

# Independent review of IP and growth

A response from the brand perspective

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# Overview

The Anti-Counterfeiting Group and the British Brands Group appreciate this opportunity to respond to the call for evidence in this independent review of intellectual property (IP) and growth.

Not many years ago, IP languished in an esoteric backwater, which seemed to be reserved for lawyers, trade mark agents and complicated concepts, such as patents. Now it is regarded as an important powerhouse for future economic growth.

While very much welcoming this development, which rightly places a far greater value on IP as a national asset than previously, we would also like to sound a note of caution. The UK's strong IP framework overall already offers the necessary protection for ideas, inventions and innovation, and has proved many times over to be adaptable, as well as robust. It is already supporting many exciting new developments, particularly online.

The IP framework provides the means for transforming an idea into an economic asset, which can then be traded as such. But IP in itself is neither the source of innovation and creativity, nor in isolation the means for achieving increased economic output.

It is risky to attempt to re-engineer an existing legal framework, in any policy area, simply in order to try and influence market forces and artificially stimulate growth. Following this Review, it will be essential to model the consequences of any decision before making policy changes.

We are sure that we will not be alone in urging the government also to focus on the many other factors which influence growth, which we touch on in our response.

Branding is dependent on the full range of IP rights and the successful monetisation of the innovations and ideas which initially give rise to those rights. We will demonstrate that it is a significant, if under-recognised, economic force contributing to national growth and global competitiveness, in both offline and online markets. As such the IP rights on which brands depend deserve better standards of protection and enforcement than currently exist.

With the Review's focus on potential barriers to growth, we will examine in our response those which are particularly relevant to the creation and building of brands in the UK, and to the protection and enforcement of the IP rights behind branding.

In the Call for Evidence, Professor Hargreaves states "...the question at the heart of this review is what, if anything, should we do to change the UK's IP system in the interests of promoting more rapid innovation and economic growth? It is through that lens that I will be assessing all responses."

We have divided our response into sections which correspond with topics of relevance to our respective remits, all of which feed in to recommendations which are designed to help answer this question.

We have identified areas where changes will support future growth but which do not involve any change to the IP framework itself:

- government to assess the economic importance of branding (and the IP on which it depends), to recognise a significant aspect of the UK economy;
- include the role of branding in the government's growth plans, actively involving the Treasury and BIS, as a first step in defining a strategy for the UK as a world class market;
- recognise counterfeiting as an economic threat, both to industry and to the national economy, and ensure that enforcement is consistent and effective – nationally on the ground, online, in source countries and at the UK frontier;
- review the way in which IP policy and IPR enforcement are currently managed within government, to achieve greater efficiency and effectiveness (including an assessment of the role of the IPO);
- in competition terms, recognise and promote the pro-competitive beneficial nature of branding and IP to support coherent, consistent policies and address the inhibiting effect on innovation of powerful retailers also being direct product competitors;
- explore the potential to segment SMEs by their differing approaches to and needs for IP;
- examine the education needs of SMEs to encourage better access to and use of the IP systems for registration and protection of their rights.

As regards the barriers which may lie within the IP framework which can and should be addressed:

- allow companies to obtain their own remedies against parasitic trading that feeds off the reputation of familiar branded products;
- licensing of IP rights could certainly be easier – even finding out who owns the relevant rights can be hard;
- more streamlined procedures are needed for registering and protecting IP rights, with less expensive solutions for obtaining remedies when rights are infringed;
- much smarter enforcement is also needed, to deal with the huge global problem of IP crime (counterfeiting and piracy);
- we need to find ways to reduce the costs of IP protection and IPR enforcement, particularly for SMEs.

As a matter of principle, it remains crucial to achieve a fair balance between all the various rights and interests involved. In the past, balance in the IP system has evolved over time, via market forces, new media and new business models, which have found their own level, mainly via consumer choice.

We would urge government to ensure that any future drive for growth is not at the expense of that balance, nor at the expense of an IP framework which is, in all important respects, fit for purpose.

# Independent review of IP and growth

## 1 Introduction

### 1.1 Anti-Counterfeiting Group and British Brands Group

The Anti-Counterfeiting Group and British Brands Group are pleased to provide joint input to the independent IP Review announced by the Prime Minister on 4<sup>th</sup> November 2010. Both organisations represent brand manufacturers in the UK and a list of members is available on request.

The Anti-Counterfeiting Group (ACG) campaigns on behalf of consumers and legitimate businesses for recognition of the economic and social cost of counterfeiting.

The British Brands Group provides the voice for brand manufacturers of all sizes and across a range of sectors. It champions the benefits of branding and the potential for brands to deliver choice and value to consumers in an environment of vigorous but fair competition.

Both organisations are cross-sectoral and work closely with similar national organisations in other Member States, at European level and internationally.

### 1.2 Brands and the IP Review

In November the Prime Minister called for:

“a review of IP laws, to see if we can make them fit for the internet age. I want to encourage the sort of creative innovation that exists in America.”

The Review’s Call for Evidence is significantly wider, inviting “fresh evidence on the extent to which the current IP system successfully promotes innovation and growth and how it could do so more effectively”. Our input seeks to address these points, while noting that the Review’s short time frame prevents the generation of fresh evidence.

Despite the breadth of the call for evidence, we are conscious of the Review’s focus on copyright and patents. However, branding is a powerful force in stimulating and commercialising innovation, and contributes strongly to growth and global competitiveness in both online and offline markets. This makes branding directly relevant to key themes of the Review. To ignore it would be to understate significantly the importance of IP to the UK economy.

Furthermore, successful brand building may involve the full range of IP rights. Because of the interwoven nature of the IP system, any change may well impact on branding, something we urge the Review to take into account.

Finally, as the Review is looking at barriers to growth in the IP system, we have structured our response accordingly.

## 2 Brands, IP and Growth

### 2.1 What are brands?

To some, a brand may mean a trade mark, or perhaps a logo or company identity. These definitions significantly over-simplify brands and undervalue their economic importance. They are best understood as:

"A reputational asset which has been developed over time so as to embrace a set of values and attributes, resulting in a powerfully held set of beliefs by the consumer and a range of other stakeholders."<sup>1</sup>

Brands rest in the minds of individuals and represent the sum of that individual's understanding of a product or service, shaped by personal experience, word of mouth, advertising and many other forces, some positive and some negative. Brands are therefore personal, guiding individual economic behaviour.

The economic significance of brands rests in this focus on the individual combined with the potential to achieve significant national and international scale:

"All economic power lies in the hands of the consumer but it is fragmented and must be accumulated before it can be harnessed. .... Each of us has a small amount of money to spend, but there are billions of us. Getting us to spend in a concerted way is like herding cats, and can only be achieved by coercion (taxes) or by brands (shopping)."<sup>2</sup>

The role of the individual is becoming ever stronger with the growth of social media. This is enabling a closer dialogue between companies and individuals. The traditional model of broadcasting brand messages is being supplemented by individual conversations, making brands more active and volatile and companies more accountable.

The ingredients of a successful brand may be many, but the essential elements will include: a strong, relevant promise to the consumer; a superior performance which consistently matches or exceeds expectations; distinctiveness in the marketplace which allows consumers to distinguish it from competitors; and a clear, common understanding of what it stands for. It is important for brand-building in the UK that companies are able to protect and enforce their consistently-portrayed and consumer-recognised brand features, as they are in countries such as France and Germany. Examples include the metallic blue, silver and red iconography of **Red Bull** drinks and the black, red and gold colour combination of the **Mars** chocolate bar.

The brand model is versatile, being relevant to big and small companies (**Coca-Cola** drinks; **Fyne Ales** beer<sup>3</sup>), products and services (**Burberry** clothing; **Direct Line** insurance) and product ingredients (**Lycra** fabric). It is relevant in consumer markets (**Dove** soap) and business markets (**The Economist** magazine), online (**ComparetheMarket.com** web service) and offline (**Pret A Manger** restaurants).

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<sup>1</sup> Westminster Business School, "[Valuing brands in the UK economy](#)" (2008)

<sup>2</sup> Simon Anholt, "[Brands beyond business](#)" (2005), Brands Lecture.

<sup>3</sup> FT.com, "[Fyne Ales wins best brand award](#)", February 2011

Many successful British-owned SMEs have been set up in the last ten years and developed thriving retail, online and export businesses. **Fish 4 Dogs** fish-based pet food, **The Organic Pharmacy** beauty products, **ASOS** online apparel and accessories and **GHD** hair straighteners are examples.

When we refer to branded “products” in this submission, we include this wide scope, not distinguishing between products or services, on or offline, and consumer or B2B markets.

As brands work at the level of the individual, they are vulnerable to change, affected by word-of-mouth, the advent of new, better technology, the actions of competitors and many other forces. Companies must therefore work continuously to ensure relevance and maintain consumer preference. The **Netscape** browser, **Sinclair** technology, **Ratners** jewellery and **Yardley** cosmetics are all examples that failed to do this.

## 2.2 Brands and IP

The building of brands depends on effective and enforceable IP rights, whether registered or unregistered, and their protection:

- Trade marks** protect the distinctiveness of brands by protecting brand names and other "signs" including logos and familiar "get up" and advertising elements such as the **Rolls Royce** flying lady or the **Intel Inside** jingle; enable consumers to distinguish between products; provide shortcuts to the brand in consumers' minds (for quick, informed purchasing decisions); allow investments in marketing, social responsibility and other reputation-enhancing initiatives to be captured and also traded e.g. through licensing and/or franchising;
- Design** protects the distinctiveness of shapes and configurations of products and of packaging designs;
- Copyright** protects the distinctiveness of branded content, online content, marketing materials, commercials, advertising jingles, product labels and manuals;
- Patents** protect inventive elements in products, processes and packaging that may yield superior performance. This may grow markets or create new ones and may enhance reputations;
- Passing off** prevents consumers being misled into thinking one product is made by – or approved by – another.
- Trade secrets** protect both technical know-how and commercial information such as marketing and new product development plans against unauthorised use by others to whom this information has been provided in confidence.

It is important to stress that the full range of IP rights are important to the creation and building of brands. With one notable exception, addressed later in this submission, the UK framework of IP rights works well in practice in both online and offline markets, encouraging investment and presenting no barriers to growth.



## 1

### Barrier to growth

Potential changes to the IP system that may inhibit brand building in the UK.

### Recommendation

As branding and IP rights are so interwoven, with brands' success dependent on effective protection of many IP rights, any review of the UK's IP regime may have implications for branding. The review to acknowledge such implications and take them into account in recommendations.

## 2.3 Brands and the economy

The UK's brands play a prominent role in the economy, both domestically and globally via exports. The UK's most valuable brand is Vodafone, valued at £17,932m.<sup>4</sup> The Review presents a rare opportunity to shape the UK's performance and reputation as a world-class market in which to create and build brands, an opportunity we trust will be grasped.

Brands contribute to the economy in significant ways:

### **Consumer confidence and protection**

Consumers know, and can have confidence in, what they are buying with familiar brands. Consistency lies at the heart of branded products, reinforced by a guarantee of quality. Consumer confidence encourages consumption while trust in the brand encourages the trial and take-up of new technology and ideas;

### **Share performance**

The importance and value of brands to companies is well documented, with league tables published by [Brand Finance](#), [Interbrand](#) and [Millward Brown](#), amongst others. These tables illustrate their financial value, with the brand often accounting for 50% or more of the organisation's market value. It has been calculated that the total *intangible* value of Interbrand's top 100 amounted to a staggering \$988,287,000,000,<sup>5</sup> providing insight into the economic importance of intangible over tangible assets. Some 65% of the value in the UK economy is intangible, for example, ranking it fourth in the world.<sup>6</sup>

The impact of branding on share performance has also been measured, with Futurebrand finding that strongly branded companies outperform weakly branded companies.

The importance of branding has recently been illustrated by the publication of a new ISO standard for brand valuation, recognising that brand value plays an ever-growing role in business activities,



Source: Futurebrand

<sup>4</sup> Brand Finance, "[Top 50 British brands 2010](#)"

<sup>5</sup> Brands Lecture, Simon Anholt, "[Brands beyond business](#)" (2005)

<sup>6</sup> Brand Finance, "[Global Intangible Tracker](#)", p.33 (2006)

including strategic planning, tax planning, fund raising, mergers and acquisitions, partnership working, licensing and franchising, and dispute resolution / litigation.

### ***A spur to competition***

Branded companies continuously seek to meet consumers' unmet needs – whether the needs of different consumers or the differing needs of the same consumer. The result is a plethora of competing choices, with brands (underpinned by IP rights) providing the mechanism for consumers to quickly, efficiently and accurately exercise their choice. The net effect is a range of products competing on the basis of quality, performance and price.

### ***Export performance***

Brands contribute directly to export performance. Scotch whisky, which is predominantly branded, represents 25% of all the UK's food exports, at £2.82 billion. They also provide a halo effect for other exports from the UK, at the same time directly influencing perceptions of the UK abroad (i.e. its reputation).<sup>5</sup> Finally, brands create wealth around themselves. US research suggests that branded companies tend to generate between 2½ - 3 times as many jobs in the place they are based as appear on the payroll.<sup>5</sup>

### ***Responsible business***

Branding links the interests of business with those of society, providing a strong mechanism for companies to be held accountable for their actions. A recent study "[Brands and responsible business](#)" explores this link further, indicating the significant investment made by branded companies. This aspect of branding is particularly significant to the Review and its emphasis on social innovation.

More on the economic importance of brands can be found in the Westminster Business School study "[Valuing brands in the UK economy](#)" and an article in British Brands "[The economic importance of brands](#)".

It is surprising that, in light of branding's significant value and its contribution to the economy, there is little government recognition of its role. It barely features in government trade or economic policy, for instance.

This is a significant omission and a potential barrier to growth, particularly as government has expressed the wish to grow the economy in a balanced, socially responsible way, areas of strength for branding. Branding operates across sectors and is not geographically constrained. **Ty Nant** water is based in Bethania, Wales; **Barr's** soft drinks in Cumbernauld, Scotland; **Vimto** soft drinks in Newton-le-Willows, Merseyside; and **Bottlegreen** soft drinks in South Woodchester Gloucestershire.

Certainly the UK is well-placed to be an economy that better harnesses the power of brands. It possesses significant strengths in its branding capabilities, particularly with its world class brand-focused creative industries (e.g. advertising, design and branding agencies) which deliver significant export value in their own right.

The study by Westminster Business School is, we believe, the only study in this field. Its key findings, based on the available evidence for 2006, are:

- an estimated 1 million people are employed in the creation and building of brands in the UK (4% of all employed);
- companies spend some £33 billion on branding, equivalent to total expenditure on computer software and scientific R&D combined;
- this represents an investment in the UK economy of some £16 billion, approximately 12% of all intangible investment.

The study notes the Treasury's recognition that branding is an intangible investment, underlining its importance to the long-term health of the UK economy. It also notes however that the value of brand equity held by firms is simply not captured in official estimates.

The IPO in 2009 led an important conference ("Branding in a modern economy") to understand better the contribution of branding and explore how the UK may become a stronger market in which to create and build brands. An important recommendation in the post-conference [report](#) was the need for more work and it is encouraging that the IPO has launched a study as part of its 2011 research programme. It is noteworthy however that BIS and the Treasury are yet to engage visibly in this initiative.

## 2

### **Barrier to growth**

Government has yet to acknowledge the economic importance of branding (and the link to the IP on which it depends), as a result overlooking a significant aspect of the UK economy.

### **Recommendation**

The review to call for the economic role of branding to be measured and assessed in the context of the government's growth plans, actively involving the Treasury and BIS, alongside the important work already being undertaken by the IPO. This to be a first step in defining a strategy for the UK to be a world class market in which to create and build brands.

## 2.4 Brands and growth

To reinforce our view that branding is relevant to any review focused on growth, we look at the IP Review's key themes and the relevance of branding to them:

### ***Entrepreneurialism***

Branding is consistent with entrepreneurialism, as it communicates the relevance and value of a commercial proposition succinctly and effectively to consumers, differentiates an enterprise from its competitors, generates loyalty and provides a strong asset on which to build future innovation. Examples include start-ups in recent decades such as **Dyson** electrical products, **Innocent** drinks, **Green & Black's** chocolate and **lastminute.com** travel.

### ***Economic growth***

Branding contributes directly to economic growth in a number of ways:

Growing new markets – Marketing communication translates new inventions, innovations and technology into terms that are meaningful and deliver value to consumers. The resulting reputation increases consumer confidence in taking up new ideas and new ways of living and working, significantly reducing the risk of the

unknown. Examples include the **Apple iPod, iPhone and iPad**; the **Mars** bar which created the chocolate bar category and moved subsequently into ice cream (the first chocolate countline to do so); and **Febreze** fabric refresher that also created a new category and later diversified into allergen reducers, air fresheners and candles.

