VIII.

Penalties, Restitution, and Forfeiture

VIII.A. Introduction

This Chapter discusses the penalties for intellectual property crime, concentrating on the sentencing guidelines, restitution, and forfeiture.

This Chapter does not address the sentencing issues raised by former Attorney General John Ashcroft's September 23, 2003 *Memorandum on Department Policies and Procedures Concerning Charging Criminal Offenses, Disposition of Charges, and Sentencing*, *available at* http://www.usdoj.gov/opa/pr/2003/September/03_ag_516.htm, which instructs that "federal prosecutors must charge and pursue the most serious, readily provable offense or offenses that are supported by the facts of the case, except as authorized by an Assistant Attorney General, United States Attorney, or designated supervisory attorney in the limited circumstances described below." For more on charging decisions, prosecutors should consult the Attorney General's Memorandum, and also Chapter IX of this Manual, which specifically addresses charging decisions in intellectual property cases.

VIII.B. Statutory Penalties

The maximum statutory penalties for intellectual property crimes are addressed in the chapters on the respective substantive laws and are summarized in Appendix I.

VIII.C. Sentencing Guidelines

This subsection addresses the interpretation and application of the United States Sentencing Guidelines ("U.S.S.G.") in intellectual property prosecutions, primarily § 2B1.1 for Economic Espionage Act cases, § 2B5.3 for all other intellectual property offenses, and § 3B1.3 for crimes in which the defendant abused a position of trust or used a special skill. This subsection should be read in conjunction with the sections covering penalties in the chapters that present the substantive offenses, as well as with the chapter on victims' rights.

This Manual does not address the issues raised by *United States v. Booker*, 543 U.S. 220 (2005), in which the Supreme Court held that the United States Sentencing Guidelines must be considered at sentencing but are only advisory. As with other crimes, prosecutors should generally continue to seek sentences within the guidelines range in intellectual

property prosecutions because they are presumptively reasonable. Memorandum from Assistant Attorney General Christopher A. Wray, *Guidance Regarding the Application of United States v. Booker and United States v. Fanfan, 2005 WL 50108 (Jan. 12, 2005), to Pending Cases*, at 5 (Jan. 19, 2005). The intellectual property guidelines have been intricately fashioned through amendment and re-amendment, often incorporating and reacting to court decisions. For general guidance on this issue, prosecutors should consult Deputy Attorney General James B. Comey's January 28th, 2005 *Memorandum on Department Policies and Procedures Concerning Sentencing*, which directs that"federal prosecutors must actively seek sentences within the range established by the Sentencing Guidelines in all but extraordinary cases."

For assistance with any sentencing issues specific to intellectual property crimes, please call CCIPS at (202) 514-1026 for assistance.

VIII.C.1. Offenses Involving Copyright (Including Bootleg Music, Camcorded Movies, and the Unauthorized Use of Satellite, Radio, and Cable Communications), Trademark, Counterfeit Labeling, and the DMCA

VIII.C.1.a. Applicable Guideline is § 2B5.3

U.S.S.G. § 2B5.3 governs sentencing for the following offenses:

- Criminal copyright infringement, 17 U.S.C. § 506, 18 U.S.C. § 2319
- Criminal violations of the Digital Millennium Copyright Act, 17 U.S.C. § 1204
- Trafficking in counterfeit labels, illicit labels, and counterfeit documentation or packaging, 18 U.S.C. § 2318
- Trafficking bootleg audio and video recordings of live musical performances, 18 U.S.C. § 2319A
- Unauthorized recording of motion pictures in a movie theater, 18 U.S.C. § 2319B
- Trafficking in counterfeit trademarked, service-marked, or certification-marked goods, services, and labels, documentation, and packaging for goods and services, 18 U.S.C. § 2320
- Unauthorized reception of cable and satellite service, 47 U.S.C. §§ 553(b)(2), 605 and 18 U.S.C. § 2511

The guidelines' Statutory Index, U.S.S.G. App. A, refers these statutes to U.S.S.G. § 2B5.3.

The one exception is the Digital Millennium Copyright Act, which is not listed in the guidelines' index at all. A statute not listed in this index should be sentenced under "the most analogous guideline." U.S.S.G. §§ 1B1.2(a), 2X5.1. In DMCA cases, the most analogous guideline is § 2B5.3. The DMCA was intended to safeguard the copyright protections for copyrighted works, and copyright crimes are sentenced under § 2B5.3. Moreover, § 2B5.3 implicitly refers to the DMCA in an application note that requires an adjustment for use of a special skill under U.S.S.G. § 3B1.3 "[i]f the defendant de-encrypted or otherwise circumvented a technological security measure to gain initial access to an infringed item." U.S.S.G. § 2B5.3 cmt. n.3 (2005). Although the DMCA and U.S.S.G. § 2B5.3 are not a perfect fit, they are the best match under the current guidelines.

Section 2B5.3 has been amended a number of times. It was amended on May 1, 2000, to "ensure that the applicable guideline range for a defendant convicted of a crime against intellectual property" would be "sufficiently stringent to deter such a crime and to adequately reflect" consideration of "the retail value and quantity of the items with respect to which the crime against intellectual property was committed." No Electronic Theft (NET) Act of 1997, Pub. L. No. 105-147, § 2(g), 111 Stat. 2678 (1997). Among other things, the May 2000 amendments increased the applicable base offense level from 6 to 8 and increased the number and type of special offense characteristics to include not only the infringement amount, but also characteristics for manufacturing, uploading, or importing infringing items; for infringement not committed for commercial advantage or private financial gain; and for risk of serious bodily injury or possession of a dangerous weapon in connection with the offense. *See* U.S.S.G. App. C (Amendments 590, 593). Section 2B5.3 was amended again effective October 24, 2005, adding a new specific offense characteristic (2) addressing infringement of pre-release works, renumbering offense characteristics (2)-(4) as offense characteristics (3)-(5), clarifying the definition of uploading for technical purposes, and clarifying that the court can estimate the infringement amount using any relevant information. *See* U.S.S.G. App. C (Amendment 675).

As of this writing, U.S.S.G. § 2B5.3 is likely to be amended again during 2006 pursuant to the Stop Counterfeiting in Manufactured Goods Act, Pub. L. No. 109-181, § 1, 120 Stat. 285, 287-88 (Mar. 16, 2006). It asks the Sentencing Commission to explore how the guideline should account for items that facilitate infringement such as counterfeit labels and DMCA circumvention devices. See also Section III.E.5. of this Manual.

As is discussed in Section VIII.C.2. of this Chapter, the Economic Espionage Act is sentenced under U.S.S.G. § 2B1.1.

VIII.C.1.b. Base Offense Level

U.S.S.G. § 2B5.3's base offense level is currently 8, up from a base offense level of 6 for offenses committed before May 1, 2000. *See* U.S.S.G. App. C (Amendments 590, 593). The base offense level was raised from 6 to 8 to reflect that "the vast majority" of intellectual property offenses involve more than minimal planning. *Id.*

VIII.C.1.c. Adjust the Offense Level According to the "Infringement Amount"—U.S.S.G. § 2B5.3(b)(1)

Under U.S.S.G. § 2B5.3(b)(1), the base offense level is then adjusted according to the "infringement amount," an estimate of the magnitude of infringement. "Similar to the sentences for theft and fraud offenses, the sentences for defendants convicted of intellectual property offenses should reflect the nature and magnitude of the pecuniary harm caused by their crimes. Accordingly, similar to the loss enhancement in the theft and fraud guideline, the infringement amount in subsection (b)(1) serves as a principal factor in determining the offense level for intellectual property offenses." U.S.S.G. § 2B5.3 cmt. backg'd. The mechanics of calculating the infringement amount are covered in U.S.S.G. § 2B5.3 cmt. n.2.

VIII.C.1.c.i. Formula

The infringement amount is generally calculated by multiplying the number of infringing goods by the goods' retail value. *See* U.S.S.G. § 2B5.3 cmt. n.2(A),(B).

If the defendant infringed a variety of items, the infringement amount is the sum of the individual infringement amounts for each type of item. *Id.* cmt. n.2(D). The infringement amount for each type of item is calculated independently of the others, including whether the retail value should be that of an infringing (counterfeit) item or an infringed (legitimate) item. *Id.* See Section VIII.C.1.c.iii. of this Chapter. The individual infringement amounts are then aggregated into a total infringement amount, which is then plugged into the loss table in U.S.S.G. § 2B1.1. See Section VIII.C.1.c.v. of this Chapter.

VIII.C.1.c.ii. Number of Infringing Items

The number of infringing items can be easy to calculate. Victims or their representatives can often help verify the number when the number depends on whether an item's copyright or trademark has been registered. For a list of industry associations that represent victims, consult Appendix G of this Manual. When the number of infringing items is difficult or

impossible to calculate, however, reasonable estimates are allowed. See Section VIII.C.1.c.iv. of this Chapter.

In determining the number of infringing items, the biggest questions are often whether or to what extent to include items that are incomplete, such as items in the process of production, or that merely facilitate infringement, such as labels and packaging. These questions are discussed at length in Sections III.E.5. (sentencing issues concerning counterfeit marks) and VI.E.5. (sentencing issues concerning counterfeit and illicit labels, documentation, and packaging for copyrighted works) of this Manual. They are also likely to be addressed in upcoming guideline amendments that will be considered after this Manual is published mid-2006.

A recurring question is whether the infringement amount should include all the infringing items that the defendant acquired or only those that he provided to another, such as a customer or co-conspirator. If trafficking is an element of the crime, then the infringement amount should include all items the defendant acquired because the intellectual property crimes define trafficking to include obtaining control over the infringing product with the intent to transport, transfer, or dispose of it. *See United States v. DeFreitas*, No. 98 CR. 1004(RWS), 2000 WL 763850, at *1 (S.D.N.Y. June 13, 2000) (trademark case), *aff'd on other grounds*, 8 Fed. Appx. 58 (2d Cir. 2001). The infringement amount should also include all the items the defendant acquired if he is convicted of an attempt, *id.*, or conspiracy. In such cases, the infringement amount should include all infringing items in the defendant's inventory, plus all infringing items that had been transferred out of inventory.

Determining the number of infringing items in a DMCA case can be a challenge because a defendant can violate the DMCA without engaging in any infringement. See Chapter V of this Manual. The guideline and its commentary give no help. Because these issues are complex and are also likely to be addressed in guidelines amendments that will be considered after this Manual is published in 2006, prosecutors are encouraged to consult CCIPS for guidance at (202) 514-1026.

VIII.C.1.c.iii. Retail Value

The major issues with determining the retail value are what to do when the items have not been fully manufactured, how to value items that facilitate infringement, which market should be used for reference, and whether to use the value of a counterfeit or a legitimate item. These questions are addressed below.

- **Incompletely Manufactured Items**

How to value items whose manufacture is incomplete is treated in Sections III.E.5. and VI.E.5. of this Manual.

- **Items that Facilitate Infringement Such as Labels and DMCA Circumvention Devices**

How to value items that do not infringe but instead enable infringement—such as counterfeit labels, packaging, and documentation, as well as DMCA-violating circumvention devices—raises complex issues. These issues include whether to use the value of the item that facilitates infringement (such as the label or circumvention device) or the item that would be infringed, and how to value items that could facilitate the infringement of a variety of items that have disparate prices (such as clothing labels that could be attached to low-priced children's clothing or high-priced men's suits or ladies' dresses). These issues are discussed briefly in Sections III.E.5. and VI.E.5. of this Manual, and are also likely to be addressed in upcoming guideline amendments that will be considered after this Manual is published in 2006.

- **Choosing the Correct Market**

"[T]he 'retail value' of an infringed item or an infringing item is the retail price of that item in the market in which it is sold." U.S.S.G. § 2B5.3 cmt. n.2(C). To define the relevant market in which the items are sold, the government should focus on the market's geographic location, whether it exists on the Internet or in real-world storefronts, and whether it is sold in a legitimate market or a black market.

- **Infringing/Counterfeit vs. Infringed/Authentic Retail Values**

Infringing items often trade for much less than authentic items. Using the retail value of one rather than the other can easily mean the difference between months and years in prison, if not between prison and probation. Consequently, whether to use the retail value of counterfeits or authentic items is often the predominant issue at sentencing.

The general rule of fitting the punishment to the harm applies to selecting the retail value. Intellectual property crimes create four basic types of harm: (1) the fraud on consumers who were tricked into buying something inauthentic (at the defendant's prices), (2) the legitimate income that rights-holders lost (at legitimate prices) when consumers mistakenly bought the defendant's items, (3) the rights-holders' inability to control the use of their property, whether consumers were defrauded or not, and (4)

the defendant's unjust enrichment (at the defendant's prices) by using the rights-holder's intellectual property unlawfully.

To value these harms, the law simplified the inquiry into whether the defendant caused or was likely to have caused the victim to lose sales or not. If so, the maximum measure of harm is the victim's lost sales, which are valued at the victim's own prices. If not, the maximum measure of harm is the defendant's gain, which is valued at what the defendant took in, at his own prices. And if the counterfeit price was hard to determine, then the harm should be computed at the legitimate item's price for ease of calculation.

The guidelines, however, originally directed courts to account for these harms by using only the retail value of infringing (counterfeit) items. *See* U.S.S.G. § 2B5.3(b)(1) & cmt. n.1 & backg'd (1998). But this presented some difficulties when the counterfeit items had been distributed for free, such as pirated software and music that was freely available over the Internet, which would have resulted in an infringement amount of $0. Nor did the Guidelines explain how to calculate the retail value of the infringing items when that value was difficult to determine: whereas the retail value of legitimate items is easily measured, the retail value of counterfeit items is not always obvious.

