

Counterfeiting in Our Own Backyard

By Daniel A. Schnapp and Barri A. Frankfurter

I. Introduction

The United States economy loses between \$200 billion and \$250 billion each year as a result of counterfeiting and piracy.¹ Counterfeiting, which can be generally described as the creation of a product, often of inferior quality, using a trademark that is virtually indistinguishable from a registered trademark without approval, is a substantial threat to brands worldwide.² Companies that own the intellectual property rights associated with products, as well as consumers who use those products, have a significant interest in identifying counterfeit goods and preventing their sale because, among other things, the consumption of counterfeit goods can pose a serious threat to public health and safety.

Fake handbags and electronics are no longer the sole target of counterfeiters; infringers are also seeking to replicate pharmaceutical, food and beverage products, which presents a greater chance of harm to companies and consumers alike. Clearly, this presents an even greater threat to consumers, as these counterfeit products are not manufactured in accordance with quality control standards set by organizations like the Food and Drug Administration. Likewise, counterfeit goods are no longer solely manufactured abroad. Owners of trademarks and copyrights must also keep watch for counterfeit goods manufactured right here in the United States.

II. Case Study

Recently, Living Essential LLC, the owner, manufacturer and distributor of 5-hour ENERGY, was subject to a severe counterfeiting scam in which counterfeit 5-hour ENERGY was manufactured and sold within the United States.

A. Background Facts³

Living Essentials maintains a facility in Wabash, Indiana where it manufactures authentic 5-hour ENERGY using strict quality control standards. Living Essentials then sells 5-hour ENERGY directly or through independent brokers across the United States. In an effort to distribute 5-hour ENERGY in Mexico, Living Essentials partnered with Baja Exporting LLC and created Spanish-language labels and packaging to facilitate an entry into the Mexican market. Living Essentials sold 5-hour ENERGY to Baja Exporting LLC at a discounted price from what it charges distributors within the United States. Contrary to the agreement with Living Essentials, Baja Exporting LLC attempted to sell the 5-hour ENERGY, intended for distribution in Mexico, in the United

States at American prices. Sales in the United States were proving difficult, however, as a result of the Spanish-language labels on the 5-hour ENERGY intended for sale in Mexico. Accordingly, to facilitate this improper conduct, Baja Exporting LLC swapped out the Spanish-language labels with English-language labels with the assistance of a company named Midwest Wholesale Distributors.

To take the scam even further, “Tri Mex,” an affiliate of Midwest Wholesale Distributors, ordered counterfeit English-language 5-hour ENERGY display boxes. Midwest Wholesale Distributors also ordered counterfeit 5-hour ENERGY labels to shrink-wrap onto authentic 5-hour ENERGY bottles that were intended for distribution in Mexico. Then, Baja Exporting LLC and Midwest Wholesale Distributors contacted Advanced Nutraceu-tical Manufacturing LLC in an effort to find a manufacturer of bottles and caps that would contain the running man logo found on authentic 5-hour ENERGY bottles. Not only did Advanced Nutraceu-tical Manufacturing LLC find a manufacturer that could make the counterfeit bottles and caps, but it also filled those bottles with counterfeit 5-hour ENERGY and delivered cases of the product, in the amount of 75,000 bottles per day, to Midwest Wholesale Distributors’ facility in California. The fake 5-hour ENERGY was brewed, labeled and packaged in a factory in San Diego, California. Ultimately, millions of counterfeit bottles of 5-hour ENERGY were sold to distributors in California, Florida, Illinois, Michigan, Pennsylvania and Texas.

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Living Essentials was finally alerted to this scheme when a salesperson for Paramount Sales, an independent broker, noticed that Pitco Foods, one of the major purchasers of 5-hour ENERGY, stopped placing orders. Living Essentials conducted an investigation and obtained a box of 5-hour ENERGY from Pitco Foods and inspected the product. Living Essentials determined that the 5-hour ENERGY was counterfeit and noted that the counterfeit

bottles and caps were slightly different from the authentic bottles and caps, and the color, taste and smell of the counterfeit 5-hour ENERGY was not the same as the authentic 5-hour ENERGY. Living Essentials immediately retained private investigators and sent them to visit retail locations across the United States to inspect and quarantine the counterfeit 5-hour ENERGY. Ultimately, the private investigators confiscated over 2.6 million counterfeit bottles of 5-hour ENERGY and stored them in facilities located in California and New Jersey.

B. The Court's Decision

After the investigation, on October 25, 2015, Living Essentials initiated an action titled *Innovation Ventures, LLC, Living Essentials, LLC and International IP Holdings, LLC v. Ultimate One Distributing Corp., et al.*, in the United States District Court, Eastern District of New York against twenty separate defendants, including Baja Exporting LLC, Midwest Wholesale Distributors and Advanced Nutraceutical Manufacturing LLC. Living Essentials alleged that the defendants violated the Lanham Act, the Copyright Act of 1976 and New York state law and common law. Likewise, agents of the Federal Bureau of Investigation and Food and Drug Administration arrested a number of people in June 2015 and charged them with conspiracy to traffic in counterfeit goods, conspiracy to commit criminal copyright infringement and conspiracy to introduce misbranded food into interstate commerce stemming from the illegal distribution of the counterfeit 5-hour ENERGY.⁴ Ultimately, United States District Judge Kiyo A. Matsumoto handed Living Essentials complete victory by summary judgment to the tune of a \$20 million judgment, plus attorneys' fees and the cost of the investigation.