Growing existing markets – branded products continually innovate to remain relevant and sustain competitive advantage and, in doing so, grow categories. For example, **Finish** dishwasher tablets have continually evolved, most recently with Max in One, All in One and Quantum, to help grow this category to a value of £200 million. **Olay**, originally a WWII burns treatment, launched new **Olay Regenerist** variants that contributed to 90% growth of its category in 2007-8.

Helping companies enter new sectors – a strong reputation in one sector may provide a springboard for diversification, helping companies move into totally new sectors. For example, **Caterpillar** used its strong reputation in earth-moving equipment to move into rugged consumer fashion. The ability for companies to license and franchise the IP rights that underpin their brands provide the foundations for such diversification, delivering significant economic value in the process.

The ability to license IP rights further drives growth by allowing companies to maximise returns from their brands, for example through merchandise. We do not have figures for the size of the brand licensed market in the UK but the value of licensed product in Western Europe is estimated at \$32.9 billion.<sup>7</sup>

Helping companies achieve scale – Franchising, underpinned and enabled by IP rights, allows companies to achieve scale and expansion domestically and into overseas markets that may be impossible through organic growth. Examples include **Burberry, Karen Millen, Monsoon, Accessorize and Oasis**. The UK franchise Industry in 2010 was estimated to be worth £11.8 billion, comprising 842 business units and employing 465,000 people (39% of franchise owners being women).<sup>8</sup>

## 2.5 Brands and innovation

*"There is a paucity of empirical study in this area...and.. no conclusions to be drawn at this stage regarding the link between trade marks and innovation, but I've seen enough evidence in the early running to say that trade marks are incredibly important in the innovative process.*

*Stuart Graham, chief economist of the USPTO*

While there may be continuing debate about the contribution of trade marks to innovation, there is increasing recognition of their value. Furthermore, studies into the relationship between branding and innovation throw further light on this relationship.

A study by consultancy PIMS (already submitted to the IP Review team) shows that branding, at least in consumer goods sectors, provides a positive stimulus for innovation (which is in turn positive for productivity and positive for economic growth). This is attributed partly to a competitive stimulus and partly to the ability of companies to earn a

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<sup>7</sup> EPM Communications Inc, The Licensing Letter

<sup>8</sup> BFA/Natwest Franchise Survey 2010

return from their investments through branding (and, by inference, through the IP rights that make branding possible).<sup>9</sup>

### **Commercial innovation**

The Call for Evidence invites input on the extent to which the IP system promotes innovation and growth and how it could do so more effectively. Recognising that brands are reliant on IP rights, work by PIMS throws light on this.

The 1998 PIMS study “of brands and growth” found that:

- branding in consumer markets boosts competitive innovation;
- branded businesses invest more in innovation, which is strongly associated with business growth and employment growth; and
- successful brands must deliver improving value to consumers through innovation, if they are to continue to prosper.

This work was updated in 2004 in the study “Brands, innovation and growth” mentioned above. This found that, through their brands, companies were better able to communicate with end users with the result that they:

- grew better as a result of innovation advantage;
- gained a greater private return on innovation; and
- showed a better productivity return from investments in innovation.

Furthermore, the study found that the impact of value added per employee as a result of higher investment in R&D is approximately double that of industry as a whole, creating the incentive to increase the level of innovation and providing funds for further innovation.

### **3**

#### **Barrier to growth**

No government study has been undertaken into the contribution of branding to innovation, while privately-funded studies indicate significant effects.

#### **Recommendation**

The PIMS analyses (1998 and 2004) provide a strong hypothesis for understanding drivers for innovation in other sectors beyond fast-moving consumer goods (FMCG). The review to call for the analyses to be extended to other sectors, identifying those where branding may deliver similar effects.

### **Social innovation**

We have already touched on the effect of branding in stimulating investments in areas of social responsibility. Through their brands, companies are incentivised to “do the right thing”, in turn stimulating investments in innovation in areas such as sustainability.

Product-specific examples include investment by **Coca-Cola** in reducing the weight of its glass bottles by 20%, the **Ariel** “Turn down to 30” initiative which saved some 60,000

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<sup>9</sup> PIMS, “[Brands, Innovation and Growth](#)” (2004) and British Brands newsletter, “[Brands, Innovation and Growth](#)” (2004)

tonnes of CO<sub>2</sub> emissions and the development by **Dulux** of its **Ecosure** product that delivers on both sustainability and performance.

Social innovation also plays a crucial part in delivering challenging initiatives linked less directly to product performance, such as “Water of life” from **Diageo**. Launched in Africa in 2006, this programme aspires to extend access to clean water to 1 million new people in Africa every year through 2015.

Branding represents a positive force for social innovation, with IP rights playing a crucial role by underpinning investments in reputation.

### 3 Brands and the IP legislative framework

We have stated that the UK framework of IP rights generally works well in both on and offline markets (section 2.2). It lays down common principles that apply across business and commerce, irrespective of platform or business model. This adaptability has developed over many years in other countries too, providing a high level of consistency and certainty. In general, the greatest scope for improvement lies not in amending the framework but in making enforcement more effective. However there is one notable exception – the inadequate provisions in the UK to tackle parasitic trading (see below).

While the legislative framework may remain generally fit for purpose, the nature of the modern marketplace, strongly influenced by new technology, is such that there is now a pressing need for:

- faster, more cost-effective ways to protect rights;
- more effective use of existing interim and long-term measures to deal with infringers, both criminal and civil;
- more international collaboration to improve enforcement of the law.

These matters do not affect the substantive UK IP rights themselves but are important to protect brand value.

#### 3.1 Misleading “parasitic” packaging



A current example of a familiar branded product and a competitor in similar packaging

Parasitic copies trade on the reputation of familiar products while carefully avoiding blatant infringement of exclusive rights. Consumers are hampered in making informed decisions, may buy products by mistake and face higher prices (as the copy benefits from

a higher reputation than it warrants). In economic terms, the copy free rides on the familiar product which is deprived of its return on investment, faces increased costs and loses its all-important distinctiveness. A detailed account was given to the [Gowers Review](#) (See pages 46-50 and annexes 7-9).

There is some important historical background to note:

- UK legal remedies against parasitic copying are often ineffective and are out of step with most other Member States (unfair competition laws provide effective redress while passing off does not);
- The problem was first raised in Parliament in 1994, seventeen years ago;
- The Gowers Review concluded five years ago that “passing off does not go far enough to protect many brands and designs from misappropriation” (paragraph 5.84), recommending that the Unfair Commercial Practices Directive be given a chance to work, with government consulting if it proved ineffective (Recommendation 37);
- While this Directive (implemented in the UK as the [Consumer Protection from Unfair Trading Regulations](#) (CPRs) in 2008) states misleading packaging is unlawful (see in particular clause 5 and Schedule 1, clause 13), it is not enforced in the UK (companies were not given rights of civil action and the authorities with duties to enforce in practice do not do so due to lack of resource and other priorities);
- government, aware of enforcement concerns during the Parliamentary process, promised a review in 2010. This has not materialised. However the IPO has commissioned a study, due for completion in summer 2011.

Legitimate competitors need effective tools to redress parasitic copying. The desired remedy is for copiers to be required to re-package products quickly. This would restore fair competition, maintain consumer choice, preserve the all-important distinctiveness of branded products and allow consumers to make informed decisions.

Since the Gowers Review, a significant [study](#) has been undertaken into the consumer impact of parasitic packaging on consumers. A dossier of examples on the market in 2010 is available on our [website](#) and a comparative analysis of legislative provisions in Member States (which indicates the UK’s shortcomings) is available on request. The European Commission is also looking into the practice and has commissioned a study.

#### **4**

##### **Barrier to growth**

The UK lacks effective remedies for companies to take action against parasitic trading that feeds off the reputation of familiar branded products.

##### **Recommendation**

The review to call on Government to condemn publicly the practice of parasitic copying and to consult on appropriate remedies without delay. It should also contribute to the work being undertaken by the European Commission.



## 4. Brands, counterfeits and the enforcement regime

At ACG's meeting with Professor Hargreaves (as a member of the deputation from the Alliance against IP Theft) on 16<sup>th</sup> February 2011, he explained that there was as yet no evidence to suggest that trade marks pose any barrier to innovation or growth. With nothing concrete before us to prove or disprove, perhaps the most helpful approach is to identify the barriers we see in IPR enforcement to successful innovation and growth, with particular reference to the branded goods industries, and propose next steps or solutions, as appropriate.

### 4.1 Introduction and context

In light of the significant contribution made by brands to the UK economy (see Section 2), it follows that product counterfeiting, a direct attack on brands, poses a significant barrier to that contribution being fully made, and to the continuing growth of the market for legitimate manufactured goods in the UK.

Counterfeiting is a serious organised crime recognised as such by the Home Office and the Serious Organised Crime Agency (SOCA)<sup>10</sup> with links to other such crimes on a global scale.

The UK is one of the largest consumer markets for fakes per capita in the world (the largest producers of counterfeits being in the Far East and other developing countries). We are known internationally as 'Fake Britain' which does not help our status generally on the world stage.<sup>11</sup>

Counterfeiting has three main areas of impact in the UK:

- loss to the economy and the Exchequer;
- consumer harm;
- links to other serious organised crime.

The first area of impact is of most relevance to the scope of this Review. Not only is it of great importance in its effect on national prosperity, an unsafe shopping and trading environment also affects consumers' and retailers' confidence, other essential elements for a successful and expanding economy.

In order to illustrate the scale of the problem, we have taken two different examples of where counterfeiting is rife:

#### SCALE - CLOTHING AND FOOTWEAR

The British fashion industry is among the most successful of our manufacturing industries, with an international influence, and great reputational value for the UK – an industry currently said to be worth £37 billion to the British economy and one of our largest employers. It also happens to be one of the sectors most targeted by counterfeiting.

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<sup>10</sup> <http://www.soca.gov.uk/about-soca/library>

<sup>11</sup> <http://www.independent.co.uk/life-style/fashion/features/fake-britain-the-rise-of-the-imitation-industry-462571.html>

This industry is very active in supporting its start-up businesses, mainly designers, with funding and awards, aiming to help create successful brands. The chair of the British Fashion Council states that (a) more British-based manufacturing is developing in this sector, generating more innovation and growth, but (b) more is needed to support these new businesses – from education, to financial expertise, access to funding and export.<sup>12</sup>

In order to give some idea of the scale of the threat posed by counterfeiting to this valuable industry sector, the headline results of an independent consumer survey into the whole clothing and footwear sector (which also includes e.g. sportswear, as well as fashion goods) are:

Total UK spend, just on clothing & footwear fakes per annum **£3.009 billion**  
(cost to the Exchequer around £800m in lost tax revenues)

Cost to UK industry and retailers per annum **£3.482 billion**  
(i.e. what consumers would have spent on genuine products, if fakes not available  
e.g. a genuine M&S handbag for the £25 it cost to buy a fake plastic Gucci)

The UK clothing and footwear market was worth an estimated £46.05 billion in 2009, accounting for 5.3% of total consumer spending. The value of the legitimate clothing & footwear market in the UK is around £50 billion p.a. so these counterfeit purchases represent over 6.5% of the market.<sup>13</sup>

The research also shows that, in this industry sector:

- one in four of the UK population have knowingly bought fake clothing or footwear in the past year (44% in the past three years);
- although fake clothing & footwear are largely made overseas, three-fifths of the respondents had bought the majority of their fake goods in the UK.

## SCALE - THE INTERNET

The internet is a fantastic growing retail market for branded goods, increasingly the preferred consumer choice for access to and delivery of such goods. For example, on Christmas Day 2010 it was estimated that online sales were up 29% on the previous year to £132 million, with Boxing Day sales at £281 million<sup>14</sup> with record sales the previous Christmas too.<sup>15</sup>

Brands are also increasingly using social networking sites and other innovatory viral services such as YouTube to reach their markets (see section 4.4.1).

Unfortunately, the internet is also a growing source of counterfeits: according to the same consumer survey for clothing and footwear above, over a third of those who buy fakes do so via online auction sites such as eBay. The Google AdWords facility is another conduit for counterfeits (see section 4.4.2).

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<sup>12</sup> <http://www.conservativebusiness.co.uk/home/london-fashion-week/11>

<sup>13</sup> [http://www.just-style.com/market-research/clothing-footwear-industry-2010\\_id93790.aspx](http://www.just-style.com/market-research/clothing-footwear-industry-2010_id93790.aspx)

<sup>14</sup> <http://www.imrq.com/ImrqWebsite/User/Pages/PressReleases.aspx?pageID=85&parentPageID=0&itemID=367&pageTemplate=7&isHomePage=false&isDetailData=true&specificPageType=5>

<sup>15</sup> <http://www.netimperative.com/news/2009/january/christmas-day-3.8m-brits-spent-a3102m-online>

Another growing trend is for whole websites to be fake, as well as selling counterfeit goods. Well-known brands such as UGG ® Australia have a very proactive strategy for dealing with such illegal sites, which both use their trade marks in the domain name, and sell counterfeit versions of their products.<sup>16</sup> The report on their enforcement activities in 2010 makes instructive reading - see their press release.<sup>17</sup>

We believe that digital online businesses need to be as vigilant as brand owners in fighting this kind of sabotage, particularly as their new sites and services become successful mature enterprises, more worth attacking. So we will examine the enforcement issues for brands on the internet in more detail below, which will also feed in to issues around international enforcement.

#### INTERNATIONAL CONTEXT

Nowhere better is the need for coherent collaborative international enforcement highlighted than in the statistics published each year by the EU Commission (DG TAXUD) which show that millions of fake products are seized by EU customs at EU borders – but customs also estimate that this is only about 3% of what is on the market.<sup>18</sup>

The EU contains many of the destination countries for fakes, while the source countries shown in these statistics are mainly Far East or other non-EU locations.

The Organisation for Economic Co-operation & Development (OECD) estimates that the value of the cross-border worldwide trade in fakes is in excess of \$250 billion annually (this excludes domestically produced and internet fakes).<sup>19</sup>

The recent Global Congress in Paris<sup>20</sup>, organised by the World Intellectual Property Organisation (WIPO), Interpol and the World Customs Organisation, shows the prominence which these bodies now give to '*the growing menace associated with internet trade and... nurturing respect for IP... to find sustainable solutions that take account of the role and rights of stakeholders, as well as the cost to them, of fighting counterfeiting and piracy*'<sup>21</sup>. The outcomes from this Congress are awaited and can be forwarded when available.

Interpol has reported both to the US government and to the EU Commission that it has tracked profits from counterfeiting, via sophisticated money-laundering, to Middle East terrorist organisations.<sup>22</sup> The report to the US House Committee on International Relations is available in hard copy and referenced by Interpol's press release here, with some further context offered by a press article.<sup>23</sup> (Interpol's later report to the EU Commission is not publicly available as far as we know.)

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<sup>16</sup> [http://www.uggaustralia.co.uk/counterfeit-education/counterfeit-edu.en\\_GB.pg.html](http://www.uggaustralia.co.uk/counterfeit-education/counterfeit-edu.en_GB.pg.html)

<sup>17</sup> <http://www.deckers.com/investors/PressReleaseText.asp?compid=91148&releaseID=1514384>

<sup>18</sup> [http://ec.europa.eu/taxation\\_customs/customs/customs\\_controls/counterfeit\\_piracy/statistics/index\\_en.htm](http://ec.europa.eu/taxation_customs/customs/customs_controls/counterfeit_piracy/statistics/index_en.htm)

<sup>19</sup> [http://www.oecd.org/document/23/0,3343,en\\_2649\\_34173\\_44088983\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/23/0,3343,en_2649_34173_44088983_1_1_1_1,00.html)

<sup>20</sup> <http://www.ccapcongress.net/>

<sup>21</sup> [http://www.wipo.int/pressroom/en/articles/2011/article\\_0001.html](http://www.wipo.int/pressroom/en/articles/2011/article_0001.html)

<sup>22</sup> <http://www.interpol.int/Public/ICPO/speeches/SG20030716.asp>

<sup>23</sup> <http://www.interpol.int/public/icpo/pressreleases/pr2003/pr200319.asp>;  
[http://www.timesonline.co.uk/tol/news/uk/article432410\\_ece](http://www.timesonline.co.uk/tol/news/uk/article432410_ece);

This suggests not only that the serious money made by the fakers does not benefit the economy which hosted the crimes, but that it actively supports other serious organised criminal activities.

#### 4.2 The evidence

How to evidence the economic impact of counterfeiting has long been a challenge for experts around the world which, despite best efforts, has still not been fully met. We refer here to the most recent studies and reports available.

