

# ***Global Piracy of Intellectual Property and Survival of the U.S. Textile Industry: An Accelerating Problem Requiring More Aggressive Solutions.***

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### **EXECUTIVE SUMMARY**

The modern American textile industry is a high-tech, capital and intellectual property intensive industry which produces thousands of new designs every year. Intellectual Property Rights (IPR) are vitally important to American textile companies and are under attack by the illegal pirating of the IPR of American manufacturers.

According to a recently conducted textile industry survey, over half of the textile companies responding said that IPR is either somewhat or very important to their business. Over half of the companies responding said that IPR theft is experienced "some" or "a lot." *All* of the companies who said IPR was important to them had experienced at least some theft.

Review of the survey results shows that although U.S. textile companies are generally satisfied with the enforcement of their IPR rights as against domestic infringers, they are generally *not* satisfied with their ability to enforce such rights against foreign infringers. Although some surveyed companies are very active in pursuing enforcement of their IPR, many are not. Mostly those that have not done so are frustrated by the seeming inability to deal with foreign infringers, whose products make up an increasing percentage of infringements.

The U.S. Department of Commerce has recently estimated that "IPR infringement cost some textile companies \$100 million or more annual in lost sales." Textile executives are also convinced the problem is getting worse.

This "white paper" will examine the importance of IPR in the modern American textile industry and the devastating effect of IPR theft. It will also make several recommendations to the U.S. government for enhanced international textile IPR enforcement. Our recommendations touch on several areas including:

- o Enhancements to trade law section 337
- o Enhanced civil penalties for foreign-based infringements
- o US Customs presence at trade shows
- o Making IPR violations a recognized ground under WTO retaliation
- o Re-aligning U.S. Customs priorities with respect to seizures of textiles versus apparel.
- o Criminal penalties for infringers
- o Defining systematic copying as an IPR violation
- o Effective IPR enforcement as an explicit negotiating goal under TPA
- o Use of non-tariff barriers (NTBs) to fight against piracy
- o Executive branch punishing of IPR offenders
- o Enhanced publicity and education.

## INTRODUCTION

The modern American textile industry is a high-tech, capital and intellectual property intensive industry which produces thousands of new designs every year--in fact leads the world in design and other intellectual property development. It is an industry that employs 970,000 people, whose jobs are dependent on the development of original designs of a patentable, copyrightable, or trade-markable nature.

The importance of Intellectual Property Rights (IPR) to American textile companies has always had tremendous historical importance--from the time Samuel Slater first appropriated English IP and took it to America. Yet today its importance is greater than ever. The purpose of this white paper is *first* to sketch out the extent of and reasons for that IPR importance, and *second* to suggest ways in which the U.S. Government could help U.S. textile companies more effectively utilize and enforce their IPR as a competitive advantage.

As U.S. trade policy continues to result in the hollowing out of one industry after another, and produces the most devastating trade deficit ever recorded in the known history of the universe, it is more important than ever that U.S. manufacturing be assisted to succeed with whatever advantage it has left. As foreign manufacturing has opportunistically taken advantage of the much lower tariffs that the U.S. imposes than other countries, the looser foreign environmental standards, their laxer individual hygiene and safety requirements, their poorer work conditions and depressed wages, and so forth, many foreign manufacturers have also tried to gain yet another advantage by illegally pirating the IPR of American manufacturers. This is a problem cutting across many industries.

No industry has been more affected by these tactics than textiles. Although the textile/apparel trade deficit ranks *only* third among U.S. industries behind electronics (high-tech) and automobiles (high-ticket), the textile/apparel industry has nevertheless been, percentage-wise, nothing short of devastated by the excess of imports. This is not the place to recite all the well-understood facts of job losses and the like, but it is worth noting that recent estimates place the percent of U.S.-consumed apparel still actually made here at under ten percent. Rather the focus here is on one of the few remaining sources of competitive advantage that U.S. textile companies still can pursue, namely IPR--so long as even this advantage is not stolen from them by world-wide IPR pirates.

