

# US Customs' enforcement of IP rights on the rise

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When much of a product's value is in its IP, firms must seek enforcement of their IP rights

For tax executives busily engaged in transfer pricing compliance and planning, one area of constant focus centres on the issue of intangibles. While payments for intangibles between related parties can cover many kinds of intellectual property ("IP") and services, the most traditional kinds of IP are patents, trademarks, and copyrights. Often payments for these kinds of IP involve third parties and other non-related entities. Although tax executives are keen on "parking" these payments in low-tax jurisdictions, they often overlook the possible need to report these payments to customs authorities when these payments relate to imported merchandise covered by, e.g., a license or royalty agreement.<sup>1</sup>

However, a related issue has taken on new importance in 2010. US Customs and Border Protection ("Customs") has identified the enforcement of intellectual property rights ("IPR") as one of the agency's top priorities for the foreseeable future. In essence, imported counterfeit goods bearing illegal trademarks/copyrights and infringing on patents held by others are flooding the US market, resulting in a surge of seizures and other actions by Customs' Offices of Fines, Penalties & Forfeitures throughout the United States. To prevent the importation of these illegally imported goods in the first instance, Customs is taking new steps to try and prevent these goods from entering the commerce of the United States.

Customs effectuates IPR enforcement through the co-ordination of multiple offices, including the Office of International Trade, the Office of Field Operations, the Office of Information and Technology, and the Office of International Affairs and Trade Relations. IPR enforcement is such a high priority that Customs has formed an intra-agency "Working Group" to internally co-ordinate IPR enforcement efforts among all of the involved Customs offices and officials.

In addition to its internal efforts, Customs has also engaged in targeted outreach to members of the trade community to assist its efforts at IPR enforcement. Customs offers education programmes to inform IP rights owners about their rights and recourses under Federal IP laws. Where possible and appropriate, Customs also endeavours to share information regarding suspected instances of IPR infringement with rights holders. Additionally, Customs has developed the Intellectual Property Rights e-Recordation system. This system allows rights owners to electronically record their trademarks and copyrights with Customs, which in turn facilitates IPR seizures by making IPR recordation information readily available to Customs officials.

## I. Summary of 2009 seizure statistics

Customs' increased focus on IPR enforcement has resulted in a dramatic increase in the number IPR-related seizures over the past few years – 2005 saw 8,022 such seizures, while that number nearly doubled to 14,841 in 2009. The total domestic value of IPR seizures from 2009 was US\$260,697,937.00. Shipments from China comprised the vast majority of this value, totalling US\$204.7 million, or 79 percent of the total value. Seized shipments from Hong Kong were a distant second, totalling US\$26.8 million in value, and shipments from India came in third, totalling US\$3 million in domestic value.

Footwear was by far the item most frequently seized by Customs for IPR violations, and accounted for US\$99.7 million (or 38 percent) of the total value of infringing goods. Chinese shipments accounted for 98 percent of the seized footwear shipments, by value. The next two top categories of seized merchandise were consumer electronics (US\$31.7 million) and handbags, wallets, and backpacks (US\$21.5M).

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## II. IPR rights enforced by customs

There are three broad categories of intellectual property rights that Customs monitors for possible IPR infringement: trademarks, copyrights, and patents. The following provides a brief overview of the monitoring and enforcement mechanisms in place for each IP category.

### A. Trademarks

In principle, Customs provides infringement protection to any trademark that a mark owner has registered with the United States Patent and Trademark Office (“USPTO”). As a practical matter, however, Customs generally only enforces infringement against trademarks which have also been officially recorded with Customs via the e-Recordation system. Thus, trademark holders wishing to protect their intellectual property must first register a trademark with the USPTO’s principal register, and must then use the e-Recordation system to record the mark with Customs. The e-Recordation system<sup>2</sup> gathers the information that 19 C.F.R. Section 133.2 requires for trademark recordation, such as:

- the name, address, and citizenship of the mark holder;
- the manufacturing locations of legitimate goods bearing the trademark;
- the names and addresses of all persons and companies authorised to use the trademark; and
- information about any related foreign companies that are authorised to use the trademark outside of the United States.