Notwithstanding the original guidelines' silence as to a legitimate item's retail value, the courts recognized its relevance in a variety of circumstances. The Second Circuit clarified that high-quality fakes should be valued at the retail price and lower-quality fakes should be valued at the counterfeit price. *See United States v. Larracuente*, 952 F.2d 672, 674-75 (2d Cir. 1992). Other courts recognized that a genuine item's price could help determine a counterfeit item's retail value when it otherwise was difficult to determine. *See United States v. Slater*, 348 F.3d 666, 670 (7th Cir. 2003) (refusing to assess zero value to free software distributed over the Internet because courts "need only make a reasonable estimate of the loss, given the available information"); *United States v. Bao*, 189 F.3d 860, 866-67 (9th Cir. 1999) (stating that the retail value of genuine merchandise is relevant as a ceiling for the retail value of infringing items); *United States v. Cho*, 136 F.3d 982, 985 (5th Cir. 1998) (stating that it is "not clear error for the district court to rely on the retail value of genuine items [to assess] the retail value of the [counterfeit] items," particularly when it is difficult to calculate the counterfeits' price); *United States v. Kim*, 963 F.2d 65, 69 (5th Cir. 1992) (holding that evidence of genuine items' retail value was relevant to the retail value for the counterfeits in absence of other evidence of counterfeits' value); *United States v. DeFreitas*, No. 98 CR. 1004 (RWS), 2000 WL 763850, at *2 (S.D.N.Y. June 13, 2000). In fact, the *Slater, Bao*, *Kim* and

DeFreitas courts ultimately relied on the retail price of the infringed (legitimate) goods, even though the former guideline's plain language referred only to the retail value of the infringing (counterfeit) merchandise.

On May 1, 2000, the sentencing guidelines caught up to the case-law by concentrating on the harm the defendant caused, whether he displaced the victim's legitimate sales, and how hard it is to calculate the counterfeit's value. *See* U.S.S.G. App. C (Amendments 590, 593). Application Note 2(A) to U.S.S.G. § 2B5.3 now instructs the court to use the retail value of an authentic item if *any one* of the following situations applies:

- **The infringing item "is, or appears to a reasonably informed purchaser to be, identical or substantially equivalent to the infringed item," U.S.S.G. cmt. n.2(A)(i)(I)**

Differences in appearance and quality therefore matter if they could be ascertained by "a reasonably informed purchaser." An infringing item that could fool only an uninformed purchaser would be valued at the counterfeit retail value.

- **The infringing item is a digital or electronic reproduction,** *id.* **cmt. n.2(A)(i)(II)**

For digital or electronic reproductions, use the retail value of an authentic item regardless of whether they appear authentic to a reasonably informed purchaser or not. A counterfeit movie DVD with an obviously counterfeit label would be valued at the authentic item's retail value, even though nobody would be confused into mistaking the counterfeit for an authentic DVD. The Commission's theory is likely that a digital or electronic reproduction is a perfect substitute for the real thing, whether its outer trappings look legitimate or not. The guideline does not distinguish between types of digital reproduction, such as when the digital or electronic reproduction is not a perfect substitute because its quality was degraded, as with a camcorded movie or a musical song that has been reproduced at a lower sampling rate than CD quality.

- **The counterfeit was sold at 75% or more of the authentic item's retail price,** *id.* **cmt. n.2(A)(ii)**

Again, the Commission likely reasoned that counterfeits sold at less than 75% of the authentic item's retail price are unlikely to fool consumers, or that consumers who would pay less than 75% of the authentic retail price would be unlikely to pay full price even if given the chance to do so.

- **The counterfeit's retail value "is difficult or impossible to determine without unduly complicating or prolonging the sentencing proceeding,"** *id.* **cmt. n.2(A)(iii)**

As is discussed in Section VIII.C.1.c.iv. of this Chapter, reasonable estimates of the counterfeit and authentic retail prices are acceptable, but speculative guesses or overly time-consuming calculations are not.

- **The offense involved illegal interception of satellite cable signals in violation of 18 U.S.C. § 2511, where "the 'retail value of the infringed item' is the price the user of the transmission would have paid to lawfully receive that transmission, and the 'infringed item' is the satellite transmission rather than the intercepting device,"** *id.* **cmt. n.2(A)(iv)**

Presumably this rule would also apply to the illegal interception of cable and satellite service under statutes other than 18 U.S.C. § 2511, such as 47 U.S.C. §§ 553(b)(2), 605 and 17 U.S.C. § 1204.

- **The retail value of the authentic good is a better approximation of the harm than the value of the counterfeit,** *id.* **cmt. n.2(A)(v); or**
- **"The offense involves the display, performance, publication, reproduction, or distribution of a work being prepared for commercial distribution. In a case involving such an offense, the 'retail value of the infringed [authentic] item' is the value of that item upon its initial commercial distribution,"** *id.* **cmt. n.2(A)(vi)**

This is part of the Sentencing Commission's solution to the so-called "pre-release problem"—that is, how to value an infringing copyrighted work whose infringement occurred before the rights-holder put the authentic work on the market itself. Confronted with widely diverging estimates of the harm caused by pre-release piracy, the Commission determined that a pre-release work's retail value should equal its anticipated legitimate retail value, but that a 2-point upward adjustment should be added for all pre-release offenses. *See* U.S.S.G. § 2B5.3(b)(2). See also Section VIII.C.1.d. of this Chapter. Both these provisions were added on October 24, 2005. U.S.S.G. App. C (Amendment 675).

If any one of the above situations applies, the retail value is that of the infringed (legitimate) item.

If none of these situations apply, the retail value is that of the (infringing) counterfeit item. *See* U.S.S.G. § 2B5.3 cmt. n.2(B) & backg'd; *id.* App. C (Amendment 593). This includes cases involving the unlawful recording of a musical performance in violation of 18 U.S.C. § 2319A. U.S.S.G. § 2B5.3 cmt. n.2(B).

VIII.C.1.c.iv. Determining Amounts and Values—Reasonable Estimates Allowed

How to determine the infringing or infringed item's retail value? Any relevant source of information is appropriate. Actual prices are preferable, such as prices determined from the defendant's price list, prices charged during undercover buys, or actual retail prices for specific items in the legitimate manufacturer's catalogue. Approximations may be necessary, however, and they may include estimations of the average counterfeit prices in the market or region as determined by experts, or the average retail price for a product line in the manufacturer's catalogue.

The same rule goes for determining the number of infringing items: actual counts are preferable, but approximations are appropriate.

The courts allowed approximations of the infringement amount even before the guidelines did so explicitly. *See United States v. Foote*, 413 F.3d 1240, 1251 (10th Cir. 2005) (allowing analysis of defendant's bank records to aid in determining infringement amount); *United States v. Slater*, 348 F.3d 666, 670 (7th Cir. 2003) (confirming that district courts have "considerable leeway in assessing the retail value of the infringing items" and that courts "need only make a reasonable estimate of the loss, given the available information," citing the former U.S.S.G. § 2F1.1, now replaced by § 2B1.1); *United States v. Kim*, 963 F.2d 65, 69-70 (5th Cir. 1992) (analogizing to fraud guideline for principle that reasonable estimates are acceptable).

Now, however, U.S.S.G. § 2B5.3 explicitly states that reasonable estimates are acceptable. On October 24, 2005, Application Note 2(E) to U.S.S.G. § 2B5.3 clarified as follows:

> (E) Indeterminate Number of Infringing Items.—In a case in which the court cannot determine the number of infringing items, the court need only make a reasonable estimate of the infringement amount using any relevant information, including financial records.

See U.S.S.G. App. C (Amendment 675). The reference to financial records is likely an incorporation of the holding in *Foote*.

Although statistical precision is preferable, it is not necessary. For example, in a case that turned on whether the 3,947 infringing pieces of computer software on a server were functioning or nonfunctioning, the FBI tested 71 programs and found that 94% were functioning. *United States v. Rothberg*, No. 00 CR 85, 2002 WL 171963, at *4 (N.D. Ill. Feb. 4, 2002), *aff'd on other grounds*, 348 F.3d 666 (7th Cir. 2003). To calculate the total number of functioning programs, the court multiplied the percentage from the sample (94%) by the total number of programs (3,947). *Id.* The court acknowledged that "the selection of the 71 programs was not random," but found that the selection was nevertheless "a reasonable basis for determining an estimate." *Id.*

Whatever estimates the parties offer, however, the parties must explain how their estimate was calculated and why. In *Rothberg*, *supra*, the government first estimated the number of functioning programs based on a mathematical function it claimed derived from "information regarding [data] transmission error rates [the government] obtained from companies that maintain telephone lines." *Id.* at *3. The court rejected this estimate because the government had not explained how it "had derived the calculation or why it should be considered a reasonable basis for estimating the number of functioning programs." *Id.*

Although U.S.S.G. § 2B5.3 speaks only of estimating the number of infringing items, there is no reason to believe that it abrogates earlier law allowing the estimation of retail values. *E.g.*, *Slater*, *supra*; *United States v. Foote*, No. C.R.A. 00-20091-01-KHV, 2003 WL 22466158, at *6 (D. Kan. July 31, 2003) (estimating infringement amount from trademark counterfeiting by subtracting legitimate income from bank deposits, and further discounting by the percentage of sales attributable to non-infringing items), *aff'd*, 413 F.3d 1240, 1251-52 (10th Cir. 2005).

VIII.C.1.c.v. Cross-Reference to Loss Table in U.S.S.G. § 2B1.1

Once calculated, the infringement amount sets the scope of the enhancement in U.S.S.G. § 2B5.3(b)(1):

- An infringement amount below or up to $2,000 results in no increase;
- An infringement amount above $2,000 and up to $5,000 results in a 1-level increase; and
- An infringement amount above $5,000 increases the offense level according to the loss table in U.S.S.G. § 2B1.1(b)(1) (Theft,

Embezzlement, Receipt of Stolen Property, Property Destruction, and Offenses Involving Fraud or Deceit).

When consulting U.S.S.G. § 2B1.1, look only to the loss table in subsection (b)(1); other portions of that guideline—including the base offense level, other offense enhancements, and the commentary—are inapplicable. *See* U.S.S.G. § 1B1.5(b)(2). Moreover, U.S.S.G. § 2B5.3(b)(1)'s citation to the loss table in U.S.S.G. § 2B1.1 does not mean that the infringement amount should equal the victim's loss. Rather, the infringement amount approximates the victim's loss, but need not equal it. *See U.S. v. Cho*, 136 F.3d 982 (5th Cir. 1998); *see also* U.S.S.G. App. C (Amendments 590, 593) (discussing infringement amount as similar to loss and an approximation of harm). On this technical point, *United States v. Sung*, 51 F.3d 92, 95 (7th Cir. 1995) is technically incorrect when it confuses the infringement amount with the loss incurred. Although the infringement amount is often characterized as describing the "loss" to the victim, it is not necessary for the government to show that the copyright owner suffered any actual pecuniary loss. *See U.S. v. Powell*, 139 Fed. Appx. 545 (4th Cir. July 19, 2005) (applying 2003 Guidelines, finding enhancement under § 2B1.1 table based on infringement amount of more than $250,000 was proper even though the victim suffered no pecuniary loss; sentence vacated and remanded on other grounds) (unpublished opinion).

VIII.C.1.d. Pre-release Piracy Increases the Offense Level by 2—U.S.S.G. § 2B5.3(b)(2)

Distribution of a copyrighted item before it is legally available to the consumer is more serious than the distribution of already available items. U.S.S.G. App. C (Amendment 675). Consequently, effective October 24, 2005, the Sentencing Commission added a 2-level enhancement for offenses that involve the display, performance, publication, reproduction, or distribution of a work being prepared for commercial distribution. *See* U.S.S.G. § 2B5.3(b)(2). A "work being prepared for commercial distribution" has the meaning given in 17 U.S.C.§ 506(a)(3). U.S.S.G. § 2B5.3 cmt. n.1. See also Chapter II of this Manual.

The 2-level increase for pre-release piracy applies not only to the online pre-release offense set forth in 17 U.S.C. § 506(a)(1)(C) (which by definition involves pre-release piracy over publicly-accessible computer networks), but also to any copyright crimes under § 506(a)(1)(A) or (B) that involve pre-release piracy done through any other medium, such as a § 506(a)(1)(A) conviction for selling pirated pre-release movie DVDs.

VIII.C.1.e. Manufacturing, Importing, or Uploading Infringing Items Increases the Offense Level by 2—U.S.S.G. § 2B5.3(b)(3) [before October 24, 2005: § 2B5.3(b)(2)]

The offense level is increased by 2 levels if the offense involves the "manufacture, importation, or uploading of infringing items." U.S.S.G. § 2B5.3(b)(3). (Before the October 24, 2005 amendments, this provision was numbered § 2B5.3(b)(2). *See* U.S.S.G. App. C (Amendment 675).) If, after applying § 2B5.3(a), (b)(1), (b)(2), and the 2-level increase in (b)(3), the offense level is less than 12, then it must be increased to 12. U.S.S.G. § 2B5.3(b)(3).

This upward adjustment reflects the need to punish those who introduce infringing goods into the stream of commerce. U.S.S.G. App. C (Amendments 590, 593).

Uploading is particularly troublesome because it not only introduces infringing items into the stream of commerce, but also enables further infringement of the works. U.S.S.G. App. C (Amendments 590, 593). "'Uploading' means making an infringing item available on the Internet or a similar electronic bulletin board with the intent to enable other persons to (A) download or otherwise copy the infringing item; or (B) have access to the infringing item, including by storing the infringing item in an openly shared file." U.S.S.G. § 2B5.3 cmt. n.1 (Oct. 24, 2005). Uploading does not include merely downloading or installing an infringing item on a hard drive on a defendant's personal computer, unless the defendant places the infringing item in an openly shared file. *Id.* (Before the October 24, 2005 amendments, "uploading" was defined in § 2B5.3's first and third application notes. The 2005 amendments consolidated the definition into the first application note and clarified the circumstances in which loading a file onto a computer hard drive constitutes uploading. The amendment made no substantive change, however. *See* U.S.S.G. App. C (Amendment 675).)

Manufacturing and importing infringing items are also singled out for a 2-level increase because those actions introduce infringing items into the stream of commerce. U.S.S.G. § 2B5.3 App. C (Amendments 590, 593).

Although the guidelines do not define "manufacturing," the important distinction is between manufacturing (which gets the 2-level increase) and mere distribution and trafficking (which do not unless they involved importation or uploading). In the case of counterfeit trademarked goods, manufacturing should include not only producing the item, but also

applying a counterfeit label to it, since an item does not become counterfeit until a counterfeit label is used in conjunction with it.

