



**Submission of the**  
**International AntiCounterfeiting Coalition, Inc.**  
**to the**  
**United States Trade Representative**  
**Special 301 Recommendations**

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**February 12, 2007**

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February 12, 2007

Ms. Sybia Harrison  
Special Assistant to Section 301 Committee  
Office of the United States Trade Representative  
600 17<sup>th</sup> Street, NW  
Washington, D.C. 20508

**Request for Public Comment--Identification of Countries Under Section 182 of the Trade Act of 1974 (as amended), 72 Fed. Reg. 5 (January 9, 2007)**

Dear Ms. Harrison:

On behalf of the International AntiCounterfeiting Coalition, Inc. ("IACC"), and its members, I respectfully submit the following report in response to the United States Trade Representative's request for comments identifying countries that deny adequate and effective protection and enforcement of intellectual property (IP) rights. This year the IACC reports on fourteen (14) countries.

The IACC is the largest multinational organization representing exclusively the interests of companies concerned with product counterfeiting and copyright piracy. Our members consist of approximately 175 corporations, trade associations, and professional firms and represent total revenues of over \$750 billion. The IP owners among our membership represent a broad cross-section of industries, and include many of the world's best known companies in the apparel, automotive, consumer goods, entertainment, pharmaceutical, personal care and other product sectors.

The IACC is committed to working with government and industry partners in the United States and elsewhere to strengthen IP protection by encouraging improvements in the law, allocation of greater political priority and resources, and raising awareness regarding the enormous—and growing—harm caused by IP violations.

Letter to Ms. Harrison  
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We look forward to working with the USTR in its efforts to promote IP protection globally and we are available at any time for clarification of any issues raised in the attached submission.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Nils Victor Montan". The signature is fluid and cursive, with a prominent vertical stroke at the beginning and a horizontal stroke at the end.

Nils Victor Montan  
President

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## INTRODUCTION

This report has been prepared by the International AntiCounterfeiting IACC, Inc. (“IACC”) in response to the United States Trade Representative’s (“USTR”) request for written comments, pursuant to Section 182 of the Omnibus Trade and Competitiveness Act of 1988, 19 USC § 2242 (“Special 301”), regarding governments that deny adequate and effective protection and enforcement of intellectual property (“IP”) rights. The IACC has filed Special 301 submissions with the USTR since 1997.

The IACC, based in Washington, D.C., is the largest and oldest association representing exclusively the interests of companies concerned with product counterfeiting and copyright piracy. Our members consist of approximately 175 corporations, trade associations, and professional firms. The total revenues of IACC members represent over \$750 billion annually.

The IACC is actively involved in research, advocacy and educational programs targeting counterfeiting and copyright piracy on a global level.

Working in concert with other government and industry partners, the IACC has been in the leadership of a number of recent initiatives that have aimed to strengthen IP laws and enforcement policies of governments, including the passage of the Stop Manufacturing in Counterfeit Goods Act, enacted in March, 2006.

Despite the considerable resources applied by both the public and private sector to address the global problems of counterfeiting and piracy, there is substantial anecdotal and statistical evidence indicating that these problems continue to grow in size and scope. Information from industry and government sources, including Interpol, the World Customs Organization, and the World Intellectual Property Organization confirms that this growth is due in part to the increasing involvement of more sophisticated organized criminal networks operating across national boundaries. It is also now widely recognized that free trade zones established in a growing number of countries are increasingly exploited by these networks in order to facilitate the global distribution of fakes.

While government leaders and policy makers are more cognizant of the negative implications tied to the trade of illicit goods, the need for greater priority to be given to anti-counterfeiting efforts remains dire. Counterfeiting and piracy pose serious threats to public health and well-being, cause substantial losses in tax revenues, hindered development of both domestic and international markets, and diminish incentives for global innovation. Regrettably, government leaders and other policy makers in certain countries, including some of our largest trading partners, do not yet appear to understand the economic and social costs of tolerating IP crime.

The IACC intends and hopes that the recommendations for legal and policy reform set forth in this submission will provide a useful guide for national governments as they consider introducing “best practices” adopted elsewhere, and as they assess whether their laws and enforcement practices meet the minimum standards of protection

set out in the Agreement on the Trade-Related Aspects of Intellectual Property (the “TRIPS Agreement”) by the World Trade Organization (“WTO”).

The key to stemming the flow of counterfeit and piratical goods does not come in the form of a “magic bullet.” There is no single law or treaty that will provide the answers that government and industry are seeking, and no single trade organization that will solve this problem. Anti-counterfeiting is a moving target in all countries, including the United States, and there is a constant need to review laws and the sufficiency of government resources allocated to criminal enforcement and training. New technologies, including the Internet, and the increasing sophistication of counterfeiters and pirates require that government and industry work ever more closely in assessing not only the adequacy of laws but their effectiveness in practice. The global counterfeiting problem can only be addressed successfully by fostering cooperation at all levels – within industries, between industry and government, and between governments – to ensure that law enforcement has the legislative tools and the financial and personnel resources necessary to meaningfully enforce the law.

Articles 41 and 61 of the TRIPS Agreement require WTO members to provide criminal enforcement remedies that are effective and that provide a deterrent to further violations. The TRIPS Agreement also requires that the countries provide adequate enforcement against IP violations through customs. But it is becoming increasingly clear that, in order to provide truly “effective” enforcement, governments need to do more than implement the minimum standards of the TRIPS Agreement. The IACC applauds USTR’s work in concluding Foreign Trade Agreements (“FTAs”) and other international agreements that are having a positive impact in raising the standards of protection and introducing best practices.

Below is a chart indicating the countries analyzed in the IACC’s Special 301 submissions since 1997. In this year’s submission the IACC has chosen to focus on fourteen countries. As in last year’s submission, China, Canada and Russia remain our members’ greatest concerns.

The IACC will continue to provide USTR and other government agencies with information and views on the situation in other countries through separate submissions, and we would be pleased to respond to questions regarding any particular jurisdiction, upon request.

Finally, the country submissions reflect a number of common problems that warrant particular attention:

- The need for substantially greater political will and resources to combat IP crime;
- The need to ensure greater use of criminal enforcement tools, which create substantially greater deterrence, rather than relying excessively on administrative measures, such as customs seizures, which yield only economic sanctions;
- The need for greater cooperation and coordination among different government enforcement bodies, including police, Customs, and other administrative

- enforcement bodies;
- The adoption of sentencing and other guidelines that will lead to stronger criminal and administrative sanctions;
  - The need to eliminate numerical thresholds for criminalizing IP cases, and to encourage criminal investigations in any case where there is a basis for suspicion of a crime;
  - The need for Customs and other enforcement authorities to provide IP owners with earlier access to information needed to pursue investigations and legal actions;
  - The need for greater reliance on “creative” enforcement tools, including third-party and landlord liability strategies; and
  - The need for greater transparency regarding the results of government enforcement work.

**IACC RECOMMENDATIONS  
1997 - 2007**

	97	98	99	00	01	02	03	04	05	06	07
Argentina				WL	WL	WL					
Australia		WL									
Belize								WL	PWL	PWL	WL
Bolivia							WL				
Brazil				WL	WL	WL		WL			PWL
Bulgaria						WL		WL			
Canada				WL	OO	WL	WL		WL		PWL
Chile		WL		--	WL	WL	WL		WL		
China	PFC		306	306	306	306	306	306	PFC/306	PFC/306	PFC/ 306
Costa Rica										PWL	PWL
Columbia			PWL			WL					
Czech Republic											PWL
Greece		PWL	PWL								
Hong Kong					OO						
Hungary							WL				
India							WL	PWL	WL		
Indonesia	PWL	PWL			WL	PWL					
Italy				WL	WL	WL					
Japan					WL	WL		WL			
Jordan								WL			
Kazakhstan						WL					
Korea		WL	WL	WL							
Kuwait									WL		
Lebanon								PWL			
Libya								WL			
Malaysia				WL	PWL		PWL	PWL	PWL	PWL	WL
Mauritius								WL			
Mexico		OO	WL	WL	OO	WL	WL	PWL	PWL	PWL	WL
Pakistan								WL			
Panama							WL	WL	WL		
Paraguay					306	306	306	306			PWL/ 306
Peru											SM
Philippines							PWL	PWL	PWL	PWL	WL
Poland							PWL	PWL	PWL		
Romania								WL			
Russia				PWL	PWL	PWL	PWL	PWL	PWL	PWL	PWL
Saudi Arabia						WL	WL	WL	WL		

	97	98	99	OO	01	02	03	04	05	06	07
Singapore				PWL		WL	WL				
South Africa					WL	WL	WL				
Taiwan	OO	OO	WL	WL	PWL	PWL	PWL	WL	WL		
Thailand				PWL		WL	WL	WL			
Turkey							WL	WL	WL		
Ukraine					WL	PFC		PFC			
UAE						WL	WL	WL	WL		SM
Venezuela								WL			
Vietnam						WL	WL				PWL

**Abbreviations**

PFC: Priority Foreign Country; 306: Section 306 Monitoring; PWL: Priority Watch List; WL: Watch List; OO: Other Observations; SM: Special Mention

## CHINA

### **Recommendation:     **Priority Foreign Country; Section 306 Monitoring****

#### **Introduction**

Industry concerns about intellectual property rights (IPR) enforcement in China remain by-and-large unchanged since the issuance of IACC's Special 301 report to USTR of February 10, 2006.<sup>1</sup>

The IACC is pleased that these concerns were fully reflected in the USTR's 2006 301 report<sup>2</sup> and also in its December 2006 WTO Compliance report<sup>3</sup>. Our members also appreciate the extensive efforts made by the USTR, the Department of Commerce, Department of State, and the USPTO to engage with China over the need for it to comply with the TRIPS Agreement of the WTO and other relevant bilateral accords on IPR enforcement. The IACC encourages the continuance of those efforts to address the very real global problem that counterfeiting in China creates.

#### **Recent Developments**

Over the last 12 months various enforcement arms of the Chinese Government have improved their performance in relation to IPR enforcement. This is apparent in the higher number of criminal investigations against trademark counterfeiters being pursued by the Chinese police – the Public Security Bureaux ("PSB"). The Supreme People's Court (SPC) recently announced a 52% increase in the number of IPR offenses related convictions in 2006 (a total of 796). Chinese Customs meanwhile conducted 2,473 seizures of infringing goods with a value of over US\$25 million - an increase of nearly 100% compared to 2005.<sup>4</sup> Chinese Customs and

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<sup>1</sup> See [http://www.iacc.org/resources/2006\\_USTR\\_Special\\_301.pdf](http://www.iacc.org/resources/2006_USTR_Special_301.pdf). The views expressed in this report are mirrored in reports from other industry associations, including the United States Chamber of Commerce (see <http://www.uschamber.com/default>) and the International Intellectual Property Alliance (IIPA) (see [www.iipa.com](http://www.iipa.com)).

<sup>2</sup> See [http://www.ustr.gov/Document\\_Library/Reports\\_Publications/2006/2006\\_Special\\_301\\_Review/Section\\_Index.html](http://www.ustr.gov/Document_Library/Reports_Publications/2006/2006_Special_301_Review/Section_Index.html).

<sup>3</sup> See [http://www.ustr.gov/assets/Document\\_Library/Reports\\_Publications/2006/asset\\_upload\\_file688\\_10223.pdf](http://www.ustr.gov/assets/Document_Library/Reports_Publications/2006/asset_upload_file688_10223.pdf)

<sup>4</sup> See Chinese Government enforcement statistics, summarized at: <http://www.customs.gov.cn/YWStaticPage/4712/6cd25a01.htm>.

police have also reportedly worked successfully together to transfer at least five administrative IPR cases for criminal investigation in the last year.

IACC members also applaud the initiatives of the Ministry of Commerce (MOFCOM) and its local branches in strengthening coordination in anti-counterfeiting and anti-piracy, evidenced in particular by the establishment of 50 IPR complaint service centers in major cities and the significantly increased level of awareness-raising initiatives with respect to IPR protection.

The trend towards greater coordination and focus in IPR enforcement and policy making is also reflected by the issuance in last March of a new “Action Plan”<sup>5</sup> which sets out a range of initiatives to be pursued between 2006 and 2007 which describes in detail the government’s plans for improving IPR laws and regulations, strengthening enforcement, increasing public awareness and promoting greater cooperation with industry and foreign governments in IPR protection. The Action Plan and statements from senior Chinese government leaders recognize the important links between IPR protection, innovation and development.

Notwithstanding the above progress, the experience of IACC members over the last year suggests that much more needs to be done, as the available evidence clearly indicates that, on the whole, counterfeiting in China remains as bad or worse as it was before the Action Plan was introduced. The extent of the problem across virtually all regions remains staggering.<sup>6</sup>

Our members report that the current criminal and administrative enforcement mechanisms in China only rarely have the desired deterrent impact.<sup>7</sup> This is just as true for smaller rights holders as it is for our larger, more experienced and better resourced members. Almost all of our members believe their investments in enforcement at all levels – production, wholesale, retail and on the Internet – render disappointing results.

The reasons for these continuing problems are varied, but perhaps the most important are a lack of political will in key regions and gaps in Chinese legislation.

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<sup>5</sup> See English version at [http://www.ipr.gov.cn/ipr/en/info/Article.jsp?a\\_no=3326&col\\_no=102&dir=200604](http://www.ipr.gov.cn/ipr/en/info/Article.jsp?a_no=3326&col_no=102&dir=200604).

<sup>6</sup> See Quality Brands Protection Committee member survey at <http://www.qbpc.org.cn/en/about/references/QBPCrelated/survey/>, which indicates that 41% of respondents reported at least 11% of their products in the PRC market were counterfeit (19% reported 11-25%; 9% reported 26-50%, and 13% reported 51% or more). 59% of respondents said that counterfeits represented up to 10% of the market.

<sup>7</sup> See results of the 2006 survey of members of the Quality Brands Protection Committee at <http://www.qbpc.org.cn/en/about/references/QBPCrelated/survey/>, in which 70% of respondents characterized their counterfeiting problems in 2006 as the same or worse as compared to the prior year.

IACC members report that local protectionism remains strong in certain regions, particularly the counterfeiting hot-spots of Chaoyang District in Beijing and the Baiyun and Huadu Districts of Guangzhou. Continuing problems in these and other regions demonstrate the limitations in the influence of central government authorities.

The failure of China's IPR protection regime is perhaps best illustrated by the continuing roaring trade in counterfeit fashion, jewelry, sports and apparel products in well-known retail and wholesale markets such as the Silk Market, Tianyi Market and Yaxiu Market in Beijing and the Ziyuangang Market in Guangzhou. Counterfeiting in these locations continues to attract global attention and remains largely undiminished, despite the best efforts of administrative enforcers and brand owners over the course of 2006.<sup>8</sup>

Meanwhile, the problem of counterfeit exports from China continues to grow, spurred in large part by increasing use of the Internet as the main platform for promotion and sales.

Seizure statistics from the Department of Homeland Security (DHS), other government and from IACC members all indicate that China remains the largest single source of counterfeit products exported to other countries. Indeed, during 2006, the trend in this regard appeared to worsen, as the DHS reported last November that China was the source of 81% of all infringing items seized at America's borders, up from 69% during the prior year. If seizures from Hong Kong (normally just a transshipment port) are added, the total for 2006 was 87%.<sup>9</sup>

### Building on Progress

IACC members have been pleased by the USTR's and the Commerce Department's increased engagement with the Chinese Government on counterfeiting and piracy, including through the JCCT process. This increased engagement is probably responsible for the notable increases in criminal enforcement seen against trademark counterfeiters over the last three years. However, to effect real change in the marketplace, China has been called upon to consider much deeper reforms—and not simply gradual increases in enforcement actions.

Regrettably, the Chinese Government has so far resisted calls for more systemic changes to the PRC's IPR laws and systems. The usual refrain heard from the

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<sup>8</sup> See below for further information on IACC member experimentation with landlord liability initiatives in Beijing.

<sup>9</sup> See DHS statistics at: [http://www.cbp.gov/xp/cgov/newsroom/news\\_releases/012007/01112007\\_1.xml](http://www.cbp.gov/xp/cgov/newsroom/news_releases/012007/01112007_1.xml) . [http://www.cbp.gov/linkhandler/cgov/import/commercial\\_enforcement/ipr/seizure/trading/fy06\\_ipr\\_stat.ctt/fy06\\_ipr\\_stat.pdf](http://www.cbp.gov/linkhandler/cgov/import/commercial_enforcement/ipr/seizure/trading/fy06_ipr_stat.ctt/fy06_ipr_stat.pdf). Seizures of China-sourced fakes during 2006 in the EU were reported to be approximately 60% of the total. See [http://ec.europa.eu/commission\\_barroso/kovacs/speeches/Counterfeit\\_Statistics2005\\_061110.pdf](http://ec.europa.eu/commission_barroso/kovacs/speeches/Counterfeit_Statistics2005_061110.pdf).

Chinese Government is that China's legal traditions and enforcement efforts are just misunderstood and inadequately publicized. IACC members respectfully disagree.

China has traditionally relied upon administrative enforcement to tackle counterfeiting and copyright piracy. While useful in many ways, administrative penalties are normally limited to fines, which, practice shows, are by themselves insufficient to deter further infringements.

China's Criminal Code only applies to IPR infringements where certain value thresholds are met - US\$6000 for individual offenders and US\$18,000 for corporate infringers. In theory, administrative raids which result in evidence of infringement above these thresholds should be transferred to the PSB for criminal prosecution. However, transfers of administrative cases have in practice been relatively rare, notwithstanding recent efforts of the Ministry of Public Security (MPS) to encourage them.<sup>10</sup> The Chinese Government has recently reported that out of 33,900 trademark cases handled by China's primary administrative enforcement body for trademark violations, the Administrations for Industry and Commerce (AICs) in 2006, only 111 were transferred to the PSB. This represents a decrease of 52% from the prior year.<sup>11</sup>

The MPS has emphasized that it is willing and eager to accept complaints directly from IPR holder. Where direct filings have been made by rights holders they have, in fact, proved more successful for more experienced IACC members when dealing with larger-scale cases against factory targets. However, given their limited resources and the current thresholds for prosecution and conviction, the PSBs are understandably reluctant to dedicate resources to cases involving smaller-scale factories and mere traders. By the same token, IACC members - many of which are best characterized as small and medium-sized enterprises (SMEs) - are often unable to dedicate the resources needed to pursue criminal cases. The net outcome is a sense among infringers in China that the risks of criminal prosecution are extremely low.

Foreign governments and industry associations, including the IACC, Quality Brands Protection Committee (QBPC), the International Trademark Association (INTA) and others, have for years consistently recommended to the Chinese government a range of systemic reforms which are based on solid experience with international practice. The more critical recommendations include the following:

- substantially increasing resources and training for criminal enforcement, particularly in problem regions, such as Guangdong Province, and likewise with respect to export-related cases;

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<sup>10</sup> The MPS issued four sets of regulations in early 2006 to promote criminal transfers and tactical cooperation with key administrative enforcers, including the Administrations for Industry and Commerce, the National Copyright Administration and Customs. IACC members have seen few signs that these new regulations are being actively implemented.

<sup>11</sup> See SAIC statistics reported at <http://www.saic.gov.cn/hdxw/news.asp?newsid=1189> .

- strengthening the deterrent impact of administrative enforcement;
- taking more effective measures in problem regions to address “protectionism” - which currently undermines both administrative and criminal enforcement; and
- reducing or substantially eliminating thresholds and other obstacles to the commencement of both criminal investigations and prosecutions of violators. This could be accomplished in the short term through judicial guidelines and in the longer term through amendment of the PRC Criminal Code.<sup>12</sup>

Regrettably, the State Council’s March 2006 Action Plan does not heed these recommendations. Instead, Chinese Government officials have effectively refuted each of them in the press and in bilateral discussions by asserting time and again that the current allocation of resources for criminal enforcement is adequate, administrative enforcement is sufficient, and China’s Criminal Code is fully consistent with both the TRIPS Agreement and China’s internal economic conditions.<sup>13</sup> This is regrettable as the reforms proposed would principally benefit local industry, rather than foreign rights holders, and would likely pay for themselves by stimulating local innovation and production.

The current logjam in inter-governmental discussions over enforcement reforms could soon lead to a WTO dispute, or series of disputes, which could be counter-productive in a number of ways, particularly if the Chinese government misunderstands the motives behind such complaints. The Chinese government has already sent clear signals that it would regard the threat of WTO complaints as akin to commencement of a trade war and it appears this has stifled open research and debate over legal reforms among Chinese experts. Indeed, there are indications that studies commissioned by Chinese government departments regarding the economic impact of counterfeiting and enforcement policies have been kept confidential, in part to hide dirty linen that might embarrass the Government and in part to deny foreign governments evidence that might be useful in WTO proceedings.<sup>14</sup>

IACC members appreciate the resource limitations faced by China - and indeed all countries - in the battle against counterfeiting. Our members are likewise

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<sup>12</sup> Following consultations in December 2006 between USTR and the Chinese Government, it now appears that this may only be accomplished through the amendment of China’s Criminal Code.

<sup>13</sup> The rejection of reforms by Chinese officials expressed in the press and industry consultations has led some observers to conclude that the Chinese Government has adopted a secret policy under which counterfeiting and piracy are acceptable tools for promoting local development. Few, if any, IACC members take this conspiratorial view.

