen not to commit funding for this study. Although Gillette in particular, and our manufacturing colleagues in general, is seeking to learn more on our own about markets for counterfeit, stolen, or illegally diverted goods, our efforts cannot take the place of a well-funded, comprehensive government study on the subject. The Department of Commerce should be urged to begin this study immediately.

Change Domestically Provides Leverage Globally

This afternoon, I have described the devastating global impact of counterfeiting. I have also suggested that this Committee might take action to close legal loopholes in current U.S. counterfeiting laws and strengthen law enforcement. These changes are vital for our anti-counterfeiting efforts here in the United States. But they are also essential to our ability to improve anti-counterfeiting efforts abroad. We need international cooperation, but we will not get it unless we first put our own house in order.

As much as we need mandatory seizure and destruction of counterfeiting equipment here at home, we need it even more overseas. The Office of the U.S. Trade Representative has made

clear, however, that it is not prepared to negotiate for mandatory confiscation and destruction abroad when U.S. law does not contain these provisions. Not surprisingly, our trade negotiators are loath to negotiate with other countries an agreement with which the United States could not comply under existing laws. We need to have mandatory seizure and destruction domestically right away so that our trade negotiators have a foundation to press for the minimum necessary enforcement around the world.

Finally, there is little prospect of making more progress in the fight against counterfeiting inside China unless its civil enforcement, currently limited to seizing inventory and imposing fines, is supplemented by more effective criminal enforcement with seizure and destruction of equipment and prison sentences. In some cases criminal enforcement does occur, but all too often counterfeiters continue in operation and view the occasional seizure of product as one more cost in an otherwise lucrative business.

China is the source of the vast majority of counterfeit goods sold in the United States. In addition to combating counterfeiting within its borders, the Chinese government also must stop the export of counterfeit products. The United States should work with the Chinese government to create an effective program to stop the trafficking of counterfeit goods at the point of export.

Now, around the globe, brand owners, industry coalitions, and governments are joining the fight against counterfeiting. This is not a problem we can solve overnight, and it is not a problem we can solve alone. We need global cooperation. To get it, however, we first need to close the loopholes in current federal criminal laws to criminalize trafficking in fake labels and packaging for all goods. We also need to provide our law enforcement agencies with authority to seize the machinery of counterfeiting. And we need to devote the resources to study this problem comprehensively, so that we can arm ourselves with more information about this problem in ways that will allow us more effectively to fight it.

I applaud the commitment and engagement of this Committee, as reflected in these hearings today, to renew governmental efforts to combat counterfeiting. In my testimony, I have described three modest measures that represent a ready starting point for these efforts. As leaders in global commerce, we owe it to shareholders, employees, and consumers here and around the world to protect the integrity of brand names and the quality of the products we sell.

Thank you for your time. I would be happy to answer your questions.

STATEMENT OF
CHRISTOPHER A. WRAY
ASSISTANT ATTORNEY GENERAL
CRIMINAL DIVISION

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

PRESENTED ON

MARCH 23, 2004

Mr. Chairman and Members of the Judiciary Committee:

Thank you for inviting me to testify before you today. This is an extremely important topic, and I commend you, Mr. Chairman, for holding this hearing. This hearing will provide the American public with an important look at the growing threat of intellectual property (IP) crime, particularly in the areas of piracy involving physical goods. Today I am pleased to share with the Committee, the Department of Justice's enforcement efforts in combating intellectual property crime.

We are at a pivotal time in the history of intellectual property rights enforcement. A number of factors have come together to create unprecedented challenges to intellectual property rights holders and to law enforcement. Some of these factors include the fact that:

- The value of intellectual property is increasing;
- It is now cheap and easy to reproduce and distribute copyrighted and trademarked products;

- Millions of illegal copies can be disseminated throughout the world with the simple click of a button. This makes detection more difficult than in the past;
- Every copy - whether in physical form or online – is perfect or near perfect;
- There is only sporadic and inconsistent enforcement throughout the world, which is compounded by the emergence of organized crime syndicates in international piracy and counterfeiting.

