Anti-Piracy strategies adopted by companies in China: a comparison between multinational corporation and small and medium-sized enterprise

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Abstract:

Piracy, though a global phenomenon, is most rampant in China. Hence, it is prudent for companies to proactively design anti-piracy strategies to protect their intellectual properties. This paper demonstrates the strategic solutions obtained by companies in China taking the cases of the Walt Disney and Grand Smart, a Chinese licensee of Disney. A comparative analysis of anti-piracy strategies of the large multinational corporation (MNC) Disney and those of the relatively smaller local firm, Grand Smart is conducted through secondary research. Findings reflect that Disney's strategies, to avert third party copying and licensee overrun, are mainly formal and proactive in nature. Contrarily, Grand Smart, having limited resource and power, apart from complying with licensors' formal anti-piracy strategies, mainly applies informal solutions. Notwithstanding these differences of formal or informal strategies, both companies consciously apply some kind of solutions to combat with piracy, which is also recommended for other companies operating in China regardless of their sizes.

Keywords: piracy; anti-piracy strategy; China; Walt Disney; licensee; intellectual properties; MNCs; multinational corporation; SMEs; small and medium-sized enterprise.

1. Introduction

Intellectual property (IP) has been a subject of study for academics and practitioners for 100 years, within which piracy has attracted continual attention. However, piracy emerged as critical international business issue since rise of the phenomenon during mid-80s (World Intellectual Property Organization [WIPO], 2004). Yang, Sonmez, & Bosworth (2004) defines piracy as 'unauthorized use or reproduction of another's work'. Whereas, counterfeiting, a type of piracy, means 'deliberate attempt to precise duplication of goods with the intention of deceiving customers' (McDonald & Roberts, 1994). Counterfeited and pirated goods account 5%-7% of world trade volume. Piracy is most dominant in industries like, software, music, books, pharmaceuticals, spare-parts, toys and branded cloths, perfumes, footwear etc (WIPO, 2004). This phenomenon causes loss of US$12-$15 million/year to US industries (WIPO, 2004). Among 90 countries accused for piracy, China is regarded as 'the International Capital of Piracy' and appeared on "USTR Priority Watch List' in 1992 and 1995 (Yang et al., 2004). In 2004, $134million worth of Chinese counterfeited goods was seized by US Customs, accounting two-thirds of their annual IP seizures (Clark, 2005). Two factors are responsible for piracy at epidemic-level in China; Firstly, Inadequate enforcement of IP laws and secondly, the collectivist culture of China (Yang, 2005). Chinese IP law has many loopholes which can be exploited by infringers. Additionally, the enforcement is influenced by bureaucracy and corruption (Prendergast, Cheun, & Phau, 2002). Even judges who do not take bribes may rule in favour of a local pirate factory over a foreign IP rights holder in order to save Chinese jobs (McKinsey, 2003). Moreover, China, with a strong history of government censorship and control over ideas, and its distinct lack of private property rights, looked upon intellectual property as a collective good owned by the state. China wrote their first intellectual property laws in the beginning of the 20th century under pressure by foreign governments. They have added and improved these laws only at the pressure of foreign governments. Thus, it can be surmised that significant problems will erupt when two such opposing viewpoints clash (International Piracy, Technology, and Intellectual Property [IPTIP], n/d). Despite, no western company can ignore the potential of Chinese market with a population of 1.3bn and GDP growth-rate of 7.8%-especially when western market for licensing is saturated whereas that of China is boosting (Bashford, 2003). Being aware of the prevailing condition of piracy and in contrast, the promise of Chinese market, it is critical for multinational corporations (MNCs) to design appropriate anti-piracy strategies to exploit the latter and simultaneously, deal intelligently with the former.

Therefore, this paper sheds light on the anti-piracy strategies adopted by MNCs in China conducting secondary research taking case of The Walt Disney and GrandSmart, one of Disney's Chinese licensees. Particularly, through comparative analysis of these two companies, the paper also aims to focus the difference of anti-piracy strategies of MNCs and local companies which are relatively smaller.