<sup>14</sup> By contrast to the current secretive climate, the State Council’s Development Reform Center (“DRC”) issued two economic impact studies in 2000 and 2003, which confirmed that counterfeiting had already begun taking a heavy toll on local enterprises and tax revenues. See <http://www.qbpc.org.cn/en/about/references/drcreports>.

aware that there are legitimate differences between the laws and enforcement systems in China and those in the rest of the world. However, the IACC believes that open debate and detailed research will help to bridge the differences between local laws and international practices, and present China with significantly better policy alternatives. The current position of the Chinese Government does not seem to encourage this.

IACC members hope China will agree to begin steps towards modernization of its Criminal Code as soon as possible. We believe a closer review of the Criminal Code and current enforcement practices by the State Council, National People's Congress (NPC) and other Chinese experts will no doubt generate solutions to a wide range of challenges and close a number of gaps in the current law which are unrelated to TRIPS compliance.

The State Council and NPC are already planning to amend the Trademark Law and Copyright Law by 2008 – presumably in time for the Beijing Olympics. These laws only deal with civil and administrative enforcement of IPR, and the IACC believes it makes good sense to consider an amendment of the Criminal Code in tandem with these revisions.

## **Counterfeiting**

### **Scope of the Problem**

Counterfeiting in China during 2006 continued to cause severe harm to virtually all IACC member companies. Its impact continues to be felt in the domestic market, as well as in other markets to which counterfeits are exported.<sup>15</sup>

The range of products affected is the same as in prior years and includes electronics, pharmaceuticals, household appliances, computer peripherals, auto parts, lighters, optical media, toys, apparel, footwear, luxury accessories (including handbags, jewelry, watches and eyewear) and cigarettes.

DHS statistics indicate that about 70% of the fake goods seized at U.S. borders were fashion, apparel, and footwear, while the remainder included electronics, pharmaceuticals, medical devices, cigarettes and other items.<sup>16</sup>

Counterfeit drugs are currently estimated to occupy about 9% of the market inside China, although for certain items, the penetration of counterfeits is understood to exceed 30%. Counterfeits are continuing to directly threaten consumer health in China, resulting in numerous deaths during the course of 2006.<sup>17</sup> Meanwhile, exports of

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<sup>15</sup> See footnote 6.

<sup>16</sup> See footnote 9.

<sup>17</sup> See [http://news.xinhuanet.com/english/2007-01/10/content\\_5588254.htm](http://news.xinhuanet.com/english/2007-01/10/content_5588254.htm) reporting 11 deaths caused by fake pharmaceuticals made by Qiqihar Pharmaceutical Co. Ltd.

counterfeit Chinese drugs to the developing world are in epidemic proportions, as evidenced by recent reports from countries such as Nigeria, where local authorities believe 68% of all pharmaceuticals are counterfeits - with most coming from China and India.<sup>18</sup> Recent studies by the pharmaceutical industry suggest that these problems are likely to get significantly worse,<sup>19</sup> no doubt due at least in part to the deepening of trade links between counterfeiters globally, facilitated in part by the Internet.

There are signs that counterfeiters are increasingly targeting SMEs--typically small companies that sell specialty products in niche markets.<sup>20</sup>

IACC members continue to regard Guangdong Province as the biggest problem spot for counterfeiting in China. Members also report serious problems in the provinces of Zhejiang and Fujian. Counterfeiting in certain cities in these provinces (and elsewhere) poses critical concern to members in various industries, as set out in the following table:

Guangzhou / Dongguan (Guangdong)	fashion / sports equipment
Shenzhen (Guangdong)	IT / fashion / cosmetics / e-commerce in all products
Beijing	fashion / IT
Chaoyang / Jieyang (Guangdong)	cigarettes / pharmaceuticals
Yiwu (Zhejiang)	wholesale center for almost all products
Ningbo (Zhejiang)	general consumer goods

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<sup>18</sup> See <http://www.law.com/jsp/article.jsp?id=1165413311674>, which also contains a detailed examination of how counterfeit pharmaceuticals are distributed globally. See also <http://westafrica.andnetwork.com/index?service=direct/1/Home/recent.titleStory&sp=151257> for reports concerning the impact of counterfeit textile designs on local producers in Nigeria.

<sup>19</sup> See report in <http://www.inthesetimes.com/site/main/article/2845/> referring to a study by the Center for Medicines in the Public Interest indicating that counterfeit drug sales are expected to reach \$75 billion globally by 2010, a more than 90 percent increase from 2005. This study refers to India and China as the main sources of fakes.)

<sup>20</sup> See testimony of SMEs before the US-China Economic and Security Review Commission from June 2006 at [http://www.uscc.gov/hearings/2006hearings/hr06\\_06\\_08\\_09.php](http://www.uscc.gov/hearings/2006hearings/hr06_06_08_09.php). Complaints from SMEs in Europe, Japan and the U.S. are increasing the pressure on governments to press China for more rapid progress on a range of IPR issues. See also Dallas News, July 18, 2006, at [http://www.dallasnews.com/sharedcontent/dws/bus/stories/DN-chinapiracy\\_18bus.ART0.State.Edition1.17a2c9c.html](http://www.dallasnews.com/sharedcontent/dws/bus/stories/DN-chinapiracy_18bus.ART0.State.Edition1.17a2c9c.html).

Cixi (Zhejiang)	auto parts
Wenzhou (Zhejiang)	lighters
Quanzhou / Jinjiang (Fujian Province)	footwear

IACC members report that counterfeiters are continuing to respond to increased enforcement by going deeper underground, particularly by establishing unlicensed “underground” manufacturing facilities, often operating at night.

Furthermore, IACC members report much more extensive and sophisticated use of the Internet for both domestic and international trade in counterfeits. This includes through well-known B2B portals, such as Alibaba.com and Taobao.com, as well as through some smaller sites. Fashion and apparel brands are common the victims, but sites offering fakes of high-tech products, such as computer peripherals and other electronic products, are now proliferating, with most operators seemingly based in or near the city of Shenzhen. To illustrate the trend, the IACC recently conducted a search of ten major apparel and footwear brand names in Taobao.com which revealed over 1.9 million “hits”. Searches of non-fashion brands also revealed troubling results – for example, over 6,100 hits were revealed for each of two brands in the household product and information technology sectors.

While not all of the trade in the above brands relates to counterfeits, there is good reason to believe a significant portion does.

Private investigations into parties offering counterfeits over the Internet are normally time-consuming and rarely achieve the goal of identifying the vendor, as the vast majority of advertisers provide false contact details and otherwise go to great lengths to hide their true identity and location. Given the difficulty in investigating Internet traders, combined with the sheer number of them, most IACC members are only able to pursue a handful of such cases in any given year.

Anecdotal reports from members and police in various countries suggest that overseas counterfeiters that source from China are engaged in a highly organized and profitable business which renders profits in the millions of dollars annually.<sup>21</sup>

<sup>21</sup> To illustrate, see The Oregonian (July 30, 2006), reporting on a counterfeiter of Nike and other brands that was found to have generated US\$2.5 million in profits over two years See <http://www.oregonlive.com/news/oregonian/index.ssf?base/news/1154154316261040.xml&coll=7&thispage=1#continue>; and Report on Australian counterfeiting ring which likewise netted over US\$1 million, see The Age, Aug. 3, 2006 (Australia) - <http://www.theage.com.au/news/National/Huge-haul-of-fake-designer-gear-seized/2006/08/03/1154198249386.html>.

## Progress and Problems in Enforcement

Overall, despite measured progress in criminal enforcement, IACC members report that the impact of their investments in enforcement has been negligible. Enforcement sweeps against factory and distribution targets are still perceived as temporary or cosmetic measures which are unlikely to prevent the recurrence of counterfeiting. Several of our members have reported having conducted two, three or more administrative raids before finally stopping infringers through intervention by the police.

Over the course of 2006, China's top leaders appear to have responded positively to increasing pressure from both overseas and local companies for a more coherent Government IP policy. President and Communist Party General Secretary Hu Jintao gave speeches promoting the need for stronger enforcement under the slogan of "building an innovation society".<sup>22</sup> Premier Wen Jiabao and other leaders have explained the need for better IPR protection in positive ways, pointing out the benefits for building a more competitive local industry.<sup>23</sup>

To tighten planning and coordination on anti-counterfeiting and other IP issues, the State Council issued an Action Plan in March 2006, which included an extensive list of public awareness, enforcement, research and legislative initiatives to be undertaken between 2006 and 2007.<sup>24</sup> Although there are obvious gaps in the Action Plan, there is no doubt the Chinese Government is taking IPR protection more seriously, and increasing the level of coordination and leadership devoted to the issue.<sup>25</sup> Particular efforts are being made by the Economic Crimes Investigation

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<sup>22</sup> See <http://www.china.com.cn/chinese/2006/May/1221360.htm> reporting on speech of May 27, 2006 (in Chinese).

<sup>23</sup> Premier Wen has been quoted as stating that China's IPR enforcement efforts "will carry the full force of steel and will definitely not be something as soft as bean curd". See Financial Times, September 5, 2006, <http://search.ft.com/ftArticle?sortBy=gadatearticle&queryText=wen+jiabao&y=0&aje=true&x=0&id=060906001073&page=10>. See also, [http://www.sipo.gov.cn/sipo\\_English/gfxx/zyhd/200609/t20060908\\_110268.htm](http://www.sipo.gov.cn/sipo_English/gfxx/zyhd/200609/t20060908_110268.htm)

<sup>24</sup> The English version of the Action Plan is available at: [http://www.ipr.gov.cn/ipr/en/info/Article.jsp?a\\_no=3326&col\\_no=102&dir=200604](http://www.ipr.gov.cn/ipr/en/info/Article.jsp?a_no=3326&col_no=102&dir=200604). Since the issuance of the Action Plan, the Government has used the portal <http://www.ipr.gov.cn> to promote public awareness of new initiatives and progress in IPR protection, including anti-counterfeiting. This portal provides access to an impressive array of data, but there is little critical commentary or links to other sites dealing with more sensitive issues, including counterfeiting and piracy.

<sup>25</sup> While some observers have criticized establishing the leadership organ for IP coordination and policy making within the Ministry of Commerce (MOFCOM), there are few other obvious options, as the State Intellectual Property Office (SIPO) is still viewed by other ministries as too much of a competitor. The fact that leadership in IP coordination in the US lies with the US Department of Commerce should not be forgotten in this regard.

Division (ECID) of the MPS, under the able leadership of Director Gao Feng, which established an IP Crimes Bureau on January 1, 2006. The Bureau has several officers exclusively focused on IPR protection.

Significant pilot projects are also being pursued in various cities, most notably in Shanghai, where the Pudong prosecutors' office has established a unified database intended to provide access to information on IPR violations dealt with by all major enforcement bodies in the city.

IACC members have been heartened by improvements in cooperation with the Chinese police and prosecutors in many cities over the course of 2006. This is reflected in the latest available statistics from the SPC and MPS, which indicate an increase of 52% in the number of criminal convictions for IPR crimes, to a total of 769 cases (involving both foreign and domestic rights holders).<sup>26</sup> In addition to these cases, Chinese courts reportedly convicted offenders in 1,508 cases under Art. 140 of the Criminal Code, which outlaws the sale of “fake and shoddy” goods. Many of these cases also involved the counterfeiting of trademarks.<sup>27</sup>

Members report that criminal enforcement in China is rarely an automatic process, as it is in many other countries. Instead, rights holders normally need to dedicate significant time and resources in liaising with authorities at all levels in order to achieve positive results. And in most cases, this liaison requires drawn-out argumentation and lobbying, e.g., pressing police to commence investigations based on reasonable suspicion a crime has been committed, arguing for a proper valuation of seized counterfeits and the prompt transfer of cases to the police, pressing for admission of critical evidence (including circumstantial evidence), arguing for more severe sentences, and other matters.

IACC members believe that amendment of the Criminal Code would help greatly in simplifying the procedures for pursuing counterfeiting cases, and eliminating the current ambiguities and loopholes that provide safe harbor to counterfeiters.

As indicated above, some of our members are finding it much easier to pursue criminal cases than they did three years ago. Police, prosecutors and judges in many cities clearly have a much greater understanding of IPR and the importance of criminal enforcement, and the trend is improving. However, this progress is not reflecting itself in a significant reduction in the level of counterfeiting for our members. As enforcement increases, the counterfeiters that inflict the most damage continue to get smarter and take greater measures to shield themselves from detection. Consequently, real progress will only be achieved by increasing the number of criminal

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<sup>26</sup> This 52% increase is consistent with the increase in PSB arrests of IPR offenders in 2005—51%. See the IACC's 2005 301 report at [http://www.iacc.org/resources/2005\\_USTR\\_Special\\_301.pdf](http://www.iacc.org/resources/2005_USTR_Special_301.pdf)

<sup>27</sup> Regrettably, the SPC has not been able to track the actual number of trademark counterfeiting cases which were decided under Art. 140.

investigations, and in targeting both large and small targets in a strategic manner which is carefully designed to generate the maximum deterrence.

Particular attention will clearly need to be given to intensifying criminal enforcement in hot-spots, such as Shenzhen, Guangzhou, Dongguan, Yiwu and Beijing.<sup>28</sup> There are encouraging signs that the police in some of these cities are finally gearing up to respond to the challenges at hand, and members report ground-breaking meetings with PSBs in Guangzhou and Beijing during the course of 2006 which will hopefully lead to positive results in the course of 2007.<sup>29</sup>

Given cost and other considerations, IACC members continue to file the vast majority of their complaints through administrative authorities - principally the AICs. As noted above, in theory, cases which meet relevant numerical thresholds should be transferred to the PSB for criminal investigation. But while complete statistics are not yet available, it appears that out of 33,900 cases handled by the AICs in 2006, only 111 were successfully transferred to the police, representing less than 0.3% of the total. The total also represents a drop of 52% in the total number of transfers as compared to 2005.<sup>30</sup> The IACC is hoping that these figures are incorrect and that the State Administration for Industry and Commerce ("SAIC") will soon publish updated figures which indicate a stronger performance.<sup>31</sup>

Moreover, IACC members report continuing resistance from local AICs and pricing bureaux in adopting the price of the legitimate product as the basis for case valuations – normally a sign of protectionism and a total barrier to rights holders who

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<sup>28</sup> The State Tobacco Monopoly recently disclosed that over 1,700 cigarette counterfeiters had been arrested, presumably by local PSBs, during the course of 2006. See <http://www.china.org.cn/english/GS-/195786.htm>. This probably represents more arrests than in any other industry. It is widely known that Chinese tobacco companies contribute additional funds to facilitate the involvement of police in anti-counterfeiting work.

<sup>29</sup> In Guangzhou, the Guangdong Provincial PSB recently established a liaison office in the Guangdong IP Office to help in promoting greater cooperation and coordination with administrative enforcement authorities. See <http://www.southcn.com/news/gdnews/nanyuedadi/200612110639.htm> (in Chinese). In Shenzhen, the police are reportedly in the process of establishing a team of 36 officers dedicated to IPR enforcement, and as of November, Shenzhen police had already initiated 94 cases, up from 74 in the full 12 months of 2005 - see [http://www.chinadaily.com.cn/china/2006-12/20/content\\_763128.htm](http://www.chinadaily.com.cn/china/2006-12/20/content_763128.htm). Notwithstanding this obvious progress in Shenzhen, counterfeiting of a range of items—particularly IT equipment and fashion—remain at critical levels, and recidivism following administrative raids is likewise extremely common.

<sup>30</sup> See <http://www.saic.gov.cn/hdxw/news.asp?newsid=1189>.

<sup>31</sup> Chinese officials have informally suggested that the disappointing number of official transfers is misleading, since raids are often conducted jointly by AICs and PSBs, and then recorded as PSB matters. But even if true, the total number of criminal cases remains disappointing.

either lack the required know-how or the resources to lobby for proper handling of cases.<sup>32</sup>

At present, there is insufficient published data regarding the success of the AICs and Technical Supervision Bureaux ("TSBs") with respect to administrative penalties imposed in cases they have dealt with. Interim data suggests that the number of cases handled by AICs throughout the country declined from the prior year by about 13%, from 39,800 to 33,800. The number of cases involving foreign trademarks reportedly increased by about 10%, to 7,439. IACC members believe this may reflect an increase in small-scale raids conducted on an *ex-officio* basis and not reported to them. Regrettably, AIC penalty decisions are not generally published - a step which the IACC recommends to facilitate transparency and to assist rights holders in identifying and targeting repeat offenders.

### Laws and Regulations

*Criminal Code* - The IACC's last 301 report contains a detailed examination of the obstacles to effective enforcement presented under the current Criminal Code as well as the December 2004 SPC/SPP judicial interpretation on IP crimes, which reduced most numerical thresholds by 50%.<sup>33</sup> By and large, the experience of IACC members during 2006 supports this earlier analysis and the IACC's main recommendations are still applicable, i.e.:

- China should urgently begin research towards the amendment of the Criminal Code to eliminate the need for "serious circumstances" or "relatively large sales", and adopt criteria for criminalization that are consistent with international practice and Art. 61 of the TRIPS Agreement, which mandates a standard of "commercial scale" for criminal liability.
- Pending amendment of the Criminal Code, the SPC and SPP are encouraged to issue a new judicial interpretation to lower existing numerical thresholds, clarify pricing methods to eliminate the current deviations by local authorities, and introduce clear and practical non-numerical criteria for criminalization – including those that encourage reliance on circumstantial evidence of the scale of an infringement from the rights holders and evidence of repeat offences (i.e.

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<sup>32</sup> Under the judicial interpretation on IP crimes issued December 2004 by the SPC and Supreme People's Procuratorate, legitimate product prices should in principle be used to calculate case values where there is no evidence of the infringer's actual sales prices charged in prior transactions. Infringers will only rarely keep written records of their prior sales and they will likewise normally refrain from providing other evidence of their prior transactions. Consequently, in principle, the AICs and police should normally adopt legitimate product prices as the basis for calculating case values. In some regions, this is accepted practice, while in others, alas, it is the exception, rather than the norm. See further discussion below regarding thresholds.

<sup>33</sup> See [http://www.sipo.gov.cn/sipo/flfg/sfjs/200412/t20041229\\_66782.htm](http://www.sipo.gov.cn/sipo/flfg/sfjs/200412/t20041229_66782.htm).

continued infringement despite receipt of warnings or government enforcement action).

Chinese officials tasked with debating the suitability of the current thresholds for criminalization have expressed concerns that any lowering of the standards will result in unacceptably high numbers of convictions and incarcerations. The IACC wishes to emphasize that, while our members believe more convictions are necessary, they need not always include imprisonment in order to create deterrence. Instead, police, prosecutors and courts can increase deterrence by increasing fines and seizing infringers' assets.

Further, under international practice, police and prosecutors will, by necessity, use discretion in determining which cases to accept and which to refer for resolution through administrative action, civil litigation or settlements. A proper use of this discretion is, of course, critical.

*Trademark Law* - As noted above, the March 2006 Action Plan of the State Council indicates plans to amend the PRC Trademark law by 2008. Drafts of the revised law that have been circulated for industry comment do not appear to propose any significant departures from the current law (last amended in 2001).

The Action Plan suggests that, pending amendment of the Trademark Law, the SAIC might issue new guidelines to help strengthen administrative enforcement. There are however no indications that the SAIC is actively drafting them.

Industry had originally hoped the proposed guidelines would be issued quickly, in particular to establish more detailed criteria for local AICs to rely upon in calculating fines and determining when infringing products, raw materials and production equipment may be seized and destroyed. The need for such guidelines, explained in detail in the IACC's Special 301 submission,<sup>34</sup> has been widely acknowledged by many Chinese officials over the last few years. IACC members believe these regulations are still sorely needed, as fines imposed by local AICs clearly remain too low to create a meaningful deterrence in most cases.

Meanwhile, IACC members report continuing problems with AIC enforcement:

- the return of product to counterfeiters following raids (apparently under improper circumstances);

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<sup>34</sup> The Implementing Regulations to the Trademark Law, issued by the State Council in September 2003, provide for significantly greater maximum fines—up to 300 percent of the illegal business amount—and a discretionary fine of up to RMB 100,000 (US\$12,000) in cases where the scope of an infringement cannot be determined due to the lack of evidence. These regulations also contain provisions permitting the destruction of counterfeit goods and equipment used primarily to make counterfeits. The Trademark Office of the SAIC had been expected to issue rules since 2002 to give guidance to local AICs in the calculation of fines and the conditions under which infringing goods and related production equipment may be destroyed. Without such rules, local AICs are left a high degree of discretion, which experience indicates they are unlikely to exercise in an aggressive manner, absent pressure from higher-level political authorities.

- occasional demands by AICs to pay exorbitant costs for the destruction of seized product or their purchase at auction<sup>35</sup> (The auctioning of counterfeits is not permitted under the TRIPS Agreement or indeed the current Trademark Law in China.);
- resistance by AICs in providing copies of penalty decisions to rights holders and their agents (particularly noted when complaints are filed with the Economic Inspection and Supervision Divisions of the AICs),<sup>36</sup>
- continued demands for “case handling fees” (ban an fei), without issuance of receipts;
- resistance of some AICs to handle complaints based solely on evidence of notarized purchases organized by IPR holder; and
- new requirements by AICs in certain regions (including Beijing, Guangzhou and Shenzhen) that powers of attorney to local investigators and lawyers be notarized and legalized. This requirement can delay enforcement for weeks - and in some cases months - thereby giving infringers time to avoid enforcement entirely. These requirements do not apply to local trademark holders, which presents questions of discrimination.

*Transfer Regulations* – Between January and March 2006, the MPS issued four sets of regulations with the Supreme People’s Procuratorate (SPP), the SAIC, the General Administration of Customs, and the National Copyright Administration respectively. Each of these regulations was designed to encourage local administrative authorities and the police to cooperate more closely on strategic planning and joint investigations, as well as to establish more detailed procedures to hold officials more accountable in the course of handling case transfers. As indicated above, and based on information from IACC members, the new regulations do not yet appear to have been effectively implemented.