Effective protection and enforcement of IP rights are key to the UK's prosperity and our evidence shows:

- (1) how IP protection and enforcement supports innovation and growth;
- (2) how IP crime (counterfeiting and piracy) impacts on the economy.

#### INTERNATIONAL CHAMBER OF COMMERCE (ICC)

There is strong evidence of the importance of an effective IP framework to support both innovation and growth. Most recent is a report entitled **Intellectual Property: Powerhouse for Innovation and Economic Growth**<sup>24</sup> published online by the ICC on 3<sup>rd</sup> February 2011.

As the 'knowledge economy' advances, more and more of the value that firms and the overall economy achieve will come from high value-added intangibles – including IP in inventions, brands and works. In many companies even now, 80% or more of their market value is attributable to intangibles, including IP. In some small companies, the only value is the intellectual property they own in an exciting innovation that they have developed. IPR has truly become an 'intellectual currency' helping to promote economic growth, company competitiveness and innovation world-wide. *Report page 2*

This report is the result of collaboration between two ICC initiatives:

BASCAP (Business Action to Stop Counterfeiting & Piracy)<sup>25</sup> was formed in 2004 to take a leading role in the fight against counterfeiting and piracy, mobilising industry across all affected sectors, pooling resources and expertise and working closely with governments and law enforcement, to raise awareness of the issues and respect for IP.

The ICC's Commission on Intellectual Property contributes world business views to governmental and intergovernmental debates on key IP issues facing the international business community.<sup>26</sup>

The report explores the benefits of IP protection in strengthening national economies, driving innovation and technology, fostering new ideas, and enhancing society and culture. It is essential reading in the context of this question.

For example, it quotes the fact that IP protection is identified in World Economic Forum (WEF) surveys as:

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<sup>24</sup> [Intellectual Property: Powerhouse for Innovation and Economic Growth](http://www.iccwbo.org/bascap/id1127/index.html)

<sup>25</sup> <http://www.iccwbo.org/bascap/id1127/index.html>

<sup>26</sup> <http://www.iccwbo.org/policy/ip/id2465/index.html>

*"one of the key national 'institutions' within which individuals, companies and governments interact to generate income and wealth in the economy. As ICC has noted in the past, the countries that are perceived as having the strongest intellectual property protection are routinely found to be among the most economically competitive countries in the WEF surveys. Those perceived as having the weakest IPR systems tend to rank among the bottom for growth and competitiveness."*

As it also reports, the WEF has found that:

*"The quality of institutions [which include intellectual property] has a strong bearing on competitiveness and growth. It influences investment decisions and the organization of production and plays a central role in the ways in which societies distribute the benefits and bear the costs of development strategies and policies. For example, owners of land, corporate shares, or intellectual property are unwilling to invest in the improvement and upkeep of their property if their rights as owners are insecure."*

Foreign Direct Investment (FDI) is important for growth, and there is evidence that it is directly influenced by the strength of a country's IP protection. The report refers to an extensive data survey by the Organisation for Economic Cooperation and Development (OECD) of a range of 120 countries classified as developed, developing or least-developed, covering the fifteen-year period 1990-2005. The study involved a regression analysis of the relationship between various measures of technology transfer and a set of indexes that quantify the strength of IP rights, whilst controlling for other factors. The results of the study showed a positive correlation between the strength of IP rights and FDI<sup>27</sup>.

The OECD's Trade & Development library contains a presentation delivered by one of its senior economists – Douglas Lippoldt – to a meeting in Paris in November 2010, where it is suggested that a 1% increase in protection for trade marks results in a 3.8% increase in FDI<sup>28</sup>.

Mr Lippoldt has published many other interesting and relevant papers on the relationship between IPR protection and economic development and seems to be convinced that intellectual property matters for economic development, whether in mature or in developing economies:

*"Based on more than a decade of experience, the empirical evidence indicates that an appropriate degree of IPR protection does help to deliver access... to goods, services and FDI from abroad, as well as boosting domestic innovation."<sup>29</sup>*

## FURTHER EVIDENCE

The other important body of evidence we wish to refer to relates to the economic impact of IP crime, which undermines legitimate business, puts consumers at financial risk and deprives national exchequers of revenues. It follows from this that long-term lack of

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<sup>27</sup> <http://www1.american.edu/academic.depts/cas/econ/faculty/park/Web%20Page%20Update%2010-08/Tech%20Transfer%20w-Doug%20Lippoldt.pdf>

<sup>28</sup> [http://www.stockholm-network.org/downloads/meetings/Lippoldt\\_IP\\_Academy\\_Ankara\\_Nov\\_2010.pdf](http://www.stockholm-network.org/downloads/meetings/Lippoldt_IP_Academy_Ankara_Nov_2010.pdf)

<sup>29</sup> [http://gem.sciences-po.fr/content/publications/pdf/Lippoldt\\_Stronger\\_IPRs12102010.pdf](http://gem.sciences-po.fr/content/publications/pdf/Lippoldt_Stronger_IPRs12102010.pdf)

effective enforcement in the UK undermines both innovation and economic growth, by allowing the threat posed by IP crime to continue, and increase, unchecked.

Several of the factors determining economic growth have a close relationship with enforcement standards – especially confidence both in the rule of law and in the effectiveness of its protection, which (among other things):

- encourages certainty for investment and business development;
- fosters consumers' ability to rely on the quality and availability of products and services and thereby stimulates the marketplace;
- helps to create a safe environment for legitimate business and consumers;
- sends the right message, that IP is valuable and attacks upon the rights of IP owners are unacceptable.

Economic growth requires, among many other things, investment and planning. Neither of these is encouraged if it is uncertain whether all kinds of valuable rights in an enterprise will be protected, and that the rule of law will be generally respected, in a given country.

A new Global Impacts Study conducted by Frontier Economics has just been published by BASCAP, examining the global economic and social impacts of counterfeiting and piracy.<sup>30</sup>

OECD produced a detailed study and report in 2007, which attempted to estimate the value of the cross-border trade in fakes worldwide.<sup>31</sup> This excluded:

- the value of domestically produced and consumed counterfeit products;
- the value of digital piracy; and
- impacts on society, governments and consumers.

The OECD study originally concluded that international trade in counterfeit and pirated goods could have been as much as \$200 billion in 2005.

An update was issued in November 2009<sup>32</sup> based on the growth and changing composition of trade between 2005 and 2007. It was suggested that counterfeit and pirated goods in international trade grew steadily over the period 2000-2007 and could amount to up to \$250 billion in 2007.

The new BASCAP report draws out the additional impacts which were left unquantified in the OECD report, introducing methodologies for estimating the magnitude of these additional cost categories. It projects forward the magnitude of the problem of counterfeiting and piracy to 2015, and provides a starting point for future analytical work.

Link to [Executive Summary](#)

Link to [Full Report](#)

The key findings of the report, based on 2008 data, are:

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<sup>30</sup> <http://www.iccwbo.org/bascap/index.html?id=40991>

<sup>31</sup> [http://www.oecd.org/document/4/0,3746,en\\_2649\\_34173\\_40876868\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/4/0,3746,en_2649_34173_40876868_1_1_1_1,00.html)

<sup>32</sup> [http://www.oecd.org/document/23/0,3343,en\\_2649\\_34173\\_44088983\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/23/0,3343,en_2649_34173_44088983_1_1_1_1,00.html)

- the total global economic value of counterfeit and pirated products is as much as \$650 billion every year;
- international trade accounts for more than half of counterfeiting and piracy (the updated estimate is \$285 billion to \$360 billion);
- domestic production and consumption accounts for between \$140 billion and \$215 billion;
- digitally pirated music, movies and software accounts for between \$30 billion and \$75 billion;
- counterfeiting and piracy are estimated to cost G20 governments and consumers over \$125 billion every year;
- approximately 2.5 million jobs have been destroyed by counterfeiting and piracy;
- online IP crime has grown substantially over the last decade, to the point where it now accounts for between 6.5% and 12% of the total value of counterfeit and pirated products consumed.

There are also impact projections to 2015, not reproduced here, which indicate that, whether or not legitimate economies grow, counterfeiting will probably remain a growth industry for some time yet.

ACG contributed to the UK-specific case study in this new report (see page 41 onwards of the report). Mexico was the other selected country.

Applying their methodology to four chosen sectors (luxury goods, food and beverages, pharmaceuticals, software) in the UK, and then extrapolating to the total UK economy, Frontier Economics reports that:

- counterfeiting costs the UK government **€4.1 billion** in lost tax revenue and increased welfare spending; this is 2.5% of total Treasury receipts, more than 1½ times what the UK currently spends in total on Customs activity (not just IPR enforcement) and just less than half the UK's overseas aid commitment in 2010;
- **380,000 jobs** are lost in the short run (defined as 'less than a year') with almost **31,000** permanent job losses (due to the impact of counterfeiting on the value of legitimate industry);
- an increase in counterfeiting which raises the UK crime rate by just 1% would increase the economic and social cost of crime in the UK by **€1.7 billion**; this represents more than 80% of total expenditures on the courts service in the UK and almost 5% of total expenditure on the criminal justice system in the UK.

Also interesting, and relevant to the growth issue, is the estimated impact on Foreign Direct Investment (FDI) – across the G20 economies – of concerns about IPR enforcement, leading to lost investment which could give rise to additional tax losses of more than \$6.25 billion.

Just one final point of interest here, specific to the UK: there is ample evidence that – in addition to depriving the Exchequer of millions of pounds in revenues through non-payment of tax<sup>33</sup> (and contrary to a surprisingly frequent claim made by those trying to weaken protection for IP rights), counterfeiters do not spend their profits in the legitimate economy and so do not contribute to its growth.

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<sup>33</sup> tobacco and spirits being two obvious examples

But a weapon exists in the UK which we believe can be used to put many counterfeiters out of business for good, as their profits can be traced, frozen and seized under the Proceeds of Crime Act 2002 (POCA). Its incentivisation scheme currently allows investigators, prosecutors and the courts involved in POCA confiscation proceedings to share in 50% of recovered criminal assets, the other 50% going to the Exchequer. We have examples of individual counterfeiting cases where POCA has been successfully used, but no systematic statistical evidence since this is not available to us.

IP crime is a lifestyle offence under POCA and thus triggers its confiscation proceedings. Swingeing financial sanctions can be imposed on defendants which far exceed the penalty for the original offence, as evidenced by one of the early successes under POCA, where Waltham Forest trading standards obtained a confiscation order for over £330,000 against a convicted counterfeiter, who had only received a fine of £50 for each of the four specimen counterfeiting offences to which he had pleaded guilty. He was given six months to pay or go to prison for five years.

More recently, an Essex trader was given a community service order for the actual offences, but a POCA confiscation order was also made for £300,000. See the case of Lawrence in the list of cases in the 'In Court - Press Releases' section of ACG's website, linked below.<sup>34</sup>

One of the best aspects of POCA is that if the order is not paid within the time specified, the offender will go to prison, with no remission. If he still does not pay on his release, he will go back inside. Without POCA, both these offenders would have walked free following conviction, to continue with their criminal activities unchecked.<sup>35</sup>

This is a potentially huge economic contribution, which can be made by the criminals responsible via the incentivisation scheme, both to resources for enforcement and generally to the UK economy.

Some streamlining of POCA's procedures is required, to speed up some of the processes and ensure that criminal assets are more quickly located and frozen, for example, but we understand that this has already been recognised by the government and is receiving attention, which is most welcome.

Three fine examples, out of many, will serve to illustrate this, and the value of pursuing counterfeiters in order to sequester their criminal gains:

- the case of Braha with an £11 million order under the Proceeds of Crime Act, which started as a UK counterfeiting investigation of fake Burberry items and led to the discovery of a huge VAT carousel fraud in the Caribbean;<sup>36</sup>
- Operation Augusta, the biggest eBay scam yet prosecuted, involving an international ring of golf-club counterfeiters led by a UK man whose assets here were modest and whose millions were invested mainly in the Far East;<sup>37</sup>

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<sup>34</sup> [http://www.a-cg.org/guest/news\\_media/guest\\_newsdesk\\_in\\_court\\_press\\_releases.php](http://www.a-cg.org/guest/news_media/guest_newsdesk_in_court_press_releases.php)

<sup>35</sup> <http://ns1.acgwebsite.net/guest/pdf/POCAcases.pdf> see last page

<sup>36</sup> [http://www.a-cg.org/guest/pdf/10\\_04\\_19\\_brahaPOCA.pdf](http://www.a-cg.org/guest/pdf/10_04_19_brahaPOCA.pdf)

<sup>37</sup> <http://www.dailymail.co.uk/news/article-1255342/eBay-fake-golf-club-scam-gang-face-jail-international-ring.html>



- the case of Lily Lee, head of a UK clothing counterfeiting ring, where, South Yorkshire Police have just informed us, the defendant has recently been ordered to pay a second additional amount of £800,000 or face another 10-year prison sentence, in addition to the £2.3 million which was the subject of the original confiscation order.<sup>38</sup>

## 5

### **Barrier to growth**

Counterfeiting is an economic threat both to industry and to national economies. Increasing use is made of the Proceeds of Crime Act in counterfeiting cases, but more awareness of IP crime being a lifestyle offence is needed to encourage more prosecutions, so that POCA can come into play.

### **Recommendation**

Regarding counterfeiting as an economic crime will help to raise its profile and realise its important place in any national serious organised crime strategy, but particularly, in this context, its usefulness as a trigger for POCA confiscation proceedings. More awareness should be encouraged amongst law enforcement of how POCA can be used in IP crime cases as a means of accessing significant criminal funds. (See Section 5 below for more on how POCA can be used to add economic value to IPR enforcement, making IP crime a worthwhile area of criminality to target more robustly in future.)

## 4.3 Enforcement

In the context of analysing the way in which growth is supported, an important objective of any IPR enforcement framework must be to provide the necessary certainty and stability which derives from the effective rule of law, in order for innovation and economic growth to occur successfully.

Another important objective is to deliver effective sanctions against serious organised criminals, in order to protect growth of legitimate industries, maintain consumer confidence and ensure that government revenues, and ongoing investments in our industries, are not eroded.

For both of these objectives to be achieved, we need a declared policy of nothing less than zero tolerance, in order to provide the necessary deterrent, while also ensuring that in practice enforcement responses are proportionate.

In practice this policy may not be wholly deliverable, but the message being sent, to the consumer of fakes and the criminal alike, must be clear and unequivocal, as must government's position as a champion of IP-rich industries.

IPR enforcement falls into two categories in relation to brands:

- enforcing the criminal provisions of the Trade Marks Act 1994; and
- civil enforcement of individual IP rights, which also has a European dimension with the Enforcement Directive.

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<sup>38</sup> [http://www.rart.gov.uk/North+East+Rart/News/2010/NE\\_News\\_2011.htm](http://www.rart.gov.uk/North+East+Rart/News/2010/NE_News_2011.htm)

#### 4.3.1 Criminal IPR enforcement

We have recently become aware of a view within official circles connected with the management of IP in government that *'legitimate trade and commerce (in both the online and physical worlds) should not be hampered by overly restrictive enforcement'*.

This came as a surprise, as it is the reverse of the policy which we would expect to prevail, to achieve the right balance of interests which need to be struck in IPR enforcement – namely the interests of the legitimate rights holder and the consumer, versus the interests of serious organised criminals.

We have not seen any indication of what might be regarded as 'overly restrictive' nor an example of the undesirable effects enforcement may have on legitimate enterprises.

So we are not aware of any evidence which indicates that any given level of enforcement does in fact 'hamper' business. On the contrary, all the available evidence indicates that counterfeiting has a serious economic impact, and that levels of enforcement are inadequate, and that this is what is hampering enterprises, whether online or offline, established or new, involving digital or physical products.

'Compliance' is a term more applicable to regulatory or certain civil offences, but neither the criminal offence of counterfeiting, nor civil IPR infringements, are regulatory in nature. (This may be an example of the way IP crime is characterised because trading standards is the lead agency for enforcing the relevant laws - see Section 5 below).

By the same token, in terms of promoting economic growth, 'compliance' cannot be just at 'an acceptable level', nor would deterrence work if only 'blatant' infringements were actionable.

We recognise that practicalities dictate a level of selectivity in which cases to prosecute or pursue. No enforcement agency could hope to take action against every suspect, in any field of criminality. In the same way commercial realities limit rights holders' ability to sue every infringer. The EU Enforcement Directive (Dir 2004/48/EC) is similarly limited to counterfeiting 'on a commercial scale'.

But the necessary conditions for promoting economic growth must include maximum certainty and confidence in the rule of law and a policy, if not a practice, of zero tolerance by the authorities.

