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A Global Guide

Anti-counterfeiting in the fashion and luxury sectors: trends and strategies

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In the popular imagination, counterfeiting is associated most often with the fashion and luxury sectors. Historically, these sectors were among the first to be impacted by counterfeiting, and it was largely due to efforts by parties in these sectors that laws to combat counterfeiting exist. Today, the market for counterfeit goods is rapidly changing as it moves from physical markets to internet-based platforms. At the same time, globalisation and recessionary economic pressures are transforming the markets for fashion and luxury goods – genuine and otherwise. These trends have once again compelled fashion and luxury brands to take the lead in the fight against counterfeiting.

This chapter explores industry and counterfeiting trends in general, as well as emerging strategies in the fight against online counterfeiting.

Industry trends

The prevailing trend in the fashion and luxury sectors is diversification into emerging markets. In the face of recessionary conditions that have hit Europe hardest of all, and depressed sales of all but the largest luxury brands, the industry has sought new opportunities through geographical expansion. There is a growing market for high-end fashion and luxury goods in emerging markets, particularly in the so-called BRIC countries (Brazil, Russia, India and

China). For example, the growth of the upper-middle class and white-collar employment in China is fuelling demand for such goods. According to a December 2012 Bain & Co report, Chinese consumers have overtaken those in the United States as the world's top buyers of luxury goods, accounting for 25% of global luxury purchases. As a result of a weak euro and lower prices due in part to import duties, 60% of their luxury purchases are made while travelling outside China. Other observers predict that as China's economy becomes increasingly consumer driven, it will become the world's largest luxury market within the decade.

Movement into growing emerging markets represents a great opportunity for fashion and luxury brands, but that opportunity comes with risks. China is still by far the world's largest producer and supplier of counterfeit goods. Many of those goods are produced for export, and Chinese consumers of high-end goods are said to place a great premium on authenticity. However, there are many notorious physical marketplaces for counterfeit goods in China, in addition to domestic online sales. Brands entering the Chinese market must do so with eyes wide open and an informed IP protection strategy.

Counterfeiting trends

The market for counterfeit goods and pirated property represents an estimated 5% to 7% of global trade, or between \$500 billion and \$600 billion annually – twice the estimated annual profits from the sale of illegal drugs worldwide (\$321 billion). Multinational rights holders collectively lose approximately 10% of their top-

line revenue to counterfeiters each year, and the number of affected brands is growing. The days during which sales of counterfeit fashion and luxury goods were largely confined to physical market districts - such as New York City's Canal Street, Beijing's Silk Alley Market and Buenos Aires's La Salada - are long gone. Online retail sales generally have grown at an annual rate of 20% or more and, according to the Office of the US Trade Representative, the volume of pirated and counterfeit hard goods sold online will soon surpass that of goods sold by street vendors and in other physical markets. As beneficial as the Internet has been for industry sales, it has been a greater boon for counterfeiters. The Internet affords counterfeiters virtually unlimited access to a worldwide customer base. Counterfeiters can create the illusion of an upscale business through the use of professional-looking websites without significant costs and thus have access to the same sales and marketing channels as legitimate brands. The Internet also allows an individual counterfeiting operation to saturate the market by driving up search engine results and using literally thousands or tens of thousands of portal websites. In short, the Internet has enabled counterfeiters to be more effective and insidious.

Electronic commerce in the form of auction, business-to-business and business-to-consumer portals has enabled non-professionals with little capital and no ties to traditional counterfeiting distribution channels to trade in counterfeit goods. These 'new counterfeiters' can easily purchase counterfeit goods wholesale over the Internet and even sell goods without ever coming into contact with them by using 'drop shipping' - a method whereby the seller solicits an order, accepts payment and fills the order through a supplier that ships directly to the customer. These individual shipments of goods are much more difficult for customs officials to detect and intercept than the bulk cargoes of old. The increasingly decentralised nature of the manufacture and sale of counterfeit goods further confounds government anti-counterfeiting enforcement efforts. Selling directly to consumers eliminates the middle man and renders counterfeiting less visible to law enforcement. Counterfeiters can use the Internet to conceal their identities and cloak themselves in virtual anonymity.