The contents of the transfer regulations are largely positive. However, IACC members are concerned over provisions in each which seem to permit the police to reject cases on the basis that the impact of the infringement is “inconsequential”.<sup>37</sup>

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<sup>35</sup> One IACC member was recently approached by an AIC in southern China seeking over US\$100,000 to fund the destruction of a consignment of seized counterfeits. In this case, the AIC threatened to release the goods into commerce if payment was not made.

<sup>36</sup> One IACC member reported that the AICs have issued penalty decisions in only five of 18 cases pursued in 2006.

<sup>37</sup> See Art. 9 - SPP/MPS Regulations: “If, following investigation, the public security authority determines that there is no evidence of a crime in a violation of the law which it discovered, or if, after investigation following the opening of the case, it is of the opinion that the **circumstances of a criminal offense are clearly inconsequential** and there is no need to pursue criminal liability, but, in accordance with the law,

These provisions are supported by Art. 15(1) of the PRC Criminal Procedure Code, which allows the police to refuse to investigate or otherwise drop pending cases where it is determined the violation “is obviously minor, causing no serious harm”. To date, these provisions in the transfer regulations have not been cited in decisions by the police or other authorities not to pursue cases. Our members are however concerned that they will eventually be exploited by protectionist officials to frustrate proper handling of cases. While we believe that authorities should be given discretion to accept or reject cases, clearer guidance should be given to avoid miscarriages of justice. To avoid such problems, the IACC recommends that the MPS and SPP require local authorities to give full consideration to circumstantial evidence of prior transactions.

*SPC Opinion on Enforcement* – The SPC issued an opinion on January 11, 2007,<sup>38</sup> which both repeats existing policies and encourages judges to take more progressive approaches to various issues arising in the course of IPR disputes. The IACC regards this new opinion as a potentially valuable tool in many respects, since it provides rights holders with new ammunition to persuade courts to impose more deterrent penalties.

The main provisions of the new opinion include the following:

- Judges are encouraged to increase compensation awards and impose civil fines (rarely imposed to date) in order to increase deterrence;
- Courts are encouraged to impose preliminary injunctions (also rare) based on an evaluation of the damage that might be caused by the infringement and the likelihood of success of the plaintiff (factors missing from earlier judicial interpretations on the subject);

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administrative liability should be pursued, it should promptly transfer the case to the administrative law enforcement authority.”

Art. 8 - SAIC/MPS Regulations: “If it is of the opinion that there are no facts establishing a criminal offence and therefore no need to pursue criminal liability, **or that legal proceedings should be instituted by the rights holder directly with a People’s Court**, and does not open a case for investigation, it shall state the reasons therefore and notify the administration for industry and commerce.”

Art. 9 - MPS (Social order) / NCA: “If the public security authority is of the opinion that the circumstances are **relatively insignificant** and no criminal offense is constituted, it shall state the reasons therefore and notify in writing the copyright authority that reported the leads.”

Art. 9 - MPS/Customs: “If, after investigation, the public security authority is of the opinion that no criminal offense was in fact committed by the Party/Parties, or that the facts of the criminal offense are **obviously insignificant** and no pursuit of criminal liability is required, it shall return the relevant goods or articles to the customs house.”

<sup>38</sup> The SPC opinion is formally called the “Opinions of the Supreme People’s Court on the Comprehensive Strengthening of Intellectual Property Trial Work and the Provision of Judicial Guarantees for Building an Innovation-Oriented Country”.

- Judges are encouraged to notify plaintiffs in civil cases of their rights to pursue private criminal prosecutions and to transfer evidence to the police for possible public prosecutions;
- Courts may now consider evidence from abroad that is not notarized and legalized, provided that the defendant does not raise credible challenges to such evidence;
- Judges may issue orders to aid litigants to obtain evidence from the other party or third parties, where such evidence cannot otherwise be obtained;
- Industry associations to take a role in “helping to remove an antagonistic mood and coordinating the resolution of conflicts and disputes”;
- Judges are to resist protectionism; and
- Local courts are to support the work of administrative enforcement authorities and to work with both the government and IPR holder (including industry associations and other experts) to devise solutions to problems as they arise.

*Trade Fairs* - New regulations on the protection of IPR at trade fairs in China entered into effect on March 1, 2006. These regulations, which are based on the long-standing rules used to deal with disputes at the Canton Trade Fair, are applicable to trade fairs with a duration of three days or longer. The new rules require trade fair organizers to remove from display items deemed to be infringing, and provide for blacklisting of exhibitors determined to violate IPR on two or more occasions. While these rules have proved useful in part at the Canton Trade Fair, their utility at other fairs remains largely untested.

Some IACC members have been unable to obtain reliable protection under the new (and old) rules due to requirements imposed by fair organizers and local administrative enforcement authorities that the rights holders provide a notarized and legalized power of attorney in favor of a local agent. This requirement has in the past effectively prevented IPR holders from seeking prompt intervention.

*Complaint Service Centers* – The March 2006 Action Plan indicated plans for the establishment of 50 “complaint filing service centers” throughout China. Most of these have now been opened.<sup>39</sup>

These service centers are intended to provide rights holders with an alternative method of filing enforcement complaints and raising policy issues with local authorities for joint deliberation. Management of the centers differs from region to region, with responsibility resting normally with either the Intellectual Property

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<sup>39</sup> See <http://jbs.ipr.gov.cn> for information in Chinese.

Office (which normally handles patent matters), the AIC or the local office of MOFCOM.

Based on the information available so far, the centers appear intended to provide ombudsman support, rather than another procedural burden, for rights holders, and so have generally been welcomed by rights holders.

On December 28, 2006, the Market Order Rectification Office (MORO) of MOFCOM, together with eight other enforcement authorities, issued general guidelines governing the service centers. Under the new guidelines, the centers are empowered to accept complaints from rights holders regarding all forms of IPR infringement, after which they will refer them to the relevant government department for handling. The process of allocation for counterfeiting and piracy cases remains unclear, but it presumably allows the center's personnel to deliberate with multiple enforcement authorities and arrive at a consensus view on which authority will take charge. Fortunately, the guidelines explicitly permit the allocation of cases to the PSBs, and they do not require (as originally feared) that complaints first be funneled through the AIC or TSB. The new guidelines suggest that the centers will provide a channel for dialogue and coordination in the handling of novel legal issues and "important" cases.

Rights holders who file complaints through the centers can obtain feedbacks on their status and results, but they are otherwise required to comply with all of the documentary and evidentiary requirements imposed by the ultimate enforcement authority handling the case. It remains unclear, however, whether a rights holder who has already filed a complaint directly with an enforcement authority can seek advice or even official intervention from a service center in dealing with protectionism, new legal issues, or other matters that arise in the course of a dispute.

IACC members have limited experience in utilizing the service centers, but the experience so far has been positive. The centers appear in some cases to have generated a sense of transparency that may reduce the influence of protectionism in the handling of IPR cases. In other cases, however, it is clear that reliance on the centers has alienated enforcement authorities - perhaps because they dislike the supervision.

#### Retail Markets – Landlord Liability

During the April 2006 JCCT meetings, China's only undertaking vis-à-vis trademarks was to take steps to address counterfeiting in retail markets. The year witnessed a number of interesting developments, mainly in response to initiatives pursued by IACC members (working in cooperation with the QBPC's Luxury Industry Working Group) targeting landlords in the Silk Market as well as other major retail markets infamous for the sale of counterfeit fashion apparel and accessories, including jewelry, leather goods, time pieces, eyewear and footwear.

The JCCT meetings were followed in June 2006 with the closure of the infamous Xiangyang Market in Shanghai, and its 800 shops which reportedly generated US\$50

million in counterfeit trade annually.<sup>40</sup> IACC members report, however, that the vendors in the Xiangyang Market quickly found new homes in other markets, including new markets such as Taobao City, where vendors are equipped with computers to facilitate e-commerce.

The news was not altogether negative, though. During 2006:

- Decisions were issued by two courts in Beijing against the landlord of the Silk Market (Beijing Silk Street Clothing Market Co. Ltd.), confirming that landlords may be held liable, both civilly and administratively, for counterfeiting which takes place on their premises;
- In decisions involving Gucci, Louis Vuitton, Prada, Chanel, and Burberry, the Beijing Higher People's Court confirmed a decision of the No. 2 Intermediate People's Court which held that the landlord had an obligation to take timely and effective measures to stop infringements once they are brought to the landlord's attention. The lower court decision had awarded the five brand owners RMB20,000 (US\$2500) each; and
- The Chaoyang District Court confirmed the legality of an administrative fine of RMB100,000 (US\$12,000) imposed in April 2006 against the same landlord, and on similar grounds as the Higher People's Court decision. This decision is now under appeal with the No. 2 Intermediate People's Court, and a decision is expected soon.

In parallel with these legal actions, IACC members have attempted to cooperate with landlords in several markets in Beijing, and ultimately executed a Memorandum of Understanding (MOU) with three landlords - including the Silk Market - in June 2006. The MOU establishes a two-strike rule under which landlords agree to suspend the leases of outlets following a first offence and terminate such leases following a second offence.

The MOU has been successfully relied upon in the 3.3 and Hongqiao markets in Beijing, whereas the Silk Market has taken extensive measures to avoid its implementation.

Indeed, a survey of the Silk Market conducted in January 2007 revealed that counterfeiting has only worsened, and dramatically so. The survey identified 4,460 infringements of 136 different international brand names, with violations observed in 937 outlets, or 65% of all outlets in the market. Among outlets selling watches, all were observed selling counterfeits. Among those selling footwear, leather goods, and eyewear, the ratios were 96%, 93% and 80%, respectively. The survey also sought to verify recidivism by 31 outlets that had been fined by the Chaoyang AIC in 2006. Most of these outlets had changed their locations (no doubt with the landlord's

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<sup>40</sup> See [http://english.people.com.cn/200607/26/eng20060726\\_286976.html](http://english.people.com.cn/200607/26/eng20060726_286976.html).

knowledge) to frustrate detection, but they were ultimately identified in their new locations. 30 of the 31 were found selling counterfeits, with some also selling the same brand for which they had been fined previously. The landlord of the Silk Market has gone to great efforts to seek to demonstrate its support for IPR, including through award programs and other educational activities for outlets. It has also forwarded warning letters to the local AIC for investigation and threatened to sue the Beijing AIC for its failure to more effectively enforce IPR in the market. However, these measures are clearly intended to divert attention from the landlord's failure to respond effectively to sightings supplied by brand owners.

There is of course little doubt that the Beijing PSB and AIC also bear responsibility for their failure to more proactively address rampant counterfeiting in the Silk Market and other markets in the city. IACC members are working with the municipal government to explore solutions, including criminal, administrative and civil enforcement, to bring counterfeiting of their brands under control. But in the meantime, IACC members believe the Beijing government's resistance to providing a reasonable level of criminal deterrence against the bigger distributors that supply the markets is untenable. The IACC also believes that the virtually unbridled counterfeiting in retail and wholesale markets in Beijing, Guangzhou, Shanghai and other major cities amply demonstrates the need for the elimination of numerical thresholds for criminal liability. While administrative and civil measures will no doubt remain the primary tools for combating counterfeit sales in these markets, the threat (however limited) of criminal liability is probably a precondition to success.

IACC members are now preparing to institute a new joint campaign to test landlord liability theories in Guangzhou and Shanghai, relying on the success (however limited) enjoyed in Beijing.

### Customs

IACC members have been particularly impressed with the achievements of the Chinese Customs over the last year in monitoring and seizing infringing goods at China's borders. The number of seizures of infringing goods - mainly counterfeits - doubled to 2,473. Customs seized a total of 196.8 million infringing items, valued at over RMB 200 million (US\$25 million). Customs in various cities have also implemented action plans to target small-scale exports of counterfeits through postal and express mail services.<sup>41</sup>

Moreover, as of October 2006, Customs reportedly had attempted to transfer at least 20 cases to the PSB for criminal investigation. Positive results have apparently been realized in at least five of these cases. Customs is clearly making good on promises to criminalize cases where possible, relying in part on the above-mentioned criminal transfer regulations issued in early 2006.

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<sup>41</sup> See for example reports on postal enforcement programs in Sichuan Province at [http://english.gov.cn/2006-09/07/content\\_381882.htm](http://english.gov.cn/2006-09/07/content_381882.htm).

IACC members report that difficulties in criminal transfers are now mainly encountered as a result of PSB reluctance to dedicate the necessary time and resources for investigations into the source of goods. This is understandable, since in most cases, the exporter identified by Customs is merely a freight forwarder, and the factory supplier is located in a different city -sometimes far away. Rather than investigating themselves, some PSBs instead seek to transfer responsibility for such cases to the PSB located in the same region as the factory. The IACC encourages the MPS and local PSBs to facilitate such transfers and, where needed, to provide the resources for travel and other incidental costs.

In 2006, the General Administration of Customs ("GAC") issued new regulations which allow frequent users of the Customs enforcement system to pay a general bond and thereby avoid the need to pay bonds following each seizure. The experience of IACC members with these new regulations is still limited.

IACC members still have a range of concerns over the following issues, and it is hoped that the GAC will consider addressing them in due course:

- Requirements (in practice) that seized counterfeits be donated to charity without the IPR owner's approval or the opportunity for monitoring;
- Low administrative fines. Relevant regulations only authorize fines up to 30% of the value of goods - far too low to generate credible deterrence;
- For cases initiated by the Customs but later transferred to Chinese courts, the lack of rules to avoid the need for double-payment of bonds;
- The need for greater cooperation between Customs and IPR holders, particularly in disclosures of information regarding the source and destination of infringing items; and
- Slow return of bonds to rights holders. IACC members report that bonds are normally returned within one to two years after seizures take place. Under relevant regulations, rights holders would normally expect return of their bonds, minus storage costs, within 6 to 12 months; the reality in practice is often different.<sup>42</sup>

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<sup>42</sup> One IACC member reports that Customs in one Southern Chinese city has not returned substantial bonds paid as early as 2004. Naturally, the brand owner fears that pressing too hard for return of the funds might harm their working relations.

## Copyright

### Optical Disc Piracy

Piracy of optical discs, combined with limits on market access, remains a critical problem for IACC members. The Chinese Government has reported having seized 150 million optical disks during 2006 - up almost 45% from the prior year. These seizures were conducted as part of over 105,000 raids, which resulted in the closure of 370 companies and criminal arrests in 350 cases. The Government has also claimed that it shut down 14 DVD plants last year.<sup>43</sup> Meanwhile, in a landmark cases decided in November 2006, a Chinese court imposed a life sentence on a pirate DVD trader, Mr. Lin Yuehua, who between 2002 and 2005 imported into China 30 million pirated optical disks, generating revenue of over US\$23 million.<sup>44</sup>

Industry efforts to measure the extent of harm from piracy to both local and foreign rights holders in the film industry were highlighted in a detailed report by the China Academy of Social Sciences published in June 2006.<sup>45</sup> IACC members also report a new sense of cooperation from MPS divisions responsible for both copyright enforcement and Internet crimes. However, IACC members have received very limited information on criminal enforcement against copyright infringers in the last few years, and our members remain concerned over the lack of transparency in the Government's record in both criminal and administrative enforcement of copyright enforcement. Furthermore, in practice, our members report extreme difficulty in convincing the local police to commence criminal investigations into copyright cases. Our members likewise report extreme difficulties in convincing administrative enforcement authorities to cooperate in the transfer of cases to the police.<sup>46</sup> The impression ultimately created among IACC members is that the Chinese police are still uninterested in criminal enforcement of copyrights - particularly those involving foreign rights holders.

Where criminal enforcement does take place, action is very often based on censorship provisions in the Criminal Code (Art. 225) rather than copyright provisions. This is unsatisfactory from a number of perspectives, but particularly with respect to accountability, since the impression given to the market is that the decision to pursue

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<sup>43</sup> See [http://news.ipr.gov.cn/ipr/news/info/Article.jsp?a\\_no=48211&col\\_no=1&dir=200701](http://news.ipr.gov.cn/ipr/news/info/Article.jsp?a_no=48211&col_no=1&dir=200701).

<sup>44</sup> See press report at: [http://www.contactmusic.com/news.nsf/article/chinese%20movie%20pirate%20sentenced%20to%20life\\_1014582](http://www.contactmusic.com/news.nsf/article/chinese%20movie%20pirate%20sentenced%20to%20life_1014582).

<sup>45</sup> See [http://www.uschina.org/public/documents/2006/07/cass\\_piracyimpact\\_e.pdf](http://www.uschina.org/public/documents/2006/07/cass_piracyimpact_e.pdf) for English version of this report. See also [http://english.people.com.cn/200611/28/eng20061128\\_325713.html](http://english.people.com.cn/200611/28/eng20061128_325713.html) for discussion of harm caused by piracy to local authors.

<sup>46</sup> In many cases, administrative enforcement authorities will refuse to consider transfers based on the history of resistance by local police to give due priority to copyright cases.

criminal enforcement rests solely with the Government, and that direct complaints by the copyright owner can be ignored.

The IACC emphasizes the need for China to review provisions in its Criminal Code to ensure full compliance with the TRIPS Agreement, and eliminate or further reduce thresholds applicable to copyright crimes. We further call on the Chinese Government and legislature to eliminate other unreasonable obstacles to copyright enforcement contained in the Criminal Code, including the “for profit” requirement for liability in Article 218 and the provision in Article 219 which limits criminal liability for vendors of infringing items to cases where it can be proved the offender has earned profits over RMB100,000 (US\$12,500).<sup>47</sup>

### Online Piracy

Online piracy is also becoming an increasingly critical concern for holders of copyright in many types of works, but particularly in music, film and software. There are currently hundreds of thousands of pirated music and music files available for downloading globally on websites operated out of China. Works become available online within a few days of their initial release and long before their formal entry into the Chinese market. Peer-2-peer file sharing services (e.g. Bit Torrent) and special music search engines (e.g. Baidu) significantly aggravate these problems.

In July 2006, the Regulations on the Protection of the Right of Communication through Information Networks entered into effect, providing rights holders with access to more reliable administrative remedies against ISPs who offer or facilitate pirated content. The regulations provide for fines up to about US\$12,000 for a range of offences, including anti-circumvention.<sup>48</sup> China also joined the WIPO internet treaties in December 2006.

Police and prosecutors in the Haidian District of Beijing also brought what appears to be the first criminal case involving online copyright piracy: the copying of software and distribution of anti-circumvention plug-ins for the popular online game “Legends of Mir 3”. An encouraging start, but there is clearly still a long way to go in generating criminal deterrence in the online environment in China.

On the civil side, Beijing courts have recently issued several inconsistent decisions regarding liability for web hosting services - thereby leaving the law in this area highly unsettled. The most noteworthy of these cases involved actions by seven international music labels against the leading Chinese portal and search engine Baidu, which provided deep-links to pirated sound recordings. The court of first instance

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<sup>47</sup> The IACC’s members in the film industry report new and troubling problems arising from the videotaping of films in Chinese cinemas. It is hoped that future revisions to the Criminal Code and other administrative regulations will facilitate the imposition of appropriate penalties for such activity, as is the case in most other countries.

<sup>48</sup> See <http://www.ncac.gov.cn/servlet/servlet.info.InfoTopicServlet?action=topiclist&id=30>.

rejected the plaintiffs' copyright claims and held in favor of Baidu. This holding was an unexpected departure from prior decisions by the very same court, including a decision involving similar violations by the Chinese web portal chinamp3.com. The IACC is closely monitoring appeals filed in both the Baidu and chinamp3.com cases.

### Software

Despite measured progress over the last few years, software piracy remains at extreme levels in China, with over 86% of software used in China being estimated to be unlicensed.<sup>49</sup> Local software makers seem to suffer to an equal degree.<sup>50</sup> However, in furtherance to its JCCT undertakings, during 2006, China continued to implement software legalization programs for government departments<sup>51</sup> and State-owned enterprises, and introduced new policies requiring personal computer manufacturers to install licensed operating systems.<sup>52</sup> As noted above, China also joined the WIPO internet treaties in December 2006. Notwithstanding the progress being made, China still has not taken steps to clarify the conditions under which end-user piracy may be criminal.

### Conclusion

The Chinese Government's efforts to date in responding to international as well as domestic concerns over high levels of counterfeiting and piracy deserve recognition and encouragement. However, it is widely accepted that the challenges being faced are large and complicated, and the measures taken by the Government to date have had limited impact on the overall level of IPR infringement in the Chinese market. The IACC, therefore, again encourages the Chinese Government and legislature to conduct a more comprehensive review of the options for legal and administrative reform, focusing particular attention on the following reforms, proposed in the IACC's 2006 submission to USTR:

- allocating much greater resources to criminal prosecutions of trademark as well as copyright offences;

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<sup>49</sup> BSA statistics were issued in May 2006. See <http://www.bsa.org/EastMediterranean/press/newsreleases/eastmediterraneanpressrelease23may2006.cfm>.

<sup>50</sup> Chinese translation software giant Kingsoft claims that 90% of its software is pirated. See <http://www.qbpc.org.cn/files/July/200607newsletter.html>.

<sup>51</sup> At the time of writing, it is still unclear whether the Government has allocated adequate funding for complete legalization of software used by Government departments. Furthermore, plans for auditing of Government departments have not been disclosed.

<sup>52</sup> The Government has not yet clarified for PC makers the types of information they will need to supply to monitor compliance.