Unfortunately the intangible nature of IP rights tends to make law enforcement and the courts less ready to treat the issue of criminal IPR infringement as seriously as theft of tangible property. Brand owners regularly experience lack of prioritising or resourcing of counterfeiting issues by law enforcement, and inconsistent – and often lenient – sentencing by the criminal courts (a maximum of 10 years being available) which tends not to reflect the damage caused by IP crime.<sup>39</sup>

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<sup>39</sup> ACG has numerous examples of such cases on its website  
[http://www.a-cg.org/guest/news\\_media/guest\\_newsdesk\\_in\\_court.php](http://www.a-cg.org/guest/news_media/guest_newsdesk_in_court.php)

In terms of policy, even the slightest hint that 'a little bit of counterfeiting is OK' sends a wholly wrong message to the serious organised criminals who control the global online or offline trade in fakes.

Similarly, consumers who make up the huge market for fakes – none bigger than in the UK – need to understand the seriousness of the problem and where their money goes (into the pockets of criminals) which has been shown to have a dramatic effect on their attitude to fake-buying. The link to other serious organised crime is now the number one deterrent for consumers from purchasing fakes.<sup>40</sup> Some believe that more of a deterrent is needed, though, and that consumers should be subject to penalties for buying fakes, as they are in France and Italy, for example.

So far this has not been a road which the UK government has wished to travel. While it might be difficult to enforce consistently (as are all such measures e.g. speeding) it is arguable that this kind of penalty could offer a level of deterrence similar to that which operates in the public mind in relation to stolen goods.

Consumer attitudes will ultimately determine whether the market for fakes remains viable or not, as many surveys have established.<sup>41</sup> Coupled with increased attention to enforcement standards in source countries (see section 4.5.1) this would offer a more effective strategy for combating counterfeiting than is currently available, and address both ends of the economic threat at the same time.

The concept of selective IPR enforcement, in order to concentrate available resources on particular sectors, was promoted last autumn in a study relating to the UK by Prof David Wall - "*JAILHOUSE FROCKS: Locating the public interest in policing counterfeit luxury fashion goods*" (with Joanna Large) – in which he claims that limited resources should mean that only safety-sensitive counterfeits – which would be directly of public interest – should be included in the UK's IPR enforcement remit.<sup>42</sup>

He also welcomed the choice of goods offered to consumers by the black market.

He reached this surprising conclusion without consulting either industry or law enforcement, and chose one of the most innovative and successful UK industry sectors, which is also most under attack in the UK from counterfeiting, to exclude from IPR enforcement.

Selective enforcement is misguided. Counterfeiters do not limit themselves to one industry sector – they fake anything which offers a quick profit, moving between sectors or faking several different kinds of product at the same time – and it would be impossible to ignore certain products in a warehouse, say, and only seize others, with millions of items involved.

Given the established evidence that a single criminal gang will produce and distribute fake alcoholic drinks, clothing and footwear and DVDs, in order to fund other serious

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<sup>40</sup> <http://today.yougov.co.uk/consumer/fakes-and-funding>

<sup>41</sup> <http://www.iccwbo.org/bascap/index.html?id=33865>

<sup>42</sup> <http://bjc.oxfordjournals.org/content/50/6/1094.abstract> (we do not have a link to the full study but understand that the IPO has a hard copy, or we can provide a further copy if required)

organised crime, Prof Wall's argument on that basis alone is not only wrong – it is dangerous.<sup>43</sup> [Note: The detailed information we would like to include about the IRA's use of counterfeiting profits to fund their terrorist activities is classified - Police Service of Northern Ireland, IP Crime Specialist Unit.]

He has also mistakenly pronounced, with no evidence to support his claim, that counterfeiting promotes the genuine brands which are under attack '*by quickening the fashion cycle and raising brand awareness*'. The owners of genuine brands would naturally prefer to decide how awareness of their brands is raised, and strongly refute this theory; no one is better placed to confirm the kind of brand damage caused by counterfeiting than the brand owners themselves.

An example of a successful criminal case last year (2010) may be instructive to illustrate the extent of this misconception – Operation Blackout, on which the BBC reported in March 2010, when the City of London Police infiltrated the UK end of an international criminal gang and seized over £3million-worth of clothing and footwear fakes, just in one operation.

If Prof Wall were in charge of our IPR enforcement, this operation would not have taken place and these serious organised criminals would still be at large.<sup>44</sup> It is worrying, though, that some credence seems to have been given to his unsupported theory in certain official quarters.

## 6

### **Barrier to growth**

Insufficient judicial awareness, and low level of understanding in Westminster as a whole, of the nature and extent of IP crime. Understanding in these fora of the realities of IP crime is patchy and the outcomes of court cases, and serious organised crime strategies, vary greatly as a result. Tendency to embrace unsupported counter-arguments misrepresenting the nature and scale of the problem while putting rights holders to strict proof.

### **Recommendation**

Extend judicial training, raise awareness within government, industry to partner law enforcement and government, starting with dialogue e.g. in more roundtables and conferences, to improve understanding, share information and establish shared objectives.

<sup>43</sup> <http://www.nio.gov.uk/buying-fakes-funds-criminality-goggins/media-detail.htm?newsID=14828>

<sup>44</sup> <http://news.bbc.co.uk/1/hi/england/london/8576880.stm>

#### 4.3.2 Civil enforcement

Judicial understanding of the importance of IP rights in civil courts is considerably greater than in the criminal justice system and our system of civil litigation is mainly criticised for its relatively high costs. Unlike many other territories in Europe, litigation costs in the UK are a deterrent to pursuing cases to full trial.

Recently, the Woolf reforms and judicial attitudes to costs are helping to foster a more cost-conscious and cost-effective approach to IP civil litigation. Mature businesses seek to enforce their IP rights in any jurisdiction where they are infringed, but equally any action has to be assessed in the context of costs. The evidence is that the UK is a particularly expensive jurisdiction in which to litigate.

The new Patents County Court is likely to assist, with a more streamlined procedure, for claims whose value falls within the threshold. We understand that, after a recent consultation, this threshold will be set at £500,000, and implemented in two stages: first in relation to disputes within the court's 'special jurisdiction' i.e. patents and designs, and then shortly afterwards in relation to copyright and trade marks issues, its ordinary jurisdiction, with a post-implementation review in 2014.<sup>45</sup>

These recent reforms of the Patents County Court may well provide SMEs with more cost effective means of enforcing their IP rights than have been previously available, with hands-on case management by the court. SMEs would also benefit from easier access to cost effective IP advice and mediation services.

A report commissioned by the now defunct Strategic Advisory Board for IP and published by the IPO in October 2010<sup>46</sup> details the results of online and telephone surveys of SMEs, as well as reviews of patent and registered design cases between 2003 and 2009:

- Over 80% of the 1858 small firms contacted rated IP as important to their business;
- Approximately 25% of the firms had been involved in an IP dispute in the past 5 years;
- However, 75% of firms did not have insurance to help meet the costs of IP disputes, stating high costs as the main reason;
- The IP disputes were as likely to be with firms of a similar or smaller size as they were to involve larger firms. An exchange of letters between solicitors was by far the most common solution tried, resolving the dispute in approximately 40% of cases;
- High level negotiation between firms was used in a third of the cases, but other methods such as mediation, use of the UK-IPO, small claims or county courts were rarely used;
- Only 13% of disputes ended up in the High Court. A significant proportion of listed patent cases - approximately 50% - involved UK versus foreign firms and settlement occurred in about 40% before trial;
- Whilst SMEs and larger companies had similar success rates, micro firms had a marginally lower success rate, especially if the micro firm was a claimant. Micro firms were also more likely to settle before trial.

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<sup>45</sup> <http://www.ipa.gov.uk/consult-2010-pcc.htm>

<sup>46</sup> <http://www.ipa.gov.uk/ipresearch-ipenforcement-201010.pdf>

#### 4.4 The online environment for brands

We agree with many others who are of the view that 'the digital age' is no different, in terms of the required legal framework, to what was needed before the eCommerce and technology boom – the point is to make it work better in some respects.

We would like to endorse, in particular, the eminently sensible evidence given to a roundtable seminar about this Review, organised by the Institute for Public Policy Research on 26<sup>th</sup> January 2011 (which was sponsored by Pearson and Google and attended by members of the IP Review Panel) by digital media legal expert Laurence Kaye, who has been practising in this field since the mid-90s.<sup>47</sup>

Our current IP framework achieves a balance between:

- (1) the exclusive rights in original ideas, inventions, works and products which are protected by IP law (be that a design, film, new cancer drug, computer game, piece of music, sports broadcast or item of clothing);
- (2) freedom of contract for the creators and producers as to how their work is transferred, licensed and used; and
- (3) availability at a fair price; in a mature democracy such as the UK, the price has long been determined by market forces largely through competition and consumer behaviour.

We already have well-established principles by which business and consumers relate, to their mutual benefit, and the advent of a new medium via which commerce is conducted does not automatically mean tearing up the existing framework.

However, because of the scale and speed of the technology and the level of anonymity enjoyed by its criminal fraternity, we do need certain changes to deal more effectively with online criminality of all kinds, and in particular for IP crime:

- faster, less expensive ways to protect and license rights;
- more international collaboration to enforce the law;
- less focus on prosecution, more on asset recovery;
- development of counter-attacking cyberspace techniques, including more use of available forensic internet investigative technology.

Solutions like these will ensure (a) that fair commercial practices are in place online as well as offline, and (b) that quicker responses are possible for consumer protection and enforcement of IP (and other) rights. But these are all practical issues or processes, and do not involve changing the structure of the IP framework.

##### 4.4.1 Brands and eCommerce

Brands have started consciously to reach out to a young digitally attuned demographic who grew up with the Internet. Digital is now at the heart of everything some companies do, and not only as an eCommerce channel.

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<sup>47</sup> <http://ipkitten.blogspot.com/2011/01/hargreaves-review-debate-begins.html>

If Facebook were a country it would be the third largest in the world behind China and India, so it makes sense for brands to have a presence there. Twitter is another communication channel for individuals representing the brands to make contact with their markets, and YouTube can also be used, to showcase new products for example.

In 2009 Burberry went one further, launching their own social networking site [artofthetrench.com](http://artofthetrench.com) (with over 11 million page views to date). The site showcases the universal appeal of the iconic Burberry trenchcoat, encouraging Burberry fans to take part by posting photographs of themselves in their own trenchcoats.<sup>48</sup>

The Review's focus on eCommerce should therefore extend beyond platform internet businesses and new digital start-ups:

- the internet is important to both established and new brands, as a means (a) to reach the consumer and deliver products and (b) to advertise and promote brand value;
- brands as signifiers of origin are even more at risk in the online environment;
- the future development of digital start-ups, once maturing, will depend on acceptable levels of protection of their own rights (much as they might initially want free use of others' creativity).

Almost all major brands and retailers now have a website showcasing their products – many also offering them for direct sale online. Increasingly, brands are using social networking platforms and viral services such as YouTube, to connect to a wider, and younger, consumer market.

But, predictably, the trade in fakes has now reached viral services e.g. Facebook members sell counterfeits via their Facebook 'page' to such an extent that the company now has a policy for reporting such activity<sup>49</sup> and there are other sites offering search facilities, allowing brand owners to check if their products are being faked on Facebook.<sup>50</sup>

So, just as new digital start-ups will require protection from pirating of their services, and even counterfeits of their actual websites (see below), effective online IPR enforcement is equally crucial for the brands.

#### 4.4.2 Online enforcement

The Office of Cyber Security (within the Cabinet Office) now leads on eCrime in the UK, and has just published a report which estimates that cybercrime costs the UK economy £27 billion annually, the equivalent of 2% of UK GDP.<sup>51</sup>

- IP theft and industrial espionage are the main culprits;
- IP theft from business has the greatest economic impact of any type of cyber crime, estimated to be £9.2 billion per annum;
- the hardest hit sectors are pharmaceuticals and biotech, electronics, IT and chemicals;
- £3.1 billion annual economic cost of cyber crime to UK citizens;
- this includes an estimated £1.8 billion for identity theft and £1.4 billion for online scams.

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<sup>48</sup> <http://artofthetrench.com>

<sup>49</sup> [http://www.facebook.com/terms.php?ref=pf#!/legal/copyright.php?howto\\_report](http://www.facebook.com/terms.php?ref=pf#!/legal/copyright.php?howto_report)

<sup>50</sup> [www.facesearchd.com](http://www.facesearchd.com)

<sup>51</sup> <http://www.cabinetoffice.gov.uk/resource-library/cost-of-cyber-crime>

It is important to emphasise that the process of shopping online – with an increasing number of counterfeits for sale and of actual fake websites run by criminals, for example – carries an ever higher risk of ID theft, cloned credit cards and so on, as well the risks to consumers inherent in the trade in fakes.

Consumer confidence is crucial for the various eCommerce markets to develop, and efforts to enforce all relevant laws need to be as robust and as visible as possible.

However, more legal clarity is required to determine the liability of ISPs (internet service providers) for illegal third party content or activity on their sites, including IP crime. This is an issue which ultimately resides at EU level with the eCommerce Directive (see below).

There have been many well-chronicled disputes between rights holders and Google, for example in relation to their AdWords facility, selling keyword-based advertising to a brand's or retailer's competitors. Companies pay to appear on screen, alongside the genuine brand in the search result, after a famous brand name is entered into the Google search engine (e.g. by a consumer looking for a particular product or online retailer).

The relevance, in the context of this submission, is that this facility in the Google search engine is widely used by sellers of counterfeit goods to advertise their wares and direct consumers to their websites. The question is to what extent Google should be responsible for the problems caused to rights holders by the extensive abuse of the AdWords facility, which is highly profitable, netting Google over £2 billion in the UK alone last year (based in the Republic of Ireland, Google paid no UK tax on this profit).

There have been findings against the practice in the USA (though not clearly finding Google itself liable).<sup>52</sup> In the EU, a massive case brought by Louis Vuitton against Google eventually went to the European Court of Justice, which ruled that Google should not be held liable for trade mark abuse, but companies buying into the AdWords facility have to make it clear in their search entry that they have no connection with the genuine brand.<sup>53</sup>

The current law does not help to establish how ISPs such as Google might routinely take responsibility for criminal offences committed via their services, without cumbersome and expensive legal procedures. It seems illogical that they have so little responsibility, when they profit from abuses of their services and could technically be committing money-laundering offences or shown to have amassed the equivalent of criminal assets under POCA.

For example, the eCommerce Directive (2000/31/EC)<sup>54</sup> establishes a 'safe haven' regime for "hosting providers":

- Article 14 establishes that "hosting providers" are not responsible for the content they host as long as (1) the acts in question are neutral intermediary acts of a mere technical, automatic and passive capacity; (2) they are not informed of its illegal

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<sup>52</sup>[http://www.abajournal.com/news/article/binder\\_binder\\_awarded\\_292k\\_suit\\_claimed\\_google\\_competitor\\_purloined\\_ips\\_nam/](http://www.abajournal.com/news/article/binder_binder_awarded_292k_suit_claimed_google_competitor_purloined_ips_nam/); <http://www.linksandlaw.com/adwords-google-court-usa-greico.htm>

<sup>53</sup> <http://www.guardian.co.uk/business/2010/mar/23/google-louis-vuitton-trademark-legal-case>

<sup>54</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32000L0031:EN:HTML>



- character, and (3) they act promptly to remove or disable access to the material when informed of it;
- Article 15 precludes member states from imposing general obligations to monitor hosted content for potential illegal activities.

ISPs already monitor their content for their own purposes, with sophisticated systems in place. As with any legitimate business in 'realtime', which host other businesses and services, all ISPs should ensure that

- those who use an ISP's online environment for their own business, for profit, act legally and responsibly; and
- consumers who access those businesses, via the ISP as host, are both safe and aware of the need for vigilance.

Another example is eBay which has always carefully positioned itself as a 'trading platform' and claimed the protection of the 'safe haven' provisions, despite hosting the auctions from which it takes commission (and owning PayPal, which is the means used by many to pay for their online transactions). Like Google, eBay has structured its business so that it minimises its liabilities outside the USA, and does not pay any tax in the UK – it used to have an UK office, but its EU business is now based in Luxembourg.

Over some years, under pressure from rights holders, law enforcement and latterly government, eBay has developed more effective procedures to police activity on its sites, and to identify and hand over to law enforcement the biggest offenders, who are selling counterfeit products of all kinds, from fake electrical goods to counterfeit perfumes, car headlights and airbags (all of which have serious safety implications).<sup>55</sup>

Appropriate, proportionate enforcement techniques to combat online criminality also need to be more focussed on practical solutions – in line with the strategy we understand is being developed by the Office of Cyber Security, which will rely less on prosecution, and will consist also of counter-attacking cyber-techniques and more use of the assets recovery regime under POCA.

