

# Brand Piracy ✕ BY SHERRI MILES

IN AN OCEAN OF IMITATIONS, HOW TO PROTECT YOUR PRODUCT WHEN DOING BUSINESS IN CHINA



Whether you're on Canal Street in New York City or Nanjing Road in Shanghai, utter the right brand name and you can be deep in the basement of a hair salon, snack house, or t-shirt shop in a room bursting with fake bags and watches. In China, however, it doesn't stop there: knockoffs are haggled over in open "fake markets," sold in malls with spinoff storefronts—Buckstar coffee, Pizza Huh, Hike—and hawked on Taobao, China's eBay, often for one-tenth of the price of the real product. Doing business in a country that tolerates counterfeits, knockoffs, and lookalikes can seem daunting, but with the right preparation, a brand can compete for real in the fastest-growing economy in the world.

#### WILL THE REAL CHIVAS PLEASE STAND OUT?

It's 2:00am in Taipei, Taiwan, and John McDonnell's phone is ringing. This is not an unusual event since friends back home in America often forget the clock is different on the other side of the world. But this time, it's the local police. They've captured guys in a garage filling empty Chivas Regal Scotch bottles with colored water and resealing them.

"That is true counterfeit," said McDonnell, BSBA '83, chief operating officer and executive vice president of Patrón Spirits. "Imagine what happens to your brand when someone buys a bottle of Chivas and they get that God-awful taste in their mouth."

At the time, McDonnell was country manager for Joseph E. Seagram & Sons and living in Taipei, Taiwan. "We went and rounded up all the brands that copied Chivas Regal in the marketplace. There were



123 different look-alikes in Taiwan. I brought my sales force into the conference room where I'd lined up 20-30 of the brands, and I said, 'Please tell me, which one is Chivas Regal?' My sales people couldn't pick out the real Chivas. They couldn't tell me the brand they sell in the marketplace. That's how close these look-alikes came to Chivas Regal. The wheels came off the bus."

The first thing McDonnell did was train his sales force in the differences between the real product and the fakes, pointing out the subtle variations of the look-alikes and teaching them the value of the brand. A 12-year-old scotch has to be aged a minimum of 12 years, for example, and will taste significantly different from colored, flavored water.

"It was very important that they went out to the retailer and educated them as well," said McDonnell. "There are many different wholesalers: people ride around on Vespa motorbikes selling liquor to people or use their garages; it's not the traditional route to market. It's the wild, wild west," he said.

In 1996, Chivas sold 250,000 cases in Taiwan, but by 2001 the numbers had dropped to 25,000 cases. "We never cut back the advertising. The case drop was attributed to the knockoffs that people were buying. We know from extensive research and taste tests that what happened to Chivas Regal could have been prevented. It's all because we didn't register the trade dress properly."

Trade dress is the appearance of a product and its packaging. It needs to be protected as much as the trademark, which is the name, symbol, and motto legally identifying a company or its product. Without the trade dress properly registered, the shape, label, color, design, and other packaging of the product can be copied. In the case of Chivas, counterfeiters found 123 ways to copycat the original, making minor variations in box packaging, name and age changes on the label, and subtle modifications to label design. For consumers not proficient in the English language, the knockoffs appear the same.

"In my business, there's nothing positive about this. My product is being consumed into the body. If you go to a restaurant and order a Diet Coke, and it doesn't come in a bottle or can and doesn't taste right, you ask for something else. If someone asks for Chivas Regal, and they get something that tastes like colored water, they say, 'What else are you serving?' Once people start drinking it and it's not what they expected, you lose that customer forever."

After Taiwan became a member of the World Trade Organization in 2001, it no longer allowed this practice. Today, however, there remains a secondary market in China and Taiwan where a bottle of Chivas Regal empty is worth \$10 to counterfeiters to be refilled, and sold again.

In 2005, McDonnell joined Patrón as the COO. Having had his fingers burned with the Chivas Regal experience, he took all the steps that Seagram didn't take to protect its trade dress and trademark. "Right away, I knew when we wanted to go into Asia with Patrón, we had to register the name, trademark, trade dress, bottle, label, URLs, on-line social clubs, everything."

"The value of the company has grown because we own the trademark and trade dress in all these markets," said McDonnell. In five and a half years, sales have grown from 200,000 cases to 1.75 million cases. "Five years ago, the value of the company was \$150 million. Today, in 125 countries registered with our trademark, the brand is worth \$4 billion." Patrón still isn't sold in mainland China, although it has been registered there, because the government hasn't yet allowed 100 percent agave tequila to be on the market. When that day comes, McDonnell is ready.

#### A PLACE FOR FAKES

One day while visiting Shanghai, Giana Eckhart, associate professor of marketing at the Sawyer Business School, made it her goal to

## Take aways

### lessons

- US trademark law is atypical
- think international early
- prioritize markets
- register all aspects of trademark, trade dress
- register website URLs, social clubs
- get quality legal counsel
- creatively protect brand integrity

### observations

- demand for counterfeits is strong
- purchasing counterfeits is acceptable
- fakes can signal brand desirability
- consumers are savvy about counterfeits
- minimal cannibalization of brand
- minimal brand dilution
- brand signals are important

### strategies

- contact the registry early
- be careful of your Chinese name
- be vigilant in looking for copycats
- check for cybersquatters
- consider hiring a third party to monitor
- monitor Tao Bao internet shopping site
- educate employees on brand value
- verify your partners
- get contracts in Chinese and English
- specify damages in contracts
- seek administrative legal route

find and buy a real DVD. She spent all day looking but never found one. In China, real DVDs can be purchased at a mall or department store, but often those retailers aren't centrally located or easily accessible. "In many product categories, it is difficult to find the real thing," said Eckhart, an expert on brands and consumer behavior in China. "You might want to watch the real Black Swan movie and not the fake one, but it's actually quite difficult to navigate this in the marketplace."

