

House Energy and Commerce
Subcommittee on Commerce, Trade, and Consumer Protection

“Product Counterfeiting: How Fakes Are Undermining U.S. Jobs,
Innovation, and Consumer Safety

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I am Steve Arthur, Vice President of Government Affairs for GMA, the Grocery Manufacturers Association, and I am very pleased to be here today to talk about an issue of intense concern to our member companies and manufacturers across the country.

GMA is the world's largest association of food, beverage and consumer product companies. Led by a board of 42 Chief Executive Officers, GMA applies legal, scientific and political expertise from its more than 120 member companies to vital public policy issues affecting its membership. The association also leads efforts to increase productivity, efficiency and growth in the food, beverage and consumer products industry. With U.S. sales of more than \$500 billion, GMA members employ more than 2.5 million workers in all 50 states.

GMA has been fighting counterfeiting for a long time and is a member of the Coalition Against Counterfeiting and Piracy, an industry group created by a joint initiative between the U.S. Chamber of Commerce and the National Association of Manufacturers to act as the interface between business and the U.S. Government's Strategy Targeting Organized Piracy (STOP!) program.

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 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. Many industries are affected, including consumer products, automotive, pharmaceutical, electronics, textiles and others.

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. However, 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.

For example, in December, 2003, Australian customs officials stopped 52,000 containers of counterfeit shampoo at port. Last week, officials in India seized a large quantity of bottled water with spurious marks as well as many counterfeit personal care consumer products. Canadian based Gieschen Consultancy, which tracks counterfeit product enforcement incidents, reports that in the first quarter of 2005, there were 279 incidents of intellectual property theft world wide, valued at a loss of \$396 million dollars. Of particular interest to GMA member companies, this total included counterfeit milk drinks, wine, rum and soy sauce, as well as industrial goods and supplies such as insecticides and detergents and counterfeit perfumes and cosmetics.

Our member companies who make food, beverage and consumer products have rigorous quality controls to ensure their products are safe for proper human use and consumption. Counterfeit products are not subject to those same quality standards. As long as the packaging looks similar, it might enter the supply chain without any quality controls at all.

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. If you compare that to the earlier number I referenced regarding enforcement actions, its clear that only a small percentage of counterfeit products are caught and the counterfeiters prosecuted. 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 by law-abiding, hard-working Americans 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 property and move them back into the supply chain. These criminals feed on those buyers or distributors who are willing to turn a blind eye in return for a good deal. In other cases, the buyer is truly unaware that the goods he or she is purchasing are

stolen or counterfeit. In addition, the same networks used to distribute counterfeit products also ease the transport of illegal drugs into U.S. markets.

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. Paramilitary groups in Northern Ireland have funded terrorist activities through the sale of pirated products. Protection rackets in Italy no longer demand just money from retailers; instead, they want shelf space to sell counterfeit goods. In testimony before the Senate Homeland Security Committee, the Los Angeles Sheriff's Department testified that many arrested for counterfeit product crimes in Los Angeles are Hamas and Hezbollah sympathizers and supporters. 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.

It is clearly not just the food, beverage and consumer products industry that is targeted. This committee is also hearing about counterfeit pharmaceutical and automotive products. These counterfeits can and have caused serious injury and even death.

Domestic Efforts

The first step in combating counterfeiting worldwide is to improve enforcement at home. We need to close some of the legal loopholes that allow counterfeiters to escape prosecution, and we need laws that give enforcement agencies better tools to fight counterfeiting.

GMA is pleased that the House has taken this first step by approving HR 32, the *Stop Counterfeiting in Manufactured Goods Act*, by Congressman Knollenberg. As this committee knows, this bill will close a loophole in the federal criminal code that allows phony products to be shipped to the United States without brand markings, so they can pass through customs without any apparent violation. Counterfeit labels are then added and the products are sold through a variety of channels. HR 32 will allow authorities to prosecute the people who do the labeling and packaging here. It will also allow for the forfeiture and destruction of any confiscated counterfeit labels or products that would bear those labels.

In addition, the bill gives law enforcement officials the ability to seize and confiscate the equipment and assets – such as machine tools and computers – used to produce counterfeit products, labels, and packaging. Without this ability, law enforcement officers are 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. GMA strongly supported the passage of HR 32 and will now work just as vigorously for its passage in the Senate.

