

**WRITTEN TESTIMONY OF ROBERT M. CHIAVIELLO, JR. ON
BEHALF OF LUV N' CARE, LTD. AND ADMAR
INTERNATIONAL, INC. TO THE U.S. HOUSE OF
REPRESENTATIVES COMMITTEE ON SCIENCE, SPACE AND
TECHNOLOGY, SUBCOMMITTEE ON OVERSIGHT AND
SUBCOMMITTEE ON RESEARCH & TECHNOLOGY**

Executive Summary

International unfair competition through the sale of counterfeit and pirated products has been dramatically increased by the combination of unrestricted online retailers and an open unregulated boarder that permits counterfeiters and pirates to directly ship to consumers in the US their counterfeit and pirated products. A growing concern involves sales of knock-off products from third party sellers who acquire and ship small quantity lots and individual packages from foreign locations to US consumers completely bypassing US laws and regulations relating to intellectual property, product health and safety requirement and without paying state and local taxes.

Luv n' care, Ltd. and Admar International, Inc.

Luv n' care, Ltd. (LNC) is a baby products company located in Monroe, Louisiana. LNC has been in business for more than forty years and in that time has excelled as a designer, manufacturer and seller of innovative, high quality and attractive products for babies and small children. LNC's products are sold under the NUBY brand and are among the most popular and well-known baby products in the industry. The NUBY brand and logo are famous throughout the United States

and worldwide. Based on its innovative, high quality and attractive designs, LNC is now known as one of the leading baby product companies in the United States and throughout the world. LNC protects the intellectual property in its innovative, high quality and attractive products through a combination of patents, trademarks and copyrights. Admar International, Inc. (Admar) owns and manages the intellectual property developed and used by LNC.

Representative examples of LNC's products are set out below:



Types of Unfair Competition

There are two forms of unfair competition affecting LNC. LNC faces unfair competition from the sale of knock-off or counterfeit products that are copies of or colorable imitations of LNC's products. While the knock-off products may visually resemble LNC's products they are often made using substantially inferior materials and workmanship and without regard to US health and safety regulations.

The counterfeiters then market their knock-off products directly to consumers by unlawfully using LNC's trademarks and copyrights in their online advertising. In many instances, the consumer is tricked into purchasing the knock-off product thinking it is the legitimate LNC product. As a result of these unlawful activities by the knock-off sellers LNC and Admar are losing millions of dollars in sales.

Another form of unfair competition relates to foreign competitors who do not comply with US health and safety regulations placing consumers at risk when they receive knock-off goods that are counterfeits of inferior quality and that do not comply with US health and safety laws and regulations. These unscrupulous sellers enjoy cost advantage in two respects. One, they use inferior less expensive materials of poor quality and two, they do not incur the expense of complying with US health and safety laws and regulations. LNC will inevitably have a higher cost structure as it uses high quality and relatively more expensive materials and bears the cost of complying with US health and safety laws and regulations. Consumers, regardless of how cost conscious they may be, will oftentimes select the less expensive product where they can discern no differences. This is

particularly problematic with online sales as the consumer cannot discern quality differences from photographs and this is especially true where the seller unlawfully expropriates a photograph from the original seller or brand owner.

The Knock-Off Products Industry

Counterfeiting and pirating popular branded products is an industry, primarily centered in China. As soon as a product is successful, Chinese manufacturers rush to copy the product or knock it off.¹ The knock-off manufacturers do not now typically copy the product identically but, in most instances, make small modifications, usually to cut corners on quality and make the product cheaper. The knock-off is almost always made of inferior poor-quality materials and regard for fit and finish is often ignored. The knock-off manufacturers will sometime offer their knock-off products directly to consumers but in most instances, they will sell directly to online sellers and small retailers via online marketplaces such as Alibaba. In addition to cutting costs by using inferior and less expensive inputs, the knock-off manufacturers also enjoy a cost advantage by not having to incur the expense of

¹ A knock-off is distinguished from a copy by exhibiting small variations from the original whereas the copy is identical. In either case it is hard for the untrained consumer to distinguish the original from the copy or knock-off.

complying with US health and safety laws and regulations. They also have a further cost advantage by not having to incur the research and development costs in creating a new product.

