

Chinese banks a haven for web counterfeits

May 8 2015, by Erika Kinetz



This Saturday, April 11, 2015 photo shows a counterfeit Tiffany & Co., website on a computer monitor in Beijing. In 2014, Tiffany sued to shut at least 199 new counterfeiting websites, but another generation of copycats has already sprung up. (AP Photo/Ng Han Guan)

Kim Sbarcea knew exactly what she wanted. She typed "Tiffany Elsa Peretti mesh earrings" into Google and scrolled through impeccable photos of the delicate \$450 diamond-shaped earrings until she chanced upon a pair for—deal of deals!—\$32.

The website, tiffany-outletsale.com, looked legit and Sbarcea assumed Tiffany & Co. would not let an unauthorized site use its name. Besides, she could pay by credit card.

She hit the buy button.

In that instant, on a Saturday morning in 2011, Sbarcea's \$32 was sucked from the living room of her house in Christchurch, New Zealand, into the global counterfeiting market. The money trail left by counterfeiters almost always leads to China, where banks have emerged as key conduits in an illegal industry that by one estimate is expected to be worth \$1.8 trillion this year.

At least three prominent Chinese banks serve as safe havens for counterfeiters, who use them to process credit card payments for fakes or move their money around the globe, The Associated Press has found. A review of hundreds of pages of court documents from cases in the United States and China—along with interviews with lawyers, investigators, government officials and industry representatives—shows that a lack of legal cooperation between the West and China is allowing counterfeiters to use Chinese banks as financial shelters.

Recent attempts by U.S. and European companies to follow counterfeiters' money into China have hit a wall, frustrating efforts to deal a more decisive blow to the global trade in fakes, which has endured despite years of raids.

Five lawsuits filed in the U.S. against counterfeiters reveal a pattern to how they use Chinese banks to move money beyond the reach of U.S. law enforcement. Counterfeiters sold fakes online in the U.S., using credit cards or PayPal to process payments. Then, records show, they transferred millions of dollars in illicit earnings to accounts at two of China's largest state-owned banks, the Bank of China and the Industrial

and Commercial Bank of China—as well as the smaller China Merchants Bank.

The banks do not dispute that the accused counterfeiters held accounts at their branches, but they refuse to comply with U.S. court orders to disclose information or freeze the funds, saying that would violate Chinese bank secrecy laws. They say they do not support counterfeiting, have broken no laws and are caught in a jurisdictional dispute between China and the U.S.

Tiffany & Co. seeks \$58.5 million in damages in a New York federal court from an online counterfeiting ring that spans three continents. Tiffany said it traced PayPal transfers to five accounts at the Bank of China, ICBC and China Merchants Bank, and also found that the Bank of China was processing credit card payments for one defendant. A Latvian bank handed over details about the illicit money flows, but the Bank of China refused to cooperate, U.S. court documents show.



In this Wednesday, April 8, 2015 photo, customers walk near a shop selling refurbished or second hand items from brands such as Gucci, Chanel and Cartier at the Silk Street market in Beijing. (AP Photo/Ng Han Guan)

Gucci seeks \$12 million in damages in a New York federal court from a counterfeiting ring it says sold millions worth of fake handbags and wallets to U.S. consumers. Using records provided by JPMorganChase, Gucci traced \$530,000 in transfers from counterfeiters in the U.S. to Bank of China accounts. But the Chinese bank refused to freeze those funds for Gucci—instead it secretly froze over \$890,000 of the accused counterfeiters' money to cover its own legal costs in the fight with Gucci, Chinese court documents show.

Two more lawsuits were filed by the U.S. Justice Department, which traced millions of dollars in online sales of counterfeit sports jerseys to Bank of China and ICBC accounts in China. Tiffany filed a fifth lawsuit against another group of counterfeiters.

It's not surprising that Chinese banks would be a natural choice for counterfeiters: According to the latest U.S. Department of Homeland Security data, nearly nine out of every 10 fakes seized at U.S. borders come from China or Hong Kong.