Mr. Chairman, there is no question that the intellectual capital of this nation is among our greatest resources. People around the world desire the products of the American creative community – be it entertainment, such as movies and music, clothing, shoes, or even pharmaceutical products. At the same time demand for American products increases, these products also become the target of criminals seeking to profit off the hard work and creativity of others.

Current technology gives intellectual property rights holders unprecedented opportunities to distribute their works to a worldwide audience. Likewise, there is far greater public access to all kinds of legitimate works. Unfortunately, as the factors I just described illustrate, the same technology has given criminals almost equal opportunity to commit massive and widespread copyright infringement and trademark counterfeiting. In many instances, resourceful criminals use technology to violate both trademark and copyright laws simultaneously by creating and selling products, such as software, which appear legitimate to the average consumer when in fact they are not. As I am sure others at today's hearing will testify to in great detail, this criminal activity has severely harmed American industry. The harms to our economy and our citizens should be plain. Businesses cannot survive in an environment where black market goods are more

available and cheaper than legitimate goods. Small businesses are forced to close and bigger businesses must downsize. Piracy also deprives consumers of their absolute right to be assured that the products they buy are safe and legitimate.

Under Attorney General Ashcroft, the Department has made the protection of intellectual property rights a law enforcement priority and has waged an extremely aggressive and successful campaign against IP crime. Specifically, we have focused our resources on complex, multi-defendant, multi-district and international, intellectual property cases. Large scale operations like Operation Buccaneer and Operation Safehaven, targeting online piracy, have struck at the heart of the highly-organized online piracy world. In Operations such as Buccaneer and Safehaven, which will be discussed in greater detail below, we have targeted the leadership of the organized online piracy world, known as the "warez" scene. As a result of these efforts, defendants are receiving the longest sentences ever imposed for online piracy – between 33-50 months. We are also reaching across borders to pursue prosecutions of foreign co-conspirators, in countries such as the United Kingdom, Sweden and others. We have also taken the unprecedented step of seeking extradition, from Australia, of one of the warez scene's most notorious and well-known figures. Geographic boundaries cannot be allowed to insulate pirates and counterfeiters from the reach of law enforcement. I would also note that this has all occurred in an environment where law enforcement resources and priorities have had to be realigned to respond to the threat of terrorism. Mr. Chairman, the Department's substantial and largely successful efforts have made significant inroads in the fight against global piracy. But this progress must continue, and we are committed to doing our part to combat piracy.

Since the beginning of his tenure, Attorney General Ashcroft has worked to ensure that the prosecutorial resources needed to address intellectual property crime are in place and managed efficiently and effectively. Since becoming the Attorney General, he has expanded the size and number of Computer Hacking and Intellectual Property (or CHIP) Units operating in larger U.S. Attorney's Offices from just one to thirteen. These specialized units consist of dedicated federal prosecutors, whose primary focus is prosecuting high tech crimes, including IP crimes.

The CHIP Units compliment the already existing network of Computer and Telecommunications Coordinators (CTCs) that serve in every United States Attorney's Office across the country. The CTCs regularly receive specialized training in the investigation and prosecution of high-tech crimes, including intellectual property crimes. Many of the 94 U.S. Attorneys Offices have two or more CTCs to help meet the growing demand for trained high-tech prosecutors.

Working closely with the CHIP Units and the CTC network is the Criminal Division's Computer Crime and Intellectual Property Section, also known as CCIPS. CCIPS is a highly specialized team of thirty-five lawyers who focus exclusively on computer and intellectual property crime. With the deeply appreciated support of Congress, we have significantly increased the size of CCIPS over the past two years, allowing us to substantially increase our IP enforcement efforts both here and abroad. For the first time, CCIPS has a Deputy Chief whose sole responsibility is to oversee and manage a team of attorneys in the Section dedicated exclusively to IP enforcement. At present, there are twelve CCIPS attorneys working full-time on the IP program. CCIPS attorneys are developing a focused and aggressive long-term plan to combat the growing

threat of piracy. They are continuing to develop and implement the Department's overall anti-piracy strategy, assisting AUSAs in the prosecution of intellectual property crimes, and reaching out to international counterparts to ensure a more effective world-wide response to intellectual property theft.

