



AMERICAN FREE TRADE ASSOCIATION
(“AFTA”)

1000 NW 57th Court, Suite 600

Miami, Florida 33126

Telephone: (888) 600-1479

www.aftaus.com

www.americanfreetradeassociation.com

**HOUSE SUBCOMMITTEE ON CRIME, TERRORISM AND
HOMELAND SECURITY**

COMMITTEE OF THE JUDICIARY

United States House of Representatives
Hearing on
Stolen or Counterfeit Goods Legislation (HR 4216)

March 28, 2012
Washington, D.C.

Testimony of
AMERICAN FREE TRADE ASSOCIATION
Gilbert Lee Sandler, General Counsel



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 2 of 12

BACKGROUND

This statement is offered on behalf of the American Free Trade Association (“AFTA”). AFTA is a not-for-profit trade association of independent American importers, distributors, retailers and wholesalers, dedicated to preservation of the wholesale and discount marketplace to assure competitive pricing and distribution of genuine and legitimate products for the benefit of all American consumers.

AFTA has been an active advocate of parallel market interests and opponent of counterfeit goods for over twenty-five years. It has appeared as *amicus curiae* in the two leading Supreme court cases affirming the legality of parallel market trade under the federal trademark, customs and copyright acts (*Kmart Corp. v. Cartier, Inc.*, 486 U.S. 281 (1988), and *Quality King Distributors v. L’Anza Research International, Inc.* 523 U.S. 135 (1998)), participant in numerous lower court decisions and has testified and worked with this and other Congressional Committees and federal agencies on parallel market and anti-counterfeiting laws, regulations, policies and procedures.

I am Gilbert Lee Sandler, an attorney admitted to practice in Florida and New York, and also a licensed customhouse broker. I am a founding member of the law firm Sandler, Travis & Rosenberg, P.A., and a principal of its affiliated consulting company Sandler Travis Trade Advisory Services. I have served as General Counsel to AFTA for over twenty-five years, and have practiced in the area of international trade for over forty years, first serving as a Department of Justice trial attorney defending decisions of the Customs Service. Since 1975 I have been in private practice representing importers and exporters on a broad range of regulatory issues affecting imports and exports, including enforcement of intellectual property laws at our nation’s



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 3 of 12

borders.

SUMMARY OF POSITION

On behalf the American Free Trade Association (“AFTA”), we respectfully request that any legislation providing for the early release of coded samples to rights holder adopt procedures to safeguard against unnecessary release and harmful abuse of commercially sensitive information that CBP will be providing to intellectual property owners. For convenience of reference, we have attached a short 2-page summary of talking points prepared by our Association at the time it first reviewed HR 4216.

Our members and supporters strongly support efforts by the Congress and the Administration to give more effective tools to CBP to identify and stop the importation of counterfeit goods into the United States. However, we also strongly support facilitation of lawful importations of branded products, including those traded on the lawful parallel or “gray” market.

The proposed legislation would provide a small tool helpful in limited circumstances for certain types of products, but would also create a far-reaching and significant risk that CBP will be providing highly sensitive commercial information to competitors of parallel market importers and that information could be used to damage, disrupt or destroy legitimate and lawful trade in genuine brand name products.

- The vast majority of branded products can be determined by CBP or the rights holder to be genuine or counterfeit without access to the “tracking” codes on product labels and packaging. The Bill includes no provisions to eliminate such unnecessary disclosures, nor does it direct CBP to do so.



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 4 of 12

- Those rights holders who seek to control distribution and pricing beyond their rights under U.S. law, can use the disclosed information to impose such anti-competitive controls through their market and commercial power, if not through litigation, regulation and legislation. The Bill includes no provisions or direction to CBP to avoid such abuses.
- The sensitive nature of the disclosures is a problem which has been identified by CBP and the President's Intellectual Property Enforcement Coordinator and one which can be addressed by statute or implementing Customs regulations permitting importers of detained goods to demonstrate their legitimacy.

