



Peggy Chaudhry  
Alan Zimmerman

# **The Economics of Counterfeit Trade**

Governments, Consumers,  
Pirates and Intellectual  
Property Rights

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# Preface

The expansion of world trade has brought with it an explosive growth in counterfeit merchandise. Estimates put the world total for counterfeit products at about one half trillion dollars annually, although it is impossible to accurately determine the true size of the counterfeit market. What is known is that this illicit trade has infected nearly every industry from pharmaceuticals to aircraft parts. Software and music piracy are easy targets widely reported in the media. In 2007, the Business Software Alliance (BSA) estimated that 38% of personal computer software installed worldwide was illegal and the losses to the software industry were \$48 billion worldwide. The Recording Industry Association of America (RIAA) reported a 58% increase in the seizures of counterfeit CDs. Overall, a wide range of industries agree that there is a severe problem with the protection of intellectual property rights (IPR) throughout the world, yet there have been virtually no attempts to describe all aspects of the problem.

This work aims to give the most complete description of various characteristics of the IPR environment in a global context. We believe a holistic understanding of the problem must include consumer complicity to purchase counterfeit products, tactics of the counterfeiters (pirates) as well as actions (or inaction) by home and host governments, and the role of international organizations and industry alliances. This book establishes the full environmental aspects of piracy, describes successful anti-counterfeiting actions and then prescribes measures IPR owners should take to protect their intellectual property.

While there have been many articles in the popular and business press that focus on counterfeit trade, there have been only a small number of books published on the subject that address the predicament facing nearly every industry in a dispassionate, intellectual manner. We believe this book fulfills a unique need for a thorough review of all aspects of the IPR problem.

This book is not targeted at consumers although we hope they will find it enlightening. This is a research-based book that can serve as the basis for further inquiries by academics, institutional researchers, and professionals in the international business and legal communities. We believe it should be a useful reference for government officials, managers, and law professionals who are combating counterfeiting as part of their everyday responsibilities in countries throughout the world.

This work is a result of our continuing interest in the subject of counterfeit products. Extensive travel to China and other countries or just walking the streets of New York reminds us that this is a pervasive problem. For about 10 years each of us has been working on various aspects of the problem and we have each published journal articles and delivered conference presentations based on the research we have been doing over that period. We would be remiss if we did not thank Victor Cordell for stimulating our interest in the subject and contributing to our early publications. In addition we would like to recognize the involvement of John Peters whose facility with statistics has been invaluable. Finally, we are grateful for the assistance of Stephen Stumpf, Fred J. Springer Chair in Business Leadership, for sponsoring the funding of research and conference presentations through the Villanova School of Business. Overall, it is evident from the preceding remarks and forthcoming acknowledgments that this book is a result of the inspiration and support of many colleagues. Nevertheless we accept complete responsibility for the text including any errors that may have inadvertently occurred.

September 2008

Peggy Chaudhry  
Alan Zimmerman

## **Dedication by the Authors**

### **Dr. Peggy Chaudhry**

I would like to devote the book to my family. I want to recognize my husband, Sohail for his endless encouragement of my research endeavors. I sincerely acknowledge my parents, Dave and Evelyn, who always supported my career aspirations. Finally, I thank my children, Matt and Aeysha for giving me the motivation to succeed.

### **Dr. Alan Zimmerman**

This book is dedicated to my family whose interest and help has been invaluable. First to my wife Lori for her unstinting encouragement. Also to the next generation: Craig, Dan, Howie, Karen and Matt and their respective partners. And the next: Alex, Abby, Emma, Hannah, Luke, Natalie, Owen, Phoebe, Sophia and Samantha. With this collective intelligence we can solve any problem.



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## **Dr. Alan Zimmerman**

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# Chapter 1

## Introduction

### 1.1 Overview

The desire to own a prestigious brand seems to have spread across the world. But multiple factors conspire to prevent most consumers from acquiring a real Prada handbag or Rolex watch. Many search for black-market vendors in places like Chinatown in New York City, venturing like Toth (2007) down dodgy alleys into dingy basements to find fakes at nearly unbelievable prices. Others find counterfeit look-alikes on the Internet when entering the word “replica” in Google yields nearly 14 million hits. (Replica is the code word on the Internet for counterfeit product.) On the web, it is easy to buy lookalike Rolex watches, Armani sunglasses, Guerlain perfume or the ubiquitous Vuitton handbags complete with phony logo. But things may be changing. On 1 July 2008 a French court ruled that eBay was to pay the owner of the Vuitton brand, LVMH, some €40 million (\$63 million) for failing to prevent counterfeit products being sold over its website (Tait, 2008). On the other hand just two weeks later a New York court ruled against Tiffany & Co. in a similar case. This decision essentially frees eBay from responsibility for assuring that products offered on its site are not counterfeits (Stone, 2008).

But counterfeit products are not limited to designer perfumes, handbags and other highly visible consumer items. Software, DVDs and music are vulnerable to copying. Microsoft claims up to 40% of its software is pirated on a global basis (Anti-counterfeiting amendments, 2004). There is also a large market for phony pharmaceuticals and the results have been catastrophic in various countries. The World Health Organization (2006) estimates the sale of counterfeit drugs at approximately \$40 billion per year now and growing to \$75 billion by 2010. Industrial products are not immune to piracy. The Organization for Economic Cooperation and Development [OECD] (2007c) reports that more products than ever are being counterfeited and the types are expanding. Some authors have identified counterfeit sewer pumps, aircraft bolts and helicopter blades creating major problems for purchasers (Hopkins, Kontnik, & Turnage, 2003; Naim, 2005).

Product counterfeiting is a major problem for brand owners in nearly every country. Many stakeholders are injured by the widespread availability of pirated products. The beneficiaries of these products on the one hand are innocent consumers