Working in concert, CCIPS, the CTC Network, and the CHIP Units create a formidable, multi-pronged approach to prosecuting intellectual property crimes.

Significant Prosecutorial Accomplishments:

In the past few years we have had a substantial impact on counterfeiting and other piracy - including both online and traditional hard goods activities. I would like to take just a few minutes to highlight some of our most recent accomplishments.

Just a few weeks ago, in one of the longest sentences imposed for these types of crimes, a Richmond, Virginia man, Ben John Barbot, was sentenced to 70 months in prison and ordered to pay $1.7 million in restitution for criminal copyright infringement and trafficking in counterfeit goods. The defendant had distributed well over $7 million worth of counterfeit Microsoft software products through multiple Internet-based stores he created. The software products he distributed were extremely high quality counterfeits that had been produced and imported from rogue production plants in Asia. The ability to distinguish between the genuine article and the counterfeit one is more difficult than ever before. Counterfeiters, realizing the economic potential of their crime, are becoming more sophisticated in creating and trafficking in near perfect counterfeits, such as those sold by Mr. Barbot.

There are other examples of successful prosecutions involving counterfeiting or copyright infringement involving physical goods;

- In 2003 a Columbia, South Carolina man was sentenced to seven years in prison and ordered to pay over $3.4 million in restitution to Nike and Tommy Hilfiger for trafficking in thousands of counterfeit T-shirts and other products and engaging in money laundering.
- Also last year, a California man was sentenced to 24 months in federal prison and ordered to pay more than $200,000 in restitution for multiple violations including criminal copyright infringement, and trafficking in counterfeit labels. The defendant operated a videocassette reproduction center where he produced and then sold thousands of counterfeit movie videocassettes at various locations throughout California.
- Our efforts also extend beyond our own borders. Later this month, a Ukrainian man is scheduled to be extradited to the United States from Thailand to face prosecution for his piracy and counterfeiting activities. The man sold counterfeit software through websites and eBay auctions in excess of $3 million dollars. Some of the software was shipped with counterfeit trademarks and logos.

Another reason for strong intellectual property enforcement is the need to protect public health and safety. Criminals, whose only goal is profit, will not hesitate to sell counterfeit baby formula or pharmaceuticals which endanger the health of the consumer.

One recent example of this occurred in Alabama earlier this year. In January, an Alabama man pled guilty to twenty-eight counts of counterfeiting and pesticide misbranding charges. The defendant sold mislabeled and adulterated pesticides needed to

control mosquitoes and West Nile Virus to municipalities and private businesses in a number of southern and mid-western states. The defendant falsely identified the brand name of the pesticide, the manufacturer, and the active ingredients.

Similarly, in 2002 the Department convicted a California man on federal charges involving a conspiracy to sell counterfeit baby formula. After selling thousands of cases of counterfeit baby formula to our most vulnerable population, the defendant fled to Canada in 1995. He was arrested there in 2001 and in 2002 was brought to the U.S. to stand trial. He received a sentence of 3 years and 8 months in prison. Had the defendant succeeded in completing his scheme, his profits would have likely reached in excess of $4.3 million. The potential harm to the babies is, of course, daunting.

As these cases illustrate, the potential consequences of intellectual property offenses go beyond lost sales, and cut right at the heart of public health and safety. Counterfeit products often deprive consumers of their right to safe and legitimate products. Worse yet, counterfeit pharmaceuticals, pesticides and food products harm society's most vulnerable members including our children and those who are ill, or injured. We are actively exploring ways to increase the use of criminal trademark and counterfeit-labeling laws to help protect the health and safety of all our citizens.

