

DISCUSSING PRODUCT COUNTERFEITING IN A BASIC MARKETING COURSE

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ABSTRACT

Trademark counterfeiting is a growing problem for consumer and industrial marketers. This paper relates an educational perspective to the trademark counterfeiting problem. Suggestions for including a discussion of counterfeiting in the basic marketing course are included.

INTRODUCTION

Marketers face a multitude of challenges when competing in a market. One challenge that marketers face is the task of differentiating their products from those of the competition. Normally this effort involves creating a unique product concept and building a reputable brand name. Unfortunately, a successful brand name often attracts emulators hoping to skim short-term profits without making a similar capital investment as did the legal owner of the brand. In some cases, emulators may compete illegally by counterfeiting the brand name product. The problem with counterfeit products has reached epidemic proportions as worldwide sales of counterfeits have increased from \$8 billion in 1982 to over \$23 billion in 1985 (*Business Week* 1985; Dugan 1984). During the same period, counterfeit products resulted in a sixfold increase in the loss of jobs in the United States from 131,000 to 770,000. Additionally, the counterfeit problem is predicted to get worse in the future as developing countries view product counterfeiting as a source of much needed hard currency and as a way of assimilating technology into their countries (Ball 1984; Dugan 1984).

The threat that counterfeit products pose for marketers makes it imperative that marketing students understand the nature of the problem and potential courses of action that can be taken to control product counterfeiting. However, since the topic isn't covered in most marketing principles textbooks (e.g., Boone and Kurtz 1986; Kinnear and Bernhardt 1986; Kotler 1986; McCarthy and Perreault 1987; Stanton and Futrell 1987; Zikmond and d'Amico 1986), many marketing students may not be getting this exposure. Even books on new product development (e.g., Urban, Hauser, and Dholakia 1987) and the legal aspects of marketing (e.g., Stern and Eovaldi 1984) do not address the problem of product counterfeiting. To address the shortcomings of these textbooks, this article will provide marketing educators with the educational perspectives of product counterfeiting which may be used in the basic marketing course. This will be accomplished by discussing the meaning of product counterfeiting; relating the determinants and legal considerations of product counterfeiting; highlighting individual firm and industry efforts to control

product counterfeiting; and illustrating where in the basic marketing course product counterfeiting may be integrated.

WHAT IS PRODUCT COUNTERFEITING?

Many activities are related to product counterfeiting. In legal terms, counterfeiting involves the unauthorized copying of some or all parts of a product such that the copy would confuse or deceive the consumer. An example of a counterfeit would be a cola drink packaged with the Coca-Cola logo. A fake is a slang term for counterfeit. An imitation uses a name or shape which differs from the original but is close enough that the consumer will associate the imitation with the original. For example, the Izod alligator logo could be imitated with a lizard. (Imitations per se are not illegal. However, if the purpose of an imitation is to defraud the consumer, then it would be illegal.) A knockoff is a product that copies the design of an original product but carries a different brand name. Piracy is the copying of a creation with the purpose of the copy passing as the original. Computer software and audio recordings are often pirated. Passing off involves a simulation of an original trademark.

DETRIMENTS OF PRODUCT COUNTERFEITING

The detriments of product counterfeiting involve both short and long-term costs which impact society and the marketer of the brand name being counterfeited. The short-term cost that counterfeiting inflicts on society is the loss of tax revenue that would have been generated from the sale of the more expensive brand name product and duties from illegally imported counterfeits. The long-term economic and social cost born by society involves the loss of jobs to counterfeiters who operate in cheap labor markets - e.g., Mexico and the Philippines.

The cost of controlling counterfeiters can be substantial and can have a significant impact on the profitability of a brand name marketer. For example, Chanel, which produces the often imitated Chanel No. 5 perfume, spends approximately \$1.2 million annually on security against counterfeiters (*Business Week* 1985). Social costs also are incurred in attempts to control counterfeiting since resources are directed away from investments in research and development and new equipment.

Counterfeiting also takes a toll on consumers by defrauding them into paying brand name product prices for counterfeits of inferior value and unenforceable warranties. For example, in 1985 counterfeits manufactured in the Far East and in South America not only copied the trademark and packaging of Carrera eyeglasses but inserted in the package a registration card complete with a false serial number (Green 1985). Optyl's Carrera Division estimated the fake warranties cost it millions of dollars in consumer goodwill beyond the \$10 million it lost in sales.

