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**HEARING ON “FINDING AND FIGHTING FAKES: REVIEWING THE STRATEGY  
TARGETING ORGANIZED PIRACY”**

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Good morning Chairman Voinovich, members of the Subcommittee. Thank you for this opportunity to testify, and update you on the steps that the Department of Homeland Security has taken to improve the enforcement of intellectual property rights as part of the Administration’s Strategy Targeting Organized Piracy (STOP). Under Secretary Asa Hutchinson participated in the STOP! announcement with DHS’s interagency partners. Both U.S. Customs and Border Protection (CBP) and U.S. Immigrations and Customs Enforcement (ICE) are full participants in the STOP! initiative.

My testimony focuses on the contributions that CBP, the primary agency responsible for border enforcement, has made to STOP.

CBP, as the guardian of the Nation’s borders, safeguards the homeland – foremost, by protecting the American public against terrorists and the instruments of terror, while at the same time enforcing the laws of the United States and fostering the Nation’s economic growth through lawful travel and trade, including the laws and regulations related to the protection of IPR. Each year, the number of seizures of counterfeit and pirated merchandise made by the Department of Homeland Security rises dramatically. Since 2000, the number of seizures has more than doubled. Interpol estimates that 7% of global trade involves counterfeit and piratical goods. Although CBP’s IPR enforcement efforts have been successful, the flood of infringing imports requires us to explore new ideas for IPR enforcement.

Today, I will discuss new approaches CBP is taking as part of STOP to enhance and complement traditional methods of DHS's IPR enforcement. With its STOP initiatives, CBP is diversifying its IPR enforcement portfolio and moving beyond our traditional methods. These approaches improve our ability to identify high-risk companies and shipments while maintaining the flow of legitimate trade. In addition, our STOP initiatives include greater cooperation with the business community and other government agencies to provide improved IPR protection. CBP has

- Created and tested an innovative statistical model for assessing IPR risks at our borders
- Established a program of post-entry verifications, or "IPR audits", designed to identify business practices that leave us vulnerable to IPR violations, and to determine the scope of a company's IPR violations
- Collaborated with PTO to make it easier for businesses to enforce their trademark rights at the border
- Issued proposed regulations to enable CBP to better enforce U.S. copyright[s] protection for sound recordings and motion pictures, or similar audio-visual works.

#### **Statistical Risk Modeling for IPR Enforcement**

CBP's IPR risk model is designed to enhance current efforts by CBP officers to identify counterfeit and pirated goods at our borders. It builds on CBP's already strong border enforcement efforts by providing greater analytical targeting for IPR infringing shipments and importers.

The IPR risk model is a computer-based statistical model that diversifies CBP's approach to risk assessment and targeting; complements current enforcement efforts; and offers potential improvement in utilization of resources. CBP uses traditional

targeting programs and reviews of transaction documentation to identify and target imports for examination for potential IPR violations. These two approaches depend upon the experience and knowledge of CBP officers, and require significant use of officer resources. Unlike our traditional approaches, the model applies statistical analysis techniques and external information to assess IPR risk. The risk model gives significant emphasis to CBP's IPR enforcement and import data while infusing other agency assessments on IPR risk, including information from the USTR's Special 301 Report on IPR threats throughout the world. CBP is also consulting with industry, including the National Association of Manufacturers and representatives of the pharmaceuticals industry, to identify and include risk indicators into the CBP IPR risk model where feasible.

The model consists of various statistical factors that form a "model" of the significant characteristics of IPR infringing imports. These factors are combined using a two-step statistical formula to calculate risk scores for individual imports. Scores for individual importations can be aggregated to provide an assessment of IPR risk for entities such as importers.

CBP has successfully completed first phases of testing the model and is working toward national validation of the model. The IPR risk model is being developed to identify both individual imports and companies found to be high risk for IPR violations. Individual imports are targeted for cargo examinations. Importers identified as being high-risk may be candidates for CBP's post-entry verification, another of CBP's STOP initiatives aimed at increasing the effectiveness of IPR enforcement efforts.