Accordingly, we submit this testimony to describe the problem and to suggest solutions which will allow CBP to focus more vigorously on anti-counterfeiting efforts while diminishing or eliminating unintended damage to lawful importers and importations. We urge the Committee to examine those issues and adopt amendments which will eliminate and alleviate those problems.

GENERAL DISCUSSION

We have characterized the coded or unredacted sample disclosure authorized under HR 4216 as a small and limited tool for CBP because it serves only to speed the decision-making on the relatively small number of situations in which CBP has already detained imported goods and singled them out as suspicious from among the vast volume of shipments arriving daily at more than 300 U.S. seaports, airports, express consignment centers and postal facilities. This tool will not stop the counterfeit goods from eluding CBP detection and entering into the U.S., because it addresses only those goods CBP has already detained as suspicious.



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 5 of 12

The bigger and more perplexing challenge for CBP and the Congress is how to “reduce the haystack” which CBP must search to find counterfeit goods, so that its suspicions are more efficiently and effectively directed at the straws and needles in that huge haystack that are *not* genuine. The magnitude of the targeting problem has increased, as counterfeits reportedly have moved from large traditional shipments to the smaller, more numerous shipments arriving by international mail and express courier: CBP reports that in FY2011 the number of seizures increased 24% over the preceding year, but that the value of the goods seized decreased by 5% because of the larger volume of low value shipments arriving by mail and courier.

This targeting problem has been highlighted and tabled by CBP in the Intellectual Property Subcommittee of the statutory advisory committee on CBP Commercial Operations (COAC) which I serve on along with many rights holders, importers and government officials. CBP has acknowledged that its detentions often are directed at genuine goods imported by authorized licensees and lawful parallel market importers. Thus, COAC reported at its public meeting last month that it is exploring “haystack reduction” procedures such as (1) verification of trusted importers who are authorized licensees and legitimate parallel market importers, (2) identification of secure authentic distribution chain management systems and (3) adoption or support of enhanced technology such as “secure serialization” of branded products. These are initiatives which we encourage both the Administration and the Congress to consider, as they more directly and comprehensively address the need for more effective, efficient and targeted anti-counterfeiting efforts at our borders without jeopardizing confidential business information.

The Problems with HR 4216. There are at least four concerns which should be addressed if CBP is to be authorized to make early disclosure of coded or unredacted samples to



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 6 of 12

rights holders: (i) it should not provide trademark owners with information usable to disrupt lawful parallel market trade; (ii) it should permit importers an opportunity to address questions about their importations before it shares information outside the government, (iii) it should avoid unnecessary disclosures which would otherwise constitute violations of the Trade Secrets Act, and (iv) it should be limited in scope to suspected “piratical” and “counterfeit” goods, rather than extended to goods suspected or even found to “infringe” copyrights..

Release of Coded or Unredacted Sample Releases Commercially Damaging information. While United States law and economic policy hold parallel market trade to be lawful and desirable, there are many trademark owners who are dedicated to the elimination of parallel market trade through legislative, regulatory, judicial and commercial practices.

The list of trademark owners who have taken such action is extensive and well known from reported court cases and ITC proceedings, including Coty, Davidoff, Montblanc, Parfums Givenchy, Omega, Sebastian, Paul Mitchell, Original Appalachian Artworks, Nestle, et.al. The list of retailers who sell brand name products traded in the parallel market is also long and well-known from public records, including CVS pharmacy, Costco, Wal*Mart, Filenes Basement and K-Mart, et.al.

There is no doubt that there is commercially sensitive supply chain and transactional information coded onto products, packaging and labels which could be used by anti-parallel market trademark owners to disrupt or destroy competitive distribution of their products. We have often provided CBP officials, members of Congress and the trade in general, examples of tracking codes placed on brand-name products or their packaging (in addition to the batch codes used for quality control and recall purposes) and used to identify downstream distribution of



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 7 of 12

products. The codes are often invisible to the consumer and are generally not decipherable by them. The distribution information sought concerns the sales beyond the first sale limitation on distribution rights under U.S. copyright, trademark and patent law.