While counterfeiters have historically

focused primarily on a short list of upscale brands, such as Rolex and Louis Vuitton, due to the ease of online marketing and sales and recessionary economic conditions, they are additionally targeting brands in the middle market. A number of factors have caused this shift. First, there is less risk in the middle market: big luxury brands have pursued aggressive anti-counterfeiting enforcement programmes that have caused counterfeiters major losses and resulted in big judgments, whereas smaller brands can less afford to crack down. Second, the economic downturn has left significant excess capacity in factories in China and elsewhere that production of counterfeit goods can fill. Third, counterfeiters can price middle-market brands at a level comparable to a bargain offered by a legitimate vendor - for example, at a 25% to 50% discount. High-volume sales of lower-priced items at prices closer to retail may be even more lucrative for counterfeiters than sales of high-end items priced significantly below retail. Finally, the recession has caused consumers to cut back and even middle-market brands priced at retail can seem out of reach.

A study released by MarkMonitor® has found that for every shopper searching for counterfeit goods, 20 others are seeking value-priced and sale goods, and one in five of those bargain hunters are intercepted by counterfeiters' rogue websites.

Counterfeiters have enthusiastically and adeptly employed social media and other internet-based means as marketing tools. Google and other search engines are the primary drivers of e-commerce, and counterfeiters aggressively elbow up Google rankings by using search engine optimisation measures, which must constantly change to keep up with evolving search algorithms. Counterfeiters create YouTube videos to market their sites and message YouTube users to proliferate them. They create Twitter feeds and Facebook pages, and Pinterest users' 'boards' incorporate 'pins' of images from counterfeiters' rogue websites alongside those from legitimate vendors' websites.

Enforcement strategies

While the situation may sound dire, there are strategies that rights holders can adopt to stem the tide of global counterfeiting.

However, rights holders must first understand the scope of their counterfeiting issues, which vary across industries and even across brands. Online counterfeiting is enabled by technology, and to understand the scope of the problem, technology may be required in the form of proprietary software to track and link instances of counterfeiting. In dealing with the problem, there is no one-size-fits-all approach, and it usually makes sense for rights holders to employ various tactics simultaneously.

Judicial solutions

As legislative solutions such as the Stop Online Piracy Act and the Protect IP Act have wilted in the face of opposition, a judicial solution has emerged as the single most integrated solution to tackle counterfeiting on the Internet. Following the precedent set in *The North Face Apparel Corp v Fujian Sharing Import & Export Ltd*, No 10-Civ-1630 (SDNY), luxury and apparel rights holders are using the Lanham Act in US courts to obtain orders allowing them to shut down websites *en masse*, restrain counterfeiters' financial accounts and hold third parties (advertising companies, back-end providers, registries, payment systems, search engines and social media sites) accountable once they are on notice that a website is selling counterfeit wares. While success for this method was initially measured by its ability to restrain large amounts of moneys in accounts in the United States, as those moneys have decreased (but not disappeared), the strength of this strategy lies in its ability to link hundreds or thousands of websites to a common source, take those websites down *en masse* (even those directed solely to Europe or elsewhere), and require third parties to cease service to these websites. Under the right factual circumstances, this type of litigation produces an ongoing order that can react more quickly to match the speed with which online counterfeiters establish new websites.

Voluntary third-party solutions

As more third parties – including trade boards, online marketplaces, payment processors, registrars, registries and search engines – have become willing or unwilling participants in the burgeoning counterfeiting trade, rights holders are turning to these third parties for

cooperation in the fight against counterfeiters, with mixed or limited results. While some of these participants claim lack of jurisdiction or 'free internet speech', what cannot be ignored is that given the scope of counterfeiting, many of these legitimate third parties are making substantial revenue from counterfeiting.