#### **Detecting IPR Vulnerabilities through Post-entry Verifications**

CBP is testing ways to expand IPR enforcement efforts that go beyond the traditional examination of containers at the border by bringing a new focus and new skills to IPR enforcement. Specifically, CBP is employing the skills of auditors and other

resources to the evaluation of a business's systems to determine if there are weaknesses that lead to IPR violations.

Approximately two dozen companies will be subject to an IPR audit this year, based upon risks identified by the newly developed IPR risk model and/or as evidenced by past IPR violations.

Based on preliminary findings from ongoing audits, violations have been identified in several areas including importers of electronics, toys, textiles and recreational motorized cycles. Efforts are also underway to determine the appropriate remedial or punitive actions necessary.

CBP auditors review such documentation as purchase records, product specifications, general and subsidiary ledgers, and payment records. Financial records hold key information that allows auditors to identify potential IPR violations. Such information includes:

- a) Purchase Orders provide details about the goods being purchased, including a description of the goods, price per unit, quantity, shipping instructions, delivery date, and payment terms. When counterfeit goods are seized, purchase orders can be instrumental in determining the quantity of infringing goods the manufacturer was contractually obligated to produce. In addition, purchase orders will often indicate the parties involved in the manufacture and/or trading of the illicit goods.
- b) Product Specifications provide detailed technical specifications and requirements of products and are used by designers, engineers, and quality managers involved in the manufacturer of goods. Reviews of product specifications often indicate placement of trademarks or copyrights, or specify use of trademarked products (i.e. YKK zippers or Intel processors)

- c) General and Subsidiary Ledgers are where all accounting transactions are recorded for a company. When a company legitimately has rights to use a copyright or trademark, evidence can be found in the financial records of license agreements and royalties. Detailed transactions are typically recorded in subsidiary ledgers, such as accounts payable and inventory. These accounts can be instrumental in tracing the parties being paid for the illegal goods as well as the quantity of goods flowing through the inventory.
- d) Payment Records provide details on remittances made for purchases. Companies conducting international business often make use of letters of credit or wire transfers to pay for products. Analysis of the remittances determines the parties involved in the counterfeiting scheme and the illicit financial gains.

Audits may also review for business records that are kept by small companies, such as:

- a) Correspondence rather than formal purchasing contracts, purchase orders, or product specifications.
- b) Financial records kept in an ad hoc form, rather than a formal system.
- c) Payment records that could be made by alternate remittance systems, such as money orders, cashier checks, credit cards, traveler's checks, Western Union, or various other electronic payment methods.

Due to its initial success, additional companies will be selected for post-entry verifications and the audit findings will be incorporated into the IPR risk model.

#### **Facilitation of Recordation of Trademarks**

CBP and PTO are currently working to create a hyperlink from PTO's website to a CBP webpage explaining the recordation process and providing the recordation

application. This link will help businesses, particularly small businesses lacking experience in working with CBP, to better enforce their trademarks rights.

In preparation for establishment of this link, CBP is currently in the final phases of developing a real-time, on-line recordation system through which recordants will be able to apply and pay for recordations at the CBP website. CBP expects that the new system will greatly reduce the length of time it takes to record intellectual property rights with CBP, and significantly reduce CBP's administrative burdens related to recording both trademarks and copyrights. We expect to roll out the on-line recordation system later this summer. When this is completed, we will be ready to establish a link at the PTO website.

### **Proposed Copyright Regulation**

CBP issued proposed regulations to allow U.S. copyrights for sound recordings and motion pictures, or similar audio-visual works, to be recorded with CBP while copyright registration is pending at the Copyright Office. The early recording will provide CBP with the information it needs to prevent importation into the U.S. of pirated goods.

CBP has received and analyzed comments from the public on the proposed rulemaking and has drafted its final rule accordingly. At this time, CBP and DHS are currently reviewing the final rule through the normal approval process.

### **Conclusion**

With our STOP initiatives, CBP has broken new ground in the fight against counterfeiting and piracy. We will continue to work with DHS Headquarters, our colleagues at ICE, and our other partner agencies, as well as industry, to continuously improve our targeting and enforcement efforts to deprive IPR violators of their illicit financial gains. Thank you again, Chairman Voinovich, and the members of the Subcommittee for this opportunity to testify. I would be happy to answer any questions you may have.