2. Piracy in China

Disney is one of the major IP-oriented firms of world possessing IP assets worth 86% of its market capitalisation (Yang, 2006a). Disney is divided into four major business segments; studio-entertainment, park and resorts, consumer products and media-networks (Walt Disney, 2005). Currently, Disney has 100 licensees in China covering different consumer goods (Walt Disney, 2005). Grand Smart, based in Hong-Kong while manufacturing in China, is working for Disney since 1991 . Their portfolio of Disney characters includes Mickey Mouse, Winne-the-Pooh, Princess and Toy-Story for which they produce product-lines like toys, handbags, kids' furniture, bathroom accessories, gift and collectibles, stationary etc. (Grand Smart, 2009). Therefore, the scope of the paper is limited to the IP aspects i.e. trademark and copyright, related to consumer products of Disney which Grand Smart produces.

After opening of Hong-Kong Disneyland, manufacture and distribution of counterfeited Disney products in China have boosted notably. Fake Disney wristwatch is available for US$9 and Mickey-Vampire toy for US$3.70 which are one-third of original prices. Recently, officers seized about 37,500 infringed Disney toys, stationery and handbags worth US$193,100. Sellers usually mix original products with fake ones for evading customs (Associated Press [AP], 2005). Hence, 'slavish-copying', meaning reproduction of low-quality goods through exact imitation of trademark, design, fabric and colours (Yang et al., 2004), is one of Disney's major concerns in China. This activity is also a concern for Grand Smart as it affects the businesses of licensees as well. Hence, their Marketing Manager commented, 'we are very worried about the counterfeit problems as it affects our business' (Lim, 2005). Figure-1 reflects, in China, Disney consumer products have medium risk to be victim of piracy, however, enjoy favourable legal protection (Walt Disney, 2005).

Moreover, licensed producers in China are also accused for exceeding stipulated production limit and unofficially selling and even exporting those at low price (this phenomenon in known as 'licensee overrun') (Yang et. al., 2004). Additionally, licensees are also found to be involved with IP-leakage of licensors. For instance, within four months of forming three joint-ventures by Yamaha in 1990, they discovered five out-of six Yamaha motorcycles sold in China are counterfeited as their Chinese partners sold its technology to counterfeiters and rivals (Parloff, 2006). Therefore, along with third-party infringement, Disney's concerns include licensing-overrun and leakage of company secret by Chinese licensees.

Being pressured by foreign investors, Government of China has improved IP law, which, however, still lacks specificity and hence, stress the need for interpretation . However, Chinese government is developing stringent IP laws, establishing national anti-counterfeiting agencies to coordinate efforts between 14 agencies to evade piracy (Prendergast et. al., 2002). In 2003, the Chinese authorities imposed fines of $30 million on people caught violating patents; trade marks and copyright (Clark, 2005). Although judicial enforcement of China has improved recently, it is still infected by bureaucracy and corruption and thus out-of-court settlement is the most favoured option (Yang, 2006b) and also encouraged by government . Therefore, it is prudent for companies, even large MNCs, to avoid litigation and have anti-piracy strategies. Hence, to prevent above forms of piracy proactively both Disney and Grand Smart have strategic solutions.