The importance of information to rights holders who would eliminate parallel market trade cannot be underestimated. My career in handling parallel market cases actually began with a court case in which the rights holder's objective was to identify the importers of its goods on the parallel market, and continues twenty-five years later with cases in which the rights holder is more focused on identifying suppliers of its products on the parallel market than in obtaining relief against the defendant. In 1983, Parfums Stern sued Customs and 100 unknown John Doe importers, seeking a Court order directing Customs to disclose the names of companies importing their branded perfume products. In 2011, Coty sued a small company that removed tracking codes from imported products, largely to obtain discovery of their list of customers dealing in unauthorized Coty products.

There is also no doubt that unless directed otherwise, CBP officers at ports of entry may routinely provide this sensitive information to trademark owners whenever they are inspecting goods arriving from an "unauthorized shipper" or imported by an "unauthorized importer" since unauthorized importers are likely to be regarded as "high risk" by CBP officers reviewing the recordation records. CBP has no system to validate lawful parallel market importers.

There Is No Reason or Need to Exempt Detained, Suspicious Importations from the Well-established Practice of CBP to Provide Importers with an Opportunity to Protect their Interests. CBP has a long history of working directly with importers to validate their compliance and cure any issues in advance of taking action, both at the direction of Congress and



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 8 of 12

based on its own approach to enforcement and facilitation of lawful trade at our nation's ports.. Seizures are preceded by notices of detention as required statute (19 USC 1499(c) and 1595a), civil penalties are preceded by pre-penalty notice as required by statute (19 USC 1592(b)), liquidation decisions to increase duty, tax and fee assessments are preceded by requests for information and notices of proposed actions by regulation (19 CFR 152.2). The statutory concept that importers must exercise "reasonable care" in their importations, and that CBP must provide information needed to exercise that care, is a "shared responsibility" with CBP referred to as "informed compliance". It contemplates that there will be a meaningful sharing of information between CBP and the importer to avoid and resolve issues. Customs Modernization and Informed Compliance Act (Pub. L. 103-182). There is no reason for CBP to routinely bypass the importer to consult with a potential competitor of the importer based upon a suspicion that the detained goods are piratical or counterfeit.

Potential Disclosure of information Protected by 18 USC § 1905. The Administration has recognized that providing samples will often reveal information protected by the Trade Secrets Act: CBP routinely removes or "redacts" sensitive information from suspicious articles and packaging before providing samples to IPR owners; the IPEC's 2010 Strategic Plan on Intellectual Property Enforcement specifically stated (at page 8) that while anti-counterfeiting efforts would be enhanced by sharing samples with IPR owners, nonetheless "The U.S. Government will ensure that appropriate safeguards are implemented to protect personally identifiable information, including compliance with the Privacy Act, as warranted."

The IPEC addressed this concern in its 2011 proposed legislation which would provide importers with a 5-day notice of suspicion and a 7-day opportunity to address the suspicion of



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 9 of 12

the CBP officer. The bill includes neither a defined suspicion to trigger disclosure any safeguard procedures such as recommended by the IPEC. The IPEC proposals, to our knowledge, continue to be under active consideration by the Congressional committees developing Customs Reauthorization legislation.

Possible Solutions. There are many procedural alternatives, and combination of alternatives under which Congress can enhance the anti-counterfeiting efforts of CBP while avoiding destruction of lawful importations.

1. Limit implementation to electronic parts (or parts for national defense purposes). We believe this is the proper interpretation or implementation of the temporary provision for disclosure of samples contained in Section 818(f) of the National Defense Authorization Act (NDAA) on “Detection and Avoidance of Counterfeit parts”. This interpretation of the law was eloquently described by Congressman Conyers on the Floor of the House during debate on the bill (copy of testimony attached).