Counterfeit consumer products have the potential to inflict more than economic harm on consumers. Product liability costs to the brand name marketer may increase when counterfeit affect the health and safety of consumers. To give just a few examples:

- Several children were burned when their counterfeit Cabbage Patch Kids, stuffed with rags soaked in kerosene, broke open and exposed the rags to the children (Business Week 1985).
- In 1978, the Federal Food and Drug Administration recalled over three hundred heart pumps, which maintain a patient's heartbeat during surgery, because they contained an \$8 counterfeit part (Rakoff and Wolff 1983).
- A counterfeit of G. D. Searle's Ovulen 21 birth control pill, which contained low levels of estrogen resulted, in several product liability actions when it caused heavy bleeding and/or unwanted pregnancies (Business Week 1985).
- Counterfeit amphetamines and tranquilizers were traced to several deaths in the United States in 1985 (Business Week 1985).
- Counterfeit polio vaccines have been given to unsuspecting patients (Rakoff and Wolff 1983).
- Fake brake shoes have caused numerous car and bus accidents which have resulted in many injuries (Business Week 1985).

Finally, the damage that a counterfeit can inflict on a brand name marketer's reputation can be severe a cost and have a lasting impact. For example, Chevron Corporation's reputation took a long time to repair when a counterfeit pesticide bearing the Chevron brand name was used on the coffee crop in Kenya with devastating effects (Green 1985). Two-thirds of the 1979 crop was lost to insects because ground chalk was substituted for the insecticide in the counterfeit pesticide.

LEGAL CONSIDERATIONS IN PRODUCT COUNTERFEITING

The legal aspects of product counterfeiting involve a myriad of federal, state, and international trademark laws. The marketing student should become aware of these laws in order to know how government is attempting to protect brand name marketers. Counterfeit legislation passed at each of these levels are now discussed separately.

Trademarks

Trademarks offer some protection against product counterfeiting. A trademark is a registered word or design used by a marketer to identify and protect a unique product offering. The trademark protects against the use of the same mark, or a similar one that is confusing, by a marketer of a similar product (Diamond 1981). The offending mark does not need to be an exact copy of the trademark in order for it to be considered a counterfeit, only that the mark causes consumers to be mistaken, confused, or deceived (Diamond 1981). The protection a trademark provides a consumer product marketer allows the marketer to distribute a product over a wider area and increase sales by establishing a connection between the trademark and the quality of the product (Rakoff and Wolff 1983).

Federal Law

The first official consideration of a federal trademark statute occurred in 1791 when Boston sailmakers requested a mark that would differentiate their sailcloth from other sailmakers (Rakoff and Wolff 1982). However, no action was taken on this initiative until 1870 when the expansion of interstate commerce across a large geographical area rendered most state laws designed to control counterfeiting ineffective. At that time, the Trademark Act of 1870 was passed. However, the Act made no provision for criminal actions to punish those who counterfeited trademarked products. The absence of this provision made the Act an ineffective deterrent to product counterfeiting.

A hodge podge of federal trademark legislation was passed starting in 1881. Again, the legislation provided for civil but not criminal penalties. In 1946, the Lanham Act was passed to replace earlier trademark laws. The Lanham Act provided for the registration of a trademark and civil penalties for infringing on a trademark, up to three times the amount of the damages incurred by the brand name marketer. The Act also provided for injunctions to prevent infringement, and the destruction of counterfeit inventories that are seized. However, the Lanham Act was ineffective in dealing with product counterfeiting because the it did not provide for criminal sanctions and placed the burden on the brand name marketer to discover and build a case against a suspected counterfeiter.

The Federal Trademark Counterfeiting Act of 1984 took a major step toward controlling consumer product counterfeiting by rectifying many of the problems that plagued earlier federal legislation. The Act provided for severe penalties for convicted counterfeiters. First time offenders now face fines of up to \$250,000 for individuals and \$1 million for companies. Jail sentences of up to 5 years for counterfeiters may also be imposed. Repeat offenders face fines of up to \$5 million and 15 years in prison. In the first year and a half that the law was in effect over 500 civil suits and several criminal actions were brought against counterfeiters (Crandell 1986).

State Law

Most states have statutes designed to control consumer product counterfeiting. Usually the statutes pertained to consumer fraud. Although many states' laws provide for criminal penalties, most of the laws are ineffective deterrents because they consider consumer product counterfeiting a misdemeanor. However, in 1984 California became the first state to pass specific legislation that imposed felony criminal penalties against counterfeiters (California Business and Professional Code 1986). The law provides for fines of \$5,000 for individuals (\$100,000 for corporations) and up to one year in county jail. Repeat offenders may receive the same jail term but fines increase to \$50,000 and \$200,000 for individuals and corporations, respectively.

International Law

Despite the international scope of consumer product counterfeiting, few attempts have been made at the international level to curtail counterfeiting. Although the few treaties that exist provide for the registration of trademarks, the treaties do not have a mechanism for prosecuting counterfeiters, and therefore, have been ineffective (Rakoff and Wolff 1983). The International Anti-Counterfeiting Code, which has been jointly proposed by the U.S. and the European Common Market, offers a better chance of controlling consumer product counterfeiting. The Code would require signatory countries to seize counterfeit products when they attempt to clear customs (Rakoff and Wolff 1983).

