



Counterfeiting

A global spread
A global threat

2011 Edition
Advanced Unedited Edition

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First published 2011.

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ACKNOWLEDGEMENTS

This Report was prepared by the Emerging Crimes Unit of the United Nations Interregional Crime and Justice Research Institute (UNICRI), under the supervision of Ms. Angela Patrignani. The following individuals contributed towards the research and drafting of this Report:

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- Salome Stevens, Intern.

The drafting of the Report was supported by the contribution of different Agencies and Organizations. In particular, noticeable support was provided by:

- Europol
- The Italian Guardia di Finanza
- The Italian National Anti-Mafia Bureau
- The Italian Prosecution Office attached to the Court of Naples, Vice Chief Prosecutor Fausto Zuccarelli
- The National Authorities of the Kingdom of Thailand.

UNICRI would also like to thank all of the experts, Law Enforcement Officers, and Representatives of National Authorities who provided us with valuable information during the interviews we have conducted.

The realization of this Report was made possible thanks to the support of the Italian Ministry of Economic Development and the Italian Ministry of Foreign Affairs.

LIST OF ABBREVIATIONS

- AGC: Allied Glass Containers
- ALAFARPE: Peru's Association of Pharmaceutical Laboratories
- ASEM: Asia Europe Meeting
- BASCAP: Business Action to Stop Counterfeiting and Piracy
- CACN: Canadian Anti-Counterfeiting Network
- CCPCJ: United Nations Commission on Crime Prevention and Criminal Justice
- CEBR: Centre for Economic and Business Research
- DIGEMID: Peruvian General Directorate of Medicines, Supplies and Drugs
- EU: European Union
- FAA: United States Federal Aviation Authority
- FBI: United States Federal Bureau of Investigation
- FDA: United States Food and Drugs Administration
- FSHSS: Russian Federal Service for Health Sphere Supervision
- GACG: Global Anti Counterfeiting Group
- GMA: Grocery Manufacturers Association
- ICE: United States Immigration and Customs Enforcement
- IPR: Intellectual Property Rights
- MEMA: Motor and Equipment Manufacturers Association
- NAFDAC: Nigerian National Agency for Food, Drugs Administration and Control
- NQCL: National Quality Control Laboratories
- OECD: Organization for Economic Cooperation and Development
- OLAF: European Commission Anti Fraud Office
- RAPO: Russian Anti-piracy Organization
- SFDA: Chinese State Food and Drug Administration
- SUPs: Suspected Unapproved Parts
- TAXUD: European Commission Taxation and Customs Union
- TRIPs: Trade Related Aspects of Intellectual Property Rights
- UNICRI: United Nations Interregional Crime and Justice Research Institute
- U.S.: United States of America
- WCO: World Customs Organization
- WTO: World Trade Organization

FOREWORD

There is a general and spread tendency in underestimating the seriousness and gravity of counterfeiting. When UNICRI wrote its first Report dedicated to this issue in 2007, our choice was clear: we will foster the change of this attitude and show how dangerous counterfeiting is for the society as a whole.

We presented the hazardousness of this activity by touching upon several elements of concern directly linked to this crime. On that occasion we focused in particular on the health and safety consequences for citizens that certain categories of counterfeit products can cause and on the involvement of organized crime in this illicit trade. If in 2007 we considered such aspect as one of the several aspects that should allow us to change our perception of counterfeiting, with the 2011 Report we have put organized crime at the core of the problem. The research efforts spent in these years convinced us that organized crime involvement is the most compelling aspect that has to be taken into account when tackling counterfeiting. This view does not neglect nor underestimate the serious risks created by counterfeit products for consumers: to the contrary, these aspects have been fully taken into account into this Report.

Counterfeiting is today a rampant business involving extremely complex distribution networks and increasingly flooding the markets of all countries in the world with dangerous and potentially deadly products. Organized crime is the reason behind this global spread. Criminal organizations are the real managers of this trade, having transformed counterfeiting into a veritable illicit mass production and distribution enterprise.

The spread of counterfeit products we are experiencing today would not be possible without the involvement of unscrupulous criminals, who everyday sell counterfeit medicines to unaware patients, put adulterated food and beverages on supermarket shelves, and make our children play with counterfeit toxic toys.

The illicit reproduction of certain product categories is cause for greater concern, because of the negative consequences they can have on consumers' safety. However, the counterfeiting of all products must be strongly condemned and fought as it gives criminal

organizations an incredible operative capacity in consequence of the noticeable profits that derive from this activity.

There is no doubt today that counterfeiting is an emerging global threat managed by criminal organizations and, we must add, a rapidly growing and expanding one. For this reason UNICRI welcomes the discussion on this topic started during the works of the 19th session of the United Nations Commission on Crime Prevention and Criminal Justice (UNCCPCJ) held in Vienna in May 2010. We are honored for the invitation from the UNCCPCJ to update our 2007 Report, *Counterfeiting, a global spread, a global threat*, and to present its updates to the 20th Session of its works.

The possibility of discussing these issues within this important international forum is a first but significant step to consider placing the fight against counterfeiting within the wider fight against transnational organized crime, starting the engines of a needed and deeper cooperation among Member States on this topic. UNICRI is ready to support this process and will continue to enhance the spread of knowledge regarding counterfeiting, the criminals and its consequences, while further implementing concrete actions that will have the potential to represent a step forward in the fight against this emerging form of crime.

Kristiina Kangaspunta
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1. COUNTERFEITING: A GLOBAL SPREAD, A GLOBAL THREAT

1.1 Introduction

In 2007 the United Nations Interregional Crime and Justice Research Institute (UNICRI) published its first Report on counterfeiting and organized crime: *Counterfeiting, a Global Spread a Global Threat*.¹ The purpose was to collect, systematize and present a consistent set of information on the involvement of organized crime in the production and distribution of counterfeit products together with the consequences that this illicit activity creates for society as a whole.

The 2007 Report contributed to raising awareness on these issues, supporting an international discussion on the seriousness of counterfeiting and offering concrete proposals on possible ways forward. By highlighting the shortcomings, of national and international responses to counterfeiting as well as through a comprehensive analysis of the problem, these proposals were presented as Recommendations, intended to support a necessary step forward in the way in which the problem of counterfeiting and piracy was perceived, analyzed and confronted. These efforts have led to the design of the UNICRI Programme on counterfeiting: a series of projects² intended to concretely contribute to the implementation of the 2007 Report's Recommendations.

The findings of the Report and its Recommendations received international recognition on the occasion of the 2008 Global Anti-Counterfeiting Awards, when an international panel of experts awarded UNICRI with a High Commend for its excellent

¹ Refer to: UNICRI (2007), *Counterfeiting, a Global Spread a Global Threat*, December. The Report is freely downloadable from <http://counterfeiting.unicri.it/report2008.php>

² The programme covers the thematic areas identified in this study, trying to address the complexity of counterfeiting with a multidisciplinary response. Research projects aimed at improving the knowledge on the problem are flanked by training activities implemented in cooperation with law enforcers, while a new series of project proposals explore the importance of technology in fighting against counterfeiting and organized crime, protect consumers and support data collection. For more information, please visit UNICRI website dedicated to counterfeiting: <https://ctf.unicri.it>

work on the preparation of the Report as well as for its efforts in trying to put the proposed Recommendations into practice the practice.

The most important recognition for UNICRI's work has certainly been the invitation by the United Nations Commission on Crime Prevention and Criminal Justice (CCPCJ Decision 19/1 of 2010 entitled "Strengthening crime prevention and criminal justice responses to counterfeiting and piracy")³ to present the 2007 Report with its updates to the 2011 session of its works. The consideration by the CCPCJ of the links between counterfeiting and organized crime is an important sign that the situation is changing and that counterfeiting today is regarded as a serious threat by an increasing number of governments and International Organizations.

Responding to the CCPCJ invitation, the purpose of this Report is to build upon what was previously done, presenting those elements that characterize counterfeiting as a serious emerging threat managed by criminal organizations. This update will present how the situation has evolved in the last four years and whether the risk factors highlighted in 2007 have increased or decreased. To this end, the Report refers to statistical trends but also to case studies, which can concretely testify how serious and widespread the problem is. The presentation of general information on the phenomenon together with the most important definitions allows this Study to be used also as a standalone research tool. In this view, the general analysis on the trends of the phenomenon is subsequently completed by specific considerations regarding the consequences created by counterfeiting and its links with organized crime.

The methodology used for the update of the Report was based on the comparative analysis and direct retrieval of data and information from a variety of sources. Statistics and cases presented in already published Reports have been compared and enriched with information, data and case studies obtained directly from experts, Law Enforcers and National Authorities. For this purpose, interviews have been conducted with international police organizations, like Europol, and National Prosecution Offices, which provided for the possibility to also obtain confidential information, investigations and case studies. The

³ ECOSOC (2010), *United Nations Commission on Crime Prevention and Criminal Justice. Report on the nineteenth session* E/CN.15/2010/20, available online: http://www.unodc.org/documents/commissions/CCPCJ_session19/Draft_report/E2010_30eV1054137.pdf [last accessed on 22 March 2011].

cooperation established with National Authorities of different Countries made it possible to obtain updated statistics relative to IPRs infringements.

It may be anticipated that many of the problems highlighted in the 2007 Report are still present, and refer mainly to the limited amount of information available regarding both the links between counterfeiting and organized crime, and the consequences for society at large created by this crime. In 2007, these considerations were reflected in some of the Report's Recommendations. UNICRI thus started the preparation It may anticipated that many of the problems highlighted in the 2007 Report are still present, and refer mainly to the limited amount of information available regarding both the links between counterfeiting and organized crime, and the consequences for society created by this crime at large. In 2007, these considerations were reflected in some of the Recommendations. UNICRI started the preparation of specific Reports analyzing the situation of specific product categories particularly sensitive to consumers' health and safety, highlighting the impact of criminal organizations on their production and trade. The first of such Reports focusing on counterfeit medicines is currently in its final stage before publication. The information collected during its preparation allowed to present more detailed specifications on this category of products also in the present Report.

Deepening the research efforts is of utmost importance, because in four years, the situation has hardly changed. If on the one hand the general information on counterfeiting and its diffusion is more "present" in the news and in studies and reports, on the other hand it is still difficult to find qualified information regarding its real threats, both in terms of consumers' health and safety and in terms of its criminal management. Apart from a few laudable examples,⁴ it is still very difficult to identify comprehensive sources of information that analyze the complexity of counterfeiting, and the plurality of negative effects it creates on societies from the economic and social point of view.

The quest for cases and data often collides with the lack of systematically collected information, which is hardly ever sufficiently publicized. This has constituted a serious difficulty also in the preparation of this update, especially with reference to certain categories of products. As it will be more closely elaborated during this Report, many of the

⁴ An example is the Business Action to Stop Counterfeiting and Piracy (BASCAP) Database on Counterfeiting incidents, available on BASCAP website, <http://www.iccwbo.org/bascap/id1127/index.html> [last accessed on 22 March 2011].

problems that encountered in 2007 are still there and the Recommendations proposed are still valid.

1.2 General Elements

For a better understanding of the various issues approached in this Report, some general concepts related to intellectual property rights and counterfeiting are hereinafter introduced.

Intellectual property rights include an economic element. In certain cases - such as copyright – there is an additional moral aspect which, however, does not undermine the possibility of these rights to be commercially exploited by the respective rights holders. It is this component – and the profits that may be derived from it – that constitutes the deepest root cause of the counterfeiting phenomenon. As it will be presented later on in this Report, over time and in conjunction with the evolution of the social-economic environment, other causes have been added.

A note to Article 51 of the World Trade Organization (WTO) *Agreement on the Trade Related Aspects of Intellectual Property Rights (TRIPs)*⁵ specifies and distinguishes between the concept of counterfeiting and the one of piracy by referring to counterfeit trademark goods and pirated copyright goods. The former concept includes violations related to the unauthorized affixing – on a product or on its package – of a trademark identical to one that is validly registered for the specific product or of a trademark that cannot be distinguished from the latter.⁶ The concept of pirated copyright goods, on the other hand, refers to usurping goods, i.e. products which are unauthorized copies of products protected by intellectual property rights.⁷

⁵ Refer to: World Trade Organization (WTO) (1994), *Agreement on Trade-Related Aspects of Intellectual Property Rights - TRIPs*, 15 April, available online: http://www.wto.org/english/tratop_e/trips_e/t_agm0_e.htm [last accessed on 22 March 2011].

⁶ “‘counterfeit trademark goods’ shall mean any goods, including packaging, bearing without authorization a trademark which is identical to the trademark validly registered in respect of such goods, or which cannot be distinguished in its essential aspects from such a trademark, and which thereby infringes the rights of the owner of the trademark in question under the law of the country of importation.” Refer to: World Trade Organization (WTO) (1994), *Agreement on Trade-Related Aspects*, cited, Art. 51, note 14, (a).

⁷ “‘pirated copyright goods’ shall mean any goods which are copies made without the consent of the rights holder or person duly authorized by the rights holder in the country of production and which are made directly or indirectly from an article where the making of that copy would have constituted an infringement of a

The terms counterfeiting and counterfeit goods will be used in a broader meaning throughout this Report in accordance with a trend emerging in the majority of the international reports and studies, whereby the two cases provided for by the agreement of the World Trade Organization are included within these umbrella terms.⁸ This choice will ease the analysis, and will allow a joint discussion on the counterfeiting and piracy phenomena – as they often involve common causes and effects. Specific attention will be paid to highlighting, if necessary, any specific elements of these two categories.

The term counterfeiting is hereby defined as the illegal reproduction or imitation of products. Emphasis will be placed on attempting to provide a criminological interpretation of counterfeiting, dissecting its links with organized crime and analyzing its complexities. The phenomenon is essentially a process in which an illegal product is supplied to an aware or unaware final user, whereby the production only represents the spark initiating the engines of a complex and branching chain of illegal distribution.

This Report is meant to enhance a better understanding of the phenomenon and its evolution in recent years. Even to someone tackling this problem for the first time, it is obvious that counterfeiting is in constant growth with evolving “targets”. This statement may serve as a potential starting point for our analysis, while the causes underlying this expansion, its negative effects, the involvement of organized crime as well as the risks linked to the occurrence of certain types of replicated products on the market, will be analyzed subsequently.

1.3 Counterfeiting: A growing phenomenon

copyright or a related right under the law of the country of importation.” Refer to: World Trade Organization (WTO) (1994), *Agreement on Trade-Related Aspects*, cited, Art. 51, note 14, (b).

⁸ “Technically the English term *counterfeiting* only refers to specific cases of trademark infringement. However, in practice, the term is allowed to encompass any making of a product which so closely imitates the appearance of the product of another as to mislead a consumer that it is the product of another. Hence, it may also include the unauthorized production and distribution of a product that is protected by other intellectual property rights, such as copyright and neighboring rights. This is in line with the German term *Produktpiraterie* and the French term *contrefaçon*, which both cover a broader range of intellectual property infringement”. Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact of Counterfeiting*, page 5, available online: <http://www.oecd.org/dataoecd/11/11/2090589.pdf> [last accessed on 22 March 2011].

All the studies on this phenomenon, as well as the different reports of International Organizations involved, usually contain observations on its growth. The increase in volume of “fakes” and their penetration of legal markets reflect at least two factors: 1) an increase in the types of products which are counterfeited and 2) an increase in the number of parties involved in this illegal activity. These two factors also include others: an improvement of the external quality of replicated products making it increasingly difficult to distinguish them from the originals, as well as an extremely well organized production and distribution network of such goods.

Some international studies and reports should be taken into consideration for estimates on the current size of the problem. For this purpose, we have compared data and estimates that have been made available in the last years. What is immediately evident is that recent estimates are confirming the massive growth of counterfeiting while, at the same time, the methodology used for their compilation shows that more attention is given to better specify and define the context of the analysis. Thus, recent studies are proposing a better defined picture of the problem clearly explaining how a certain result has been achieved. This unfortunately does not mean that there is a widespread availability of data or that all of the estimates accurately depict the phenomenon. Sector-specific data are still difficult to obtain, while the reliability of the estimations is hindered by the fact that the phenomenon refers to illegal thus obscure markets. For the same reasons, the exact incidences of illegal commerce with respect to the legal one is difficult to measure. The estimates reported hereunder must therefore serve as useful indices to understand trends relating to the phenomenon, bearing in mind that the nature of the latter prevents exact estimation.

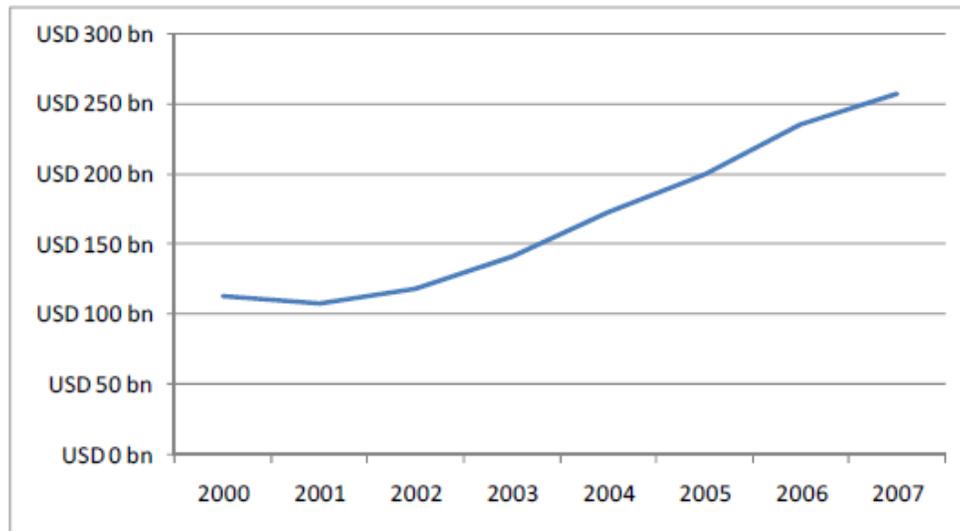
In addition, on many occasions consumers are not aware that they have bought a counterfeit product since counterfeiters are able to infiltrate the licit supply chain. From the research perspective, the conclusion is that many cases remain unreported since the victims are unaware of the illicit nature of the product they have bought. In many other cases the situation is aggravated by additional factors, since a considerable number of countries do not foresee generally available reporting mechanisms and/or do not designate competent authorities to receive such reports.

For what concerns counterfeiting as a criminal activity, the situation is even more complicated. A number of countries do not consider counterfeiting a crime, foreseeing only civil remedies against the perpetration of these acts. Furthermore, in the countries in which counterfeiting is considered a crime, the existence of different legal definitions coupled with different ways in which data collection and systematization is organized, render data comparison very difficult, hindering the possibility to propose global reliable statistics on the criminal dimension of the phenomenon. The research and comparison work here conducted has nonetheless allowed identifying the most recent estimates on the dimension of counterfeiting at the global level, to extrapolate statistical trends, and to collect and present a few significant case studies.

The following estimates represent the global growth of the problem. According to the Commission of the European Communities counterfeiting accounts for between 5 to 7 per cent of the total legal market,⁹ while the *Organization for Economic Cooperation and Development* (OECD), in its 2009 Report “The Economic Impact of Counterfeiting and Piracy of Tangibles Products: an Update”, affirms that, in 2007, the estimated volume of internationally traded counterfeit goods would have reached 250 billion USD.¹⁰ The OECD Report shows a noticeable increasing trend in the production and distribution of counterfeit products (see Figure 1). The estimated volume of internationally traded counterfeit products would have passed from 200 billion USD in 2005 to 250 billion USD in 2007, increasing the percentage of these products from 1.85 per cent to 1.95 per cent within the global trade. This apparently small variation in percentage is in reality extremely alarming considering that the volume of international trade has doubled during the same period of time.

⁹ Refer to: Commission of the European Communities (1998), *Green Paper – Combating Counterfeiting and Piracy in the Single Market*, COM(98)569 final, Brussels, 18 October, page 4, available online: http://europa.eu/documents/comm/green_papers/pdf/com98_569_en.pdf [last accessed on 22 March 2011]. Refer also to: OECD (1998), *The Economic Impact*, cited, page 23; and Noble R. K. (2003), *The Links between Intellectual Property Crime and Terrorist Finance*, text of public testimony before the United States House Committee on International Relations, 16 July, available online: <http://www.iccwbo.org/uploadedFiles/BASCAP/Pages/links.pdf> [last accessed on 23 March 2011].

¹⁰ In this estimation the OECD considered only internationally traded products and did not include those domestically produced, sold and consumed. Furthermore, digital piracy was not included. If nationally produced and sold as well as digitally pirated products exchanged via the Internet were considered, the estimate would increase by many hundreds of billions of USD. Refer to: Organization for Economic Cooperation and Development (OECD) (2009), *The Economic Impact of Counterfeiting and Piracy: an Update*, 18 November, page 1, available online: http://www.oecd.org/document/50/0,3746,en_2649_34173_39542514_1_1_1_1,00.html [last accessed on 22 March 2011].

Figure 1: Evolution of trade in counterfeit and pirated products (upper limit)

Source: Organization for Economic Cooperation and Development (OECD) (2009), *The Economic Impact of Counterfeiting*, p. 1.

The growth rate of counterfeiting is associated with the significant development of international commerce, the internationalization of the economy, the large-scale distribution of new technologies, the opening of new markets and the gradually increasing importance of exploiting Intellectual Property Rights (especially the marketing of ‘brands’ or ‘status’ goods) in multiple sectors. The typologies of counterfeit goods has also significantly expanded due to the rapid distribution of new technologies, which allow for relatively simple and accurate replication of most products present in current markets while not complying with the elevated qualitative standards of original goods. It is often stated that today there are no products on the market which could not be counterfeited; this statement is becoming true for almost every product.

Counterfeiters themselves are usually not simple “artisans” committed to accurately reproduce goods and re-sell them within a relatively limited market. This form of counterfeiting has progressively become less profitable and there is a current trend towards large-scale mass production of virtually all consumer products. What drives the interest of counterfeiters is: 1) the elevated market demand for certain products and 2) that such products are easily reproducible with the technology at their disposal. The widespread diffusion of technology at a low price and the significant economic power owned by criminal organizations led to the consequence that potentially every product on the market

can be replicated by counterfeiters and is actually a potential target for their business.¹¹ The phenomenon has thus developed from a small-scale activity to a highly organized industry which has an international market of reference, but also incorporates an international network of productive-distributional structures. This network is currently one of its strong points, making it comparable to a global industry.

Market strategies of current modern entrepreneurial structures – whereby the decentralization of productive activity is considered a competitive edge – are also fully applicable to the counterfeiting industry. Generally speaking and given notable exceptions, this illegal industry tends to center production in developing economies, while distributing its products in more industrialized markets.¹² The global nature of the phenomenon must therefore be analyzed from the dual perspective of the replicated goods, as well as the differentiation between the location of production and the one of distribution.

Further interesting considerations derive from the trends of the phenomenon in the recent years as extrapolated through a comparative analysis. These trends are alarming in many ways, but two elements deserve to be highlighted at this point. First of all, and even if considering that these data are only perceptions of the phenomenon and not an accurate representation of the latter, the dimension of the global trade in counterfeit goods has reached disturbing proportions. The following information and graphic elaborations have been prepared with the purpose of showing that the problem is extremely serious and that there are no signs of recession. The second element of concern refers to certain categories of counterfeit products potentially dangerous for consumers' health and safety. The conducted comparative work shows an alarming increase in seizure of these products in the recent years, even in the case in which the global number of counterfeit products seized was decreasing, as in the case of the European Union data.

¹¹ “As regards the sectors hit by the phenomenon, infringers are no longer targeting only luxury goods with a prestigious reputation (perfumes, watches, leather goods and other accessories) but also a wide range of sectors. [...] Custom operations have revealed that the phenomenon may also affect such highly diverse sectors and goods as spectacles, fountain pens, garden gnomes, garden furniture, playing cards, biscuits, circuit breakers and even saucepans.” Refer to: Commission of the European Communities (1998), *Green Paper*, cited, page 8.

¹² “The trade in counterfeit items is now organized on a global scale with known producers in countries and regions such as China, Taiwan, India, Turkey, Singapore, Iran, Latin America, Belgium, Denmark, France, Spain, Italy, Germany, the United Kingdom and Portugal. Products are distributed through extensive networks of importers-exporters in countries such as Belgium, Italy, the Netherlands, Spain, Argentina and the Czech Republic”. Refer to: Majid Y. (2005), “A Deadly Faith in Fakes: Trademark Theft and the Global Trade in Counterfeit Automotive Components”, in *Internet Journal of Criminology*, page 7, available online: <http://www.internetjournalofcriminology.com/Yar%20-%20A%20Deadly%20Faith%20in%20Fakes.pdf> [last accessed on 22 March 2011].

A recent document by the Canadian Anti-Counterfeiting Network (CACN) on this issue confirms the above, noting the explosive growth of the phenomenon in Canada over the last ten years. This explosive growth is characterized by a gradual expansion of the type of counterfeit goods and a shift towards large-scale consumer products. The document also confirms the increase of organization in managing the production and trade of these products, besides the growing difficulty in distinguishing the “fakes” from the originals. This difficulty highlights the greater emphasis counterfeiters place on production as well as the widespread use of technology, as further confirmed by seizures of counterfeit goods by competent authorities.¹³

Statistics provided by the European Commission Taxation and Customs Union (TAXUD) refer to the number of seizures at the European Union (EU) borders in relation with goods suspected of infringing an Intellectual Property Right (IPRs). According to the Commission Regulation No. 1891/2004, national customs across the EU are obliged to provide TAXUD with statistics on the number of cases involving the seizure of goods suspected of infringing IPRs that, once elaborated, are published by TAXUD in an annual report. However, it must be noted that TAXUD statistics take into account only: goods that are being imported into the EU, goods being exported out of the EU, re-exports, transshipments, and goods in transits. Consequently, all counterfeit goods produced and consumed within the same country, or within the EU market are not included. As a result, any assessment made on the extent of counterfeiting on the basis of these statistics may underestimate the real magnitude of the phenomenon. In addition, the general accuracy of statistics based on seizures needs to be properly weighed, as many factors (i.e. new legislation, customs performance, effectiveness of customs risk assessment methods) may influence the interception of counterfeit products. Thus, an increase or decrease in seizures may not exactly represent the actual trend of the trafficking of counterfeit goods.¹⁴ However, such statistics may allow assuming the general tendencies of the phenomenon.