Technologies are available to monitor both wholesale and retail distribution sites. These technologies are extremely accurate and have been accepted as forensic evidence by courts all over Europe where rights holders have taken action against large scale distribution sites. The recording of publicly available IP addresses and provision of those to ISPs is also under consideration as part of so called "graduated response" initiatives in a number of European countries.

In terms of the sale and advertising of counterfeits, the internet is fast becoming the sales channel of choice – almost complete anonymity for the seller, the fact that a consumer does not see items prior to purchase and the challenges of law enforcement across many jurisdictions make this a rapidly growing use for the internet. (As well as the economic challenges this presents, when the goods are pharmaceutical products, automotive parts or suchlike, there is a significant risk to public health and safety.)

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<sup>55</sup> <http://pages.ebay.co.uk/safetycentre/keepingebaysafeandbuildingtrust/counterfeititems.html>

There are recognised technological solutions available for crawling the billions of web pages of the internet, auction and marketplace listings to detect IP rights abuse, by searching for brand names, which can then be filtered to find the most egregious infringements, such as sites attempting to steal financial credentials or sell unregulated pharmaceuticals (in a recent study, it was found that there were over three thousand unregulated online pharmacies accessible to the British public).

The Metropolitan Police e-Crime Unit took down 1,200 fake websites last year for IP crime offences and are working on over 2,000 more, both with the help of UK domain registry Nominet.<sup>56</sup> US Homeland Security's Immigration & Customs Enforcement (ICE) has also launched a take-down campaign on the same basis.<sup>57</sup> Both are finding international criminal networks and activity behind the websites.

ACG member MarkMonitor, a leader in enterprise brand protection, offers comprehensive solutions and services that safeguard brands, reputation and revenue from online risks.

At the request of the US Chamber of Commerce, it conducted an independent study of online traffic trends to rogue sites, identifying and prioritizing some of the worst offenders based on traffic, as well as identifying location information.

Using 22 major brands as criteria, ranging from pharmaceuticals, luxury goods, and apparel to entertainment titles and software, MarkMonitor used its patented technology to comb the Internet for sites suspected of offering counterfeit goods or pirated digital content.

They published a report in January 2011, simultaneously in the US and UK, on the scale and complexity of online piracy and counterfeiting.

According to this report, sites selling counterfeit goods using the trade marks of one or more of the 22 genuine brands chosen for this survey, including prescription drugs and luxury goods, generated more than 92 million visits per year.<sup>58</sup>

As regards the host location of the sites categorized as 'counterfeit', 73% were hosted in North America or Western Europe. Eastern European countries hosted another 14% of the sites while 9% of the sites were hosted in Asia.

This kind of scale and spread of illicit activity poses a new challenge for enforcement agencies around the world, but we do not believe it is symptomatic of any need to change the law. A new standard of international collaboration is needed, from sharing intelligence to coordinating enforcement actions across jurisdictions.

We are also seeing a growing awareness of the scale of the problem here in the UK. Nominet is launching a new policy process and as part of this SOCA have put forward a proposal for an Issue Group to discuss developing an abuse policy for dealing with .uk domain names that are being used in connection with criminal activity.

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<sup>56</sup> <http://news.bbc.co.uk/1/hi/uk/8392600.stm>

<sup>57</sup> <http://www.ft.com/cms/s/2/2df7c1d4-fcac-11df-bfdd-00144feab49a.html>

<sup>58</sup> [http://www.a-cg.org/guest/publications/guest\\_publications\\_industry\\_surveys\\_and\\_reports.php](http://www.a-cg.org/guest/publications/guest_publications_industry_surveys_and_reports.php)

It will be important for everyone's work to link together e.g. Interpol has a global cybercrime remit.<sup>59</sup>

It is also noteworthy that commercial reality may now be starting to reflect the true scale of the online problem. For example, a recent internal investigation at China's largest eCommerce group, Alibaba (its main shareholder being Yahoo! – whose brand name includes the exclamation mark) has led to the resignation of its CEO. While popular with legitimate traders for its cheap Chinese goods, it is also a major source of online counterfeits.<sup>60</sup>

We have provided quite a level of detail here because we believe that that digital platform and content businesses are not dissimilar from other eCommerce enterprises, such as the brands, in their need for effective online enforcement to protect their creativity and investment in the longer term.

All legitimate trade and commerce is under threat from online fraud of all kinds, and in our view it is impossible for enforcement to be 'too restrictive' in this environment. In the case of counterfeiting, for example, 'freedom to trade' means unfettered criminal gain. And new internet businesses will need a robust online enforcement framework too, on which to rely as they grow into mature businesses worth attacking.

## VOLUNTARY SOLUTIONS

### Internet Stakeholder Forum

After two years of negotiation between rights holders and major internet platforms, moderated by a team from DG MARKT, a Memorandum of Understanding has just been agreed on the sale of counterfeit goods over the internet. The MOU will shortly be signed by all stakeholders. It is a 12-month pilot, to build trust and cooperation with the internet platforms, so that counterfeits will be removed from their sites without going to court. (We are unable to disclose any further details for the moment, but an announcement will be made by DG MARKT when the MOU is ready for signing.)

### Industry self-help/thinking laterally

ACG is looking to support a project where brand owners will work in partnership with the credit card companies, to ensure that they remove their payment services from infringing websites. A similar project has already launched with the recording industry, in partnership with the City of London Police. Initially the credit card companies were reluctant, but they are now working closely with industry, and payment services are being removed in as little as 2 days.

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<sup>59</sup> <http://www.interpol.int/Public/TechnologyCrime/default.asp>

<sup>60</sup> <http://www.bbc.co.uk/news/business-12521833>

## 7

### **Barriers to growth**

Lack of clarity in ISP liability. More international collaboration needed (e.g. to share intelligence about the criminal operations behind the sites, and to take down illegal websites).

### **Recommendation**

Explore opportunities to encourage more responsibility from ISPs for online counterfeiting, including a voluntary code of practice with brand owners, following the EU lead of DG MARKT. Involve other interests who can help to remove websites e.g. credit card companies. More understanding of available technologies and how to use them against the perpetrators. Establish operational coordination with other countries e.g. USA, to pilot a drive for more joined-up enforcement on a global scale.

## 4.5 International issues

First, it is important to reiterate that we do not believe that the digital/online environment requires a different legal framework.

However, the internet's particular challenges highlight the urgent need for consistent standards of enforcement, and the difficulty of liaising between enforcement agencies on an international level. It allows total anonymity and even false identities not only for people but for entire websites and businesses, with a scale and speed of criminal operations far greater than in the physical world.

It therefore requires much smarter international collaboration by the enforcement agencies, Interpol, EU Customs, the World Customs Organisation and others, with the support and participation of rights holders. When it works, the results are staggering, as can be seen from the multi-agency success of Operation Jupiter, led by Interpol.<sup>61</sup>

### 4.5.1 Enforcement in source countries

Enforcement of IP rights operates as a barrier to legitimate trade when it is ineffectual. If IPR enforcement is working efficiently and promptly in a given country where a company wishes to expand, this is not a barrier, quite the opposite, as it is to the advantage of legitimate companies with IP rights to protect.

However, the systems and processes for initial registration of rights, which then give a company the basis for enforcing them, can vary significantly, with some countries having bureaucratic procedures and taking years to grant registration. Businesses require the certainty provided by efficient trade mark systems, ensuring that existing right holders and legitimate new entrants are protected.

Embedding IPR enforcement issues into UK trade policy will help to raise awareness at government level and encourage higher standards of enforcement in problem countries.

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<sup>61</sup> <http://www.interpol.int/Public/FinancialCrime/IntellectualProperty/OperationJupiter/Default.asp>

China and other Far East countries are prime sources of counterfeits, with patchy IPR enforcement regimes. We are also seeing an increasing flow of fakes from other countries such as Turkey and Russia.<sup>62</sup>

In relation to both online and offline counterfeits, a major objective must be to improve IPR enforcement in source countries, in order to stop exports of counterfeits to the markets of Europe and America.

HM Revenue & Customs is currently participating in an EU-China initiative to start a systematic process of interception at Chinese ports. If shipments of suspected counterfeits cannot be stopped, telephone notifications are made by English-speaking Chinese customs officers direct to the UK port of destination so that a seizure can be made on arrival.

The US monitors their trading partners' IPR enforcement performance annually, by taking evidence from industry and other stakeholders, which results in the so-called 'Special 301' report issued by the US Trade Representative each spring (2011's is due soon).

2010's Special 301 Report once again highlights the prominence of IPR concerns with respect to China.<sup>63</sup> US Trade Representative Ron Kirk was quoted as saying:

“We are seriously concerned about China’s implementation of ‘indigenous innovation’ policies that may unfairly disadvantage U.S. IPR holders. Procurement preferences and other measures favoring ‘indigenous innovation’ could severely restrict market access for American technology and products. Creating an environment that nurtures innovation and entrepreneurship is a worthy goal, but China must maintain a level playing field.”

The Report identifies a wide range of other serious concerns, ranging from the challenge of internet piracy in other countries, to ongoing systemic IPR enforcement shortcomings in many trading partners.<sup>64</sup>

One of Britain's most successful inventors in recent years, and owner of an iconic brand, James Dyson, has repeatedly expressed his concern at the economic impact of the unfair competition for UK brands resulting from China's continued propensity for counterfeit production as an integral part of their national economy, with its own widespread and illegal business model.<sup>65</sup>

The Prime Minister did raise IP as a talking point when he visited Beijing with a UK trade delegation in November 2010, which is a most welcome start. But it was not clearly signposted for the media, resulting in some unfortunate negative comment.<sup>66</sup>

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<sup>62</sup> <http://www.notofakes.com/Resources/TravelAdvisory/Europe/Turkey/tabid/417/Default.aspx>;  
<http://www.worldtrademarkreview.com/issues/Article.ashx?q=75cc6556-b559-487f-8ac3-b6001229b6c0>;  
<http://en.rian.ru/papers/20100924/160710284.html> (*third item*)

<sup>63</sup> <http://www.ustr.gov/about-us/press-office/reports-and-publications/2010-3>

<sup>64</sup> [http://www.ustr.gov/webfm\\_send/1906](http://www.ustr.gov/webfm_send/1906)

<sup>65</sup> <http://www.fmwf.com/media-type/news/2011/01/the-risks-china-presents-british-firms-written-by-james-dyson/>

<sup>66</sup> <http://www.telegraph.co.uk/finance/comment/damianreece/8118606/David-Cameron-should-be-focusing-on-intellectual-property-not-human-rights.html>; <http://www.dailymail.co.uk/news/article-1328327/Cameron-Globalisation-reverse-unless-China-corrects-trade-imbalance.html>

It is crucial that the UK clearly declares an intention to take a strong position internationally and to encourage effective IPR protection and enforcement through sustained dialogue, via embassies and trade organisations locally, as well as during the occasional high profile state visit:

- to realise greater value for UK exports;
- to reduce economic crime in general, and IP crime in particular;
- to provide advice and support for British business abroad;
- to combine forces with other countries which suffer from counterfeiting (US and some EU countries in particular) to promote a joint campaign for better enforcement standards.

From anecdotal information we have received from colleagues in our sister organisations around the world, we are aware of an attitude amongst many governments in developing countries that Europe and America should not lecture them on standards of IP protection when their own houses are not in order.

This could provide an additional spur to the idea of repositioning IP policy and enforcement, to achieve higher standards ourselves (see section 5 below). Meanwhile, the obvious riposte is that we are the recipients of their counterfeits, and as such are entitled to ask that remedies are found to stop the commercial scale of counterfeit production in, and shipment from, their countries.

The use of trade policy as a means of influencing other countries' enforcement standards has been successfully driven forward by the EU Commission (in fact, when Peter Mandelson was EU Trade Commissioner he provided splendid support for industry in its enforcement efforts against counterfeits in the Silk Market).<sup>67</sup>

China does not hesitate, of course, to protect its own IP interests - for example, the IPR enforcement lockdown for the Beijing Olympics was extraordinary.<sup>68</sup> But the standard of IPR enforcement for established foreign brands is still unsatisfactory and there are no quick fixes.

The problem is illustrated by US efforts to formalise a commitment by China to improve IPR enforcement there, by filing a complaint with the World Trade Organisation. This was not totally successful.<sup>69</sup> With the appointment of the US IP Enforcement Coordinator (see section 5 below) the US is adopting a less combative stance, and turning to diplomacy and trade missions to achieve their objective.

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<sup>67</sup> <http://www.ft.com/cms/s/0/3474452c-f68b-11da-b09f-0000779e2340.html#axzz1EyXBO3Qz>

<sup>68</sup> <http://www.chinahearsay.com/protecting-olympic-related-ipr>

<sup>69</sup> [http://www.wto.org/english/tratop\\_e/dispu\\_e/cases\\_e/ds362\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds362_e.htm)

## 8

### **Barrier to growth**

IPR enforcement in source countries is not yet delivering the best and most obvious solution to the proliferation of counterfeits flooding Western markets (increasingly via the internet), which is to cut off the supply.

### **Recommendation**

A declaration by the UK to address this as a priority with its international trading partners, accompanied by practical steps to support better enforcement efforts in problem countries. See section 5 below and the need to embed IP policy into trade and economic policies, training of embassy staff etc.

NB There is also a serious issue with Free Trade Zones, of which there are now over 3000 in 135 countries, including 500 established in India alone in 2009. The purpose of these derestricted areas is to encourage cross-border trade between countries, to stimulate economic growth and attract foreign/new investment to traditionally underdeveloped parts of the host countries.

We do not propose to go into great detail here, as it is a complex (fascinating) subject but would be happy to elaborate that would be helpful.

For now, suffice to say that this concept illustrates what can happen when a situation is over-engineered in order to manipulate conditions into producing somewhat artificial growth, while providing too few of the normal controls, which we are concerned may be the unintended outcome of the current government thinking behind this Review.

#### 4.5.3 Enforcement at the UK frontier, and the EU dimension

HM Revenue & Customs (HMRC) now derives its powers to enforce IP rights at the UK frontier solely from a problematic EU Regulation<sup>70</sup> which is currently under review. The UK Border Agency (UKBA) now carries out IPR and other enforcement procedures on HMRC's behalf, with some excellent results, at ports, airports and the postal hub at Coventry:

But serious issues arise from the difficulties posed, by several aspects of the EU Regulation, for rights holders in their efforts to partner UKBA/HMRC in enforcing their rights at the frontier, including:

- the cumbersome procedure which has to be followed by rights holders in order for counterfeits to be seized and detained;
- the restriction on use of information from Customs by rights holders in their own enforcement actions;
- the current interpretation of the provisions in the EU Regulation relating to goods in transit, which prevents Customs in a member state from detaining goods which are in transit through the EU, from one non-member state to another, unless there is evidence that those goods will be placed on the market in the country in which they are seized (i.e. within the EU).

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<sup>70</sup> Council Regulation (EC) No 1383/2003 concerning customs action against goods suspected of infringing certain intellectual property rights and the measures to be taken against goods found to have infringed such rights

This last issue has been the subject of lengthy litigation in the UK by Nokia Corporation, seeking to clarify this interpretation in favour of a sensible outcome for rights holders, in a case where fake mobile phones were transshipped via the UK from China to Brazil. The central question of law is currently on referral to the European Court of Justice awaiting their ruling. ACG's latest e-Newsletter carries the details on page 1.<sup>71</sup>

We are concerned that the balance of interests in relation to IPR enforcement at the frontier is weighted far too much against the rights holder.

The burden should be on the importer or owner of the goods in question, to come forward and claim them (which they rarely do, if the goods are fake, for obvious reasons) rather than on the rights holder.

This was the procedure in the UK, before it was brought into line with the EU Regulation - goods were detained by customs, once in possession of evidence from the relevant rights holder that the goods were counterfeit, and held for a reasonable time to enable the owner or importer to come forward. If they failed to claim the counterfeits, destruction followed.

## 9

### **Barrier to growth**

The EU Regulation now wholly governs customs IPR enforcement procedures in the UK and is not satisfactory as per the issues outlined above. This poses a massive obstacle to effective trading practices and enforcement of rights, which are essential for successful business growth.

### **Recommendation**

More support from HM Government for the rights holders' position in the dialogue with the EU Commission (DG TAXUD), and recognition of the need to change the current provisions. If more counterfeits could be seized at the frontier, and intercepted in transit, the impact of counterfeiting within the UK, and globally, would be greatly reduced.

#### 4.5.4 The international framework

A given IP issue is often not limited to a single country and, in the context of counterfeiting, products often move across jurisdictions. As noted above, "joined up" enforcement is desirable, including information-sharing between enforcement authorities and rights holders.

But unless IP laws are fully harmonised, it is hard to see a role for "international" courts other than e.g. to clarify points of principle (as is presently done in Europe by the European Court of Justice). The practical application of the law stays anchored within a specific jurisdiction.