- establishing specialized IPR enforcement units within Chinese police and prosecutors, especially in key hotspots, such as Guangzhou, Shenzhen, Yiwu;
- promptly issuing promised regulations to promote the transfer of administrative cases to the police - in particular Customs cases;
- amending the Criminal Code to ensure compliance with the TRIPS Agreement of the WTO, as well as with the objective needs of the market. Pending amendment of the Code, prompt clarification of numerous ambiguities and loopholes contained in the December 2004 judicial interpretation on IPR crimes;
- introducing greater transparency regarding Government enforcement efforts, including regular issuance of more detailed statistics;
- substantially increasing publicity and public education about IPR protection and Government enforcement work;
- adopting new measures to allow higher-level criminal and administrative enforcement authorities to promptly address local protectionism and other obstacles to effective enforcement, e.g., through the adoption of new database and reporting systems;
- strengthening administrative enforcement by the AICs and TSBs through the adoption of new enforcement guidelines and procedures;
- eliminating notarization and legalization requirements for Powers of Attorney submitted with AIC complaints;
- expanding Government efforts to press landlords to self-police against counterfeiting in retail and wholesale markets, not only for fashion but for all types of products, and throughout China;
- requesting the SPC and NPC to issue new standards for awards of statutory damages and issuance of preliminary injunctions, as well as new rules that will reduce the amount of bonds required for evidence and asset preservation under the Trademark Law and Copyright Law in cases of egregious counterfeiting and piracy; and
- considering new measures for using administrative means to control counterfeiting, including through greater regulation of the supply of raw materials for drugs and other products, as well as access to industrial-grade electricity, etc.

Finally, the IACC strongly encourages the Chinese Government to carefully review its procedures for gathering and publishing enforcement data so that the public will have a better tool for measuring progress.

## **BRAZIL**

### **Recommendation: Priority Watch List**

#### **Introduction**

Following the 2004 report by the Brazilian Chamber of Deputies Commission of Inquiry into Piracy, the Brazilian government has made visible efforts to fight counterfeiting. In recent years, Brazil has taken important steps to improve the protection and enforcement of trademarks and copyrights against counterfeiting, including the formation of the National Council to Combat Piracy. Brazil has adopted modern legislation, provided necessary legal rights and remedies to right holders, and given greater authority to customs agencies. Even civil remedies can be effective. Courts in Brazil now regularly order provisional measures in civil and criminal infringement matters within 48 hours, and have awarded significant damages to prevailing right holders.

Unfortunately, the important steps taken by Brazil's government have not been enough to deter the widespread importation, production, and retail sale of counterfeit products in Brazil, particularly in the infamous "tri-border" area encompassing the borders with Paraguay and Argentina<sup>53</sup>. This is partly because the scope of the problem in Brazil far exceeds the public resources now devoted to customs authorities and law enforcement. There are also practices, notably the absence of central customs recordal and inconsistent criminal prosecution, that contribute to the problem. If these shortcomings are corrected, there are opportunities for improving the results of anti-counterfeiting efforts in Brazil.

#### **Nature and Scope of Counterfeiting in Brazil**

Brazil is an end market for counterfeit products, in part, because it is the largest consumer market in South America. Because its long, largely unpatrolled frontier with Paraguay and other South American countries makes smuggling comparatively easy, the majority of counterfeit products available in Brazil are thought to have been produced elsewhere. According to a 2005 survey by Federation of Industries of the State of Rio de Janeiro, counterfeit products are often among the best selling products on the informal market, with sales topping 88 percent of the market share. Coupled with this is a significant amount of locally produced counterfeits, particularly toys and clothing.

The result is that counterfeit products are widely available in large volumes in Brazil, and purchases of counterfeit products amount to billions of dollars annually.

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<sup>53</sup> An excellent article describing the problem in the tri-border area is Sverdlick, Ana R, "TERRORISTS AND ORGANIZED CRIME ENTREPRENEURS IN THE "TRIPLE FRONTIER" AMONG ARGENTINA, BRAZIL, AND PARAGUAY" 9 *Trends in Organized Crime* 84 (2005)

According to surveys conducted by IBOPE, a Brazilian consultancy, the estimated loss attributed to counterfeit products in 2006 for just three industrial sectors – toys, clothing, and footwear – was over 46 billion Brazilian reais, or over US \$25 billion at current exchange rates.<sup>54</sup> What's more, many Brazilian consumers are now in the habit of buying counterfeits. According to the IBOPE surveys, 74 percent of survey respondents in three major cities - São Paulo and Rio de Janeiro and Belo Horizonte –have purchased pirated products, and many of these say they buy counterfeits frequently.

### **Border Control**

The implementation of the Action Plan by the National Council to Combat Piracy (CNCP) as well as the shipments seized along the Paraguayan border by the Federal Police and the Federal Revenue Bureau have resulted in the expected reductions of counterfeit goods in major distribution hubs and trade in general.

The Brazilian Customs Administration (COANA) has authority to conduct ex officio detentions of suspected counterfeit products. Based on additional resources from the federal government, the Customs Administration significantly increased its enforcement efforts in 2006. In particular, the Customs Administration was responsible for 1,025 enforcement actions in 2006 – over 50 percent more than in 2005 – and seized nearly 2,500 vehicles used in counterfeiting. The value of counterfeit products seized was US\$ 287 million – about the same as in 2005. As part of its plan to increase customs enforcement action by 100 percent, the Customs Administration also inaugurated a new headquarters in the city of Foz do Iguacu, State of Paraná, which is on the frontier with Ciudad Del Este in Paraguay. This increase in border enforcement may have contributed to a decrease in the counterfeit products available in the most notorious markets, such as Rua 25 de Março and its environs.

Unfortunately, increased border enforcement on the frontier between the Brazilian state of Paraná and Paraguay appears to have simply redirected counterfeit imports to other frontiers. Based on an increase in counterfeit products seen in this region, counterfeit products are now entering the center west region of Brazil through the Brazilian states of Mato Grosso and Mato Grosso do Sul. Other routes may also be used, as counterfeit products are available in distant states such as Pernambuco and Ceará on Brazil's northeast Atlantic coast and Rio Grande do Sul in the far south.

This unfortunate situation is the result of a severe lack of resources that threatens to undermine the Customs Administration's anti-counterfeiting plan. Even with the recent investment by the federal government, much more needs to be done. According to the Revenue Bureau Inspectors and Auditors Union (Unafisco), the 1,300 customs agents now employed by the Customs Administration is less than one-quarter of those needed at a minimum to impose effective border controls on the Brazilian frontier. Moreover, large swaths of the Brazilian frontier are uncontrolled, i.e. without

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<sup>54</sup> The IBOPE surveys were commissioned by the National Association for the Guarantee of Intellectual Rights – ANGARDI, in partnership with the United States Chamber of Commerce and the Brazil-U.S. Business Council.

regulated border crossings, and customs facilities outside major ports often lack personnel and equipment.

Another positive note is that rights holders have reported success in enlisting Customs officials to detain suspected counterfeits pursuant to administrative procedures. Nonetheless, Brazil lacks both a centralized IPRs database, and formal procedure for nationwide recordal of intellectual property rights with customs authorities. To improve this performance, Brazil should also create a central customs center for IPRs together with a formal, centralized trademark recordal system with nationwide effect.

### **Criminal Enforcement**

Brazil has taken important steps to increase the role of law enforcement in anti-counterfeiting programs. In 2006 the Brazilian Federal Police launched 6,930 new police inquiries in 2006, all of them related to copyright violation and smuggling, and increased significantly the number of seizures at Federal highways. Specialized anti-counterfeiting law enforcement teams and facilities were established in the Brazilian states of São Paulo, Rio de Janeiro, Pernambuco, and Paraná. Brazil took steps to coordinate the enforcement activities of the Customs Administration and the Federal Police, such as training in anti-counterfeiting for both customs agents and police agents.

Brazil should continue to provide the support necessary to sustain and expand the anti-counterfeiting activities of law enforcement. Such steps are necessary to disrupt the widespread availability of – and, it is hoped, the demand for - counterfeit products in Brazil.

The Brazilian federal and state governments should also establish and fund more specialized anti-counterfeiting police unit. State police, together with the Federal Police, constitute a major part of Brazilian law enforcement, but the majority of them lack specialized anti-counterfeiting training. The absence of specialized personnel delays and impedes police inquiries, resulting in poorly conducted investigations and little prospect for identifying the distributor, importer, or manufacturer profiting from counterfeiting. This lack of training is compounded by a chronic lack of resources for state police.

In addition, Brazil should take the following steps to improve criminal prosecution of product counterfeiting.

The Brazilian Congress should enact legislation to extend authority for public prosecution to trademark counterfeiting. Such legislation would authorize prosecutors to institute and prosecute actions against alleged counterfeiters. Legislation doing so for copyright piracy was enacted several years ago. In contrast, there is no authority for public prosecution of trademark counterfeiting, which remains a private criminal offense prosecuted by the right holder, in which the participation of the prosecutor is

limited. The public deception and public safety issues raised by counterfeit products justify extending public prosecution authority for trademark counterfeiting.

The Brazilian Congress should also enact long-pending legislation that would increase imprisonment and other penalties for criminal product counterfeiting. Under current law, prison sentences for product counterfeiting range from a minimum of one month to a maximum of 12 months, which is too lenient to either deter counterfeiting or to motivate public prosecution. Consequently, the Brazilian Congress should enact legislation, such as Bill No 333/1999, which would increase prison terms for counterfeiting to a minimum of two years to a maximum of four years.

There is another serious problem – the reluctance by state public prosecutors – especially outside the states of São Paulo and Rio de Janeiro – to prosecute counterfeiting offenses. For example, Law 9,099/95 provides that first-time offenders who can satisfy other requirements will not face prosecution for crimes with a minimum imprisonment of two years or less. Product counterfeiting falls into this category, and will continue to do so even if the Congress enacts pending legislation. Other theories of prosecutorial limitations anticipate the statute of limitations for crimes in ways that foreclose criminal prosecution.

The application of these prosecutorial rules and practices are not limited to IP crimes, but rather are based on constitutional rules that are applied to all cases. Indeed, they illustrate the current trend in Brazilian law to convert imprisonment penalties into alternative penalties or into community services. Nonetheless, these rules and practices fall far short of what is required by TRIPS Agreement Article 61, namely providing “imprisonment and monetary fines sufficient to provide a deterrent” for willful trademark counterfeiting. Consequently, in practice, few alleged counterfeiters are found guilty by the courts, and those that are receive light sentences that are readily converted into community service orders or other alternative penalties.

### **Public Education**

The importance of public anti-counterfeiting education is illustrated by the results of the IBOPE surveys, which showed that three-quarters of survey respondents in major Brazilian cities have purchased pirated products, and many are likely to be frequent purchasers of counterfeits.

In response, the Brazilian National Council to Combat Piracy created a public campaign called: “Pirates, get away! Only use genuine”. In addition, there are other ongoing educational programs, such as “prize for creativity on fighting piracy”, “game of citizenship” and “click to denounce”. Fortunately, the Brazilian media has taken interest in the counterfeiting problem, probably because of its association with both corruption and risk to public safety. Consequently, the media frequently publishes or broadcasts articles on product counterfeiting that have prodded authorities to take action.

## **Conclusion**

IACC commends the Brazilian government's efforts in responding to international concerns over the high levels of counterfeiting and piracy. However, it is clear that the challenges in Brazil are deep and complicated. Accordingly, the measures taken by the Brazilian government have only had a limited impact on the rampant counterfeiting in the country.

The IACC therefore recommends that the Brazilian Government take the following steps:

- Make IP enforcement a political priority and devote significantly greater resources to customs authorities and law enforcement, particularly along its borders;
- Issue laws and regulations needed to create a proper recordal system for IP rights by Brazilian Customs;
- Train the judiciary and judicial officers so that they are better able to adjudicate IP cases consistently and in line with international standards;
- Substantially increase publicity and public education regarding IPRs;
- Adopt new measures to allow higher-level criminal and administrative enforcement through the adoption of new database and reporting systems;
- Establish and fund more specialized anti-counterfeiting police unit;
- Train State and Federal Police so that they are better able to deal with IPR violations and enforce IP laws;
- Establish specialized IP enforcement units within Brazilian police and prosecutors, at least in key hotspots;
- Enact legislation extending the authority of public prosecutors to institute and prosecute actions against trademark counterfeiters;
- Enact long-pending legislation increasing the imprisonment and other penalties for criminal product counterfeiting; and
- Strengthen government leadership and coordination among the various law enforcement authorities responsible for anti-counterfeiting and anti-piracy.

## CANADA

### **Recommendation: Priority Watch List**

#### **Introduction**

In its 2006 submissions, the IACC noted that with few exceptions, "IACC's members report a continuing lack of proactive effort by Canadian customs and prosecutors in dealing with counterfeiting." It also reported that "the government's continued 'reactive' approach to counterfeiting, inadequate coordination among enforcement bodies, poor cooperation among the authorities and industry in most regions, and gaps in relevant legislation all pose serious obstacles to effective and current enforcement in Canada."

Regrettably, for 2007, IACC's members report that there have been no substantive changes on these issues since its 2006 submissions. Although no substantive changes have been effected, on February 6, 2007 an all party Industry Committee tabled a report in Parliament calling for government action on copyright reform, counterfeiting and piracy. IACC members await the government's response.

#### **Legislative Gaps**

##### **Trademark**

In its 2006 submission, the IACC reported that "Canada's *Trade-marks Act* is in urgent need of amendment." No legislative amendments have been tabled by the Canadian government<sup>55</sup>. In anticipation of a favorable response by the Canadian government to the Industry Committee's report, IACC members report that there are at least three (3) key areas in which amendment is required:

- importation of merchandise bearing a protected trademark that is not manufactured by or on behalf of the trademark holder ("Counterfeit Merchandise") should be included as an infringement/offense under the *Trade-marks Act*;
- an express foundation for *ex officio* enforcement work by Customs should be added by the establishment of an IP recordal system; and
- express criminal prohibitions respecting trademark infringement and passing off and related sanctions as in the *Copyright Act* should be added.

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<sup>55</sup> The Canadian Anti-Counterfeiting Network ("CACN") has prepared and submitted two (2) Position Papers to the Canadian government detailing proposals for reform (see <http://www.cacn.ca/resources>)

Absent specific criminal provisions in the *Trade-Marks Act*, prosecution of trademark counterfeiting can only be pursued under the *Criminal Code*. Proceeding under the *Criminal Code* has two significant drawbacks: proof of knowledge and intent is difficult to establish, because the unique nature of product counterfeiting does not easily fit into general case law respecting proof of *actus reus* and *mens rea*; and prosecution of *Criminal Code* offenses are the responsibility of the provinces and therefore provincial Crown attorneys. Provincial Crown attorneys have the responsibility of prosecuting all Criminal Code offenses, and therefore cannot develop the expertise or devote the resources to prosecuting IP crime.

Separately, the absence of criminal provisions in the *Trade-marks Act* presents practical complications to law enforcement. In a recently released decision of the Federal Court of Canada that dealt with a civil action for copyright and trademark infringement respecting counterfeit Microsoft operating systems and related manuals, both the RCMP and the Québec provincial police had executed search warrants against the defendant's premises prior to the commencement of civil proceedings. Following execution of the provincial search warrant, the provincial police determined that fraud charges were the appropriate charges to be laid in the circumstances. Because the seized merchandise contained both copyrights and trademarks, the Provincial Crown to whom the matter was referred advised that the *Copyright Act* contained criminal provisions, and therefore the enforcement of that act fell upon federal, rather than provincial, authorities. Accordingly, the Crown declined to proceed with fraud charges, and the provincial police returned the counterfeit merchandise to the defendant. Before the rights holder could make the appropriate application to Court, the merchandise was returned by the provincial police to the defendant. The merchandise returned by the police was disposed of under - in the words of the judge - "extremely suspicious circumstances." (See *Microsoft Corporation v. 9038 - 3746 Québec Inc.*, 2006 FC 1509 (FCTD) @paragraphs 52-53 and 4)).

Amending the *Trade-marks Act* in the manner suggested would provide a stronger basis for the RCMP and federal prosecutors to handle counterfeiting cases.

### **Copyright**

In its 2006 submissions, the IACC reported that there remain significant obstacles for rights owners to pursue criminal investigations and prosecutions against copyright infringers in Canada. In addition to Customs issues (which also support a recordal system for copyrights, under current guidelines), the RCMP generally limits their actions to cases involving larger-scale commercial enterprises. Presently, copyright infringement at the retail level is not considered a priority, thereby leaving an obvious gap in the enforcement net.

### **Customs**

Both as a matter of law and policy, Canada continues to embrace a reactive approach to the involvement of Canadian Border Services Agencies ("CBSA" or

“Customs”) in the monitoring and seizure of counterfeit goods at the border. As previously reported, under existing Canadian legislation, Customs is only explicitly authorized to take action after the rights holder obtains a Court order and provides detailed information regarding an anticipated shipment of counterfeit goods. This system is clearly onerous and burdensome to IPR holders, and the lack of clear legislation permitting Customs to engage in *ex officio* monitoring and enforcement is a critical obstacle to effective enforcement in the country. As well, Customs officers are expressly precluded from "targeting" shipments.

IACC members have reported that in circumstances where a rights holder obtains information as to the country of origin of a shipment, general information as to the quantity of the counterfeit goods being imported, as well as the approximate date of arrival in Canada, such information is insufficient to enable a rights holder to obtain a court order, and, because Customs cannot “target” this shipment, Customs cannot take any action to intercept, inspect or detain the shipment of counterfeit goods. Both a recordal system and the ability to take *ex officio* action could fill this gap; however, Canada still lacks a system allowing for the recordal of trademarks and copyrights with Customs.

Where shipments of counterfeit goods have been seized, IACC members have witnessed cases in which the offending items have been released by the CBSA due to a claimed lack of resources. In such cases, because of stated privacy issues, the authorities have generally refused to provide rights holders with the information needed to conduct follow-up investigations and to otherwise pursue civil remedies.

Also, as detailed below, Customs has been less than receptive to increased training of Customs personnel to assist in identification of counterfeit merchandise.

Canada's customs enforcement regime remains out of step with practice in the European Union, the United States and other countries -- including many developing countries, as Canadian legislation and practices continue to fail to recognize the critical importance of border enforcement.

As previously reported, Canada’s existing border regime is at variance with the Model Legislation currently being developed by the World Customs Organization (“WCO”), an organization to which Canada belongs. Article 9.01 of the WCO’s draft Model Legislation states:

Customs’ powers to act *ex officio* are a key feature of effective border enforcement regime. **In the vast majority of cases Customs officers are the only ones to know when and which allegedly infringing goods are transported. Therefore, unless customs are empowered and obliged to act on their own to stop suspected shipments at the borders, the border measures will remain ineffective.** TRIPS Agreement Article 58 introduces the possibility to give Customs an *ex officio* powers, as such powers are an essential feature of effective border measures it is

recommended that WCO Members States include a provision to that effect in the national laws. (Emphasis added.)

The lack of priority given to IP protection by Canadian Customs is evidenced by the lack of policy pronouncements on the issue. Indeed, review of the CBSA's public website indicates a failure to mention trademark or copyright enforcement in the list of current "enforcement initiatives". The failure of the Canadian government and its border services agency to place counterfeit products on the national "radar" is further evidenced by a January 12, 2007 news release trumpeting the government's investment of over \$430 million for smart secure borders. The press release is silent on the issue of counterfeit products. The press release also refers to the fact that, of this money, \$11.6 million is being invested in the "partners in protection" program. The program is described as "enlisting the cooperation of private industry in efforts to enhance border security, combat organized crime and terrorism, and help detect and prevent contraband smuggling" -- noteworthy for its omission of any reference to counterfeit merchandise. Similarly, the description of partners in protection on the CBSA's website again omits any reference to counterfeit merchandise.

As in the past, a review of the CBSA's website's index fails to show any reference to either intellectual properties or copyrights or trademarks. In fact, a search of the CBSA website database under the term "intellectual property" located a bulletin respecting copyright and trademarks and Customs; however, the publication referenced was issued in 2000 and last modified in August 2005. The referenced publication continues to refer to the reactive approach to Custom's addressing the importation of counterfeit merchandise, which has been reported previously as being ineffective.

### **Industry Cooperation**

IACC's members have attempted to stimulate greater government initiatives and cooperation with Canadian Customs through an affiliated coalition of member companies organized under the umbrella of the CACN. CACN members have organized training seminars throughout Canada over the last year, mainly to assist local law enforcement personnel in product identification. Regrettably, participation by Canadian Customs at these seminars has been disappointing. In addition, while stakeholders have sought to draw attention to counterfeiting issues via seminars, Customs representatives have generally declined the opportunity to participate. Likewise, with rare exceptions, industry requests to conduct training for local Customs authorities at various ports generally have been declined.

For example, in May 2006, the IACC held its semi-annual conference in Toronto, Ontario. In conjunction with the Toronto meeting, IACC members sought to initiate training of Customs officers on how to identify counterfeit product. The IACC's members who were in attendance offered to attend at various ports, including those ports bordering the Ontario/New York border or any other location in the Toronto, Hamilton or London areas. After considerable delay, CBSA declined IACC members' offer to conduct such on-site training, stating that "it wished to study the issue and discuss a

comprehensive training policy and program." Nothing further has been heard by these IACC members on the issue subsequent to May 2006.

As recently as the 11th Annual Kestenberg Siegal Lipkus LLP Conference on Anti-counterfeiting held in Toronto in December 2006, members of CBSA were invited to speak on a variety of issues respecting IP enforcement at the border such as case studies, best practices and techniques and/or a successful Customs interdiction respecting counterfeit merchandise. Although Customs officers were in attendance at the conference, none were authorized to speak.