¹³ “In February 2003, Peel Regional Police for example seized counterfeit Epson and Hewlett-Packard computer ink and Laser Jet cartridges with packaging so close to the genuine products, including security holograms and lot numbers, a police detective involved in the case could not tell the difference”, in Isaac B., Osmond C. (2006), *The Need for Legal Reform to Address Intellectual Property Crime*, Canadian Anti-Counterfeiting Network (CACN), Position Paper, January, pages 7 – 8, available online: <http://counterfeiting.unicri.it/docs/cacn,%20the%20need%20for%20legal%20reform.pdf> [last accessed on 22 March 2011].

¹⁴ It is often noticed that the analysis of seizures provides rather an indication concerning Customs’ performance.

In 2009 alone, 43,572 cases involving the seizure of goods suspected of IPR infringement were registered at the EU borders (with a decrease from the 49,381 cases registered in 2008). This phenomenon has been on the increase since 1999 when just one tenth of the total amount of seizures was registered (i.e. 4,694 cases, see Table 1). The total amount of confiscated items in 2009 reached the approximate number of 118 millions (see Table 2).¹⁵

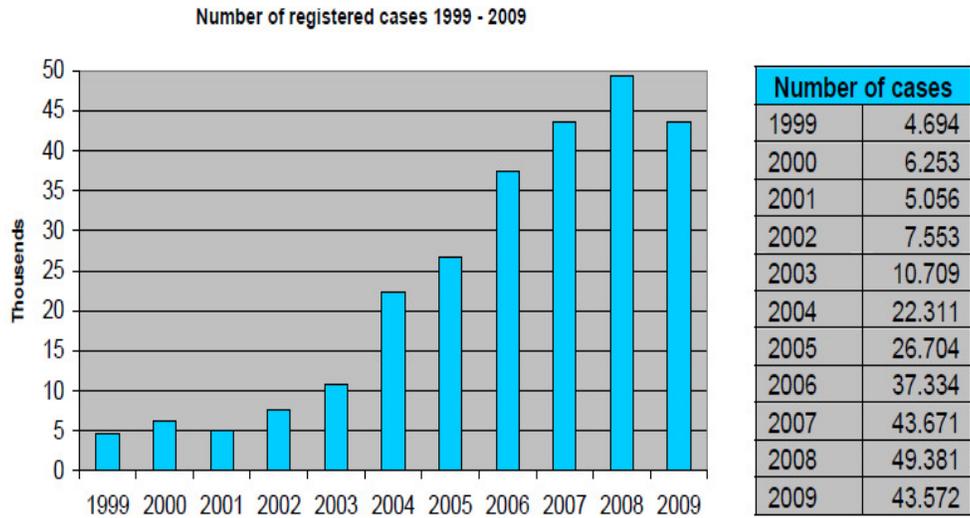
Comparing the 2009 data with situations registered during the previous years, it is possible to obtain some indications on the tendency of the phenomenon. In 1999, seizures of counterfeit goods within the EU totaled almost 25 million goods and reached more than 67 million in the year 2000. Ninety-five million items were seized in 2001, while in 2002 and 2003 respectively 85 and 92 million goods were reported. TAXUD data show a significant increase in seized goods in the years of 2004 and 2006: more than 103 million goods in 2004 and more than 128 million in 2006 following a decrease in 2005. After 2007, when the figure registered was similar to the one of 2005, in 2008 the EU customs registered the highest number of products seized, a total of 178 million goods, while in 2009 a total of approximately 118 million items seized were registered.

It has to be noted that this remarkable increase in seizures from 1999 should be interpreted not only as the result of the growth of the phenomenon, but also as the consequence of a more efficient legislation adopted within the EU regarding customs controls.¹⁶

¹⁵ Refer to: TAXUD (2010), *Report on EU Customs Enforcement of Intellectual Property Rights. Results at the EU Borders – 2009*, page 9, available online on: <http://images.12312.gov.cn/201007/20100723110450165.pdf> [last accessed on 22 March 2011].

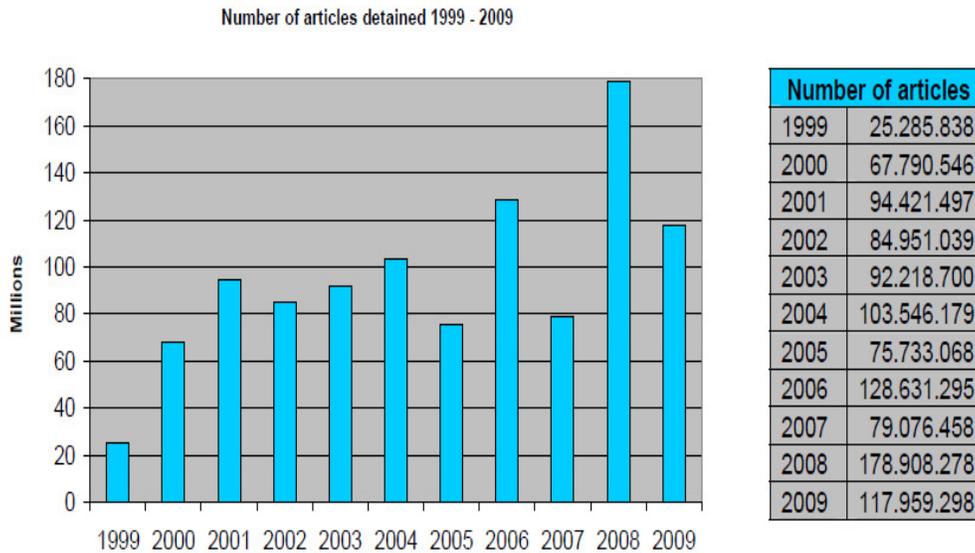
¹⁶ On this regard, mention has to be made of Regulation 1383/2003 of the Council of the European Union aimed at strengthening customs cooperation to more effectively counter the trade in counterfeit and pirated products, enhancing the efficacy of customs controls, and harmonizing the procedures for filing an application for customs action by the right holder.

Table 1



Source: TAXUD (2009), *Report on EU Customs Enforcement of Intellectual Property Rights*, p. 9

Table 2



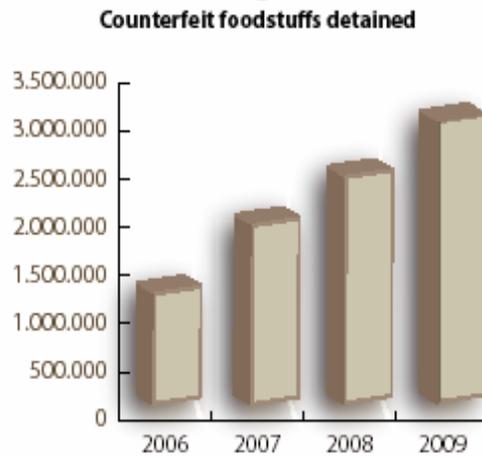
Source: TAXUD (2009), *Report on EU Customs Enforcement of Intellectual Property Rights*, p. 9

Although the 2009 statistics showed a decrease in both the total amount of cases registered and the total amount of products seized with respect to the previous year, it has to be underlined that in the same year TAXUD registered an increase in the seizure of

counterfeit products potentially dangerous for consumers' health and safety. Medicines, for instance, represented 10 per cent of the entire amount of detained goods.¹⁷ The TAXUD Report pointed out that counterfeiting is not solely affecting luxury goods and that counterfeit products for everyday use are on the increase (i.e. shampoos, toothpaste, toys and electrical appliances). Counterfeit products intended for daily use and products potentially dangerous for consumers' health and safety constituted 17 million items intercepted in 2009, accounting for 18 per cent of the total amount.¹⁸

More detailed trends for the latter products can be obtained by confronting the data of the TAXUD Reports of the last years, with reference to both the number of articles detained (see Tables 3, 4 and 5) and the number of cases registered (see Tables 6, 7 and 8). These trends are particularly alarming as they show an increase in the trade of counterfeit goods potentially dangerous for consumers' health and safety.

Table 3

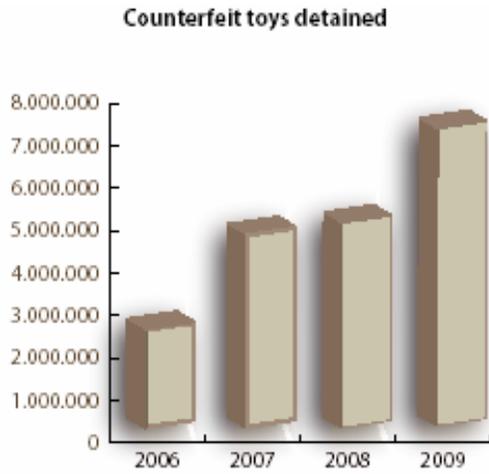


Source: UNICRI elaboration on data TAXUD Annual Reports 2006-2009

¹⁷ Refer to: TAXUD (2009), *Report on EU Customs Enforcement of Intellectual Property Rights*, cited, p. 21.

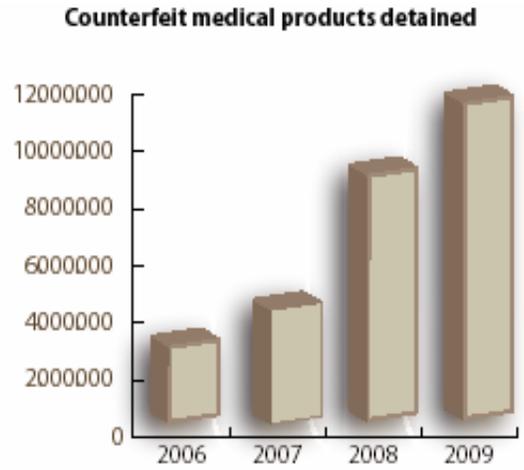
¹⁸ Refer to: TAXUD (2009), *Report on EU Customs Enforcement of Intellectual Property Rights*, cited, p. 2.

Table 4



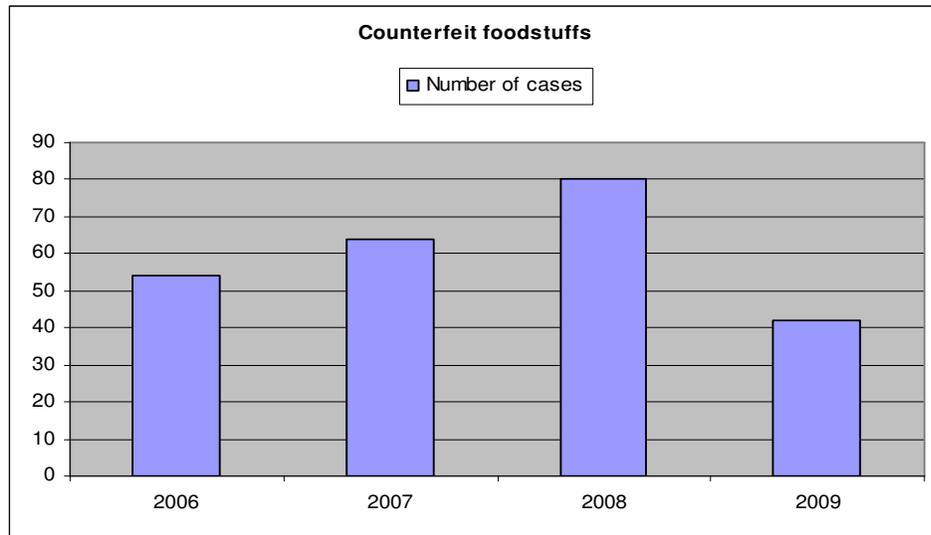
Source: UNICRI elaboration on data TAXUD 2006-2009

Table 5



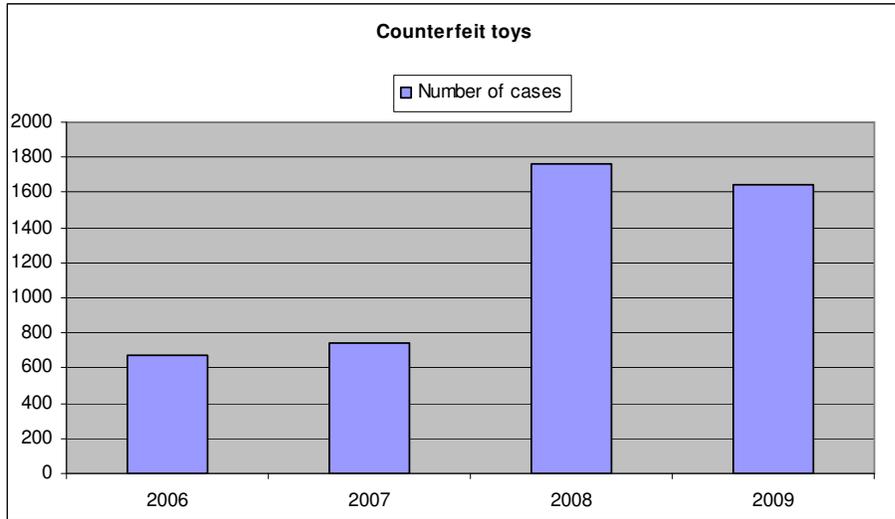
Source: UNICRI elaboration on data TAXUD 2006-2009

Table 6



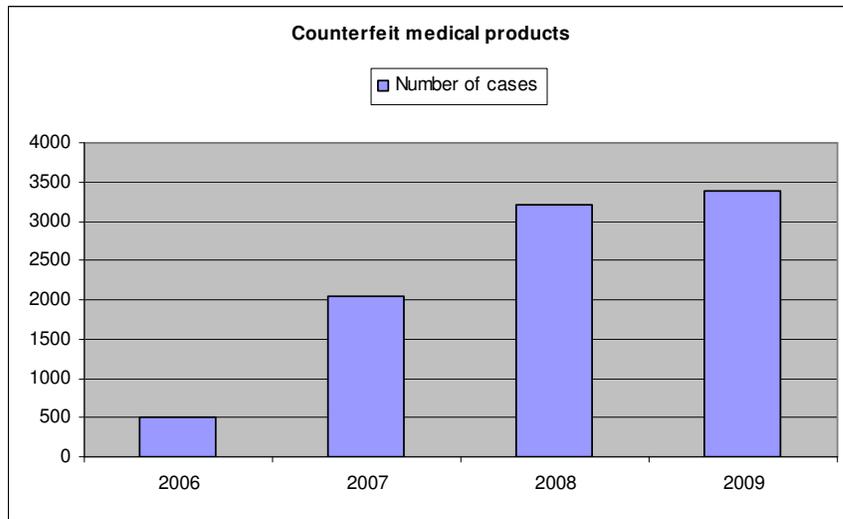
Source: UNICRI elaboration on data TAXUD Annual Reports 2006-2009

Table 7



Source: UNICRI elaboration on data TAXUD Annual Reports 2006-2009

Table 8



Source: UNICRI elaboration on data TAXUD Annual Reports 2006-2009

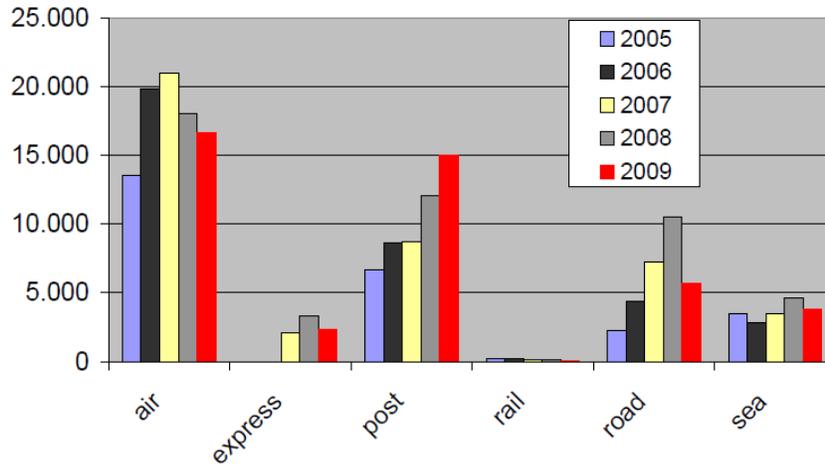
For what concerns the provenance¹⁹ of counterfeit goods seized at EU borders in 2009, the TAXUD Report proposes a breakdown taking into consideration the origin of goods per number of products detained. For the overall figure, China is still the prevalent country of provenance (more than 64 per cent of the total amount of products detained), confirming a trend that has been valid since 2003. This data should be properly weighed and linked to what was mentioned about counterfeiters' market strategies. Such strategies resemble very closely those of legitimate producers, who find it more profitable to produce in locations characterized by a lower cost of labor, while the demand is fueled by consumers from more industrialized countries.

Other countries were also identified as main countries of provenance for specific products/sectors. This is the case of Turkey for the category "foodstuffs", Egypt for "toys" and of the United Arab Emirates for what concerns "medicines". Finally, the analysis of the means of transport used in 2009 (see Table 9) confirms the trends already registered in the 2008 TAXUD Report, showing an increase in the use of shipments through the postal service.

¹⁹ Correctly the report mentions that the provenance of the goods is considered with reference to the country from where they were sent to the EU and not their real origin (i.e. where they were actually produced) as this is often difficult to ascertain due to infringers practices aimed at hiding the country of production/real origin of the goods. Refer to: TAXUD (2010), *Report on EU Customs Enforcement of Intellectual Property Rights*, cited, page 13.

Table 9

Registered cases by means of transport



Source: TAXUD (2009), *Report on EU Customs Enforcement of Intellectual Property Rights*, p. 15

Outside the EU, counterfeiting activities are mainly reported by statistics received by National Authorities and in the Reports produced by the *World Customs Organization* (WCO). For instance, statistics kindly provided for UNICRI Report by the Kingdom of Thailand show that more than 16,000 cases were initiated by the Royal Thai Police in the years 2009 and 2010, leading to the arrest of several suspects. These cases involved more than 10,000,000 goods. Statistics concerning the number of charges for Trademark infringement brought to the Thai International Property and International Trade Court for the years of 2006 to 2010, show that, each year, an average of 3,500 cases are being presented to the Court.²⁰

The WCO Report of 2009²¹ allows considerations made for the European Union to be extended to other geographical areas. The WCO provides statistics on the number of seizures made by customs authorities within member countries of the organization.

²⁰ These cases refer to: counterfeiting of trademarks, imitation of trademarks, importation, distribution, and being in possession for distribution of goods bearing counterfeit trademarks, and giving or offering services under counterfeit trademarks. Refer to: Thai National Authorities, unpublished materials.

²¹ Refer to: World Customs Organization (WCO) (2009), *Customs and IPR Report*, available online: http://www.wcoomd.org/files/1.%20Public%20files/PDFandDocuments/Reports/Extract_IPRReport2009.pdf [last accessed on 22 March 2011].

These statistics are usually collected by the WCO through the Customs Enforcement Network system (CEN).

In 2009, a total number of 13,280 cases involving the seizure of counterfeit goods were reported by the national customs administrations of the WCO Member States (Table 10), while the total number of products seized totaled 291 million (Table 11).

Table 10

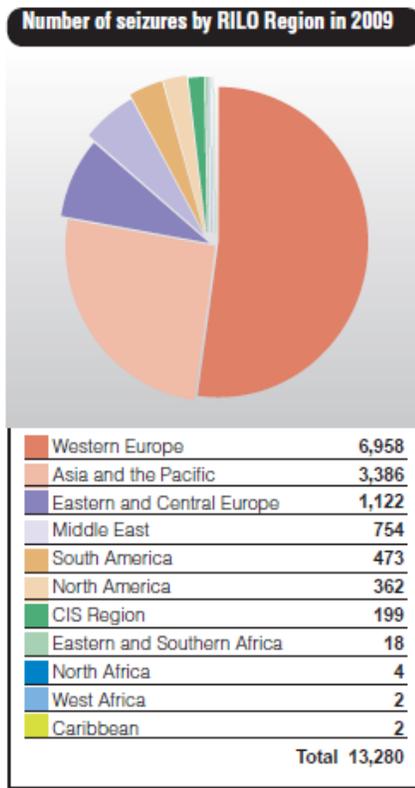
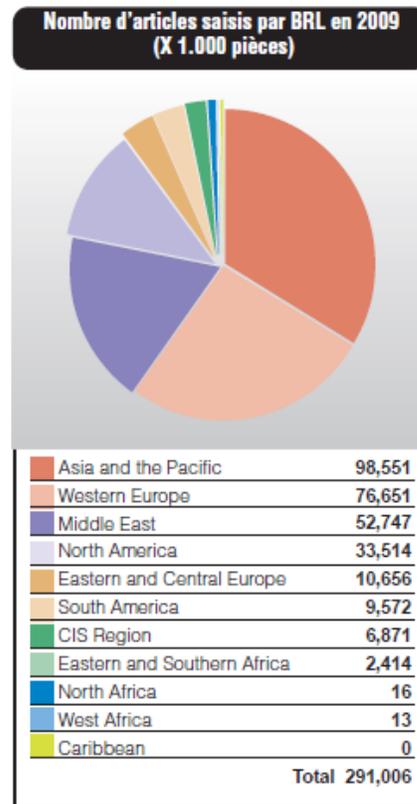


Table 11



Source: World Customs Organization (WCO) (2009), *Customs and IPR Report*, p. 7

The WCO data, similarly to the ones of TAXUD, show an alarming increase in the trade of counterfeit products potentially dangerous for consumers' health and safety. This is the case for counterfeit pharmaceutical products and counterfeit spare parts. The great majority of seizures were performed by customs administrations and only 178 cases were

the result of cooperation between customs and police forces. However, these few cases totaled almost 15 per cent of the entire amount of products seized, meaning that detection activities can greatly benefit from an improved inter-agency cooperation. As shown by Table 12 and 13, countries of all continents are affected by what concerns both the number of cases registered and the number of items seized in 2009. Even if these data constitute a sign of the presence of the problem, they have to be, in particular, positively interpreted, proving the great commitment of the respective national authorities in the fight against IPR infringements.

Table 12

Top 10 Reporting countries by number of seizures		
Country	2008	2009
China		1,752
Germany	1,473	1,429
United Kingdom	1,049	1,322
France	1,121	1,213
Japan	871	920
Italy	117	816
Spain	812	563
Saudi Arabia	5	437
Hungary	527	430
Mexico		362

Table 13

Top 10 Countries in terms of seized items (X1,000 pieces)		
Country	2008	2009
China		91,739
Qatar	360	35,282
Mexico		33,514
Italy	10,888	21,830
Spain	14,004	18,341
Saudi Arabia	2	15,670
Malta	3,023	7,936
Russian Federation	14,990	6,817
Netherlands	78,123	5,772
France	7,074	4,358

Source: World Customs Organization (WCO) (2009), *Customs and IPR Report*, p. 7

With regard to the presence of dangerous products on the market, statistics recently provided by the Kingdom of Thailand on Trademark infringements show a number of cases involving products affecting consumers' health and safety, as medicines, cosmetics and mobile phones.²²

²² Of the 126 cases registered from 2004 to the beginning of 2011, involving more than 1,640,000 units of counterfeit goods, 19 cases involved counterfeit products potentially dangerous for consumers' safety. Refer to: Kingdom of Thailand, unpublished materials.

The WCO data also register both the origin country – in the same sense used by the TAXUD data – and the actual country of departure. In both cases, the top 10 list is very similar and it is interesting to note that in the reports 99 different countries were identified as country of origin (see Table 14), and 122 as country of departure (see Table 15).

Table 14

Top 10 Origins by seizure numbers		
Country	2008	2009
China	3,938	5,544
India	600	983
Hong Kong, China	369	571
Turkey	234	188
Thailand	246	175
Seychelles	59	100
United Arab Emirates	104	86
Pakistan	59	63
Italy	63	58
United States	73	56

Table 15

Top 10 Departure countries by seizure numbers		
Country	2008	2009
China	5,119	6,983
India	547	949
Hong Kong, China	639	871
Turkey	329	247
United Arab Emirates	167	245
Thailand	368	244
Rep. of Korea	258	186
Seychelles	60	100
United States	108	84
Argentina	29	74

Source: World Customs Organization (WCO) (2009), *Customs and IPR Report*, p. 9

For what concerns the concealment methods, in the majority of the cases counterfeit items were concealed in freight, while in many other cases the items were concealed in postal or express packages. With reference to detection methods, in the majority of cases the counterfeit items were found during routine checks, while in many other cases the detection was the result of profiling exercises. Finally, Table 16 presents data on the transit countries where the highest number of cases were registered.

Table 16

1st Transit countries		
Country	2008	2009
Germany	869	662
Netherlands	443	286
Hong Kong, China	144	251
France	217	240
Chile	63	96
Belgium	83	93
Mexico		68
Finland	44	57
Spain	130	54
Greece	42	45

Source: World Customs Organization (WCO) (2009), *Customs and IPR Report*, p. 9

1.4 Causes underlying the growth of the phenomenon

The underlying causes of the “counterfeiting phenomenon” are multiple and should be considered in more detail. Modern trade allocates increase importance to the trademark as a direct expression of producer quality and reputation. These characteristics represent some of the reasons guiding the choices at the basis of the creation of a “consumer basket”. Manufacturing companies, thus, have made significant investments to ensure greater quality for their products so as to attract a greater number of buyers. Quality controls are a natural consequence of this process, given that the compliance of marketed products with pre-determined standards is an element that is directly linked to the reputation acquired by the producer and consequently to the market share attained by the latter.

The importance of the “brand” and its impact on consumers’ choice is of considerable appeal to counterfeiters, who take advantage of an entrepreneur’s reputation by replicating the relevant trademark or products, and by marketing them under her/his brand without having to sustain the costs of the legal company. Costs are generated from compliance with elevated qualitative standards, product advertising and payment of taxes and authorizations.

The opportunity to exploit the reputation of an entrepreneur in a given market is, however, not sufficient to explain such a widespread distribution of the phenomenon, particularly its significant growth and evolution. There are additional elements that have served as catalysts for a process which has currently reached such an enormous scale. As previously noted, the globalization of markets and trade has to be taken into account, as the trading of replicated products has greatly benefited from it. In addition, significant profit opportunities have emerged in new markets following the collapse of highly regulated economic regimes or the partial introduction of market economies in countries such as China.

The broad range of counterfeit products on the market is determined by a number of causes which essentially make counterfeiting a highly profitable business. The concept of profitability should be further analyzed, particularly with reference to the meaning ascribed to this term by parties involved in illegal operations. The concept is, in this case, composed of two primary elements: 1) the high profit attainable from the sale of one single counterfeit good compared to that attainable from the sale of a different type of illegal product; and 2) the low risk deriving from this activity in comparison to other illegal activities. As described more fully later on in this Report, the high level of profitability inherent in counterfeiting has attracted the interest of organized crime.