In the single market, with free movement of goods, and a higher degree of harmonisation, there is more scope for regional enforcement and regional remedies, and this is already manifested e.g. in the ability for national courts handling Community Trade Mark or

<sup>71</sup> [http://www.a-cg.org/guest/pdf/acg\\_news\\_new\\_year\\_2011.pdf](http://www.a-cg.org/guest/pdf/acg_news_new_year_2011.pdf)



Registered Community Design cases to grant pan-European relief against defendants domiciled in their jurisdiction. Similarly, it is possible to make a customs notification which registers IP rights for enforcement action covering the whole EU.

To summarise the international picture in which the idea of such courts would be considered, there is already a comprehensive long-established worldwide legal structure for IP rights in TRIPs (the Trade-Related Aspects of Intellectual Property Rights) governed by the World Trade Organisation.<sup>72</sup>

A number of other international bodies and forums are already closely involved in developing various aspects of this global IP framework, each with their own distinct areas of interest and expertise - including the World Intellectual Property Organisation (WIPO) and the European Union.

The EU Directive 2004/48/EC on the enforcement of intellectual property rights was introduced in 2004, with two years allowed for implementation by all member states. Some countries have still not fully implemented it.

The Directive incorporates civil law measures under the TRIPs Agreement into the EU legal framework. It goes beyond the minimum provisions laid down in that Agreement as it also covers, for example, damages, corrective measures and evidence. In addition, the Directive is based on the practices enshrined in the legislation of the Member States that proved to be most effective before the Directive was adopted (the 'best practices approach'). Member States may also add sanctions and remedies that are more favourable to rights holders. The Directive was therefore designed to provide a minimum but flexible legal framework for enforcing intellectual property rights.

The Commission is currently consulting on its first assessment of the implementation and impact of the Directive, as required by its Article 18.<sup>73</sup>

The assessment is based both on the Commission's appraisal of developments and on feedback received from Member States via national reports, which, in turn, reflect views expressed by industry, legal practitioners, consumers' associations and other interested parties.

From the concerns expressed in the assessment, it is clear that there are several areas where the Directive is not thought to have been successful in its objective to harmonise civil enforcement of rights throughout the EU, including the internet (which has grown exponentially since the Directive was first drafted in 2003), the position of ISPs (see page 7) the use of measures such as injunctions, the procedures for gathering evidence, costs of destruction of counterfeits, and the lack of deterrence in the measures relating to damages.

*"... in such cases, it should be considered whether the courts should have the power to grant damages commensurate with the infringer's unjust enrichment, even if they exceed the actual damage incurred by the rights holder."*

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<sup>72</sup> [http://www.wto.org/english/tratop\\_e/trips\\_e/trips\\_e.htm](http://www.wto.org/english/tratop_e/trips_e/trips_e.htm)

<sup>73</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:0779:FIN:EN:PDF>

Here in the UK there is also an issue with the kind of damages which should be available to rights holders in civil infringement cases. Currently, the civil damages regime provides recompense only for the cost of a license, had one been issued, and may in addition attempt to take account of the profits the infringer might have made from this particular infringement. It therefore offers no deterrent and little solace for the rights holder.

As stated in the conclusion to the Commission's assessment of the Directive:

Infringements of intellectual property rights cause widespread economic harm. A significant number of products infringing intellectual property rights now pose a real threat to consumer health and safety. Proper protection of intellectual property rights is fundamental to stimulate innovation and culture in a competitive, wealth-generating, knowledge-based economy. Different interests have to be carefully balanced.

The story of this Directive's progress so far well illustrates the challenge of trying to achieve consistent standards of enforcement across Europe, and may help to show how complicated it would be to introduce a new level of international courts.

The Commission is addressing the issues in various ways, for instance by including ambitious chapters on intellectual property rights in bilateral trade agreements and through participation in international initiatives, such as the Anti-Counterfeiting Trade Agreement (ACTA), which adds a whole new level of standard-setting to the international IP network (see below).

So while the current situation is quite complex, and remedies for international disputes or issues take time to resolve, our opinion is that the option of introducing international courts poses insuperable logistical hurdles and inefficiencies. Even if this could work, the loss of sovereignty issues would militate against such a solution.

At a global level, and at the time of writing, the new ACTA is in its final stages, with formal adoption expected in Spring 2011. This agreement is a new plurilateral treaty for improving global standards for the enforcement of IPR, to more effectively combat trade in counterfeit and pirated goods.<sup>74</sup> GlaxoSmithKline's public position paper illustrates its importance.<sup>75</sup>

A look at the relevant IP web page of DG TRADE, which includes a link to more information about ACTA<sup>76</sup>, also provides a useful insight into the complexities of existing international IP laws and enforcement.

At international level we believe that the pressing need is not for new courts, but for better coordination of existing enforcement resources, with smarter use of IT, more sharing of data and more collaborative operational activity.

An example of a potentially useful new initiative is the Rapid Information Exchange on counterfeiting and piracy - a report was produced for the EU Commission last August.<sup>77</sup>

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<sup>74</sup> <http://ec.europa.eu/trade/creating-opportunities/trade-topics/intellectual-property/anti-counterfeiting>

<sup>75</sup> <http://www.gsk.com/policies/GSK-Public-Position-on-ACTA.pdf>

<sup>76</sup> <http://ec.europa.eu/trade/creating-opportunities/trade-topics/intellectual-property>

This is an ongoing project 'to achieve more effective cooperation networks and swift exchanges of strategic information between national contact points from all Member States on counterfeit and pirated products and services'.<sup>78</sup>

There are several other important initiatives to create a more efficient system of intelligence-sharing, for example a database already set up by the World Customs Organisation, and a new database being developed within EU Customs, due to go live later this year. At the moment, though, multiple inputs are required from stakeholders and it is to be hoped that a common or linked system will eventually result.

## **10**

### **Barrier to growth**

Lack of common and sufficiently effective IPR enforcement standards. Slow rate of change/improvement following legislation or treaties. EU holds the key to harmonisation of enforcement throughout member states but rights holders' interests are not always supported by government in Brussels. UK also needs to have coherent strategies of its own in bilateral relations.

### **Recommendation**

Actively monitor consequences of ACTA to ensure that it has the required effect. Embed IP policy in UK trade, economic and development areas of government. Strengthen government representation for IP interests in Brussels and in other international fora.

In the next section we will examine an even more important priority (in our view) - how to refocus IP policy and IPR enforcement in the UK.

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<sup>77</sup> [http://ec.europa.eu/internal\\_market/iprenforcement/docs/study\\_information\\_en.pdf](http://ec.europa.eu/internal_market/iprenforcement/docs/study_information_en.pdf)

<sup>78</sup> <http://ec.europa.eu/idabc/en/document/7802/5637.html>

## 5 Repositioning IP within government

If the UK is going to re-assert its competitiveness in the world economy, a coherent strategy for realising and harnessing the true value of IP is essential, both to protect precious IP rights and to stimulate sustainable growth and innovation in all sectors.

If this objective is to be met, responsibilities for IP policy and IP rights protection and enforcement must be appropriately integrated into government. We do not believe this to be the case currently. The organisational structure must align with the objective, something we think is possible to achieve with no significant resource implications – indeed, there may be savings.

Various other ongoing reviews and initiatives – for example the protection of IP online (Culture Media & Sport select committee), the Trade White Paper, the Home Office's development of the UK's serious organised crime strategy, the work of the Office of Cyber Security, major changes to the structure for consumer protection, and SOCA's IP Crime Action Plan (in development) – also offer opportunities to consider relocating IP policy, and IP rights protection and enforcement, within the national political and legal frameworks.

To position IP as a significant contributor to growth, IP policy needs to be a more central focus in government remits, international trade agreements and the aid given to less developed countries (where IP regimes are still weak), both to strengthen existing markets for UK innovation and to secure new ones.

IP policy and IPR enforcement are both currently fragmented across many different government departments. An important achievement of a previous IP Minister, David Lammy MP, was the introduction of cross-departmental IP meetings but we suggest the real solution must go further. All aspects of IP need to be gathered together, and led by a minister in Cabinet who can oversee and coordinate not only IP policy, but also the creation, protection and enforcement of IP rights.

### 5.1 Positioning IP policy

#### The Intellectual Property Office (IPO)

While the IPO leads on policy, and has strengthened its team significantly with the recruitment of several economists, it must be recognised as an executive agency primarily engaged in specific aspects of the IP system (mainly the grant of registered rights) and not a government department. Its main location in Newport does not help.

To be influential and fully constructive in terms of the economy, IP policy needs to be properly connected into the heart of the country's economic policymaking. Similarly, while the IPO is responsible for aspects of IPR enforcement, it is not an enforcement body.

With the 'knowledge economy' being so crucial to the country's future economic health, this is not the best way to manage the most valuable asset needed for such a challenge.

The Gowers Review of IP (2006)<sup>79</sup> identified the principal functions of the Patent Office (as it then was) as:

- award: granting UK patents as well as registering UK trade marks and designs;
- awareness: responsibility for raising awareness of IP-related issues among businesses and consumers;
- policy: advising ministers on IP policy;
- tribunal function: Patent Office has a role in deciding disputes in respect of patents, trade marks and both registered and unregistered design rights; and
- enforcement: leading the development of the UK IP crime strategy

Gowers concluded that some restructuring was required for the IPO to become fit for purpose in the 21<sup>st</sup> century. We believe that another searching review of the IPO's role and functions is required to redefine its principal functions according to its strengths, so that it can deliver the right level of support for business through well-defined responsibilities.

It is important to recognise areas where the IPO delivers:

- consultation with users and responsiveness to their needs is high
- assistance to SMEs applying directly
- efforts to educate have improved since Gowers<sup>80</sup>
- there is a speedy registration system
- better use of IT technology to improve processes
- free access to register for information on registrations, law, process
- links to Companies House and registers worldwide etc

Opinion is divided on the way it fulfils its important role in the international arena, especially within the EU, and in relation to the US. For example, the IPO advised the government in submitting observations about a case before the European Court of Justice last year (Nokia's transit case, as mentioned in Section 4 above) and requested input from stakeholders. ACG duly submitted a detailed opinion, but did not know if the government actually made any observations to the ECJ, although we did ask at the time.

When ACG followed this up some time later, the IPO official's reply was: *"I am afraid that it is not government policy to comment on whether or not the UK proposes to intervene in specific cases. The case details you are requesting will be available to the public in the Curia website in due course"*.

It was unclear whether this was an IPO or a government-inspired response. In fact the UK government's observations were never made public, as far as we know, but we recently heard quite by chance, and unofficially, all about the observations which the government made in this case (based on whatever advice the IPO had provided to it).

This lack of transparency is unhelpful, and the level of support which rights holders might expect from the IPO in specific matters and issues remains unclear. Perhaps we are expecting too much, but little guidance or advice was available to rights holders during the negotiation of terms for ACTA, for example, where the EU Commission acted on

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<sup>79</sup> <http://www.official-documents.gov.uk/document/other/0118404830/0118404830.pdf>

<sup>80</sup> <http://www.ipa.gov.uk/chinaroadmap.pdf>

behalf of all member states and the IPO led the UK's participation in that process. Industry took its own steps to participate and assist in negotiations via a Business Response Group (led by the International Trademark Association and BASCAP).

Currently, rights holders again seem to be left to deal largely on their own with the EU Commission's consultation on the Enforcement Directive (see Section 4). The IPO called a meeting about this recently (which ACG could not attend), after which it was reported that when rights holders asked for guidance, the IPO's response was 'We just wanted to hear from you.'

We do not have direct experience of the IPO's mediation service but understand from others that it is helpful and supportive in the civil arena – clearly, rights holders cannot consider mediation as a solution to IP crime.

As regards IP policy, the Gowers Review was concerned about the lack of distinction between the IPO's operational and policy functions. We cannot comment on how successfully the two have been separated internally (Gowers Review p 113). From our perspective, policy activity falls into several different areas, in two of which the IPO is appropriately engaged (though with varying success):

- advice to Ministers about existing IP policy;
- representing UK business interests in specific discussions e.g. ACTA.<sup>81</sup>

But a coherent strategic view of IP policy is often lacking. Businesses need a certain level of expertise and commercial awareness from the IPO, to support their enterprises, and as part of the right environment for growth.

The IPO's position in BIS, without a Minister of its own, reduces the influence the IPO can have on the formation or implementation of policy, either within that department, or in conjunction with other departments. And we feel that the IPO has not always been able to understand industry's issues sufficiently.

One option is to have a separate policy unit, with links to others in trade, the Treasury and health, for example, to provide the necessary perspective and centralised cohesion, in order to manage proactive policy development - particularly in relation to changes in the economy, and development in other relevant policy areas.

Gowers recommended that 'An independent board should be given a clear and coherent remit to provide a strategic overview of policy and to challenge government policy-making. In addition, it should advise on how the UK's interests should be pursued in international IP negotiations.' (Gowers Review p 112). Instead, SABIP was born, commissioned some external research, and was then disbanded.

We would strongly urge the government to revisit this recommendation.

Responsibility for IP policy overall should be escalated to a dedicated Minister for IP (or Minister for Innovation & Growth) who would provide focus to the role of IP in the

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<sup>81</sup> Anti-Counterfeiting Trade Agreement - for more on ACTA, see above and below

economy, deliver the required influence in government and ensure that IP policy was effectively integrated across government.

Currently, it is often not the IPO which is responsible for implementing a policy decision. Other departments with some measure of responsibility for aspects of IP policy include DCMS, BIS, the Home Office, DCLG, the Ministry of Justice and the Treasury.

One recent example where such a role would have been valuable concerns the Department of Health's consideration for tobacco products to be in plain packaging. This has significant ramifications for IP rights, IP protection and enforcement, and branding. Such initiatives require full consideration and impact assessment prior to the formulation of government policy, something that we believe can only be achieved if IP is recognised as a significant economic force and championed by a Minister and officials with the influence and understanding to ensure scrutiny is both undertaken and thorough.

We believe that how management of all the policy aspects of IP is structured in the UK is the starting point for providing a coherent supportive environment for future growth and innovation across all industries.

More awareness at grass roots in Westminster would also be welcome, and there is a ready vehicle in the All Party IP Group, which has successfully re-grouped following the change of government.<sup>82</sup>

## **11**

### **Barrier to growth**

The IP Office does not deliver coherent and powerful IP policy and cannot lead other departments effectively in policy-making or policy implementation. Not enough understanding generally within government of the importance of IP and innovation in its drive for growth.

### **Recommendation**

IP policy should be the direct responsibility of a dedicated Minister for IP (or Minister for Innovation & Growth) with the necessary authority and influence to ensure that relevant IP issues are properly embedded in trade and economic policy. The existing structure of policy units should be examined to see how best to join up IP policy-making across government.

The role of the IPO and performance of all its functions should be reviewed, to allow it to play to its strengths.

## 5.2 IPR enforcement

Criminal enforcement for IP rights is similarly problematic in the UK and we suggest that it needs reorganisation and strong leadership. Unusually, all the criminal provisions of the Trade Marks Act 1994 are currently enforced in the United Kingdom primarily by trading standards departments within local authorities, not by police or Customs as in almost all other countries.

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<sup>82</sup> <http://www.allpartyipgroup.org.uk>

Trading standards is primarily a regulatory service, usually located in the environmental health department of a local authority, with no power of arrest (for this they call on police support) and no formal training in criminal procedures, detection, investigation or prosecution.

Despite best efforts by some authorities, their responsibility for enforcing the law against a serious organised crime on a global scale (see below) – without even the power of arrest – is becoming increasingly untenable, particularly in relation to major international IP crime cases which originate in, or centre on, the UK.

In almost every other country in the world, the police (often within an economic crime unit) tend to be responsible for tackling IP crime within their borders, and we will address this anomaly – and a proposed solution – below.

Currently, the IPO leads on IP crime in some respects, within its Directorate of Copyright and Enforcement. Although this has no enforcement powers, and cannot participate in enforcement actions, it now has an enforcement unit with an intelligence hub database, which gathers and matches intelligence from rights holders and law enforcement agencies. This is helping to join up organised crime group mapping and identification of targets, in particular.

We applaud this initiative, which is enhancing understanding of the links between counterfeiting and other serious organised crime, and identifying more opportunities to disrupt and deter the criminals.

The enforcement unit is also the secretariat for the IP Crime Group, launched in 2005, which was set up to help to drive a national IP crime strategy, which still does not exist in any meaningful sense (this has a long history, which we would be happy to elaborate on in another forum, but would take pages to explain here).<sup>83</sup>

The Group consists of law enforcement, industry and government representatives, and meets bi-monthly to share information and highlight new or recurring concerns at a policy level, but it does not engage directly with operational issues. There are several workstreams in progress, such as a guide to IP crime in the workplace (including the use of illegal software, for example) which will provide an online toolkit to help businesses operate within the law.