Manufacturing should encompass not only the production of counterfeit trademarked hard goods, but also the performance of counterfeit service-marked services and the production and reproduction of pirated copyrighted works under 17 U.S.C. § 506; counterfeit labels under 18 U.S.C. § 2318; bootleg music recordings under 17 U.S.C. § 2319A; camcorded movies under 18 U.S.C. § 2319B; and illegal circumvention devices under 17 U.S.C. § 1204.

If a defendant conspired with or aided and abetted another person who manufactured, uploaded, or imported infringing items, the defendant can qualify for this 2-level increase even if he did none of these things himself. The increase is triggered by whether the *offense* involved manufacturing, importation, or uploading, not whether the *defendant* performed these tasks. *See* U.S.S.G. § 2B5.3(b)(3) ("If the *offense* involved the manufacture, importation, or uploading ...") (emphasis added); U.S.S.G. § Ch. 2 (Introductory Commentary) ("Chapter Two pertains to offense conduct.").

VIII.C.1.f. Offense Not Committed for Commercial Advantage or Private Financial Gain Reduces the Offense Level by 2—U.S.S.G. § 2B5.3(b)(4) [before October 24, 2005: § 2B5.3(b)(3)]

The fourth offense characteristic, located in guideline § 2B5.3(b)(4), decreases the offense level by 2 levels if the offense was not committed for commercial advantage or private financial gain, but the resulting offense level cannot be less than 8. (This characteristic was renumbered from § 2B5.3(b)(3) to 2B5.3(b)(4) in the October 24, 2005 amendments. *See* U.S.S.G. App. C (Amendments 590, 593, 675).)

The defendant bears the burden of proving that he is entitled to this offense characteristic, because it is structured as a decrease rather than an increase. *See generally United States v. Ameline*, 409 F.3d 1073, 1086 (9th Cir. 2005) (en banc); *United States v. Dinges*, 917 F.2d 1133, 1135 (8th Cir. 1990); *United States v. Kirk*, 894 F.2d 1162, 1164 (10th Cir. 1990); *United States v. Urrego-Linares*, 879 F.2d 1234, 1238-39 (4th Cir. 1989).

For a complete discussion of what qualifies as conduct done for the purposes of commercial advantage or private financial gain, see Section II.B.4. of this Manual (copyright). The interpretation of commercial advantage and private financial gain in copyright cases applies equally to U.S.S.G. § 2B5.3 for any type of intellectual property crime because the

statutory and guidelines definitions are nearly identical. *Compare* U.S.S.G. § 2B5.3 cmt. n.1 (defining terms) *with* 17 U.S.C. § 101 (same).

VIII.C.1.g. Offense Involving Risk of Serious Bodily Injury or Possession of a Dangerous Weapon Increases the Offense Level by 2—U.S.S.G. § 2B5.3(b)(5) [before October 24, 2005: § 2B5.3(b)(4)]

If the offense involved conscious or reckless risk of serious bodily injury or possession of a dangerous weapon, the offense level is increased by 2. U.S.S.G. § 2B5.3(b)(5). If the resulting offense level is less than 13, then it must be increased to level 13. *See, e.g., United States v. Maloney*, 85 Fed. Appx. 252 (2d Cir. 2004) (applying 2-level enhancement for possession of a dangerous weapon in connection with conviction under 18 U.S.C. § 2318(a),(c)(3) and § 2, even though defendant was acquitted at trial of a felon-in-possession of a firearm charge).

This enhancement was partially motivated by the health and safety risks from counterfeit consumer products such as counterfeit batteries, airplane parts, and pharmaceuticals. *See* U.S.S.G. App. C (Amendments 590, 593). The October 24, 2005 amendments renumbered this enhancement from U.S.S.G. § 2B5.3(b)(4) to § 2B5.3(b)(5). *Id.* (Amendment 675).

VIII.C.1.h. Decryption or Circumvention of Access Controls Increases the Offense Level—U.S.S.G. § 3B1.3

The 2-level enhancement for use of a special skill under U.S.S.G. § 3B1.3 "*shall* apply" if the defendant decrypted or circumvented access controls. U.S.S.G. § 2B5.3 cmt. n.3 (emphasis added) (formerly n.4, before the Oct. 24, 2005 amendments, *see* U.S.S.G. App. C (Amendment 675)).

Because the note quoted above refers only to the circumvention of access controls, it is unclear whether the special skill enhancement must also apply to decrypting or circumventing copy controls. There is no policy-related reason to treat access and copy controls differently at sentencing. In fact, U.S.S.G. § 3B1.3 applies to any defendant who commits an intellectual property crime while using a special skill. See Section VIII.C.2.i. of this Chapter for a more detailed description of what constitutes a special skill.

This enhancement may not be assessed for use of a special skill if the adjustment under U.S.S.G. § 3B1.1 (Aggravating Role) is also assessed. *See* U.S.S.G. § 3B1.3.

VIII.C.1.i. Upward Adjustment for Harm to Copyright or Mark-Owner's Reputation, Connection with Organized Crime, or Other Unspecified Grounds

The fourth application note for § 2B5.3 (formerly application note 5, before the October 24, 2005 amendments) states that an upward departure may be warranted if the offense level determined under § 2B5.3 "substantially understates the seriousness of the offense," such as when the offense substantially harmed the victim's reputation in a way that is otherwise unaccounted for, including in calculating the infringement amount, and when the offense was in connection with or in furtherance of a national or international organized criminal enterprise. U.S.S.G. § 2B5.3 cmt. n.4; *id.* App. C (Amendments 590, 593).These two examples are not, however, exclusive.

VIII.C.1.j. Vulnerable Victims—U.S.S.G. § 3A1.1(b)

Intellectual property crime defendants are likely to qualify for an upward adjustment under U.S.S.G. § 3A1.1(b) if they knew or should have known that they were selling counterfeit products to vulnerable victims. A prime example of this would be selling counterfeit pharmaceuticals that are distributed or redistributed to sick patients. *See United States v. Milstein*, 401 F.3d 53, 74 (2d Cir. 2005) (affirming vulnerable victim adjustment for distributing counterfeit and misbranded drugs "to doctors, pharmacists, and pharmaceutical wholesalers, knowing that those customers would distribute the drugs to women with fertility problems and to Parkinson's disease patients").

VIII.C.1.k. No Downward Departure for the Victim's Participation in Prosecution

The court may not depart downward on the ground that the victim participated in the prosecution. In *United States v. Yang*, 281 F.3d 534 (6th Cir. 2002), *cert. denied*, 537 U.S. 1170 (2003), *on appeal after new sentencing hearing*, 144 Fed. Appx. 521 (6th Cir. 2005), a prosecution for theft of trade secret, mail fraud, wire fraud, and money laundering, the trial court departed downward 14 levels on the ground that the victim participated too much in the prosecution, specifically in calculating the loss it suffered. The 6th Circuit reversed, concluding that "the victim's participation in the prosecution is wholly irrelevant to either the defendant's guilt or the nature or extent of his sentence," and is therefore not a permissible basis for a downward departure. *Yang*, 281 F.3d at 545, 546.

VIII.C.2. Offenses Involving the Economic Espionage Act

VIII.C.2.a. Applicable Guideline is § 2B1.1, Except for Attempts and Conspiracies

Unlike most other intellectual property offenses, which are sentenced under U.S.S.G. § 2B5.3, completed EEA offenses (both § 1831 and § 1832) are sentenced under U.S.S.G. § 2B1.1. *See* U.S.S.G. App. A. The choice of U.S.S.G. § 2B1.1 instead of U.S.S.G. § 2B5.3 likely reflects the idea that EEA offenses are primarily about stolen property rather than infringement. The superficial difference between stealing and infringement is that one physically dispossesses the victim of his property and the latter does not. However, the EEA punishes those who steal trade secrets without dispossessing the victim of his trade secret, and even after a trade secret is physically stolen, the victim may still use the information itself. The overlap between misappropriation and infringement therefore makes U.S.S.G. § 2B1.1 an interesting fit for the EEA.

An EEA attempt or conspiracy is sentenced under U.S.S.G. § 2X1.1 (Conspiracies, Attempts, and Solicitations), which uses the offense level calculated under U.S.S.G. § 2B1.1 and decreases the base offense level 3 levels "unless the defendant completed all the acts the defendant believed necessary for successful completion of the substantive offense or the circumstances demonstrate that the defendant was about to complete all such acts but for apprehension or interruption by some similar event beyond the defendant's control." U.S.S.G. § 2X1.1(b)(1),(2). The 3-point reduction will rarely apply in EEA attempt cases resulting from undercover stings because in those operations the defendant has generally completed all necessary acts short of the actual receipt of what the defendant believed was a trade secret.

VIII.C.2.b. Base Offense Level—U.S.S.G. § 2B1.1(a)

The base offense level for a completed EEA crime is 6. U.S.S.G. § 2B1.1(a)(2).

VIII.C.2.c. Loss—U.S.S.G. § 2B1.1(b)(1)

The defendant's sentence is driven largely by the value of the misappropriated property. Under U.S.S.G. § 2B1.1(b)(1), the offense level increases according to the amount of the loss.

VIII.C.2.c.i. Use Greater of Actual or Intended Loss

This loss figure is "the greater of actual loss or intended loss." U.S.S.G. § 2B1.1 cmt. n.3(A). "Actual loss" is "the reasonably foreseeable pecuniary harm that resulted from the offense," whereas "intended loss (I) means the pecuniary harm that was intended to result from the offense; and (II) includes intended pecuniary harm that would have been impossible or unlikely to occur (e.g., as in a government sting operation, or an insurance fraud in which the claim exceeded the insured value)." *Id.* cmt. n.3(A)(i-ii).

VIII.C.2.c.ii. Reasonable Estimates Acceptable

Whatever method is chosen to calculate loss, the government's calculation need not be absolutely certain or precise. "The court need only make a reasonable estimate of the loss." U.S.S.G. § 2B1.1 cmt. n.3(C).

VIII.C.2.c.iii. Methods of Calculating Loss

Guideline § 2B1.1's application notes outline a number of general methods for calculating the loss, many of which are included as methods to estimate the loss:

- "[T]he reasonably foreseeable pecuniary harm that resulted from the offense," U.S.S.G. § 2B1.1 cmt. n.3(A)(i)
- "The fair market value of the property unlawfully taken or destroyed or, if the fair market value is impractible to determine or inadequately measures the harm, the cost to the victim of replacing that property," n.3(C)(i)
- "The cost of repairs to damaged property," n.3(C)(ii)
- "The approximate number of victims multiplied by the average loss to each victim," n.3(C)(iii)
- "The reduction that resulted from the offense in the value of equity securities or other corporate assets," n.3(C)(iv)
- "More general factors, such as the scope and duration of the offense and revenues generated by similar operations," n.3(C)(v)
- "[T]he gain that resulted from the offense as an alternative measure of loss[,] only if there is a loss but it reasonably cannot be determined," n.3(B)

In a trade secrets case, calculating the loss can be complicated. First, consider the situations under which the defendant can be convicted: (a) merely conspiring to misappropriate a trade secret that the victim has not fully exploited to create a product; (b) receiving a trade secret, but not using the trade secret; (c) stealing a trade secret at no cost; (d) stealing a trade secret for an agreed-upon bribe; (e) receiving a trade secret and using it to create a product that has not been completed; (f) receiving a trade secret, using it to create a product, introducing the product, but not yet selling it; (g) receiving a trade secret, using it to create a product, and selling the product at a loss; (h) receiving the trade secret, using it, and selling the product at a profit, while the victim continues to profit from its own sales; and (i) receiving the trade secret, using it, and selling a product that displaces the victim's sales. These situations do not exhaust the possibilities. They illustrate, however, several complicating factors:

- whether the defendant paid anything for the secret
- whether the defendant was paid anything for the secret
- whether the defendant used the secret
- whether the defendant used the secret and made money from its use and
- whether the victim's sales decreased, increased, or increased at a lower rate than they would have had the misappropriation not occurred

The final complicating factor is that trade secrets are, by definition, not traded in an open market that allows the easy calculation of a trade secret's price or value.

The variety of misappropriation scenarios, the variety of evidence available, and the broad principles of valuing trade secrets in criminal and civil law lead to one clear recommendation: prosecutors, agents, and courts should consider the variety of methods by which a trade secret can be valued, develop whatever evidence is reasonably available, and then be pragmatic about choosing which method to use, as long as it is equitable, appropriately punitive, and supported by the evidence. The cases bear this out.

- **Criminal Cases**

Few reported federal criminal decisions describe how to value trade secrets, but those that do tend to focus on the trade secret's research and development costs. In *United States v. Wilson*, 900 F.2d 1350 (9th Cir. 1990), a mail fraud case, a research associate offered to sell financial and research

data from his employer, a biotechnology and pharmaceutical firm, to a competitor. The defendant argued that the documents were worth their fair market value: the $100,000 to $200,000 that the competitor said it would have paid for them—the competitor worked with law enforcement to set up a sting—or the $200,000 that the defendant had said that he would sell them for. *Id.* at 1356. The Ninth Circuit, however, noted its "refus[al] to require a strict market value approach in determining the value of stolen goods," because that approach "measures only the gain to the defendant while virtually ignoring the harm suffered by the victim." *Id.* (citations omitted). Although the court acknowledged that the buyer's and seller's prices were relevant, it held that the trial court was entitled to value the documents at the victim's research and development costs for the information contained in the documents, especially because those costs indicate the intended loss to the victim. *Id.* Those costs totaled $4 million, although the trial court generously reduced the total by 75 percent, to $1 million, to give the defendant the benefit of every doubt. *Id.* at 1355.

Similarly, in *United States v. Ameri*, 412 F.3d 893, 900 (8th Cir. 2005), an employee stole his employer's proprietary software, which the evidence showed was at the heart of a $10 million contract, had no verifiable fair market value because it was not available separately, alternatively had a fair market value of $1 million per copy, and was developed for about $700,000. Faced with these figures, the Eighth Circuit affirmed the trial court's loss estimate of $1.4 million, which appears to be the $700,000 in development costs times 2, the number of copies the defendant made. *Id.* at 900-01.