### **Resources and Coordination**

There is a clear lack of adequate resources and training dedicated not only by Customs but within the federal RCMP (the Royal Canadian Mounted Police) and provincial police units responsible for IP enforcement. Police resources in and near key points of entry to Canada remained particularly understaffed.

In earlier submissions, the IACC reported on Canada's joint forces operations between Customs and the RCMP at border points located in Vancouver and Toronto and Montréal. It was reported that the joint force operations were intended to intensify cooperation and coordination among Customs' and law enforcement's handling of counterfeiting and piracy cases.

IACC members report that after a promising start, the joint force operations have bogged down due to inadequate resource and prioritization. Unlike both the US Customs' and European Union Customs' published reports and pronouncements indicating an increased number of seizures of counterfeit merchandise, IACC members report that Canada cannot provide similar evidence. In fact, the CBSA's public website does not report statistics respecting seizure of counterfeit merchandise as other customs authorities do.

Beyond the borders, law enforcement's resource issues and priorities continue to hamper efforts at combating the spread of a counterfeit merchandise in Canada.

For example, IACC members report that:

1. In October/November 2006 a major importer and distributor of products to convenience/variety/dollar and other stores was found to have large quantities of counterfeit electrical products. Despite the fact that a number of these products could seriously compromise the safety and security of Canadians, the RCMP originally declined the case and it was then brought to the attention of York Regional Police. The Chief of Police referred the matter to his staff who advised that they would not deal with any IP matters as a matter of policy and that those matters should be referred to the RCMP. They stated that in the event a particular person could be

charged with a particular crime then they would consider the matter on an individual basis, since the case in question presented no evidence initially that could be said to implicate one or more individuals as distinct from a company, they declined to act. In a lengthy, cumbersome and costly procedure, the rights holder was forced to proceed in civil court. Unfortunately, during this time lag, it is unknown how many potentially dangerous electrical products were sold to the Canadian public.

2. The largest detachment/federal enforcement section of the RMCP in Canada dealing with IP is the GTA Federal Enforcement Section. The Toronto West Section in particular has, in the past, been active in dealing with anti-counterfeiting matters; however, there have been recent budget cut backs which have reduced the number of officers available for IP crime.
3. In the majority of instances involving Customs seizures Federal Crown prosecutors who have the jurisdiction to prosecute Copyright offenses are more receptive to proceeding with cases as compared with Provincial Crown prosecutors who have jurisdiction respecting trademark offenses under the Criminal Code . Therefore, if the merchandise seized only involves trademarks, prosecutions are less likely.
4. The RCMP mandate relates to terrorism and organized crime issues. In addition, products that present health and safety issues are also a priority. Absent health and safety issues or apparent organized crime or terrorism, there are very few IP cases that the RCMP can or is willing to take on. IACC members report that this prioritization has resulted in a large number of cases involving substantial quantities of counterfeit product coming into Canada without detention or prosecution. This merchandise then finds its way into the marketplace. Since only Customs and the RCMP are aware of the shipments, industry remains unaware; therefore it cannot take any independent steps to seek to prevent these counterfeit goods from entering the Canadian stream of commerce.

## **Conclusion**

Last year, the IACC reported that problems with counterfeiting in Canada needed to be much higher on the overall political agenda. The IACC expressed the hope that continued attention to the problem by the US government would help stimulate further attention to the issue by government and legislative leaders in the country. Although last year, the USTR placed Canada on its Special 301 Watch List, with an out of cycle review, there has been no substantive movement in response. IACC's professed "hope" for reform, echoed by the discussion of Canada in the USTR's 2006 Special 301 Report, remains unfulfilled.

Therefore, IACC continues to recommend the following steps by the Government of Canada:

- Make IP enforcement a political priority and devote significantly greater resources to Customs, police and prosecutors, particularly at key points of entry such as Vancouver, Toronto, Montréal and Halifax;
- Take other meaningful steps necessary to facilitate the imposition of significantly greater judicial and administrative penalties against counterfeiters and copyright pirates;
- Strengthen existing legislation to deal with counterfeiting in greater detail, including through revision of the *Trade-marks Act* to provide for criminal penalties and thereby close existing loopholes in the law;
- Revise Customs rules and the *Trade-marks Act* to facilitate *ex officio* seizures by Customs against infringing product intended for the Canadian market as well as transshipments, and the destruction of seized items;
- Issue laws and regulations needed to create proper recording system for IP rights by Canadian Customs;
- Amend the Canadian Customs and trademark legislation, as needed, to otherwise bring Canadian law up to international standards and in particular, to eliminate unreasonable obstacles to the confiscation and destruction of infringing goods and early disclosure of information needed by IP owners, to facilitate private investigations and civil actions against importers and overseas suppliers; and
- Strengthen government leadership and coordination among the various law enforcement authorities responsible for anti-counterfeiting and anti-piracy.

## COSTA RICA

### **Recommendation: Priority Watch List**

#### **Introduction**

IACC members report seriously increasing counterfeiting activity in Costa Rica with more counterfeits being exported to surrounding markets. The heightened levels of counterfeiting are partly the result of government policy against the use of criminal enforcement against counterfeiters, as well as, the continuing lack of resources and training for police, prosecutors, and Customs officials. These factors clearly show that the Costa Rican government is refusing to take counterfeiting and copyright piracy seriously.

The IACC therefore recommends Costa Rica be placed on the Priority Watch List.

#### **Trademark**

##### *Criminal Enforcement*

Costa Rica's IP enforcement legislation<sup>56</sup> generally conforms to the requirements of the TRIPS Agreement and the CAFTA-DR Trade Agreement<sup>57</sup>. However, the current Attorney General's ("Fiscal General") policies clearly indicate a lack of interest in the use of criminal investigations and prosecutions in dealing with anti-counterfeiting. As a result, IACC members report an almost nonexistent criminal enforcement system. This constitutes an obvious violation of Article 61 of the TRIPS Agreement, which requires the Costa Rican government to provide effective and deterrent enforcement and criminal enforcement against violations occurring on a commercial scale.

In early 2004, the head of the General Prosecutor Office ("GPO") adopted an unwritten policy of not prosecuting IP crimes unless they have a direct effect on public health or safety. In adopting this policy, the GPO relied on Article 22(a) of the Costa Rican Code of Criminal Procedures, which gives prosecutors the option of foregoing criminal prosecutions where the facts or their legal effects are deemed to be so insignificant such that prosecutions are not justified. On the basis of this "insignificance principle" policy, prosecutors are permitted to dismiss complaints without investigation. As IP offenses have been deemed "insignificant", IACC members have not been able to successfully pursue criminal enforcement in Costa Rica for the last two years.

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<sup>56</sup> The current IP regime in Costa Rica was approved in 1999 and entered into effect in 2000. See Ley de Procedimiento de Observacion de los Derechos de Propiedad Intelectual 8039 (Observance Procedures for Intellectual Property Law – 8039), published October 27, 2000.

<sup>57</sup> Formally known as the "Central America Dominican Republic Trade Agreement" or "CAFTA-DR".

Additionally, IPR holders have encountered several operational problems with investigations. Investigations have been abandoned because of the prosecutor's requirement that police verify the investigation report. There have also been instances of the prosecutor himself calling counterfeiters to discuss the complaint filed against them. Predictably, the counterfeiter proceeded to dispose of evidence.

Prosecutors have justified the current policy in relation to IP crimes based on various arguments, including the following:

- That the main objective of IP owners is to seek economic compensation, which can be obtained through civil and administrative remedies, thereby rendering criminal prosecution unnecessary and undesirable. *This argument obviously ignores Costa Rica's obligations under Article 61 of TRIPS, and the underlying policy purposes thereof, i.e., the recognition that criminal investigations are very often the only way to effectively uncover the facts and that the economic penalties alone do not normally have a sufficient deterrent impact;*
- Criminal penalties must be proportional to the harm caused, and due to the economic nature of IP crimes, prison sentences are disproportionate. *This argument again fails to recognize the irreplaceable deterrent impact of criminal sanctions, created in part by the stigma of criminal convictions and the heightened risks to violators who engage in recidivism. It also ignores the fact that courts have the power to impose fines and suspended sentences in less serious cases;*
- The victim's economic interests are not truly harmed by counterfeiting, since counterfeiters sell to different consumers than do the makers of the legitimate product. *This is not always true, and in any case, it ignores the other harm created by counterfeits to both IP owners and the public interest;*
- The Costa Rican criminal system has limited economic and human resources, and the Prosecutor's Office must only prosecute serious crimes that affect the public at large. *Clearly, counterfeiting poses serious challenges to the public interest, including through tax losses, unfair competition with smaller companies, fuelling of the "underground economy", etc; and*
- That IP owners have the economic resources to conduct private prosecutions ("querella"), and public funds should not be used to prosecute claims on their behalf. *As seen in other countries, government involvement in the investigation phase is essential, since IP owners lack the means to obtain the required evidence in more complicated cases and where infringers take extraordinary means to avoid detection.*

The Costa Rican government's decision to regard IP offenses as "insignificant" has a direct impact on the markets of IACC members and has harmed the foreign investment environment in the country. In fact, at least one clothing manufacturer has already moved production facilities out of the country as a result of these problems.<sup>58</sup>

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<sup>58</sup> Another apparel company that has been the victim of widespread counterfeiting is considering terminating its long-standing sponsorship of a major tourist event in Costa Rica due in part to the government's failure to adequately enforce IP rights.

The IACC has been particularly discouraged by the Attorney General's 2004 decision to disband the Direccion de Investigaciones Especiales del Ministerio de Seguridad Publica (aka, the Directorate of Special Investigations of the Ministry of Public Security).<sup>59</sup> This body had effectively partnered the police in investigations into IP crimes. However, by order of the Attorney General, all investigative work handled by this authority was transferred to the Office of Judicial Investigations ("OIJ"), the performance of which has been less impressive.

The OIJ does not have a specialized IP investigations unit, and IACC members report a continuing lack of cooperation which has, in specific cases, resulted in the loss of evidence and suspected leaks of information on pending investigation which has allowed counterfeiters to relocate their production and storage facilities.

### Administrative Enforcement

In the past, IACC members had positive experiences with the Direccion General del Registro Publico (the "DGRP" or General Directorate of the Public Registry). The DGRIP is the equivalent of the USPTO, but also has the power to deal with counterfeiters through its administrative enforcement powers.

However, recently IACC members report that the level of cooperation enjoyed has been less satisfactory. Moreover, the jurisdictional and investigative powers of the DGRP, and the administrative sanctions they are authorized to impose by law are far more limited than those of the police, prosecutors and courts in criminal actions.

The result of almost non-existent criminal enforcement and ineffective administrative enforcement has been rampant and mushrooming counterfeiting in Costa Rica.

### Customs

IACC members report positive experiences with the Direccion de Investigaciones de la Policia Fiscal de la Direccion General de Aduanas (the Office of Investigations of the Fiscal Police of the Directorate of Customs). Customs has proved supportive and willing to work closely with IP owners in monitoring and seizing infringing items passing through their jurisdiction. As with the DGRP, however, Customs is an administrative body with limited jurisdiction and investigative powers. Moreover, IACC members report that Costa Rican Customs suffer from a severe lack of resources needed to perform their duties.

Consequently, Costa Rica is becoming a major supplier of branded components (including labels and tags) used by counterfeit producers in other countries in Central America, and indeed a "haven" for such suppliers. Many counterfeiters are flocking to

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<sup>59</sup> This entity was previously known as the Centro de Investigaciones de la Fuerza Publica ("CIFP") (Investigation Center for the Public Force).

Costa Rica from Colombia, Peru, China, Taiwan, India and other Central American countries.

### **Conclusion**

While Costa Rican law seems adequate on its face, IACC members have in practice been unable to obtain satisfactory results in their enforcement work. IACC therefore strongly recommends that the Costa Rican Government adopt the following measures:

- Retraction of the unwritten policy of the Attorney General against criminalization of IP offences and issuance of written policy papers which reaffirm the government's commitment to criminal enforcement and cooperation with IP owners in the war against counterfeiting and copyright piracy;
- Establishment of a special unit within the OIJ to deal with IP enforcement issues;
- Additional IP training for Customs, police, prosecutors and judges;
- Strengthened efforts to combat corruption and leaks of information on pending investigations and planned raid actions by government enforcers on counterfeiters; and
- Increased funding for customs inspection and enforcement work.

## CZECH REPUBLIC

### **Recommendation: Priority Watch List**

#### **Introduction**

IACC's members have become increasingly concerned over recent months by reports of numerous large and small open air markets dotting the entire border of the Czech Republic with Germany and Austria. These border areas are isolated from Prague, some 2 to 3 hours drive from the Capital.

There are over 50 such markets along the 700 kilometer border and the goods for sale are largely counterfeit and pirate. The number of stalls selling counterfeit and pirated goods ranges from as few as 20 to as many as 400. Indeed, several of these markets are quite large, comparable in size to the infamous Warsaw Stadium in its prime.

Many of the markets are also moving from being collections of shacks or tent structures into increasingly formal and well established in nature.

The sale of goods is marketed directly to Germans and Austrians who stream over the Czech border to buy cheap counterfeits and pirated wares. Pictures taken of these border crossings shown long lines of buses filled with German and Austrian tourists. The situation is somewhat reminiscent of the Tri-border area of Paraguay, Brazil and Argentina.

Almost all of the markets are managed and controlled by non-Czechs, many of whom immigrated to the Czech Republic from Germany following reunification. There are some estimates that sizable numbers of these individuals are not legal citizens or residents of the Czech Republic.

Often the lands upon which the markets are situated are owned by the local town councils or the Czech State itself. The markets are leased in some instances from the State for as much as 17,000 Euros a year. Over the years, some individuals have purchased their own stands from the State, and, in other cases, entire markets are leased by one individual who sub-leases the stands.

These markets are condoned by the local Czech authorities and seem to have been neglected by the central government in Prague. There are reports of occasions where local law enforcement agencies have been unwilling to take action or, in other cases are not equipped to handle the sheer number of pirate outlets and the scope of the infringing activity. The Czech police also do not have the right of entry into the stalls without a warrant which in past practice has been shown to be difficult to obtain.

## **Trademark**

The markets all contain vast quantities of counterfeit trademarked goods, including the goods of many of IACC member companies. Goods have been identified ranging from, among other things, spirits and tobacco to sports apparel and shoes as well as clothing and accessories. Industry representatives have conducted test purchases and the vast majority of the goods seem to have originated from China.

## **Copyright**

The markets engage in the massive sale of pirated CDs, DVDs, software and other copyrighted material. It is conservatively estimated that more than one million pirate recordings and films are on sale every day. Evidence has been recovered suggesting that one trader can expect to earn up to 1,000 Euros per day. According to IFPI, annual losses to the recording industry alone are conservatively estimated to be around 30 Million Euros.

## **National Governments**

While we have seen increased enforcement actions taken against these markets, including a sizeable raid at the beginning of December 2006, it is obvious, from the size and breadth of these markets that Czech, German and Austrian officials have failed to control this increasing level of cross border counterfeiting and piracy.

## **Conclusion**

In a recent positive development, the government of the Czech Republic has passed new legislation which seeks to regulate to some degree the markets. The market managers are obliged to ensure that they know the identity of the individual in control of each and every stall in the market. However, given the criminal networks that operate these markets, there is no doubt that market owners and stall operators are already well known to one another and part of the same organized crime syndicate. So, while, this new regulation is a positive step, much more needs to be done to confront and eradicate the piracy and counterfeiting taking place along the Czech border as set forth above.

These recommendations include:

- The Czech government should implement market licensing rules and laws that make the owners, landlords and landowners of these markets liable for the piracy and counterfeiting taking place in these markets;
- Special attention should be focused on the Asia Dragon Bazar for enforcement purposes and monitoring.

- Stall holders should be subject to an operating license, which includes the obligation to refrain from the sale of counterfeit and pirated goods and mandating the immediate withdrawal of the license for such violations;
- The Interior Ministry and other law enforcement authorities should take repeated and sustained ex officio action against the sale and distribution of counterfeit of pirated goods;
- The speed and efficiency of criminal enforcement (at the police investigation, prosecutorial and judicial levels) should be substantially improved, leading to rapid and deterrent punishment of all persons involved in the sale and distribution of counterfeit and pirated goods; and
- All relevant law enforcement authorities should receive a mandate to have the access to inspect all premises related to suspected pirate activity upon probable cause, including warehouses, storage facilities, irrespective of whether these are locked or publicly accessible.

## PARAGUAY

### **Recommendation: Priority Watch List/Section 306 Monitoring**

#### **Introduction**

The United States has monitored Paraguay under Section 306 since 1998, when the United States identified Paraguay as a Priority Foreign Country and conducted a Special 301 investigation. The United States terminated this Special 301 investigation of Paraguay later in 1998, when the two countries entered into a comprehensive Memorandum of Understanding (MOU) under which Paraguay committed itself to improve its protection and enforcement of IPRs.

Paraguay had made efforts to improve the protection of IP, particularly by increasing the number of raids and seizures of pirated and counterfeit goods. The measures adopted by the Paraguayan government in the fight against counterfeiting and piracy focus mainly on improving the work of the specialized law enforcement agencies, such as the Specialized Technical Team (Unidad Tecnica Especializada, or UTE) and border control authorities, such as the CUSTOMS Special Enforcement Technical Team (Unidad Tecnica Aduanera de Vigilancia Especial, or UTAVE). Paraguay is also considering pending legislation to amend its IP laws.

Nonetheless, these efforts have fallen short of Paraguay's obligations under the MOU on IPRs, which Paraguay and the United States are currently negotiating to extend the term of the MOU. As observed by the USTR in 2006, "Paraguay continues to have problems providing effective IPR protection due to porous borders, ineffective prosecutions for IPR infringements, and the lack of consistent deterrent sentences, including imprisonment, in court cases." Consequently, product counterfeiting remains a serious problem in Paraguay.

#### **Nature and Scope of Counterfeiting in Paraguay**

In part, because Paraguay is a land-locked country, many imported products – both genuine and counterfeit - initially enter Paraguay through free trade zones located at ports of entry in Brazil, but which are legally Paraguayan territory. From these Paraguayan free trade zones, products are transshipped to their ultimate destinations in Brazil and other countries.

In general, Paraguay is not an end-market for counterfeit products. Paraguayan imports widely exceed local demand, and most imported merchandise – principally from Asia - is not destined to satisfy the internal market's needs, but are destined to other countries in the Tri-Border region, where Paraguay shares a frontier with Brazil and Argentina. Consequently, Paraguay is a way station for counterfeit products from Asia

on their way to larger and more affluent markets in Brazil and other neighboring countries.<sup>60</sup>

But Paraguay is also a producer and exporter of counterfeit tobacco products. Counterfeit tobacco products made in Paraguay are not intended for local consumption, but for export to neighboring countries as well as countries in the Middle East and Asia.

Paraguay's dual role as way station and production center for counterfeit products is cause for concern. Paraguay may have the dubious accomplishment of creating a self-reinforcing two-way trade in counterfeit products, exporting locally made counterfeit cigarettes to Asia and importing Asian-made counterfeit electronics and other products to neighbors in South America. If so, the interests of local producers and distributors of counterfeit products could be well entrenched against anti-counterfeiting efforts.

Despite these considerable challenges, the Paraguayan government has failed to provide border enforcement and law enforcement agencies with the political and financial support required to control product counterfeiting. Moreover, Paraguay's large and pervasive information – and thus unregulated – economy is conducive to corruption among public officials and even their involvement with organized crime.

### **Border Control**

Counterfeit exporters in Paraguay are reported to use sophisticated methods to produce accurate forgeries of labels and packaging that are difficult for both consumers and law enforcement to distinguish from genuine products. Counterfeit exporters also elude border control measures by shipping dismantled goods across national frontiers, and then reassembling the component pieces in clandestine facilities.

A proposed Regulatory Decree by the Paraguayan executive branch could offer some improvement in customs recordal and transparency by public authorities. The proposed decree would establish a central trademark recordal procedure and regulate administrative procedures by which Paraguayan customs authorities would detain suspected counterfeits before allowing their importation. The U.S. Government should ask the Paraguayan government for an opportunity to review and comment on the proposed Regulatory Decree.

But it is evident that the improvements that would be provided by the Regulatory Decree are not enough to provide adequate protection and effective protection for U.S. trademark owners in Paraguay. Transshipping through Paraguay and its free trade zones provides product counterfeiters with many opportunities to escape detection by border control measures. As the U.S. Trade Representative observed in its 2006 Special 301 Report:

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<sup>60</sup> Please see our report on Brazil for more information on the presence of imported counterfeit products in Brazil.

Transshipped and in transit goods pose a high risk for counterfeiting and piracy because customs procedures may be used to disguise the true country of origin of the goods or to enter goods into customs territories where border enforcement for transshipped or in transit goods is known to be weak.

Even though the Tri-Border region of Paraguay, Brazil, and Argentina is a constant concern for regional security, Paraguay and its neighbors have been unable to control abuses of transshipment or to stem the trade cross-border movement of counterfeit products. In particular, Paraguay still lacks an efficient surveillance and control system that would enable improvement in the fight against counterfeiting and piracy.

Because counterfeit exports from, and transshipping via, Paraguay introduce counterfeit products into Brazil and other countries, Paraguay should also conduct initiatives to cooperate with customs authorities in neighboring Brazil and Argentina.

But Paraguay can make other reforms on its own initiative. Because transshipping via Paraguay is a significant avenue for product counterfeiting in the Tri-Border region, the U.S. Government should insist that the Paraguayan government take steps to address transshipping of counterfeit products through Paraguay and its free trade zones. These should include controls on counterfeit exports, stricter regulation of import licenses, and requiring customs declarations to identify trademarks on shipped products. Paraguay should also make general reforms of its border control measures, and provide more resources to this understaffed and financed agency.