In this Wednesday, April 8, 2015 photo, customers look at products in a shop selling refurbished or second-hand items from brands such as Gucci, Chanel and Cartier at the Silk Street market in Beijing. Gucci has won at least three cases against counterfeiters in Chinese courts since 2008, but was awarded a combined total of only 650,000 yuan (\$104,560) in damages. (AP Photo/Ng Han Guan)

'HEIGHT OF HYPOCRISY'

In the past, Chinese banks have released information about accounts in China in response to some U.S. court orders, but cooperation was inconsistent. Now China's banks, regulators, courts and diplomats are delivering one message: Bank secrecy is a matter of national sovereignty.

In a May 2013 letter, the Chinese Embassy in Washington complained to the U.S. State Department about subpoenas served "time and again"

demanding that Chinese banks release information about accounts in China and freeze assets held there. The embassy wrote that such demands amounted to "wrongful acts that disrespect China's sovereignty and laws." Chinese regulators later warned that the issue could "undermine" Chinese-American relations.

The usefulness of Chinese banking records is clear. In one case, U.S. lawyers used transaction information from a Shanghai bank account produced on the order of a New York court to help crack a network that shipped counterfeit blood glucose test kits for diabetics, which the FDA said could cause "serious injury or death," to 600 U.S. pharmacies.



In this Friday, March 6, 2015 photo, pedestrians walk past a shopping mall selling luxury brands in Beijing. Use of the Internet has made it harder to fight counterfeiting using traditional methods, such as seizing containers of fake goods at ports. Modern counterfeiters sell direct to consumers and ship merchandise in small packages and create complex financial and logistical structures that are tough to untangle. (AP Photo/Ng Han Guan)

"I've had repeated cooperation from Chinese banks, but I can't tell you if I'd get it today," said Geoffrey Potter, a partner at New York's Patterson Belknap Webb & Tyler law firm. "Either it's against the law or it's not. Now they've taken this public position, they'll probably have to be consistent."

Banks have become more vigilant about protecting customer data—even within China—since 2010, when China's consumer protection law was broadened to include financial clients, said Zheng Junguo, an associate professor at China University of Political Science and Law in Beijing.

"If there is some leakage, customers will no longer trust them," she said.

China's top leadership has begun to take intellectual property protection seriously as it steers the country's economy away from low-end manufacturing toward innovation. But Beijing seems to want the legal fight against counterfeiting waged on its own terms and in its own courts, which many critics say are not yet up to the task. Banking information can be obtained by filing a lawsuit in China, but Chinese courts are reluctant to order the release of detailed account records, three intellectual property lawyers in China said. Another option is to make a request through the Hague Convention, which critics dismiss as too cumbersome.



In this March 11, 2015 photo, counterfeit branded bags appear on display in a room hidden from the public area of a popular shopping mall in Beijing. A review of hundreds of pages of court documents from cases in the United States and China, along with interviews with lawyers, investigators, government officials and industry representatives, show that a lack of legal cooperation between the West and China is allowing counterfeiters to use Chinese banks as financial shelters. (AP Photo/Mark Schiefelbein)

The U.S. also restricts the flow of financial information, but does facilitate access to evidence for lawsuits anywhere in the world. A U.S. judge can order a bank to hand over account details, without a lengthy lawsuit. The U.K., Hong Kong and Singapore have similar provisions to ease access to evidence that can help fight transnational crime, lawyers said. China does not.

"Why should the Bank of China have some sort of competitive advantage that counterfeiters can use their bank and shield their assets, whereas if they had people doing banking with Chase, Chase would turn it over?" Gucci's lawyer, Robert Weigel, asked a U.S. judge in 2011, according to a court transcript.



