

HBR Case Study

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Can Knockoffs Knock Out Your Business?

Counterfeiting of Ruffin products is on the rise. The company’s CEO is obsessed with putting a stop to it. How far should he go?

SPLINTERS OF WOOD flew in all directions as the battering ram crashed through the bolted warehouse door. The police cordon surrounding the building waited nervously as Hong Kong’s elite special unit swarmed inside, shouting what Ted Dwayne could only imagine was “Put your hands up, or we’ll shoot!” and “Police!” in Cantonese.

As a client-service director for Brand Protection Services Limited, Ted used his nearly 20 years of law-enforcement and private-investigation experience to track down and bring to justice counterfeiters of his clients’ wares. He had been working this particular case for almost a year now and was in Hong Kong to make sure the sting operation, intended to seize literally tons of fakes of his client company’s products, went down without a hitch. Despite the dramatic expansion of the Hong Kong Police’s Commercial Crime Bureau in recent years, the tracking of counterfeiters beyond street-level vendors still required months of work – and, on occasion, some assistance from individuals like Ted.

For this case, Ted had stalked a ring of criminals from a mall bust in northern Georgia, which netted a cache of purses, shoes, and watches worth more than \$10 million on the street, to a labyrinth of tunnels under New York’s Chinatown. From there he had followed the trail to this waterfront warehouse in



Hong Kong, filled to the ceiling with knockoffs of high-quality brands. The police had been especially happy to get Ted’s tip-off because the crates held not only clothing and jewelry but also cosmetics and pharmaceuticals – ersatz products that might threaten people’s health and lives.

The current operation was yet another success, Ted thought as he watched the action from the relative safety of a storefront across the street, but it was just the tip of the dragon’s tail. This wasn’t some third-world machine shop stamping out fake watches so cheap they turned

your wrist green; it was a highly organized global syndicate funding everything from street crime to international terrorism. And, Ted knew, once the tail was cut off it was destined to grow back. In recent years, the number of seizures like this one had increased dramatically around the globe, doubling in the United States, and still the problem seemed to be getting worse, not better.

As the lockdown continued, Ted made his way to a quieter spot a few blocks from the building. It was time to report to the client.

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In Too Deep

Bill Bronson reached for the cell phone on the nightstand in his hotel room. He glanced at the alarm clock: It was 4:20 AM in Dubai. As the CEO of Ruffin – “the world’s leading provider of clothing, accessories, and recreational equipment for today’s explorers” – Bill spent considerable time traveling the globe, so he was used to taking calls in the middle of the night.

“The raid went down,” said the voice on the other end of the line. Bill easily recognized Ted Dwayne’s thick Long Island accent. “The timing was perfect. They got over 100 tons of stuff. A few of the ringleaders, too – a half dozen of them were in cuffs when I left to call you.”

Bill took in the details and hung up elated. It felt satisfying to catch the crooks who’d been ripping off his products – all the more so because his own life had been put in danger by one of the fakes,

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a knockoff of his company’s diving watch, 19 months ago. Even now, Bill could recall the terrible sensation of his near-death experience.

He had been 80 feet below the surface of Subic Bay, exploring the wreck of the *USS New York*, when he had found it nearly impossible to breathe. His watch indicated he had been down no more than 20 minutes, so how could an air supply that would normally last him more than an hour be gone? That’s when he realized the bezel was no longer locked, and the instrument he had thought was his company’s premier dive watch was, in fact, useless. He shot to the surface in desperation and then spent the next three days in and out of a recompression chamber, undergoing hyperbaric oxygen treatment to stave off the sometimes-fatal bends.

Just after his recovery, Bill abruptly fired the Ruffin marketing director who had given him the watch just to see if Bill could recognize it as a knockoff, intending to let Bill in on the joke long be-

fore he could ever actually use the thing. Then Bill hired detectives to find the source of the fake and track down illegal replicas across the company’s entire product line. Finally, he used the publicity surrounding his experience as a bully pulpit for a series of attacks against the trade bureaus, and even governments, of

environment the company was developing. It would include skiing, scuba diving, rapids rafting, surfing, mountain climbing, and motocross – all in the same indoor facility.