The U.S. Government should also insist that Paraguay provide greater authority and more resources to its border enforcement agencies. Both steps should be part of negotiations to extend the IPRs MOU between Paraguay and the United States.

### **Criminal Enforcement**

Paraguay also needs to make significant improvements in criminal law enforcement against product counterfeiting. Despite some favorable results and the key role of the public prosecutor in Paraguay – in particular special trademark prosecutors – much more needs to be done.

With respect to legal reform, the Paraguayan Congress has promoted a study of the Penal Trademark Law, which main goal is to replace current weaknesses in the current Penal Code in regards to infringements against IPRs. This study should be conducted promptly, and laws and regulations found to be necessary should also be promptly enacted. The U.S. Government should ask the Paraguayan government for an opportunity to review and comment on the study of the penal trademark law and its conclusions.

Paraguay should also require the National Police and the Prosecutor Office to conduct more thorough and serious investigations. This will help to determine the real focus of counterfeiting and avoid pursuing mere piracy intermediaries.

### **Education**

The Paraguayan government currently conducts public education campaigns to prevent counterfeiting, along with money laundering and related crimes. These campaigns should be made on a continuing basis. There remains an ongoing need for technical assistance to train police, prosecutors, and judges, as well as customs officials.

### **Conclusion**

The current Paraguayan government has taken important steps to fight product counterfeiting, but much more remains to be done to address the export and transshipment of counterfeits. Ongoing negotiations to extend the MOU with Paraguay provide an opportunity for the U.S. to require Paraguay to take the following steps:

- Make general reforms of its border control measures, including stricter regulation of import licenses, and requiring customs declarations to identify trademarks on shipped products;
- Establish a central trademark recordal procedure and administrative procedures by which Paraguayan customs authorities would detain suspected counterfeits before allowing their importation;
- Take steps to address transshipping of counterfeit products through Paraguay and its free trade zones, including controls on suspected counterfeit exports;
- Promptly study and promulgate measures to correct current weaknesses in the current Penal Code in regards to trademark infringement and product counterfeiting;
- Require the National Police and the Prosecutor Office to conduct more thorough and serious investigations of trademark counterfeiting;
- Cooperate with customs and law enforcement authorities in neighboring countries of the Tri-Border region, in particular Brazil and Argentina; and
- Provide more resources to border control and law enforcement authorities.

## RUSSIA

### **Recommendation: Priority Watch List**

#### **Introduction**

For each of the past seven years, the IACC has recommended Russia's inclusion on the Priority Watch List of the USTR's annual Special 301 Report. Despite some progress that has been made during the course of the last decade through legislative reform, IACC members have consistently reported a lack of effective enforcement, both internally and at the country's borders. The most recent information provided by IACC members during the preparation of this report confirms that the lack of enforcement remained a critical concern throughout the past year.

In last year's submission, it was noted that the Russian government had shown indications of a new commitment to addressing the considerable problems it faced in the areas of product counterfeiting and copyright piracy, in giving IPR protection higher priority, and in enacting necessary legislative reforms. Throughout the course of the past year, these facts have been borne out to some degree, most notably during the course of bilateral negotiations with the United States government, in which the Russian trade negotiators acknowledged the need for improvements in a number of specific areas.<sup>61</sup> The introduction of Part IV of the Russian Civil Code, has caused significant concern among IACC members, and in the opinion of several members, has drawn much-needed attention away from the lack of enforcement.

While the Russian government is seen by many as "saying the right things" with regard to needed action on IPR issues, the IACC recommends maintaining Russia on the Priority Watch List until the Russian government demonstrates action in line with its positive rhetoric. Trademark counterfeiting and copyright piracy remain at unacceptably high levels, in a wide variety of product sectors. Though IACC members support the increasing engagement of the Russian government there is still a great deal of work to be done, and a decision to lower Russia to the Watch List could be interpreted wrongly as an indication that the protection and enforcement of IPR in Russia has improved significantly and is no longer a major concern of US industry.

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<sup>61</sup> See U.S. – Russia Bilateral Market Access Agreement – Side Letter on IPR; available at: [http://www.ustr.gov/assets/World\\_Regions/Europe\\_Middle\\_East/Russia\\_the\\_NIS/asset\\_upload\\_file148\\_10011.pdf](http://www.ustr.gov/assets/World_Regions/Europe_Middle_East/Russia_the_NIS/asset_upload_file148_10011.pdf)

## **Trademark**

Trademark counterfeiting has remained a problem during the past year for IACC members from nearly every product sector – most notably the food and beverage, apparel, tobacco, pharmaceuticals, automotive, consumer goods, and information technology. In a survey conducted in early 2006, nearly half of the respondents stated that the counterfeit goods they encountered were manufactured primarily within Russia, with the balance originating in China and former Soviet republics.<sup>62</sup> The implication of such findings is itself troubling to IACC members, in that it is indicative that both domestic manufacturing and border control remain problematic.

Concerns related to the enforcement of IPR have been exacerbated by the current legislative climate in Russia. In last year's submission, the IACC noted that despite considerable progress in developing its legislative regime, recent amendments to the Russian criminal code appeared to represent significant steps backward.<sup>63</sup> These included ambiguous and relatively high thresholds which were seen as hampering enforcement and prosecution of counterfeiting offenses. The regression of the Russian legislative regime was seen as continuing in 2006 with the introduction, and subsequent passage, of Part IV of the Civil Code in the Duma. While many in the Russian government have touted the new Part IV as a significant improvement over the current law<sup>64</sup>, brand owners in the United States<sup>65</sup>, Russia<sup>66</sup>, and elsewhere have been largely critical of its adoption. This criticism has focused on the substantive provisions that have been adopted, and the manner in which the legislation was put forth, as well as the potential consequences that such sweeping changes could have on the enforcement environment within Russia.

Substantive review of Part IV by Russian legal experts has found numerous ways in which the legislation strays from international norms on IPR and fails to comply with the requirements set forth in TRIPS. Among the problems with the trademark provisions of the new civil code are:

- The lack of a uniform likelihood of confusion standard consistent with international norms;
- The granting of IPRs in domain names;

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<sup>62</sup> See Coalition For Intellectual Property Rights press release dated May 24, 2006. Available at: [http://www.cipr.org/activities/findings/eng/pressrelease\\_052406.htm](http://www.cipr.org/activities/findings/eng/pressrelease_052406.htm)

<sup>63</sup> See IACC's 2006 Special 301 Recommendations. Available at: [http://www.iacc.org/resources/2006\\_USTR\\_Special\\_301.pdf](http://www.iacc.org/resources/2006_USTR_Special_301.pdf)

<sup>64</sup> See, e.g., statements of First Deputy Prime Minister Dmitry Medvedev, quoted in "Piracy Bill Clears Hurdle in Duma", Moscow Times, September 21, 2006.

<sup>65</sup> See, e.g., US Industry Joint Letter to Ambassador Robert Portman, dated April 11, 2006, re: Part IV, signed by fifteen industry associations.

<sup>66</sup> See Position Statement of RusBrand, re: Part Four of the Civil Code of the R.F., dated March 2006.

- Failure to prohibit registration of marks that violate well-known marks;
- Failure to provide for publication of applications prior to registration; and
- A lack of pre-registration opposition procedures.

These changes, in addition to numerous other sweeping amendments to the current law have caused many to become concerned about the potential negative impact that the new Part IV could have on enforcement actions in Russia. The new provisions will likely require significant additional regulatory action and judicial interpretation to determine the full effect of the amendments on the legislative landscape. This will, in turn, likely undo years' worth of law enforcement training that members have undertaken since the opening of Russian markets in the early 1990s.

Equally troubling to IACC members though has been the lack of input sought or accepted by the Russian government from either domestic or foreign rights holders, and the minimal debate and discussion of the new code, as well as the apparent disinterest on the part of the Putin administration in hearing any critical review of its proposed amendments. Prior to the introduction of the civil code reform in the Duma, representatives of US industry, including the IACC, raised their reservations to the administration. Russian officials' responses tended to downplay the draft version of Part IV as little more than an academic exercise, asserted that it had not originated with the administration, and further stated that US industry's concerns were unfounded and based on misunderstandings of the legislation. Despite requests from US and Russian rights holders that the Russian government seek input and review from the World Intellectual Property Organization, to our knowledge, no such critique of Part IV has been requested to date. The perceived lack of transparency in the adoption of these major changes to the law has led some to question the legitimacy of the Russian government's asserted commitment to strengthening IPR protection and enforcement, and to bringing the Russian legal system into line with international norms.

IACC members have reported little or no improvement with regard to several problem areas identified in last year's report to the USTR. Among these, are continuing issues of piracy at the registry – a problem compounded by overly formalistic and narrow interpretation of Russia's current laws. As noted in the above discussion of the Part IV reforms, IACC members believe the lack of transparency, and the unavailability of access to records of pending applications or pre-registration opposition proceedings will cause the problem of piracy at the registry to become further entrenched. Additional problems related to the disposition of infringing items and instrumentalities, and to domain name piracy also continue to be of concern to IACC members.

Finally, some members have reported significant decreases in the availability of counterfeit goods within Russia's larger cities and urban areas. These decreases however have been attributed largely to an increase in large retailers with well-established supply chains which keep legitimate goods in stock, and to some degree public awareness campaigns regarding the threats inherent in purchasing counterfeit goods. Further, these members generally noted concurrent increases in the availability of counterfeit goods in more rural, outlying areas away from urban centers.

## **Copyright**

Copyright piracy continues to be a major concern for IACC members from the recording and motion picture industries, as well as producers of both entertainment and business software. The specific problems cited in the IACC's 2006 report remain major concerns, despite some reports of slight reductions in piracy rates. Following years of piracy rates upwards of 80-90%, some content producers have experimented with alternate business models – for example, providing for the earlier DVD release of motion pictures – in an effort to penetrate markets dominated by pirate product. Other entertainment software producers have sought to increase control over their products in the market and eliminate the risks of licensee misconduct by moving into the market directly, and manufacturing their own optical discs in Russia. Absent significant improvements in domestic enforcement by Russian authorities however, it is unlikely that the progress that has been realized will be sustained or expanded upon.

Perhaps the greatest focus of the copyright industries' concerns in Russia is the number of illegal optical disc manufacturing plants currently operating in the country, with an annual capacity that far outstrips the legitimate market for domestic consumption. Russia remains a source of exports of pirate products to Europe, despite repeated assurances that the Russian government has placed a greater priority on regulating and policing the operations of optical disc manufacturers. IACC members have yet to report substantial improvement in this area. In addition, despite similar assurances from the Russian government with regard to addressing online piracy, the continuing operation of the Allofmp3.com, the world's largest commercial online music piracy website, has remained a major frustration among copyright owners.<sup>67</sup>

In addition to these issues related to enforcement issues, the copyright interests within the IACC have expressed significant concerns about the copyright provisions of Part IV of the Civil Code, and will continue to seek revisions to the recently-passed legislation.

## **Customs**

Enforcement at Russia's borders remains a major concern for IACC members. As noted in our 2006 submission, Russia's Customs Code fails to provide for ex officio enforcement against counterfeit and piratical goods that are not recorded with Customs. Though Russian officials at the Federal Customs Service have claimed significant improvements in the number of seizures of infringing goods<sup>68</sup> and concomitant administrative actions<sup>69</sup>, members still report significant problems with the current border

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<sup>67</sup> As of 2/9/07, the site was still in operation.

<sup>68</sup> [http://www.amcham.ru/events/high\\_profile/speakers2006/customs\\_lozbenko](http://www.amcham.ru/events/high_profile/speakers2006/customs_lozbenko)

<sup>69</sup> [http://www.amcham.ru/doing\\_business/russian\\_customs/ip\\_customs](http://www.amcham.ru/doing_business/russian_customs/ip_customs)

control regime. The FCS also lacks the authority to destroy counterfeit goods that have been seized, which raises concerns about such goods returning to the stream of commerce – concerns that are exacerbated by reports of official corruption. Members are encouraged by the FCS’s acknowledgement of the need for improved processes for disposition, and by the proposal from FCS to amend the Customs Code to grant more expansive ex officio authority to Customs personnel.

## **Conclusion**

While the Russian government has demonstrated an increased willingness to discuss the need for reform of its IPR regime, the progress from those positive statements into practical improvements to legislation and enforcement has been slow in coming. The IACC’s members will be closely monitoring the implementation of the Part IV reforms which are set to take effect in 2008. Early discussions with government officials have been constructive, and IACC members are hopeful that the concerns that have been voiced herein, and in other forums will be considered seriously, and acted on accordingly.

The members of the IACC applaud the efforts of the USTR in negotiating the Bilateral Market Access Agreement and Side Letter on Intellectual Property Rights, as these provide a positive framework both for bringing Russia’s legislative and enforcement regimes in line with international norms, and for clearly gauging substantive action taken by the Russian government to that end. Further, the commitments made by the Russian government overlap, to a large degree, with the measures that IACC members recommend for adoption. These recommendations include:

- Improving implementation of existing IP laws through the adoption of more expansive and less formalistic interpretations of IP laws and procedures, and greater investment in the training of law enforcement officials;
- Establishing and enforcing strict regulations for the licensing and operation of optical disc plants;
- Eliminating, or alternatively, clarifying the current thresholds for criminal prosecution of counterfeiting offenses, and issuing guidelines to clarify the valuation of goods at issue in such cases;
- Enacting legislation necessary to implement the WIPO Internet Treaties
- Requesting an independent review by WIPO, of the legislative amendments to be enacted under Part IV of the Civil Code, prior to their effective date in 2008;
- Amending the Customs Code to provide ex officio protection for trademarks and copyrights that are not yet recorded with Customs authorities;
- Adopt legislation to provide for the verified destruction or disposition of infringing goods, and the instrumentalities used to produce or facilitate such offenses; and
- Adopt a new dispute resolution mechanism comparable to the UDRP for domain name disputes in the .ru zone.

## VIETNAM

### **Recommendation: Priority Watch List**

#### **Introduction**

In tandem with the country's impressive economic development, counterfeiting in Vietnam appears to be growing in scope, scale and complexity.

Fakes in Vietnam are now becoming an everyday part of life in the consumer market and industry.<sup>70</sup> The majority of counterfeits continue to be imported mainly from China. Of course, this fact is commensurate with almost every other country in the world; all of whom report that the majority of the counterfeit goods sold in their markets emanate from China. Vietnam is also an exporter of counterfeits to other countries of locally-made fakes, as well as, those originating in China<sup>71</sup>.

IACC members report continuing difficulties in obtaining effective and deterrent remedies through administrative enforcement and this is clearly contributing to the overall problem. Criminal enforcement against counterfeiters and copyright pirates has, to date, been extremely rare.

Vietnam became a member of the WTO in January 2007 and is in the process of taking a variety of steps to strengthen its IP laws and regulations to ensure compliance with the TRIPS Agreement.

Three new laws: the Law on Intellectual Property (IP Law), the Competition Law and the Commercial Law provide the backbone of Vietnam's anti-counterfeiting legislation, particularly with respect to administrative and civil enforcement. These three new laws render Vietnam's IP legislation largely compliant with TRIPS. However, these laws still lack implementing regulations, and do not address criminal enforcement of trademarks, which is governed by Vietnam's Criminal Code.

Vietnam's enforcement regime parallels that of China to a great degree, including its extreme reliance on administrative enforcement tools. And, as in China, IACC members are deeply concerned by provisions in the Vietnamese Criminal Code which

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<sup>70</sup> The prevalence of counterfeits in Vietnam was actually acknowledged recently by the Director of the Market Management Bureau ("MMB") Mr. Nguyen Duc Thinh, who was quoted on the MMB's official website as stating that counterfeits can now be easily found in Vietnam in almost all public areas including markets, shops, trade centers, offices and houses. See official website of the MMB at <http://www.l.mot.gov.vn/qltt/index.asp?id=131> (in Vietnamese).

<sup>71</sup> Vietnamese officials have privately estimated that as much as 80 percent of counterfeits circulating in Vietnam originate from China. Most goods are smuggled across the relatively porous border shared by the two countries.

creates unacceptable obstacles to the criminalization of counterfeiting and copyright piracy.

Criminal liability against counterfeiters in Vietnam currently requires that rights holders and police produce evidence of prior sales which exceed specified numerical thresholds, failing which a violation would be deemed a mere administrative offence. These thresholds discourage Vietnamese police from commencing investigations into potential criminal cases.

Vietnam's judiciary and police are now reported to be drafting a joint Circular as a temporary measure to render the Criminal Code in compliance with the TRIPS Agreement, and to reduce relevant thresholds to the point where they meet the "commercial scale" standard required under Art. 61 of the TRIPS Agreement. The IACC is hopeful that this task will be completed swiftly, that Vietnamese police and prosecutors will make themselves more available for criminal enforcement actions, and that Vietnam will follow through on plans to modernize its Criminal Code provisions on IP protection by 2008. IACC members look forward to working together with relevant parties in Vietnam to assist in the process of modernizing the IP provisions of the country's Criminal Code, currently scheduled for amendment in 2008.

Copyright piracy is also at extreme levels in Vietnam, with unlicensed software used by most businesses and even government offices. There is clearly a lack of public awareness about the need for copyright protection in the country, and a long way to go in developing a credible deterrence through enforcement. However, progress was reported with respect to software piracy during 2006. On April 2006, the Ministry of Finance of Vietnam and Microsoft signed an agreement providing for the sale of 15,000 licenses for Microsoft products. The Ministry of Finance is reportedly the first Government bureau to use software with full copyright compliance in its IT system.<sup>72</sup>

### **Counterfeiting Situation**

Neither industry nor the Vietnamese government has published reliable and official statistics which accurately measure the scale of counterfeiting in the country.<sup>73</sup> However, there are clear indications the problem is serious, and getting worse. The Market Management Bureau (MMB) reported last year that the number of administrative cases involving fakes increased 300% from 1998 to 2004, from 2000 to 5977<sup>74</sup>. Meanwhile, complaints filed with the National Office of Intellectual Property (NOIP)

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<sup>72</sup> See: Tien Phong online newspapers at <http://www.tienphongonline.com.vn/Tianyong/Index.aspx?ArticleID=44807&ChannelID=3> (Vietnamese)

<sup>73</sup> Partial data gathered by government departments is sometimes revealed in speeches of government officials, but these are normally limited to particular sectors, and the original reports have not been made available to industry.

<sup>74</sup> See <http://www1.mot.gov.vn/qltt/index.asp?id=45> (Vietnamese).

seeking verification of infringements rose nearly 70% from 2003 to 2005, from 354 to 596<sup>75</sup>.

National police recently reported that between 2001 and 2006, local police had investigated 1260 cases involving counterfeits and other fake products<sup>76</sup>. As in China, most of these cases likely involved products that posed a risk to human health. But as a practical matter, IACC members are routinely advised by local counsel that criminal enforcement simply is not a practical option.

Counterfeiting appears to be most serious in the main cities of Vietnam—Hanoi and Ho Chi Minh City.<sup>77</sup>

Trademark infringements which do not qualify as “counterfeiting” are also becoming increasingly common in Vietnam, and are resulting in serious consumer confusion. Such infringements also increasingly involve the registration of highly similar marks with the NOIP which manages Vietnam’s trademark registration.

Fortunately, the Drug Administration Bureau of Vietnam (DAB) requires pharmaceutical manufacturers to conduct availability searches for trademarks before registering products with their department. But, this has still not been entirely successful in preventing infringement and consumer confusion.

### **Progress Made Against Anti-Counterfeiting**

As indicated above, a new IP Law was enacted in 2006, and once implementing rules are issued, the new IP Law is expected to increase the effectiveness of anti-counterfeiting action and eliminate confusion as to which government departments are responsible for the enforcement of particular rights.<sup>78</sup>

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<sup>75</sup> See

[https://203.162.163.40/noip/resource.nsf/vwResourceList/0459E247C1628CAE4725713A003F5366/\\$FILE/report2005m.htm](https://203.162.163.40/noip/resource.nsf/vwResourceList/0459E247C1628CAE4725713A003F5366/$FILE/report2005m.htm) (Vietnamese). The statistics of the MMB and the NOIP overlap to a great degree, as enterprises will often submit the same cases first to the NOIP for verification, after which the complaint will be forwarded to the MMB for enforcement action.

<sup>76</sup> The General Department of Police under the Ministry of Police recently disclosed that local police had investigated 1260 cases between 2001 and 2006. See Vietnam Investment Review online at <http://www.vir.com.vn/Client/Dautu/dautu.asp?CatID=56&DocID=12117> (Vietnamese).

<sup>77</sup> The total population of Vietnam is 83.1 million, and the population of Hanoi in 2005 was 3.1 million, and that of Ho Chi Minh City 5.9.

<sup>78</sup> The IP Law and other new legislation set out in greater detail the responsibilities of various government organs. These include the Inspectorate under the Ministry of Science and Technology, the MMB, Customs, the Economic Police and the courts. The Inspectorate under the Ministry of Science is responsible for all administrative anti-counterfeiting activities, the MMB is responsible for domestic trade, the Economic Police is responsible for counterfeiting crimes, Customs is responsible for Import-Export anti-counterfeiting activities and the courts are responsible for judicial activities. According to The New Major Laws, independent IP assessment organizations and individuals will be, for the first time, established to take charge in verifying whether an activity constitutes infringement, as well as evaluating damages, if any.