PRODUCT MARKETER ATTEMPTS TO CONTROL COUNTERFEITERS

Efforts to control the growth of counterfeit products has involved individual product marketers and trade associations. Individual efforts to control counterfeiting have ranged from installing in-house security forces to the adoption of sophisticated high technology. In several cases, in-house security forces have combined with the Federal Bureau of Investigation agents, customs officials and local police to run sting operations or stage raids on factories and warehouses of suspected counterfeiters. For example, in 1984 cooperative sting operations netted Ford Motor Company more than one million counterfeit parts from 28 manufacturers and distributors. Ford followed the sting operations by suing all 28 counterfeiters (Business Week 1985).

Other marketers have built into their products innovative ways of detecting counterfeits. Beginning in 1987, VISA credit cards have included a hologram which makes them difficult to duplicate (Crandell 1986). The hologram is expected to reduce the more than \$100 million annual fraud loss VISA has suffered largely as the result of counterfeit cards. Levi-Strauss weaves a microscopic-fiber which is visible only under a special light into the fabric it uses to make its clothes. When Levi-Strauss suspects a store of carrying fakes, it buys a sample from the store and tests the product with the special

light (Couretas 1985). Micro-printing and trace chemical elements also are being used by companies in the production of their products or packaging as a means of testing the authenticity of their products.

Marketer trade associations also have increased their efforts to control counterfeit consumer products. For example, in 1978 only fifteen firms belonged to the International Anticounterfeiting Coalition, but by 1985 the number had grown to over 300 firms (Couretas 1985). The Toy Manufacturers of America (TMA) has established a network of trade associations in several countries to trace counterfeit Transformer robots and other toys (Business Week 1985). They also helped educate their members to sell to reputable retailers and counterfeit toys have been banned at TMA trade shows.

PRESENTING PRODUCT COUNTERFEITING IN THE BASIC MARKETING COURSE

The information presented in this paper may be discussed in several parts of the basic marketing course. These areas include marketing environments, marketing strategy, product development, and international marketing. The legal history leading to the passage of the federal Trademark Counterfeiting Act of 1984 would be a timely example when discussing how the political and legal environments influence marketing activities. Trademark legislation could be used as an illustration of how government regulation can protect marketers.

Counterfeiting also influences the development of marketing strategy, in that it is a threat to the differentiation of products through trademarks. The educator may point out that the marketer has several possible actions to choose from if confronted with a counterfeit problem. For example, a hands-off strategy may be adopted which allows other marketers to address the problem. Alternatively, a marketer may withdraw from a market where counterfeiting is a problem. Thirdly, the marketer may implement a warning strategy. This strategy would consist of informing consumers of the problem with counterfeits. Finally, a prosecution strategy, which is the most expensive but has the greatest deterrence effect, may be selected. This strategy would involve a periodic examination of each channel member's operations, including purchasing procedures and inventory. If a channel member is found with counterfeit products, the brand name marketer would prosecute the member to the full extent of the law.

In the marketing management portion of the course, product counterfeiting is especially relevant to the topics of information systems, branding, product development, and distribution. Here, one may illustrate how the marketing information system may be used to monitor the environment for the potential counterfeits. Case examples of Cabbage Patch Kids and Chevron may be used to present what detriments counterfeiting holds for reputable brand names.

In discussing product development, one may stress the threats counterfeiting pose for a successful

brand name and marketer attempts to control for the counterfeiting of their products. Some of these control procedures were highlighted earlier and include the inclusion of microscopic fibers, visible with a special light, in Levi pants and the use of printing operations by the Ford Motor Company.

Reselling is the major distribution topic of the basic course where product counterfeiting is especially pertinent. Given the era of designer clothes, watches, and other consumer products, retailers have an interest in controlling product counterfeiting because they effect the profit margins for designer items. In addition, under the Trademark Counterfeiting Act of 1984, retailers face notice letters and seizure orders if they are caught with inventories of counterfeit products. Notice letters are written requests initiated by the manufacturer and sent to retailers and wholesalers demanding that they stop selling counterfeit products. If the wholesaler or retailer does not cease this activity, the manufacturer may get a seizure court order. This order allows the manufacturer to seize sales records and counterfeit inventories, which then can be used in civil proceedings against the wholesaler or retailer.

Finally, product counterfeiting may be presented in the international portion of the basic course. The discussion may focus on the reasons that foreign countries allow counterfeiters to operate within their borders. Among the major reasons are that developing countries look at product counterfeiting as a source of much needed currency and a way to disseminate technology into their economies. Product counterfeiters also are a source of jobs. In addition, and although beyond the scope of this article, different countries' anticounterfeit legislation may be discussed.

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