The first element to be considered is the cost of production of a replicated good. Counterfeiters make use of the cheapest materials available, without concern for the level of toxicity of such materials or their possible inconsistency with respect to the function of the good. The goods produced in this manner are then marketed at prices that are

significantly higher than their actual production costs. The margin between the sales price and the production costs depends on the type of replicated product, the type of consumer targeted, and the method chosen by counterfeiters to penetrate the market. If the targeted consumers are “aware” buyers, then the sales price – despite being still significantly higher than the production cost – will typically be lower than the price of the original one. If, on the other hand, there is an attempt to deceive potential buyers by penetrating the legal market and re-selling the products to “unaware” consumers by means of the same sale channels, prices may be equal to those of the originals. This technique is especially used in the sale of certain types of counterfeit products which, due to their very nature, would rarely be knowingly acquired considering the risk associated with their utilization. This category includes, for example, spare vehicle parts, toys and medicines.

Regardless of the method applied, it is interesting to compare the profits derived from such activity to those of other crimes in order to understand profitability of counterfeiting for criminal organizations. The advantage of counterfeiting in comparison to other activities is due to both the actual economic margin attainable from each unit sold as well as the risk associated with exercising the activity. This latter component involves the probability of being caught by law enforcers as well as the severity of penalties that are applicable in the case of conviction.

A similar comparison could be made, for example, with respect to illegal drug trafficking. Experts in this sector, particularly the managers of anti-counterfeiting agencies and customs controls, estimate that the trade of replicated goods at the international level is at least as profitable as illegal drug trafficking,²³ although other authorities believe that counterfeiting is significantly more profitable,²⁴ being capable of

²³ According to the Head of the French Anti-counterfeiting Unit, the profits of counterfeiting are similar to those of drugs trafficking, about €10 per Euro invested, refer to: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon et criminalité organisée*, 3rd edition, page 9, available online: <http://counterfeiting.unicri.it/docs/Union%20des%20Fabricants.Rapport%20sur%20la%20contrefacon%20et%20la%20criminalite%20organisee.3eme%20edition2005.FRENCH.pdf> [last accessed on 22 March 2011].

²⁴ According to the Chairman of the Danish customs and excise association, counterfeiting brings in more money than drugs trafficking, refer to: Union des Fabricants (UNIFAB) (2003), *Counterfeiting & Organized Crime*, cited.

generating profits up to eight times greater than those achieved through drug trafficking. A particularly interesting economic study on this topic was published by Pierre-Jean Benghozi and Walter Santagata and is presented in Box 1.

BOX 1

The study considered the economic elements determining the propensity to produce counterfeit goods. The latter is a function of the value of the material utilized to produce the good as well as the economic value of the Intellectual Property Right incorporated in it, its market share and the number of licenses granted by the party retaining the rights. The function reads as follows:

if $0 \leq ([I_{pv} * M_s + L] / M_v) \leq \alpha$ then $p(i) = 0$
if $\alpha \leq ([I_{pv} * M_s + L] / M_v) \leq \beta$ then $p(i) = a * ([I_{pv} * M_s + L] / M_v) + b$
if $\beta \leq ([I_{pv} * M_s + L] / M_v)$ then $p(i) = 1$

while $p(i)$ refers to the probability that a certain product (i) will be counterfeited, M_v is the economic value of the material utilized to create good (i), I_{pv} refers to the economic inherent value of good (i), M_s is the market share of good (i) and of any goods that can replace the latter, L refers to the number of licenses granted by the producer, α and β represent value limits, a and b are constants, with $a = 1 / [\beta - \alpha]$ and $b = -\alpha / [\beta - \alpha]$.

According to the interpretation of Benghozi and Santagata, the variables mentioned above would quantitatively affect the propensity to counterfeit a good, increasing or decreasing the probability as a result of changes in its performance. In particular, costly production materials would decrease the profitability of reproducing the good due to the lack of clear competitive advantages while the opposite would apply to an easily replicable good. The economic value of intellectual property rights inherent to the product is another element that directly affects the probability of counterfeiting, similarly to the relationship between counterfeiting propensity and the number of licenses granted by the producer.

Increasing the number of licensees enhances the probability that one of the latter may decide to abuse the license and develop an illegal activity. Finally, as the market share of a product increases, the potential demand for the replicated good also increases and controls over the more extensive market become more arduous.

Refer to: Benghozi, P., Santagata W. (2001), *Market Piracy in the Design-based Industry: Economics and Policy Regulation*, in "Economie Appliquée", no.3.

Since it is an illegal activity, the second element highlighted above – the risk linked to the activity itself – becomes critical. It is potentially one of the elements having the most appeal for criminal organizations given the lack of adequate deterrents within the applicable legislations of various countries. The lack of deterrence is the result of a distorted vision of the effects of this phenomenon on the part of legislators and competent authorities. Despite an increasing awareness on the scale of the problem, legislations in various countries have been hampered by a purely economic analysis of the phenomenon whose negative effects are believed to solely affect producers from a financial point of view. First of all, this point of view does not take into account the significant consequences caused by the involvement of organized crime in the management of such activities as well as the risks for the health and safety of citizens and public order. This perspective is also limited from another point of view: it also ignores the damage caused to government revenues related to the existence of traded goods which are not taxed.

The result of an incorrect perspective on the phenomenon has led to the adoption of inadequate standards or to the lack of rigorous law application. Despite the progressive change in a number of countries, there is still a widespread failure in terms of legal prevention and deterrence, thereby creating the strong profitability – defined in both of its meanings – which characterizes counterfeiting and increases the interest that organized crime shows in it. Given this situation, counterfeiting has also become one of the preferred channels to launder money at a low risk.²⁵

- The demand for counterfeit goods: the role of consumers

An additional element characterizing the existence of this illicit trade must be mentioned: the role of consumers and their attitude towards buying counterfeit products. This element does obviously not include the unaware buyer who has no intention of buying a non-original product and is a victim of deceit from the counterfeiters.

²⁵ Refer to: Union des Fabricants (UNIFAB) (2003), *Counterfeiting & Organized Crime*, cited, page 10.

At first glance, the demand for illicit goods is in general linked to the price and availability of the goods under consideration. The existence of easily accessible sales points for such products has a beneficial effect on the market of replicated goods. With regards to counterfeit products, the emergence of the Internet has also contributed to the possibility of easily acquiring different types of products anonymously, regardless of the location of the buyer – thereby allowing counterfeiters to exploit or create actual online “bazaars” that are specialized in the sale of replicated goods.

More elements should be considered when analyzing the dimension the demand for counterfeit goods has reached. As noted in a recent Research Report published by UNICRI,²⁶ the extensive business of counterfeiting relies on one postulate: consumers must be convinced of the benefits they are obtaining by purchasing counterfeit products.

Counterfeiters have to be persuasive in showing that this is a winning game for consumers and that the possibility of buying a low quality product is simply part of the game plan. Consumers must be convinced that this is a good bargain, fooling producers who market their products at such high prices. Aware buyers may at most perceive themselves as “accomplices” of the counterfeiter, but never as victims. They may think that they are accomplices to an activity that, in their opinion, does not produce any consequences for them, their beloved ones or their society. This attitude prevents citizens from considering counterfeiting as a socially unacceptable behavior, while in some cases it may even be considered a way to react to the power of rich multinational corporations. One of the many elements missing in this perception is that criminal organizations are taking advantage of this attitude to gain enormous profits thanks to the general belief that this phenomenon creates neither consequences nor victims. As we will see throughout this Report, however, the reality tells a completely different story, revealing the dark side of counterfeiting.

²⁶ Refer to: UNICRI (2010), *Strategies for Technical-Juridical Training and Awareness Raising on Counterfeiting*, Turin.

The lack of information and awareness on the phenomenon and its consequences is an aspect that consumers sometimes have in common with law enforcers. If we consider luxury goods, CDs or DVDs, and to a certain extent, electronic devices, consumers are often attracted by the lower prices of non-original goods, by their vast diffusion and availability and by a high degree of certainty that they will not be punished for purchasing counterfeit goods. Consumers seldom realize that this behavior may cause serious consequences for them and for society at large. Consumers do not acknowledge that they have been cheated by purchasing a low quality product. On the contrary, aware buyers of counterfeit products often consider themselves smarter than those paying more to purchase the original product.

So far, few surveys have been conducted with the attempt to improve the understanding of what motivates consumers to purchase counterfeit goods. Some recent studies, however, have tried to summarize and collate the information gathered, often through interviews, to gain a less fragmented view of the results obtained. Consumer profiling at the global level is quite rare. It is difficult to find comprehensive studies analyzing cross-cultural consumer behavior in different markets, comparing results and highlighting some relevant common points between individuals from very different market realities. Two main exceptions are the studies conducted by the Gallup Organization²⁷ and the *Business Action to Stop Counterfeiting and Piracy* (BASCAP)²⁸ in 2006 and 2009. The former research concerns a survey which involved 64,579 interviews in 51 countries,²⁹ while the latter covers only five countries³⁰ but is very extensive and comprehensive in terms of content and elements analyzed. Analyzing these studies is

²⁷ Refer to: The Gallup Organization (2006), *Global Consumer Awareness, Attitudes and Opinions on Counterfeiting and Piracy*.

²⁸ Refer to: BASCAP (2009), *Research Report on Consumer Attitudes and Perceptions on Counterfeiting and Piracy*, November, available online: http://www.iccwbo.org/uploadedFiles/BASCAP/Pages/BASCAP-Consumer%20Research%20Report_Final.pdf [last accessed on 22 March 2011].

²⁹ Argentina, Armenia, Austria, Belarus, Bolivia, Belgium, Chile, Colombia, Costa Rica, Cuba, Denmark, Dominican Republic, Ecuador, El Salvador, Estonia, Finland, France, Georgia, Germany, Greece, Guatemala, Haiti, Ireland, Italy, Jamaica, Kyrgyzstan, Latvia, Lithuania, Luxembourg, Malaysia, Moldova, Nepal, Netherlands, Panama, Paraguay, Peru, Philippines, Portugal, Puerto Rico, Republic of Korea, Russian Federation, Spain, Sri Lanka, Sweden, Thailand, Trinidad and Tobago, Ukraine, United Kingdom, United States, Uruguay, Vietnam.

³⁰ India, Mexico, Republic of Korea, Russian Federation, United Kingdom.

particularly useful for identifying the reasons behind consumers' motivations to purchase counterfeit goods.³¹

An initial analysis could lead to the conclusion that the main reason influencing consumers to buy counterfeit goods is predominantly their lower price, leading to assume that counterfeit goods would be particularly attractive only for consumers with lower incomes. In reality, empirical studies³² have shown that a significant number of high-income consumers (both in industrialized countries and in emerging economies) buy non-authentic goods.

In their study, Eisend and Schuchert-Gueler³³ summarize some variables in an integrated scheme which is useful to understand consumers' choices. The authors identify four broad groups of variables: (a) person; (b) product; (c) social and cultural context; (d) location and mood at the time of purchase. In this model, these four variables interact and determine the consumers' attitude towards counterfeiting and influence the decision to purchase counterfeit goods. The consumers' attitude towards counterfeiting and the decision to purchase counterfeit goods are in turn reflected in the consumers' behavior.

Furthermore, the demand for counterfeit goods is often determined by the status value associated with the ownership of a certain type of product; this is particularly true in the case of luxury goods. It constitutes an added value to be considered when evaluating the difference in price between originals and replicated goods. Similarly to their analysis of the propensity towards the production of replicated products, Benghozi and Santagata implemented a study focused on the reasons for the demand for counterfeit goods by an aware consumer. Their interpretation is valid for "status" products, such as designer clothing, watches or sunglasses. In this case, the buyer sacrifices the quality of the original product and is tempted to buy the counterfeit due to: the price and the status

³¹ Refer to: UNICRI (2010), *Strategies for Technical- Juridical Training and Awareness*, cited.

³² Among others refer to: BASCAP (2009), *Research Report*, cited; Bird R. (2007), *Counterfeit Drugs: The Consumer Perspective*, University of Connecticut, 1 November; Eisend M., Schuchert-Gueler P. (2006), "Explaining Counterfeit Purchases: A review and preview", in *Academy of Market Science Review*, no. 12, available online: <http://www.amsreview.org/articles/eisend12-2006.pdf> [last accessed on 22 March 2011]; The Gallup Organization (2006), *Global Consumer Awareness*, cited.

³³ Refer to: Eisend M., Schuchert-Gueler P. (2006), *Explaining Counterfeit Purchases*, cited.

value associated with owning the good in question.³⁴ The latter conclusions of the study are further evaluated in Box 2.

³⁴ Benghozi and Santagata hypothesize that the status value of a good (i) can be distinguished from its quality by the formula $Q_i = f(S_i, Z_{ij})$, where Q_i is the quality of the product (i). The formula illustrates that the latter is a function of both the status value S as well as other qualitative characteristics (Z) which vary from 1 to j for the individual good (i). Refer to: Benghozi P., Santagata W. (2001), *Market Piracy in the Design-based Industry: Economics and Policy Regulation*, in "Economie Appliquée", no. 3, page 9.

BOX 2

Consumers' behavior and choice depend on consumers' knowledge – or lack thereof – relative to the quality of the original and replicated goods. Benghozi and Santagata formulated four different hypotheses. The first hypothesis is of greater interest and provides for an aware consumer who has knowledge of the quality level of both products. In this case, the consumer will choose the counterfeit product if the loss deriving from the different quality/price ratio is less than the advantage associated with the improved image/status created by owning the luxury good. The status value therefore plays a key role in influencing the choices of the aware buyer.

If L = the loss deriving from the purchase of a non-original good, ΔQ = the quality difference between the two products, ΔP = the price difference between the two products and $W(Sf)$ = increased gain in status from owning the good, it is possible to formulate the following hypotheses:

if $L(\Delta Q/\Delta P) < W(Sf)$ then the conscious consumer will acquire the counterfeited good

if $L(\Delta Q/\Delta P) > W(Sf)$ then the conscious consumer will not acquire the counterfeited good

if $L(\Delta Q/\Delta P) = W(Sf)$ then the conscious consumer will be indifferent with respect to buying either product.

In addition to luxury goods, this hypothesis also seems capable of explaining the purchase of replicated audio-visual materials. The second and third hypothesis provide for a consumer who is aware of either the quality of the original or the replicated product. In this case – and given the assumption of a rational consumer – the latter will want to acquire information on the quality of these products and will sustain some costs which are added to the quality loss deriving from the purchase of a non-original product – thereby decreasing the appeal of the counterfeit good. The last hypothesis provides for a consumer that is not aware of the quality of either of the products. This would therefore entail research on the quality of both goods and even higher costs than those involved in hypotheses two and three, thereby further decreasing the propensity to acquire the non-original goods.

In the second hypothesis, the consumer will acquire the counterfeited good if $L([Cfs + \Delta Q]/\Delta P) < W(Sf)$, where Cfs = costs sustained for obtaining information on the quality of the fake good.

In the third hypothesis, the conscious buyer will, on the other hand, lean towards buying the counterfeit good if

$L([Cso + \Delta Q]/\Delta P) < W(Sf)$, where Cso = costs sustained for obtaining information on the quality of the original good.

Finally, the fourth hypothesis predicts that a conscious consumer will acquire the counterfeited good if $L([Cfs + Cso + \Delta Q]/\Delta P) < W(Sf)$. As noted above, the three hypotheses assume increasing costs for the consumer and illustrate cases where the counterfeiting market has lower demand.

Refer to: Benghozi, P., Santagata W. (2001), *Market Piracy in the Design-based Industry: Economics and Policy Regulation*, in "Economie Appliquée", no.3.

2. THE DANGERS AND EFFECTS OF COUNTERFEITING

In the 2007 Report, UNICRI called the attention to the complexity of counterfeiting and on the consequences caused for society at large by this illicit activity. After several years, the situation remains quite unchanged and estimates confirm its huge spread. Some of the tables presented in the previous chapter confirm an element already mentioned in the 2007 Report: counterfeiters constantly expand the counterfeit product typologies to maximize profits. Data on seized counterfeit goods confirm that this expansion has led to the counterfeiting of products which are potentially dangerous for the health and safety of consumers. The counterfeiting of products like medicines, food and beverages, toys and spare parts for the automotive sector is, unfortunately, very widespread. Far from being a “victimless crime”, it is evident that counterfeiting involves a series of significant “costs” of a variety of kinds for the society.

Although today there is more information available on the effects of counterfeiting, it is still true that some kinds are more evident or known than others. Economic prejudices for legitimate producers, for instance, are mentioned numerously by non experts and the public during surveys. On the contrary, other consequences like job losses or prejudices to the consumers’ health and safety are not as widely established. The same can be said for organized crime involvement. The latter contributed to the diffusion of a perception of counterfeiting that underestimates the seriousness of this illicit activity and the dangers it creates. It is only by considering the global picture of the problem that the real threats to society posed by counterfeiting are revealed.

As highlighted in the 2007 Report, the *replicas* of original products and their introduction into the market entail a series of consequences, not exclusively affecting producing companies and intellectual property rights holders, but also producing

potential devastating social and economic effects. In addition, some negative effects are common to all types of counterfeiting, while others are specific to certain categories of goods and are linked to the function of these products. An analysis of the consequences of the phenomenon must therefore include those risks potentially jeopardizing the health and safety of consumers, in addition to any economic losses sustained by companies, workers and governments.

The economic element will be analyzed at first, given that it represents the minimum common denominator of the phenomenon; the dangers associated with counterfeiting, as well as some of its characteristics, will be analyzed in relation to certain sensitive products, in particular: toys, spare parts for automobiles and aircraft, food and beverages, and medicines.

2.1 Economic losses

- Note on the proposed estimates

As mentioned, the difficulty in obtaining data is common to all the consequences of this illicit activity. The counterfeiting trade (from the production to the distribution and selling phase) is performed through underground channels, often creating a parallel underground market whose dimension and value are difficult to assess. For this reason, in some cases the estimations presented during the 2007 Report have not been updated. Efforts have been undertaken in attempting to find more recent information on some specific production sectors. The scarcity of reliable information constitutes a noticeable barrier in this respect, and some studies conducted almost ten years ago are, in some cases, still considered the only source of reliable data. Consequently, the information presented in this part of the Report is intended to serve as a basis for discussion, since it refers to different volumes of international trade and does not always consider the noticeable increase it registered in the last years.

- Legitimate producers

The most noticeable cost created by counterfeiting involves the economic losses affecting the market and legitimate producers in general. It is important to note that the counterfeiter – for a legitimate producer – is not only a criminal stealing his/her own intellectual property. Counterfeiters introduce an element of unfair competition into the market, because of the enormous competitive advantages they can exploit. Counterfeiters are not subject to taxation; are not required to comply with any regulations on workers' compensation and safety; are not required to comply with quality control processes; take full advantage of the research implemented by the producer of the original product; do not bear research and development costs; use low quality raw materials attainable at very low cost; and realize high profits allowing for significant sums to be re-invested in other operations, both legal or illegal. For many legitimate producers, especially those operating in less developed countries, a counterfeiter is very often a competitor they cannot beat forcing them to stop their commercial or entrepreneurial activity and thereby in the long run contributing to the undermining of development possibilities in these countries.

Some further considerations can better clarify the prejudice borne by legitimate producers. The replication and marketing of any non-original product clearly results in significant damages to the producing industries. The creation of a product is preceded by multiple studies and Research and Development (R&D) investments as well as the development of market positioning strategies and promotions. In addition, there are actual production costs which are largely linked to the compliance with predetermined qualitative standards. The legal firms are forced to compete with illegal entities not respecting market rules and not complying with production standards. From a purely economic perspective, the illegal enterprise is characterized by some advantages providing an initial and immediate competitive edge over the legal producer. Aside from the practice of placing production centers in less developed countries – exploiting the lower labor and raw material costs, a practice also common to large firms marketing legal products – the illegal company also benefits from the economic advantage derived from

the use of low quality raw materials. This allows the illegal company to attain significantly lower production costs. In addition, the illegal company does not sustain promotional costs for the product, as it exploits the image of the legal good that it intends to replicate, or any administrative costs associated with financial statements and accounting.

The result of this competitive advantage is the marketing of goods that do not only imitate the original product and infringe intellectual property rights but are also offered at very low prices, effectuating a significant distortion in the market. Although it is not possible to state that all sold counterfeit goods would have resulted in an equal number of acquired original goods in the absence of counterfeiting – due to the difference in sales prices – the effect on the legal company essentially involves a shift in the demand curve relative to its products which are sold in lower amounts and at lower prices.

The existence of counterfeit products sold as originals in the legal market entails a further consequence: the possibility that the distributors of the products of legal producers may – in good or bad faith – decide to acquire supplies from insecure sources that offer the same goods at lower cost. Previous references were made to the high number of unaware consumers who acquire a replica believing it is original. This element involves significant fallout for producing companies and represents one of the “hidden” costs of counterfeiting. The unaware buyer will directly associate the low quality of the acquired good with the producer; which results in a loss of goodwill with respect to the producer and towards the efforts implemented by the company in order to guarantee product quality and gain market share.³⁵ A loss of goodwill with respect to the trademark will result in a decrease in future sales of the company and adds to the previously discussed economic damages. In addition, and in the case in which the illicit nature of the product will not be proved, the legislation of certain countries will hold a producer liable for any damages to the consumer caused by the products, since the latter has acquired the product

³⁵ “...consumers who are deceived into believing that they bought a genuine article when it was in fact a fake, blame the manufacturer of the genuine product when it fails, creating a *loss of goodwill*. Even cheaper and obvious copies that are bought in good faith represent a serious threat to the company that wants its brands associated with quality and exclusivity.” Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact*, cited, page 22.

in good faith and was unaware of the illegal origin of the product. The consumer may sue the producer for damages, with the obligation of the producer to sustain additional costs for legal defenses.³⁶

The difference between forecasted and actual revenues has the additional effect of decreasing the propensity to invest in the product. Decreased investments not only imply a lower degree of innovation but also lead to slow-downs in technological progress, within a global social/economic context where such progress is deemed essential. These will also result in negative fallout on other companies which are linked to the producer, such as suppliers and advertising agencies.³⁷ Taken to the extreme, it is possible that the income loss may compromise the actual stability of the industry and result in the loss of job positions. Thus, if an industry or entrepreneurial activity constantly hit by counterfeiters may experience an economic loss in the short term, the unfair competition created by counterfeiters may, in the long term, constitute a cause for reduced investments, innovation, and R&D, putting at risk the very existence of the legitimate enterprise.

The current scale of the phenomenon is enormous. A recent Report of the *Unions des Fabricants* presents figures of the incidence of counterfeiting in the automotive sector and related, in particular, to the two “giants” Renault and PSA (the *Peugeot-Citroen Group*). According to Renault's declarations, counterfeit automotive spare parts would represent 5 to 10 per cent of the spare parts market in the European Union, and 20 per cent of the market outside the European Union. The French *Comité National Anti-Contrefaçon* affirms that the economic prejudice for a single car manufacturer would

³⁶ Currently effective legislation in some countries may go even further: “Recent changes in the product liability laws in a number of countries include provisions for manufacturers in relation to counterfeit of their products. The manufacturer of the genuine product may now find her/himself embroiled in expensive litigation to prove that she/he has taken the necessary measures to protect her/his product from being counterfeited.” Refer to: Lowe P. (1999), “The Scope of the Counterfeiting Problem”, in *International Criminal Police Review*, page 93.

³⁷ “From the point of view of the economic and social consequences, the counterfeiting and piracy phenomenon leads in the case of firms, many of which invest considerable sums in research, marketing and advertising, to a reduction in turnover and the loss of often hard-won market share, not to mention the non material losses and moral prejudice which they suffer as a result of the damage to their reputation.” Refer to: Commission of the European Communities (1998), *Green Paper*, cited, page 10.

consist more than 130 million Euros per year.³⁸ Estimates proposed by the *Motor and Equipment Manufacturers Association* (MEMA) in this sector quantify losses derived from the marketing of counterfeited automobile spare parts to be equal to 12 billion dollars per year.³⁹

Further estimates for other sectors of production can be found in the “Sector Getaways” of BASCAP. Following these estimates, the *International Federation of Spirits Producers* affirms that counterfeit alcoholic beverages would cause a loss of approx. 1 billion USD annually to legitimate producers.⁴⁰ Regarding the clothing sector, losses would be quantifiable in 12 billion USD for the year 2008, with the shoe industry registering the same losses annually. Regarding the electronics sector, the U.S. *National Electrical Manufacturers Association* reported a loss of 23 billion USD annually caused by the market of counterfeit batteries.⁴¹

For what concerns the creative industries, a recent Report written by TERA Consultants, proposes an assessment of the losses sustained by industries in the European Union market because of copyright infringements. The Report affirms that these losses could have reached the value of 10 billion Euros in 2008 and predicts an increasing trend leading to losses in 2015 that could range between 32 to 56 billion Euros.⁴² One of the most important toy industries based in Toronto, Canada, estimated losses of 10 million dollars already in 2003 due to the presence of imitations of its products on the market.⁴³

One of the few studies that tried to assess the economic impact of counterfeiting in the European market is the one commissioned to the *Centre for Economic and Business*

³⁸ Refer to: Union des Fabricants (UNIFAB) (2010), *L'impact de la contrefaçon vu par les entreprises en France*, April, page 74, available online: <http://www.unifab.com/downloads/RAPPORTUNIFABavril2010.pdf> [last accessed on 22 March 2011].

³⁹ Refer to: MEMA Brand Protection Council (2009), *Intellectual Property: Protecting Valuable Assets in a Global Market, Special Report*, page 2.

⁴⁰ Refer to: BASCAP, *Sector Gateways*, available at <http://www.iccwbo.org/bascap/id7608/index.html>

⁴¹ Refer to: BASCAP, *Country Gateways*, cited.

⁴² Refer to: TERA Consultants (2010), *El fortalecimiento de la economía digital: la importancia de defender el empleo en las industrias creativas de la UE*, 3 March, page 9-10, available online: http://www.e-dato.com/documentos/INF_buildingadigitaleconomyfinales.pdf last accessed on 22 March 2011].

⁴³ Refer to: Isaac B., Osmond C., *The need*, cited, page 10.

Research (CEBR) by the *Global Anti Counterfeiting Group* (GACG) in 2004. It reported the purely economic losses sustained by the European market, illustrating, for instance, that the effect of counterfeiting on the pharmaceutical market were quantifiable in 1,554 million Euros in lost revenues and a consequent loss of 292 million Euros in net income.⁴⁴

- Governments

Legitimate producers are not the only ones sustaining economic losses caused by counterfeiting, even if economic damages affecting producing companies and Intellectual Property Rights holders is the characteristic that is at first associated with this phenomenon. This concept of economic damage, however, proves to be restrictive and must be extended so as to include various other affected parties, including national governments.

The illegal nature of these activities results in the creation of an underground economy involving production-distribution-sales which avoid the normal channels of legal regulation or those relative to taxation. This element is common to countries which produce fakes as well as the destination countries.