Bill easily found Kamil and Nels in the marketplace. As they finished greeting one another, a slight man approached

“The raid went down,” said the investigator. “They got over 100 tons of fakes.”

countries that appeared to tolerate the creation and sale of fake products.

Almost two years later, it *still* nagged at Bill that he had been so easily deceived. As an experienced outdoorsman who had reached the summits of peaks on all seven continents, Bill Bronson was not one to be careless about his equipment. In fact, finding so much of it inadequate had been the reason he had started Ruffin and driven it to become the world’s number one maker of adventure gear and clothing. Had he just gotten careless with age, or was something going on that permitted today’s fakes to fool even someone as demanding as he was?

A Plan to Foil Fakes

No project was too outrageous for Dubai: With more than 35 shopping centers, and a new one being opened seemingly every week, the place was a retailing gold mine – the perfect location for launching Ruffin’s latest marketing and sales campaigns, Bill thought as he moved briskly through the streets of the emirate.

It was several hours after his wake-up call from Hong Kong, and Bill was on his way to the gold souk to meet with Kamil Zafir, the head of Ruffin’s Middle Eastern operations, and Nels Volgren, the company’s design chief. From there, the three would head to a nearby restaurant for a working lunch. Nels was in town to address the technical requirements of the Ruffin-branded adventure and retail

and quietly said, “Watches? Top quality,” and then offered a litany of high-end brand names.

“Get out of here!” Bill snarled. The CEO glared at the quickly disappearing figure. “When are we finally going to be able to do something about this?” he said to Nels and Kamil.

Bill had meant the question rhetorically, but Kamil’s response was quite literal. “You might want to go easy – well, for a little while anyway – on the whole counterfeiting thing,” he began a bit cautiously. “The word is, some important folks here are worried that you might stir things up, like you did in China after the accident. They’ve made a serious effort here to keep copycats out, and if you make trouble, well, I don’t think we’d continue to get the kind of fantastic cooperation we’ve seen on the adventure project so far.” As Kamil’s voice trailed off, the Ruffin managers were again approached – this time by two different street vendors.

Nels saw the CEO’s jaw tighten, and as Kamil made a big show of sending the vendors on their way, the design chief spoke up. “We’ve done a top-to-bottom review of the design of all our products, just like you asked, Bill. Faking them is going to become nearly impossible in the next 12 months,” he assured his boss. “The Ruffin logo will be woven into fabrics, rather than embroidered, and will be laser-etched onto product surfaces



with fine textures that consumers can feel. We're also placing microtags in the plastics we're using to create our products. Special devices can then read the codes in these tags at any point in a product's life cycle." A unique 24-character alphanumeric identifier was also being sewn or etched into each Ruffin product, Nels said, and customers could then enter the code online to verify the product's authenticity. "The odds of guessing a valid number would be astronomical," the designer pointed out.

Bill was impressed – once again, he thought, Ruffin is on the forefront of technology. "It sounds like you took me at my word when I said spare no expense. Are the costs reasonable enough?"

"They're not cheap," the design chief admitted, "but on a per-unit basis we're managing to keep them to a tiny percentage of our retail prices. What is costly is trying to get buy-in from all our relevant business heads, making sure they're all doing the right things, all in the same way."

"We've been doing some simple things," Kamil added, "like performing spot checks on our contractors' raw materials orders. If we find they're ordering too much, we have a pretty good idea they're making extra for the gray or black markets."

Bill was glad to hear this. A study he had commissioned a year ago found that as many as a third of the company's customers had unintentionally purchased a fake version of a Ruffin product. The new technologies would help reduce



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that number, but Bill knew from his capital-budgeting meeting that sooner or later even these approaches would most likely be copied: Ruffin had bought the laser-etching equipment from a high-quality Chinese maker at a very low price, and potential counterfeiters could easily do the same.

Also troubling to Bill was the study's finding that two-thirds of the surveyed consumers were willing to buy a replica of a Ruffin product if the price were right – and would even brag about it to their friends. That's what really kept those guys selling on the street. Granted, two-thirds also said they would not buy fakes if they knew they could serve jail time for it, but would consumers ever face such a reality? It was hard enough prosecuting the folks making and selling the stuff. And after the company had spent years working with – and sometimes suing – online vendors and auction houses to get them to get rid of the fakes, counterfeit sales on the internet were still rampant.