The next step in the knock-off industry distribution chain is the knock-off sellers who take advantage of the online marketplace offered by Amazon and eBay. These knock-off sellers create very low overhead online stores where they promote and sell their knock-off products directly to US consumers. The knock-off sellers are often physically located outside the US and most often in China. The knock-off seller offers the knock-off product directly to US consumers with no indication that the seller is located outside the US. Purchased knock-off products are then shipped directly to the US consumer via the foreign postal services, UPS or other carriers. In other cases, the knock-off seller will arrange to have the sales fulfilled by Amazon or other third parties. In the case of products fulfilled by Amazon, the seller will ship small quantities (less than container loads) to an Amazon fulfillment center. In almost every instance of a foreign knock-off seller, the seller uses a fake name, no contact information is provided, and the domain name

owner is hidden behind privacy settings. The knock-off products almost never include any indications of the manufacturer.

The sellers create online storefronts that often use brands in headlines and banners and embedded in the metadata or as key words. Some particularly flagrant knock-off sellers will even use photographs of the branded product and sometimes copy actual photographs of the product posted on the branded sellers website. The clear intent of these knock-off sellers is to create as close a look and feel as possible to the branded product, so the consumer is tricked into thinking that the knock-off seller is selling the branded product. Knock-off sellers also purchase ad words from Google and other search engines that include the brand name so that a consumer searching for the branded product will receive search results promoting the knock-off product. Without careful examination it is likely the consumer will be tricked into believing that the ad is sponsored by the brand owner creating a likelihood that the consumer will purchase the knock-off product instead of the branded product.

These problems are further exacerbated by the fact the knock-off sellers hide their identities and are often located outside the United

States. In a typical situation a knock-off seller will offer the knock-off products using a fictitious name with no identifying information. If notified of the infringement, the typical knock-off seller will remove the item or close the online store and reopen a new store under a different name selling the same products. LNC has been informed that Amazon alone has over 80,000 third party sellers making it almost impossible for a brand owner to comprehensively police that marketplace.

The knock-off manufacturers and sellers have inherent and substantial cost advantages verses the cost borne by the brand owners and can offer the knock-off product at a slightly lower price point. But because the knock-off manufacturers and sellers enjoy such a substantial cost advantage, they can reap enormous profits. So long as there is a substantial profit potential, the knock-off industry will continue to flourish.

Uncontrolled Exports to the US

Recently, LNC has observed a new sales model where knock-off sellers distribute products directly to US consumers in small quantities and oftentimes in individual packages. In the past, sellers would acquire products in large, typically container size, quantities. The

containers would be shipped to the US through conventional channels that were subject to US Customs and Border Control supervision. While it was a challenge to stop knock-off products at the border, it was possible if the manufacturer was known. Now, with the proliferation of online retail outlets, knock-off sellers, whether they are manufactures or re-sellers, can ship directly to US consumers from locations outside the US. LNC has observed knock-off shipments delivered via the national postal service, UPS and freight consolidators. The shipping companies do not provide detailed shipper information and the packaging typically does not include either a valid or direct return address. Generally, there is no indication on the packaging identifying the goods or the seller.

Online Retailers & Electronic Flea Markets

Online retailers such as Amazon have two selling models. In one model, the online retailers buy products from the manufacturers and resell those products online for their own accounts. In these instances, the online retailers are acting conventionally. In the second model, the online retailers acts as a service provider making available to third parties an online storefront where the third party seller can for the

most part sell whatever it wants. The service provider generally integrates third party sellers into its payment and delivery systems but claims it does not direct the activity of the seller or have any control over what is offered for sale. In this model, the service provider is acting like the owner of a digital flea market. It does not appear that the service providers exercise any supervision over who sets up the online storefront or whether those sellers comply with US laws and regulations and aside from blocking an offending storefront on occasion, no other remedial action is available.

Intellectual Property (IP) Infringement

The United States offers strong protection for patents, trademarks and copyrights. LNC takes advantage of all these forms of IP protection and has obtained numerous utility patents for its innovations both in the United States and throughout the world. LNC has also obtained design patents for its unique and attractive product designs. For its trademarks, LNC relies primarily on its common law rights but has registered its NUBY brand in the US and throughout the world. LNC also enjoys copyright protection for its graphical and sculptural works.