A recent Report commissioned by BASCAP to *Frontier Economics* contains indications on the economic damage suffered by governments. This Report proposes estimates for the G20 countries and specific information for two countries examined as “case studies”: Mexico and the United Kingdom.⁴⁵ The analysis considered the effects

⁴⁴ Refer to: Center for Economic and Business Research (CEBR) (2000), *Economic Impact of Counterfeiting in Europe*, Global Anti-Counterfeiting Group, June, pages 2-3.

⁴⁵ The choice of the sectors of production and of the countries for the case studies is justified by the researchers as follows “The sectors were chosen on the grounds that they are representative of the type of sectors in which counterfeiting is likely to occur, and because these sectors make up a substantial element of economic activity in both the UK and Mexico. The UK and Mexico were chosen as they represent two large G20 countries, but two that differ enormously. The UK as a more developed economy is primarily a recipient of counterfeit products. Mexico, as a less developed economy, is also a recipient of counterfeit products, but also may be exposed to other costs as a source of counterfeit products.” in *Frontier Economics* (2009), *The Impact of Counterfeiting on Governments and Consumers*, page 5, available online:

of counterfeiting in four main production sectors, namely: pharmaceuticals, luxury goods, software, and food and beverages. The results are then extended to consider the effects on the whole economy of the country and not solely in the considered sectors. These two case studies allowed the researchers to show the potential costs of counterfeiting for governments in the G20 area.⁴⁶ The proposed estimates at the country level for the two “case studies” quantify the losses sustained by the Mexican Government in 1,4 billion Euros per year due to lost taxes and increased welfare spending,⁴⁷ a result of the negative effects counterfeit products may have on the health and safety of consumers and the need for the government to provide healthcare assistance. In the case of the United Kingdom, the losses would account for 4,1 billion Euros annually in taxes and increased welfare spending. At the G20 level, the proposed estimates are alarming. Tax losses and increased welfare spending would amount to 62 billion Euros annually, while 14,2 billion Euros would incorporate the cost of deaths caused by counterfeiting and 100 million Euros the cost of increased health services. Considering that counterfeiting fuels organized crime activities, another 20 billion Euros could be added at the G20 level as increased costs of crime.⁴⁸

Older estimates were presented in the CEBR Report that presented estimates on the tax losses sustained by Member States of the European Union. These losses were projected at 3,731 million Euros in the toy and sports clothing sector. Losses relative to other sectors were similarly high, totaling 7,581 million Euros in the clothing and footwear sector and 3,017 million Euros in the perfume and cosmetics sector.⁴⁹ As previously noted, significant economic damages are also recorded in countries where

<http://www.iccwbo.org/uploadedFiles/BASCAP/Pages/Impact%20of%20Counterfeiting%20on%20Governments%20and%20Consumers%20-%20Final%20doc.pdf> [last accessed on 22 March 2011].

⁴⁶ Refer to: Frontier Economics (2009), *The Impact of Counterfeiting*, cited, page 5.

⁴⁷ The report affirms that another 520 million Euros of tax losses could be added considering the lost Foreign Direct Investments that are a consequence of the lack of trust of foreign investors concerning the protection of their IPRs in the country, leading them to avoiding investing in Mexico. Refer to: Frontier Economics (2009), *The Impact of Counterfeiting*, cited, page 7.

⁴⁸ Refer to: Frontier Economics (2009), *The Impact of Counterfeiting*, cited, page 3.

⁴⁹ Refer to: World Intellectual Property Organization (WIPO) (2004), *WIPO National Seminar on Intellectual Property for Faculty Members and Students of Ajman University*, page 4, available online: http://www.wipo.int/meetings/en/details.jsp?meeting_id=5943 [last accessed on 22 March 2011].

counterfeit goods are produced. Yearly losses affecting the Chinese Government would amount to 3 billion USD, while those relative to Russia are of one billion.⁵⁰

The negative impact of counterfeiting on revenues of legal companies indirectly affects the volume of taxes collected by governments. In the long term, the lack of incentives for innovation and the decreased production will result in a decrease of the Gross National Product. This, in turn, may affect the growth rate of the country's economy. According to estimates supplied by the CEBR, by affecting the level of wealth that is created by the various "economic parties" within EU countries, counterfeiting causes a net reduction in the Gross Domestic Product of 8,042 million Euros.⁵¹ It should also be noted that additional reductions in tax revenues are caused by the illegal employment conditions of workers exploited in the production of counterfeit goods; it is, indeed unlikely that the counterfeiters comply with laws relating to worker rights and compensation.

2.2 Social consequences

Besides the economic risks, counterfeiting also involves broader negative effects on the social context of a country, considered in this report under the category of "social consequences". These are some of the less communicated negative effects of counterfeiting and certainly some of the less known and considered. This category includes the job losses together with the prejudice caused to sustainable development. Specific attention will then be given to the analysis of certain counterfeit products that constitute a real threat for consumers' health and safety, contributing to the increase of the social hazardousness of counterfeiting.

The loss of numerous job positions is a consequence of the damages sustained by companies as a result of counterfeiting. The negative effects on employment are

⁵⁰ Refer to: APCO (2003), *Global Counterfeiting*, cited, page 2.

⁵¹ Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts*, cited, page 18.

significant and represent yet another “hidden” cost of counterfeiting. Even if it is extremely difficult to assess the real impact of counterfeiting with respect to job losses, recent reports propose estimates relative to specific geographical areas. In the UK and Mexico, for instance, counterfeiting would respectively cause the loss of 380,000 and 480,000 jobs annually.⁵² In the G20 area, the losses would reach the value of 2,5 million jobs annually.⁵³

In the sector of the creative industries, copyright infringements would have caused the loss of approx. 185,000 jobs in the EU area in 2008. Predictions for 2015 assess possible job losses in this sector between approximately 611,000 and 1,216,000 jobs.⁵⁴ Estimations proposed by the *U.S. India Business Council* with reference to the situation in India – hosting the biggest cinema industry in the world – affirm that 820,000 jobs would have been lost in 2007 in this sector.⁵⁵ Further estimates for the EU market affirmed that counterfeiting was causing the loss of 100,000 job positions every year.⁵⁶

The economic problem therefore becomes a social problem. The loss of a single job position may result in a family tragedy for the employee or the worker who no longer has any income.⁵⁷ Social costs also affect workers in countries where replicated products are produced since, in most cases, they are employed under conditions of real exploitation without any form of guarantee due to the unlawful nature of their employment. Counterfeiting hampers the labor market and the dignity of workers also because of the ring of labor exploitation often created by the managers of this illicit activity. While the

⁵² Refer to: BASCAP (2009), *Research Report*, cited, page 4.

⁵³ Refer to: BASCAP (2009), *Research Report*, cited, page 8.

⁵⁴ Refer to: TERA Consultants (2010), *El fortalecimiento*, cited, page 9-10.

⁵⁵ Refer to: Union des Fabricants (UNIFAB) (2010), *L'impact*, cited, page 80.

⁵⁶ Refer to: Council of Europe (CoE) (2004), “Counterfeiting: Problems and Solutions”, in *Report of the Committee on Economic Affairs and Development*, 11 February, available online: <http://assembly.coe.int/documents/WorkingDocs/doc04/EDOC10069.htm> [last accessed on 22 March 2011].

⁵⁷ “But it wasn’t only lives that were lost or harmed by counterfeiting during the year. Livelihoods were also destroyed. Fifty employees at Danoon Ceramics lost their jobs and the factory, a major employer in a small town in Scotland, faces closure because the products they make are being counterfeited extensively in China. This is far from unusual and many firms in different parts of the world are facing similar problems.” Refer to: International Chamber of Commerce (ICC) Counterfeiting Intelligence Bureau (2006), *The International Anti-Counterfeiting Directory*, page 4, available online: <http://counterfeiting.unicri.it/docs/IACD2006.pdf> [last accessed on 22 March 2011].

links between counterfeiting, organized crime and different criminal activities managed by the same criminal organizations will be further analyzed in the next chapter of this Report, the social consequences created by the criminal management of counterfeiting are hereunder addressed.

Criminals often resort to the exploitation of illegal immigration and of victims of human trafficking to obtain their workforce. Once recruited or forced to comply with the wishes of the criminal organizations, victims are used for both the manufacturing and the selling processes. Moreover, this workforce is often composed by children, literally exploited and kept as slaves. This should be one of the issues to be reminded and underlined to those who believe that counterfeiting can generate new and fresh work opportunities in countries characterized by a lower level of industrialization. The reality is quite different, and what counterfeiting is really creating are more opportunities for exploitation and more opportunities for criminals to obtain huge profits.

- Threats to the health and safety of consumers

The product's low quality may as well result in serious consequences for consumers in terms of risks for their health and safety. Available case records are extensive. Before considering the significant risks linked to counterfeit products examined in case studies, it is useful to introduce the topic by presenting some examples that illustrate how this risk may also be found in types of replicated products apparently less dangerous for consumers. Particular attention will be given to the use of the Internet by counterfeiters as a facilitating factor in the trade of their illicit goods.

Apparently harmless components may result in significant risks for consumers' health and safety if their production does not comply with pre-determined standards. Counterfeit cell-phone batteries are a very good example. They are unfortunately currently very widespread.⁵⁸ These batteries do not contain adequate internal

⁵⁸ "Ainsi, il existe des affaires de contrefaçon de batteries des téléphones portables de mauvaise qualité vendue sous la marque Nokia dont 30 à 40 ont explosé blessant grièvement certaines personnes dont une

mechanisms that prevent overloading and may easily explode; they also tend to contain an elevated percentage of mercury, which make them potentially damaging for consumers' health (as they may cause eye, ear, kidney and immune system problems).⁵⁹

The creativity and unscrupulousness of counterfeiters seems to have no limits. Cosmetics, for example, are a sector in which criminals seem very active, and reported cases are a cause of serious concern. There are examples of the seizure of counterfeit shampoo in North America⁶⁰ as well as Zambia⁶¹ that contained bacteria or even acid. In July of 2007, numerous packages of counterfeit toothpaste were discovered on the Spanish market containing diethylene glycol, a substance which is highly toxic for the human body. Spanish authorities seized 100,000 toothpaste tubes; according to the daily newspaper *El Pais*, 10,000 packages were distributed in the hospitals of Valencia. In 2007 and 2008 the French Authorities intercepted several cosmetics, as counterfeit lipsticks and soaps that could have caused serious skin problems.⁶²

The deaths of numerous individuals, who believed to have acquired a safe product at a convenient price; who were unaware of traveling on a means of transportation utilizing counterfeit spare parts; who were confident about healing their diseases with effective and tested medicines: these cases serve as the final warning call for identifying counterfeiting as a serious crime. They also illustrate the need to adequately respond to such an unscrupulous and dangerous activity.

famme en Finlande et une en Hollande.” (“There are cases of counterfeit mobile phones batteries of bad quality sold as Nokia, 30 to 40 of which have exploded, wounding a number of people, among which one woman in Finland and one in Holland”). Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impact*, cited, page 38.

“Several shipments of counterfeit batteries from China have been seized by RCMP and Canada Border Service Agency officers (CBSA). The batteries contained mercury (despite packaging representing that they did not) raising environmental issues, and they exploded under sustained load.” Refer to: Isaac B., Osmond C. (2006), *The need for legal reform*, cited, page 14.

⁵⁹ Refer to: APCO (2003), *Global Counterfeiting*, cited, page 13.

⁶⁰ “In early 2003 U.S. Customs officials seized 17,000 bottles of counterfeit shampoo contaminated with potentially harmful bacteria that were being imported into the United States from Canada. Health Canada Product Safety officers subsequently found and removed the same counterfeit products from drug stores in British Columbia and Saskatchewan and from hair salons in the Greater Toronto Area.” Refer to: Isaac B., Osmond C., *The need for legal reform*, cited, page 15.

⁶¹ “Law enforcement in Zambia seized counterfeit shampoo containing acid.” Refer to: World Intellectual Property Organization (WIPO) (2004), *WIPO National Seminar*, cited, page 9.

⁶² Refer to: Union des Fabricants (UNIFAB) (2010), *L'impact de la contrefaçon*, cited, page 52.

It has to be noted that a detailed overview of certain productive sectors particularly susceptible of creating negative effects for the consumers' health and safety was already contained in the 2007 Report. Data concerning the extension and impact of counterfeiting in these specific sectors were not easy to find. UNICRI underlined this aspect in the Recommendations of the 2007 Report, calling for the need to conduct further research on the social consequences of counterfeiting. In an attempt to implement part of the Recommendations contained in the first Report and improve the availability of information on health and safety risks created by specific categories of counterfeit goods, UNICRI conducted further research on this topic. The publication of reports dedicated to these sectors of production has become part of the UNICRI Programme on counterfeiting. The first sector being analyzed has been the one of counterfeit medicines and its Report will be published in the next months.⁶³ However, we are able to anticipate some of its findings in this updated version of the 2007 Report. Further reports dedicated to other specific products will be produced by UNICRI in the following years.

2.2.1 Medicines

According to the WHO definition, a counterfeit drug is a pharmaceutical product whose origin and/or identity specifications have been deliberately and fraudulently modified. This commonly accepted meaning falls within the broader concept of *substandard medicines* and may also be applied – again, in accordance with the WHO guidelines – to medicines that are not protected by a patent, such as generic drugs. The meaning associated with “counterfeit medicines” incorporates various cases that are ascribable to the adulteration/replication of a product and/or tampering of the relevant packaging:⁶⁴

⁶³ The Report will analyze in particular the involvement of organized crime in the trade in counterfeit medicines as well as the peculiar situations existing in developed and less developed countries.

⁶⁴ Refer to: Harper J., Gellie B. (2006), *Counterfeit Medicines Survey Report*, Council of Europe, page 140.

- Products containing the same active ingredients and the same excipients of the original pharmaceutical agent, correctly packaged and labeled, but illegally imported into a country.
- Products containing the same ingredients of the genuine medicine, with genuine packaging, but containing incorrect amounts of ingredients.
- Products which – despite being identical from an external point of view and have genuine packaging – do not contain any active ingredients.
- Products externally similar to original products with genuine packaging, but containing harmful substances instead of the same active ingredients.
- Products with counterfeit packaging and correct amounts of active ingredients.
- Products with counterfeit packaging but with different amounts of active ingredients.
- Products with counterfeit packaging that contain a different active ingredient.
- Products with counterfeit packaging that do not contain active ingredients.

The counterfeiting of medicines may also involve products being initially genuine but whose packaging was modified declaring a higher level of active ingredients than the actual amount of the product, thereby allowing for an increase in sales price. Expired drugs may also be placed within packages that report a later expiration date.

There is, unfortunately, yet another type of trafficking in addition to counterfeit drugs which often overlaps with it. This is the commerce of false active pharmaceutical ingredients, the raw materials constituting a pharmaceutical agent. This commerce poses a very high risk for consumers' health and safety also because norms regulating the distribution of active ingredients – at least in several countries – are not characterized by the same severity as those regulating the production and distribution of finished drugs. It is possible that certain authorized producers of drugs may unknowingly market counterfeit medicines due to the utilization of fake active ingredients during

manufacturing. The possibility that the fake active ingredients may be used by legitimate manufacturers in good faith constitutes a high risks factor.⁶⁵

Counterfeit medicines are almost entirely an underground problem whose measurement is very hard, particularly when taking into consideration the difficulties that the authorities and experts often encounter in distinguishing a counterfeit medicine from an original one. Notwithstanding this difficulty, some estimates are available.

According to the WHO, counterfeit medicines would represent approximately 10 per cent of the entire amount of medicines worldwide. Countries such as the USA, Australia, Canada, Japan, New Zealand and those within the EU would have a very low proportion of counterfeit medicines of no more than 1 per cent of market value.⁶⁶ However, the considerable amount of counterfeit drugs cases declared on an annual basis by more industrialized countries prove that this problem affects, to a greater or a lesser extent, both developed and less developed countries. Mainly in Africa and partially in Asia and in Latin America, counterfeit medicines' sale would range from 10 per cent to more than 30 per cent of the national legitimate markets. In the transitional economies of

⁶⁵ A classification of criminal practices was also implemented with regards to the counterfeiting of active pharmaceutical ingredients (API). These practices are classified as follows: 1. "API procurement from uncontrolled/non Good Manufacturing Practice (GMP) origin" – done by some authorized finished medicinal product (FP) manufacturers because uncontrolled API source is cheaper. 2. "Illegal API relabeling/repackaging" – unauthorized API material may also be shipped in containers labeled with the name of a different API. 3. "Ghost API manufacturing plant" – API (possibly not produced via the registered manufacturing process) not manufactured by the 'registered producer' is sold to a FP marketing authorization holder (MAH) (who may be unaware of this fact, as API label mentions only the authorized manufacturer; a broker/trader may play a crucial role in this practice). 4. "Ghost API supplier" – MAH purchases API willingly and knowingly from a different manufacturer from that specified in the marketing authorization (in this case the manufacturing process will normally differ from that described and authorized in the marketing authorization). 5. "Paper curtain" – API manufacture performed through different process from that specified in the marketing authorization (a double documentation system may be used at the manufacturing site: one hidden set containing the true data and another set containing faked data that comply with authority requirements and regulations; such documentation system may even be in place at a site where the API is not manufactured at all). 6. "Authorized facades" – manufacturer/trader with approved certificate of suitability and drug master file supplies API material from a large number of unauthorized manufacturers (all labeling mentions only the authorized manufacturer. This set-up is believed to be widespread in terms of API material imported from China and possibly also India. In addition forged certificate of analysis and other forged documents will also be used in such situations). 7. "Illicit intermediate production" – unauthorized API materials from obscure sources are blended with the registered API material". Refer to: Harper J., Gellie B. (2006), *Counterfeit Medicines*, cited, pages 12 – 13.

⁶⁶ Refer to: IMPACT (2006), *Counterfeit Medicines: An Update on Estimates*, page 1, available online: <http://www.who.int/medicines/services/counterfeit/impact/TheNewEstimatesCounterfeit.pdf> [last accessed on 22 March 2011].

many of the former Soviet Republics there is an estimate of above 20 per cent of market value.⁶⁷

According to the *Centre for Medicine in the Public Interest*, counterfeit drug sales would generate 75 billion USD globally in 2010, an increase of 92 per cent with respect to 2005.⁶⁸ The size of the problem is also confirmed by statistics gathered and elaborated by national health and safety regulatory authorities. Just after a case of fake heparin in 2008, the *United States Food and Drugs Administration* (FDA) issued statistics reporting an 800 per cent increase in the incidence of fake drugs within the period of 2000-2006. TAXUD on 16 December 2008 announced the results of the MEDI-FAKE action, a two-month operation across the external borders of the EU implemented by the customs services of all the Member States and coordinated by TAXUD: the operation achieved tremendous results, with more than 34 million illegal pills⁶⁹ seized within these two months, ranging from antibiotics, anti-cancer, anti-malaria and anti-cholesterol medicines to painkillers, and Viagra.⁷⁰

In the Russian Federation, the *Federal Service for Health Sphere Supervision* (FSHSS) reported that in 2006, 10 per cent of all drugs on the Russian market were counterfeit. However, and according to other estimates, these rates climb up to 20 per cent as there is a growing problem of “look-a-like” drugs in the Russian market. The situation seems to be even worse in some countries of the ex-Soviet Union. In Ukraine, for instance, it is estimated that 40 per cent of the drugs circulating in the country’s market may be counterfeit.⁷¹

⁶⁷ Refer to: IMPACT (2006), *Counterfeit Medicines*, cited, Ibidem.

⁶⁸ Refer to: Center for Medicines in the Public Interest website: <http://www.cmpi.org/in-the-news/testimony/counterfeit-drugs-and-china-new/> [last accessed on 22 March 2011].

⁶⁹ Refer to: European Commission (2008), *Customs: Millions of Illegal Medicines Stopped by MEDI-FAKE Action*, Press release, ref. P/08/1980, Brussels, 16 December, available online: <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/1980&format=HTML&aged=0&language=en&guiLanguage=en> [last accessed on 22 March 2011].

⁷⁰ Refer to: TAXUD (2008), *Commission Initiatives for Fighting Counterfeit*, available online: http://ec.europa.eu/taxation_customs/customs/customs_controls/counterfeit_piracy/commission_initiatives/index_en.htm [last accessed on 22 March 2011].

⁷¹ Refer to. The News Today (2006), *Fake Medicines Are Everywhere. On a Daily Basis Many Unknowingly Risk Death*, 11 August, available online:

According to the *Peru's Association of Pharmaceutical Laboratories* (ALAFARPE), the sale of counterfeit drugs in Peru has risen from an estimated 40 million USD in 2002 to a 66 million USD in 2006. The *General Directorate of Medicines, Supplies and Drugs* (DIGEMID) of the Department of Health (MINSA) in Peru seized around 460,000 adulterated and expired medicines in 2005 alone.⁷²

In 2005, the Dominican Republic's Public Health Department reported that 50 per cent of pharmacies in the Dominican Republic operated illegally and 10 per cent of the medicines that arrived in the country were fakes. Some of the medicines found had expired over 10 years before.⁷³

In Kenya, a random survey by the *National Quality Control Laboratories* (NQCL) and the *Pharmacy and Poisons Board* found that almost 30 per cent of the drugs were counterfeit with some of them containing chalk powder and water but being marketed as original products. According to figures from the *Kenyan Association of Pharmaceutical Industry*, counterfeit pharmaceutical products would account for approximately 130 million USD annually in sales in the country.⁷⁴ In 2004, the *Ebonyi State Task Force on Counterfeit and Fake Drugs* in Nigeria reported that approximately 48 per cent of various goods and drugs imported into the country were substandard or counterfeit.⁷⁵

The phenomenon is similarly widespread with reference to the kind of drugs that can be fraudulently produced and traded. Experience on the phenomenon has shown that almost every existing medicine can be counterfeited, regardless of its kind, composition, form and purpose. What is of great concern is that counterfeiting has found its way into critical drug classes and targets specific consumers' categories by perfectly identifying each market needs and demands.

<http://www.thenewstoday.info/2006/08/11/fake.medicines.are.everywhere.html> [last accessed on 22 March 2011].

⁷² Refer to World Health Organization (WHO) (2006), *Counterfeit Medicines, Fact sheet n° 275*, available online: <http://www.who.int/mediacentre/factsheets/fs275/en/> [last accessed on 22 March 2011].

⁷³ World Health Organization (WHO) (2006), *Counterfeit Medicines*, cited.

⁷⁴ World Health Organization (WHO) (2006), *Counterfeit Medicines*, cited.

⁷⁵ World Health Organization (WHO) (2006), *Counterfeit Medicines*, cited.

It is possible to identify clear market choices operated by counterfeiters, especially with reference to distribution of different categories of medicines in developed and less developed countries. This market differentiation follows the demand for specific pharmaceutical products that exist in a given socio-economic context and shows the high level of organization and the planning capacities owned by the managers of this trade. A significant difference remains in terms of the type of counterfeit medicines which reach these two markets. In Europe, the United States and Canada, for instance, the trafficking of fake medicines primarily involves pharmaceutical products that are lifestyle-related. These so-called lifestyle drugs include pharmaceutical agents against male sexual dysfunction, substances which aid in weight loss, fake steroids, or other products which slow down the aging process.

The counterfeiting of medicines in less developed countries, on the other hand, is even worse. The replicated drugs are typically those used to treat the most serious diseases such as medicines against malaria, vaccines of all types, antibiotics and anti-retro-virals for HIV. The differences in counterfeit products between these two market “types” reflect the specific marketing strategy adopted by counterfeiters. Drugs with the highest market share and/or profitability are marketed. Furthermore, counterfeiters can count on an almost rigid demand curve in developing countries due to the need to combat epidemics or serious diseases, the elevated cost of drugs designed for these functions and the low supply of such products combined with the constant need for medical supplies and low levels of wealth. Counterfeiting activities are often facilitated by relatively ineffective legislative protection, the difficulties with which authorities are able to effectively act against organized crime, the existence of illegal parallel supply chains.⁷⁶ In addition in many less developed countries, regulatory bodies are often not present or, in cases where they do exist, they may be equipped too weakly to properly address the problem.⁷⁷

⁷⁶ Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact*, cited, page 17-18.

⁷⁷ Refer to: Bate R. (2008), *Making a Killing. The Deadly Implications of the Counterfeit Drug Trade*, page 14-24.

The trafficking routes that are used for the trade in counterfeit medicines connect the markets of less developed countries with those in Europe and North America in a variety of ways. The raw materials and counterfeit drugs often originate in Asia, America and Eastern Europe and reach the most profitable markets through various trade routes depending on the type of product. The European continent is also a site hosting production centers for counterfeit medicines. The presence of such centers in Europe, as well as the complexity of the utilized trade routes, is clearly illustrated by a case involving the marketing of counterfeit Zantac – a drug used to treat gastritis – in which the raw materials were derived from Turkey while the manufacturing process was implemented in Greece. The final product was then marketed through a Dutch importer by means of a Swiss “broker”.

It is opportune to reflect on an additional element of danger characterizing this type of illegal trafficking. The presence of lower concentrations of active ingredients compared to the amounts required by the manufacturer has a potentially even more alarming effect as this may ease the development of new strains of viruses, parasites and bacteria with a greater resistance to the specific pharmaceutical agent. The lower quantity of active ingredient may not be sufficient to completely eradicate these pathogens agents within the human body, thereby favoring the development of new and more resistant strains. This is particularly true, for example, in the case of malaria or HIV.

Counterfeit medicines may be inserted into the distribution chain in multiple ways and at almost all levels. The complexity of the distribution process, potential illegal behaviors, the scarce and rarely implemented controls in the distribution and repackaging phases, and the existence of transportation documents that can easily be modified are a few of the factors which weaken the system. The effect of parallel trade and the use of the Internet as a distribution channel also create uncertainties.

- Repackaging

Further difficulties for the identification of counterfeit drugs arise when original pharmaceutical products transit in various countries, and numerous importers, retailers and distributors are involved. The repackaging process taking place throughout the distribution and shipment procedure is a necessary step to ensure that the package and instructions relative to a drug are comprehensible to the final patients. This procedure though offers large possibilities of introducing counterfeit medicines into the legal supply channels. This continuous change-hands procedure may be followed to mask counterfeit medicines' provenance, making tracing almost impossible and leaving the question of who makes the counterfeit drugs difficult to answer. Repackaging may also create several opportunities linked to the adulteration of boxes. Two very common practices of falsification of packages have to do with: 1) the quantity of the active pharmaceutical ingredient (usually the greater the quantity of active ingredients, the higher the sale price of the drug); and 2) the change of the expiration date allowing the sale of expired products. The last two cases pose tangible risks for the distribution chain.