Brand Builder or Spoiler?

Two weeks later, Bill was in Beijing for the Ruffin-sponsored XL Sports event. Walking through light winter snow in the Forbidden City, he couldn't help noticing all the people wearing Ruffin coats. He was a little confused by the variety he saw; he was sure his company had never introduced more than a half dozen styles.

"Sales must be better than I thought," he ventured to Lily Wang, Ruffin's director of East Asian sales and operations. Bill had met Lily ice climbing on Mount Siguniang a few years back. He'd been so impressed with her hard-charging manner that he'd hired her on the spot.

"Sales are tremendous as you know, Bill – doubling almost every year," Lily offered. "But that won't last if we can't quickly add retail outlets. That's a bottleneck for us right now."

The CEO heard Lily's words but remained distracted by the people walking past. "Are these some of our latest

models?” Bill said, sweeping his hand across the parade ground.

Lily grinned a bit. “They’re fakes, Bill. You know it, and I know it. But with all the world’s top brands fighting for attention here, I think we’re lucky to have a few thousand free billboards walking around. Just six months ago, we weren’t all that well known in this part of the world, outside of a few big cities. Now, even in the rural areas, people know Ruffin. These aren’t exactly lost sales, you know.”

“Maybe they should be considered lost sales,” Bill replied.

Disregarding the CEO’s frown, Lily continued. “I know how important this issue is to you, but calling attention to the fakes doesn’t help; it just leaves customers wondering how good our jackets and accessories actually are if they can be copied as easily and as often as we say they are. And if we lower our prices to discourage counterfeiters, we’ll only end up hurting the brand and losing a lot of money. Besides, I’d just have all our European stores buying my product allocation here to resell there.”

By this time, the two executives had wandered through the Gate of Divine Might and out onto the street. Lily led Bill to a cart selling baked sweet potatoes, a local treat. As she purchased two, she tried to lighten his mood. “Ruffin is going to do well here, you’ll see – and very soon. When the new stores are up and running,” she said. “This is just a temporary problem.”

The Legal Bill Comes Due

“Bill, are you still with us?” The CEO was shocked back to his seat at the federal courthouse table. His mind had begun to wander to a time before all this had begun – a time when his company’s legal expenses were not a material portion of its profits.

“The district attorney got five of the 25 arrested in the New York operation to cop a plea and turn state’s evidence. That’s good news for the prosecution. But that leaves us with 20 defendants

in both the civil and criminal proceedings, and each one wants a separate trial,” Ruffin’s chief legal officer, Ben Kilgore, was saying. “We’ll need to testify at the criminal proceedings and take the lead on the civil actions.”

Bill was wondering how many employees would have to take time off to serve as witnesses, and how long he could afford to remain involved himself, when his legal counsel interrupted his thoughts again.

“I know we added three lawyers in-house only three months ago, but if we really are going to go through with all these prosecutions and class-action suits, continue to send out trade dress violation notices in all the cases where folks are copying our products, and continue our global M&A activities, patent filings, and normal business conduct, I’m going to need more help,” Ben said. The company’s retained law firm, Crabbe and Hyde, had done yeoman’s work, no question, the CLO reported, “but they are just about tapped out.”

Bill wondered now what he had gotten himself into. Was his indignation against counterfeiting after nearly losing his life just an overly emotional response to what should have been a more practical, economics-driven problem? Or was he right to pursue the threat head-on, not just because of the risks to customers but simply because it was in the best interests of the business? Was it time for Bill to press on or to move on?

How far should Bill take his campaign against counterfeiting?

Three commentators offer expert advice beginning on page 46.

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I'M A LITTLE SHOCKED at some of the Ruffin CEO's actions. He is looking at an economic problem through a very personal lens – not the reaction I would expect from the head of a multimillion-dollar global organization. His management teams in Dubai and China have a more balanced perspective: No matter how frustrating it is to coexist in a world teeming with counterfeit goods, the issue is still, at its core, purely a business one.