In this March 17, 2015 photo, Rui Wenbiao, acting director of the intellectual property division at Shanghai's High Court takes part in an interview in Shanghai. Rui said foreign companies have successfully used China's courts to fight counterfeiting, winning 90 percent of the intellectual property cases they filed in a Shanghai court in the last five years. Intellectual property protection, he said, "has already become an inherent part of our country's requirements." (AP Photo/Paul Traynor)

"I think the reason is because China is a sovereign country," U.S. District Judge Richard Sullivan responded. "Congress could fix it if they wanted

to, right, by just saying we're not going to allow this to happen, we recognize China is a safe haven for fraudsters on a massive scale and we're not going to stand for their bank secrecy laws."

China's drive for secrecy comes at a delicate time for Beijing, which is lobbying Western governments to help chase down tens of billions in stolen funds it says corrupt Chinese officials have stashed overseas, including in the U.S. President Xi Jinping's sweeping anti-graft drive is a top priority for the Communist Party, which has disciplined over 100,000 officials for corruption.

"It's the height of hypocrisy," said Robert Barchiesi, the president of the International Anti-Counterfeiting Coalition.



In this Saturday, March 7, 2015 photo, a woman waits in front of the headquarters of the Bank of China as security guards patrol the building in

Beijing. At least three prominent Chinese banks, including the Bank of China, serve as safe havens for counterfeiters, who use them to process credit card payments for fakes or move their money around the globe, The Associated Press has found. (AP Photo/Ng Han Guan)

'EXPLOSION OF COUNTERFEITING'

Kim Sbarcea (SE-BAR-CHA) didn't know it, but five days before she bought her earrings, Tiffany filed a lawsuit to shut down the bogus Tiffany outlet site, along with 222 others.

It was one of what Tiffany's lawyers described as a massive number of lawsuits filed in the wake of an "explosion of counterfeiting over the Internet."

That explosion has made it harder to fight counterfeiting using traditional methods, such as seizing containers of fake goods at ports. Modern counterfeiters sell direct to consumers and ship merchandise in small packages, one pair of earrings at a time. They create complex financial and logistical structures that are tough to untangle.

The ongoing Tiffany case, for example, involves websites registered in Denmark, Latvia, Cyprus, the U.K. and Hong Kong. Defendants include a man with addresses in two countries, as well as six Chinese and one Russian with no known addresses. Credit card payments were routed through layers of websites and processed by Latvian and Chinese banks, according to court documents.



In this Monday, March 23, 2015 photo, a man carries a child past the Shanghai High People's Court. Foreign companies have successfully used China's courts, winning 90 percent of the intellectual property cases they filed in a Shanghai court over the last five years, according to Rui Wenbiao, an intellectual property judge. But these efforts remain orders of magnitude smaller than the problem, numbers show. (AP Photo/Ng Han Guan)

"That's an almost impossible structure to crack unless enforcement bodies are willing to talk to each other and share information," said Douglas Clark, an intellectual property lawyer at Hong Kong's Gilt Chambers.

Nearly all the banks used by global counterfeiters to move money are Chinese. Some websites even advertise their links with Chinese banks, according to the International Anti-Counterfeiting Coalition, a non-profit industry group whose members include Apple Inc., Procter & Gamble, Tiffany & Co., and 21st Century Fox.

"We've found over the years that 90 percent plus of those banks reside in China," Barchiesi said, adding that Chinese banks have faced "significant fines" from credit card companies because of their efforts.

The coalition said it has helped shut down over 4,900 accounts used to process payments for more than 200,000 websites selling counterfeit goods since 2012. IACC records of account closures show that not just the Bank of China, but also two other state-controlled banking giants—the Bank of Communications and the Agricultural Bank of China—have processed credit card payments for counterfeiters.

MasterCard requires banks that process payments to make sure their merchants are legitimate and watch for signs of irregular activity. If banks don't do adequate monitoring, they can be fined.