Finally, *United States v. Kwan*, No. 02 CR. 241(DAB), 2003 WL 22973515 (S.D.N.Y. Dec. 17, 2003), considered whether "proprietary hotel contact lists, hotel rate sheets, travel consortium contact lists, travel consortium rate sheets, and cruise operator rate sheets"—all useful in the travel industry—met the jurisdictional threshold for interstate transportation of stolen property under 18 U.S.C. § 2314 by being worth more than $5,000. *Id.* at *1. The court found most persuasive an argument for a value over $5,000 based on the documents' cost of production, which it estimated by noting the salary of people who created the documents and the amount of time they would have spent gathering the information and creating the documents. *Id.* at *9 & n.12. In all these cases, the loss or market value was defined largely by development costs.

Some civil trade secret cases have measured the replacement cost using the victim's research and development costs. *See Salsbury Labs., Inc. v. Merieux Labs., Inc.*, 908 F.2d 706, 714-15 (11th Cir. 1990) (holding that research and development costs for misappropriated vaccine were a proper

factor to determine damages); *cf. University Computing Co. v. Lykes-Youngstown Corp.*, 504 F.2d 518, 538 (5th Cir. 1974) (holding that development costs should be taken into consideration with a number of factors, including "the commercial context in which the misappropriation occurred"). *But see Softel, Inc. v. Dragon Med. & Scientific Communications, Inc.*, 118 F.3d 955, 969 (2d Cir. 1997) (holding that it is usually appropriate to measure damages based on development costs and importance of secret to plaintiff only after a defendant completely destroys the value of the trade secret).

An interesting exception to using development costs to value trade secrets is *United States v. Pemberton*, 904 F.2d 515 (9th Cir. 1990), in which a legitimate buyer's price was selected. After the defendant was convicted for receiving stolen property, namely technical landscape and irrigation design drawings for a 450-acre commercial development, the trial court had to select among valuation methods, including valuing the drawings at what the drawings were purportedly worth to defendant—zero; the $1,200 cost of the materials on which they were drawn; the $65,000 cost of replacing the drawings in full; and the $118,400 contract price for the drawings (80 percent of the full contract price, given that the drawings were 80 percent complete when stolen). *Id.* at 516 & n.1, 517. Without a price from an open market, since the drawings were unique, the appellate court affirmed the trial court's choice of the $118,400 contract price.

Why use the buyer's price in *Pemberton* rather than the development costs, as had been done in the *Wilson*, *Ameri*, and *Kwan* cases? There appear to be three differences. First, in *Pemberton* the buyer's price came from a legitimate market transaction rather than a black-market transaction that would have undervalued the property. Second, in *Pemberton*, the buyer's price was apparently higher than the development costs. Third, and this is related to the second point, in *Pemberton* the drawings that were stolen likely could have been used for one project only, the real estate development by the legitimate buyer, whereas the trade secrets in *Wilson*, *Ameri*, and *Kwan* included general information that could have been used over and over again by illegitimate buyers. Research and development costs for a one-off project are likely to be less than the legitimate buyer's price (since this is the only opportunity the trade-secret holder can recover his overhead), whereas research and development costs for a replicable product or service will likely exceed a legitimate buyer's price (since the trade-secret holder can recover his overhead through repeated sales). It may also be that the criminal cases are largely consistent with civil cases' tendency when there is evidence for more than one measure to "award that amount which is most beneficial to the injured party." 1 Richard Raysman & Peter Brown, *Computer Law: Drafting and Negotiating Forms* § 6.03A (2005).

- **Civil Cases**

Prosecutors should also be aware of how civil cases measure losses from trade secret misappropriation. *See supra*; *cf. United States v. Olis*, 429 F.3d 540, 546 (5th Cir. 2005) (holding that "[t]he loss guideline [in U.S.S.G. § 2B1.1] is skeletal because it covers dozens of federal property crimes," and therefore "[t]he civil damage measure [for securities fraud] should be the backdrop for criminal responsibility both because it furnishes the standard of compensable injury for securities fraud victims and because it is attuned to stock market complexities").

Unfortunately, beyond reinforcing the criminal cases' use of research and development costs, civil measures of damages provide little hard and fast guidance. The Uniform Trade Secrets Act echoes the Sentencing Guidelines' generalities:

> Damages can include both the actual loss caused by misappropriation and the unjust enrichment caused by misappropriation that is not taken into account in computing actual loss. In lieu of damages measured by any other methods, the damages caused by misappropriation may be measured by imposition of liability for a reasonable royalty for a misappropriator's unauthorized disclosure or use of a trade secret.

Uniform Trade Secrets Act § 3(a) (1985). In determining damages under the Uniform Trade Secrets Act, courts base the trade secret's market value on the victim's loss or the defendant's gain, depending on which measure appears to be more reliable or greater given the particular circumstances of the theft. *See University Computing Co. v. Lykes-Youngstown Corp.*, 504 F.2d 518 (5th Cir. 1974); *Vermont Microsystems, Inc. v. Autodesk Inc.*, 138 F.3d 449, 452 (2d Cir. 1998). With such broad principles, "the general law as to the proper measure of damages in a trade secrets case is far from uniform." *Telex Corp. v. International Bus. Machs. Corp.*, 510 F.2d 894, 930 (10th Cir. 1975) (concerning misappropriation of trade secrets and confidential information relating to electronic data processing systems).

As might be expected, civil cases use a variety of methods to value trade secrets:

- the value placed on the trade secrets by the parties
- the victim's lost profits
- the defendant's realized profits
- the defendant's saved costs from misappropriation

- a reasonable royalty to the victim, when there was otherwise no gain or loss

1 Richard Raysman & Peter Brown, *Computer Law: Drafting and Negotiating Forms* § 6.03A (2005). When there is evidence for more than one measure, "the court will frequently award that amount which is most beneficial to the injured party." *Id.*

Civil cases often note that if the victim's loss were the only appropriate measure of damages, someone caught red-handed stealing trade secrets could not be punished if he had not yet used the information to the owner's detriment. As a result, in such circumstances most Uniform Trade Secrets Act cases have computed the trade secret's market value by focusing on the defendant's gain. *See, e.g., University Computing*, 504 F.2d at 536 (holding that damages for misappropriation of trade secrets are measured by the value of the secret to the defendant "where the trade secret has not been destroyed and where the plaintiff is unable to prove specific injury"); *Salisbury Labs., Inc. v. Merieux Labs., Inc.*, 908 F.2d 706, 714 (11th Cir. 1990) (ruling that under Georgia's UTSA, damages for misappropriation of trade secrets should be based on the defendant's gain). Under the more recent Federal Sentencing Guidelines, the court may use a defendant's gain as a loss for the victim in certain circumstances. *See* U.S.S.G. § 2B1.1 cmt. n.3(B) (2004).

A number of civil cases determine trade secrets' market value by calculating a "reasonable royalty," that is, the amount the thief would have had to pay the victim in licensing or royalty fees had he legitimately licensed the stolen technology. *See, e.g., University Computing*, 504 F.2d at 537. When the defendant has not yet realized sufficient profit to readily indicate the stolen information's market value, the preferred estimate is the "reasonable royalty" (or "forced licensing") measure. *See* Uniform Trade Secrets Act § 3(a) (1985) ("In lieu of damages measured by any other methods, the damages caused by misappropriation may be measured by imposition of liability for a reasonable royalty for a misappropriator's unauthorized disclosure or use of a trade secret."); *Vitro Corp. v. Hall Chem. Co.*, 292 F.2d 678, 683 (6th Cir. 1961); *see also Vermont Microsystems, Inc. v. Autodesk, Inc.*, 138 F.3d 449, 450 (2d Cir. 1998). Other federal cases using the "reasonable royalty" method include *Molex, Inc. v. Nolen*, 759 F.2d 474 (5th Cir. 1985); *University Computing Co.*, 504 F.2d 518; *Linkco, Inc. v. Fujitsu Ltd.*, 232 F. Supp. 2d 182, 186-87 (S.D.N.Y. 2002) (holding that a "reasonable royalty is the best measure of damages in a case where the alleged thief made no profits"); *Carter Prods., Inc. v. Colgate-Palmolive Co.*, 214 F. Supp. 383 (D. Md. 1963).

But calculating a reasonable royalty may prove more difficult and may unduly prolong or complicate sentencing in cases where the defendant has not yet manifested his intention to use the stolen technology and there is no readily ascertainable benchmark for determining a reasonable royalty.

- **Practical Guidance on Gathering Evidence**

Because of the flexible nature of valuing trade secrets, prosecutors and investigators should try to obtain the following types of evidence, if available and applicable:

- the amount the defendant paid for the trade secret
- the amount for which the defendant sold or tried to sell the trade secret
- the amount for which similar trade secret information sold in the legitimate open market
- a reasonable royalty, based on what a willing buyer would pay a willing seller for the technology in an arms-length transaction
- the trade secret owner's research and development costs; and
- the market price that the defendant actually received or paid in exchange for the technology

VIII.C.2.d. Intent to Benefit a Foreign Government, Instrumentality, or Agent—U.S.S.G. § 2B1.1(b)(5)

The offense level is increased two points if the defendant knew or intended the offense to benefit a foreign government, foreign instrumentality, or foreign agent. *See* U.S.S.G. § 2B1.1(b)(5).

VIII.C.2.e. Sophisticated Means—U.S.S.G. § 2B1.1(b)(9)(C)

If the offense involved "sophisticated means," the offense level is increased by 2 levels, and if the resulting offense is less than 12, it must be increased to 12. U.S.S.G. § 2B1(b)(9)(C). "'[S]ophisticated means' means especially complex or especially intricate offense conduct pertaining to the execution or concealment of an offense," which includes "hiding assets or transactions," among other things. *Id.* cmt. n.8(B).

The sophisticated means enhancement will often apply to trade secret offenses, because these crimes are often committed by corporate insiders who have the need and opportunity to take extensive precautions to shield their actions from their employers. A defendant can receive the adjustment for sophisticated means in addition to the adjustment for use of a special

skill under U.S.S.G. § 3B1.3. *See United States v. Rice*, 52 F.3d 843, 851 (10th Cir. 1995) ("The purpose of the special skill enhancement is to punish those criminals who use their special talents to commit crime. In contrast, the sophisticated means and more than minimal planning enhancements [in predecessor guideline to § 2B1.1] are designed to target criminals who engage in complicated criminal activity because their actions are considered more blameworthy and deserving of greater punishment than a perpetrator of a simple version of the crime. We therefore see no double counting here."); *United States v. Olis*, 429 F.3d 540, 549 (5th Cir. 2005); *United States v. Minneman*, 143 F.3d 274, 283 (7th Cir. 1998).

VIII.C.2.f. Upward Departure Considerations—U.S.S.G. § 2B1.1 cmt. n.19(A)

A non-exhaustive list of factors in which an upward departure should be considered is set forth in Application Note 19 to U.S.S.G. § 2B1.1. The factors that are most likely to be relevant in a trade secret case are intending, risking, and causing non-monetary harm, such as emotional harm, because many EEA cases involve disgruntled employees or former employees out for revenge. U.S.S.G. § 2B1.1 cmt. n.19(i),(ii).

VIII.C.2.g. Downward Departure Considerations—U.S.S.G. § 2B1.1 cmt. n.19(C)

Application Note 19(C) to U.S.S.G. § 2B1.1 suggests that a downward departure may be warranted if the offense level "substantially overstates the seriousness of the offense." EEA defendants are likely to raise this as a basis for downward departure if the loss amount greatly outweighs the amount of the actual or intended gain or loss, as sometimes happens when the trade secret is valued by research and development costs.

VIII.C.2.h. Abuse of a Position of Trust—U.S.S.G. § 3B1.3

Trade secret offenses committed by corporate insiders often deserve the 2-level adjustment for abuse of a position of trust under U.S.S.G. § 3B1.3. The adjustment is appropriate when the defendant had "professional or managerial discretion (i.e., substantial discretionary judgment that is ordinarily given considerable deference)" and the position of trust "contributed in some significant way to facilitating the commission or concealment of the offense." *Id.* cmt. n.1. A defendant can receive the enhancements for abuse of a position of trust and sophisticated means simultaneously. *Cf. United States v. Straus*, 188 F.3d 520, 1999 WL 565502, at *5 (10th Cir. 1999) (table) (holding that abuse-of-trust and more-than-

minimal-planning enhancements, the latter in a predecessor to U.S.S.G. § 2B1.1(b)(9)(C), can be applied to same conduct simultaneously).

VIII.C.2.i. Use of Special Skill—U.S.S.G. § 3B1.3

Trade secret defendants who use their specialized technical knowledge to understand and use the misappropriated trade secret will often qualify for an adjustment for use of a special skill under U.S.S.G. § 3B1.3. *See, e.g.*, *United States v. Lange*, 312 F.3d 263, 270 (7th Cir. 2002).

"'Special skill' refers to a skill not possessed by members of the general public and usually requiring substantial education, training, or licensing. Examples would include pilots, lawyers, doctors, accountants, chemists, and demolition experts." U.S.S.G. § 3B1.3 cmt. n.4. Special skill includes any type of special skill, not just one gained through advanced education. In *Lange*, it applied to a mechanical drafter, an EEA defendant who committed his offense using his associate's degree in graphic design and his ability to work with his former employer's engineering drawings in AutoCAD. *Lange*, 312 F.3d at 270.

A defendant can receive the adjustment for use of a special skill in addition to the adjustment for sophisticated means under U.S.S.G. § 2B1.1(b)(9)(C).

VIII.C.2.j. No Downward Departure for Victim's Participation in Developing the Case

As noted in Section VIII.C.1.k. of this Chapter, the court may not depart downward on the ground that the victim participated in the prosecution.

VIII.D. Restitution

"'The principle of restitution is an integral part of virtually every formal system of criminal justice, of every culture and every time. It holds that, whatever else the sanctioning power of society does to punish its wrongdoers, it should also ensure that the *wrongdoer is required to the degree possible to restore the victim to his or her prior state of well-being*.'" *Attorney General Guidelines on Victim and Witness Assistance*, Art. V.A. (Dep't of Justice May 2005) (emphasis added in original) (quoting S. Rep. No. 104-179, at 12-13 (1996), *reprinted in* 1996 U.S.C.C.A.N. 924, 925-26).

In intellectual property cases, there are two types of victim: the owner of the intellectual property that was infringed or misappropriated, and any

consumer who was lured into purchasing the infringing goods by fraud. Both types of victim usually qualify for restitution if they have suffered a loss.