- Diversion

The term diversion refers to those cases in which a product designed for a specific market or function is re-marketed in violation of the producer's instruction. This phenomenon occurs in two forms: it may be limited to the national territory of a country or may become international in scope. In both cases, through diversion the products will not reach their intended destination but will be marketed at full price. The motivation underlying these operations is the difference in purchase price between a product that is marketed at full price and one that is allocated for specific purposes. This difference allows for the attainment of significant profits. With regards to international diversion, the international exchanges are implemented through multiple transfers and involve frequent repackaging of the product, thereby providing opportunities for counterfeit products to penetrate the legal distribution chain. The multiple transfers and repackaging also make the authentication phase very difficult for retailers.

- Parallel trading

Parallel trading is a legal commercial practice in the European Union; however there is an ongoing debate on its actual effect on the penetration of counterfeit goods within the market. It is necessary to consider several possible ways in which this practice may facilitate counterfeit goods entering the market. These considerations essentially relate to the number of commercial operators through which the product is distributed; the number of “transfers” within the distribution chain and; the number of repackaging opportunities. All these phases may increase and may facilitate the entry of counterfeit products within the distribution system in the absence of a specific regulatory framework.

Parallel trading involves a drug that is sold in a given country that after having already moved through the various stages of the ordinary distribution chain, is again acquired by the major distributors, and is entered into the parallel distribution chain. The product is then transferred to a new more lucrative market by means of parallel intermediaries/distributors. The times a pharmaceutical product is being transferred can be numerous. It is estimated that, on average, a drug which is entered into the parallel market may be subject to 20-30 intermediary transactions. This extension of the distribution chain creates a problem of verifiability with respect to the source from which each intermediary receives the product. There is no mechanism for verifying the licenses of parallel importers; similarly, there is no obligation for the parties involved in the parallel distribution process to record product batch identification numbers.

A change in the country of sale of the drug necessarily implies that the package and prescription instructions will be modified or replaced, a phase that, as previously seen, is not free from risks, creating possibilities through which counterfeiters may infiltrate the legitimate supply chain.

- The Internet

The Internet is exploited by criminals to conduct their illicit traffics and has become a facilitating factor for their business. A wide range of counterfeit products can be found on auction websites or are advertised and sold on the Internet, from luxury goods to medicines, from spare parts to fake batteries.

In this context, attention is to be given to online advertisement through the use of spam,⁷⁸ as this has become one of the main means used by criminals to lure their potential victims and boost their sales. A study recently conducted by UNICRI, whose results will be published in the next months, shows how spammers – usually recruited by criminal organizations to advertise their products or often members of the criminal organization themselves – are able to retrieve information on the user preferences and consequently tailor the range of products to be offered. This way they maximize the possibility of success of their action, since there is a high probability the user will be offered exactly what he or she is looking for.

People suffering from different types of illnesses, especially those perceived as taboos (for example sexual or psychological problems), may turn to the Internet for medical advice and treatments. Without any prescription requirement and review, or any origin and quality guarantee of the product purchased, patients are defenceless. A characteristic example showing how the cyber environment may contribute to the spread of counterfeit medicines is represented by an operation conducted by the FDA in which they found that 85 per cent of the drugs that buyers believed to be coming from Canadian pharmacies were actually coming from 27 other countries. In this case, original spam messages (emails sent in bulk for advertisement and promotion reasons) were sent from an address licensed to someone in the Russian Federation, the website server the counterfeiters were using was located in China, the credit card payee phone number was in the United Kingdom, the card payment was processed in Australia and the drugs were mailed from Chicago.⁷⁹

⁷⁸ Spam is unsolicited e-mail received by the owner of an e-mail account.

⁷⁹ Clark E. (2008), *Counterfeit Medicines*, cited.

It must be noted that there are by all means online pharmacies that do operate with transparency – respecting national and international rules, and terms of distribution and sale of medicines, and whose suppliers are reliable pharmaceutical companies. However, this is only one side of the coin as there are many unscrupulous online businesses run by criminals hidden behind well created websites. The WHO estimates that medicines purchased via the Internet are counterfeit in over 50 per cent of cases in which Internet sites selling the products hide their IP address.⁸⁰

Due to the impersonal nature of online commercial exchanges, the Internet guarantees anonymity. Consequently, the investigations implemented by law enforcement officials are considerably more difficult and, as a result, the risk of being subject to sanctions, seizures of goods or criminal proceedings decreases for criminals. Counterfeiters have obviously grasped this opportunity. In 2004, an investigation of various Internet sites and the pharmaceutical distribution chain was implemented by the United States Immigration and Customs Enforcement (ICE). The investigation showed that primary Internet sites could rely upon an additional 650 affiliated sites and that the total value of distributed counterfeit drugs was equal to 25 million USD. Furthermore, an unauthorized distribution network for medicines that had originated in India and extended throughout North America was uncovered.⁸¹

2.2.2 Toys

The toy industry possesses all of the appealing characteristics for counterfeiters. First of all, it is a very extensive sector with a significant economic incidence whose value in Europe was estimated by the *Centre for Economics and Business Research* to be more than 35 billion Euros in 2000. In addition to the potential revenues which may be attained, the particular market composition is quite attractive since it is dominated by a few large producing companies which also operate as distributors.

⁸⁰ IMPACT (2006), *Counterfeit Medicines*, cited.

⁸¹ The UNICRI Report on counterfeit medicines which will be published in the next months contains a detailed analysis of the use of Internet for counterfeiting of medicines.

The toy industry tends to amplify those characteristics which are described as profitability components for counterfeiting given the large scale of the market as well as regulations which, in certain cases, offer less protection compared to other sectors. The incidence of counterfeiting for this sector within the European market is of 12 per cent and – according to estimates made by *Toy Industries of Europe* – causes losses for producers totaling one and a half billion Euro per year.⁸²

The countries of origin of these products are mostly in Asia, particularly China and Thailand, but there are also numerous other products from other countries such as Poland and Turkey where it is believed that the volume of production of counterfeit toys is actually higher than that of original toys.⁸³ However, the noticeable presence of counterfeit toys in Poland and Turkey should also be linked to their role as transit countries for counterfeit products coming from Asia and intended for the European Union market.

The analysis of the number of seizures presented in the previous chapter provides an estimate relative to the number of counterfeit toys which are introduced into the EU market. These estimates are very useful in determining the economic incidence of the problem which may reach levels equal to one fourth of the production of a company. This is the case, for example, of a French toy producer. Total sales for one of its top products was close to 2.2 million pieces while 850,000 counterfeit pieces had been imported into France and Germany.⁸⁴

These data become extremely alarming if we consider that the end users are children. It is important to underline that original toys are subject to very severe regulations and quality controls as well as specific tests that precede their introduction in the market so as to ensure that their utilization does not involve any type of risk for

⁸² The organization *Toy Industries of Europe* – which represents the interests of toy producers with respect to European institutions – states that one out of every ten toys is counterfeited. Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 66.

⁸³ Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 68.

⁸⁴ Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 66.

children. An object which is placed in the hands of a child must be designed and produced considering child behavior. A toy must not have parts that are easily detachable and can be potentially swallowed. The materials themselves, as well as the colors used must not contain any toxic agent. Following controls and on the basis of the toy's composition, its size or the size of its parts and its structure, the product will be classified as suitable or not suitable for a certain age group; particular care is given to toys classified for children under the age of 36 months. These controls are obviously not implemented by counterfeiters whose only interest is to market the products at a good price and with the lowest possible cost of production. The range of replicated products for children is unfortunately very broad, and several parts of such products may be dangerous. The consequences may be very serious and the primary reason for concern is linked to the difficulty in identifying them because of their close similarity to the originals.

The collection and systematization of cases concerning this category of counterfeit products is not widespread and the few cases available that testify the seriousness of the problem mostly refer to incidents and seizures that happened in the EU or in the United States. Further studies should be conducted to assess the incidence of the problem at the global level and present how counterfeit toys are a real threat for children all around the world.

A concrete example is a case of 2009, when the Italian police seized counterfeit merchandise from China worth more than Euro 20 million during raids on 17 warehouses in Rome. Italy's financial police affirmed that 18 Chinese citizens were being investigated for allegedly importing counterfeit goods including clothes, electronics and some 150,000 children's toys. Other cases are presented in UNICRI website dedicated to counterfeiting.⁸⁵

2.2.3 Spare parts for motor vehicles and aircraft

⁸⁵ Refer to: UNICRI website on counterfeiting: <https://ctf.unicri.it>

From an economic perspective, the market for aircraft and motor vehicle spare parts is a thriving sector for counterfeiters. In the case of aircrafts, this is essentially assured by the elevated market price of these products while, in the case of motor vehicles, profitability is guaranteed by the massive distribution of vehicles and therefore the widespread commerce of spare parts. In both cases, replicated goods are introduced within a legal market with relative ease by means of black or parallel markets. In essence, however, the two product sectors (aircraft and motor vehicle) present different characteristics and sizes and should be analyzed separately.

A) Aircraft

Spare parts for aircraft are generally produced by a variety of small firms and are subject to severe regulations in order to guarantee compliance with strict safety standards. This is due to the specific characteristics which these products must have in order to fulfill their specific functions. Any form of structural failure or malfunctioning of the motor can result in catastrophic consequences. Even the production of screws, bolts and supporting components – in addition to more sophisticated spare parts – must comply with specific requirements and produce products of elevated resistance and durability.

In recent years and following the detection of counterfeit spare parts, controls on the supply of these products have been reinforced; the risk of utilizing a counterfeit spare part, however, remains very high. In order to tackle the problem, the civil aviation authorities in the U.S. (Federal Aviation Authority – FAA) and Australia (*Civil Aviation Safety Authority – CASA*) have designed specific programs for the purpose of expanding monitoring activities and controls with respect to products that are suspected to be non-compliant. This category – generally referred to as SUPs (*Suspected Unapproved Parts*) – includes various types of spare parts whose common characteristic is their non-compliance with requirements needed for their approval as safe products that are

therefore authorized to be installed on an aircraft.⁸⁶ This category also includes counterfeit products.⁸⁷

The U.S. *Federal Bureau of Investigation* (FBI) has identified the four most common types of fraud affecting SUPs and their introduction within the distribution chain. The first consists in attaching a valid FAA label to a used spare part that has not been modified or changed; the label will certify the servicing of the product or the latter's refurbishing. Another method consists in manufacturing the spare parts in compliance with the producer's specifications but utilizing low-quality materials. The third method consists in buying and re-selling overproduced parts from legitimate manufacturers. Although these spare parts are not counterfeited, it is possible that these products are production rejects and therefore also potentially dangerous. Finally, another type of fraud involves the acquisition of damaged spare parts, or parts which are nearing the end of their useful residual lives, and re-selling them as renewed spare parts.⁸⁸ These types of fraud are obviously not only implemented within the U.S. but are found in all countries.

⁸⁶ "...Examples of parts that are not eligible for use...are parts rejected during the production process because of defects, parts for which required documentation has been lost, parts that have been improperly maintained, and parts from military aircraft that have not been shown to comply with FAA requirements... 'Unapproved Parts' also occur when a supplier that produces parts for an approved manufacturer directly ships to end users without the approved manufacturer's authorization or a separate, applicable Parts Manufacturer Approval (PMA). An example of this is 'production overrun' parts. Because these parts are not authorized by the Production Approval Holder, one cannot assume that they have met all the requirements of the approval holder's required quality control process." Refer to: U.S. Department of Transportation – Federal Aviation Administration (1995), *Suspected "Unapproved Parts" Program Plan*, 6 October, pages 1-4, available online: <http://www.faa.gov/aircraft/safety/programs/sups/media/supfnl11.pdf> [last accessed on 22 March 2011].

⁸⁷ "Counterfeit parts, a type of 'unapproved part', may be new parts that are deliberately misrepresented as designed and produced under an approved system or other acceptable methods even though they were not so designed and produced. Counterfeit parts may also be used parts that, even though they were produced under an approved system, have reached a design life limit or have been damaged beyond possible repair for aviation standards, but are altered and deliberately misrepresented as acceptable, with the intent to mislead or defraud." Refer to: U.S. Department of Transportation – Federal Aviation Administration (1995), *Suspected "Unapproved Parts" Program Plan*, cited, pages 1-3.

⁸⁸ Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact*, cited, page 15.

Data derived from an investigation carried out by the U.S. *Department of Transportation*⁸⁹ – although relative to the 1990s – illustrate a growing trend within the market of counterfeit spare parts for aircraft. When the investigation was launched in 1990, the problem of counterfeit spare parts was not yet a priority and only nine reports were recorded. Due to more severe controls, these reports increased to 52 in 1991, 362 in 1992 and 411 in 1994. The figures relative to 1995 and 1996 reported a slight decrease but the numbers continue to be concerning, totaling 317 and 320 reports, respectively.⁹⁰

Estimates relative to the size of this market in the United States are cause for further concern. Experts in this sector believe that the counterfeit market may be equal to 10 per cent of the legal market with all *Suspected Unapproved Parts* included within the estimate. This widespread distribution is the direct consequence of the high level of profitability of these products. A simple component such as a nut – given the requested characteristics of resistance and duration – may cost circa 400 USD.⁹¹ Counterfeiters do not comply with safety specifications for the spare part and may therefore produce the product at very low cost and re-sell it on the market at a very high price, thereby attaining significant profit margins.

Although it is difficult to unequivocally link the cause of an aircraft disaster to the utilization of a counterfeit spare part – due to the problems inherent in verifying the causes of such accidents – it is, in any case, possible to illustrate a few examples where it was suspected that the accident was caused by the installation of a non-compliant spare part. These examples also dramatically illustrate the phenomenon and highlight the number of human lives which are sacrificed for the economic interests of unscrupulous criminals. One example is the case of the Norwegian aircraft Convair 580 which crashed due to a counterfeit bolt in the tail structure of the airplane in 1989 when flying from

⁸⁹ Agents participating in the investigation were authorized to investigate airline companies, suppliers, producers, distributors and authorized repair centers. Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact*, cited, Ibidem.

⁹⁰ Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact*, cited, Ibidem.

⁹¹ Refer to: Organization for Economic Cooperation and Development (OECD), (1998), *The Economic Impact*, cited, Ibidem.

Norway to Germany, resulting in the death of 55 people.⁹² A recent Report on counterfeiting published by the Union des Fabricants affirms that a tragic incident in the year 2000 involving a Concorde whose fuel tanks exploded, would have been caused by a counterfeit spare part lost by an aircraft during the take off phase departing before the Concorde and subsequently hit by the Concorde itself.⁹³

One issue is certain: the market for non-compliant spare parts for aircraft is very large and there are many accidents which could be potentially attributed to these counterfeit parts. A confidential file of U.S. authorities published in *Business Week* estimated that – in the period between 1973 and 1993 – 166 airplane accidents in the U.S. alone were caused by the use of counterfeit spare parts.⁹⁴

The Internet has become a huge marketplace also for these products. An article printed in the weekly magazine “*L’Espresso*”⁹⁵ reported on the recent spread of Internet sites dedicated to the sale of counterfeit spare parts for aircraft whose origin is quite obscure. Acquiring these spare parts is as easy as carrying out a normal session of online shopping. There are no specific procedures designed to verify the identity of the buyer or seller and the only thing that matters is implementing the transaction. The parts on offer include components used in devices for tire pressurization, vanes for turbines, propeller brakes and entire engines – all easily acquired online. A potential buyer only needs to have sufficient liquid funds and all ordered parts, along with documentation, will be conveniently delivered to the domicile of the purchaser, thereby attaining significant savings.

B) Motor vehicles

⁹² Refer to: Lowe P. (1999), *The Scope*, cited, page 95.

⁹³ Refer to: Union des Fabricants (UNIFAB) (2010), *Counterfeiting and Organized Crime*, cited, page 44.

⁹⁴ Refer to: Di Feo G., Gatti F. (2005), “Fermate quell’aereo” (“Stop that airplane”), in *L’Espresso*, 19 December, available online: <http://www.md80.it/bbforum/viewtopic.php?f=28&t=4292&start=0&st=0&sk=t&sd=a> [last accessed on 22, March 2011].

⁹⁵ Refer to: Di Feo G., Gatti F. (2005), “Fermate quell’aereo” (“Stop that airplane”), cited, *Ibidem*.

Similarly to the case of spare parts for aircraft, the market of spare parts for motor vehicles is very appealing to counterfeiters due to its size and the relative ease with which replicated products can be marketed and sold on legal markets.

Even for this market, counterfeit products fall within a broader category of goods: unauthorized spare parts. This category includes: warehouse surpluses of authorized distributors which are sold directly at a sales point without the authorization of the manufacturer; imports from a parallel market, including original spare parts that are transferred from one market to another without the authorization of the manufacturer; and copies of spare parts produced by independent suppliers. The latter are legal if: they possess the same quality level of the original spare part; they are not labeled with counterfeit trademarks; and they are identified as non-original spare parts when sold to the final user.⁹⁶

This market – particularly in recent years – has grown significantly in conjunction with the increase in motor vehicles across the world.⁹⁷ This growth has been particularly noticeable in countries with elevated growth rates but with relatively low pro-capita income levels. China is an obvious example: the number of circulating vehicles between 1990 and 2002 has quadruplicated; a similar increase in circulating vehicles was reported in Thailand between 1987 and 1997.⁹⁸ These markets are traditionally affected by the counterfeiting phenomenon, which is stimulated, amongst other things, by the elevated price of the original product in relation to the purchasing power of the average salary. Counterfeit spare parts can be purchased at 50 per cent of the price of an original, thereby promoting the demand for such products and creating the conditions for attracting producers and distributors of counterfeit spare parts in the market.⁹⁹

⁹⁶ Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact*, cited, page 14.

⁹⁷ It is estimated that the current figure of 500 million automobiles across the globe will double by 2015. Refer to: Majid Y. (2005), “A Deadly Faith in Fakes: Trademark Theft and the Global Trade in Counterfeit Automotive Components”, in *Internet Journal of Criminology*, page 14, available online: <http://www.internetjournalofcriminology.com/Yar%20-%20A%20Deadly%20Faith%20in%20Fakes.pdf> [last accessed on 22 March 2011].

⁹⁸ Refer to: Majid Y. (2005), “A Deadly Faith in Fakes”, cited, *Ibidem*.

⁹⁹ Refer to: Majid Y. (2005), “A Deadly Faith in Fakes”, cited, *Ibidem*.

Similarly to other markets, it is again difficult to provide accurate and reliable data on the scale of the problem. However, it is possible to provide estimates which highlight an extended market that should be cause for concern. Of the 12 billion USD that are globally lost by the automotive industry as a result of sales of unauthorized spare parts, the *Motor and Equipment Manufacturers Association* (MEMA) estimates that 3 billion are to be attributed to the incidence of counterfeiting in the U.S. market only.¹⁰⁰ *General Motors* estimates that 1.2 billion dollars were lost by its company and its distributors.¹⁰¹ In the UK, the market for such spare parts is estimated to be equal to 10 per cent of the national market.¹⁰²

A greater degree of uncertainty relative to the incidence of counterfeiting within the legal market is reported in Europe: the European Commission estimates an incidence of 5-10 per cent of the European market in contrast to the estimate of the *International Federation of Automotive Aftermarket Distributors* which is less than 1 per cent.¹⁰³ Aside from this significant discrepancy of the two estimates – perhaps due to sector interests – there is no doubt that the motor vehicle spare parts sector is a thriving market for counterfeiters, as illustrated by the results of some seizures and investigations. According to these investigations, there would be 57 companies manufacturing counterfeit spare parts in France alone supported by a network of 44 distributors.

During another investigation conducted in France in the period between the fourth quarter of 2002 and the third quarter of 2003 by the *Direction Générale de la concurrence, de la consommation et de la répression des fraudes* a total of 154 French facilities were inspected (including mechanical repair centers, body shops, distributors and specialized importers) and 1,200 counterfeit spare parts were found. These spare

¹⁰⁰ Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact*, cited, page 14.

¹⁰¹ Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact*, cited, Ibidem.

¹⁰² Refer to: World Intellectual Property Organization (WIPO) (2004), *WIPO National Seminar*, cited, page 11.

¹⁰³ Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 75.

parts originated from Belgium and the Netherlands although the judges believed that these countries only served as transit points for the products,¹⁰⁴ which are generally manufactured in China, Singapore, Turkey but also Italy, Spain and Portugal.¹⁰⁵

Two recent Reports analyze the situation in the USA and India. Even if the two countries present a different socio-economic context, both have a huge market for automotive spare parts. The Report on India provides estimates on counterfeit spare parts in the national market that would reach approximately 37 per cent of the licit trade.¹⁰⁶ The same Report also confirms that counterfeiters are able to penetrate the legitimate supply chain and sell their products as originals. The price differential between a counterfeit and an original product would consequently not be an indication in the hands of the final consumers to guide their purchases, since both products would be sold at the same price. More vigilance and integrity is thus required by the various actors of the legitimate supply chain (distributors in particular) operating before the products reach the consumer. They should not be lured by underpriced products offered as originals, especially considering the high external quality of counterfeit products.¹⁰⁷

The penetration into the legitimate supply chain is also a key element of the Report on the U.S. market for auto parts. There are several possibilities through which counterfeit products may enter the supply chain, many of which have to do with unauthorized distributors and brokers that operate as entry points also for legitimate or gray market products. Furthermore, the Internet is indicated as an important source for distributors to acquire counterfeit auto parts (also in good faith).¹⁰⁸ The Report indicates that the use of Free Trade Zones has become a common practice used by counterfeiter to

¹⁰⁴ Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 75.

¹⁰⁵ Refer to: Organization for Economic Cooperation and Development (OECD) (1998), *The Economic Impact*, cited, page 14.

¹⁰⁶ Refer to: Koshy J., *Counterfeiting of Auto parts*, page 1, available online: <http://www.iccwbo.org/uploadedFiles/BASCAP/Pages/COUNTERFEITING%20OF%20AUTO%20PARTS-%20India.pdf> [last accessed on 22 March 2011].

¹⁰⁷ Refer to: Koshy J., *Counterfeiting of Auto parts*, cited, page 2.

¹⁰⁸ Refer to: MEMA Brand Protection Council (2009), *Intellectual Property: Protecting Valuable Assets in a Global Market*, Special Report, June, page 6, available online: <http://www.iccwbo.org/uploadedFiles/BASCAP/Pages/IntellectualPropertyVers3.pdf> [last accessed on 22 March 2011].

mask the real origin of the products. By passing through several countries and exploiting the lower level of controls of Free Trade Zones, counterfeiters may avoid that their products become suspicious because of their country of origin.¹⁰⁹

The spare parts which are most frequently counterfeited are those which are broadly utilized. Counterfeiters concentrate on a handful of easily replicable products with low cost and an effortless marketing.¹¹⁰ The most replicated products include, in fact, fenders and bumpers, brake pads, shock absorbers, hoods, steering wheels, oil filters, windshields, fuel pipes.¹¹¹ As noted above, counterfeiters are very attentive in giving the product an external resemblance that is as close as possible to the original one. Auto parts installers may consequently be deceived and in good faith when installing a counterfeit part because of the difficulty with which a counterfeit part can be distinguished from the original. A recent test conducted on U.S. authorized installers and repair shops confirmed this situation.¹¹²

Also with regards to counterfeit auto parts, counterfeiters benefit from certain competitive advantages allowing them to market products at extremely low prices. These advantages are essentially derived from an absence of quality controls on the final product which is, on the contrary, tested multiple times by manufacturing companies in

¹⁰⁹ Refer to: NEMA Brand Protection Council (2009), *Understanding the Flow*, cited, page 8-9.

¹¹⁰ “The two following examples taken from a sales catalog from the parallel market are a good illustration of this:

1. Only five Citroen BX parts on offer: front bumper, windscreen, windscreen seal kit, bonnet and headlights.
2. Only ten Peugeot 205 parts on offer: front wing (right and left), bonnet, headlights, indicator, windscreen, front cross-member, radiator and cooling fan.”

Refer to: Brut J.P. (1999), *Car Parts Counterfeiting*, in *International Criminal Police Review*, 1999, page 10.

¹¹¹ Refer to: World Intellectual Property Organization (WIPO) (2004), *WIPO National Seminar*, cited, page 11.

¹¹² Approximately half of the technicians asked to tell the difference between real and counterfeit oil filters were unable to do so and careful examination was needed by the ones who recognized the fake component. However, in the daily work, technicians tend to trust the product they are installing and do not conduct a careful examination of the latter before installing it. Refer to: Zipser N. (2007), *Counterfeit Auto Parts: A growing Industry Epidemic*, 4 April, page 2, available online: www.iccwbo.org/.../Counterfeit%20Auto%20Parts%20-%20A%20Growing%20Epidemic.doc [last accessed on 22 March 2011].

order to guarantee the required duration and safety levels.¹¹³ The lack of quality in spare parts may result in significant risks for users. When a counterfeit or low quality product is installed on a vehicle, the risk is that its overall functionality becomes compromised. Even spare parts that are not of fundamental importance will serve specific functions and any defects in their operation can result in very serious consequences. Consider, for example, a steering wheel or its components built from low quality materials that could easily break; an engine hood which does not crumple on impact but penetrates the vehicle; fuel pipes which break and present a fire hazard; brake pads that are ineffective due to the materials of which they are built (compressed mud or wood) and increase the pull-up distance and are set on fire during intense usage; or a windshield that is not sufficiently resistant and disintegrates.

These examples are unfortunately not hypothetical cases, but are based on documented incidents in which counterfeit spare parts caused serious accidents.

The elevated social costs caused by the trafficking of counterfeit spare parts are therefore undeniable and are even higher if we consider that there are no official statistics on accidents caused by such products. In addition – and unlike the aircraft sector – there is no legal requirement for authorities to investigate the causes of an accident unless the latter had lethal consequences. A high number of accidents which fortunately did not result in deaths could have been caused by counterfeit products given their widespread distribution; these accidents are not, however, investigated and their causes are not ascertained, thereby creating an obscure area that prevents the phenomenon from being clearly defined.

2.2.4 Food and beverages

¹¹³ “Every vehicle component is the subject of stringent specifications, drawn up of a result of long and costly research. The Peugeot-Citroen Group spends 7.5 billions francs on research, 10% of which is exclusively on safety, partly in the form of 400 crash tests in the most extreme conditions. Before they can be put on the market, all vehicles and their parts undergo component-type approval tests and, in France, these are carried out in conjunction with the technical automotive union, the UTAC.” Refer to: Brut J-P. (1999), “Car Parts Counterfeiting”, cited, page 10.