Online Piracy and Counterfeiting

Although the focus of this hearing is on intellectual piracy in its physical form, technology and the Internet play an increasing role in counterfeiting. Today's technology allows criminals to use sources both online and off to create infringing products. Thus, in many instances, it is difficult, if not impossible, to separate physical piracy from piracy

occurring over the Internet. It is often through the digital transmission of copyrighted material over the Internet that pirates obtain perfect logos to affix to counterfeit goods. Likewise, criminals obtain from Internet sources the newest and most cutting edge copyrighted works which they reproduce in physical form and distribute in massive quantities around the world. Criminals, like Ben John Barbot who I described above, also use the Internet to identify potential customers and to market and sell their infringing goods – essentially operating a "mail order" business through the Internet.

A few years ago, in South Carolina, we successfully prosecuted a criminal who operated a website called fakegifts.com to sell counterfeit luxury items, including fake Rolex watches and designer handbags around the country. Even though he had almost $16 million in civil judgments against him, he refused to stop his illegal activity because, in his words, he was "making too much money" to stop. He was ultimately sentenced to 24 months in prison and ordered to pay restitution.

We have had numerous cases involving the online auction site eBay which criminals have abused to auction off counterfeit or other infringing goods to the highest bidder. For example, in one case, a man pled guilty to selling unauthorized reproductions of the motion picture "Any Given Sunday" and compilations of National Hockey League highlights and professional fight footage on eBay as well as defrauding bidders of approximately $15,000 on auctions for Sony Playstation 2 video game consoles.

One emerging, and troubling trend, is the apparent belief among many engaged in counterfeiting online is that their actions are legal so long as they acknowledge upfront that their goods are in fact fake, or "replicas." A simple Google search will reveal

numerous websites that candidly acknowledge selling fake or counterfeit goods. Court after court, however, has ruled that this behavior too is criminal. It does, however, point out the pressing need to educate the public about not only the importance of strong intellectual property rights enforcement, but also what is acceptable and what is illegal.

Organized Criminal Activity and Piracy:

As noted, in the past few years the Department has increasingly focused on highly organized criminal organizations engaged in online piracy. In the context of hard goods piracy and counterfeiting, highly organized criminal groups are also emerging. Organized crime syndicates have begun to use piracy and counterfeiting as a means to fund their illicit activity. It is not surprising that organized crime has begun to fill this role. The nature of piracy has undergone a complete transformation over the past several years. Traditionally, piracy operations were small, often run by individuals or a loose collection of people trying to make a quick buck in what has been perceived to be a fairly "risk-free" criminal enterprise. Today, with low overhead and the possibility of substantial financial reward, piracy is big business. It has become a world-wide, multi-billion dollar illicit economy which robs legitimate industries and creators of income, while driving up costs for consumers. It is against this backdrop that criminal organizations are playing a more prominent - and dangerous - role in piracy around the globe.

Significantly, organized crime syndicates have substantial resources to devote to their illegal operations. This has allowed them to increase the scope and sophistication of their criminal activity. Further, by nature, these syndicates control international

distribution channels which allow them to move massive quantities of pirated goods, as well as other illicit goods, throughout the world with relative ease. In fact, we have learned that organized crime syndicates, which are traditionally competitive, now partner with one another across borders to expand their operations at home. Small factories overseas are able to churn out thousands of products annually, ranging from software, to movies, to games, all of which find their way into the black market both overseas and in the United States.

It is a lucrative endeavor for these criminals and, as one might expect, these groups do not hesitate to threaten or injure those who attempt to interfere with their illegal operations. We have received numerous reports from overseas that industry representatives have been threatened, attacked and their property vandalized when their anti-piracy efforts struck too near the illegal operation. Information from overseas indicates that this problem similarly impacts foreign government officials fighting piracy. Some reports from abroad show that raids of factories (producing pirated goods) can often turn into full blown shoot-outs. These world-wide criminal syndicates are formidable foes. The very involvement of organized criminal syndicates, and their apparent willingness to resort to violent means to protect their piracy operations, underscores the critical need for enforcement. We are committed to working closely with our foreign counterparts to address this real and emerging threat.