While this offers a useful discussion forum, industry and law enforcement are developing more useful partnerships outside this Group. For example, the Real Deal Campaign for Fake Free Markets<sup>84</sup> is a unique collaboration to stop the sale of fakes in markets, funded by industry. For the past two years rights holders in all affected industry sectors, law enforcement and market organisers and stallholders have joined forces to clean up markets throughout the UK - in the past year 117 markets have already signed up to a voluntary charter, with many more targeted for this year.

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<sup>83</sup> <http://www.ipo.gov.uk/pro-policy/pro-crime.htm>

<sup>84</sup> <http://www.realdealmarkets.co.uk/>



Like the Internet Stakeholder Forum mentioned in Section 4 above, this is an example of a successful voluntary initiative to address the problem of lack of regulation (markets being the prime source of fakes offline). Many are increasingly of the view that it is essential to try and reach such voluntary agreements, rather than resort to more regulation, where at all possible.

Some trading standards authorities fulfil the IPR enforcement to a high standard, but unfortunately they are in the minority, and are not always in 'hot spot' areas for counterfeiting, so the national picture is very patchy. This may be a fact of life where local councils have so many competing priorities but it does give rise to many problems for rights holders and results in more counterfeit products staying on the market.

One downside of POCA as it currently works, with resources so stretched, is that some authorities now only act where financial recovery is likely, but are not equipped to devote the necessary resources in order to run more than one or two of these cases a year.

Our members have reported instances where they have allocated their own resources to operations which mobilise not only trading standards but also police, immigration and Department of Work & Pensions staff, for example a raid on a large Sunday market, but the operation is cancelled at short notice for lack of resources, including withdrawal of police support because of other priorities.

It is no longer feasible for IPR enforcement to be dealt with like this. The IPO does not have the necessary powers. Trading standards work at local level, while counterfeiting is a serious organised crime on a global scale and those fighting it must be able to take the necessary actions internationally, maximising available resources.

Our thinking is at an early stage and this issue has several interlocking solutions, which need further discussion and consideration outside of this review:

#### 5.2.1 Assets recovery

As mentioned in section 4 above, IP crime is a lifestyle offence under the Proceeds of Crime Act 2002, a model piece of punitive legislation which is envied around the world. Therefore, an IP crime offence automatically triggers the Act's confiscation provisions.

However, prosecutions are expensive and time consuming for a local council with many other statutory responsibilities. Most local authority lawyers (understandably) do not know much about major criminal prosecutions, let alone IP crime and Proceeds of Crime Act confiscations. But under the Proceeds of Crime Act's incentivisation scheme, investigators and prosecutors can share in half the recovered assets, which could eventually make such actions self-funding.

Specially trained and accredited financial investigators must conduct Proceeds of Crime Act proceedings. Some are now trained within local authorities, but not enough of them. The police are much better resourced for this work, and we have evidence of increasing interest in IP crime as forces realise the ways in which pursuing the criminals involved can lead to solving other crimes, finding organised criminal gangs and recovering substantial criminal assets.

**12**

**Barrier to growth**

Trading standards lack the resources to pursue confiscation proceedings often enough, because of the high initial costs with no guarantee of success. Some authorities now pursue only high-value cases of IP crime. The high risk/cost generally of bringing major international criminal gangs to justice, and seizing their assets, inhibits full use of POCA, which could be a huge source of funding for the justice system.

**Recommendation**

Examine feasibility of transferring responsibility for IPR enforcement e.g. to the police. Review the current provisions for criminal confiscation and identify ways to speed up the process. Examine the options for future conduct of proceedings to escalate the benefits of using POCA to make the criminals pay for the cost of bringing them to justice.

5.2.2 The Home Office serious organised crime strategy

The Home Office and the Serious Organised Crime Agency (SOCA) are already in overall charge of serious organised crime, and are showing increasing interest in top-level IP crime. (The Proceeds of Crime Act falls within the Home Office's remit.)

Local consumer protection aspects of IP crime, such as the innocent purchase of fakes, can continue to be dealt with by trading standards, as can related statutory criminal enforcement functions at local level.

At national operational level, the police may already have the capacity and expertise to include all large-scale IP rights enforcement in their remit, though resourcing will need to be clarified before considering the practicalities of transferring all responsibility.

City of London Police is the national lead for fraud in general and already has several successes in large-scale IP crime cases. An example (from section 4) is Operation Blackout in March 2010, a transatlantic operation with US Immigration & Customs Enforcement (ICE) in which counterfeit clothing and footwear worth £3.5 million was seized and an international criminal gang smashed.<sup>85</sup>

We understand that the government's preferred strategy to deal with serious organised crime is to follow the money, which we welcome as the most effective deterrent. Although the UK's assets recovery regime is the envy of the world, it is not being used effectively against one of the most profitable low-risk crimes of all.

Our views are obviously subject to the full implications of cuts in public spending, once known. Risks will be attached to whichever course is followed by government, but we believe that all the issues can be effectively addressed by restructuring IP policy and IP rights enforcement.

This proposal also needs to be seen in the context of the UK's part in establishing effective international enforcement strategies - the future success of which will determine whether or not the internet can be successfully policed.

<sup>85</sup> <http://news.bbc.co.uk/1/hi/england/london/8576880.stm>

**13**

**Barrier to growth**

Ineffective, fragmented and localised IPR enforcement delivered via trading standards, and counterfeiting not sufficiently recognised within government as a serious organised crime.

**Recommendation**

Further consideration should be given to including enforcement of the criminal provisions in the Trade Marks Act 1994 and the Copyright Designs & Patents Act 1988 in the new Home Office organised crime strategy, dealt with in the same way as all other serious organised crimes, with the police and SOCA primarily responsible. Consumer-related issues with counterfeit and pirated products at local level could continue to be dealt with by trading standards as part of their new consumer protection and enforcement remit.

See US model below.

5.2.3 A leader for the UK's IPR enforcement strategy

Interestingly, ACTA contains several provisions that encourage signatories to appoint someone responsible for coordinating national IP rights enforcement and contributing to the international enforcement effort.

To date, only one European country, Italy, has made a serious attempt to create a national co-ordinator, appointing Giovanni Kessler to the role in 2007. Unfortunately, after a promising initial two-year period, the post was scrapped.

At that time, the Italians also called on the European Commission to appoint a specialist EU anti-counterfeiting commissioner to tackle the growing economic problems caused by counterfeit goods. However, including such a function in a commissioner's portfolio has not yet been attempted. It would be hard to decide under which portfolio it would fall – dividing up the responsibilities between all 27 European commissioners is complex.

At present, counterfeiting and related enforcement issues fall under the remit of several directorates, include DG TAXUD (European Customs) and DG MARKT (Internal Market, with Unit D3 leading on such matters as the EU Observatory on Counterfeiting and Piracy).

Here in the UK, we first need to decide which department should lead operationally on IPR enforcement, and then establish a centralised body, which will include representatives from all agencies, to coordinate at strategic level, integrated with the national serious organised crime strategy.

5.3 The US IPR Enforcement Model

In common with many other European countries, the UK has a different political and legislative system from the United States. Rights holders lobbied long and hard in the US for more priority to be given to IP rights in its economic and trade policies, and for more effective IPR enforcement.

President Obama has responded with a comprehensive plan, and great changes have been introduced there, with support right from the top. We are keen for government here to scrutinise the resulting US strategies in relation to IPR enforcement, to see how their methods might add value in the UK.

### 5.3.1 IP Enforcement Coordinator (IPEC)<sup>86</sup>

In 2009 Victoria Espinel was appointed as the IPEC. Confirmed by the Senate, she reports directly to the White House, a measure of how highly the new post is regarded.

After soliciting comments from a wide range of stakeholders, Espinel published the Joint Strategic Plan on IP Enforcement last year which, among other things, seeks to develop robust data-driven economics in order to quantify effectively and demonstrate to policymakers the cost of IP crime to the US economy.<sup>87</sup> The level of buy-in from all relevant US agencies and government departments is impressive.

The IPEC's joint strategic plan is a potential blueprint for any successful IPR enforcement strategy. One of the most important features is the buy-in by all government departments and the total support for this strategy of the President, the Vice-President and the Attorney-General, in particular.

Historically, the US has always aimed to be the world leader, and this new initiative is no exception. An important part of the IPEC's remit is to develop a coherent US international enforcement strategy, partly with its trade policy as a vehicle. For example, the coordinator has already visited China as part of the US trade representative's team. All IP-rich nations need to assess this new post as a potential model and to ensure that their own international standing is maintained, particularly once Espinel has entered the next phase and begins to work towards the strategy's objectives: increasing transparency, ensuring efficiency and coordination nationally, enforcing IP rights and securing the supply chain internationally. The European Commission is monitoring her progress with interest, but is awaiting further developments before considering something similar at EU level.

Most European countries have a different political and legislative system to the US and are simply not yet ready to graft this kind of role onto their IP frameworks and enforcement regimes. There are challenges, such as whether the role may usurp or interfere with the enforcement powers of other agencies, but there is scope for such an appointment, as the Italians indicated over three years ago.

In the UK, the first step is to determine where IP policy and IP rights enforcement should sit within our political and law enforcement system. Only then should such an appointment be considered.

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<sup>86</sup> <http://www.whitehouse.gov/omb/intellectualproperty>

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[http://www.whitehouse.gov/sites/default/files/omb/assets/intellectualproperty/intellectualproperty\\_strategic\\_plan.pdf](http://www.whitehouse.gov/sites/default/files/omb/assets/intellectualproperty/intellectualproperty_strategic_plan.pdf)

### 5.3.2 The National IPR Co-ordination Center<sup>88</sup>

This is another prong of the same push within the US to create a joined-up IPR enforcement strategy. This has a task force structure and is managed within the Department for Homeland Security. It houses the FBI's IP HQ as well as Immigration and Customs Enforcement investigations. One of its latest notable achievements is Operation In Our Sites (US internet takedowns, see section 4 above).

### 5.3.3 Early in February 2011, two new committees were launched.<sup>89</sup>

- A Cabinet level *Senior Intellectual Property Enforcement Advisory Committee* heads of the Departments responsible for intellectual property enforcement, including the Departments of Justice, Homeland Security, Commerce, Health and Human Services, State, Treasury, Agriculture and USTR;
- The *Intellectual Property Enforcement Advisory Committee* - representatives from the agencies responsible for designing and carrying out the Administration's strategy for stopping intellectual property theft.

#### **Remarks by the US President on Innovation and Sustainable Growth- September 21, 2009**

"That's why it's essential that we enforce trade laws and work with our trading partners to open up markets abroad; that we reform and strengthen our intellectual property system; that we sustain our advantage as a place that draws and welcomes the brightest minds from all over the world; and that we unlock sources of credit and capital which have been in short supply as a result of the financial crisis."<sup>90</sup>

It can be seen that a strong coherent structure is swiftly emerging in the US to provide the necessary support for an effective IP framework, which is seen as crucial to the country's future. It is good to see these initiatives being framed in the context of global competitiveness, export growth and job creation, though this is a move in the opposite direction to that recently taken in the UK, as trading standards is restructured into other areas of responsibility and there is not even a dedicated Minister for IP.

The most important lesson from the US model is to look at how IP is now embedded in all relevant policy areas connected with promoting US innovation and growth.

#### **14**

##### **Barrier to growth**

The UK enforcement model still has no strong leadership, despite best efforts by individuals within law enforcement to bring IP crime up the political and operational agenda.

##### **Recommendation**

The US IPR enforcement model warrants further attention – especially the extent to which it offers a blueprint for a successful national IPR enforcement strategy. Further analysis of the work of the Co-ordination Center and the new Committees would also be of benefit.

<sup>88</sup> <http://www.ice.gov/iprcenter>

<sup>89</sup> <http://www.whitehouse.gov/blog/2011/02/08/president-establishes-intellectual-property-enforcement-advisory-committees>

<sup>90</sup> <http://www.whitehouse.gov/omb/intellectualproperty/quotes>

## 6 IP and competition

### 6.1 Brands and competition

Competitive markets have long been heralded as crucial to successful economies, with competition providing a spur to innovation and value to consumers. An effective competitive market is one where competition between suppliers is vigorous but fair, barriers to entry are low to encourage a diversity of players and products, and consumers are confident and able to make well-informed purchasing decisions.

Branding, underpinned by IP rights, represent a strongly pro-competitive force.

- brand investments in reputation, captured in trade marks, enable consumers to identify clearly one offer from another, to have the confidence that their choice will at least meet their expectations and to have access to speedy redress when needed (with the branded company keen to preserve its reputation). The result is high levels of consumer confidence;
- branded companies continually seek to deliver added-value to consumers, resulting in consumers being presented with a wide range of choices reflecting the needs of different consumers (for example, the different positioning of **Yorkie** and **Galaxy** chocolate) or the differing needs of the same consumer (for example, **Walkers** crisps for everyday, **Sensations** crisps for a more exotic experience, and **Tyrells**, **Red Sky** and **Kettle** crisps for more premium occasions). These everyday examples illustrate the diversity and choice provided by brand manufacturers, how brands help consumers choose quickly and accurately between offers, and the vigorous competition that results, based importantly on price, performance and quality (i.e. not just price).

Some economists have argued that branding, by creating consumer loyalty, may create a barrier to market entry as consumers may be reluctant to switch to a competitor. Such an analysis is over-simplistic. Creating products that consumers value and setting benchmarks for quality which consumers then consider the minimum do not inhibit competition. The success of new products such as the **Firefox** search engine and **Dyson** vacuum cleaners suggests that incumbent brands do not pose a barrier to new entrants, even in mature markets, and instead act as a spur to innovate.

In a free market economy, where companies are making significant investments in their product offerings and in their reputation, those companies should be able to determine the distribution and marketing strategies that they consider optimal. Should they prove sub-optimal, market forces present the most appropriate remedy, opening up opportunities for competitors to exploit.

### 6.2 IP and competition law

Competition law (which fosters competition) and IP rights (which protect rights owners and consumers) have very different aims, though they complement each other. For example IP, by enabling investment and allowing one offer to be quickly and easily identifiable from another, facilitates competition.

The current balance between IP and competition law is finely drawn and we would urge extreme caution were there any move to change it.

We are conscious that there are some who see IP rights as monopolistic and thereby *per se* bad. This view fails to take into account the innovation and diversity (and as a result, competition) that such rights reflect and generate, and the contribution they make to economic and employment growth. It also fails to reflect the subtleties of the inbuilt checks and balances within the IP system itself such as permitted exceptions to the rights and the fact that copyright and unregistered design rights only protect against copying, not independent creation. Such anti-IP views are of particular concern when expressed by regulatory authorities, reinforcing the importance of strong awareness of the economic role of IP.

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### **Barrier to growth**

The absence of a coherent government view on the positive contribution of IP to the economy and competition inhibits coherent, consistent policies.

### **Recommendation**

The economic value of IP rights, including their relationship with innovation, diversity, competitive markets and economic and employment growth, requires evidence, articulation and acknowledgment within Government and regulatory bodies. The review is well-placed to highlight this need.

In response to the Review's specific questions:

- we consider the current IP and competition frameworks to be finely balanced and to operate well together. We would urge extreme caution were there any proposal to change this balance;
- we are not aware of any instances where competition is hindered by lack of transparency;
- we have no experience of anti-competitive impacts arising from the IP system;
- we do not foresee any opportunities to stimulate growth or innovation through a re-balancing of competition and IP regimes.

### 6.3 IP and unfair competition law

In contrast to the current position in the UK, specific provisions in unfair competition laws in various other members states provide branded companies with effective redress against parasitic copying as described in section 3 above. The nearest equivalent in UK law is passing off but this is more limited in scope.

An unfair competition-type approach, focused on parasitic trading, would provide civil rather than criminal sanctions (as compared to the current – under-enforced – remedies under the UK implementation of the Unfair Commercial Practices Directive). No additional monopoly rights would be conferred, allowing each individual case to be considered on its merits.

### 6.4 Selective distribution

Some branded companies make the commercial decision to distribute their products through selective distribution systems (i.e. retailers that are required to meet certain standards) as a means of differentiating themselves from competitors and exerting

greater control over consumers' brand experience. These are regulated under European competition rather than IP law, with revised competition rules and guidelines published last year<sup>91</sup>, permitting such systems as long as, for example, the producer and distributor fall below a 30% market share test and agreements do not set retail prices.

Importantly, the new guidelines recognise that selective distribution systems can be justified on the basis of the characteristics of the products being sold, including their image, and set out parameters for online sales to ensure they are as consistent as possible with those set out for bricks-and-mortar outlets.