2. Adopt an objective standard for when CBP “suspects” an import to be counterfeit and may share this sensitive information. This is an area in which the Congress, or CBP at the direction of the Congress, should work with the trade to establish rational standards. A “suspect” product should be:

- a. one which CBP has made an effort to validate the genuineness of the goods through communication with the importer,
- b. has specific information regarding indicia that the goods are counterfeit, etc.

3. Adopt an objective standard for when CBP “may” share the information. It should be limited to:



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 10 of 12

- a. Trademarks which are recorded with CBP,
 - b. Situations where the trademark owner has demonstrated that verification of authenticity cannot be done by CBP officials or by an independent third party, or
 - c. Product categories which CBP has determined are beyond its capacity to validate (e.g., electronic chips, et.al), or
 - d. Products in which there is no history of parallel market battles, and
 - e. Situations in which CBP has determined that providing “redacted” samples, packaging and labels would not be sufficient.
4. Adopt “bonding requirements” which require the trademark owner to:
- a. limit its use of the information to validating authenticity of the goods, and
 - b. post a bond sufficiently high to compensate the importer should the goods be determined to be genuine and the trademark owner uses the information for other purposes which cause economic harm to the importer.
5. Adopt the statutory provisions proposed by the Intellectual Property Enforcement Coordinator, which would require notice to the importer within 5 days and a response by it within 7 days (both occurring while the goods are still in the control and custody of CBP and without extending the existing 30-day period for CBP to determine whether or not the goods are genuine).
6. Eliminate language in HR 4216 which would authorize disclosures where there is a suspicion that goods or their packaging “infringes the copyright”. Disclosures should be limited to suspected “piratical” goods and packaging. The broader references to potentially infringing goods is likely to authorize disclosures in connection with genuine goods, such as those where



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 11 of 12

rights holders are seeking to establish or expand limits on import or distribution rights of genuine products under copyright and trademark laws, interpretations of the Lever-Rule regarding genuine goods with alleged material, physical differences, et.al. CBP should not be a decision-maker or a source of information in these disputed areas.

7. Disclosures should only be authorized for trademarks and copyrights which are “recorded” with CBP under its regulations, rather than all trademarks registered with the PTO. This requirement will assure that CBP has a searchable database to assist its inspections and determinations and up-to-date contacts for communicating efficiently with the proper employees and representatives of the rights holder. It also establishes confirmation of the commitments of the rights holder to cooperate with CBP in a timely fashion, to establish the need for disclosures to verify authenticity and to post any required undertakings involved in the receipt of confidential and commercially sensitive information.

CONCLUSION

We appreciate the opportunity to testify on these issues and are prepared to provide additional information, or work with this Committee to fashion a reasoned and effective approach to disclosures are authorized where warranted and necessary and that this well-intentioned legislation is not open to abuse by those who would stifle competition, limit distribution, and raise prices of branded products in the US marketplace.

Subcommittee members and staff are invited to contact AFTA’s General Counsel, Gilbert Lee Sandler, Esq., or other members of our Board should they wish to discuss any matter raised in this statement in more detail or in the event there are any remaining questions or doubts regarding our concerns regarding the impact of the Stolen or Counterfeit Goods Legislation on



AMERICAN FREE TRADE ASSOCIATION

Testimony on Stolen or Counterfeit Goods Legislation (HR 4216)

Washington, D.C.

March 28, 2012

Page 12 of 12

the American consumer or the competitive, domestic marketplace.

We thank you for providing us this opportunity to have our testimony made a part of the record of today's hearing.