GMA also supports the Administration's Strategy Targeting Organized Piracy (STOP!) initiative, which was launched in 2004 and brings together the U.S. Trade Representative, the Departments of Commerce, Justice, and Homeland Security to stop the distribution of counterfeit goods. The effort is broad in scope and brings a new approach, new tools and new pressure to bear through a coordinated effort from the federal government, the private sector and America's international trading partners.

A key element of the STOP! initiative is the development of purchasing guidelines for manufacturers and retailers to ensure that global supply chains are free of illicit goods. As a coordinator for the Coalition Against Counterfeit Products task force, GMA is working with other associations that represent food, beverage and consumer product manufacturers and retailers to accomplish this objective. The task force is developing voluntary guidelines to prevent illicit goods from entering the supply chain and prevent criminals from exploiting alternate sourcing strategies. The final document is expected to be completed by September, 2005. These guidelines will then be available for use by other industries.

Change Domestically Provides Leverage Globally

Passage of HR 32 is essential to our ability to improve anti-counterfeiting efforts abroad. The Office of the U.S. Trade Representative has made clear 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 domestic mandatory seizure and destruction so our trade negotiators have a foundation to press for this minimum necessary enforcement around the world.

In 2004, the Office of the U.S. Trade Representative, in a "Special 301" annual review, reported that more than 66% of counterfeit goods seized by the U.S. Customs Service at ports of entry into this country were traced to China. In addition to combating counterfeiting within its

borders, the Chinese government also must stop the export of counterfeit products. The United States should continue to work with the Chinese government to create an effective program to stop the trafficking of counterfeit goods at the point of export.

GMA is encouraged that the U.S. Government is taking the issue of intellectual property theft and counterfeit products seriously. In April 2005, as part of the Administration's Strategy Targeting Organized Piracy (STOP!), the United States traveled to Singapore, Hong Kong, Tokyo and Seoul to explore avenues for increased cooperation, improved coordination, and expanded information exchanges as an initial step in garnering international support to work together to stem the trade in fakes. A series of 17 U.S. proposals were shared with government officials from these countries generating fruitful discussions, interest and commitments to continue working together on this shared concern. And just last week, officials representing seven United States Government agencies traveled to Europe to meet with German, United Kingdom, French and European Commission officials to discuss cooperation to crack down on global piracy and counterfeiting.

In addition to having appropriate prosecutorial powers in the U.S. and other countries, it is important to understand the scope of product counterfeiting globally in terms of damage to rights holders and countries that harbor counterfeiting. GMA has long advocated engagement with the Organization for the Economic Cooperation (OECD) to address this issue. With the support of the U.S. government, the Organization for Economic Cooperation and Development announced in April 2005 that it will conduct a study to determine the scope of the problem and the damage product counterfeiting does on a global basis. The project will also analyze existing

public and private anti-counterfeiting efforts to develop a set of best practices to guide future efforts in the fight against counterfeiting.

The project will include a three-phase study on the adverse impacts of counterfeiting and piracy; a series of four regional workshops, envisioned to take place in Russia, Brazil, India and China in 2006; and two Global Forums, focusing on various aspects of the problem, one planned for 2006 and the second in 2007.

OECD is scheduled to co-host a two-day meeting with the World Intellectual Property Organization in October, 2005 in Geneva to develop metrics and examine statistical issues, and also plans to circulate an outline for the Phase one study to governments, asking them to circulate more widely for feedback. A final report is expected in May, 2006.

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.

Summary of Points

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. Many industries are affected, including consumer products, automotive, pharmaceutical, electronics, textiles and others.

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.

Counterfeiting frequently is part of a larger criminal enterprise involving the theft of legitimate goods. Organized crime and terrorist groups use the sale of counterfeit goods to raise money for illegal activities and violence.

GMA supports Senate passage of HR 32, the *Stop Counterfeiting in Manufactured Goods Act*, by Congressman Knollenberg. The bill will close a loophole in the federal criminal code that allows phony products to be shipped to the United States without brand markings, so they can pass through customs without any apparent violation. In addition, the bill gives law enforcement officials the ability to seize and confiscate the equipment and assets – such as machine tools and computers – used to produce counterfeit products, labels, and packaging.

GMA also supports the Administration's interagency Strategy Targeting Organized Piracy (STOP!) initiative. The effort is broad in scope and brings a new approach, new tools and new pressure to bear through a coordinated effort from the federal government, the private sector and America's international trading partners.

GMA is working with other associations on a key element of the STOP! initiative to develop purchasing guidelines for manufacturers and retailers to ensure that global supply chains are free of illicit goods.

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