This section discusses restitution in intellectual property crimes. For more detailed guidance on restitution principles and procedures, prosecutors should consult the *Attorney General Guidelines on Victim and Witness Assistance*, cited above, as well as the *Prosecutor's Guide to Criminal Monetary Penalties: Determination, Imposition and Enforcement of Restitution, Fines & Other Monetary Impositions* (Dep't of Justice Office of Legal Education May 2003).

VIII.D.1. Restitution is Available—and Often Required—in Intellectual Property Prosecutions

Most criminal intellectual property defendants must pay their victims restitution.

Intellectual property offenses in Title 18 require restitution under the Mandatory Victims Restitution Act of 1996 ("MVRA"), codified in part at 18 U.S.C. § 3663A ("Mandatory restitution to victims of certain crimes"). Under the MVRA, restitution is mandatory following any "offense against property under [Title 18] ... including any offense committed by fraud or deceit ... in which an identifiable victim or victims suffered a pecuniary loss." 18 U.S.C. § 3663A(c)(1)(A)(ii),(B). Intellectual property crimes are offenses against property in two senses: some defraud unwitting customers into paying money for infringing products, and all involve intellectual property, which is property as much as any tangible property. *See, e.g.*, *United States v. Carpenter*, 484 U.S. 19, 26 (1987) (stating that confidential information, another type of intangible property, has "long been recognized as property"); *United States v. Trevino*, 956 F.2d 276, 1992 WL 39028 (9th Cir. 1992) (table) (in counterfeit trademark prosecution, affirming order of restitution to nuclear power plant victim that had purchased counterfeit circuit breakers). The few cases on point confirm that intellectual property offenses are "offense[s] against property" for the purpose of § 3663A. *See United States v. Chay*, 281 F.3d 682 (7th Cir. 2002) (noting that a conviction under 18 U.S.C. § 2318(a) for trafficking in counterfeit documents and packaging for computer programs was an "offense against property" under 18 U.S.C. § 3663A and thus required mandatory restitution); *United States v. Hanna*, No. 02 CR. B64-01, 2003 WL 22705133 (S.D.N.Y. Nov. 17, 2003) (stating that a conviction under 18 U.S.C. § 2320 for trafficking in counterfeit trademarked handbags and other goods requires full restitution under 18 U.S.C. §§ 3663A, 3664). *See also United States v. Cho*, 136 F.3d 982, 983 (5th Cir. 1998) (mentioning

restitution in trademark counterfeiting case); *United States v. Manzer*, 69 F.3d 222, 229-30 (8th Cir. 1995) (upholding restitution award of $2.7 million in mail fraud, wire fraud, and copyright infringement prosecution for the sale of modification and cloning packages for unauthorized decryption of premium channel satellite broadcasts); *United States v. Sung*, 51 F.3d 92, 96 (7th Cir. 1995) (mentioning restitution in trademark counterfeiting case); *United States v. Bohai Trading Co.*, 45 F.3d 577, 579 (1st Cir. 1995) (same—restitution amount of $100,000); *United States v. Hicks*, 46 F.3d 1128, 1195 WL 20791, at *3 (4th Cir. 1995) (table) (upholding restitution award in satellite decryption and copyright case).

These cases support the proposition that restitution is mandatory in all Title 18 intellectual property offenses, including § 1831 (economic espionage to benefit foreign government, instrumentality, or agent), § 1832 (general economic espionage), § 2318 (counterfeit and illicit labels and counterfeit documentation and packaging for copyrighted works), § 2319 (copyright), § 2319B (camcorded movies), and § 2320 (goods, services, labels, documentation, and packaging with counterfeit marks). In addition, Congress recently made clear that restitution must be ordered in appropriate § 2320 cases. *See* 18 U.S.C. § 2320(b)(4) (as amended by the Stop Counterfeiting in Manufactured Goods Act, Pub. L. No. 109-181, § 1, 120 Stat. 285, 286 (enacted March 16, 2006)).

This list might also include violations of § 2319A (bootleg music and music video recordings), but defendants might argue that those crimes are not offenses against property on the ground that bootleg music and music video recordings do not infringe copyrighted property, see Section II.F. of this Manual (describing § 2319A's constitutional basis as the Commerce Clause rather than the Intellectual Property Clause), or any other type of property, and that any revenues from these offenses do not represent an actual pecuniary harm to the victim because bootleg music and music video recordings do not decrease artists' sales. Prosecutors may wish to consult CCIPS at (202) 514-1026 to discuss restitution in § 2319A convictions.

There are two principal exceptions to mandatory restitution provided for in § 3663A: "if (A) the number of identifiable victims is so large as to make restitution impracticable; or (B) determining complex issues of fact related to the cause or amount of the victim's losses would complicate or prolong the sentencing process to a degree that the need to provide restitution to any victim is outweighed by the burden on the sentencing process." 18 U.S.C. § 3663A(c)(3). Defendants can be expected to argue for one or both of these exceptions in cases of online copyright piracy that involve a large number of copyrighted works owned by a large number of victims, in cases of retail counterfeit goods cases that were sold to a large

number of defrauded customers, and in trade secret cases that involve complex issues of valuation. "This 'exception' was intended to be used sparingly, and the court is expected to use every means available, including a continuance of the restitution determination of up to 90 days, if necessary, to identify as many victims and harms to those victims as possible. 18 U.S.C. § 3664(d)(5); *U.S. v. Grimes*, 173 F.3d 634 (7th Cir. 1999)." *Prosecutor's Guide to Criminal Monetary Penalties: Determination, Imposition and Enforcement of Restitution, Fines & Other Monetary Impositions* 28 (Dep't of Justice Office of Legal Education May 2003). Department policy also requires that "[w]hen this exception does apply, the prosecutor should nevertheless *seek restitution for the benefit of the victims to the extent practicable*," *Attorney General Guidelines on Victim and Witness Assistance* Art. V.F. (Dep't of Justice May 2005) (emphasis added), such as by asking the court to order restitution "for those victims and harms the court *can* identify," *Prosecutor's Guide to Criminal Monetary Penalties* at 30 (discussing similar exception for discretionary restitution). How to ensure restitution in such situations is addressed below in the discussion of how to set the restitution amount.

Another possible exception to mandatory restitution may exist for criminal trademark, service mark, and certification mark cases under 18 U.S.C. § 2320 in which the mark-holder neglected to use the ® symbol (or other proper notice) and the defendant lacked actual notice that the mark was registered. See Section III.E.3. of this Manual. In those cases, however, even though restitution might not be awarded to the mark-holder, it should still be awarded to any customers of the defendant who were defrauded into buying what they thought were authentic goods or services. *Id.*

Although technically not an exception to the mandatory restitution provisions in 18 U.S.C. § 3663A, there are two classes of intellectual property crimes for which there is no mandatory restitution under § 3663A. The first class consists of those intellectual property offenses located outside Title 18 of the United States Code. Mandatory restitution applies only to an "offense against property under this title [18]," 18 U.S.C. § 3663A(c)(1)(A)(ii), which by definition excludes intellectual property offenses located outside Title 18. These include violations of the Digital Millennium Copyright Act, 17 U.S.C. § 1204, and the unauthorized reception of cable and satellite service as prohibited by 47 U.S.C. §§ 553(b)(2), 605.

The second class consists of any intellectual property offenses located in Title 18 that might be characterized as not being "offense[s] against *property*." § 3663A(c)(1)(A)(ii) (emphasis added). Examples might include violations of 18 U.S.C. § 2319A (bootleg music and music video recordings).

Fortunately, even in the cases discussed in the previous paragraphs, there are other mechanisms to obtain restitution. For intellectual property offenses that are located in Title 18 but are not offenses against property, discretionary restitution is available under 18 U.S.C. § 3663(a)(1)(A). For intellectual property offenses that are located outside Title 18, restitution is available under a plea agreement. *See* 18 U.S.C. § 3663(a)(3). And, finally, discretionary restitution can be ordered for *any* intellectual property crime—in fact any crime at all, whether an intellectual property crime or not, whether in Title 18 or not, and whether an offense against property or not—as a condition of probation, or of supervised release after imprisonment. *See* 18 U.S.C. §§ 3563(b)(2) (probation), 3583(d) (supervised release). A good example of these principles is *United States v. Lexington Wholesale Co.*, 71 Fed. Appx. 507 (6th Cir. 2003) (unpublished), in which a defendant was convicted for selling infant formula repackaged with counterfeit trademarks and without an accurate "use by" date, which resulted in one count for criminal trademark violations under 18 U.S.C. § 2320 and one count for misbranded food or drugs under Title 21. 71 Fed. Appx. at 508. The sentencing court imposed restitution to the victim of the misbranding count only, which the defendant argued was improper because restitution is authorized only for offenses under Title 18, not Title 21. *Id.* The appellate court affirmed restitution on the ground that it was authorized as a condition of probation and also by the plea agreement. *Id.* at 508-09.

In deciding whether to award discretionary restitution, the court must consider not only the victim's loss, but also the defendant's financial resources. 18 U.S.C. § 3663(a)(1)(B)(i); *see also* § 3563(b)(2) (allowing court to order restitution to a victim as a condition of probation "as [] reasonably necessary" and without regard to the limitations on restitution in § 3663(a) and § 3663A(c)(1)(A)). Mandatory restitution requires full restitution. *Prosecutor's Guide to Criminal Monetary Penalties* at 29-30. There is, however, a presumption for full restitution, even in discretionary restitution cases. *Id.* The Department's policy is to require full restitution in discretionary cases (assuming the defendant's current or future economic circumstances warrant it), but in discretionary cases to require nominal payment if economic circumstances so warrant. *Id.* at 30.

In deciding whether to order discretionary restitution, the court should also consider whether "the complication and prolongation of the sentencing process ... outweighs the need to provide restitution." 18 U.S.C. § 3663(a)(1)(B)(ii). Again, however, the Department advises that "prosecutors should only ask the court to apply this provision narrowly, i.e., only to whatever portion of restitution it may be applicable, and to

impose restitution for those victims and harms the court *can* identify." *Prosecutor's Guide to Criminal Monetary Penalties* at 30.

Department policy requires consideration of the availability of restitution when making charging decisions, and to structure plea agreements to provide restitution whenever possible. *See Attorney General Guidelines on Victim and Witness Assistance* Arts. V.C.1. (stating that "[w]hen exercising their discretion, prosecutors shall give due consideration to the need to provide full restitution to the victims of Federal criminal offenses," among other charging considerations), V.D.1.-.6. (plea agreements, including required provisions and supervisors' duties for approval relating to restitution). If one of the charges would require restitution, the plea agreement should require full restitution even if the defendant pleads guilty to a charge that would not require restitution. *Id.*

VIII.D.2. Victims Include Owners of Intellectual Property and Consumers Who Were Defrauded

Prosecutors should consider all victims who suffered a loss, from the holder of the intellectual property to the direct purchaser and the ultimate consumer of the infringing good.

Generally, the intellectual property rights-holder whose works were infringed or misappropriated qualifies for restitution. This is clear in cases involving copyrights, trademarks, and trade secrets. As noted in Section VIII.D.1. of this Chapter, DMCA offenses do not qualify for mandatory restitution. Moreover, the cases suggest that in DMCA or DMCA-like cases, the company whose technological measures are circumvented is not entitled to restitution unless the company also owns copyrighted works that were infringed as a result of the circumvention. *See United States v. Oliver*, No. 8:02CR3, 2005 WL 1691049, at *5 (D. Neb. July 18, 2005) ("Even if Sony had made money as a result of the defendant's criminal conduct [in modifying Sony Playstations to play pirated games in violation of the DMCA], it simply does not negate the fact that the defendant is guilty of violating Sony's copyright [by modifying the game machines to play pirated Sony games]."); *United States v. Hicks*, 46 F.3d 1128, 1995 WL 20791, at *1 (4th Cir. Jan. 20, 1995) (table) (holding that defendant convicted of selling modified satellite TV descrambling devices in violation of 47 U.S.C. § 605(e)(4) was not liable for restitution to descrambling device manufacturers because they had been fully compensated when they originally sold their devices, but ordering restitution to satellite service providers for what customers would have paid for the additional channels they could receive because of the defendant's modifications). Industry associations that represent intellectual property rights-holders can, in some

circumstances, help identify rights-holders and receive and distribute the restitution to the rights-holders.

Defrauded purchasers—if any—are entitled to restitution as well. *See, e.g.*, *United States v. Trevino*, 956 F.2d 276, 1992 WL 39028 (9th Cir. 1992) (table) (in counterfeit trademark prosecution, affirming order of restitution to nuclear power plant victim that had purchased counterfeit circuit breakers). A defendant who has defrauded a large number of consumers can be expected to argue that restitution is not required because the class of defrauded consumers is impracticably large or difficult to identify. *See* 18 U.S.C. § 3663A(c)(3). There are procedures for ordering restitution for victims who can be identified by name but cannot presently be located at a particular address. *See United States v. Berardini*, 112 F.3d 606, 609-12 (2d Cir. 1997).

Consumers who knew that they were purchasing counterfeits generally do not qualify as victims, because they have not been harmed. Distinguishing between consumers who were and were not defrauded may be a challenge.

In determining whether an involved party qualifies as a victim for the purpose of restitution, the court will distinguish between those harmed by the defendant's relevant conduct and those harmed by the offense of conviction. (The rest of this paragraph consists largely of excerpts from the *Prosecutor's Guide to Criminal Monetary Penalties: Determination, Imposition and Enforcement of Restitution, Fines & Other Monetary Impositions* 32 (Dep't of Justice Office of Legal Education May 2003), with minor edits.) The court is statutorily authorized to impose restitution only to identifiable victims of the acts that are part of the offense of conviction. In *Hughey v. United States*, 495 U.S. 411, 413 (1990), the Supreme Court held that the restitution statutes limit restitution to "the loss caused by the specific conduct that is the basis of the offense of conviction." Restitution is not authorized for acts merely related to the offense of conviction, such as acts that are within "relevant conduct" under guideline sentencing (U.S.S.G. § 1B1.3), but are outside the actual offense of conviction itself. Under the primary restitution statutes, a victim is "a person directly and proximately harmed as a result of the commission of an offense for which restitution may be ordered." 18 U.S.C. §§ 3663A(a)(2), 3663(a)(2). Where the offense of conviction includes a scheme, conspiracy, or pattern of criminal activity, however, restitution can be imposed for the entire scheme, conspiracy, or pattern. Therefore, prosecutors should charge such offenses to indicate the specific nature and full extent of the acts that constitute the scheme, conspiracy, or pattern of which the offense of conviction is involved, in order to permit the broadest imposition of restitution.