A traditional strategy is to send takedown notices directly to internet service providers (ISPs) which host website content. ISPs in many countries are generally responsive upon notice, ceasing services within 48 hours to a website that is suspected of selling counterfeits. Unfortunately, the counterfeiter often simply redirects its content to an ISP in a country where takedown notices are not as effective. Another traditional strategy is to file a Uniform Domain Name Dispute Resolution Policy (UDRP) proceeding where a domain is confusingly similar to a rights holder's trademarks. Unfortunately, fewer than 20% of counterfeit websites include a trademark in the domain name. The procedural framework for UDRP proceedings could not have contemplated the needs of combating today's scope of online counterfeiting, and has proven to be expensive and slow against a moderate to large online counterfeiting problem.

Many trade board websites allow rights holders to report instances of counterfeiting on their platforms and will delist the products voluntarily. This is a global approach utilised by e-commerce platforms ranging from eBay in the United States to Taobao in China. eBay's Verified Rights Owner Programme will remove auctions that are identified as fake by an authorised brand representative and will also provide the seller's name, address and phone number on request. Taobao has keyword filters that prevent sellers from posting banned items and price filters that weed out luxury goods offered at prices that are too low to be legitimate.

However, these programmes have also made it more difficult to hold e-commerce platforms liable for infringement. In the United States, the Second Circuit found that eBay could not be held liable for the trademark infringement of Tiffany goods, in part because Tiffany had failed to take advantage of the Verified Rights Owner Programme. Similarly, Chinese courts have limited platforms' duties to timely honouring notice and delist requests, and have generally

declined to hold platforms liable for trademark infringement unless it is shown that the platform had knowledge of specific infringing acts. In contrast to the courts in United States and China, courts in Europe have developed stricter standards for e-commerce platforms. French courts have ruled that eBay violated trademark laws by passively allowing counterfeit sales. The European Court of Justice has held that the safe harbour provisions of the E-commerce Directive apply only to hosting providers that are passive and neutral. An online marketplace that helps to promote and optimise the presentation of goods for sale (eg. eBay) is not passive. While developments in Europe are encouraging, the law is still unsettled and rights holders should continue to work with e-commerce platforms to remove counterfeit goods.

Relatively new cooperation programmes include the Ads Integrity Alliance started in June 2012 - a joint initiative between Google, AOL, Facebook and Twitter to combat paid-for advertisements for counterfeit goods. In 2011 Google claimed to have disabled more than 130 million paid advertisements and 800,000 advertisers that violated its policies, including advertisements that promoted counterfeit goods. Google may also remove content from search engines for copyright violations under Section 512 of the Digital Millennium Copyright Act, which requires online service providers to remove copyright-infringing material from their service at the request of copyright owners (a common practice among counterfeit sites, typically through unauthorised use of product images). However, Google will not remove content from search engines for trademark violations other than pursuant to court order.

Another cooperation programme is the IACC Portal Programme, started by the International Anti-counterfeiting Coalition and G2 Web Services, LLC. This allows participating rights holders to alert payment processing networks of counterfeit sales so that the counterfeiters' merchant accounts can be revoked. As of October 2012, 906 individual merchant accounts had been terminated as a result of rights holder reports. The principal drawback of this process is that counterfeiters can effectively switch among multiple payment processing accounts to mitigate their losses.

Government solutions

Government action, both country specific and across countries, is crucial as one part of the effort to reduce counterfeiting. However, while government cooperation – and particularly cooperation between governments – is key to the fight against counterfeiting, reliance on government entities cannot, in most instances, be the sole strategy for a single rights holder.

Examples of recent successes include the US Immigration and Customs Enforcement's homeland security investigations in November 2012, in which law enforcement agencies from Belgium, Denmark, France, Romania, the United Kingdom and Europol seized 132 domain names that were illegally selling counterfeit merchandise online to unsuspecting consumers. In another 2012 collaboration success, US and Chinese authorities worked together to shut down a major counterfeiting operation in Guangdong Province. The operation resulted in the arrest of 73 people, the shutdown of 37 websites selling counterfeit handbags, and the seizure of 20,000 counterfeit bags and enough machinery and raw materials to construct an additional 50,000 bags. This operation was estimated to be worth \$802 million.

Conclusion

The rise of counterfeiting is a global problem that requires aggressive strategies. However, rights holders should not lose hope – a comprehensive brand protection strategy, including the solutions discussed here, as well as consumer education and trade group involvement, will lead to a return on investment for years to come.

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