That's not to say it's an easy problem to manage. Increasingly, businesses in all sectors (pharmaceuticals, toys, music, food, and personal-hygiene products) are being forced to fend off look-alikes. Because of better manufacturing technologies, the quality of copycat goods has improved exponentially. As these products look more and more "real," consumers have fewer and fewer qualms about buying them – driving up demand further.

In the world of fashion, it's a particularly difficult problem. Counterfeits in this industry can quickly dilute brand value because of overexposure. That's what happened when I was at Calvin Klein from 1998 to 2003: Countries like Turkey and Russia were flooded with

compensated). But ultimately, the outcome of Calvin Klein's crime-fighting plan paled next to the amount of time and money we devoted to it. That's why I think it will be near impossible for Ruffin to get to a place where it can declare 100% victory.

The business of counterfeiting is just too large and profitable at this point. Especially in recessions, the black market thrives. Knock-off products give bargain seekers a chance to show off and enjoy a high-end experience without having to pay top dollar. Even when you explain to consumers that these counterfeits may come from factories where human rights are not respected, they continue to buy.

To mitigate the effects of copycat products, Bill should work on building up the strength of the Ruffin brand instead of getting into testy exchanges with shady street characters. To paraphrase a recent quote from Patrizio Bertelli, CEO of Prada: Worry about who's copying you, yes, but worry more about building and maintaining a brand that others will want to copy. Bill can do this in several ways, not the least of which is increasing Ruffin's retail

presence in China, Dubai, and elsewhere. Establishing more single-brand stores and high-level retail outlets would all but guarantee consumers that they are getting real-deal Ruffin goods. These stores could also showcase Ruffin's distinctive product lines in ways counter-

feiters can't and could serve as a platform for encouraging one-to-one relationships with customers.

The CEO should continue in his efforts to stay on the leading edge of innovation and technology. That could be an important point of differentiation for his company, particularly if Ruffin tells customers as much as it can about what it's doing to protect the originality of its products.

Counterfeiting is a business problem that must be fought with business smarts, creativity, retail strategy, IT, and teamwork with worldwide partners – not vengeance.

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fakes of our jeans and tops, so it was impossible to develop real businesses there. Conversely, when we were in the very preliminary stages of developing a presence in China, all the CK replicas floating around were actually helpful in creating awareness of the brand.

Like Bill Bronson, we engaged a top law firm and a worldwide network of "enforcers" to help us get the counterfeits off the streets and out of the cyberalleys. We learned, as Bill has, that this fight has to be expansive (carried out at a worldwide level, involving multiple outside parties), which means it also is expensive (all those partners expect to be

Counterfeits make me incensed too – we just end up being the R&D facility for less-than-ethical entrepreneurs.



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BILL SHOULD definitely move ahead in his battle against copycat Ruffin products, but he needs to be less scattershot in his approach. He'd be better off targeting a few potentially big hits, making an example of the worst offenders, rather than attempting to put every counterfeiter across the globe out of business. When you try to flex your muscles everywhere, that's when your expenses go through the roof.

Bill's emotions about knockoffs come from a pretty horrific event, of course, and he's much more public with his feelings than I would be. But the notion that people are counterfeiting my company's products makes me incensed too. We just end up being the R&D facility for a set of less-than-ethical entrepreneurs.

At Victorinox Swiss Army, we invest heavily in brand protection. While we outsource the production of some goods (luggage and apparel) and components (the casings for our watches), we select our manufacturers with great care to make sure the designs we share with our partners won't be used to create a couple hundred (or a few thousand) unauthorized copies of our products.

We monitor websites that sell our goods, checking to see if they're operated by one of our 10,000-plus approved resellers worldwide. We've had people arrested, and we've helped organize raids. Once products are seized, specialized equipment – for instance, instruments that gauge the molecular structure of the stainless steel in a watch or pocket knife – helps us determine their pedigree.

The biggest allies for us – and a resource that Bill needs to take greater advantage of – have been U.S. and international customs and border patrol officers. Over the past few years, customs has confiscated thousands of faux VSA fragrances, tools, and timepieces

so they could be destroyed before they even hit the streets. We communicate early and often: We inform customs officials about our typical ports of entry, consignee and consignor data, and so forth, which makes it that much easier for officials to sniff out illegal activity. The people creating and selling the fakes don't have to do R&D, marketing, or advertising, it's true, but they've still got to invest in raw materials and manufacturing. Having 14,000 products (or more) seized at a port and, ultimately, smashed under a bulldozer is probably a far more effective deterrent to them than chasing away one or two street sellers.