If the acts for which restitution is sought cannot be tied together with a scheme, pattern, or conspiracy, then the acts outside the offense of conviction generally do not trigger restitution. Under this rule, restitution is generally not triggered by one kind of act if the offense of conviction describes another kind of act, even if the acts are logically related in purpose or intent—for example, if the offense of conviction is *possession* of stolen credit cards, some courts will not impose restitution for the victims of the *use* of the cards. *See, e.g., United States v. Blake*, 81 F.3d 498 (4th Cir. 1996); *United States v. Hayes*, 32 F.3d 171 (5th Cir. 1994). However, some courts apply this rule more strictly than others. For example, to determine the existence of a scheme and what acts it included, some courts will consider the facts alleged in the indictment, proven at trial, or admitted in the plea colloquy. *See, e.g., United States v. Jackson*, 155 F.3d 942 (8th Cir. 1998); *United States v. Ramirez*, 196 F.3d 895 (8th Cir. 1999); *United States v. Hughey (II)*, 147 F.3d 423, 438 (5th Cir. 1998) (suggesting that restitution might have been triggered by acts not in the indictment had they been established by the trial record).

If *no* scheme, conspiracy, or pattern encompasses the acts for which injured parties seek restitution, restitution will likely be limited in two respects. First, a party who was injured solely by an act outside the offense of conviction—such as a party whose losses were proved only as relevant conduct—cannot obtain restitution. Second, a party who *was* injured by the offense of conviction can obtain restitution only for the offense-of-conviction acts and not acts proved only as relevant conduct at sentencing—even relevant conduct that counted towards the loss or infringement amount; however, some courts may still allow restitution for this type of relevant conduct if it is alleged in the indictment or proved at trial, not just at sentencing. The exception to both these limitations is, of course, restitution ordered pursuant to a stipulation in a plea agreement. *See* 18 U.S.C. § 3663(a)(3).

Application of these principles to an intellectual property crime occurred in *United States v. Manzer*, 69 F.3d 222 (8th Cir. 1995), in which the court ordered $2.7 million in restitution from a defendant convicted of mail fraud, wire fraud, and criminal copyright infringement for trafficking in cloned computer chips. The cloned chips would allow satellite descrambling devices to decrypt cable satellite signals without authorization. The defendant objected to the $2.7 million restitution award on the ground that it included sales not identified in the indictment. *Id.* at 229-30. The Eighth Circuit disagreed, holding that the mail and wire fraud counts alleged a scheme to defraud that "encompass[ed] transactions beyond those alleged in the counts of conviction," including the sales not

otherwise identified in the indictment. *Id.* at 230 (citation and internal quotation marks omitted). Note that the restitution might have been limited to the sales alleged the indictment if the defendant had pleaded to or been convicted of only the copyright charge.

There are several ways to help ensure that restitution is awarded for harm caused. As part of any plea deal, the government should require the defendant to plead to the counts that offer maximum restitution, or the government should insist upon a comprehensive plea agreement that provides restitution to the victims of relevant offense conduct (whether the statutes or offenses of conviction provide for it or not). *See* 18 U.S.C. § 3663(a)(3) (allowing court to order restitution as provided in plea agreement); *Prosecutor's Guide to Criminal Monetary Penalties: Determination, Imposition and Enforcement of Restitution, Fines & Other Monetary Impositions* 22-24 (Dep't of Justice Office of Legal Education May 2003).

At the beginning of the case, prosecutors should draft the indictment to maximize restitution. *Id.* at 21. As the Executive Office for United States Attorneys counsels:

> Prosecutors should avoid the "scheme" restitution pitfalls by:
>
> a) Charging offenses that involve the statutory elements of an "intent to defraud" or "intent to deceive" in the traditional wire/mail fraud (or conspiracy) format, where the scheme (or conspiracy) is described in detail and incorporated by reference into each specific act count; and
>
> b) Making sure the dates alleged as the beginning and end of the scheme or conspiracy include all acts in furtherance of the scheme or conspiracy for which restitution should be imposed.

Id. at 22. Moreover, "[s]imply tracking the statutory language of such offenses does not clarify if the acts of conviction are part of a scheme, i.e., whether different kinds of acts make up a scheme to 'defraud' or 'deceive.' Numerous restitution orders have been vacated in such cases due to ambiguity of the 'scheme' issue." *Id.* The same concerns apply to whether acts in addition to those alleged as overt acts of a conspiracy can qualify as part of the conspiracy for purposes of awarding restitution. The *Prosecutor's Guide to Criminal Monetary Penalties* discusses specific ways to structure restitution provisions in a plea agreement to maximize restitution. *Id.* at 23-24.

VIII.D.3. Determining a Restitution Figure

Once the government has identified the people and entities who might be classified as victims—consumers who were defrauded and intellectual property rights-holders—the next question is how to calculate what the victims are owed, if anything.

To begin with, as discussed in the prior section, the restitution award must be based on the loss caused by the defendant's offense of conviction.

After determining which victims and transactions qualify for restitution, the government must determine how the restitution should be calculated. The most important principle is that restitution is intended to make the victims whole by compensating them for their losses. *See* 18 U.S.C. §§ 3663(a)(1)(B)(i)(I), 3663A(b), 3664(a); *U.S.S.G.* § 5E1.1(a). This principle has several consequences.

First, the restitution order should require the defendant to return any of the victim's property that he took. *See* 18 U.S.C. §§ 3663(b)(1)(A), 3663A(b)(1)(A), 3664(f)(4)(A). This principle applies across all intellectual property offenses:

- In trade secret offenses, the defendant should be required to return the trade secret and any other items that he took from the owner of the trade secret.
- In infringement cases, the defendant should be required to return the money he accepted from the customers he defrauded (if any—in some cases the customers knew that they were receiving counterfeits). Although the defendant might argue that he is entitled to offset the value of the goods the defrauded customers received, often that value is next to nothing. *Compare cf. United States v. West Coast Aluminum Heat Treating Co.*, 265 F.3d 986, 992 (9th Cir. 2001) ("And, by reducing the loss calculation to account for the partial benefit gained by the government, the district court remained consistent with the rule that the victim's loss should be offset by the victim's benefit.") *and United States v. Matsumaru*, 244 F.3d 1092, 1109 (9th Cir. 2001) (holding that restitution of the purchase price for the business the victim paid for and was promised but did not receive, must be offset by the value of the van and business license he did receive) *with United States v. Angelica*, 859 F.2d 1390, 1394 (9th Cir. 1988) (affirming trial court's refusal to offset restitution award by value of substitute property given to victims, because there was "no abuse of discretion in the district court's decision to disregard the value of the inexpensive garnets

that were unwanted by the victims and substituted for their diamonds as part of the fraudulent scheme") *and United States v. Austin*, 54 F.3d 394, 402 (7th Cir. 1995) (holding that "even if the [counterfeit or misrepresented art] pieces Austin sold ... were not completely worthless, $0 was the best estimate of their worth" for purposes of calculating loss).

- In infringement cases—and perhaps trade secret cases as well—the defendant should also compensate the intellectual property rights-holder victims for any sales that he diverted from them. *See United States v. Sung*, 51 F.3d 92, 94 (7th Cir. 1995) (holding, in criminal trademark prosecution, that "[r]estitution in a criminal case is the counterpart to damages in civil litigation"). If the defendant's conduct did not divert any sales from the victim, then the victim is entitled to no restitution. *See United States v. Foote*, No. CR.A. 00-20091-01-KHV, 2003 WL 22466158, at *7 (D. Kan. July 31, 2003) (refusing to award restitution to trademark-holders because the government proposed no reliable estimate of the victim's losses and citing cases for the need to prove lost profits). A defendant is most likely to divert sales from the victim when he has defrauded customers into thinking that his product or service is authentic, although he may have a counter-argument if his prices were sufficiently under the authentic price that his customers would have been unlikely to pay the victim the full price for the real thing. A consumer who pays $20 for a high-quality (or even a low-quality) fake purse might not have paid full price ($120 to $700) for the real purse, and thus his purchase of the fake might not represent a lost sale to the victim. Similarly, some computer users who download a $60,000 engineering program for free from an infringing website or peer-to-peer network may be "trophy hunters" who would not have paid full price for an authorized copy, whereas other downloaders may be businesspeople who would have paid full price had the free download not been available. Restitution orders should differentiate between these situations, to the extent possible. Prosecutors might also try to introduce evidence establishing that the availability of high-quality infringing works affected the market for the victim's product. *See Brooktree Corp. v. Advanced Micro Devices, Inc.*, 977 F.2d 1555, 1579 (Fed. Cir. 1992) (civil case upholding "actual damages" calculation based on evidence that plaintiff had been forced to lower its prices as a result of defendant's infringing activities).

- Restitution based on lost sales is not calculated by the defendant's gain, but rather by the victim's loss. *Foote*, 2003 WL 22466158, at *7. For example, in *United States v. Martin*, 64 Fed. Appx. 129 (10th Cir. 2003), the total value of the items infringed was $1,143,395, but the restitution equaled only $395,000—the retail value multiplied by the rights-holder's profit margin. Nevertheless, the defendant has no right to have his *own* costs offset against his gain. *United States v. Chay*, 281 F.3d 682, 686-87 (7th Cir. 2002).

- When the evidence of infringement consists of the defendant's inventory of infringing product rather than his actual sales—and the defendant therefore argues against any restitution for lack of actual diverted sales—the government may argue that the inventory is a reasonable estimate of the defendant's past sales. This argument is likely to be most persuasive when the defendant's inventory is counted after he has been in business for a long time. Inventory is more likely to overstate past sales when a business is just starting out, and to understate past sales when the business has been successful and ongoing for a substantial time.

- At least one court has held that restitution in a criminal intellectual property case can be based on the amount of statutory damages that the victim could have obtained from the defendant in a civil case, but this was a case in which the statutory damages likely understated the actual damages. *See United States v. Manzer*, 69 F.3d 222, 229-30 (8th Cir. 1995) (upholding restitution award in descrambler case of $2.7 million for 270 cloning devices based on minimum statutory damages of $10,000 per device, where victim provided loss figure of over $6.8 million). Statutory damages are available in civil suits for a variety of intellectual property violations. *See e..g.*, 15 U.S.C. § 1117 (c) (statutory damages of $500-$100,000 (up to $1 million if infringement was willful) per counterfeit mark per type of goods or services); 17 U.S.C. § 504(c) (statutory damages of $750-$30,000 (up to $150,000 if infringement was willful) per infringed work); 47 U.S.C. § 605(e)(3)(C)(i)(II) (statutory damages of $10,000-$100,000 per violation). *See also* Roger D. Blair & Thomas F. Cotter, *An Economic Analysis of Damages Rules in Intellectual Property Law*, 39 Wm. & Mary L. Rev. 1585, 1651-72 (1998) (discussing economic theory of statutory damages in copyright law).

- If the defendant earned a profit from his crime but the court finds that restitution is too difficult to calculate, the court can

nevertheless take away the defendant's gain by imposing a fine in the amount of his gain. *See Foote*, 2003 WL 22466158, at *7.

Second, the restitution order should compensate the victim for any money spent to investigate the defendant's conduct, whether during the victim's own investigation or while helping the government investigate and prosecute. These costs often arise in intellectual property cases: employers conduct internal investigations into their employees' theft of trade secrets, and copyright and trademark-holders often hire private investigators to monitor and investigate suspected infringers. The mandatory and discretionary restitution statutes both authorize restitution "for lost income and necessary child care, transportation, and other expenses related to participation in the investigation or prosecution of the offense or attendance at proceedings related to the offense." 18 U.S.C. §§ 3663(b)(4), 3663A(b)(4). These provisions have been interpreted to cover not only the victim's expenses in helping the government, but also the costs of the victim's own investigation. *See United States v. Brown*, 150 Fed. Appx. 575 (8th Cir. 2005) (per curiam) (awarding restitution to victim company for staff investigation costs into reconstructing and correcting financial records related to defendant's embezzlement, where defendant contested proof of amount but not whether investigative costs as a category are awardable); *United States v. Beaird*, 145 Fed. Appx. 853 (5th Cir. 2005) (per curiam) (affirming $200,000 award of restitution for attorney's fees and litigation expenses associated with assisting the FBI's investigation), *cert. denied*, 126 S. Ct. 1382 (2006); *United States v. Gordon*, 393 F.3d 1044, 1049, 1056-57 (9th Cir. 2004) (discussing reimbursement of investigative costs in depth, in case affirming $1,038,477 in restitution for costs of company's internal investigation and responses to grand jury subpoenas), *cert. denied*, 126 S. Ct. 472 (2005). *See also United States v. Susel*, 429 F.3d 782, 783 (8th Cir. 2005) (per curiam) (affirming award of software company's administrative and transportation expenses during participation in the investigation and prosecution of the offense in criminal copyright case).

Third, in deciding whether to award discretionary restitution, the court must consider not only the victim's loss, but also the defendant's financial resources. 18 U.S.C. § 3663(a)(1)(B)(i); *see also* 18 U.S.C. § 3563(b)(2) (allowing court to order restitution to a victim as a condition of probation "as [] reasonably necessary" and without regard to the limitations on restitution in § 3663(a) and § 3663A(c)(1)(A)). Mandatory restitution requires full restitution. *Prosecutor's Guide to Criminal Monetary Penalties* at 29-30. There is, however, a presumption for full restitution, even in discretionary restitution cases. *Id.* Department policy requires full restitution in discretionary cases (assuming the defendant's current or

future economic circumstances warrant it), unless economic circumstances warrant nominal payment. *Id.* at 30. In no case shall the fact that a victim has received or is entitled to receive compensation with respect to a loss from insurance or any other source be considered in determining the amount of restitution. 18 U.S.C. § 3664(f)(1)(B).