In this March 24, 2015 photo, people walk up stairs next to a sign reading "Shanghai Intellectual Property Court" in Shanghai. As China seeks growth from innovation, intellectual property protection has become more important to its top leadership. China opened three intellectual property courts late last year, symbols of a growing commitment to fight counterfeiting that has been felt as far away as Washington. (AP Photo/Paul Traynor)

Barry Wong, head of customer security for MasterCard in Asia, would not disclose what fines have been levied against Chinese banks, but said Chinese banks facilitate sales of more counterfeit products than banks

anywhere else in Asia. "Whether they facilitate with the conscious realization that this money came from selling counterfeit products is something you can't tell," he said.

Visa said in an email that the company is "committed to ridding our payment system of merchants that engage in illegal transactions."

The IACC's Barchiesi said counterfeiting would be significantly reduced if Chinese banks would do the due diligence Visa and MasterCard require. Instead, he said, Chinese banking executives at a meeting in Beijing asked him for a reward for rooting out counterfeiters.

"I said the reward you get is you get to keep a merchant account and transact for Visa or MasterCard," he said. "You want a bounty now?"

The banks, all of which have U.S. branches, say they are committed to the fight against counterfeiting, but must prioritize Chinese laws. The Bank of China said in an emailed response that U.S. lawsuits had put it in an "impossible position," caught between "U.S. court orders that compel BOC to freeze, turn over or disclose information about bank accounts in China, and Chinese law, which requires the bank not to freeze or turn over accounts in China."

The banks told AP that they actively cooperate with Chinese regulations and Hague convention requests, and punish counterfeiters caught using their payment processing systems. They deny or claim no knowledge of counterfeiting-related fines levied by Visa or MasterCard.

"We are resolutely against making or selling any counterfeit goods," ICBC said in an email. "We are fully willing to cooperate under a legal framework with all parties to take strong action."

PayPal told AP that it doesn't condone its service being used to violate

intellectual property rights.

"As a leader in global online payments, PayPal is helping Chinese merchants understand the importance of respecting intellectual property in order to create sustainable international growth," the company said in a statement.

American courts remain undecided about how much jurisdiction they should claim over foreign banks that have U.S. branches. Some fear forcing disclosures could diminish New York's appeal as a global banking hub.

In the Tiffany case, a U.S. District Court judge told the Bank of China, ICBC and China Merchants Bank to freeze defendants' assets and ordered the Bank of China to hand over account details.



In this Saturday, March 7, 2015 photo, paramilitary police patrol near the

headquarters of the Bank of China in Beijing. A review of hundreds of pages of court documents from cases in the United States and China, along with interviews with lawyers, investigators, government officials and industry representatives, show that a lack of legal cooperation between the West and China is allowing counterfeiters to use Chinese banks as financial shelters. (AP Photo/Ng Han Guan)

In the Gucci lawsuit, a judge in New York's Southern District found the Bank of China in contempt when it refused to provide account information and freeze defendants' assets. He ordered the bank to pay \$75,000, plus \$10,000 for each day it failed to comply, but those fees were overturned on appeal as too punitive.

Appeals court judges, echoing an opinion from the U.S. Department of Justice, said the lower courts' rulings on the Tiffany and Gucci cases should have more carefully considered whether it's fair to force Chinese banks to take actions that are illegal in China. The verdict was widely seen as a victory for Chinese banks. Gucci, Tiffany and their lawyers declined to comment on the ongoing litigation.

THE CHINESE WAY

In New Zealand, Sbarcea's earrings arrived in the mail in a Tiffany-blue box that was, on second glance, not quite the right shade. Inside was a cheap plastic container with a pair of earrings that didn't look much like the Elsa Perettis she wanted. They felt, she said, as if they were made of tin.

Sbarcea fired off a barrage of angry emails. She refused to return the

earrings at her own expense, as the company demanded, and instead fought for a refund of the \$11 shipping fee, which was supposed to be free.

"Well people, it's embarrassing to admit this, but—I've been the victim of a very shoddy Chinese company," she wrote on her blog a few weeks later. "I am soooooooooooooo annoyed."

In China, the fight against fakes has been heating up. Three intellectual property courts that opened late last year are symbols of the growing commitment to protection, which is becoming a more important issue as Chinese companies begin to innovate.