Selective distribution systems that comply with the guidelines are pro-competitive as they increase inter-brand competition, enabling branded companies to further differentiate their offer to consumers (i.e. at both the product and retail level) and increase consumer choice as a result. Such systems are vulnerable however to the effects of grey trade, reinforcing the need for companies to have effective tools to address such trade when it occurs without their consent.

Companies such as **Anya Hindmarch** handbags and leather goods and **Smythson** stationary adopt a selective distribution business model while **Ted Baker** apparel and handbags and **Letts Filofax** stationary adopt a business model aimed at wide distribution to the mass market.

## 6.5 Grey trading

By grey trading we mean the importation of goods into the single market from other non-EU countries without the consent of the trade mark owner.

Branded companies that operate in both the EU and other markets may well be vulnerable to grey trade and may look to trade mark rights embodied in EU trade mark law to prevent such trade from outside the EU.

Branded products represent ready markets for grey traders, due to companies' investments in product quality and reputation. The added value some command provide a further attraction (grey traders face no barrier in importing cheap generic products but tend not to do so because their profit margins would not be high enough).

A wide range of goods are grey traded, including soap, cola, toothpaste, alcoholic drinks, batteries, razor blades, sunglasses, engine oil, car tyres, motorcycles, shoes, CDs, mobile phones, nappies, clothes, accessories, car parts, toiletries and many more.

The current trade mark regime is appropriate to the nature of the (high cost) European economy and any change would be damaging, for a range of reasons:

- where arbitrage is fuelled by exchange rate fluctuations or high costs in specific markets (e.g. the UK), companies in those markets would be economically punished, reducing their ability to invest and innovate;

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<sup>91</sup> [Commission Regulation \(EU\) No 330/2010 of 20 April 2010 on the application of Article 101\(3\) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices \(Text with EEA relevance\)](#)



- manufacturers would be under greater pressure to move to low cost countries. This would be a net loss to the UK in terms of investment and jobs, while fuelling the competitiveness of countries such as India and China;
- it may no longer be economic to supply countries where prices are lowest, due to the risk of grey trade (these may be the very poorest economies). Market withdrawal would reduce consumer choice and competition in those countries. It may also reduce economies of scale which would be price inflationary;
- it would be much more difficult to develop and grow new overseas markets by reducing prices to prompt trial. This would inhibit significantly UK exports;
- it will be harder for UK companies to compete in overseas markets on the basis of price, and to survive price wars, as this will create an opportunity for grey trade.

The current regime is intended to favour consumers. However, in many instances, grey imports are sold to consumers at full prices, as grey traders and their retailers seek to maximise their own profits.



During its grey trading dispute with Levi Strauss, Tesco sold parallel traded goods at full prices. There is no evidence that retailers would price differently were goods 'grey'.

Grey imports may also present specific consumer disadvantages:

- lack of consistency of product — grey goods may be: formulated for different market tastes and climatic conditions; last season's stock; or salvage;
- subject to less quality control, as such goods circulate outside official supply chains;
- guarantees may be invalidated;
- be accompanied by incomprehensible foreign language labels and instructions.

The current regime also helps control the trade in fakes. Counterfeiters have been known to infiltrate unofficial supply chains, mixing counterfeit goods with grey traded goods. **Nike** for example discovered counterfeit goods in batches of grey traded sportswear and **GlaxoSmithKline** found a UK wholesaler selling grey traded toothpaste from South Africa alongside purportedly grey traded, but in fact counterfeit, toothpaste from the Middle East. Customs officers can only check a small percentage of shipments; if the numbers of shipments from unauthorised channels were to increase, more counterfeits would pass undetected.

Retailers generally are free to source very low priced commodities on the world market as well as branded goods, as long as this does not contravene the rights of the specific brand owner.

It has been put to us by the IP Review team that wealth generated by grey traders could circulate in the UK economy and contribute to growth. This premise would depend on the country where the trader was domiciled and could only displace the contribution made by existing trade. If the UK, any economic benefit would need to be offset by an expected reduction in investment and innovation in the UK by companies which have a demonstrable record for generating economic value added. The loss of jobs as more operations move to lower cost economies would also need to be factored in, along with any detriment to consumers. We are not aware of any such economic study, but would expect such an analysis to endorse strongly the status quo.

## 6.6 IP and buyer power

While we do not believe the IP system gives rise to anti-competitive impacts, we do believe there to be instances where buyer power may inhibit the proper functioning of the IP system.

A recent Competition Commission market investigation into the grocery sector found that all large retailers and wholesalers have potential buyer power in relation to at least some suppliers.<sup>92</sup> With ongoing consolidation in a number of retail markets, we believe this also holds true in sectors other than grocery, with large retailers acting as gatekeepers to consumers, deciding on what products it will stock and on what terms.

The scale of some retailers is now such that suppliers are dependent on them and negotiating power rests decisively with the retailer. This is particularly acute in relation to retailers with own label ranges and in relation to smaller suppliers. For example, the Competition Commission found that Tesco accounted for 20-30% of large suppliers' sales while Tesco's largest supplier accounted for only 2.7% of the retailer's total purchases (the median supplier accounted for 0.0024% of Tesco's purchases).<sup>93</sup>

We are aware of instances where suppliers, seeking listing for innovative products, have faced demands from retailers to hand over IP rights as a condition of listing. This we consider to be an abuse of buyer power and an inhibitor to innovation and growth. Suppliers will not invest in innovation if they risk losing IP rights as a condition of

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<sup>92</sup> Competition Commission, "[The supply of groceries in the UK market investigation](#)", paragraph 35 (2008)

<sup>93</sup> Competition Commission, "Supermarkets", paragraphs 11.17-11.18 (2000)

securing important routes to market, as their ability to earn a return will be placed in jeopardy.

While we currently make no recommendation for action, policymakers should be aware of and monitor the effects of buyer power on the functioning of the IP system.

#### 6.7 Retailers as customers and competitors (Trade secrets)

Retailers with own label ranges are double-agents, acting on the one hand as retail customers of suppliers, providing route to market, and at the same time as direct competitors via their own label products. This gives the retailer access to information that would not be available to competing manufacturers and which competing manufacturers would generally be prohibited from sharing as being contrary to competition law. This gives retailers near perfect information, as they will know the new product and marketing plans of all their suppliers many months in advance and well before other product competitors. This information can then be used freely to plan their own label ranges and marketing tactics. In addition to this advance knowledge, retailers enjoy significant competitive advantages, including the setting of the retail price of their own and of competing products and controlling the in-store and online sales environment for all products stocked.

The transfer of highly sensitive commercial information between horizontal competitors would normally be considered a breach of competition rules, but is not in this instance due to the retailer's customer (vertical) role. There are direct negative implications for innovation, as retailers may launch competing own label equivalents far sooner than would otherwise be possible due to the advance information to which they are privy. This reduces the time the innovator has to earn a return on its significant innovation investment.

In such circumstances, trade secrets and confidentiality could have some role in preventing sensitive commercial information being passed from the retail buyer to the retail specifier / producer of that retailer's own label products. In practice, the scale and consequent negotiating power of the retailer is such that confidentiality agreements are rendered ineffective as suppliers are inhibited from enforcing them.

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##### **Barrier to growth**

Buyer power inhibits suppliers enforcing confidentiality agreements with powerful retailers who stock own label ranges. Such retailers are thereby able to launch competitive products much sooner than other competitors, reducing the time available for innovators to earn a fair return from their significant investments and risk.

##### **Recommendation**

The review to highlight the implications for innovation where sensitive commercial information is exchanged with retailers who are also horizontal competitors. Regulatory guidance is required to establish confidentiality for information imparted to secure retail listings, preventing its transfer to competing own label products.

## 7 SMEs and access to IP services

### 7.1 Barriers facing SMEs in accessing IP services

The main barriers to SME's exploiting profitably their innovations are not the current IP structure but a range of other factors such as:

- the lack of access to funds for start-ups;
- the short term view of funders;
- the requirement that the IP be assigned to the funder as security;
- the lack of affordable insurance;
- the consequences and life-long effects of failure in the UK (in contrast to the US);
- the predatory actions of some retailers.

The main IP-related barriers that some, but not all, SMEs face are (1) a lack of awareness of IP and how the IP system works, and (2) a lack of money for investing in IP protection and associated professional advice. In our view the government could do more to educate people about IP, as discussed further below.

We do not consider that there is an inherent issue of cost in relation to the IP system that is impeding the UK economy. SMEs sometimes consider that they are at a financial disadvantage compared with larger companies when they engage with the IP system but this concern is not limited to the IP system; it applies to commercial activities more generally. The introduction of new rules for the Patents County Court should address one of the biggest areas of concern. Sometimes, the problem for SMEs is simply that the small scale of their activities is not sufficient to justify the costs of IP protection. This should not, of itself, be a cause for concern.

Nor do we consider that the UK IP system is inherently "user-unfriendly". Protection of copyright, trade marks, designs and confidential information is relatively straightforward. The patent system is more complex, which is partly due to the technical subject matter of patents, and partly due to the way in which patent law and practice has developed internationally. It might be possible, in theory, to design a patent system that is more user-friendly. However, if such a move were thought both desirable and realistic, it would almost certainly need to be done at an international, rather than a national level.

If the government wishes to encourage or "pump-prime" the SME sector, then clearly one way of doing this would be to subsidise the cost of accessing IP services. However, general tax incentives (eg the "patent box" and R&D tax credits) may be thought a more suitable way of encouraging the growth of SMEs than focussing on the IP system as such.

It is important to distinguish different types of SME that may wish to protect and exploit IP. The IP-awareness, levels of understanding and financial resources of SMEs vary considerably. The following broad categories are suggested; although by no means comprehensive, they may help to focus attention on the varying needs of SMEs.

1. "**Sophisticated SMEs**": Sophisticated start-up companies that receive venture capital or business angel funding, and which invest in high-quality professional advice. For example, this category will include many technology spin-outs from universities. Some of these companies are set up with a view to eventual Stock

Market flotation or a trade sale to a larger (often, multinational) company, and their senior management is likely to have prior business experience and be used to working with patent agents and lawyers.

2. **“Graduate SMEs”**: New businesses started by university students and graduates. This category will include some computer games and internet-based companies. Graduate SMEs are likely to be inexperienced in IP issues but, with access to the right information, could become sophisticated users of IP.
3. **“Traditional SMEs”**: Traditional SMEs, including family businesses, that might benefit from a greater access to IP services, but whose business focus and experience do not include IP. For example, this might include a stationery supply company that could benefit from franchising its operations (including registering trade marks and maintaining a package of confidential information), or a furniture maker that could benefit from registering its designs. This category is likely to be the least sophisticated of the three when dealing with IP issues, perhaps becoming aware of the importance of IP protection only when they find that others have copied them. At this point it may be too late or too expensive to secure their rights.

In general, Sophisticated SMEs face fewer barriers than the other two categories. They are able to access high-quality professional services, including in the IP field. Their senior management may already be familiar with business models that make use of IP (e.g. licensing, franchising) and they are likely to understand the importance of IP protection. A potential area of concern is the cost of IP litigation. However, insofar as their focus is on the UK market, the new rules for the Patents County Court may go a long way to addressing this concern.

Any efforts to improve SME access to IP services should therefore probably focus on Graduate SMEs and Traditional SMEs rather than on Sophisticated SMEs.

The main concerns of Graduate SMEs, in our view, are likely to be a lack of awareness of IP, and a lack of financial resource to make best use of it. Once familiar with the IP system, a Graduate SME will become aware of the need to be sufficiently capitalised to invest in IP protection, and will build this factor in to their business model. The main focus of any efforts to improve Graduate SMEs' access to IP services should, in our view, be on education as to how the IP system works, what it protects and why such protection may be important for the Graduate SME's business.

Traditional SMEs may experience significant barriers to accessing and making use of IP and in some cases may be inadvertent infringers of others' rights. Such SMEs are often based on very simple business models, where the main focus is on marketing and sale of goods and services (sometimes in a limited geographical area), and where the SME has limited exposure to complex legal and financial issues. In this environment, any level of legal complexity may be difficult for the SME to deal with, and the available financial resource for dealing with IP issues may be insufficient. This is not necessarily the fault of the IP system; it is just a fact of life for many Traditional SMEs. Nor is it just an issue in relation to IP. The Traditional SME may find it equally difficult to deal with other sophisticated business issues, e.g. deciding upon tax-efficient corporate structures,

complying with regulations affecting the industry sector in which the SME operates, or operating in other countries.

Information and training on IP issues will assist some, but not all, Traditional SMEs.

These barriers may mean that the least sophisticated, Traditional SMEs do not make full use of the IP system. This should not, of itself, be a cause for concern. What might be of greater concern, in our view, would be if the IP system were “dumbed down” to focus on the needs of some Traditional SMEs. In our view the UK IP system does and should take account of the needs of its main users, which include large companies, Sophisticated SMEs and Graduate SMEs.

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### **Barrier to growth**

SMEs may be too diversified a group to be considered to have common needs. Too generic an approach to IP access may not be cost-effective due to the scale of the task, while a more targeted (but not exclusionary) approach may yield stronger results.

### **Recommendation**

Explore the potential to segment SMEs by their differing approaches to and needs for IP. Determine for each segment their IP requirements and the extent to which the IP system should be made more accessible.

## 7.2 Overcoming barriers

The priority in our view is to provide SMEs with greater opportunities for training in and access to the information about IP issues. This should include training at school and at university, as well as vocational courses. We recommend that there should be increased government funding for training courses on IP subjects, designed not for the IP specialist but for people working in SMEs and business generally, including commercial, scientific and technical staff.

We note that the IPO has several initiatives in this area, including:

- Its outreach activities with schools, using the “Wallace and Gromit” characters;
- The consumer focus of parts of its website;
- The work of its Business to Business Licensing committee, which has produced several booklets on IP and IP licensing, targeted at SMEs.<sup>94</sup>

To overcome barriers to SMEs engaging with the IP system, greater investment in the IPO website would be a cost-effective solution. The impression is that the IPO is doing its best on that website, but it is ultimately a technical branch of government and it may not have the commercial and educational experience, nor the budget, to make the website truly user-friendly. This will require input from several directions:

1. Advice from IP specialists as to the technical content of the site (including greater use of experienced IP professionals);

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<sup>94</sup> This initiative was originally intended to produce standard licence agreements as recommended by the Gowers Committee. The B2B group quickly (and rightly) concluded that it was an unrealistic aspiration to produce standard licence agreements, and focussed instead on information booklets.

2. Advice from commercial/communications specialists as to how to present the technical information in a user-friendly way;
3. Advice from designers as to how to make the website visually appealing;
4. Advice from brand owners on the business perspective

Links to useful third party sites would be beneficial, not necessarily endorsing content but identifying them as sources of expertise.

Educational initiatives (and, for that matter, the consumer section of the IPO website) should be targeted at those SMEs where IP is likely to have most relevance and potential. In other words, they should not be “dumbed down” to a general consumer level but should assume a reasonable ability to assimilate complex information, for two reasons:

1. IP issues have some inherent complexity, and if SMEs are to deal with IP issues themselves rather than pay for professional advice, they need to be able to grapple with the details; and
2. Focusing resources on educating the most IP-relevant SMEs about IP is likely to show a greater return for the economy than a more general approach. The focus should be on SMEs that are more likely to build successful IP-based companies.

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### **Barrier to growth**

SMEs in IP-relevant businesses will not realise the potential of their businesses if they are unaware of, or inhibited from engaging with, the IP system.

### **Recommendation**

Understand the needs and requirements of those SMEs to whom IP is most relevant and both target and design educational initiatives accordingly. Initiatives to be professionally structured, based on a clear understanding of the needs of recipients.

A complaint sometimes heard from small-scale SMEs is that the IP system is too expensive. This is discussed above. In this context, the initiative of Creative Barcode (<http://www.creativebarcode.com/>) is interesting. In the creative design sector, SME-designers are often asked to furnish proposed designs “on spec”, before entering into any contract with the commissioner (which might, for example, be an advertising agency). The commissioner receives designs from several SMEs, chooses which design it likes best and should then enter into a contract with the relevant designer. However, it is not unknown for designs and design ideas to be used without attribution or compensation. Sometimes this happens through carelessness or ignorance of IP issues, or a failure of communication between departments of the commissioning company, rather than through a deliberate intention to cheat the designer. Creative Barcode provides a means for designers and other creators of IP to “tag” their designs with a barcode, and for commissioners to “sign up” to the principle of ethical conduct when dealing with SME-designers. The system is based as much on contract law, education and moral pressure as it is on classic IP rights. Although in its early days, this system could become a cheap and simple alternative to formal IP protection, and could be applied more widely than the creative design sector. Parallel initiatives are underway to facilitate licensing of copyright content via unique identification data associated with that content.