It is *not* the case that the countries which host the most IPR pirating do not understand the significance of IPR or the nature of their thievery. On the contrary, they promote pirating precisely *because* they understand just how important such rights are. This is demonstrated conclusively by their own actions. For example, the Associated Press reported recently that China's Ministry of Foreign Trade and Economic Cooperation brought the China Name Brand Products Show to Los Angeles, the first time in the United States. One of the show's organizers said: "Americans don't know we have our own famous brands...we want the American public to understand..."<sup>1</sup> One of the exhibitors lamented not having brand name recognition in the U.S., proclaiming "Maybe someday we'll have our own brand name in J.C. Penney".<sup>2</sup> It seems a fair assumption that the Chinese Ministry and exhibitors would object if *their* brand names were stolen.

## **IMPORTANCE OF IPR AND EXTENT OF PROBLEM OF PIRACY**

Recently the National Textile Association (NTA) conducted a survey<sup>3</sup> to help define some of the parameters of IPR's importance to the remaining U.S. textile industry. Some of the key findings of the NTA survey were:

- 1.) Over half of the companies responding said that IPR are either somewhat or very important to their business.
- 2.) Over half of the companies responding said that IPR theft is experienced "some" or "a lot." *All* of the companies who said IPR was important to them had experienced at least some theft.
- 3.) Review of the survey results shows that although U.S. textile companies are generally satisfied with the enforcement of their IPR rights as against domestic infringers, they are generally *not* satisfied with their ability to enforce such rights against foreign infringers.
- 4.) Although other IPR such as patents and trademarks are important to some U.S. textile companies, by far the largest category of IPR importance among companies surveyed is copyrights. This applies across a number of different product categories such as printed fabrics, carpets, upholstery and furniture fabrics, etc.
- 5.) Although some surveyed companies are very active in pursuing enforcement of their IPR, many are not. Only one-third of the companies surveyed have even taken the first step of threatening legal action, much less taking it. Mostly those that have not done so are frustrated by the seeming inability to deal with foreign infringers, whose products make up an increasing percentage of infringements.

In addition to the IPR survey, the NTA IP working group also conducted a brief review of literature, and discussed the problem with senior textile executives. Some of the findings from this review are summarized below:

- 1.) The American Textile Manufacturers Institute (ATMI) and the American Apparel and Footwear Association (AAFA) have both urged that IPR be a priority for the U.S. Trade Representative (USTR) in the Doha Trade Round<sup>4</sup> thus underscoring its importance.
- 2.) So far the U.S. Customs Service have been able to seize only a relatively small amount of textiles and apparel for IPR violations, but the seizures have been growing rapidly, reflecting, it is believed, the increasing severity of the problem. In 2001 some \$7.8 million was seized, but this was over twice what was seized just two years before, and up 81% over 2000.<sup>5</sup>
- 3.) *Women's Wear Daily* has recently cited the importance of brands such as Lycra®, Dacron®, Sensil®, Nano-Tex®, Polartec®, and Gore-Tex®, stating that "as more mills attempt to establish their own brands...getting the name into the minds of consumers...is one of the basic tactics in textile marketing today."<sup>6</sup>
- 4.) The U.S. Department of Commerce has recently estimated that "IPR infringement cost some textile companies \$100 million or more annual in lost sales."<sup>7</sup>

The importance of IP to textile companies is a recurring theme among textile executives. For example, George Shuster, CEO of Cranston Print Works Company, the nation's oldest textile company, has explained that "design has become such a critical core competency for the survival of so many textile companies such as ourself that the most aggressive measures are absolutely necessary against infringers. One of the few edges we have left is our intellectual property, and foreigners are trying to steal that, too"<sup>8</sup> Similarly Hank Truslow, III, President of Sunbury Textile Mill, has said of IP: "This is a very, very serious issue. We see it not as a short-term blip problem but a long-term one, and one that affects the livelihood of all of our companies. Our identities lie in our fabric and design."<sup>9</sup>