III. Practical Guidelines

A. Counterfeit Goods Can Be Manufactured in the United States

This case serves very important lessons for owners of trademarks on a going forward basis. First, companies need to be cognizant of the fact that it is possible for infringers to manufacture and distribute counterfeit goods directly in the United States. In the 5-hour ENERGY case, the counterfeit 5-hour ENERGY bottles were made and distributed from a facility in San Diego, California. What started as a scam to sell authentic 5-hour ENERGY intended for distribution in Mexico in the United States for a profit, quickly turned into something more sinister. The infringers were manufacturing the counterfeit 5-hour ENERGY without any quality control standards and then passing the product to distributors for sale to consumers.

B. Utilize Your Distributors and Sales Forces to Catch Infringers

Second, companies should utilize their distributors and sales forces to catch infringers and should also pay careful attention to ordering patterns. In the 5-hour ENERGY case, a salesperson for an independent broker uncovered the scheme because that salesperson was diligent in noticing an abnormal ordering pattern for a large buyer. In actuality, that large buyer had purchased counterfeit 5-hour ENERGY and was selling that to consumers instead of authentic 5-hour ENERGY. If the salesperson had failed to recognize the change in pattern, the scheme may have gone unnoticed for a longer period of time, which would have caused greater damage to Living Essentials and the consumers of 5-hour ENERGY.

C. Act Quickly

Additionally, if a company determines that counterfeit products are being distributed to consumers, the company should act quickly. Once Living Essentials established that counterfeit 5-hour ENERGY was available for sale to consumers, Living Essentials acted immediately to remove the counterfeit product from circulation by hiring a private investigator. The private investigator inspected and pulled counterfeit 5-hour ENERGY from the shelves of stores and was ultimately successful in seizing millions of bottles of counterfeit 5-hour ENERGY. The private investigator also assisted Living Essentials with identifying the chain-of-custody of the counterfeit bottles, which enabled Living Essentials to build a case against the infringers.

D. Use Distinct Product Packaging

Finally, the use of distinct product packaging will help protect brands from counterfeiters. Although the counterfeit bottles of 5-hour ENERGY were nearly identical to authentic 5-hour ENERGY, one of the factors that enabled Living Essentials to determine that the bottles were, in fact, counterfeit, was slight differences in the bottle design. Specifically, Living Essentials noted that the counterfeit bottles were slightly shorter than the authentic bottles, the caps of the counterfeit bottles lacked a "pimple" on top, which is found on the authentic bottles, and the "Running Man" logo that is featured on the caps of authentic 5-hour ENERGY had a different silhouette on the counterfeit bottles. Similarly, these distinctions in product packaging made it difficult for the counterfeiters to actually manufacture the counterfeit bottles of 5-hour ENERGY at the outset. The "Running Man" logo alone forced the counterfeiters to travel to Mexico and hire two Mexican companies to have the caps of the counterfeit bottles printed with the logo. Had Living Essentials not used this distinctive mark on its product, 5-hour ENERGY would have been easier to counterfeit.

IV. Conclusion

Accordingly, companies should be aware that counterfeit goods can, and are, manufactured within the United States. Although distinct product packaging can help avoid infringement to a degree, it cannot prevent it completely. If a company determines that counterfeit versions of its products are being sold to consumers, it should act quickly to rectify the situation to minimize the harm to itself and consumers.

Endnotes

1. "What Are Counterfeiting and Piracy Costing the American Economy?" U.S. Chamber of Commerce, www.uschamber.com.
2. <http://www.inta.org/TrademarkBasics/FactSheets/Pages/Counterfeiting.aspx>.
3. A full recitation of the background facts can be found in the court's summary judgment opinion. See *Innovation Ventures, LLC*,

Living Essentials, LLC and International IP Holdings, LLC, 12 CV-5354 (KAM), 2016 WL 1273232 (EDNY March 31, 2016).

4. See *United States v. Shayota*, Case No. 15-CR-00264 (ND Cal. 2016), see also <https://www.justice.gov/usao-ndca/pr/eleven-defendants-charged-nationwide-conspiracy-manufacture-and-distribute-counterfeit>.

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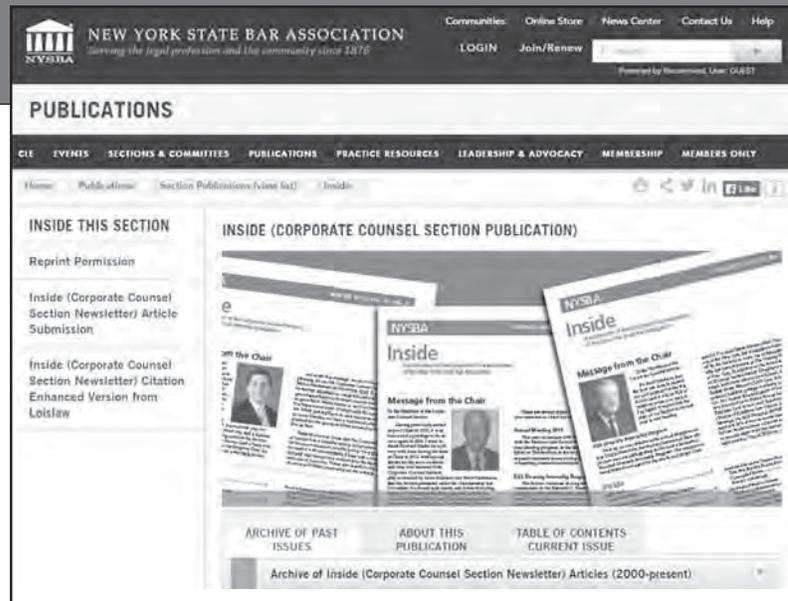
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