It's counterproductive for Bill to place any blame on consumers. Counterfeiters these days can easily go online, copy Ruffin's marketing images to post at their own sites, and dupe unsuspecting customers looking for discounts. (And the person shopping for fakes on Canal Street in New York probably isn't part of Ruffin's core, anyway.) At VSA, if a customer who unknowingly purchased a close counterfeit sends it to one of our repair centers, we'll sometimes send back an authentic replacement, and we'll tell the customer how to avoid making the same mistake in the future.

Finally, Bill might want to work on rallying his management team. The CEO and his lieutenants obviously aren't on the same page. The regional managers may be chafing against Bill's tendency to act impulsively, but even so, the strategic and financial goals he deems important should be a priority for them. He might be able to win them over by altering his public persona: working behind the scenes more, perhaps, and letting the press pick up on Ruffin's biggest successes in nabbing counterfeiters. No more sound bites of Bill acting like a big American bully.



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BILL DESPERATELY needs to professionalize his anticounterfeiting program. He should retain an outside investigator like Ted Dwayne or an outside legal team that has experience creating comprehensive brand-protection programs for manufacturing, distribution, and retail companies. Right now, there’s an awful lot of sound and fury around Ruffin’s counterfeiting problem but few well-thought-out solutions.

Executives have many variables to consider when devising a strategy against counterfeiters, and I’m not sure Bill has objectively taken stock. For instance, in which markets does he sell his products – premium, midtier, or low-end? In which countries does he manufacture and sell his goods? Is his intellectual property – including trademarks, patents, and copyrights – protected there? Has he trained national customs officers and law enforcement personnel to recognize fakes of his goods? And what does he really know about his key employees’ backgrounds and ethics? Engaging in a systematic assessment of those variables, among others, can help Bill identify

Face jackets and then importing and selling them to wholesalers and retailers throughout the United States. What’s more, any litigation efforts undertaken outside the United States, Canada, and a handful of other countries are likely to increase poor Bill’s frustration: Local cultural conditions matter quite a bit to the outcomes in these cases. If, say, the local politicians are friends of a counterfeiter you’re investigating, you may decide to focus your time and resources on a target for which there’s less chance of an “irregular” result.

Moreover, while Ruffin’s technological investments are helpful, they’re hardly a panacea. For instance, to be effective, the electronic-tag readers Ruffin is using need to be put into the hands of the people on the front lines – law enforcement or national customs personnel – not an easy or inexpensive undertaking. Customs officials have limited time to decide whether a shipment or carton warrants further inquiry. So if Bill makes it easy on them, as we do at VF – by describing the exterior of the shipping cartons and providing a list of authorized importers as well as a hotline number to call – they will be more likely to act.

The foundation for any good defense against counterfeiters is keeping tight controls over your own supply chain and distribution processes. That means being clear and consistent about the types of manufacturing partners you do business with, the countries you source from and sell in, and the rules and regulations you deem important to the future of the brand and the company. Your contracts with distribution partners should put strict limits on their activities – prohibiting, for instance, products from going anywhere but outlets you trust and where you can track them through point of sale.

Bill should continue his campaign against counterfeits; he can’t ignore the problem. But if he doesn’t handle this issue with a level head, Ruffin will pay a very steep price. 

If Bill doesn’t handle knockoffs with a level head, Ruffin will pay a steep price.

which aspects of his business might be the most vulnerable to counterfeiters. Armed with this information, Bill can then decide where to focus the dollars he’s dedicated to combating copycats – revisiting his strategy as business, legal, political, and social factors change.

Unfortunately, this battle won’t get cheaper over time. Ruffin’s legal bills will continue to stack up as the company investigates how counterfeiters of its products are organized, pursues civil litigation, and provides support to criminal prosecutions. We’ve experienced this firsthand: Recently, VF pursued (and won) sizable judgments against several enterprises in Asia that were manufacturing phony The North

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