In addition to providing the requested information, recording mark owners must also pay an application fee, currently set at US\$190.

Once a trademark owner has recorded a trademark with Customs, the mark will become part of the database Customs uses to examine shipments of goods bearing trademarks for IPR infringements. When Customs examines such shipments, it looks for IPR infringements that fall into one of three categories:

1. counterfeit trademarks,
2. confusingly similar trademarks, and
3. restricted grey market goods.

#### 1. Counterfeit trademarks

Counterfeit marks are marks that are identical or substantially indistinguishable from a trademark registered with the USPTO. Goods bearing marks that are counterfeit reproductions of recorded trademarks are prohibited from entry into the United States, and as such are subject to seizure by Customs upon importation, pursuant to 19 C.F.R. Section 133.21. In general, Customs will destroy seized goods bearing counterfeit marks, unless the importer can obtain permission from the trademark owner to import the merchandise into the United States. Importers who attempt to bring goods bearing counterfeit marks into the country are subject to severe civil penalties and possible criminal charges under a variety of Federal statutes and regulations.<sup>3</sup>

One recent case decided by the US Court of Appeals for the 9th Circuit addressed an interesting issue regarding Customs’ ability to impose civil penalties on

an importer of goods bearing counterfeit trademarks. In *United States v. Able Time, Inc.*, 545 F.3d 824 (9th Cir. 2008), the court addressed the issue of whether the Tariff Act permits the imposition of a civil penalty against an importer who imports merchandise bearing a counterfeit trademark, when the counterfeit mark is placed on goods of a kind not sold by the true mark owner. The facts at issue in *Able Time* dealt with *Able Time*’s importation of watches bearing counterfeit trademarks owned by Tommy Hilfiger. At the time the watches were imported, Tommy Hilfiger did not itself produce watches with its distinctive “TOMMY” trademark. The importer used this fact to argue that it was immune from civil penalties because the counterfeit goods did not share an “identity of goods or services” with genuine Tommy Hilfiger products. Customs argued that the Tariff Act did not impose an “identity of goods” requirement on the imposition of civil penalties, and that it was therefore irrelevant to the penalty issue that Tommy Hilfiger did not sell watches branded with its trademark.

In deciding the case, the court examined the language of the applicable sections of the Tariff Act: 19 U.S.C. Section 1526(a) (which prohibits the importation of trademarked merchandise without the permission of the mark’s owner); 19 U.S.C. Section 1526(e) (which authorises Customs to seize an imported merchandise bearing a counterfeit mark); and 19 U.S.C. Section 1526(f) (which authorises Customs to impose civil penalties upon the importer of goods seized for bearing counterfeit trademarks.) The court noted that none of the above provisions of the Tariff Act explicitly require that the owner of the trademark make products similar or identical to the counterfeit goods in order for the provisions to apply. The court likewise noted that similar provisions of the Trademark Act of 1946 (known as the Lanham Act) which are incorporated into the Tariff Act also contain no “identity of goods” requirement. The court, examining the statute provisions, concluded that all the civil penalty provision requires is that the counterfeit merchandise must

“bear a mark identical to or substantially indistinguishable from a registered trademark owned by a United States citizen or corporation, where the offending merchandise copies or simulates the registered trademark, meaning that it is likely to cause the public to associate the offending merchandise with the registered trademark . . . .”<sup>4</sup>

The court concluded by stating that

“[n]owhere does this statutory scheme require the owner of the registered mark to make the same goods as those bearing the offending mark.”<sup>5</sup>

Based upon this analysis of the plain language of the statutes, the court dismissed *Able Time*’s arguments that the legislative history of the Tariff Act supported its claim that civil penalties were prohibited in cases where the counterfeit merchandise was of a different class or kind than genuine merchandise. The court therefore held that “Customs may impose a civil penalty pursuant to 19 U.S.C. Section 1526(f) upon an importer of merchandise bearing a counterfeit mark, even though the owner of the registered mark does not manufacture the same type of merchandise.”