In 2001, the government established a steering committee to deal exclusively with counterfeiting issues (Steering Committee No. 127). This committee, led by the Ministry of Trade, which includes representatives from both the central and provincial governments, was tasked with coordination of all government departments responsible for anti-counterfeiting work.

On January 29, 2006, key ministries issued an Action Plan<sup>79</sup> to address counterfeiting as well as other IP infringements. The Action Plan has been particularly useful in helping to clarify the functions of relevant ministries and encourage greater cooperation and coordination among them.

The government has also responded to calls from industry for stronger IP protection for investors by approving the establishment in 2006 of a new industry association: the Vietnam Anti-Counterfeiting and Intellectual Property Protection of Foreign Invested Companies (VACIP), which has been led by various IACC members. VACIP works with the Vietnam Intellectual Property Association (VIPA), whose members are mainly local IP experts. These two associations are expected to organize more seminars, conferences and research projects to raise awareness of IP and to advance IP legislation.

Notwithstanding the above laudable developments, IACC members still believe the Government of Vietnam should be encouraged to significantly increase the resources and training provided for criminal enforcement of IPR. Measures are also needed to address protectionism and corruption, which frequently interfere with administrative enforcement and severely undermine the deterrent impact of the current law.

## **Laws and Regulations**

### **Criminal Enforcement**

As a full member of the WTO, Vietnam is now required to comply fully with the TRIPS Agreement. The critical provision in the TRIPS Agreement vis-à-vis anti-counterfeiting and anti-piracy is Art. 61, which mandates access to criminal enforcement in cases of willful infringements on a “commercial scale”. Vietnam’s current Criminal Code critically fails to meet the requirements of Art. 61.

Similar to provisions in China and Russia, Arts.131 and 171 of Vietnam’s Criminal Code provide for criminal enforcement mainly where it can be shown that

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The establishment of IP assessment organizations and individuals will ease the burden of State authorities in determining infringement and thus pave the way for anti-counterfeiting activities to be settled quickly and more objectively.

<sup>79</sup> The Action Plan was jointly issued by the Ministry of Science and Technology, Ministry of Culture and Information, Ministry of Police, Ministry of Trade, Ministry of Agriculture and Rural Development and the Ministry of Finance.

infringement has already been completed and the harm caused is “serious”.<sup>80</sup> These requirements are clearly inconsistent with Art. 61 of the TRIPS Agreement, in that they impose a much higher standard of proof for criminalization. These requirements also defy common sense when applied to IPR enforcement, since in virtually all cases, an infringer will in fact have engaged in significant prior sales of infringing items for a considerable period, and almost always have exceeded relevant numerical standards for criminal liability. The requirement that IP owners and judicial authorities prove such sales creates an unacceptable burden on their respective resources, and effectively creates a loophole for infringers. Experience in China, in particular, has proved that infringers are extremely adept at exploiting these loopholes, e.g., by hiding transactional records and keeping stocks of infringing products held in any one location below the relevant numerical threshold.<sup>81</sup>

The IACC consequently takes the view (consistent with its positions regarding China and Russia) that Vietnam should amend its Criminal Code as soon as possible, and adopt provisions in the law that are compatible not only with WTO standards, but which are consistent with international practice.

The IACC hopes that the Vietnamese legislature will eventually adopt amendments to the Criminal Code that will effectively provide for concurrent jurisdiction of administrative and criminal enforcement authorities over most cases.

Art. 61 of the TRIPS Agreement was clearly intended to ensure that governments retain maximum flexibility in dealing both with small-scale infringers and more clever counterfeiters that go to great lengths to appear to be operating on a small scale. Without the threat of potential criminal action, a government is deprived of a critical weapon for deterrence, and both police and IP owners are required to spend significantly greater resources to prove the full extent of prior transactions. This is a difficult task in the best of circumstances.

Under a future dual-track system, most criminal cases would be initiated upon the request of the rights holders. As in almost all countries, the police would retain the discretion to refuse to investigate or process cases based on available resources and other factors. Meanwhile, guidelines could be adopted to facilitate the transfer of cases from administrative authorities to the police for criminal investigation based on considerations of the public interest.

IP owners and police will of course, have sufficient incentive in many cases to fully investigate the scope of infringements. Nevertheless, giving police and prosecutors the power to pursue criminal cases against small-scale infringers provides a powerful

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<sup>80</sup> Another type of infringement which may be subject to criminal enforcement is “repeated act of infringement”.

<sup>81</sup> For further examination of the issues raised by threshold requirements, see the China chapters of the IACC’s 2005 and 2006 301 reports.

investigation tool. It also sends the right message to the market regarding the morality of counterfeiting and piracy.

We understand that the Supreme Court, together with national prosecutors and police, are about to issue a Circular to temporarily ensure that the Vietnam Criminal Code complies with the TRIPS Agreement. The IACC urges Vietnamese authorities to ensure that the Circular substantially relaxes requirements of proving harm and eliminates any thresholds for criminalization of smaller-scale cases. If this proves impossible for technical reasons, the IACC hopes that the Vietnamese legislature will be willing to intervene as quickly as possible to amend the Criminal Code.

It is further hoped that the proposed Circular and any future revisions to the Criminal Code will make clear that criminal enforcement is required in cases involving repeat offenders, i.e., infringers who have previously been dealt with by administrative authorities, but who continue to infringe. Future laws and guidelines in this regard will need to take into consideration the need to clarify the handling of cases involving corporate infringers as opposed to individual infringers. Under current law, most administrative penalties are imposed upon corporate entities, whereas police and prosecutors normally focus their efforts to bring criminal prosecutions action against individual violators, rather than corporate entities they control or work for.

#### Administrative Enforcement

Between 2004 and 2005, three laws dealing with anti-counterfeiting were enacted: the IP Law, the Commercial Law and the Competition Law. However, these laws only came into effect last year, and therefore IACC members have limited experience enforcing rights under these laws.

Three corresponding Decrees ( Nos. 103/2006/ND-CP, 105/2006/ND-CP, and 106/2006/ND-CP) were issued in September 2006 to provide further guidance on IP registration and enforcement. This new legislation is helpful in a number of ways, particularly with respect to clarification regarding the types of evidence needed to confirm that infringement had taken place. Just as importantly, the new laws increase the maximum fines for counterfeiters and copyright pirates to five times the value of the infringing goods.

In practice, administrative authorities have not yet begun imposing fines at levels much higher than those imposed under earlier legislation, and it is hoped that the implementing rules will be issued in order to give clearer guidance to enforcers to assist them in calculating appropriate fines. It is also hoped that future guidelines will clarify that, if the evidence obtained in a given case, is inconclusive as to the infringer's prices, reference should be made instead to the retail prices of the corresponding legitimate product.

IACC members are also concerned over certain procedural requirements which have increased the cost to rights holders without apparent justification. Among these, is

the requirement that rights holders have to now notarize and legalize declarations prior to filing.

### **Copyright**

Although Vietnam is now a full member of the Berne Convention, piracy of optical disks of audio and visual works and software remains rampant in Vietnam. There is only a very low level of public understanding of IP rights resulting in many unintentional infringements.

### **Customs**

Vietnam is still clearly in the early days of providing customs enforcement for IP rights. Some IACC members have reported positive experiences in working with Vietnamese Customs, but the lack of manpower, training and detailed implementing rules have made it difficult for our members to rely on Vietnamese Customs on a more routine and reliable basis. Regulations should be drafted to cover recordal measures, temporary seizures, verification of infringements, customs bonds to be paid by rights holders (if any), the seizure and destruction of infringing goods, administrative penalties, disclosure of information to rights holders, and the transfer of appropriate cases to police and prosecutors.

The IACC urges Vietnam to draft appropriate implementing rules as soon as possible and to consult with industry during the process.

### **Conclusion**

While Vietnam's new IP legislation is laudable in many respects and the central government appears to be fully committed in principle to promoting IP protection, much remains to be done in order to effectively protect IP rights in Vietnam. The IACC therefore encourages the Vietnamese government to continue its reform efforts, in particular through the following:

- Increase public awareness about IPR and counterfeits by organizing more seminars, conferences and training courses for enforcement authorities, enterprises and students;
- Increase training and resources for government enforcement of IPR, particularly among police, prosecutors and criminal court judges;
- Issue a new circular on criminal enforcement of IPR that brings Vietnam's Criminal Code into full compliance with the TRIPS Agreement, as well as with international practice;
- Amend Vietnam's Criminal Code to ensure TRIPS compliance and to modernize the law;

- Issue new detailed implementing regulations to facilitate more effective civil and administrative enforcement, including by Vietnamese customs; and
- Take appropriate measures to facilitate the award by local civil courts of higher compensation in counterfeiting and piracy cases.

## BELIZE

### **Recommendation: Watch List**

#### **Trademark / Customs**

In its Special 301 recommendations to the USTR in 2006, the IACC reported significant and continuing problems experienced by members in multiple product sectors, most notably, the lack of effective control at the borders and in the Corozal Free Trade Zone, as well as legislative deficiencies and ineffective enforcement of IP rights, which facilitated the flow of counterfeit products into Mexico and elsewhere in the Americas. For these reasons, the IACC recommended elevating Belize to the Priority Watch List.

Regrettably, many of the same problems previously reported have continued throughout the past year. However, IACC members are pleased to report that the overall environment in Belize has improved. Government officials in Belize have generally seemed more receptive to industry's concerns, and have been more willing to participate in training events. However, members also note that Belizean law enforcement and Customs officials are reluctant to take action absent detailed and specific information regarding shipments of counterfeit goods. This perceived unwillingness or disinterest in conducting investigations or gathering intelligence independently of rights holders' complaints is viewed by many as a major obstacle to developing a more efficient and effective enforcement regime. Further, the perceived indifference has caused some rights holders to forego seeking enforcement in many cases.

The IACC first reported the use of the Corozal FTZ as a conduit for fakes in its 2004 Special 301 recommendations; an issue which remains a major source of concern to IACC members. IACC members continue to believe that additional legislation and regulations are the key to improving enforcement in relation to goods inside and traversing the free zone. Clarification with regard to law enforcement's and Customs' authority to act and jurisdiction over IPR offenses, for example, would be helpful.

In light of the limitations on financial and personnel resources available for policing Customs issues in general, and IPR issues in particular, it is essential that law enforcement act more efficiently, and provide a real deterrent to counterfeiters. To illustrate this point, one member reported success in having a large amount of seized counterfeit product destroyed during the past year. However, the seizures of that product had taken place in 2004 and 2005, and to the member's knowledge, no criminal investigation was ever initiated following the seizure. The low risk of criminal investigation or penalties in Belize provides an incentive for counterfeiters to continue utilizing the country for the shipment of their illicit goods.

The IACC recognizes, and is encouraged by, the continuing efforts of the Belize Intellectual Property Office ("BELIPO") to educate the public, the bar, the judiciary, Customs and other law enforcement authorities on the importance of IPR. Further, the

government of Belize has demonstrated its interest in working more closely with rights holders. Despite the continuing problems noted herein, and in previous years, rights holders are more optimistic about the outlook for IPR enforcement in Belize. As a result, the IACC recommends that the USTR move Belize to the Special 301 Watch List.

### **Conclusion**

The IACC recommends that Belize be placed on the Watch List, and requests that the USTR encourage the government of Belize to:

- Clarify the authority of police and Customs over seizures, criminal investigations and other enforcement work in the CFTZ and other areas under Customs control;
- Develop more close cooperation with industry through public-private partnerships to enhance training and best practices for detection and enforcement related to IPR, thereby making more efficient use of limited resources;
- Increase the number of criminal investigations and prosecutions following seizures of counterfeit and piratical goods;
- Provide for the prompt destruction of infringing goods to minimize risks related to re-entry of illicit goods into the stream of commerce;
- Continue to educate the public, the bar, the judiciary, Customs and other law enforcement authorities on IP protection, and in particular the need to work more cooperatively with industry in effecting seizures of fakes and following up thereon with criminal investigations, prosecutions and the destruction of fakes.

## MALAYSIA

### **Recommendation: Watch List**

#### **Introduction**

In 2006, the USTR kept Malaysia on the Special 301 Watch List due primarily to the government's inability to deal effectively with exports of optical discs incorporating software, films and sound recordings. Over the past year Malaysia appears to have expanded its efforts to deal with these and other IP enforcement problems. Indeed, the Malaysian Government has pledged the creation of specialized IP courts and has proposed that copyright laws be amended to prosecute building owners who allow their premises to be used for storing, selling or distributing counterfeit materials.

In 2006, the United States launched free-trade agreement (FTA) negotiations with Malaysia. Malaysia is the United States' 10th-largest trading partner with \$44 billion in two-way trade. The U.S. is Malaysia's top export market and its largest foreign investor. The FTA negotiations have already fortified the Malaysian IP legal regime; for example, the negotiations have been an impetus for Malaysia's accession to the Patent Cooperation Treaty. The Minister of International Trade and Industry, Datuk Seri Rafidah Aziz has stated that Malaysia was committed to not only having adequate legislation, but to having it properly enforced and that the emphasis was on local companies having to realize the importance and benefits of IP.

However, Malaysia is still one of the single largest sources of pirated optical discs exported worldwide, and the government's efforts to target the kingpins behind this trade still appear so far to be inadequate despite the improvements referenced above. At the same time, while the government is finally focusing more attention on the need to address systematic problems that impede anti-counterfeiting and anti-piracy work, including through increasing enforcement manpower, most of the required reforms remain in the pipeline. Furthermore, there do not yet appear to be initiatives underway to address the near total lack of IP enforcement from Malaysian Customs. The IACC therefore recommends that Malaysia remain on the Watch List.

#### **Trademark**

As reported in 2006, counterfeiting of fashion, pharmaceuticals, batteries, computer accessories, tobacco, mobile phone batteries, food, electronics, petroleum products and toys remains problematic. IACC members have observed an increasing tendency (reflecting the global trend) for pharmaceuticals and other fakes to be traded in Malaysia via the Internet. Initiatives such as the Malaysian government's 2004 effort to reduce the sale of counterfeit drugs through mandatory placement of hologram labels have not had produced the desired results.

As elsewhere, effective action against producers and vendors of counterfeits in Malaysia will require substantially increased human and material resources. The rise of the Internet as a battlefield for anti-counterfeiting and the increasing sophistication of counterfeiters require a greater investment of time to identify and prosecute the masterminds, and the seizure of fake product and the imposition of modest fines are increasingly insufficient to deter the growth of the problem.

The Ministry of Domestic Trade and Consumer Affairs (“MDTCA”), the main IP enforcement authority in Malaysia, announced in mid-2005 that it had more than doubled its manpower to 1,500 officers, and a further increase to approximately 2,000 was recently approved. However, the MDTCA has publicly acknowledged that it requires 5,000 officers to accomplish its objectives, and interim proposals of borrowing officials from Malaysian police and other government departments have been met with scepticism due to the historical lack of cooperation between these government bodies.

The MDTCA has kept an open door to industry requests for enforcement sweeps, and has been reported to conduct regular actions against high-profile targets such as the Petaling Street market. However, the failure of the courts to process cases in a more timely fashion continues to send the message to the market that the government is not serious about anti-counterfeiting. Regrettably, official corruption and infiltration of organized crime remain serious obstacles to progress. Tip-offs of major infringers prior to raids are routine. The impression given to many foreign companies is that, notwithstanding its resource limitations, the Malaysian government can address trademark counterfeiting much more effectively if it has the political will to do so.

IACC members continue to face problems in the following areas:

- Continued long delays in obtaining registration of trademarks from the trademark registry, as well as in obtaining determinations in oppositions and cancellations against pirated marks;
- Lack of cooperation by enforcement authorities and the courts in disclosing information relating to ongoing cases;
- Inadequate penalties under the Sale of Drugs Act of 1952 and the Poisons Act of 1962 for the production and sale of fake pharmaceuticals;
- Protection for pirates of well-known marks for registrations obtained by them prior to the 2001 amendment of the Malaysian Trademark Law; and
- Difficulties in verifying whether seized counterfeits have been properly destroyed in accordance with the law.

### **Copyright**

Domestic consumption of optical discs in Malaysia is reported to be around 60 million units. However, the production capacity of licensed plants is currently estimated at 2.5 billion units. The capacity of unlicensed plants remains unclear. It will therefore come as no surprise that copyright owners regard Malaysia as one of the single largest sources of pirated optical disc content products worldwide.

Complaints from foreign governments and industry have not gone totally unnoticed. The Malaysian authorities have made some headway on cracking down on media piracy this year with the launch of an enforcement campaign known as OPS TULEN 2006 (meaning Operation Genuine 2006) aimed at eradicating the use of pirated software by small and medium-sized businesses. In July 2006, 30 MDTCA officers seized 315 CD-R burners which were capable of producing over 35 million discs per year and generating revenues of USD 47 million<sup>82</sup>.

The production of pirated optical discs is increasingly taking place in smaller and more remote locations in Malaysia, and sometimes on ships anchored offshore. Limited government resources currently make the targeting of such factories more difficult, and emphasize the need for the creation of special teams of well-trained and resourced MDTCA officers to deal with more complicated cases.

IACC members also report continuing difficulties in tracing the source of illegal optical discs due to the use of fraudulent shipping documents.

In March 2006, the Recording Industry Association of Malaysia (RIM) filed a civil suit in the High Court against the landlord and owner of a shopping complex in Malaysia for allegedly renting their premises to counterfeit video compact disc traders. The outcome of this landlord liability case, which is the first of its kind in Malaysia, could have a big impact on copyright enforcement in Malaysia and is thus eagerly awaited.

While some progress has been made in fighting copyright piracy, the International Intellectual Property Alliance (IIPA), has reported that virtually all sectors of the copyright industry suffer from high levels of piracy in Malaysia with the record and motion picture and book publishing industries hovering at close to 50% piracy, business software at 60% piracy and entertainment software at 91% piracy<sup>83</sup>.

### **Customs**

The lack of effective customs enforcement against infringements is perhaps one of the most noteworthy gaps in landscape of Malaysia's IP regime. Sadly, over the course of 2006, the Malaysian government does not appear to have taken any public steps to address this problem, which was explained in detail in the IACC's Special 301 submission from February 2006.

Malaysia's customs enforcement regime has proved almost entirely unusable due to the lack of laws and regulations that would permit *ex officio* customs seizures and for the corresponding lack of effort by Customs to monitor import or export shipments for IP compliance. Malaysian Customs has so far not established a recordal system for IP

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<sup>82</sup> [www.mppa.org/press\\_releases/2006\\_07\\_10.pdf](http://www.mppa.org/press_releases/2006_07_10.pdf)

<sup>83</sup> <http://www.iipa.com/pdf/IIPA%20MalaysiaFTA%20Request%20to%20Testify%20040406.pdf>

rights, which would naturally be essential if Customs were to begin proactive monitoring of shipments.

Malaysian Customs is authorized to seize infringing shipments, provided that the IP owner provides full details of the shipment, including the name of the ship and date and time of its presence in Customs territory. Customs also requires that IP owners pay significant bonds to facilitate the seizure of products—a requirement which has routinely deterred many IP owners from taking advantage of enforcement opportunities. Indeed, the Registrar of Trade Marks has complete discretion as to the amount of security to be deposited. Additionally, if expenses incurred by the Registrar exceed the amount of security, the excess is treated as a debt to the Government.

Assuming infringing products are seized by Malaysian Customs, IP owners are then required to commence civil proceedings in local courts to maintain the seizure order and pursue other remedies. IP owners have only 30 days to obtain an interlocutory injunction from the court to prevent the release of such goods of the goods back to the importer. This is a relatively tight deadline given Malaysian litigation timeframes. Furthermore, if the infringement action is dismissed, the IP owner may be ordered by the court to pay compensation. If the seizure was initiated under the Copyright Act 1987, infringing products can be forfeited as if they are prohibited goods under the law relating to customs. But otherwise, Malaysian Customs has no powers to impose fines or commence criminal investigations.

The Malaysian Bar has submitted proposals to render customs enforcement more effective but the Malaysian Government has yet to address them. In the absence of an effective customs regime, the whole of Malaysia effectively functions as a free trade zone for counterfeits. But the country also operates formal free trade zones which IACC members report are increasingly being exploited by counterfeiters of cigarettes and consumer goods for transshipments originating in China and other countries. It remains unclear whether the Malaysian government is fully aware of these problems and whether it has any plans in the pipeline to address them.

## **Conclusion**

Though there has been of some positive change in Malaysia, the country will need to be closely monitored during 2007 to verify whether the tentative progress realized in 2006 will continue. The stakes are enormous, given the severe impact of optical disc exports from Malaysia on markets elsewhere.

The IACC also recommends Malaysia be encouraged to take the following measures in 2007 to deal with both trademark counterfeiting and optical disc piracy:

- Significantly strengthen government efforts in criminal investigations and prosecutions against the masterminds behind optical disc plants and distribution syndicates. Also, target the kingpins behind trademark counterfeiting operations

for all types of products. Respond convincingly to political and other undue influence that might impede such investigations;

- Review the sufficiency of government efforts to target counterfeiting activities over the Internet;
- Begin drafting new laws and regulations to bring the enforcement capabilities of Malaysian Customs up to international standards, and ensure that infringements are subject to criminalization in appropriate cases;
- Adopt new measures to counter the increasing use of fraudulent documentation by international traders of infringing goods;
- Ensure adequate training of IP enforcement officials, and the creation of adequately resourced teams to deal with more complex and otherwise difficult cases;
- Follow through fully with plans to establish specialized IP courts to deal with both criminal and civil disputes, and thereby effectively clear the backlog of unresolved cases; and
- Increase transparency, information exchanges, and cooperation between enforcement bodies and IP owners.