Textile executives are also convinced the problem is getting worse. Foreign production has already exploited advantages in loose environmental regulation, poor industrial hygiene and safety standards, poor work conditions and depressed wages, and so forth. Opportunistically looking to undermine all competitive advantages U.S. producers may yet enjoy, foreign producers have increasingly targeted IP as one more asset to be appropriated, even illegally. For example, Hank Truslow believes the threat "has intensified in the last five years and exploded in the last three."<sup>10</sup> Roger Berkley, President of Weave, believes that "[t]he situation has become grossly worse, particularly with the entry of China via non-Chinese customers who go there and just tell them 'make this' and it comes back here or to other countries."<sup>11</sup>

## Recommendations

The NTA working group explored a number of different areas by which the U.S. government could help the industry better address the increasingly important issue of IPR enforcement against foreign pirates. Some of these involve Executive Branch actions, others statutory changes by the Legislative Branch. If there is a common theme to these ideas, it is that the U.S. needs to gain better leverage from the fact that all countries clamor for access to our market. This implies that the U.S. could, if it wished, impose enforcement of fundamental standards of IPR as a basic prerequisite to entry and participation in our market. It may be much more difficult to police all the markets of the world, but shame on us is the overwhelming opinion of U.S. manufacturers, if we do not at least use our own market's attractiveness as the fulcrum by which to insist that our IPR be respected by foreigners.

In no specific order of importance, our recommendations are:

- 1) *"Section 337 Improvements.* So-called "Section 337" should be strengthened to permit expedited procedures, and should be better publicized in the industry. Although Section 337 does already permit preliminary injunctive relief, these temporary exclusions and cease and desist orders take 90 days or more to decide, which, in a fashion driven seasonal industry is too long. It would be more useful if the ITC were required to make a determination with respect to temporary relief in a far narrower window (say, for example, five days). Section 337 as applied to textile IPR is an ideal area for expedited relief, since it would presumably hinge on the quickly applied "substantial similarity" test upon which injunctive relief is already given in civil textile design copyright infringement cases.

The biggest thing lacking from section 337 actions are monetary damages--they are not available. Only equitable relief is available (exclusion orders and cease and desist orders) as remedies under 337. If a party wishes to receive monetary compensation for past damages by the infringer, he would have to bring a subsequent and separate action in federal court seeking those monetary

damages. This process is drawn out. The ability to recover monetary damages in a 337 action would, therefore, be a desirable thing.

Finally, the publication of the availability of 337 actions would indeed be a helpful as it would help alert the industry of its existence.

2) *Enhanced Civil Penalties for Foreign-Based Infringements.* Foreign infringers should be subject to greater penalties than domestic infringers, say triple or even quintuple damages, and heavier statutory damages. The copyright law should be amended to carry out this objective, and the difference can be more than justified on standard deterrence principles.

One of the principal purposes of IPR infringement lawsuits is deterrence. Deterrence is the net product of the probabilities of detection, judgment and enforcement, multiplied by the level of penalty. Since detection is so much more difficult in the case of foreign infringers, and enforcement so much more problematic, in order for equal net deterrence to occur, foreign infringers must be subject to greater penalties in order to ensure at least equal net deterrence. Without such a difference, the effective penalty against foreign infringers is actually less than against domestic infringers.

There are additional rationales for such a difference in penalty between foreign and domestic infringers. The harm done by foreign infringement is greater than domestic for many reasons, including the drain of U.S. dollars outside the country, the impact on domestic manufacturing jobs, and the increase in the already unsustainable trade deficit. Also, TRIPs requires all countries to create an "effective deterrent" against counterfeiting. Since the major host countries of counterfeiting are notoriously ineffective in providing deterrent, it is incumbent on the U.S. (and any victimized country), in order to carry out its TRIPs obligations, to attempt to fill the void. Finally, there are other precedents in trade applications for different penalties for foreign violations. For example, the whole rationale of dumping cases is that producers should not be allowed to disrupt our market by entering it under cost, a rationale not applied to domestic producers.