Fourth, victims have an important role in helping to determine the appropriate amount of restitution. The government must consult with witnesses and the court to consider victims' evidence at sentencing. *See* 42 U.S.C. § 10607(c)(3)(G); *Attorney General Guidelines for Victim and Witness Assistance* Art. IV.B.2.b(4) (May 4, 2005). See generally Chapter X of this Manual (Victims). The criminal intellectual property statutes similarly require the court to consider victims' evidence at sentencing. *See* 18 U.S.C. §§ 2319(d), 2319A(d), 2319B(e), 2320(d). The pre-sentence report must also include a verified assessment of victim impact in every case. Fed. R. Crim. P. 32(d)(2)(B). Trade associations can be very helpful in providing victim impact statements, particularly when an offense involves a large quantity and variety of infringing products. See the listing of intellectual property contacts in Appendix G of this Manual.

VIII.E. Forfeiture

In intellectual property (IP) crimes, forfeiture can serve several important functions. Forfeiting infringing items removes them from the stream of commerce so they cannot be sold or redistributed. Forfeiting the tools and equipment that defendants use to commit IP crimes prevents their being used to commit further IP crime. Forfeiting the proceeds of IP crime—the revenues and profits—prevents their reinvestment in a criminal enterprise. Finally, forfeiture can serve as a powerful deterrent.

Congress has passed many forfeiture laws that address specific crimes, but in a manner that has created a complex web of forfeiture statutes. The specific IP forfeiture provisions vary with the IP crime, yet the underlying criminal IP statute will often not make it obvious which forfeiture remedies—administrative, civil, or criminal—are available.

To make IP forfeiture more standard and intuitive, Congress passed the Stop Counterfeiting in Manufactured Goods Act, Pub. L. No. 109-181, 120 Stat. 285 (enacted March 16, 2006) to expand the type of property that can be forfeited and to clarify and standardize the procedures for doing so. The Act, however, affects only counterfeit trademark, service mark, and certification mark offenses in 18 U.S.C. § 2320. Consequently, the

Administration has proposed similar amendments to the forfeiture provisions for other IP offenses.

This Chapter is not a definitive guide to forfeiture law, but rather it provides a basic overview of the forfeiture remedies available in IP crimes. Due to the intricacies of forfeiture law (including both recent changes in 2006 and possible future revisions), prosecutors with questions concerning forfeiture practice and procedure should contact the forfeiture expert in their office or the Criminal Division's Asset Forfeiture and Money Laundering Section at (202) 514-1263.

VIII.E.1. Property Subject to Forfeiture

Intellectual property crimes give rise to three general categories of forfeitable property:

- Contraband items, which include infringing copyrighted copies and phonorecords; goods, labels, documentation, and packaging that bear counterfeit trademarks, service marks, or certification marks; and unauthorized recordings of live musical performances. *See* 49 U.S.C. § 80302(a)(6). These items are generally subject to forfeiture.
- Proceeds derived from the commission of an IP offense. These are also usually forfeitable.
- Facilitating property, that is, property that was used to commit or facilitate the IP offense, such as plates, molds or masters used to produce copyright-infringing works; computers, tools, equipment, and supplies used to produce counterfeit goods; and vehicles used to traffic in any of the above. Forfeiture of facilitating property is available in many cases, but its availability varies substantially depending on the specific IP offense, the type of property, and the type of forfeiture sought.

VIII.E.2. Overview of Forfeiture Procedures

There are three types of forfeiture procedures: administrative, civil, and criminal. This section gives a brief overview and includes a table that summarizes the types of forfeiture available for each kind of property, organized by intellectual property offense.

VIII.E.2.a. Administrative Forfeiture Proceedings

Administrative forfeiture occurs when a law enforcement agency forfeits property in an administrative, non-judicial matter. As with the

other types of forfeiture procedure, administrative forfeiture is available only pursuant to a specific statute that authorizes such a procedure. Administrative forfeiture commences once an agency seizes property and then sends or publishes notice of the property seizure within the prescribed deadlines. If nobody responds to the notice by filing a claim of ownership claim within the allotted time, the property is forfeited without involving a prosecutor or judge. If a claim is filed, the seizing agency must either return the property or seek forfeiture through a judicial procedure.

Administrative forfeiture in IP offenses is usually limited to situations that implicate the customs laws. For example, Immigration and Customs Enforcement (ICE) may seize, forfeit, and destroy imported copyright-infringing products administratively pursuant to 17 U.S.C. §§ 509(b) and 603(c). ICE may also seize, forfeit, and destroy imported trademark-infringing products administratively under 19 U.S.C. § 1526(e). Administrative forfeiture may also be available for violations of 18 U.S.C. §§ 2318 and 2319A. *See* 18 U.S.C. § 2318(e); 17 U.S.C. § 509; *see also* 18 U.S.C. § 981(d); 19 U.S.C. §§ 1607-09 (administrative forfeiture of proceeds); 49 U.S.C. § 80304 (administrative forfeiture of facilitating property).

Real property and personal property (other than monetary instruments) that are worth more than $500,000 can never be forfeited in an administrative proceeding. *See* 19 U.S.C. § 1607; 18 U.S.C. § 985.

VIII.E.2.b. Civil and Criminal Proceedings

Unlike administrative forfeiture proceedings, civil and criminal forfeiture are judicial actions that require the involvement of prosecutors and the courts.

Criminal forfeiture is an *in personam* proceeding that is executed as part of a criminal defendant's sentence. It thus requires a conviction and is limited to property belonging to the defendant that was involved in the offense of conviction. Criminal forfeiture cannot reach a third party's property, even if the defendant used the third party's property to commit the crime.

Whereas criminal forfeiture is an *in personam* action against the defendant, civil forfeiture is an *in rem* action against the property itself. This means that civil forfeiture proceedings can reach property regardless of who owns it, if the government can prove that the property was derived from or used to commit a crime. Civil forfeiture proceedings are not part of a criminal case at all. The burden of proof is a preponderance of the

evidence, and civil forfeiture proceedings can dispose of property even without a criminal conviction or the filing of any criminal charges.

VIII.E.2.c. Table of Forfeiture Provisions Arranged by Criminal IP Statute

The following list indicates the types of forfeiture available for each intellectual property offense. Note that administrative forfeiture is generally available for vessels used to transport contraband items pursuant to 49 U.S.C. § 80304. Note also that even where forfeiture of proceeds is not provided for directly, it may be available indirectly through money laundering statutes.

CRIMINAL COPYRIGHT INFRINGEMENT

Administrative	**Yes.** 17 U.S.C. §§ 509(a) (forfeiture of infringing goods) and (b) (applying customs laws), 602-603 (specifically prohibiting imports of infringing copies). 18 U.S.C. § 981(d) (allowing administrative forfeiture for proceeds forfeitable civilly); 19 U.S.C. §§ 1595a, 1607-09.
Civil	
Infringing Items	**Yes**. 17 U.S.C. §§ 509(a), 602-603 (prohibiting imports).
Facilitating Property	**Yes.** 17 U.S.C. § 509(a) (plates, molds, masters and other equipment used to make infringing copies).
Proceeds	**Yes.** 18 U.S.C. § 981(a)(1)(C).
Criminal	
Infringing Items	**Yes.** 17 U.S.C. §§ 506(b), 602-603; 28 U.S.C. § 2461(c) (allowing criminal forfeiture where property could be seized civilly).
Facilitating Property	**Yes**. 17 U.S.C. § 506(b); 28 U.S.C. § 2461.

Proceeds	**Yes.** 18 U.S.C. § 981(a)(1)(C); 28 U.S.C. § 2461(c).

DIGITAL MILLENNIUM COPYRIGHT ACT

Administrative	**No.**
Civil	**None.**
Criminal	**None.**

ECONOMIC ESPIONAGE ACT (TRADE SECRET THEFT)

Administrative	**No.**
Civil	**None.**
Criminal	
Facilitating Property	**Yes (discretionary)**. 18 U.S.C. § 1834(a)(2).
Proceeds	**Yes (mandatory).** 18 U.S.C. § 1834(a)(1).

COUNTERFEIT/ILLICIT LABELS, DOCUMENTATION, AND PACKAGING FOR COPYRIGHTED WORKS

Administrative	**Yes.** 18 U.S.C. § 2318(e); 17 U.S.C. § 509(b); 18 U.S.C. § 981(d); 19 U.S.C. §§ 1595a (allowing seizure and forfeiture by Customs), 1607-09.
Civil	
Counterfeit/ Infringing Items	**Yes.** 18 U.S.C. § 2318(e); 17 U.S.C. § 509.
Facilitating Property	**Yes.** 18 U.S.C. § 2318(e); 17 U.S.C. § 509.
Proceeds	**Yes.** 18 U.S.C. §§ 981(a)(1)(C), 1956(c)(7).
Criminal	
Counterfeit/ Infringing Items	**Yes (mandatory)**. 18 U.S.C. § 2318(d).

Facilitating Property	**Yes (mandatory as to plates, molds, masters, etc.; discretionary as to other equipment).** 18 U.S.C. § 2318(d).
Proceeds	**Yes.** 18 U.S.C. §§ 981(a)(1)(C), 1956(c)(7); 28 U.S.C. § 2461(c).

UNAUTHORIZED FIXATIONS OF LIVE MUSICAL PERFORMANCES ("BOOTLEGGING")

Administrative	**Yes.** 18 U.S.C §§ 2319A(c), 981(d); 19 U.S.C. §§ 1595a, 1607-09.
Civil	
Unauthorized Recordings	**Yes.** 18 U.S.C. § 2319A(c).
Facilitating Property	**No.**
Proceeds	**Yes.** 18 U.S.C. § 981(a)(1)(C).
Criminal	
Unauthorized Recordings	**Yes (mandatory).** 18 U.S.C. § 2319A(b).
Facilitating Property	**Yes (mandatory for plates, molds, masters, etc.; discretionary as to other equipment).** 18 U.S.C. § 2319A(b).
Proceeds	**Yes.** 18 U.S.C. §§ 981(a)(1)(C), 1956(c)(7); 28 U.S.C. § 2461(c).

UNAUTHORIZED RECORDING OF MOTION PICTURES ("CAMCORDING")

Administrative	**No.**
Civil	**None.**
Criminal	
Unauthorized Recordings	**Yes (mandatory).** 18 U.S.C. § 2319B(b).

Facilitating Property	**Yes (mandatory).** 18 U.S.C. § 2319B(b).
Proceeds	**No.**

GOODS, SERVICES, LABELS, DOCUMENTATION, AND PACKAGING WITH COUNTERFEIT MARKS

***NOTE: 18 U.S.C. § 2320(b) was amended on March 16, 2006. The table below reflects these amendments. The pre-amendment provision is discussed and quoted in Sections VIII.E.4.b. and VIII.E.5. of this Chapter.

Administrative	**Yes.** 19 U.S.C. §§ 1595a, 1607-09; 18 U.S.C. § 981(d);
Civil	
Counterfeit Items	**Yes.** 18 U.S.C. § 2320(b)(1)(A).
Facilitating Property	**Yes.** 18 U.S.C. § 2320(b)(1)(B).
Proceeds	**Yes.** 18 U.S.C. §§ 981(a)(1)(C); 1956(c)(7); 28 U.S.C. § 2461(c).
Criminal	
Counterfeit Items	**Yes (mandatory)**. 18 U.S.C. § 2320(b)(3)(A).
Facilitating Property	**Yes (mandatory).** 18 U.S.C. § 2320(b)(3)(A).
Proceeds	**Yes.** 18 U.S.C. § 2320(b)(3)(A); *or alternatively:* 18 U.S.C. §§ 981(a)(1)(C), 1956(c)(7); 28 U.S.C. § 2461(c).

VIII.E.3. Choosing a Forfeiture Procedure

Although the prosecutor may commence parallel civil and criminal forfeiture cases to keep all avenues of forfeiture open, various factors may affect which procedure is best to pursue:

- **Substitute assets.** In criminal proceedings, the court can enter a money judgment against the defendant for the property's value or can order the forfeiture of substitute assets if the property has been dissipated or cannot be found.
- **Burden of proof.** In civil proceedings, the government need only prove that a crime was committed and that the property derived

from or facilitated the crime by a preponderance of the evidence. In criminal cases, the government must prove beyond a reasonable doubt that a crime was committed and that the defendant committed the crime, although the nexus between the property and the offense need be proved only by a preponderance of the evidence.

- **Criminal conviction as a prerequisite.** Civil forfeiture does not require a conviction. This is especially important if the government wants to forfeit the property of fugitives or defendants who have died, or if the government can prove that the property was involved in a crime but cannot prove the wrongdoer's specific identity. Moreover, civil proceedings may be brought against any property derived from either a specific offense or from an illegal course of conduct, and therefore is not limited to property involved in the offense(s) of conviction.
- **Ownership of property.** Criminal forfeiture reaches property only if it is owned by the defendant. Civil forfeiture should be considered if the prosecutor seeks to forfeit proceeds or facilitation property that the defendant does not own.
- **Discovery and disclosure obligations.** Civil forfeiture, governed by civil discovery rules, can result in early or unwanted disclosure of information through traditional civil discovery mechanisms such as interrogatories and depositions, and it is subject to stringent deadlines.
- **Attorneys' fees.** If the government brings an unsuccessful action for civil forfeiture, it may be liable for the owner's attorneys' fees.
- **Efficiency.** Administrative forfeiture is preferred whenever available, as it can dispose of certain forfeiture matters quickly in a non-judicial setting.

VIII.E.4. Civil Forfeiture in IP Matters

Civil forfeiture is available in some (though not all) intellectual property offenses. It is available for property connected to criminal copyright infringement, 18 U.S.C. § 2319; trafficking in counterfeit or illicit labels or counterfeit documentation or packaging for copyrighted works, 18 U.S.C. § 2318; unauthorized fixations of live musical performances, 18 U.S.C. § 2319A; and trafficking in goods, services, labels, documentation, or packaging with counterfeit marks, 18 U.S.C. § 2320. Civil forfeiture is not available if the property is only connected to

violations of the Digital Millennium Copyright Act, 17 U.S.C. § 1204, or the Economic Espionage Act, 18 U.S.C. §§ 1831, 1832. Again, the government need only prove that the crime was committed; it need not convict a specific defendant of the crime.