Counterfeit products exist everywhere. In a study Eckhart conducted that looked at attitudes toward counterfeits in eight countries, she found that in China, counterfeits are a normal part of everyday life, and the reason is tied primarily to a view of consumer ethics quite different from what is seen in the US.

For example, many Chinese consumers do not understand the concept of intellectual property—the idea that a company can own the way something should look. They don't see the "LV"

of a Louis Vuitton bag as property that can't be used. "This is not really a concept that people buy into," said Eckhart. "They say, 'If a local company can use that design on another piece of leather, it shouldn't make any difference.'"

Egalitarianism is also very much a part of the picture. Respondents in Eckhart's study said: "We earn RMB and American people earn dollars. We don't earn as much as everyone else, so we shouldn't be expected to pay those prices. We deserve to pay only a dollar or two for the counterfeit items because there is such an income discrepancy. We can't afford the real thing."

Lack of resources doesn't create lack of desire, especially when people all across the country are exposed to advertisements for global brands on the Internet and television. The Chinese want to buy these brands to be a part of the global community, but from simply an economic perspective, many don't have the means, and that's where counterfeits begin and consumer ethics end, Eckhart said. She discusses these and other findings from her study in the recent book, *The Myth of the Ethical Consumer*, co-authored by Eckhart, Timothy M. Devinney, and Pat Auger.

Interestingly, the counterfeit marketplace creates its own status hierarchy. Consumers pay much more for fakes that aren't noticeably fake. This quality range corresponds to social standing in China and progresses from fake to real, secretary to CEO.

## CHINESE NAMES: getting it right

### phonetic:

Mercedes-Benz in Taiwan "Ben-Tze" means Stupid to Death, or Stupid to the Point of Dying (bad); BMW or "Bao-Ma" means "precious horse" (good)

### conceptual:

Revlon "Lu-Hua-Nong" means "dense dew" from a famous poem; Porsche "Bao-Shi-Jie" means "swiftness to ensure short time"

### Or mixed:

Lancome "Lan Kon" means "orchid" and either "cardamon" or "red nails with balsam blossom"; Hummer: "Han Ma" means "husky valiant horse"

"People are so savvy about counterfeits in China," said Eckhart. "They aspire to own the real thing when they can afford to do so. 'Yes, of course I buy the fake because I can't afford to buy the real,' they say, but there is a flip side: 'As soon as I can afford to buy the real one, I will.' There is an aspiration to have that, and to have all the trappings that demonstrate it's real. You'll see people carrying handbags that still have the price tag on it just to signal, *this is real.*"

### PROTECTING YOUR BRAND

The Chinese government has taken measures to prevent counterfeiting, but it's still the "wild west" in many respects due to the vast size of the country and a population larger than the US and Europe combined, making enforcement difficult.

Chinese regulations protect trademarks and commercial names and designs. Applicable laws include the Trademark Law, Unfair Competition Law, and the Product Quality Law. China is a member of the World Trade Organization (WTO), the World Intellectual Property Organization (WIPO), and party to the Madrid Protocol, all requiring members to honor international trade rules and intellectual property rights.

An important distinction that sets China apart is its approach to trademark registration. "China is a "first-to-file" jurisdiction," said David Woronov, partner at Posternak Blankstein & Lund LLP. "This means there is a horse race immediately to go to Beijing to the trademark registry and to register. Most other countries have the "first-to-use" standard." The first-to-file law allows for "well-known" marks registered elsewhere (Starbucks, McDonalds, etc.) to be given priority if someone else registers them in China first, but lesser-known marks are vulnerable to being snatched up and registered by anyone who believes a brand might have future value.

"The value of your name and your brand has totally come home to roost for international businesses in the last 10-15 years," said Woronov, a specialist in international business law. "Businesses are realizing that having a brand out there, in and of itself, can be worth billions."

Woronov advises clients to contact the registry early and register the trademark, company name, and product name in Chinese and English before someone else does, and before the mark becomes generic. "Be careful of your Chinese names!" he warns. "In China you can try to do an English name in Arabic letters, and come up with what



sounds, to you, like your name in Chinese (phonetic translation) or you could do a conceptual translation that may not sound anything like your name but carries the same meaning or has a good message."

Once registered, businesses need to be vigilant about their brands, Woronov said. "Consider hiring a third-party service to monitor trademark and domain name registrations," he said, "and monitor Tao Bao for knockoffs of your product—it is a huge online resource for sales to the middle class in China."

It also helps to educate employees on the value of their brand. In Chinese culture, gifts are highly valued when celebrating Chinese New Year, marriage, the birth of children, new homes, and other major events, Woronov said. "You don't give a pirated piece of merchandise to somebody as a gift—it's considered a loss of face, and your reputation will be sullied, possibly for the rest of your life."

Lastly, get contracts in Chinese and translate them into English. Specify damages in the contracts because courts will not infer damages, unlike in the US. If you need legal enforcement, seek administrative legal routes that give "equitable remedies." The infringer is fined (criminally) and shut down, but few damages are paid to the brand owner. This quick action may be preferable to lengthy and expensive litigation in Chinese courts that are clogged with cases. (Courts in Shanghai have 20,000 cases in front of them.)

The best way to protect the integrity of a brand in China is to be prepared, develop relationships, and have good contacts, Woronov said. **SB**