The knock-off products will typically violate LNC's patents and copyrights as well as its trade dress rights in its unique and popular product configurations. The knock-off sellers will also use LNC's trademarks in promoting and advertising the knock-off products. A particularly pernicious form of trademark infringement is the use of LNC trademarks in ad word purchases from search engine providers such as Google and Bing. In this situation, in response to a consumer performing an online search using an LNC product name, an advertisement is placed at the top of the search results with a link to the knock-off seller's online store. The ad typically makes it appear that the source of the product is the actual brand owner. If the consumer clicks on the ad, he or she is connected to the knock-off seller's online store or website where the consumer can purchase the knock-off item. In some instances, the knock-off seller will use copies of LNC photographs and other promotional materials, in direct violation of LNC's copyrights, in advertising the knock-off product.

Non-Compliance with US Health & Safety Regulations

The US Food & Drug Administration and the Consumer Products Safety Commission provide various regulations governing certain

aspects of the manufacture and sale of products directed at children and infants.² For example, products that are likely to be put into the mouth of a child or infant, such as pacifiers, must meet specific size requirements to avoid creating a choking hazard. LNC uses extreme care in the design and manufacture of its products to assure that they meet all applicable standards. LNC has seen products from third party sellers that do not meet these US health and safety requirements. While these products are typically not exact knock-offs of LNC products they still constitute unfair competition to the extent these third-party sellers do not incur the expense of compliance. LNC invests substantial resources in complying with health and safety regulations, an expense that must be recovered as part of the cost of the product. Non-compliant third-party sellers do not incur these costs and enjoy an inherent cost advantage over LNC. Not only is LNC being directly damaged by the sale of these non-compliant products, but they put US consumers – infants and children – at risk.

² Examples of regulations governing the design and manufacture of baby products include: 16 CFR 1500 (hazardous substances and articles), 16 CFR 1501 (small part), 16 CFR 1510 (rattle), 16 CFR 1511 (pacifier), mandatory toy standard ASTM F963, Battery Act, PL 104-142, 16 CFR 1303 (lead in surface coatings), 16 CFR 1307 (phthalates), 21 CFR 170 through 189 (food contact materials), 21 CFR 177.1580 (BPA-based PC resins), FDA Policy Guide section 500.450 (baby bottle nipple) and The Model Toxics in Packaging Legislation.

Choking Hazards

There are regulations governing the size of objects that are targeted for children and infants and especially for objects that will be chewed or put into the mouth. There are governing regulations that specify, for example, that pacifiers must meet minimum size requirements. It is also important that items such as nipples, pacifiers and teethers be constructed of materials that are strong enough to resist separation in the mouth. If a nipple were to be detached from its base it could pose a serious choking hazard. LNC meets these regulations by carefully designing its products to meet these regulations and supervising its manufacturers to ensure that they comply with all US health and safety laws and regulations as well as LNC's strenuous quality controls. Knock-off manufacturers often use inferior plastics and add fillers to cut costs that weaken the materials. LNC has observed nipple separation in knock-off products that can pose serious choking hazards. To the extent foreign manufacturers and knock-off sellers attempt to modify LNC designs to avoid copying, they may not comply with the size regulations. LNC has observed undersized

pacifiers that could pose choking hazards. Where manufacturers and sellers can sell into the US marketplace with impunity, it encourages aggressive cost cutting and one of the first costs to be cut is compliance with health and safety regulations resulting in the distribution and sale of unsafe products to US consumers.

Strangulation Hazards

Another regulation relates to the size of loops for products such as lanyards and other items. An item to be used with a child or infant cannot have a loop that would fit over the head that might result in a strangulation hazard. This is especially problematic with adjustable loops that must have stops or other devices to prevent the loop from being too large. LNC has observed products with loops that are both too large and have ineffective stops.

Teether Regulations

Teethers are governed under the FDA as dental devices. The FDA regulations require that all manufacturing facilities used in the manufacture of dental devices be registered and approved by the FDA. LNC has invested substantial resources of time and money to qualify its manufacturing facilities. FDA regulations require that the approved

facility be listed on the packaging and that the manufacturer be listed on an FDA database. LNC has observed teether products that do not identify an authorized manufacturing facility on the packaging and do not have any manufacturing facilities listed on the FDA database leading it to believe these products were made in unapproved facilities. These unscrupulous manufacturers and sellers are distributing and selling potentially unsafe products to US consumers.