3) *US Customs Presence at Trade Shows.* Since many foreign infringers are discovered at trade shows, U.S. Customs should send representatives to textile trade shows, including the major ones in other countries such as Heimtex. Such a contact would be available to identify copyright violators on the spot and put them on a posted watch list right at the show. Such identification could discourage buyers at the earliest possible moment. In addition, the physical presence of U.S. Customs at such a booth would provide a deterrent effect in and of itself.

4.) *IPR Violations as a Recognized Ground under WTO Retaliation.* Already there are various violations which the WTO recognizes as valid reasons for trade retaliation actions. IPR violations are certainly as important as some of those already recognized rationales, and in some cases even more important. Thus, IPR violations should become a valid, recognized predicate for retaliatory actions under the WTO. The U.S. should push for such a remedy to be recognized as part of its Doha negotiations.

5.) *U.S. Customs Seizures of Textile versus Apparel.* When one studies the pattern of U.S. Customs seizures of textile versus apparel for IPR violations, it is apparent that Customs has been much more successful at seizing imported apparel embodying such violations than textile imports. This is exactly the opposite of what one might guess on *a priori* grounds, since textile copyright infringements require less complicated subjective judgments to demonstrate. Work should commence within Customs, and between Customs and the textile industry, to identify the

reasons for this discrepancy. Out of such a study might come suggestions for increasing the effectiveness of Customs surveillance and interdiction of textile IPR infringements.

6.) *Criminal Penalties.* Based on similar rationales to recommendation (2) above, legislation should criminalize certain foreign-based IPR violations. Indeed, one of the most common methods in actual practice for textile IPR violations to occur involves an American company (a customer) taking U.S. textiles to foreign manufacturers for the purpose of having them copied at less cost abroad. This especially reprehensible practice needs to be deterred. Accordingly, U.S. law should clearly define as a crime the taking of a U.S. product abroad for the purpose of having it reproduced in a foreign country, if such reproduction involves IPR violation.

7.) *Systematic Copying as an IPR Violation.* Another increasing practice of IPR infringers is to copy entire lines of textiles, but make sufficient changes on each individual design such that each taken separately can just barely escape copyright infringement tests. The sophistication of such systematic IPR pirates should no longer be availing. Such could be met by defining an IPR violation to consist of the systematic use of close copies. Perhaps language such as the "systematic use of foreign production to replicate in overall feeling and design the copyrighted designs of U.S. companies" would be sufficient to meet this challenge. Alternatively, or in conjunction, the "substantially similar" test for textile copyright infringement could be legislatively expanded to include not just very close copies but also foreign copies whose nature "evinces a purpose to replicate the overall feeling of a copyrighted textile design." Such an expanded standard is less needed domestically, because U.S. businesses are, by and large, nowhere near as much IPR pirates as foreigners.

8.) *Effective IPR Enforcement as an Explicit Negotiating Goal under TPA.* The WTO is not proving an effective mechanism to ensure IP protection. In order to achieve through its own efforts what the WTO has not, the U.S. government should commit that it will not bring back any agreement, bilateral or multilateral, under TPA unless such agreements embody strong, effective and enforceable IP safeguards. Since everyone wants even greater access to our already open market, it should not be difficult to negotiate such protections as a condition to such greater access in all future agreements, provided we only have the will just to *ask* for such safeguards. One standard might be that no trade agreements can be brought back without IP language that is at least as strong, if not stronger, than in TRIPS.