## 2. Confusingly similar trademarks

A mark that does not meet the “identical or substantially indistinguishable” legal standard for “counterfeit” may still infringe upon a trademark owner’s IPR if the mark is “confusingly similar” to a recorded trademark. In determining whether a mark is “confusingly similar” to a recorded mark, the legal standard is whether the mark copies or simulates a recorded mark to an extent that it is likely to confuse consumers about the source or sponsorship of the goods bearing the mark. Upon discovering merchandise bearing confusingly similar marks, Customs will detain the goods and give the importer 30 days to address the situation by obtaining permission from the mark owner to bring the goods into the country. If the importer does not remedy the situation within the 30-day window, Customs will seize the merchandise and begin forfeiture proceedings.

## 3. Grey market goods

The final possible category of IPR trademark infringements enforced by Customs is “grey market” goods. Grey market goods are goods that actually bear genuine and not counterfeit trademarks. What makes them “grey market” is the fact that the mark owner has only approved the goods for sale in countries other than the United States. In other words, the importer of grey market goods has not obtained the permission of the US trademark owner to import and sell the goods within the United States, but has obtained permission to sell the goods in other countries.

Customs’ ability to take action against the importation of grey market goods is more limited than against the importation of counterfeit or confusingly similar trademarks. Pursuant to 19 C.F.R. Section 133.23, Customs can only extend protection against grey market goods to recorded trademarks, and only in instances where the US and foreign trademarks are separate entities that are not related parties, i.e., parent/subsidiary or controlled by common ownership. Grey market goods that meet these requirements are subject to detention and seizure proceedings similar to those related above for goods bearing counterfeit trademarks.

## B. Copyrights

Federal statutes and regulations vest Customs with the authority to detain and seize any goods that infringe on copyrights registered with the United States Copyright Office. As with trademarks, this protection theoretically applies to all registered copyrighted works, but as a practical matter Customs only enforces infringement of copyrights that have been recorded with Customs. Copyright owners can record their copyrights with Customs using the same e-Recordation system that records trademarks. As with trademarks, the e-Recordation requires the right holder to provide the information that 19 C.F.R. Section 133.33 requires for the proper recording of a copyright, such as:

- the name, address, and citizenship of the copyright holder;
- the manufacturing locations of genuine copies of the copyrighted work;

- the names and addresses of all persons and companies authorised to make legitimate copies of the copyrighted work;
- foreign titles of the copyright, if different from the U.S title;
- an additional certificate of copyright registration issued by the US Copyright Office;<sup>6</sup>
- five photographic or other likenesses reproduced on paper of the copyrighted work, unless the work is either a sound recording or a book, magazine, periodical, or something similar that is readily identifiable by its title and author; and
- for recording of sound recordings, a statement containing the names of all performing artists and any other identifying names appearing copies of the recording

In addition to providing the requested information, recording copyright owners must also pay an application fee, currently set at the same US\$190 as that for recording a trademark.

Once a copyright owner has recorded a copyright with Customs, Customs will attempt to stop goods that infringe upon the copyright from entering the country. A good infringes upon a copyright if an average lay observer would recognise that an alleged copy was appropriated from a copyrighted work. Goods detained by Customs for possible copyright infringement fall into one of two categories: clearly piratical and possibly piratical. The Customs regulations define “piratical” as copies (of copyrighted works) which are unlawfully made, i.e., without the authorisation of the copyright owner.

Unauthorised copies of copyrighted works are clearly piratical when there is an overwhelming and substantial similarity between the protected work and the suspect work that clearly indicates that one work was based upon the other. Works that meet the clearly piratical standard are subject to seizure and forfeiture pursuant to 19 C.F.R. Section 133.42. If an imported item is not clearly piratical but Customs has a reasonable suspicion that it violates a recorded copyright, Customs may detain the goods as “possibly” piratical, pursuant to 19 C.F.R. Section 133.43. Upon such a detention the importer has 30 days to submit a denial that the goods are piratical, which Customs in turn will verify with the recorded copyright owner. If the importer does not submit a denial within 30 days, the Customs will seize the goods and begin forfeiture proceedings.