Foreign companies have successfully used China's courts, winning 90 percent of intellectual property cases they filed in a Shanghai court over the last five years, according to Rui Wenbiao, a judge. But these efforts remain orders of magnitude smaller than the problem, records show.

In 2013, for example, Chinese courts heard nearly 27,000 trademark cases, almost three times as many as in 2010, according to data from China's Supreme Court. Chinese regulators investigated 56,867 trademark cases that same year, according to public data. Contrast that with figures from Chinese e-commerce giant Alibaba, which said it took down 90 million fake items in the first nine months of last year alone.

Critics say corruption, protectionism, weak enforcement and the Communist Party's control of courts complicate the fight against counterfeiting. Chinese judgments also remain small—the maximum award in a copyright infringement case is about \$80,000—and hard to collect.



In this Wednesday, April 8, 2015 photo, Chinese shop owners and government officials officiate at a ceremony to crack down on fake products outside the Silk Street market in Beijing. The words in Chinese read: "Zero tolerance." China's top leadership has begun to take intellectual property protection seriously as it steers the economy away from low-end manufacturing toward innovation, but many critics say its courts are not yet up to the task. (AP Photo/Ng Han Guan)

Trying to use U.S. courts to pursue counterfeiters in China— as Gucci and Tiffany and even the U.S. government have done— is "an appropriate response to an uncooperative and obtuse system that isn't permitting you to cost-effectively hit the counterfeiters where they live," said Dan Plane, an intellectual property lawyer at Simone IP Services in Hong Kong.

Gucci has won at least three cases against counterfeiters in Chinese courts since 2008, but was awarded a combined total of only 650,000 yuan (\$104,760) in damages. One lawsuit was against a notorious

counterfeiting market in Beijing, which still sells fake Gucci today.

In June 2010, Gucci tried a different approach. Along with other brands belonging to France's Kering Group, the company filed a lawsuit in New York against 10 people it said operated six websites that sold more than \$2 million dollars' worth of fake handbags and wallets to U.S. customers.



In this Saturday, March 14, 2015 photo, a sign at the Silk Street market in Beijing warns customers of fake products. Use of the Internet has made it harder to fight counterfeiting using traditional methods, such as seizing containers of fake goods at ports. Modern counterfeiters sell direct to consumers and ship merchandise in small packages and create complex financial and logistical structures that are tough to untangle. (AP Photo/Mark Schiefelbein)

The counterfeiters shipped merchandise from China to a house in San

Diego, where they repackaged it and tried to pass it off as genuine, according to Gucci's lawyer. They even bought ads from Google, so their websites would appear at the top of search results for terms like "Gucci handbags," according to court documents.

Gucci tracked \$530,000 in transfers to Bank of China accounts, and a New York judge ordered the bank to freeze the funds.

The bank refused.

Instead, the Bank of China filed its own lawsuit against three of the defendants. In June, a Beijing court ruled in the bank's favor, allowing it to freeze 5,534,595 yuan (\$892,000) of the defendants' assets—not to pay Gucci, but to cover its own legal bills related to the lawsuit.



In this Monday, March 16, 2015 photo, street vendors offer counterfeited products to tourists outside a police post in front of the Silk Street market in

Beijing. China's top leadership has begun to take intellectual property protection seriously as it steers the economy away from low-end manufacturing toward innovation, but many critics say its courts are not yet up to the task. (AP Photo/Ng Han Guan)

Kim Sbarcea never got her money back. Her Elsa Peretti mesh earrings sit forgotten in a closet. "Such rubbish!" she wrote in an email. "Never wore the earrings."

Last year, Tiffany sued to shut at least 199 new counterfeiting websites, but another generation of copycats has already sprung up. There's even a new Tiffany Outlet, a top hit on Google: tiffany.4mshop.com/

It sells a \$9,800 Elsa Peretti Sevillana ring for \$49. And shipping is free.

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