## MEXICO

### **Recommendation: Watch List**

#### **Introduction**

The Mexican Government has made some, albeit small, progress in curbing the severe level of counterfeiting and piracy. The high number of players and profits involved in these illegal activities has rendered IP enforcement in Mexico a complex problem. Nevertheless, the government has shown some political will to tackle this issue by implementing reforms that may strengthen its arsenal against counterfeiters during 2007.

#### **Trademarks**

Over the years, counterfeiting and piracy have increased and crept into many sectors of the economy including public health. IACC members seeking to enforce their rights against counterfeiters in Mexico have faced a range of difficulties including a lack of political priority and resources on the part of enforcement authorities, continued corruption, increased involvement of organized crime and more sophisticated counterfeiters.

The resolution of these complex problems faced by IP owners will require more than just the amendment of laws and regulations. However, legislative action must and has indeed, been taken by the Mexican Government. The Mexican Health Law and the Federal Code of Criminal Proceedings (FCCP) were amended with effect from May 26, 2006. Articles 464, 208 Bis and 464 Ter of the Mexican Health Law were amended and a new section XV to Article 194 of the FCCP was enacted to combat the counterfeiting of medicines.

These amendments are encouraging as they provide new remedies for attacking the problem of counterfeit medicines. Criminal actions based on this new legislation, together with trademark enforcement proceedings, will strengthen legal action available against medicine counterfeiters using labels or packaging to link the counterfeited product to a legitimate mark.

Another advance in the battle against counterfeiting took place on June 15, 2006. On that date, the General Prosecutor's Office (PGR), the Mexican Institute of Industrial Property (IMPI), amongst other Mexican Government agencies, private companies and non-governmental associations, signed the National Agreement Against Piracy. In essence, the agreement sets out:

- The Mexican Government's obligation to establish a State Policy that will include a strong focus on fighting counterfeiters and protecting IP rights;
- The participation by the three Mexican branches of powers (i.e., the Legislative, Executive and Judicial) with the private sector to form a wide and strong front against IP crimes;
- A pledge to carry out Mexico's obligations under various international treaties and instruments by reforming domestic laws and public policies; and
- A pledge for a stronger enforcement of IP rights through more efficient access to and administration of justice.

It was roundly agreed that it was necessary to review the existing laws, and, in particular, to amend several articles of the Federal Criminal Code and the Industrial Property Law to allow for the prosecution of certain copyright and industrial property crimes at the initiative of the Attorney General's office (*i.e., ex officio powers of the criminal investigation agencies*).

The agreement, which is the culmination of efforts by the Mexican Government and the private sector, constitutes the first step in strengthening existing mechanisms in the fight against industrial and IP crimes. Piracy and counterfeiting have become true high-profit industries in Mexico. These illegal activities are intimately related to organized crime, such as drug trafficking and terrorism, which affect national and international security. Thus the public and private sectors have galvanized to forge an alliance against these serious crimes.

The agreement is also an important step within the Alliance for Security and Prosperity in North America (ASPAN) whose objectives include increasing productivity between Mexico, the United States and Canada through cooperation in regulatory matters. ASPAN is to form working groups to elicit the interests of various sectors, which includes the fight against piracy, and to establish specific, measurable and attainable goals. The combined force of these three governments would better promote a respect for IP.

## **1. Legal reforms**

There are two main mechanisms for the enforcement of IP rights against counterfeiters and pirates under the Mexican legislative framework:

- i.- Administrative infringement actions before the IMPI; and
- ii.- Criminal actions before the PGR.

### **i.- Administrative infringement actions before the IMPI.**

In cases involving the use of confusingly similar or partially reproduced trademarks, IMPI can enforce IP rights by means of an administrative declaration of infringement which may be issued with sanctions including fines. The IMPI may order the cessation of infringing conduct; the seizure, withdrawal from circulation or the cessation of distribution of infringing goods, and the closure of the infringers' premises. In cases

involving the unauthorized use of identical trademarks, other more efficient remedies are available.

The Mexican Supreme Court has declared that a final declaration of infringement must be obtained from the IMPI to bring a civil action claiming statutory damages/loss of profits. Administrative procedures before IMPI are formal and have disadvantages. For example, IP owners seeking seizures, or the adoption of other provisional measures, have to post a bond. Additionally, even obvious counterfeits will not be seized during official inspections if the IP owner has not filed a complaint. Nevertheless, even though the IMPI's powers are limited, given that it is an administrative office and not a criminal prosecution agency, there has been some progress in the enforcement of IP rights.

#### ii.- Criminal actions exerted by the General Prosecutor's Office (PGR).

These actions are generally more effective and can include the prompt execution of raids by Federal Agents. Importantly, there is no requirement to post a bond. Also, when the action is based on article 223 section III of the Industrial Property Law, there is no requirement to request a technical opinion from the IMPI.

However, enforcement may be delayed or hindered by the following requirements:

- Disclosure of the identities of investigators and other witnesses;
- Proof from IP owners that the public has been informed that the goods or services are protected by industrial property rights, through use of the "registered trademark" legend, or the letters "M.R.", or the ® symbol; or the "patented" legend;
- Detailed Expert Witness Reports verifying even what are obviously counterfeit goods; and
- Filing of a complaint by the IP owner without which even obvious counterfeits will not be seized.

Currently there is draft legislation before the Mexican Congress that would address these gaps, but progress has been slow. In any event, much of the draft legislation is not viable as it is impractical in many respects. Consequently, IACC members recommend a wider and more coordinated review of the legal issues and the proposed solutions by the Mexican Congress and Government.

## **2. Enforcement**

Perhaps the greatest obstacle to enforcement in Mexico is the lack of sufficient resources of the PGR, which is the main investigative and enforcement authority. The PGR and local police, who assist in conducting raids, both clearly lack sufficient manpower to respond rapidly and effectively to complaints from IP owners. IACC members commend the IMPI for leadership and resource support in organizing raid actions, but the IMPI's efforts are further hindered by the formalities discussed above.

The IACC believes that the intervention of the Mexican President's office in promoting action plans before the Congress would be useful. The IACC also recommends addressing problems with inter-agency coordination by centralizing IP enforcement efforts through the creation of an IP czar, independent of the Attorney General, and the creation of a specialized police force tasked with handling IP crime investigations.

### **Customs**

Mexican Customs officials have insufficient authority to deal with imports of counterfeit goods, as the IACC has pointed out in previous submissions. Also, the earlier introduction of an "observer system" to facilitate inspections for copyright infringements by Customs has not been effectively expanded to assist trademark owners. The IACC again calls up on the Mexican government to consider other practical short and medium-term options for facilitating the monitoring of counterfeit imports for trademark owners.

Mexican Customs is also encouraged to work more effectively with the police and other authorities in sharing information needed to facilitate investigations of counterfeiting cases.

### **Conclusion**

While piracy and counterfeiting remain a large and complex problem in Mexico, there have been notable efforts made by the Mexican government regarding these issues, both in the enforcement of IP rights and in the amendment of laws to better deal with the issue.

Furthermore, there have been modest advances in cooperation between authorities, specifically in the collaboration between IP rights holders' and Mexican enforcement agencies like the General Customs Administration (AGA). Indeed, the latter has been passing information and implementing provisional detentions that have resulted in definitive confiscation of imported counterfeits and criminal prosecutions.

The IACC therefore recommends the following measures to encourage the Mexican Government:

- To amend the Customs Law so that there is a specific and clear procedure set out for the Mexican Customs to seize the imported counterfeits ex officio;
- To eliminate unnecessary formalities required as a pre-condition to PGR seizures of counterfeit and pirated goods; and
- To increase the promotion of educational campaigns to publicize the damage caused by counterfeiting and piracy.

Although Mexico has shown some marked improvement, there are still many areas in which Mexico has to improve in the battle against piracy and counterfeiting.

## THE PHILIPPINES

### **Recommendation: Watch List**

#### **Introduction**

In 2006, the United States Trade Representative removed the Philippines from the Priority Watch List to the Watch List mainly due to progress made in the area of copyright enforcement. In particular, the Philippines had bolstered implementation of legislation passed to stop illegal production of pirated optical discs through controlling the licensing of, and conducting raids against, pirate optical disc production facilities.

However, enforcement in the area of trademark counterfeiting appears to be mixed. Therefore notwithstanding progress in certain areas in 2006, IACC members report few improvements in the key issues of concern expressed in prior years, most notably a continuing lack of government enforcement resources, and unacceptable delays in the judicial system. Consequently, the IACC recommends that the Philippines remain on the Watch List.

#### **Trademark**

Counterfeiting of a wide range of consumer and industrial products remains serious in the Philippines. IACC members report infringements of their rights for goods ranging from pharmaceuticals, food, fashion, footwear, apparel, alcoholic beverages, cosmetics, perfume, computer equipment, auto parts and cigarettes.

In addition, IACC members report continuing problems in the use of free trade zones for the transshipment of counterfeit and smuggled products to other markets, particularly in Asia. Products typically exported from the Philippines include optical media, clothing, consumer electronics, automotive products, cosmetics and toys.

IACC members have over the years been pleased with the responsiveness of Philippine police, particularly the IPR Division of the National Bureau of Investigation, in organizing criminal raids against counterfeiters and copyright pirates. However, there are reports of occasional leaks among law enforcers prior to raids which have resulted in failed seizures. The target products are moved to different locations prior to the service of search warrants, which make the search warrants ineffective as the law enforcers may only serve the search warrants in respect of the specific areas specified therein. A further problem has been caused by the difficulty in accessing police files. There have been a number of reports of police archiving files relating to infringers that are at-large, thereby reducing the chances that infringers will be located and arrested.

The significant investment of IP owners and government authorities in arranging raids continues to be undermined by the persistent failure of the Philippine courts to process both criminal and civil cases in a timely manner. It currently takes anywhere from two to even ten years for most cases to reach a conclusion, with infringers routinely extending the duration of cases by exploiting procedural loopholes and raising appeals against minor rulings. As a consequence, an increasing number of criminal cases are being settled at an early stage, and on terms that are too favorable to infringers. In many cases, IP owners question whether prosecutors are subject to undue influence in their consideration of the merits.

In light of the inordinate delay in the prosecution of civil and criminal cases, IP right holders have increasingly resorted to administrative enforcement of IP rights violations before the Bureau of Legal Affairs of the Intellectual Property Office (“IPO”). However, the Court of Appeals ruled on 18 July 2006 that the IPO does not have jurisdiction to entertain IP rights violation cases, contrary to the express provisions of the Intellectual Property Code of the Philippines. A decision is currently pending with the Court of Appeals on Motion for Reconsideration. If this ruling is sustained by the Supreme Court, this will have negative repercussions for the administrative enforcement of IP rights, as all cases currently pending with the IPO will have to be dismissed for lack of jurisdiction.

In 1998, the Philippines amended its trademark legislation to provide for minimum jail terms in counterfeiting cases. This legislation was expected to create a level of deterrence that might lead to a significant reduction in counterfeiting in the country. Sadly, the intention of the legislature has been frustrated, mainly by delays in the processing of cases, and because most prison terms are in practice suspended.

IACC members have been pleased to observe that the National Prosecution Service has established a task force of prosecutors in charge of handling IP cases; and that these prosecutors have proved more transparent and responsive than prosecutors attached to local governments. Although the task force was created to improve the dispatch of IP cases, this commendable purpose has been undermined by the continuing change in the members of the task force. Along with the change of members comes the re-assignment of cases from former members to the new members. This sometimes results in preliminary investigation being conducted all over again and thus causing delay. Indeed, the delay is further aggravated where the newly-assigned prosecutor is from outside the Metro Manila area as these prosecutors (unlike their Metro Manila counterparts) are not as conversant with IP laws.

The establishment of specialized courts could help resolve the critical problems caused by the backlog of criminal and civil cases and also ensure that judges handling IP disputes have adequate training. Such courts previously existed in the Philippines, but regrettably, the Supreme Court decided in 2003 to dismantle them. The Intellectual Property Office reportedly proposed the reinstatement of specialized courts, but the Supreme Court has rejected this proposal, citing the lack of disputes previously filed with the earlier courts outside major cities and provinces.

## **Copyright**

Copyright piracy in the Philippines remains severe, but the government is clearly trying to work more effectively with industry to address the problem.

Since the creation of the National Committee for Intellectual Property Rights (NCIPR) in 2005, NCIPR has seized P2.4 billion (about USD 50 million) worth of counterfeit items with P1.3 billion (about USD 27 million) recorded in 2006<sup>84</sup>. The estimated value of confiscated items increased from 2005 to 2006 by about 11 percent.

Nevertheless, these raids should be followed up with criminal prosecutions as otherwise there would be little deterrence value in the enforcement action<sup>85</sup>. Investigations, raids and seizures should be supplemented with more arrests and ensuing criminal actions. Finally, the cases themselves should be disposed of speedily and sentences handed down by courts should be served.

Therefore whether these new initiatives will maintain their traction and lead to meaningful reductions in copyright piracy in the longer term remains to be seen.

## **Customs**

IACC members are pleased to note that the Bureau of Customs (“BOC”) has been increasingly proactive in issuing warrants for seizure and detention for imported goods on the basis of non-payment of proper duties and taxes. During the course of seizures, counterfeits have been increasingly identified, and trademark owners informed for verification purposes. The BOC is consequently issuing more orders for the destruction of seized goods. The BOC has also been inviting IPR owners to record their rights with the BOC to facilitate enforcement. In most cases, the destruction of the counterfeits has taken place quite easily as the importers of counterfeits have rarely presented themselves to the BOC. However, criminal investigations into customs cases are still only a remote possibility.

IACC members regret to note that enforcement by Philippine Customs against both counterfeit and pirated products remains negligible. Recordal of rights with Customs is possible in the Philippines, but Customs still lacks the manpower and procedures to permit the inspection of meaningful quantities of shipments. Training is also required to assist Customs in prioritizing and profiling potential exports and imports of infringing items, and the IP enforcement team within the Bureau of Customs needs to be provided access to real-time electronic data on imports and exports.

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<sup>84</sup> <http://www.contentagenda.com/articleXml/LN564345306.html?industryid=45174> Kristine L. Alave -- *BusinessWorld*, January 30, 2007

<sup>85</sup> <http://www.iipa.com/rbc/2006/2006SPEC301PHILIPPINES.pdf> - 2006 Special 301 Report Philippines.

Legislation is now being considered that would facilitate legal action against transshipments of infringing products through Philippine waters. This legislation, which would amend the Tariff and Customs Code, would make the diversion of fakes more difficult by requiring shipping companies, agents, trans-shippers or the owner of the goods to submit a certificate of discharge issued by Customs or port officials at the port of destination.

## **Conclusion**

The IACC reiterates its earlier recommendation for the Philippine government to:

- Address systematic problems that have for too long resulted in unacceptable delays in criminal and civil actions in Philippine courts;
- Provide additional resources and training to facilitate border enforcement, including against goods in transit, and especially in free trade zones in the Philippines;
- Continue to strengthen resources for routine police investigations against trademark and copyright pirates;
- Establish specialized IP tribunals to handle civil and criminal cases, at least in major cities; and
- Implement new policies and procedures aimed at reducing the influence of corruption and protectionism that impede IP enforcement.

## PERU

### **Recommendation: Special Mention**

#### **Introduction**

A comprehensive trade agreement was put in place last year between the United States and Peru with the signing of the Peru Trade Promotion Agreement on December 12, 2006. The IACC welcomes this agreement which expands trade between the United States and Peru.

Nevertheless, the protection of IPRs is a fundament of this Agreement which increases economic opportunities and, ultimately, raises living standards in Peru. Therefore, IACC members would like to urge Peru, which was on the Watch List last year, to take the necessary measures to strengthen its IP laws and enforcement.

#### **Trademark**

Peru's IP legislation generally conforms to the requirements of the TRIPS Agreement. However, Peru's enforcement of IP legislation would seem to fall short of TRIPS compliance. IACC would like to see Peru fully implement not only substantive obligations, but enforcement obligations as well.

In particular, IACC would like to see a more robust enforcement of IP rights under the helm of the Instituto Nacional de Defensa de la Competencia y de la Proteccion de la Propiedad Intelectual (INDECOPI). IACC commends the underpinning spirit of INDECOPI to oversee and advance the protection of IP rights.

Nevertheless, IACC has been informed of an instance of INDECOPI adjudication blatantly falling short of acceptable international standards. Based on reports from consumers and its employees, a well-known U.S. trademark owner seized 1000 items of counterfeit apparel from a local retailer.

The seizure action, which had been administrated through the Trademark Office, was then appealed by the retailer to INDECOPI. The retailer stated that it had believed the seized goods, which had been manufactured abroad, to be authentic. The U.S. trademark owner acknowledged it did manufacture some of its goods abroad but stated that the seized good were clearly counterfeit.

INDECOPI recognized the U.S. trademark owner's counterfeit determination. Despite this, INDECOPI proceeded to grant the appeal stating that the retailer had purchased the goods under the belief that they were authentic. INDECOPI then ordered the return of the counterfeit goods to the retailer within 10 days.

In essence, therefore the Peruvian IP authority returned the fruits of crime back to the criminal. This absurd ruling is a clear and blatant contravention of Peru's obligation under TRIPS.

Therefore, IACC would like to see more resources channeled into training INDECOPI officials so that this coordinating and supervising IP authority is better equipped and able to deal and dispense judgments in line with international acceptable standards. Gaps in education at the judicial level severely undermine the effectiveness of the Peruvian government's efforts to enforce IP.

## **Conclusion**

While Peruvian law seems adequate on its face, IACC members have in practice been unable to obtain satisfactory results in their enforcement work, and we therefore recommend the government adopt the following measures:

- Channel more resources toward judicial training;
- Create specialized IP courts to deal with IPR disputes;
- Strengthen resources for investigation against trademark and copyright pirates;
- Take meaningful steps necessary to facilitate the imposition of significantly greater judicial and administrative penalties for IP violations;
- Make IP enforcement a political priority and devote significantly greater resources to INDECOPI, Customs, police and prosecutors;
- Strengthen government leadership and coordination among the various law enforcement authorities responsible for anti-counterfeiting and anti-piracy;
- Undertake a prompt review and revision of laws and regulations in order to facilitate inspections, seizures, criminal investigations and product destructions; and
- Continue to educate the public, the bar, the judiciary, Customs and other law enforcement authorities on IP protection.

## THE UNITED ARAB EMIRATES

### **Recommendation: Special Mention**

#### **Introduction**

The United Arab Emirates (UAE) overhauled its Intellectual Property regime in 2002 to align its IP laws with international standards. Being one of the few federal countries in the region, the seven different emirates of the UAE are governed by same IP laws. Nevertheless, the actual enforcement of IP rights varies from state to state due to the differing local cultural, social and administrative factors.

#### **Trademarks**

The UAE Trademark Law, which was enacted in 2002, is one of the most developed trademark laws in the Middle East. The law recognizes international concepts providing clear protection for "well known" trademarks and adopting the "likelihood of confusion" infringement threshold. Nevertheless, IACC members report infringements of their rights for various goods including consumer electronics, personal care and computer equipment.

#### **Copyright**

The UAE Copyright Law, which was enacted in 2002, gives clear protection to computer software, audiovisual and recorded works. In this regard, IACC acknowledges that the UAE has one of the lowest rates of business software piracy in the world, an estimated business software piracy rate of 34%<sup>86</sup>.

It is hoped that this figure will be further reduced by even more vigilant copyright enforcement by UAE authorities.

#### **Customs**

Customs Regulations have been implemented to further protect IP rights. The UAE Customs Department is required to check the certificate of origin of all imported goods and products and there are set procedures providing for the examination of goods. In general, the Customs Authorities have been very active in taking action against counterfeit and pirated goods.

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<sup>86</sup> International Intellectual Property Alliance Notice of Intent to Testify at a Public Hearing Concerning the Proposed United States – United Arab Emirates Free Trade Agreement  
[http://www.iipa.com/rbi/2005\\_Jan5\\_UAE\\_FTA.pdf](http://www.iipa.com/rbi/2005_Jan5_UAE_FTA.pdf)

However, the high volume of goods entering the free trade zones has made these zones difficult to police<sup>87</sup> so that there is only minimal or no Customs control on entry or exit of goods. The two of main gateways for the entrance of counterfeit goods into the UAE are Jebel Ali and Fujirah<sup>88</sup>. Goods passing through these two free trade zone hubs allow counterfeiters to disguise the true country of origin of goods and to distribute counterfeit products to neighboring countries. Counterfeit goods may also enter the country as separate components. These components are then assembled or packaged locally for re-export. IACC members therefore recommend that UAE customs exercise more scrutiny on goods passing through these free trade zone ports.

## **Conclusion**

The IACC recommends that the UAE Government:

- Provide additional resources and training to facilitate border enforcement, including against goods in transit, and especially in the free trade zones of Jebel Ali and Fujirah in the UAE;
- Continue to strengthen resources for routine investigations against trademark and copyright pirates;
- Establish specialized IP tribunals to handle civil and criminal cases, at least in major cities; and
- Implement new policies and procedures aimed at reducing the influence of corruption and protectionism that impede IP enforcement.

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<sup>87</sup> The Report on the Role of Free Trade Zones and Free Ports in Unchecked Cross-Border Movement of Counterfeit and Pirated Goods, May 30, 2006 by Faisal K. Daudpota, External Relations Coordinator for Anti-Counterfeiting with the International Trademark Association (INTA).

<sup>88</sup> The Report on the Role of Free Trade Zones and Free Ports in Unchecked Cross-Border Movement of Counterfeit and Pirated Goods, May 30, 2006 by Faisal K. Daudpota, External Relations Coordinator for Anti-Counterfeiting with the International Trademark Association (INTA).