## C. Patents

Due to the complex technical nature of most US patents, it is generally impossible to readily identify patents on sight, unlike trademarks or copyrights. Thus, Customs’ enforcement of patent infringements is very limited, and it does not inspect shipments for possible patent violations to the same degree as it does for trademarks and copyrights. Further, patent holders are not able to record patents with Customs, even though patents are registered with the USPTO.

Thus, Customs’ enforcement of patent infringements is limited to enforcing exclusion orders issued by the US International Trade Commission (“USITC”) pursuant to Section 337 of the Tariff Act of 1930 (19 U.S.C. Section 1337). Section 337 is a broad statute in-

tended to provide relief to US industries that have established the existence of harmful and unfair trade practices that involve imported goods. Upon finding such unfair trade practices, one remedy available to the USITC is the issuance of an exclusion order. These orders help to remedy unfair trade practices by excluding the offending goods from entry into the United States. Patent infringement is one reason that the USITC may issue such an exclusion order. These exclusion orders are then enforced by Customs. Note that this process is much more burdensome to the right holder, as it requires a patent holder to obtain an exclusion order from the USITC before obtaining Customs' assistance with the enforcement its patent rights.

However, a recent ruling by Customs Headquarters demonstrates how Customs is becoming more actively involved in determining whether products fall within the "scope" of the USITC's exclusion orders. HQ H067500 (August 5, 2009) shows that it is possible for an importer to challenge the scope of an exclusion order in order to prevent its goods from being seized at the border by Customs for patent infringement under section 337 of the Tariff Act.

The ruling concerned an exclusion order issued by the USITC which found that a large number of digital televisions produced and imported by various manufacturers contained semiconductor chips which infringed on a patent owned by a company called Funai Electric Co. Based on this finding of patent infringement, the USITC issued the order excluding all digital televisions containing these chips from entrance to the United States. Two of the importers whose products were exclusion by the order filed a ruling request with Customs headquarters, claiming that the chips contained in their specific digital televisions did not in fact infringe on the patents at issue, and thus they were not within the scope of the USITC exclusion order.

In examining the petitioners' claims, Customs conducted a series of tests and technical evaluations on the semiconductor chips used in the petitioners' digital televisions sets. These tests – which were specifically detailed within the ruling – ultimately affirmed

the petitioners' position by demonstrating that the semiconductor chips used in their digital televisions did not infringe upon the very detailed, highly technical specifications of the patents at issue in the exclusion order. Because the petitioners' chips did not process digital information in the same manner as the patented chips, Customs HQ ultimately ruled that digital televisions containing the petitioners' chips were outside the scope of the exclusion order, and thus were not excluded from entry into the United States.

### III. Conclusion

In a time of continuing economic downturn, global businesses are looking for every available avenue to increase revenue. With so much of a product's value often represented by its intellectual property component, tax executives should not overlook the need to team with legal counsel in seeking enforcement of their intellectual property rights by US Customs and Border Protection. The surge in illegally imported merchandise into the US which infringes on trademarks, patents, and copyrights continues to rise, and only a collaborative effort between rights holders and Customs will stem this unfortunate rising tide.

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#### NOTES

<sup>1</sup> See Damon V. Pike, *The Tangible Effects of Intangibles: Customs Valuation and IP*, 2008 BNA International Special Report: Transfer Pricing Aspects of IP and Intangibles 17.

<sup>2</sup> Available online at: <https://apps.cbp.gov/e-recordations/>

<sup>3</sup> See, e.g., 19 U.S.C. § 1526(f); 19 C.F.R. § 133.27; 18 U.S.C. § 2320.

<sup>4</sup> Id. at 830.

<sup>5</sup> Id.

<sup>6</sup> If the applicant's name is different from the name of the copyright owner listed on the certificate, the applicant must submit a certified copy of any assignment or other document recorded with the U.S. Copyright Office showing that the applicant owns the copyright.