Outlawed Materials

Various federal and state regulators have identified certain materials that they deem to be potentially harmful and should not be used in the manufacture of baby products. LNC designs and specifies that its products must be free of these materials and invests substantial resources in supervising its manufacturers and testing their products to ensure that no harmful materials are ever used in LNC products. LNC has observed that many knock-off manufacturers and sellers are distributing and selling products that include one or more of these banned substances. In many instances, the packaging claims that the product is free of these materials. In those cases, not only are potentially

harmful products being distributed and sold to US consumer, but they are also being lied to in false advertising and promotion.

Inadequate Judicial Remedies

Foreign manufactures and sellers take advantage of US judicial procedures and treaties to avoid prosecution in US Courts. One strategy employed by the knock-off sellers is to obfuscate and hide behind false or anonymous identities. In order to bring a direct action in US courts, there must be personal jurisdiction over the defendant. Personal jurisdiction is obtained by serving a summons and complaint on the named defendant or its agent for service of process. To serve the summons and complaint, a physical address is needed. Many, if not most, online sellers use identities that are unrelated to the real party in interest. In almost every case, the online seller does not provide a physical address or contact information. When the sellers identify is actually revealed, it is often an address in a remote part of China that upon further investigation turns out to be false. Even when an identity is revealed, and a true address located, US plaintiffs are required to serve Chinese entities under the Hague Convention. Under normal circumstances service of process under the Hague Convention in China

takes on the order of nine months. Since 2015, China has refused to complete the service of process requested by US Courts leaving US plaintiffs with any ability to serve Chinese defendants. Without complete service there is no personal jurisdiction and the US court cannot act. In the event service on the foreign defendant is completed and the defendant fails to appear, the plaintiff brand owner can obtain a default judgment that may be used to remove the knock-off defendant from an online store hosted by an online service provider. Even if the US plaintiff employs alternative service by Court order and obtains a default judgment, China refuses to honor those judgments leaving the US plaintiff with no direct remedy against the violator.

As explained below, blocking a specific knock-off online seller does not solve the problem as the knock-off seller simply continues selling the knock-off products under another name in a different online store. As the entire process of filing the complaint, completing service of process and seeking a default judgment can take upwards of a year, the plaintiff brand owner is forced to suffer additional damages with little to no likelihood of ever receiving compensation.

Inadequate Customs & Border Patrol Remedies

The US Customs & Border Patrol appear to be unprepared for dealing with a distribution model that relies on small package shipments into the US. It has always been difficult to stop shipments at the border due to the many ports of entry and the volume of shipments into the US. Typically, US Customs requires the rights owner to identify the port of entry and the vessel carrying the knock-off products. Since most of the knock-off manufacturers do one-off products or small runs, by the time the brand owner learns of the knock-off the goods are already in the US. When shipments are in smaller quantities or in individual packages, it is almost impossible for the US Customs authorities to interdict the knock-off packages. This problem is further exacerbated by the fact the actual seller/shipper is unknown to the brand owner. These inadequacies in the judicial and customs systems leave the only remedy with some private action against the service provider for the online seller.

Online Takedowns are Not the Solution

While the online service providers do provide some relief for rights owners, that relief is very limited and does not address violations

of US health and safety regulations. First, online service providers will only grant relief to rights owners that have federally registered trademarks and copyrights.³ Second, no relief is provided to common law trademark owners. Third, the takedown process is automated and subject to the vagaries of technology. While online retailers do provide procedures for escalating takedown requests, that escalation procedure adds delay and a degree of subjectivity to the process. And to the extent that relief is provided it is merely limited to blocking the online seller. Even if the knock-off seller is blocked, there is no mechanism in place to prevent that seller from setting up a new online store with a different name selling the same knock-off goods. Finally, takedown procedures are not designed to address violations of health and safety regulations. Direct action against the online service provider is difficult as US law requires notice and cases have held that the service provider is not liable for the actions of independent third parties.

Conclusion

International unfair competition through the sale of counterfeit and pirated products has been dramatically increased by the

³ While technically a patent owner can use the takedown process, in most cases the online retailer is not willing to go through the process of confirming infringement absent a court order or judgment of infringement.

combination of unrestricted online retailers and an open unregulated boarder that permits counterfeiters and pirates to directly ship to consumers in the US their counterfeit and pirated products. A growing concern involves sales of knock-off products from third party sellers who acquire and ship small quantity lots and individual packages from foreign locations to US consumers completely bypassing US laws and regulations relating to intellectual property, product health and safety requirements and without paying state and local taxes.

Respectfully submitted this 7th day of May 2018.

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