The presence of counterfeit food and beverages on the market highlights, once again, the unscrupulousness of counterfeiters. As in the sectors previously analyzed, counterfeiters' ability of exploiting loopholes in the legitimate supply chain to infiltrate their products, creating high risks for citizens, is evident. The need to strengthen the supply chain's integrity is a core element of the problem for medicines, spare parts, toys, electrical components, cosmetics and all the counterfeit products which may be potentially dangerous for consumers' health and safety. In all such cases, counterfeiters have to make consumers believe that they are buying original products and are not running any risk; otherwise their market share would be obviously more limited.

The situation of counterfeit food and beverages is similar to the one analyzed for medicines. Both products respond to human needs, being the need to heal or the need to eat and drink. Both products are directly related to the rights of people, namely the right to life and subsistence. In both cases, criminals often take advantage of the socio-economic difficulties of less developed countries to pollute their markets with dangerous and potential deadly products affecting the everyday life of people. At the same time, criminals are exploiting the increasing demand to create a global market that sets consumers' fraud as the core business.

The impact on societies is extremely serious. However, in the case of counterfeit food and beverages, the information and communication to the public is minimal and a consistent collection of cases as well as a thorough analysis of the situation have not been performed. Considering the nature of the products and of their use, this lack of information and knowledge is alarming.

- A widespread threat

The expression "counterfeit food" normally refers to the cases in which a counterfeit trademark or appellation of origin is affixed to a product without the authorization of the IPRs owner.

However, as the purpose of this Report is to discuss the real dangers that consumers run because of unscrupulous practices put in place by criminals for profit, the classification of “unauthorized food”,¹¹⁴ which considers the various categories of unauthorized food and beverages within the terms “counterfeit food” and “counterfeit beverages” will be used.

This classification shows the importance of considering adulterations in general when referring to the consequences that unauthorized food and beverages may have on consumers’ health. In particular, the Report distinguishes between:

- Counterfeiting: the unauthorized replication of a registered trademark in view of deceiving consumers regarding the origin/authenticity of the product;
- Contamination: the unintended presence of potentially harmful substances in food. It also includes pathogenic substances as salmonella and e-coli;
- Economic adulteration (also indicated as economically-motivated adulteration): the intentional fraudulent modification of a finished product or ingredient for economic gain. It includes practices aimed at substituting ingredients or introducing substances to increase the apparent value of the product or reduce its production costs;
- Food Fraud: the deliberate insertion in the market of food with the intention of deceiving consumers and obtain financial gains. Two main types of food fraud have been identified by the UK Food Standards Agency: 1) the sale of food that is unfit and potentially harmful, and 2) the deliberate mis-categorization of food that deceives consumers.

The Report further identifies six main categories of economic adulteration: 1) unapproved enhancements (increasing the apparent value, quality or strength of a product), 2) dilution (reducing the amount of a valuable component), 3) substitution

¹¹⁴ Refer to: Grocery Manufacturers Associations (GMA) and A.T. Kearney Consulting (2010), *Consumer Product Fraud: Deterrence and Detection*, available online: <http://www.gmaonline.org/downloads/research-and-reports/consumerproductfraud.pdf> [last accessed on 22 March 2011].

(replacing with a less valuable substance or ingredient), 4) mislabeling (reclassifying one product as another, including fraudulent imitations intended to be passed as genuine), 5) non-disclosure (intentional violations of the Good Manufacturing Practices), and 6) concealment (concealing a known damage or contamination).¹¹⁵

As in the case of medicines, it is undoubtedly interesting to indicate some of the reasons for the spread of counterfeit food and beverages. The most important reason could be identified in the presence of a huge market with a rigid demand curve that could provide immense profits to unscrupulous criminals. In the case of food and beverages, controls in the production and supply chain are often not as stringent as for medicines. Furthermore, the global economic crisis and the food crisis experienced by less developed countries open immense possibilities for criminals to insert low cost products into the supply chain.¹¹⁶ These possibilities rely on supply chain actors looking for increasing their profit margins by acquiring cheaper products and on the enormous number of people, especially in the African continent, in desperate need of food with limited or no resources to acquire it. The globalization has created a network of products flows where more developed countries often play the role of huge importers of food. The various steps of the supply chain and the lack of rigorous controls during the production chain, allow for the infiltration/production of food and beverages that are unfit for human consumption.¹¹⁷

An example is the case of the melamine contaminated milk that happened in China in 2008. According to the WHO, melamine is an “an organic base chemical most

¹¹⁵ The report also provides examples for the different categories of economic adulteration. An example of the first category is the case of melamine added to milk to enhance the protein value while an example of dilution is the use of water to dilute milk. Using beet sugar instead of honey is an example of substitution while sunflower oil sold as olive oil is an example of substitution. Finally, sulfites used in food to hide deterioration are an example of non-disclosure and salmonella contagion in peanuts is an example of concealment. Refer to: GMA and A.T. Kearney (2010), *Consumer Product Fraud*, cited.

¹¹⁶ An interesting explanation regarding how counterfeiters are exploiting the food crisis in less developed countries is presented by Delval in his latest book. Refer to: Delval P. (2010), *Le marché mondial du faux*, page 189-190.

¹¹⁷ For a detailed description of the Industry’s point of view in this regard, refer to: GMA and A.T. Kearney, cited, page 4 -5.

commonly found in the form of white crystals rich in nitrogen”.¹¹⁸ It is commonly found in plastics and adhesives but is also used for the production of pesticides. Melamine has a very interesting characteristic for counterfeiters, as it may allow low protein food to fool proteins quality tests. In the case of milk, these tests usually check the protein level by measuring the nitrogen content, and melamine is rich in nitrogen. Adding melamine to low protein milk will result in increased levels of nitrogen, fooling the tests measuring nitrogen levels. Adding melamine to food is forbidden by the FAO/WHO *Codex Alimentarius* or by any national authorities, as it can lead to kidney failure.¹¹⁹ As dairy companies were refusing milk without a certain amount of proteins, milk producers and suppliers started to add melamine. The result was that a huge amount of contaminated baby milk powder was put into the market, leading to almost 300,000 babies affected, almost 54,000 hospitalized and 11 deaths probably caused by its use.¹²⁰ The reaction of the Chinese authorities was extremely strong and 22 companies were put under investigation. The contaminated milk crisis also caused the bankruptcy of one of the biggest dairy suppliers in China.¹²¹ The problem of counterfeit food and beverages represents a global threat. A well organized counterfeiting ring was dismantled in 2007 by law enforcers from Togo, Benin e Senegal. Counterfeiters produced fake beverages introducing them into the market under the name of local famous brands. These organized criminals obtained fake labels and colorants from Nigeria and subsequently produced the fake beverages in unauthorized distilleries. When the National Authorities of Togo seized samples of the products on the market and tested their composition, they found an extremely dangerous pathogen agent that causes botulism.¹²²

More industrialized countries are also in the eye of the storm, as demonstrated by a series of cases. In Germany, for instance, frozen mushrooms with high radioactivity

¹¹⁸ Refer to: World Health Organization (WHO), *Questions and Answers on Melamine*, available online: <http://www.who.int/csr/media/faq/QAmelamine/en/> [last accessed on 22 March 2011].

¹¹⁹ Refer to: World Health Organization (WHO), *Questions and Answers*, cited.

¹²⁰ Refer to: Branigan T. (2008), “Chinese figures show fivefold rise in babies sick from contaminated milk”, in *The Guardian*, 2 December, available online: <http://www.guardian.co.uk/world/2008/dec/02/china> [last accessed on 22 March 2011].

¹²¹ Refer to: China View (2008), *China seizes 22 companies with contaminated milk powder*, available at http://news.xinhuanet.com/english/2008-09/17/content_10046949.htm [last accessed on 22 March 2011].

¹²² The name of the pathogen agents is clostridium and, according to Pierre Delval, its use is considered as biological weapon. Refer to: Delval P. (2010), *Le marché*, cited, page 194.

levels were seized in 2008 on their way from the Russian Federation, while in the same year Lithuanian customs seized sunflower oil coming from Ukraine and contaminated with a highly carcinogen agent.¹²³ In France, the customs seized counterfeit salad packages and counterfeit chocolate, while in Russia the WHO estimated that in 2005 40,000 people died as a result of intoxication with fake Vodka.¹²⁴ Some other significant cases are listed below.

In 2008, 14 people have been killed and over 125 people have been hospitalized in Ulan Bator, Mongolia, after a local distillery produced liquor containing methanol. The distillery was closed and the sale of all liquor throughout the capital city got banned.

In the same year, drinkers in Buckinghamshire have been told to be wary of buying cheap bottles of “Glen’s” vodka after counterfeit 70cl bottles were found on sale in Chesham, Aylesbury and Downley. Counterfeit vodka has caused blindness and even death in past instances.

In 2006, the Italian Guardia di Finanza seized 138 tons of counterfeit olive oil. The bottles and cans filled with the counterfeit oil looked practically identical to those used by famous producers.

In 2003, more than 300,000 counterfeit bottles of water were seized by the customs in the EU.

In the same year, the consumption of counterfeit wine, containing a component used to produce industrial chemicals caused the death of two people in Thailand.

In 2001, in the Chinese Guangdong Province, 308 tons of counterfeit toxic rice were discovered and seized. The counterfeit rice contained mineral oil and other substances and presented also excessive levels of carcinogen aflatoxin B1.

In the same year, several cases of counterfeit foodstuff were registered across Europe. Among these: packets of fake chewing gum (2,600,000 seized in Spain; 584,000

¹²³ Refer to: Delval P. (2010), *Le marché*, cited, page 190.

¹²⁴ Refer to: Delval P. (2010), *Le marché*, cited, page 16 and page 25.

seized in Germany; 4,400 in Denmark); hundreds of packets of counterfeit instant coffee in Germany; 7,200 packets of counterfeit cakes and 871,000 boxes of counterfeit chocolate in the Netherlands; 23,236 bottles of fake olive oil.

Unfortunately, several other cases could be added to this list.¹²⁵ The phenomenon is globally spread: a coordinated international preventive action is thus urgently needed.

¹²⁵ For further information related to counterfeiting cases, please refer to UNICRI website: <http://counterfeiting.unicri.it/>

3. COUNTERFEITING AND ORGANIZED CRIME

The 2007 UNICRI Report presented a detailed series of considerations regarding the involvement of organized crime in the management of the production and trade in counterfeit goods. A broad range of elements was covered, from the analysis of the pushing motivations for criminal organizations' involvement in counterfeiting to the presentation of concrete elements, cases and statistics that served as instruments to discuss this involvement in detail. These considerations are still entirely valid and many of the features of the criminal management of counterfeiting have not changed. The few Reports published at the international level during these years, as well as experts' presentations during conferences and events confirm what UNICRI affirmed in 2007. Consequently, this update focuses more on concrete evidence regarding the connection between organized crime and counterfeiting by discussing a series of real cases.

Before doing so and for the sake of comprehensiveness, we will introduce some of the main elements presented in the previous Report. Discussing the involvement of criminal organizations in counterfeiting without briefly explaining the evolution of organized crime in the last decades would probably lead to underestimating some important elements. If today counterfeiting is clearly one of the businesses put in place by organized crime, one of the reasons is that the opportunity to be involved in this trafficking came at a very favorable historical moment. While it is true that not all acts of counterfeiting are unequivocally ascribable to large criminal organizations, there is no doubt that a significant portion of counterfeit trafficking is managed – at a variety of levels – by organized crime.

3.1 Defining organized crime

To preliminarily define the concept of “organized crime”, we will make reference to the definition contained in the United Nations Convention against Transnational Organized Crime (UNTOC) (2000) – the most important international regulatory instrument on this subject – which identifies an organized criminal group as a “*structured group of three or more persons, existing for a period of time and acting in concert with the aim of committing one or more serious crimes or offences...in order to obtain, directly or indirectly, an economic or other material benefit*”.¹²⁶

This definition is very comprehensive as it encompasses criminal activities characterized by a certain organizational duration whereby the criminal association is implemented in order to conduct criminal acts which allow the group to generate profits. The duration of this association is not defined *a priori* and should be interpreted as any non-occasional commitment to perpetrate crimes on the part of group members. The numerical element of the definition serves the purpose of creating a distinction between the individual criminal who may be aided by an accomplice and more complex organizations which involve more people and therefore imply a greater degree of operational capacity, posing a greater threat to public order.

This definition is valid for the traditional Mafia-like organizations, which are structured in a hierarchical manner with clear division of roles, and strong connections with the territory. At the same time, this definition encompasses modern phenomena such as loose criminal networks with varying structures operating in different sectors and territories; such groups are characterized by their links with other criminal organizations, leading to the loss of rigid hierarchies and strong territorial connections. The act of committing serious crimes for economic profit is a common element to all types of criminal organizations.¹²⁷

¹²⁶ Refer to: United Nations, *United Nations Convention against Transnational Organized Crime*, Art. 2 (a), available online: <http://www.unodc.org/documents/treaties/UNTOC/Publications/TOC%20Convention/TOCebook-e.pdf> [last accessed on 22 March 2011].

¹²⁷ “The ‘transnational’ nature of a crime therefore differs from its ‘international’ nature. The latter expression refers, in fact to a criminal group that not only operates within its country of origin but also implements operations abroad (for example, it is well known that the ‘*Ndrangheta*’ families also operate in

3.1.1 The development of organized crime

The connection between organized crime and counterfeiting follows the significant expansion of the areas of interest of criminal groups. Modern criminal organizations have gradually started implementing activities often similar to what were previously labeled as “economic crimes”. This category includes the founding and management of companies operating in financial markets or regular product markets to launder proceeds deriving from other crimes committed by the same criminal group or income transferred to the group in order to implement these money laundering activities.

What is crucial in the analysis of counterfeiting is the evolution that criminal organizations underwent during the 1970s creating a network of criminal organizations operating in different countries. This network was essential for the trafficking of goods whose places of production were distant from the places of destination, as in the case of the illicit trade in narcotic substances. Narcotics, weapons and contraband products were goods characterized by elevated demand whose commerce generated significant revenues for criminal organizations. Such products required a transformation of criminal groups to adapt to new types of activity and trade.

In order to manage trafficking across different areas of the globe, criminal groups established alliances with other organizations, sharing operational tasks and creating an actual illegal production/distribution chain.¹²⁸ The new synergies not only guaranteed optimal logistics but also provided for the opportunity to market various goods by using

France, Germany, Canada, Australia, etc.). The former expression, on the other hand, refers to cooperative actions implemented by criminal groups of differing national origins in order to more effectively manage certain criminal markets”. Refer to: Zuccarelli F. (2006), *The phenomenon of trademark counterfeiting and organized crime. Domestic and international investigations for contrasting illegal replication activities*, page 2.

¹²⁸ “... in particular, narcotics and weapons but also illegal immigrants, toxic wastes pornographic material, the human slave trade, etc. These goods are normally produced in locations that differ from their areas of utilization; their transfer from one country to another is implemented by escaping controls, bribing parties entrusted with monitoring these transfers and using legal institutions such as banks and financial companies for payments. In this manner, ties between criminal organizations in different national territories are strengthened.” Refer to: Zuccarelli F. (2006), *The counterfeiting phenomenon*, cited, page 2.

the same methods and, most likely, the same trade routes. The narcotics trade is, for instance, one of the milestones in the evolution of structural relationships within the Sicilian Mafia; it initiated a series of alliances with criminal organizations from other countries to create a division of labor and to subdivide the market, thereby attaining greater operational efficiency and maximizing profits.¹²⁹ This scheme was also applied in the case of counterfeiting, by consequently exploiting a set of established practices and relationships already in place for the management of other illicit traffics.

The transformation of organized crime groups received an additional boost from the internationalization of markets and economy. Global markets for goods as well as global financial markets have resulted in a gradual weakening of national borders. Criminal organizations have managed to seize the opportunities inherent in this global transformation possibly more than national governments and their populations, and have displayed an excellent level of adaptability to the new *status quo*. This new face of organized crime became increasingly similar to a transnational commercial company combining rigid hierarchies and territorial rooting with flexible structures that are easily adaptable to changing circumstances. With links between different criminal activities in terms of both their financing and the laundering of their proceeds, commercial specialization has been repudiated in favor of the simultaneous trade and supply of different categories of illegal goods and services. Counterfeiting has become a fundamental element of this scheme.¹³⁰

¹²⁹ “In 1975, the Turkish Mafia established an alliance with the Sicilian Mafia whereby the Turks would supply basic morphine for heroine and the Sicilians would refine it. The two organizations had previously subdivided the European market, leaving the central and southern areas to the Italian Mafia and camorra and the northern areas to the Turks. A subsequent development occurred in October 1987 when the ‘Caruana’ and ‘Cuntrera’ families and the ‘Medellin’ Columbian cartel in the Caribbean island of Aruba decided to join the alliance; this new arrangement provided for an exchange of European heroine with cocaine produced in Columbia, thereby monopolizing the Atlantic narcotics market”. Refer to: Zuccarelli F. (2006), *The counterfeiting phenomenon*, cited, page 2.

¹³⁰ “The idea that each illegal trafficker specializes in a single type of good is equally obsolete... In reality, the economic and technological opportunities deriving from globalization facilitate illegal traders in switching business interests and moving from one type of good to another... Maureen Baginski, Executive Vice-director of the FBI, stated the following: ‘*The area of specialization has become the network itself and its capacity to supply, transport and deliver illegal goods in different countries. The type of good itself has acquired secondary importance*’”. Refer to: Zuccarelli F. (2006), *The counterfeiting phenomenon*, cited, page 7.

3.2 The criminal management of counterfeiting

Once recognized that counterfeiting is part of the strategies of organized crime, it is interesting to consider in more detail the specific role it plays within these strategies as well as how organized crime contributed to transform counterfeiting into a mass-production industry. These elements will be considered within the expression “criminal management of counterfeiting” and will include the motivations leading organized crime to take an active role in the production and distribution of fake products together with considerations regarding the transnationality of the crime and the various links intermingling counterfeiting with other different criminal activities.

3.2.1 Motivations and immediate consequences

While for experts and researchers on counterfeiting the organized crime’s involvement is a matter of fact, for many others – also holding important positions at the governmental, political or law enforcement level – this connection is not fully clear. One of the most common questions raised on this issue concerns the reasons at the basis of organized crime interest in counterfeiting. The reply to this question is partly included in the explanation presented in the previous chapter and is linked with the expansion of the “interests” of criminal organizations, which have become more and more prone to exploit every profit opportunity. However, an in-depth analysis of the relation between counterfeiting and organized crime allows for more interesting elements to come to the surface. The assumption that organized crime is essentially dedicated to offering illegal goods and services that are in demand within a given territory may be taken as starting point. Organized crime supplies a range of services to potential customers and, from this point of view, does not significantly differ from any legal entrepreneurial venture. The criminal activity is essentially linked to the existence of demand for illegal goods and/or services. The evolution of this demand – or rather, the changes in the object of this

demand – is among the factors that during in the ‘70s provoked a change in the criminal structures. Offering illicit goods and services often means that a production and distribution structure/network has to be put in place, with different forms and dimensions, and varying organizational levels. In some cases, the goods or services will be produced and sold within the same territory, while in others a real trading scheme will have to be created – as in the case of narcotics – leading to the establishment of alliances involving different criminal organizations. The trade in counterfeit products could follow both schemes since goods may be produced and sold within the same country, although there is a clear tendency to delocalize production to regions where labor costs are lower.

One of the motivations at the basis of the illicit trafficking in counterfeit goods is surely their high demand, but a distinction is necessary. For a wide range of replicated products we may consider valid the general assumption that wants the demand generated by the request for goods that are not available through legal distribution channels, or as a result of the price difference between a good offered by authorized retailers compared to that attainable through illegal channels. However, in the case of counterfeit goods, the demand that criminals exploit does not refer only to the illicit demand, as there is an increasing trend towards the insertion of counterfeit products within the licit supply chain. This method is usually applied to products potentially dangerous for consumers’ health and safety;¹³¹ yet it has to be noted that it is a practice quite frequently used also with reference to traditional consumer goods, as clothes or CDs/DVDs. By doing so, the demand that counterfeiters can exploit grows immensely and is a fundamental element creating a real “business case” for criminal organizations which see in counterfeiting an opportunity for immense profit.

- Profits vs. risks

Together with the demand for illicit products and/or services, organized criminals take into account the level of profitability attainable from any given illicit activity as well as the level of risk. In this regards, some of the cases analyzed in chapter 2 have already

¹³¹ In such cases it is as mentioned less probable that consumers would knowingly buy replicated products.

demonstrated the high profits deriving from counterfeiting. Further examples can be obtained from cases in which criminal organizations have been dismantled by law enforcement actions and proceeds of crime confiscated. Digital piracy seems a quite interesting example. In the U.S., for example, the Federal Authorities estimated that the revenues of a dismantled criminal organization dedicated to this trade could reach 1.2 million USD per year, while in another case, also in the U.S., it has been established that a criminal organization remitted to manufacturers of counterfeit goods in Asia 9.8 million USD.¹³²

As mentioned, the level of profitability of counterfeiting has been estimated similar, or even higher, to that of the trade of narcotics. For instance, an estimation proposed in 2005 by the UK National Criminal Intelligence Service, affirmed that a pirated DVD produced in Asia would cost approx. 0,70 USD, while the selling price from street sellers in London would reach 9 USD. This price increase is higher than 1,150 per cent, rendering pirated DVDs potentially more profitable than Iranian heroine or Colombian cocaine.¹³³ The already noticeable profit margin would considerably increase in the case in which pirated DVDs are inserted in the licit supply chain and sold as originals.

For criminals, the risk involved in counterfeiting is significantly low, given that law enforcers tend not to consider counterfeiting a top priority for action. Penalties in the majority of countries, as mentioned, are also less severe if compared with those applicable to other “serious crimes”. The relatively low level of apprehension generated by this illegal activity is due to the initial perception that counterfeiting was associated only to luxury or textile goods, and it did not generate sufficient concern to warrant incisive action by law enforcement officials. The involvement of organized criminal groups in these activities has, however, multiplied the number of goods subject to unauthorized replication, thereby leading to the “evolution” of counterfeiting and its

¹³² Refer to: RAND, Global Risk and Security Center (2009), *Film Piracy, Organized Crime, and Terrorism*, page 43 and 46, available online: http://www.rand.org/pubs/monographs/2009/RAND_MG742.pdf [last accessed on 22 March 2011].

¹³³ Refer to: RAND, Global Risk and Security Center (2009), *Film Piracy*, cited, page 28.

transformation into a large scale trade.¹³⁴ In addition, the significant potential for intimidation and corruption by organized crime has facilitated the expansion of trafficking in replicated products as well as the opportunity to offer them within normal sales channels, thereby also reaching unaware consumers. Increasing evidence of the presence in the market of counterfeit goods potentially harmful to the health and safety of consumers should disown the idea of counterfeiting being a “victimless crime”.

Illegal trading which is both highly profitable and presents low levels of risk is certainly appealing to organized crime. This appeal is enhanced by the relative logistical simplicity of the commerce itself, the widespread distribution of technologies which allow for a faithful external reproduction of the product and the possibility of exploiting existing trade routes and synergies previously created by various groups to manage other types of illegal trade.¹³⁵ The combination of these characteristics ensures that counterfeiting is an opportunity that modern organized crime will not fail to exploit.¹³⁶

In addition to these elements, counterfeiting is also an important instrumental tool for the criminal group to easily launder proceeds from other crimes. Considering that counterfeiting is a huge source of money with a relatively low risk and a tool to launder proceeds of crime, the profit vs. risks ratio is extremely favorable for counterfeiters and constitutes one of the most important motivations at the basis of organized crime involvement in this illicit activity.

¹³⁴ “La contrefaçon est passée à partir des années 1990 d’une activité artisanale – de petits ateliers clandestins – à une logique industrielle, s’appuyant sur des installations coûteuses et modernes. Les contrefacteurs n’agissent plus de manière isolée et ponctuelle et sont devenues de véritables «entrepreneurs internationaux», reliés à de grands réseaux extrêmement organisés. Jamais la contrefaçon n’a semblé aussi fortement structure” (“Counterfeiting has moved since the 1990s from an craftsman’s activity - carried out by small clandestine workshops - into a industrial logic, based on expensive and modern plants. The counterfeiters do not act nay longer in a isolated manner and have become veritable «international businessmen» connected to large and extremely organized networks”). Refer to: Union des Fabricants (UNIFAB) (2010), *L’Impact de la contrefaçon*, cited, page 9.

¹³⁵ Refer to: Centre d’Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 33.

¹³⁶ “It could be the buying; it could be the selling; it could be the manufacturing. But with the profits on offer, organized criminals are not going to leave it all to some guy in a garage, are they?” Refer to: Phillips T. (2007), *Knockoff, The Deadly Trade in Counterfeit Goods*, page 124.

As affirmed by the *Union des Fabricants* in its Reports dedicated to counterfeiting and organized crime,¹³⁷ the actual severity of the problem – especially for what concerns the mass production of goods and the organization of their distribution – would not have been reached without the involvement of criminal organizations. It is precisely this involvement that transformed counterfeiting into a mass-production industry.

- Production and distribution networks: the expansion of the counterfeiting trade

The involvement of organized crime with its financial, intimidating and corruptive power is at the very basis of the immense spread of counterfeiting. The production and distribution of counterfeit goods is today a veritable global business that can rely on a series of practices and smuggling methods successfully put in place by criminals. These considerations are valid for all the different phases of the counterfeit goods' trade: production, distribution and sale to consumers.

a) Production

The production phase is characterized by the high quantity produced, the size of some of the discovered production sites, the significant level of technology used during production and the overall entrepreneurial management. Each of these elements demonstrates the availability of large capital allocated for these activities and a high level of organization. Criminal organizations have transformed this activity into an actual mass production industry capable of supplying aware consumers and deceiving unaware ones.

The outsourcing of production by licit producers may provide an additional opportunity for counterfeiters to improve the production phase. Once the complicity of an unserious delocalized producer is ensured, it is possible to produce quantities of goods that exceed the job order amounts received,¹³⁸ and use the same production tools made available to the delocalized producer by the party owning the intellectual property rights.

¹³⁷ Refer to: Union des Fabricants (UNIFAB) (2010), *L'Impact de la contrefaçon*, cited.

¹³⁸ This is possible by implementing an unscheduled work shift or by subcontracting the received job order.

In this way, an additional advantage is attained: the production of a counterfeit good whose quality is basically identical to that of the original one.¹³⁹

Box 3 illustrates some examples relative to successful police operations showing the scale of the problem. The illustrated cases refer to different types of products and share the common characteristic of involving large quantities of goods.