American Free Trade Association

“The Association for Freedom to Trade”

www.americanfreetradeassociation.com

www.aftaus.com

1-888-600-4179

TALKING POINTS CHABOT/POE LEGISLATION (HR 4216)

- ❖ **The bill would provide rights holders with unredacted product samples before release of suspicious goods into the U.S. commerce, before any communication with the importer allowing it an opportunity to authenticate its goods or prevent disclosure and while the goods are detained and under control by CBP.**
- ❖ **The proposed disclosure authority will broadly arm rights holders with information usable to control global product distribution and pricing and to identify targets for litigation, while providing a minor if not unnecessary improvement to counterfeit determinations.**
- ❖ **Tracking codes on product packaging are often embedded by manufacturers to control downstream distribution and pricing, but are of little, if any, use in verifying product authenticity.**
- ❖ **Providing rights holders with unredacted product samples provides proprietary importation and supply chain information contained within embedded distribution tracking codes to commercial competitors without any protection or recourse for the unrelated and lawful importers.**
- ❖ **Many rights holders have been aggressively looking for any means --- judicial, legislative, regulatory and commercial -- to control product supply chains and pricing to the detriment of the American competitive marketplace.**

The Legislation Would Amend the Trade Secret Act to Specifically Authorize the Disclosure of Proprietary Trade Secrets. The Chabot/Poe Legislation would expand the authority of Customs and Border Protection (CBP) to provide IP rights holders with samples of goods offered for import or export, including their retail packaging and other packing material, to assist CBP to determine if the goods are piratical or counterfeit. These product samples often include tracking distribution codes identifying an importer's proprietary and confidential supply chain. These codes have no relevance to determining product authenticity.

The government should not provide commercial information to foster litigation or empower rights holders to disrupt lawful distribution relationships. The Chabot/Poe Legislation provides downstream distribution information to rights holders who have been looking to expand distribution control beyond the first sale (*Costco Wholesale Corp. v. Omega, S.A.* 131 U.S. 565 (2010), *Quality King v. L'Anza Distribution* 523 U.S. 135 (1998), *John Wiley & Sons, Inc. v. Kirtsaeng*, 654 F.3d 210 (2d Cir. 2010)) since many consumer products are coded solely to control downstream distribution in ways not permitted under U.S. law. Providing those codes to parties uninvolved in the importation empowers private party attacks on legitimate transactions, not protection against counterfeit goods.

The Legislation authorizes release of proprietary supply chain information without any safeguards against abuses. CBP often questions the authenticity of imported goods which are found to be authentic. Thus, rights holders receiving this information are often in competition with the importers. Any legislation should address this problem by providing for a specific determination of a need to release the information, notice to the importer and an opportunity to respond prior to release, an undertaking by the rights holder to use the information only for authentication purposes and not for commercial purposes, and the posting of adequate security to compensate the rights holders for damages suffered as a result of any abuse of this information.

Information on product labels is often irrelevant to determining product authenticity. The information and codes on a product label and discerned from tracking codes can be copied by counterfeiters and are often of no use in the evaluation of whether a product is genuine. Shampoos, for example, can only be authenticated by examination of the bottle and testing of content.



AMERICAN FREE TRADE ASSOCIATION

Talking Points - Chabot/Poe Legislation (HR4216)

Washington, D.C.

March 28, 2012

Page 2 of 3

ANY NEW LEGISLATION IMPLEMENTING ANTI-COUNTERFEITING INITIATIVES AT U.S. BORDERS MUST ALSO PROTECT U.S. IMPORTERS/EXPORTERS BY MAINTAINING CONFIDENTIALITY OF PROPRIETARY SUPPLY CHAINS.

Any such legislation must:

Contain Clear Definitions: Adopt clear definitions of “counterfeit”, “infringing” and/or “piratical” goods which specifically exclude goods manufactured under authority of the U.S. rights holders.

Establish Clear and High Thresholds for Disclosure of Product Samples: Require that the statutory standard for the Secretary determines that there is a demonstrated need shall include a finding of the specific product sectors under which qualified for the receiving of such samples. The legislation must also include a clear matrix for border officials to support a claimed suspicion that the goods presented for entry/export violate domestic intellectual property laws in the country of import. Finally, the legislation must limit disclosure of product samples to those instances where there is a supportable suspicion that the articles are more than likely counterfeit or piratical by a strict definition and matrix that eliminates subjective analysis.