VIII.E.4.a. Proceeds

The government can forfeit the proceeds of 18 U.S.C. §§ 2318, 2319, 2319A, and 2320 offenses in civil forfeiture proceedings. Under the Civil Asset Forfeiture Reform Act of 2000 ("CAFRA") amendments to 18 U.S.C. § 981(a)(1)(C), a general civil forfeiture statute, the government can seek civil forfeiture of "[a]ny property, real or personal, which constitutes or is derived from proceeds traceable to," among other things, any offense defined as a specified unlawful activity in the money laundering provisions at 18 U.S.C. § 1956(c)(7). Specified unlawful activities include criminal copyright infringement and trademark counterfeiting, 18 U.S.C. § 1956(c)(7)(D) (citing 18 U.S.C. §§ 2319, 2320), as well as any offense listed as racketeering activity in 18 U.S.C. § 1961(1). Section 1961, in turn, lists not only §§ 2319 and 2320 violations, but also violations of 18 U.S.C. § 2318 (counterfeit labels, documentation, and packaging for copyrighted works) and § 2319A (bootleg musical recordings). Thus, civil forfeiture of proceeds is available for violations of 18 U.S.C. §§ 2318, 2319, 2319A, and 2320.

VIII.E.4.b. Infringing Items, Other Contraband, and Facilitating Property

Civil forfeiture of infringing and other contraband items, as well as facilitating property, is also available for some IP offenses, but varies greatly depending on the particular offense and property involved.

For some copyright and copyright-related offenses, Title 17 provides for civil forfeiture of contraband such as infringing copies and certain types of facilitating property. Civil forfeiture is available against property that was manufactured or used in violation of the copyright laws, 17 U.S.C. § 509(a), specifically (a) infringing copies, or copies intended for infringing use; and (b) the plates, masters, or other means used for reproducing the infringing copies, as well as other devices for manufacturing, reproducing, or assembling infringing copies. *See*, *e.g., United States v. One Sharp Photocopier, Model SF-7750*, 771 F. Supp. 980, 983 (D. Minn. 1991) (holding that the government was entitled to forfeiture of copier used to produce infringing copies of a software instruction manual); *see also* 17 U.S.C. § 509(b) (incorporating administrative forfeiture provisions of Title 19 and the provisions relating to *in rem* admiralty actions). Civil forfeiture is also

available against infringing articles or unauthorized fixations imported into the United States, in some circumstances. *See* 17 U.S.C. §§ 602-603 (infringing copies); 18 U.S.C. § 2319A (unauthorized fixations of live musical performances).

For counterfeit trademark, service mark, and certification mark offenses, the forfeiture provisions changed markedly in 2006. Before the March 16, 2006 amendments, there was no civil forfeiture authority for these cases except in the context of importation or proceeds under the specified unlawful activity provisions discussed in above. However, the old version of the statute, 18 U.S.C. § 2320, included a hybrid forfeiture provision that used the civil preponderance-of-the-evidence standard but applied only in a criminal prosecution. Before its amendment, § 2320(b) provided that "[u]pon a determination by a preponderance of the evidence that any articles in the possession of a defendant in a prosecution under this section bear counterfeit marks, the United States may obtain an order for the destruction of such articles." 18 U.S.C. § 2320(b) (West 2005). Congress enacted this provision because "[e]ven if the defendant is ultimately acquitted of the criminal charge, there is no valid public policy reason to allow the defendant to retain materials that are in fact counterfeit." *Joint Statement on Trademark Counterfeiting Legislation*, 130 Cong. Rec. 31,674 (1984). *See also United States v. Foote*, 238 F. Supp. 2d 1271 (D. Kan. 2002). This provision was revised considerably, however, by the Stop Counterfeiting in Manufactured Goods Act, Pub. L. No. 109-181, 120 Stat. 285 (enacted March 16, 2006) to provide for civil forfeiture of "[a]ny article bearing or consisting of a counterfeit mark used in committing" a § 2320 violation, and "[a]ny property used, in any manner or part, to commit or to facilitate the commission of" such a violation. 18 U.S.C. § 2320(b)(1).

VIII.E.4.c. Innocent Owner Defense

In most civil forfeiture actions, the innocent owner defense allows an owner to challenge the forfeiture on the ground that he was unaware that the property was being used for an illegal purpose, or took all reasonable steps under the circumstances to stop it. *See United States v. 2001 Honda Accord EX*, 245 F. Supp. 2d 602 (M.D. Pa. 2003) (holding that CAFRA preserved the rule that the burden of proof shifts to the claimant to establish the innocent owner defense); *United States v. 2526 Faxon Avenue*, 145 F. Supp. 2d 942 (W.D. Tenn. 2001) (holding that CAFRA requires the claimant to prove the affirmative innocent owner defense by a preponderance of the evidence). There are some exceptions, however, most notably for importation offenses, and therefore prosecutors may wish

to consult with the Department's Asset Forfeiture and Money Laundering Section at (202) 514-1263 if an innocent owner is likely to submit a claim.

VIII.E.4.d. Victims' Ability to Forfeit Property

Note also that some IP rights-holders may obtain certain civil seizures that can complicate the government's criminal prosecution, not to mention its forfeiture proceedings. Mark-holders have an *ex parte* remedy for seizing infringing products and manufacturing equipment. 15 U.S.C. §1116(d). Mark-holders may also petition the court for seizure orders during a civil action against an infringer under 15 U.S.C. § 1114. Authority for an *ex parte* seizure order is provided at 15 U.S.C. § 1116(d)(1)(A). Mark-holders who seek such an order must give reasonable notice to the United States Attorney for the judicial district in which the order is sought, after which the United States Attorney "may participate in the proceedings arising under such application if such proceedings may affect evidence of an offense against the United States." 15 U.S.C. § 1116(d)(2). The mark-holder's application may be denied "if the court determines that the public interest in a potential prosecution so requires." *Id.* If the mark-holder's application is granted, then the seizure must be made by a federal, state, or local law enforcement officer. *See* 15 U.S.C. § 1116(d)(9).

Similar *ex parte* seizure remedies are available to rights-holders in copyright and counterfeit or illicit labels cases. *See* 17 U.S.C. § 503; 18 U.S.C. § 2318(f).

Prosecutors may need to participate in these civil proceedings in order to preserve evidence relevant to an incipient or ongoing criminal case, to contest the issuance of an order, to preserve an ongoing investigation, or to inform the mark-holder of his ability to initiate a parallel civil case to seize, forfeit, and destroy equipment used to manufacture the counterfeit trademark goods.

VIII.E.5. Criminal Forfeiture in IP Matters

As noted above, criminal forfeiture is an *in personam* action, and thus is available only once a defendant has been convicted, and then it is limited to property belonging to the defendant. *See United States v. Totaro*, 345 F.3d 989, 995 (8th Cir. 2003) (holding that criminal forfeiture is *in personam*, because if it allowed the forfeiture of a third party's interest, the forfeiture would become an *in rem* action and the third party could contest the forfeiture on more than ownership grounds); *United States v. O'Dell*, 247 F.3d 655, 680 (6th Cir. 2001) (recognizing that criminal forfeiture "entitles the government to forfeiture of a convicted defendant's interests and

nothing more") (citation omitted); *United States v. Gilbert*, 244 F.3d 888, 919 (11th Cir. 2001) ("Because it seeks to penalize the defendant for his illegal activities, *in personam* forfeiture reaches only that property, or portion thereof, owned by the defendant.") (citation omitted).

Even though criminal forfeiture is executed after conviction, the government should plan for criminal forfeiture during the investigation and at indictment. Pre-indictment seizure warrants can be used to seize infringing items (whether or not they are the property of a target). Moreover, the indictment should include separate forfeiture charges that identify any property that is forfeitable pursuant to the charged offenses. For forfeiture language to include in an indictment, prosecutors should consult the forfeiture expert in their office or the Criminal Division's Asset Forfeiture and Money Laundering Section.

Criminal forfeiture is available for at least some types of property in cases involving the following criminal IP statutes: copyright, 17 U.S.C. § 506, 18 U.S.C. § 2319; trade secret theft, 18 U.S.C. § 1834; trafficking in counterfeit or illicit labels or counterfeit documentation or packaging for copyrighted works, 18 U.S.C. § 2318; trafficking in goods, services, labels, documentation, or packaging with counterfeit marks, 18 U.S.C. § 2320; bootlegged recordings of live musical performances, 18 U.S.C. § 2319A; and movie camcording, 18 U.S.C. § 2319B. Currently, there are no criminal forfeiture provisions for violations of the Digital Millennium Copyright Act, 17 U.S.C. § 1204.

VIII.E.5.a. Proceeds

The government can obtain criminal forfeiture of IP crime proceeds whenever those proceeds could be forfeited civilly: 18 U.S.C. §§ 2318, 2319, 2319A, and 2320. This is because CAFRA generally provided that criminal forfeiture is available whenever civil forfeiture is available:

> If a person is charged in a criminal case with a violation of an Act of Congress for which the civil or criminal forfeiture of property is authorized, the Government may include notice of the forfeiture in the indictment or information pursuant to the Federal Rules of Criminal Procedure. If the defendant is convicted of the offense giving rise to the forfeiture, the court shall order the forfeiture of the property as part of the sentence in the criminal case pursuant to the Federal Rules of Criminal Procedure and section 3554 of title 18, United States Code. The procedures in section 413 of the Controlled Substances Act (21 U.S.C. § 853) apply to all stages of a criminal forfeiture proceeding,

except that subsection (d) of such section applies only in cases in which the defendant is convicted of a violation of such Act.

28 U.S.C. § 2461(c). As discussed above, the offenses for which civil forfeiture is available are enumerated in 18 U.S.C. § 981, and include any offense constituting "specified unlawful activity" under 18 U.S.C. § 1956(c)(7), the money laundering statute. Section 1956(c)(7)'s list of "specified unlawful activity" includes, directly or indirectly, violations of 18 U.S.C. §§ 2318, 2319, 2319A, and 2320.

Where a defendant has engaged in a monetary transaction involving the proceeds of an intellectual property offense, "knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity"—regardless of whether the crime is listed in § 1956(c)(7)—the defendant may also be charged, and the proceeds subject to forfeiture, under the money laundering statute directly. *See United States. v. Turner*, 400 F.3d 491 (7th Cir. 2005) (holding that the defendant need not know the actual source of the money, but only that it came from "some illegal activity"); *see also United States v. Khalil*, No. CR. A. 95-577-01, 1999 WL 455698 (E.D. Pa. June 30, 1999) (forfeiture involving counterfeiting popular music).

In addition, for counterfeit marks cases, the Stop Counterfeiting in Manufactured Goods Act (enacted March 16, 2006, discussed in Section VIII.E.4. of this Chapter) amended 18 U.S.C. § 2320 to provide for mandatory criminal forfeiture of proceeds (as well as other property). *See* 18 U.S.C. § 2320(b)(3)(A)(i) (as amended Mar. 16, 2006).

The Economic Espionage Act provides for mandatory criminal forfeiture of the proceeds of a violation of 18 U.S.C. § 1831 or § 1832. *See* 18 U.S.C. § 1834(a)(1).

VIII.E.5.b. Infringing Items, Other Contraband, and Facilitating Property

Generally, criminal forfeiture is available against contraband items involved in an IP offense—such as infringing items, unauthorized recordings, and counterfeit labels or marks or articles bearing such marks—and in some cases those items are subject to mandatory destruction. Facilitating property is likewise subject to criminal forfeiture in most cases, although such equipment generally need not be destroyed and can instead be disposed of in other ways, such as at auction.

Copyright offenses are subject to mandatory forfeiture: "When any person is convicted of a violation of subsection (a), the court in its

judgment of conviction shall, in addition to the penalty therein prescribed, order the forfeiture and destruction or other disposition of all infringing copies or phonorecords and all implements, devices, or equipment used in the manufacture of such infringing copies or phonorecords." 17 U.S.C. § 506(b).

Criminal forfeiture is likewise mandatory in offenses for camcording and trafficking in counterfeit and illicit labels and counterfeit documentation and packaging for copyrighted works. *See* 18 U.S.C. § 2318(d) (stating that the court must order "the forfeiture and destruction or other disposition of all counterfeit labels or illicit labels and all articles to which counterfeit labels or illicit labels have been affixed or which were intended to have had such labels affixed, and of any equipment, device, or material used to manufacture, reproduce, or assemble the counterfeit labels or illicit labels"); 18 U.S.C. § 2319B(b) (stating that upon conviction, the court "shall, in addition to any penalty provided, order the forfeiture and destruction or other disposition of all unauthorized copies of motion pictures or other audiovisual works protected under title 17, or parts thereof, and any audiovisual recording devices or other equipment used in connection with the offense").

The "bootleg" statute, 18 U.S.C. § 2319A(b), contains a similar forfeiture provision, requiring forfeiture and destruction of unauthorized recordings. However, unlike the mandatory forfeiture of equipment discussed above, the forfeiture of equipment used to reproduce unauthorized recordings of live musical performances is left to the discretion of the court, "taking into account the nature, scope, and proportionality of the use of the equipment in the offense." *Compare* 18 U.S.C. § 2319A(b) *with* 17 U.S.C. § 506(b).

For counterfeit marks cases, as noted above, until March 16, 2006, the criminal statute contained an unusual criminal forfeiture provision that allowed forfeiture of counterfeit goods upon a showing by a preponderance of the evidence (within or related to a criminal case) that the items bore counterfeit marks. *See* 18 U.S.C. § 2320(b) (West 2005). *See supra* II.E.4. Under the recent revisions to the forfeiture provisions in the Stop Counterfeiting in Manufactured Goods Act, 18 U.S.C. § 2320 now provides for mandatory forfeiture of "any article that bears or consists of a counterfeit mark used in committing the offense" and any of the defendant's property "used, or intended to be used, in any manner or part, to commit, facilitate, aid, or abet the commission of the offense." 18 U.S.C. § 2320(b)(3)(A). Any seized article bearing or consisting of a counterfeit mark must be destroyed. 18 U.S.C. § 2320(b)(3)(B).

The Economic Espionage Act, governing theft of trade secrets, provides for forfeiture of property used in facilitating the commission of the offense, considering the nature, scope, and proportionality of the use of the property in the offense. 18 U.S.C. § 1834(a)(2).