BOX 3

- In 2010, 400,000 counterfeit erectile dysfunction pills were seized in Argentina.
- In 2010, Bulgarian Police Seized 2,5 Tons of Counterfeit Washing Detergent.
- In 2010, the U.S. authorities confiscated 15,000,000 pairs of fake shoes.
- In 2010, law enforcement authorities in Malaysia seized 700,000 DVDs.
- In 2010, the U.S. authorities seized 100,000 illicit goods worth 1 million USD.
- In January 2007, 6,000 liters of counterfeit oil and almost 148,000 clothing items and 700,000 DVD's were seized in Italy.
- In September 2006, the Anti-Fraud service of the Italian customs together with the Guardia di Finanza seized 1,500,000 counterfeit clothing items and shoes whose commercial value was estimated in more than 1,5 million Euro.
- In February 2006, the Italian customs and the Guardia di Finanza seized 3,5 million counterfeit BIC pens. It was the biggest seizure of counterfeit pens ever made in the world.
- In December of 2004, French authorities seized 258 rolls of counterfeit fabric reproducing the Louis Vuitton brand. The total length of the seized fabric was 9,405 meters, sufficient to create more than 28,000 fake wallets and more than 18,000 counterfeit bags.
- In December 2004, other important seizures were carried out in France. The first involved more than 96,000 counterfeit felt animals which were not in compliance with currently effective safety standards, while the second involved more than 10,000 clothing items reproducing counterfeit trademarks. The latter originated from Spain and were en route to the Italian and French markets.

Sources: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon & criminalité organisée*, 3rd edition; Italian Customs Agency; and Website of the International Chamber of Commerce – Commercial Crime Services, <http://www.icc-ccs.org/home/cib/live-seizure-report?resetfilters=0>

b) Distribution

¹³⁹ Refer to: World Intellectual Property Organization (WIPO) (2004), *WIPO National Seminar*, cited, page 7.

In the distributions phase, varying levels of organization and complexity are identifiable.

Due to more frequent controls caused by the increasing awareness of competent authorities on the extent of the problem and its associated risks, it has become extremely complicated for the production and distribution network to disguise the real origin of the products. This is usually accomplished by avoiding any evidence suggesting an origin from “sensitive” locations which are known as sites of counterfeit goods production. Cargoes are therefore diverted several times in order to pass through different transit points for the purpose of deceiving the authorities with regards to their actual origin.¹⁴⁰ The transit or entry point is selected taking into consideration the severity of local legislation, as well as the relevant degree of application by law enforcers. A clear example of this practice was reported in connection with an interception of a cargo of counterfeit batteries in the spring of 2002 by customs authorities in Vancouver, Canada. The batteries reported an origin in the United States, despite the cargo having arrived from China. Several months earlier, U.S. officials implemented a similar operation that involved the same type of counterfeit batteries, suggesting that the cargoes were diverted to Canada. The latter was chosen as an entry point due to the lower level of border controls compared to the U.S.¹⁴¹ This problem has recently also become a key factor within the European Union, where differing legislations could serve as an element that counterfeiters can exploit for their trafficking.¹⁴²

The logistical management of the trading of counterfeit products is in general facilitated by the high volume of commercial exchanges between countries, as well as by the elevated number of containers arriving in ports and commercial hubs every day.¹⁴³

¹⁴⁰ In July of 2002, for example, the competent authorities of Roissy intercepted a cargo of more than 2.5 tons of counterfeit watches originating from Hong Kong and bound to Spain. A few days later, another cargo was intercepted: in this case, the counterfeited goods were sports clothes from Vietnam that were bound for the Czech Republic. Refer to: Union des Fabricants (UNIFAB) (2003), *Counterfeiting & Organized Crime*, cited, page 8.

¹⁴¹ Refer to: Isaac B., Osmond C. (2006), *The Need for Legal Reform*, cited, page 8.

¹⁴² “It is entirely conceivable that infringers may avail themselves of differences between national laws”. Refer to: Commission of the European Communities (1998), *Green Paper*, cited, page 8.

¹⁴³ “Consider: American imports and exports total about \$1.7 trillion a year; nearly 14 billion tons of goods and raw materials, valued at over \$8 trillion, move over the U.S. transportation system every year; On a

Since customs authorities cannot physically check all goods flowing in and out from a national territory¹⁴⁴ – at least not without causing an actual block in trade¹⁴⁵ – counterfeiters may manage to relatively easily transfer large quantities of counterfeit products.

In order to evade border controls, counterfeiters also resort to a variety of techniques to disguise the goods – by mixing original and counterfeit products or by using double bottomed transportation means. Such technique was used in the year 2000 on a Bulgarian ship transporting goods from Ukraine. The law enforcement inspection revealed that a double bottom had been created from one of the fuel tanks containing more than 220,000 pirated CD's whose market value was estimated to be 500,000 USD.¹⁴⁶

The problem becomes even more complex when the imported good is not a finished counterfeit product, as the practice of subdividing the components of a product in several shipments is also widespread. This is the case of shirts and relevant counterfeit trademarks shipped separately, or the case in which a product is delivered first followed by its counterfeit package.¹⁴⁷ In such cases, the manufacturing process is completed after delivery so as to share the risks involved in shipping. If only the container containing the shirts or the products without trademarks is intercepted, it will not be seized during customs controls. The loss would thus affect the shipment of the counterfeit trademarks or the packages. The same manufacturing or assembly process may be subdivided into several countries so as to increase the complexity of the distribution and to reduce the probability that the trade routes are traced. A well-known European case concerning

typical day, 38 million tons of commodities are shipped on the nation's transportation system; more than \$400 billion is spent each year on the movement of cargo in the United States. This creates a massive inspection challenge for law enforcement." Refer to: FIA International Research LTD. (2001), *Contraband, Organized Crime and the Threat to the Transportation and Supply Chain Function*, page 14.

¹⁴⁴ It is estimated, in fact, that only 3 per cent of containers which cross borders are subject to controls.

¹⁴⁵ "The immense size and complexity of the transportation and supply function provides organized crime groups with an almost infinite number of ways to conceal smuggled, counterfeit or pirated goods." Refer to: FIA International Research LTD. (2001), *Contraband* cited, page 13.

¹⁴⁶ Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 27.

¹⁴⁷ Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 26.

counterfeit medicines may serve as a clear illustration of this phenomenon. The raw materials – which can in turn be counterfeited – originated in Turkey while the product was manufactured in Greece. The drug was marketed through a Dutch importer by means of a Swiss “broker”.

The complexity of the distribution network makes it extremely difficult to exactly identify the supply chains, also because criminal groups are capable of deftly modifying their trade routes. As a result, on the basis of known cases it is currently only possible to identify a few of the major collection points: the ports of Antwerp, Hamburg and Amsterdam or the airports of Schipol and Roissy, in Europe. Outside of Europe, Dubai, Hong Kong and some U.S. ports serve as important transit points.¹⁴⁸ According to the *Union de Fabricants*, the majority of counterfeit products which are marketed within the EU would originate from outside the EU, specifically China, Thailand, Morocco or Turkey. However, the EU itself is a very active production center for a range of replicated products. Countries such as Italy or Portugal, for example, are often associated with the counterfeiting of clothing items, while Spain and Italy are the countries that are most highly associated with the production of fake spare parts for automobiles.¹⁴⁹ These products are not only intended for domestic markets, but are also exported. As a result, the EU community is an important strategic area for the sale, production and transit of counterfeit goods.

Some examples presented in Box 4 are very useful as practical illustrations of the concealment methods mentioned above.

¹⁴⁸ Refer to: Union des Fabricants (UNIFAB) (2003), *Counterfeiting & Organized Crime*, cited, page. 8.

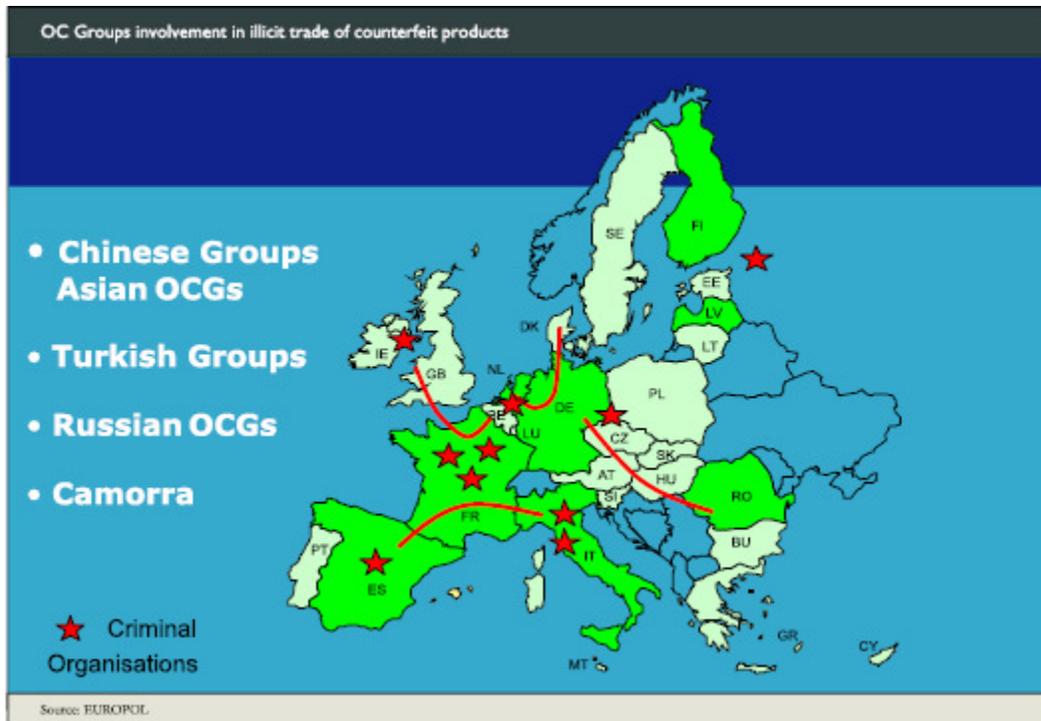
¹⁴⁹ Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 25.

BOX 4

- 1 July 2009: HP Middle East, in conjunction with Dubai Police, conducted one of the largest seizures of counterfeit printer cartridges and components worth Dh70 million in Dubai. The raid uncovered an illegal counterfeit operation in Dubai at a 600 square meters warehouse with two floors filled with packaging materials and security labels as well as finished goods. The counterfeit goods were intended for export to countries in the Middle East, Europe, and Africa. Four people were arrested and Dubai Police started a criminal investigation.
- 2007: The customs office of the port of Le Havre seized almost 410,000 counterfeit medicines (145kg) and 11 millions of medicines with a high pseudo-ephedrine content (two tones) for a total of € 5,8 million estimated value. The operation was conducted by customs officers who had been previously informed about a container originating from Syria and destined to Honduras.
- In July 2006 the Italian customs and the Guardia di Finanza intercepted various tons of counterfeit Louis Vuitton products, whose commercial value was estimated in circa 15 million Euro. The merchandise originated from China and was directed to Italy, Greece, Croatia and Montenegro.
- In July 2005 the Italian Guardia di Finanza seized a container with 15 tons of counterfeit toys. The container originated from China and passed through Hungary before being intercepted at the Italian – Slovenian border, transported by a truck.
- In September of 2003, almost 15,000 counterfeit glasses – with an estimated value of 1,262,650 Euro - were seized in the port of Roissy. The cargo originated from the port of Dubai and was en route to Abidjan.
- In December of 2003, customs officials in Roissy carried out another important seizure. In this case, almost 245,000 counterfeit labels of famous brands such as Lacoste, Timberland, Nike and Ecko were discovered. The origin of the shipment was Hong Kong and the goods were en route to Morocco.

Sources: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon & criminalité organisée*, 3rd edition; Italian Customs Agency; Emirates Business 24/7; *Emballage Digest* (2008), 17 December.

A map of the potential trade routes used by counterfeiters has been created by Europol also illustrating connections between criminal groups operating in various countries.



Source: EUROPOL, Undistributed materials

c) Reaching the consumer

The final phase of the distribution process – i.e. when the product reaches the consumer – may also be structured in a variety of ways, depending by the nature of the marketed counterfeit good and the type of consumer which the illegal product targets. In cases involving the offer of goods not posing any risks to public health and safety, such as pirated CDs or most clothing items, and if these are intended for aware consumers, it is possible that counterfeiters will resort to street trading. This may also be implemented by means of small criminal groups involved in the retailing of illegal goods.

With regards to the same type of products, the choice of the marketing method may change if the target consumer changes. If the criminal group plans to deceive unaware consumers, the goods in question must be entered into the legal distribution system. This entry occurs through several modalities. It is possible that the replicated goods are imposed to a retailer who may be blackmailed to sell them or a member of the same

organization that is entrusted with selling the goods.¹⁵⁰ There are, however, cases involving counterfeit products which were discovered in stores managed by owners in good faith deceived by the counterfeiters which inserted their products at the level of major distributors. Another modality primarily linked to the presence of Mafia-type criminal organizations involves forcing the retailer to offer counterfeit products. In some cases, this method has replaced the requirement of a “protection money fee” and is based on intimidation tactics to generate fear of retailers towards the criminal organization and prevents them from reacting.¹⁵¹ In other cases not directly linked to the replacement of this “protection money fee”, the retailer is simply threatened and intimidated in order to force the sale of replicated goods.¹⁵²

When the counterfeit product poses a risk to consumers’ health and safety,¹⁵³ the criminal group may attempt to penetrate the legal system, often at a high level of the distribution chain by operating as an actual distributor. This type of market entry provides additional benefits for the counterfeiter given the possibility of marketing significant amounts of non-original goods to retailers that are attracted by the low cost of the products.¹⁵⁴

3.2.2 Counterfeiting as an organized crime activity

¹⁵⁰ “...plusieurs personnes interrogées affirment que d’une manière générale, les détaillants qui vendent de produits de contrefaçon le savent, notamment au regard du prix du produit ou de sa qualité, et nombre de ceux qui vendent de tels produit sont de membres à part entière de cette chaîne criminelle.” (“Many interrogated people affirmed that in general retailers are aware of selling counterfeit products, with particular reference to the prize or the quality of the product, and a number of those selling such products are member of the whole criminal chain”). Refer to: Centre d'Etudes Internationales de la Propriété Industrielle (CEIPI) (2004), *Impacts de la contrefaçon*, cited, page 28.

¹⁵¹ Refer to: Confesercenti (2007), *Contraffazione e criminalità informatica* (“Counterfeiting and IT crimes”), TEMI – Centro Studi e Ricerche sulla Legalità e Criminalità Economica, , page 9.

¹⁵² “In the late 1990s, Humatrope, an Ely Lilly product, was being illegally manufactured in a factory at Pilling near Liverpool. The offender was sentenced to five years, though he maintained that he was forced to manufacture this product having been subject to assault and death threats by a Liverpool crime gang.” Refer to: Satchwell G. (2004), *A Sick Business - Counterfeit Medicines and Organized Crime*, page 49.

¹⁵³ Examples include medicines, toys, spare parts or foods and beverages.

¹⁵⁴ Refer to: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon et criminalité organisée*, 3rd edition, cited, page 15.

As already mentioned, counterfeiting is a transnational criminal activity, very often managed by the same criminal organizations that are implicated in the commission of a multiplicity of other crimes. The connections between counterfeiting and other crimes are not limited to the sharing of the same trade routes and concealment methods, or to their potential interchangeability. The *modus operandi* that criminals put in place to safeguard their illicit activities through bribery or resorting to their elevated intimidation power is also applied in the case of counterfeiting. In Malaysia, for instance, the president of a municipal council was subject to death threats after initiating actions against those selling counterfeit Video Compact Disks. In Russia, the director of the Russian anti-piracy organization (RAPO) was subject to a murder attempt which, according to evidence, was directly linked to an operation that was conducted some time before, during which 117,000 counterfeit DVDs and 1,060,000 counterfeit bags were seized. In Northern China, one of the commanders of the economic investigations unit of the Industry and Trade Administration was stabbed and killed in his office by a trader of counterfeit liquors following the seizure of more than 1,200 crates of counterfeit products from this trader during the course of an operation conducted by this commander.¹⁵⁵ Serious death threats were also sent to the former Head of the *National Agency for Food, Drugs Administration and Control* (NAFDAC) in Nigeria – Ms. Dora Akunyili – who was actively involved in combating the spread of counterfeit drugs in her country. Under her guidance, the adoption of new norms guaranteeing the authenticity of marketed drugs and more incisive police operations contributed to significantly improving the Nigerian situation. Her efforts have, however, angered criminal organizations involved in the trade of counterfeit medicines and she has been subject to intimidation threats and murder attempts. In 2003, she was assaulted by an armed gang who riddled her vehicle with bullets while she was driving home. Some months later, her office and laboratory were burned down and several armed men broke into her home when she was fortunately not present.¹⁵⁶

¹⁵⁵ Refer to: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon et criminalité organisée*, cited, page 20.

¹⁵⁶ Refer to: Phillips T. (2007), *Knockoff*, cited, pages 209-210.

Box 5 presents a collection of cases highlighting how counterfeiting is often managed by organized crime in conjunction with other crimes.

BOX 5

- In February 2005, French Authorities identified and arrested the members of a criminal organization involved in the trafficking of narcotics between France and Spain. During this operation, law enforcement officials also discovered and seized counterfeit goods, weapons and fake credit cards.
- Investigations conducted by the District Antimafia Bureau of Rome in 2005 led to the discovery of an organization involved in the importation of counterfeit goods by means of forged transportation documents. This organization was involved in money laundering activities and systematically resorted to activities for transferring and concealing capital.
- In September 2004, a criminal organization involved in the illegal trafficking of narcotics – particularly heroine and cocaine – was dismantled in France, more precisely in *Pont-Sainte-Maxence*. Following the investigations, authorities discovered that the criminal group had implemented an actual marketing effort of illegal goods, selling counterfeit and stolen goods along with drugs.
- In October 2001, a police operation conducted by Czech authorities along the Polish border led to the seizure of significant quantities of pirated CD's and narcotics.
- In November of 2000, 22,000 goods labeled with the trademark *Head and Shoulders* were seized in London from the same areas that the criminal group used as a center for drug trafficking.
- In December 1998, investigations following an operation implemented by British customs officials in a plant producing a variety of counterfeit goods – clothing items, designer bags, perfumes and champagne of 52 different brands – ascertained that the owner of the plant was involved in a variety of illegal activities and was subsequently arrested for peddling narcotics.

Sources: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon & criminalité organisée*, 3rd edition, page 18; CEIPI (2004), *Impacts de la contrefaçon et de la piraterie en Europe, Rapport Final*, 2004, pages 32-33; Italian National Antimafia Bureau, Undistributed Materials.

- Examples of criminal organizations involved in counterfeiting

The most well-known criminal organizations involved in the counterfeiting market include the Chinese triads, the Japanese Yakuza, the Neapolitan Camorra and the Russian Mafia. Cases around the world confirm the interest of these criminal organizations in

counterfeiting activities and their presentation also anticipates some of the elements that will be further analyzed in relation to the criminal management of counterfeiting (as the concealment methods of the shipments, money laundering activities, links with other crimes and the transnational element of counterfeiting).

An investigation conducted in Great Britain in 2001 revealed the existence of a Russian criminal network, which simultaneously managed various forms of trafficking. The significant presence in the country of counterfeit CDs originating from Russia or Eastern Europe called the attention of local authorities, leading to the initiation of an undercover operation. They discovered that the activities of this criminal group were not limited to the trafficking of counterfeit products, but also involved the trading of arms, pornographic materials and counterfeit credit cards. The link with these types of activities convinced the British authorities that organized crime was involved; subsequent investigations led to the arrest of several members of the organization.¹⁵⁷

Various sources and cases confirm the active involvement of organized crime of Asian origin. Some years ago, a considerable Asian criminal network involved in counterfeiting was dismantled in the region of Madrid, Spain. The operation led to the seizure of 230,000 CDs and 346 CD burners in addition to other counterfeit items, as well as a sum of 48,000 Euro.¹⁵⁸ According to the *Union des Fabricants*, the Japanese Yakuza had colonized its respective national market, shifting from the management of large-scale counterfeit trading to control over the retailing of these products. In addition, the counterfeiting market also serves as an area of alliance between the Yakuza and organized crime groups of Israeli origin.¹⁵⁹ Asian criminal organizations also appear to be active within the United States. Already in 1995, an undercover operation conducted by U.S. authorities, in collaboration with the *Asian Organized Crime Section* of the U.S.

¹⁵⁷ Refer to: Alliance Against Counterfeiting and Piracy (2003), *Proving the Connection – links between intellectual property theft and organized crime*, page 12, available online: <http://www.allianceagainstiptheft.co.uk/downloads/reports/Proving-the-Connection.pdf> [last accessed on 22 March 2011].

¹⁵⁸ Refer to: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon et criminalité organisée*, cited, page 27.

¹⁵⁹ Refer to: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon et criminalité organisée*, cited, Ibidem.

Department of State, revealed the fundamental role played by a Korean criminal group in the management of significant volumes of traded counterfeit products.¹⁶⁰ A criminal group of Asian origin also managed an important trade of counterfeit CDs which were distributed in the UK during the Christmas period of 2002. Investigations revealed that the Asian criminal organization exploited Afghan refugees seeking asylum by using them as a sales force on the streets or markets.¹⁶¹ The Chinese Triads, on the other hand, managed a significant amount of counterfeit DVDs in the UK in 2002. The retail distribution phase utilized Chinese illegal immigrants whose entry into UK territory was planned by the criminal organization itself; the latter was also involved in the trafficking of human beings from China.¹⁶²

Italian criminal organizations are also actively involved in the trafficking of counterfeit products. The Italian National Antimafia Bureau confirms the significant profitability of counterfeiting for criminal organizations. Implemented investigations confirm that the counterfeit goods are often sold at a retail level – not only by exploited immigrants but also by regular retailers who acquire such goods due to their low costs. Although the whole Italian territory is affected, the Campania region, particularly the port of Naples, is particularly active.¹⁶³ The Italian National Antimafia Bureau believes that the Camorra's interest in counterfeiting can be interpreted as an evolution of their previous activities as “*magliari*” (“merchant swindlers”) and is fully included within the growing commercial expansion of the criminal group's areas of interest. This criminal organization apparently often controls legal commercial activities through which it introduces replicated goods into the market, thereby creating a significant economic-financial web involving a variety of countries – particularly Western European countries, the United States, Brazil, Canada and Australia. This embedded financial network – which serves as confirmation of the elevated organizational level and internationalization currently attained by the Camorra – allows for the realization of capital funds which, after being “cleaned”, can be reinvested

¹⁶⁰ Refer to: APCO (2003), *Global Counterfeiting Background Document*, cited, page 21.

¹⁶¹ Refer to: Alliance Against Counterfeiting and Piracy (2003), *Proving the Connection*, cited, page 14.

¹⁶² Refer to: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon et criminalité organisée*, cited, page 27.

¹⁶³ The Italian National Antimafia Bureau states that large cargoes of counterfeit goods – transported in containers from China – were seized in the harbor areas of Naples and Gioia Tauro. Refer to: Italian National Antimafia, Unpublished materials.

in a variety of different legal commercial activities, thereby increasing the operational capacities of the organization. The Italian National Antimafia Bureau also highlights the growing links between Chinese criminal organizations and the Neapolitan Camorra. Chinese immigrants organize themselves into structures with criminal connotations for the production and marketing of counterfeit goods but also for the illegal immigration of their fellow citizens, who are exploited in these illegal production and distribution structures in Italy. Investigations conducted across the Italian territory confirm the international ramifications of counterfeit goods' trafficking and the involvement of the same organizations in other forms of illegal trading and money laundering, as well as the use of corruption and intimidation to force retailers to sell counterfeit goods. In particular, the Italian National Antimafia Bureau highlighted that several years ago individuals associated with high-level members of the Camorra had moved to Liguria (region located in the North-west of Italy at the border with France) and were forcing local retailers to acquire exclusively fake designer trademarks.

Other operational modalities of organized crime were discovered during a different investigation conducted in 2005 by the District Antimafia Bureau of Rome. In particular, the following were noted: 1) the use of forged transportation documents for the purposes of concealing the real origin of the goods;¹⁶⁴ and 2) significant transfers of capital towards China by filing tax returns inconsistent with the financial figures implied by the transfers. As a result, there was a link with counterfeiting activities in addition to operations involving money laundering.

Investigations related to operations of Camorra in Naples are enlightening. Significant elements have been discovered thanks to statements made by collaborators of justice (the so-called "*pentiti*"). The results of these interrogations confirmed that counterfeiting was managed in conjunction with other illegal activities, such as narcotics peddling, and that the proceeds deriving from counterfeiting were reinvested into various activities. In the Naples area, there were several plants producing fake leather jackets

¹⁶⁴ In the case in question, the goods originating from Singapore appeared to be from Dubai. Refer to: Italian National Antimafia, Unpublished materials.

controlled by the criminal group, and selling their goods in Italy and abroad. The criminal group managed counterfeiting activities practically in the whole world, including in Belgium, Brazil, France, Germany, Great Britain Ireland, Russia, Spain, Switzerland, and the United States. The collaborators' statements confirmed that the Camorra retained a monopoly of the business of counterfeit leather jackets and Bosch drills – produced in Hong Kong, China – in Germany. Collaborators also confirmed that the proceeds deriving from these illegal activities were significant in amount – and often greater than those attainable from the trafficking of narcotics.¹⁶⁵

- Characteristics of the criminal management of counterfeiting

There are other important aspects associated with organized crime involvement in counterfeiting, for which cases have been collected as practical examples of the criminal management of counterfeiting, namely: the transnational element and the cooperation established among various criminal organizations; the use of counterfeiting as a money laundering instrument; and the links with other criminal activities, in general. Specific attention is given to the links between counterfeiting and labor exploitation, especially for what concerns the use of victims of trafficking in persons in the various phases of the production and distribution of counterfeit products.

a) Transnationality

In 2010, Europol and Eurojust supported an operation against a criminal organization responsible for the trafficking of counterfeit products originating from China.¹⁶⁶ The goods were imported in Italy through the port of Naples, and then redistributed all over the world. To minimize the risks counterfeit labels of well-known companies were delivered separately and later affixed by the criminal gang. Once ready,

¹⁶⁵ Refer to: Italian National Antimafia Bureau, Unpublished materials.