Provide Meaningful Opportunities for Importers/Exporters to Prevent Disclosure and Verify Product Authenticity: Importers/exporters must have a meaningful opportunity to prevent disclosure of product samples before any rights holder is advised of the pending entry/export. Any legislation must include clear descriptions of the information that the Importer/Exporter can provide to CBP to verify product authenticity and prevent disclosure of product samples to any third party rights holder and require decision-making by CBP on notice to the importer.

Encourage Better Communications between CBP and U.S. Importers/Exporters: CBP must be encouraged to balance the rights of U.S. rights holders with those of U.S. Importers/Exporters and must be clearly directed to communicate confidentially and first with the importer/exporter about any shipment concerns before consulting with any third party about the pending shipment. Importers/exporters must be provided with written notice specifying the concerns a port official may have about a shipment and which also sets forth specific time frames for the Importer/Exporter to respond to that Notice before any third party is provided any information about the pending shipment.

Require Security and Undertakings from Rights Holders, and Institute Penalties in the Event of Misinformation: Rights holders must be required to post a bond or other security in an amount sufficient to provide importers/exporters with recourse in the event of intentional entry/export delay for products that are not counterfeit, infringing or piratical and that will discourage false charges against lawful U.S. businesses. Rights holders should also be required to verify, via sworn affidavits, that any information provided to them about a pending shipment, including information that may be learned from PDCs, be maintained in confidence and relied upon only to assist CBP with determining product authenticity. Moreover, in order to further protect U.S. importers and exporters, any such law must specifically include penalties against rights holders that knowingly provide false information to CBP to inflict injury upon a competitive business.

Mandate Registration and Recordation: CBP’s resources to enforce this type of legislation, which will necessarily require greater vigilance of port officials and further shipment delays, should only be expended in the event rights holders have invested in registration and recordation of their copyrights and trademarks.

Mr. CONYERS. I would like to remind my colleagues that provisions within the conference report impact our civil liberties and should have been referred to the Judiciary Committee for review.

I also support efforts to enhance the ability of Customs & Border Protection to prevent counterfeit goods from being imported into the United States. However, Section 8 of this bill will disrupt the flow of genuine brand name products into the United States.

This is true because many of the goods which CBP inspectors view with suspicion are in fact genuine goods, lawfully moving in distribution streams parallel to the authorized distributors. These transactions are desirable because they provide U.S. consumers with price competition and wider distribution of brand name products.

However, the existence of these transactions is often under attack by trademark and copyright owners who actively seek to control resale pricing and downstream distribution of the products they have already sold into commerce. Section 8 will give anti-competitive companies a new tool by giving them confidential information about competing parallel imports at their times of arrival, while they are still detained by CBP and unavailable to the importer, and without giving the importer an opportunity to prove its goods are genuine, and without even giving notice to the importer that its information has been shared with a competitor seeking to prevent its lawful transaction.

This problem could be minimized if Section 8 is limited to goods raising national security concerns or purchases by the military. I believe that is the intent of this provision of the Department of Defense Appropriation bill.

This problem could also be minimized if this bill or CBP would adopt the safeguards which the Administration proposes be included in the Customs Reauthorization Act. This would be appropriate since Section 8 provides that it sunsets when the Customs Reauthorization is adopted. The safeguards include a requirement that the Secretary find there is a need for disclosing confidential information, and that CBP provide the importer with notice and an opportunity to respond before any confidential information is released to other private parties.

For some reason, we are adopting this provision in anticipation of a more thoughtful approach in the Customs Reauthorization Act. This is not a wise or needed course of action. CBP today can provide redacted samples to IP owners and very often that is sufficient to determine if they are genuine or counterfeit.

CBP today keeps suspicious goods out of U.S. commerce while it determines if they are genuine. The safeguards proposed by the administration will not put suspicious goods into commerce nor delay the final determination of CBP because there is an existing 30-day requirement that is not altered by any proposed legislation.