Online Piracy

As noted earlier, much of the Department's focus has been on those groups that saturate the Internet with pirated products, the so-called "warez" groups. These groups

include highly sophisticated and technically savvy members whose goals are to obtain the latest and most coveted – and, sometimes, not yet released – products, including software, games, music and movies; "crack" any security measures on them; and disseminate them over the Internet to as many people as possible and as quickly as possible. The pirated works distributed by these groups ultimately filter – very quickly – through the Internet and are available world-wide within a matter of minutes.

For these reasons, I think it is critical that I touch on some of the significant work we have done in connection with Internet piracy, and, in particular, the warez scene.

Operation Buccaneer:

The Computer Crime and Intellectual Property Section, working with the CHIP Unit for the Eastern District of Virginia and the United States Customs Service, penetrated a massive international copyright piracy conspiracy code-named Operation Buccaneer which continues to yield prosecutions even today. During Operation Buccaneer, law enforcement initiated an undercover investigation which culminated in the simultaneous execution of more than 70 searches worldwide in December 2001, including searches in Australia, Finland, Sweden, Norway, and the United Kingdom.

As of today, twenty-six U.S. defendants from Operation Buccaneer have been convicted of felony copyright offenses, sixteen of those in the Eastern District of Virginia. Ten defendants have received prison sentences of between 33 to 50 months, the longest sentences ever imposed for Internet copyright piracy at the time. Five defendants are awaiting trial in the United Kingdom and other foreign investigations are ongoing. The Department has also initiated extradition proceedings against one of the prime targets

of the investigation – a well-known warez leader located in Australia. In both its scope and outcome, Operation Buccaneer is the most significant Internet piracy case ever brought, and it has sent a strong deterrent message which continues to resonate throughout the copyright piracy community.

Operation Safehaven:

Building off the success in Operation Buccaneer, CCIPS, in conjunction with the United States Attorney's Office for the District of Connecticut, and the Bureau of Immigration and Customs Enforcement ("ICE") Cyber Crimes Center, conducted a 15 month investigation called Operation Safehaven, which targeted additional significant Internet software piracy groups. In April 2003, the investigation culminated with the simultaneous execution of over 20 search warrants nationwide, resulting in the capture of many well-known and prolific members of the online piracy community and the seizure of thousands of pirated CDs and DVDs, plus dozens of computers and servers, including the largest warez site seized in the United States to date.

Through prosecutions like those in Operations Buccaneer and Safehaven and those that will follow, we will continue to send strong messages that piracy in any form will not be tolerated.

Conclusion

Finally, although we are making inroads in this battle, pirates and counterfeiters are also refining their own illicit techniques. In response to our aggressive enforcement activities, organizations and individuals have found new and more sophisticated ways to hide their illegal activity. The quality of counterfeit and pirated goods is near perfect. In

some instances, even representatives of victim companies themselves have difficulty distinguishing counterfeit goods from legitimate ones. That is how sophisticated this illicit industry has become. We have worked, and will continue to work, closely with American rights holders to ensure that we continue to respond to this threat.

Mr. Chairman, as you can see, the Department of Justice is actively pursuing intellectual property criminals engaged in all forms of intellectual property crime including counterfeiting and other forms of piracy and we believe our efforts are paying off. Though we have had great successes in our battle against global piracy, we recognize that there is much work to be done. We remain committed to this effort and will build on our success by continuing to prosecute piracy aggressively.

On behalf of the Department of Justice, I want to thank you again for inviting me to testify today. We thank you for your support over the years and reaffirm our commitment to continuing to work with Congress to address the significant problem of piracy. I will be happy to answer any questions that you might have.