¹⁶⁶ The counterfeit products were mainly power tools (as chainsaws, electric generators, drill hammers and electric generators) and clothing. The electrical goods did not comply with any EU safety standard and posed safety threats to their users. Refer to: Europol (2010), *Camorra-type clan behind massive counterfeiting of power tools and clothing*, 21 May, available online: <http://www.europol.europa.eu/index.asp?page=news&news=pr100521.htm> [last accessed on 22 March 2011].

the products were also offered through door-to-door promotion. The profitability was extremely high since, for instance, the cost of one electric generator produced in China was approximately of 35 Euro, while it was offered by the door-to-door vendors at a price of 400 Euro.¹⁶⁷ It was estimated that a team of two vendors could generate 250,000 Euro after only 2-3 months of illegal activity. The criminal organization in Naples had ramifications all over the world, reaching – besides many EU countries – also Australia. The Naples’ Prosecutor’s Office investigating this illicit trafficking discovered an articulated network of import-export of counterfeit goods. A close cooperation was established among the law enforcement agencies of the Czech Republic, Germany, France, Sweden, Spain and the United Kingdom. This operation led to the arrest of 11 individuals and the seizure of materials and assets whose value exceeded 11 million Euros. This action was part of a larger criminal investigation that had been running since more than two years, which had already led to the arrest of 60 individuals and the seizure of more than 800 tons of counterfeit goods, whose estimated value exceeded 12 million Euros.

Along with the transnational element, this case shows how criminals are attentive in trying to reduce the risk of their actions. It also shows the high profits attainable and the different distribution methods used to reach potential buyers. The transnationality of the crime is one of the main aspects of the following case: the European Commission Anti Fraud Office (OLAF) coordinated an operation, named “Operation Diabolo II”, which led to the seizure of more than 369,000 counterfeit products (as shoes, toys, cameras, headphones, hats, caps, gloves, handbags) and 65 million counterfeit cigarettes.¹⁶⁸ This operation was conducted within the framework of the Asia Europe Meeting (ASEM) and consisted in targeting and posing under surveillance containers arriving in Europe from Asia during autumn 2009. Three hundred and forty-six suspect containers were analyzed in this timeframe and 30 containers were identified as shipments of counterfeit products.

¹⁶⁷ This represented in any case an appealing price for potential buyers, since the price of an original branded electric generator is approximately of 1,250 Euros. Refer to: Europol (2010), *Camorra-type clan*, cited.

¹⁶⁸ Refer to: Europol (2010), *Europol part of a successful operation against counterfeiting*, 20 January, available online: <http://www.europol.europa.eu/index.asp?page=news&news=pr100129.htm> [last accessed on 22 March 2011].

Cooperation between Europol and Interpol subsequently led to the arrest of 89 individuals in different countries.

Another operation conducted in 2009 clearly shows the transnationality of the crime, the huge profits attainable and the exploitation of illegal immigrants in manufacturing sites. A criminal network linked to Chinese, Turkish and Italian syndicates was discovered to be at the center of a production/distribution network of counterfeit clothing. The goods mainly originated from Italy and Turkey and were then distributed throughout Europe by the criminal organization. The operation was coordinated by the Italian Guardia di Finanza – with the support of Europol, Eurojust and Interpol – in close cooperation with law enforcement and judicial authorities of several countries: Austria, Belgium, France, Germany, Italy, Luxembourg, the Netherlands, San Marino and Spain. The evidence collected led to the discovery of a series of connections among several transnational criminal groups operating in Belarus, Canada, China, Israel, Italy, Mauritius, San Marino and Turkey. These groups were also involved in other crimes and were exploiting illegal immigrants in the production centers of counterfeit products. As a result of the investigations, 12 individuals were arrested in Italy and France, 16 illicit factories were dismantled in Italy and 3 million counterfeit items were seized in Italy, Germany and France affecting more than 10 different brands and representing a value of more than 150 million Euros.¹⁶⁹

b) Money laundering

As mentioned, counterfeiting serves a dual function for the organized criminal group: a source of financing for other illegal activities and a tool to launder proceeds derived from various crimes.¹⁷⁰ There are cases in which the proceeds from other crimes

¹⁶⁹ Refer to: Europol (2009), *16 factories producing counterfeit goods dismantled in Italy*, 21 December, available online: <http://www.europol.europa.eu/index.asp?page=news&news=pr091221.htm> [last accessed on 22 March 2011].

¹⁷⁰ “The draw of counterfeiting for organized crime syndicates is that it is relatively safe due to public perceptions that counterfeiting is a ‘victimless’ crime and the corresponding ‘soft’ penalties under the law. It is also by its very nature a source of tax-free income that generates enormous profits. It is therefore targeted as a way to generate funds for other criminal activities and as a vehicle for laundering funds from other criminal activities.” Refer to: APCO (2003), *Global Counterfeiting Background Document*, cited, page 20.

are used to finance counterfeiting and cases where the opposite occurs. This double connection can also be illustrated in reference to certain cases involving the trafficking of narcotics. In 2003, local authorities in Thailand discovered and blocked a trade of counterfeit goods and cannabis where the proceeds from the latter were re-invested in the acquisition of replicated goods intended for the French market. A similar case occurred a year earlier in the United States where investigations relative to drug trafficking showed that the same criminal group was involved in the sale of counterfeit goods, whose production was financed with revenues from drug sales. A case involving the opposite situation occurred in Mexico in 2002: proceeds derived from the sale of counterfeit CDs were most likely re-invested in drug trafficking and in the exploitation of prostitution.¹⁷¹

The end result is a complex economic system whose goal is often the laundering of money derived from illegal activities; this system connects the illegal activities of the organization with various “businesses” and criminal groups. Counterfeit goods are produced or acquired with money generated from other illegal activities exhibiting a high risk level and are sold and marketed according to the modalities described above, thereby allowing these proceeds to be laundered by re-investing the amounts in activities which are characterized by lower risks for the organization.¹⁷² The economic and commercial connections are often more complex and tend to link several criminal groups. The presence of minor criminal groups connected to the bigger organizations gives rise to new money flows that must be taken into account when analyzing the economic complexity of this system. Minor groups are often useful for facilitating the final part of the illicit activity, as they control the territory where final retailers of counterfeit goods operate. Their presence creates new money flows connecting retailers to the minor criminal group – by means of “protection money” payments – as well as minor groups to large criminal organizations. The minor groups use “protection money” revenues to acquire for example, narcotics, which they can resell to retailers in their market. It

¹⁷¹ Refer to: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon et criminalité organisée*, cited, page 19.

¹⁷² Refer to: FIA International Research (2001), *Contraband*, cited, page 30.

therefore becomes possible to identify the origin of the black money laundered through counterfeiting.¹⁷³

Some recent cases relate to Asian criminal groups operating in the United States. These groups have been extremely smart in exploiting the booming trade between Asia, Canada and the United States. This is the case, for instance, for the Yi Ging and the Jah gangs. The first was a criminal organization operating in New York from the year 2000 in the production and selling of pirated CDs/DVDs, and other counterfeit goods. The organization was also involved in drug trafficking, witness tampering, extortion and gambling.¹⁷⁴ This criminal organization came to the attention of law enforcers after a raid conducted in a retail store of pirated CDs and DVDs. However, what the authorities later discovered was a veritable criminal organizations involved in several other criminal activities, including violence and intimidation, as demonstrated by the destruction of a rival group's DVD-R facility perpetrated by the gang. For this criminal organization, piracy meant a profit of approximately 1.2 million USD per year. The counterfeit goods were manufactured in China and then smuggled into New York. The payments for the counterfeits were remitted to China in cash or by money transfer, facilitating money laundering operations. The proceeds from the piracy activity were also successfully laundered, and thus any estimation on the real scale of this business became extremely difficult. The Jah organization was also operating a large-scale piracy and money-laundering operation. The system used to launder the proceeds of crime was similar to that used by the Yi Ging organization: the illegal money transfers. Law enforcers discovered that the money laundering operations run by the Jah organization were extremely important, as it operated as a veritable illegal money transfer service across the United States and around the world that was capable of laundering more than 41,6 million USD in unregulated wire transfers and bulk cash smuggling.

- *Case Study*

¹⁷³ Refer to: FIA International Research (2001), *Contraband*, cited, page 30.

¹⁷⁴ Refer to: RAND, Global Risk and Security Center (2009), *Film Piracy*, cited, page 43.

A very interesting case made available by the Italian Authorities and still ongoing in 2011 shows the presence of many elements so far underlined: the transnationality of the crime together with a clear organizational and collaborative scheme linking different criminal organizations from different countries. The case refers to the illicit operations of the Italian Camorra, which controls several production centers of counterfeit products and – through alliances with Chinese criminal groups operating also in Italy – has ensured a subdivision of tasks for the management of goods inflowing from China.

Investigations conducted in the Neapolitan area – initially started to contrast a production-distribution facility of counterfeit fashion goods – successfully dismantled a complex criminal organization dedicated to the trade of counterfeit shoes and clothing relying on a series of local and international manufacturing sites. Many of the aspects of the criminal organization came progressively to light. What initially appeared as an “interesting” production-distribution organization was in reality a complex transnational network linking Italian and Chinese criminals. The products mainly originated from China, Turkey and local factories in the Neapolitan area. Criminals often sold the counterfeit products as low-price originals through accomplices in regular shops. This was made possible thanks to the high quality of certain reproductions, leading the investigative authorities to believe that they were probably manufactured in the same factories where legitimate brand owners delocalize their production. Both channels of commerce continuously requested the trade managers an impressive number of products, leading the law enforcers to affirm that the level of production could not satisfy the demand. The criminal structures participating in this illicit trafficking were linked in a variety of ways even if they maintained their independence. The case suggests that a stable cooperation among criminal organizations originating from different countries was put in place to manage this illicit activity, while each organization was also involved in other criminal activities on its own. Various raids and seizures were conducted by the Italian Guardia di Finanza, but the criminal organization was always capable of re-organizing its production and distribution methods, showing a level of organization, ramification and economic power that was not entirely apparent at the beginning of the

investigations. This element further convinced law enforcers on the need to deepen their action.

The investigations also deepened the knowledge regarding the supplying channels. Both the Italian and the Chinese criminals relied on a complexity of relations, connecting various actors and production sites. Each supplying channel was probably in competition with the other and was completely autonomous in the purchase of the raw materials, the actual production of the goods and their delivery to the criminals that “placed an order”. Furthermore, each supplying channel was not working only for this particular criminal organization, as it was supplying also other distribution channels managed by other criminal organizations. The size and importance of the organization supplying counterfeit products from China allowed the law enforcers to affirm that the Neapolitan organization dedicated to the distribution was considerably less important if compared to the distribution network put in place by the Chinese importers. This latter criminal import-distribution network was led by a Chinese national and turned out to be extremely well organized. The leader directly kept contacts with the manufacturers in China and with various members of the organization responsible for a smooth distribution of the goods – not only clothing items but also other products, as razor blades¹⁷⁵ – in various transit countries before reaching Italy. Shipments usually passed through countries like Spain, Greece, Hungary or Austria to dissimulate their origin and make them appear at the eyes of the Italian custom authorities as an Intra-EU shipment: corruption was often used for this purpose. Once the goods reached Italy, they were stored in several different places all over the country. Many individuals from different countries participated in this criminal scheme and, at the same time, some of them were responsible for their own autonomous distribution channel, thereby creating further ramifications of the organization. The connection among the various phases and criminal groups participating to the distribution network headed by the Chinese national were obvious, since, for instance, the level of production in China was adjusted according to the level of demand generated in Italy by

¹⁷⁵ As this criminal organization was involved to import and distribution of products not only linked with counterfeit shoes and clothes, let law enforcers believe that it was independent from the distribution network target of the investigation. It is probable that the organization supplied its products also to other distributors in several countries.

the criminal organization based in this country. Many of the members of the Italian organization also owned a licit shop or importing company, allowing for an easier entry of the counterfeit products into the legitimate supply chain.

This case clearly shows a transnational element and a cooperation scheme linking several criminal organizations. It also confirms some of the distribution methods previously highlighted, for what concerns both the disguising of the real origin of the shipment and the introduction into the legal market

c) Labor exploitation, trafficking in persons and smuggling of immigrants

One of the various consequences of organized crime involvement in counterfeiting relates to the use of massive work forces in support of the significant production volumes reached by criminal ventures. Regardless of the place of production, worker exploitation is widespread and often involves minors. Counterfeiting is also linked to illegal immigration and human trafficking. Immigrants or victims of this trade are exploited by counterfeiters during the production and distribution phases and are often forced to endure grueling work shifts under poor hygienic and safety conditions. It is often the criminal organizations themselves which manage the trafficking of human beings that will subsequently be exploited as workers. As discovered during a 2002 investigation on pirated CDs conducted by the Spanish Civil Guard, part of the organization was involved in collecting the workforce while other members of the criminal group acquired the CD burners and rented apartments and basements to use as production centers. The workers were exploited in a variety of ways, either as sales “personnel” in the streets or production workers.¹⁷⁶

More recent cases concerning pirated CDs/DVDs syndicates confirmed this *modus operandi*. Victims of human trafficking or smuggled migrants are very often obliged by criminals to repay their supposed relocation debts and are exploited by criminal

¹⁷⁶ Refer to: Union des Fabricants (UNIFAB) (2005), *Rapport contrefaçon et criminalité organisée*, cited, page 17.

organizations. Labor exploitation is one possible way and is quite common. The discovery of this scenario resulted from investigations conducted in the United Kingdom which started as an interdiction of pirated DVDs.¹⁷⁷ After the arrest of two individuals accused of illicit import of pirated DVDs, law enforcers conducted a search in the apartment of one of the suspects. It was this search that revealed not only the size of the import-distribution network, but also the details regarding the functioning of the criminal group. Human trafficking activities were so discovered, as the organization forced the victims (mainly Chinese citizens) to sell pirated DVDs to repay their “debts”. The organization imported the illicit products from Malaysia into the United Kingdom while the victims of trafficking usually passed through a well-known route linking Beijing with England by way of France, Africa and Spain.

Some years later the Spanish authorities dismantled a piracy ring that was using a similar *modus operandi*. Also in this case the criminal organization was exploiting Chinese citizens, victims of human trafficking, as workforce. Further investigations discovered that it was the same criminal organization that, after having started its activities in the CDS and DVDs piracy sector, began to be involved also in human trafficking in order to obtain cheap work force for these operations.¹⁷⁸

¹⁷⁷ Refer to: RAND, Global Risk and Security Center (2009), *Film Piracy*, cited, page 55.

¹⁷⁸ Refer to: RAND, Global Risk and Security Center (2009), *Film Piracy*, cited, page 57-58.

4. CONCLUSIONS AND RECOMMENDATIONS

The information, data and cases presented in this Report have shown the complexity of counterfeiting and its links with organized crime. Two elements should be in particular highlighted:

Counterfeiting is a transnational criminal activity managed by the same criminal organizations that are involved in other serious crimes, as drug trafficking, arms smuggling, trafficking in persons, corruption and money laundering. Counterfeiting is at the same time a serious global threat endangering the whole society, as its consequences severely affect consumers' lives, producers' entrepreneurial capacities and countries' stability.

An effective response to counterfeiting must take into account the complexity of this phenomenon. Scarcity of precise data and information; lack of effective data collection mechanisms; low level of awareness on the seriousness of this crime by both law enforcers and general public; inadequate response by national governments and International Community are strictly interlinked elements, which need to be tackled in parallel for an effective response. Planning and implementing a coordinated and multidisciplinary action against counterfeiting implies the recognition of the seriousness of the problem and of the importance of dedicating appropriate resources to its contrast.

Counterfeiting affects every region in the world and is potentially a deadly trade. Recognizing this aspect is of fundamental importance in order for International Organizations, governments, and national authorities to build a shared comprehensive strategy allowing the various actors to work together towards a common goal.

This process may take a long time while organized crime is extremely fast and very well equipped to expand its illicit businesses. The following proposals indicate some crucial aspects that could facilitate a proactive preventive strategy.

4.1 Understanding the phenomenon

The knowledge of this problem is worryingly still limited. A number of factors contribute to this situation: the nature of the phenomenon – which is based on commercial exchanges occurring in an underground market and whose assessment is consequently difficult – a lack of proper communication strategies, and research efforts on its scale, magnitude and consequences.

Producing reliable knowledge on counterfeiting must be a priority. Its strategic role as basis for the identification of preventive strategies and effective actions to counter counterfeiting must be emphasized.

This implies the establishment of mechanisms for the collection, analysis and dissemination of information. Data collected should cover as many geographical areas and production's sectors as possible. This aspect was highlighted in our 2007 Report and the Recommendation proposed remains entirely valid:

“Greater efforts should be committed in identifying data which is useful for an analysis of the phenomenon in addition to systematic data collection and processing. The presence of more data would be fundamental in order to proceed with incisive actions against counterfeiting while the processing of this data would allow the effectiveness of these operations to be verified. Both the public and private sector should actively contribute towards these objectives.”

In the 2007 Report, UNICRI highlighted the difficulties encountered in providing precise figures and estimates concerning the dimension of the phenomenon and the losses caused by counterfeiting. The situation in 2011 has hardly changed. Qualified

information on the real dangers posed by the counterfeiting to consumers' health and safety and its criminal management is still lacking. The difficulty in retrieving and obtaining data is common to all the aspects of this illicit activity.

Three important aspects of counterfeiting surely deserve more attention and further research efforts: 1) *the consequences of the problem*; 2) *the involvement of organized crime*; and 3) *the role of the Internet as a facilitating factor for the trade in counterfeit products*.

1) The limited knowledge on counterfeiting is directly responsible for the underestimation of its negative effects and the diffusion of a perception that considers counterfeiting as a “victimless crime”: this also because for a long time counterfeiting was associated exclusively with luxury goods.

To respond to the need of a solid knowledge base on counterfeiting, its strategies and consequences, UNICRI started a series of specific reports dedicated to product categories with a high potential to endanger consumers' health and safety (as medicines, spare parts, toys, or food and beverages). The first of these reports has been dedicated to counterfeit medicines and will be published in the course of 2011.

2) The lack of information on the negative effects that counterfeiting causes to job positions, to taxes and revenues collected by governments, and to the sustainable development of economies has prevented adequate awareness and attention by law enforcement authorities and governments. Bound to the idea that counterfeiting was a craftsman's activity, national authorities did not properly consider the involvement of organized crime in this profitable activity. Counterfeiting has thus been given the possibility to grow undisturbed while criminals were given the chance to find a huge source of profit and further expand to an illegal industry that today is highly organized, owning an enormous market and incorporating an international network of productive-distributional structures.

In-depth research needs to be conducted to provide more evidence with regards to organized crime involvement in counterfeiting, at all its stages. Analysis should focus on how criminal organizations work and which strategies they use for the trade in counterfeit products and their insertion in the market. This information would greatly support both the spread of knowledge on the phenomenon and the design of appropriate responses at the national and international levels.

3) The use of the Internet is a facilitating factor for offering and selling counterfeit products. Counterfeiters are resorting to online advertisement through the use of spam, auction sites or fake internet sites similar to the ones of legitimate producers. Few research efforts have been dedicated so far to clearly analyze the importance of these advertising methods and if/how the various actors involved are linked to criminal organizations.

The importance of the Internet as a facilitating factor for the offering and selling of counterfeit products deserves an urgent analysis. The role played by criminal organizations in this respect and their connections with spammers or fake internet web-sites should also be further investigated. Research should also be conducted on the role of Forums or other social media facilitating the discussion among consumers interested in buying counterfeit products.

Further to general lack of data and analysis, existing data are widely scattered. For the collection of data regarding organized crime involvement the full cooperation from the law enforcement authorities is vital, but also the private sector owns a great deal of information, as in many cases brand owners have a specific department dealing with the fight against IPRs infringements. These departments have several tasks that vary from the collection of information and suspect cases to the preparation of raids in cooperation with the law enforcers. However, there are still many difficulties in information sharing.

The public and private sectors have a key role to play in data collection efforts, as both are a potential repository of important specific information. Cooperation modalities on data collection should urgently be identified, together with appropriate warranties on the proper use of the sensible data in order to respect and overcome confidentiality issues that may arise.

Particularly in some sectors, the possibility to obtain specific data upon which building up reliable estimates has to confront with serious difficulties, due to a phenomenon linked to illegal markets. Unfortunately, the sectors characterized by a scarcity of data are very often the most “critical ones” for consumers’ health and safety. In many cases the situation is worsened by the lack of reporting mechanisms, in a considerable number of countries, and/or of competent authorities to receive such report.

The creation of national and international databases and standardized collection/analysis modalities is extremely important in order to systematize all non-sensitive information obtained by law enforcement officials and private entities. Periodical review of this data and sharing of the results accomplished amongst the various parties is today absolutely critical.

4.2 Communicating the knowledge

The lack of information and awareness on the seriousness of the phenomenon and its consequences is an aspect that consumers and law enforcers often have in common. Lack of proper information on the consequences of the counterfeiting caused citizens not to consider counterfeiting as a socially unacceptable behavior and not to recognize the dangerous consequences it creates. Consumers often do not even know that products like medicines or food and beverages can be counterfeited and that their use could lead to serious health consequences. They are not properly informed on the role played by criminal organizations are behind this illicit activity. Furthermore, a great number of consumers of counterfeit products do not perceive themselves as victims of crime. On the

contrary, aware buyers of counterfeit products often consider themselves smarter than those paying more to purchase the original product.

Citizens must be informed of the real dangers created by counterfeiting, on the profits that this activity is granting to organized crime, and on the health and safety hazards posed by some categories of counterfeit goods. Proper awareness raising campaigns should be designed and implemented.

Although few information campaigns have been launched in the last few years, they were rarely designed after a proper profiling of their target audience with the consequent risk of obtaining only limited results. Innovative ways in which consumers can be “reached” and sensitized are also to be properly considered. For this reason:

In 2010, UNICRI published a series of guidelines for the design of awareness campaigns, suggesting some elements that should be taken into consideration by the campaign planners in order to maximize the possibilities of success. Funds should be invested to explore the potentialities of new technologies to channel and disseminate the information. Innovative methods as social networks should be tested and evaluated.

The 2007 Report highlighted that often, law enforcers and national authorities have a tolerating attitude towards this crime leaving to citizens’ capacity to identify the dangerousness of counterfeiting. Counterfeiting plays a very important role for criminal organizations by allowing considerable financial resources and facilitating money laundering operations. The consequences created by counterfeiting are extremely serious and do not justify any tolerance towards this crime. Even if the situation is progressively improving, the proposals of the 2007 Report are still valid.

Training and awareness programs on counterfeiting for law enforcement officials should be implemented, particularly with regards to organized crime’s

involvement, social consequences and the importance of properly contrasting its perpetration.

Counterfeiters resort to offering low cost products to distributors and retailers who, due to the external resemblance, may believe that they are discounted originals. This is a critic element for the security of the distribution chain, since the counterfeit products acquired by distributors or retailers infiltrate the legitimate supply chain where sold as originals.

Producers, distributors and supply chain's actors should also be targets of specific information campaigns on the serious risks linked to counterfeiting and the importance of respecting good distribution practices.

Fearing reduced market shares or lost of trust by consumers, producers sometime do not properly or timely communicate to the public the presence of counterfeit versions of their products on the market. Prompt communication of the dangers would be a sign of responsible action and contribute to the protection of citizens. In the long run, a responsible behavior would also lead to a growth of consumers' trust towards these producers.

Regulations should be adopted to incentivize producers in timely and proper disclosure of information regarding the presence of counterfeit versions of their products on the market.

4.3 Building up a multifaceted strategy

Both the 2007 Report as well as the present one underline how the multifaceted nature of counterfeiting requires a complex response. The many aspects and actors involved lead to the impossibility of identifying a single solution to the problem, which requires the elaboration of a strategy involving parallel actions in different sectors. The application of civil remedies is only a "palliative" to contrast the expansion of the power

of organized crime. There are very few cases of in-depth investigations in this direction, thus the involvement of organized crime rarely comes to the surface and criminals continue to carry out their illicit lucrative business undisturbed. Current poor investigations and national and international cooperation to ascertain organized crime involvement are allowing the expansion of organized crime. While counterfeiters often employ trafficked people or illegal immigrants as street sellers or in the production – besides considerations on the secondary victimization of these people – low efforts are dedicated to international investigations to dismantle the entire criminal structure.

The investigation phase should be directed to ascertain the presence of organized crime in counterfeiting cases in order to dismantle the entire criminal organization. Particular attention should be paid to the analysis of money flows, the cooperation between different criminal organizations and links with other crimes managed by the same organization. The elaboration of investigative protocols and the organization of specific training courses should be thus implemented.

In 2010, UNICRI produced a set of investigative guidelines in cooperation with the Italian Finance Police and the National Antimafia Bureau and is currently implementing a series of specialized training courses for law enforcement officials and prosecutors.

The reason why criminal organization is involved in counterfeiting is its enormous profitability combined with low risks implied if compared to other illegal activities. Even if the situation is progressively changing, sanctions and penalties for criminals involved in counterfeiting are often inadequate for the purposes of deterring the commission of a crime.

Legislative regulations should provide stronger sanctions and should be effectively applied. Legislative provisions should punish all phases linked to counterfeiting: the export, transit, harboring, sale and import of these illicit goods.

The private sector has an important role to play, as it may be a source of important information for the early detection of the counterfeit goods and the deepening of the investigations. For this reason, and as already noted, in the 2007 Report:

Strong collaboration mechanisms between brand owners and law enforcement agencies should be put in place, with the aim of facilitating the discovery and investigation activities.

International cooperation should play a significant role in support of governments' efforts against this crime. The identification of new international contrast mechanisms requires a lot of time, whilst organized crime is very dynamic and fast in adapting to new contexts: thus governments should make use of international instruments already established.

Being a global problem with a global spread, managed by transnational organized crime, international cooperation in the fight against counterfeiting is of paramount importance. The United Nations Convention against Transnational Organized Crime (UNTOC) may play a fundamental role in this respect, enhancing and facilitating the creation of a common approach against organized crime involved in counterfeiting. The recognition of its applicability in the case of counterfeiting would also allow for the use of powerful instruments that are dedicated to the fight against organized crime and that are present in both the national and international legal frameworks.

4.4 The role of the United Nations

Given the complexity of the problem and the various actors involved in its contrast or affected by its consequences, what we will be able to achieve in the next years will mainly depend on our capacity to improve the level of cooperation among these actors, both at the national and international level. The United Nations could play a fundamental

role in this regards, acting as a trustable clearing house for the collection and analysis of all information on counterfeiting, ensuring confidentiality and presenting independent reports based on this collection and assessment process. For specific production sectors posing threats for consumers' health and safety, the United Nations should also act as facilitator for a stronger cooperation among the various actors involved in the prevention and fight of counterfeit products, promoting dialogue and exchange of good practices and successful experiences.

The United Nations should take a leading role for the comprehensive collection, assessment, analysis and dissemination of information regarding the criminal management of counterfeiting and the consequences created by this crime for the entire society. The creation of a common platform with this role and responsible also for bringing together different actors involved in the fight against counterfeiting, would support the sharing of information and good practices, creating a needed step forward in the fight against counterfeiting.

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