9.) *Use of Non-Tariff Barriers (NTBs).* The United States undoubtedly has the least NTBs in the world. Other countries, however, use them very frequently to achieve both additional trade barriers in general and also to address specific objectives allegedly important to them. For example, India's notorious color testing regimes in textiles constitute a practically insurmountable NTB. The U.S. government should impose an NTB in the IPR area, which is of actual as opposed to pretended significance to the U.S. Such an NTB would be an important signal to the world of how seriously the U.S. takes the subject of IPR violations. Such an NTB could take, for example, this form: every finished fabric shipment into the U.S., or any product including finished fabric, must be accompanied by a signed certificate of the importer that the product does not embody a copyright infringement. (In the Indian example given above, the Indian government will not even permit entry on the basis of a signed certificate that the textiles seeking entry do not embody chemical violations, instead insisting on lot by lot expensive testing. In this sense, our IPR certification procedure would be far less onerous than foreign precedents). If later the certificate of IPR compliance should be proven false, legislation could further impose significant monetary penalties and loss of license. Such a declaration is eminently reasonable to require, since it simply constitutes a cautionary reminder that existing IPR laws need to be followed.

10.) *Executive Branch Punishing of IPR Offenders.* The Executive Branch could charge itself, or be legislatively required, to produce an ongoing ranking of countries which are the worst textile IPR offenders, and prohibit any further textile access to these countries until they satisfy minimum reasonable conditions to ensure IPR violations are minimized. The worst class of offenders could be denied any textile access at all. The next level of offenders could be allowed current levels of access, but be denied any increase of access until corrections are demonstrated, no matter what the excuse, be it war-on drugs, terrorism, or whatever else. IPR needs to be recognized, in other words, as a priority of the first rank.

Alternatively, the U.S. government could declare that no greater textile access will be given anywhere--no exception--until IPR is recognized and enforced worldwide at levels equal to U.S. protection. Such a policy would parallel that announced by the U.S. government that there will be no further access to the U.S. textile market until other countries lower their tariffs to give the U.S. true reciprocal access. Again, such a stand would emphasize that the U.S. is serious about the IPR issue.

11.) *Publicity and Education.* The NTA's investigation demonstrated that there are gaping holes in U.S. enforcement of IPR violations by foreign sources both because: 1) existing laws do not effectively address what has become a global problem of rapidly increasing proportions and 2) even existing laws are not widely enough understood and utilized.

Accordingly, we recommend that as changes are made in the above areas, that the current and existing laws be publicized to importers and retailers, to make sure they are educated as to the importance, and pertinent details, of the IPR issue as it relates to textiles. Such education could be significantly enhanced in the effectiveness of its message by pedagogical "stings" and raids conducted on a random, without-warning basis by the appropriate U.S. law enforcement agencies.

## Conclusion

The above recommendations would be a good start to begin to address a rapidly growing problem. The NTA suspects that its IPR concerns, while they may have aspects unique to the textile industry, are shared as well by other industries. To the extent the above suggestions would be of value to other businesses dependent on IPR protection, the NTA certainly welcomes cross-industry improvements which would assist embattled U.S. manufacturers interests of whatever sector.

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<sup>1</sup> Rogers, John, "China Striving to Establish a Brand-Name Presence in U.S.," Associated Press, September 7, 2002.

<sup>2</sup> Ibid.

<sup>3</sup> NTA Intellectual Property Survey 2002.

<sup>4</sup> U.S. Dept. of Commerce, "Report to the Congressional Textile Caucus on the Administration's on Textile Issues," September 2002 p. 5.

<sup>5</sup> Ibid.

<sup>6</sup> Greene, Joshua, "Textile Firms Try to Reel in Consumers," *Women's Wear Daily*, September 16, 2002.

<sup>7</sup> U.S. Dept. of Commerce, "Report to the Congressional Textile Caucus on the Administration's on Textile Issues," September 2002 p. 5; Ellis, Krisit, "NTA Targets Theft of Textile Properties," *Women's Wear Daily*, August 24, 2002.

<sup>8</sup> Sloan, Carole, "New Formed Group Raises Knockoff Issue," *Home Textiles Today*, September 2, 2002, pp. 1 and 26.

<sup>9</sup> Ibid.

<sup>10</sup> Ibid.

<sup>11</sup> Ibid.