3. Reasons of piracy and anti-piracy strategies adopted by companies

Consumers' ethical-attitude and purchase intention towards non-deceptive pirated goods is the most vigorously studied topic within the area of piracy (Rahim, Rahman, & Seyal, 2000; Phau, Prendergast, & Chuen, 2001). Most researchers found price benefits gained from purchase of pirated goods supersede consumers' moral values (Ang, Cheung, Lim, & Tambyah, 2001; Prendergast et al., 2002). Bauer (1960) first suggested perceived-risk associated with products affects consumers' ethical-attitude towards pirated goods. Tan (2002) argued that when perceived-risk of financial loss, product performance, public exposure and loss of reputation are high; consumers' purchase-intention towards pirated products is negative. Ang et al. (2001) found association of demographic-factors with purchase-intension e.g. low income, less educated and young consumers have positive-attitude towards pirated goods. Wang, Zhang, Zang, & Ouyang (2005) in their study about Chinese consumers' attitude towards pirated software found that personality factors like, value-consciousness and social factors like, collectivism and novelty-seeking has positive effect on attitude towards piracy. Most consumers perceive that branded products charge unjustifiably high price. Furthermore, they found consumers do not realize that purchasing pirated product is illegal and likewise other researchers (Phau et al., 2001; Prendergast et al., 2002; Ang et al., 2001), recommended companies for consumer education. Prendergast et al., (2002), based on their findings recommended some anti-piracy strategies for policy makers like, prosecuting buyers to discourage willingness, arranging consumer education campaigns etc. For manufacturers they recommended to focus on quality than price-based competition; introduce holograms, magnetic-codes; educate customers of real distributors, piracy consequences; encourage distributors to contain original products; restrict distribution at pirated-prone locations and finally, promote the embarrassment of getting caught with pirated products.

Studies consulting strategic solutions to piracy, especially in China, are limited. McDonald and Roberts (1994) suggests effective IP protection in Asia-Pacific require combined efforts of police, customs and also private investigative organizations. Hence, MNCs like, Laura-Ashley, Cartier and Revlon all maintain extensive networks with state authorities, lawyers and private firms. Papadopoulos (2004) studied the relationship between legitimate product pricing, copyright law enforcement and formation of black markets for pirated products taking sound-record companies as case. He argued that ineffective enforcement of law, monopoly distribution and high price differential between pirated and original goods are responsible for piracy- especially in developing nations where consumers are value-conscious. Therefore, he suggested record companies to lobby government for proper enforcement of law, reduce price differential between original and fake records and ensure wide distribution. Seadle (2006) conducted secondary research examining anti-piracy strategies of Recording Industry Association of America (RIAA). RIAA mainly adapts reactive-strategies that are assisting record companies in criminal trials, initiating civil litigation and mediating for damage compensation outside court. However, RIAA also organise campaign to educate citizens against music piracy. Another example of proactive anti-piracy strategy is that of Software Publishers' Association, as they, part of consumer campaign, published a manual for university authorities with five solutions to prevent software piracy (Software Publishers' Association [SPA], 1998).

Yang et al. (2004) categorised anti-piracy strategies as three different approaches; proactive, defensive and network approach. Proactive approaches include 'Budweiser strategy' suggesting technological solution i.e. sophisticated labelling, packaging; 'Contractual Surveillance' focusing formal contractual agreement with partners; 'Coca-cola Strategy' focusing penetration pricing allowing no gap for piracy; and

'Microsoft Strategy' stressing constant monitoring of market for locating piracy. Defensive approaches include 'Commercial Settlement' focusing seeking commercial compensation and 'Acquiring Strategy' suggesting acquisition of infringing companies and convert them to licensee. Finally, network approaches include 'DuPont Strategy' focusing IP reapplication with persuasive evidence; 'Manchester United (MU) Strategy' indicating networking with other victim or non-victim companies; 'Government Hand' focusing networking with state authorities for enforcement and 'Consumer Campaign' suggesting educating consumers against piracy.

Nevertheless, these strategies, mainly adapted by big MNCs, may not be applicable for relatively smaller local firms considering they have limited resources, lobbying power on government and also fear of bad publicity. Kitching and Blackburn (1999) found that SMEs prefer informal to formal anti-piracy strategies. Their defensive strategies include threatening infringers about legal action and out-of-court settlement through compensation. Only 19% of their respondent SMEs applied litigation and the rest had out-of-court settlement through threat with/without compensation. Their proactive strategies include maintaining trust-relationship with customers and suppliers, practiced by 75.9% respondents; providing IP information to selected staffs, practiced by 47.5% respondents; membership of associations, practiced by 27.7% respondents etc.

Anti-piracy strategies found and/or recommended by different researchers are summarised in Table-1

Table-I: Summary of anti-piracy strategies recommended and/or found by researchers

Literature	Found and/or recommended anti-piracy strategies
McDonald and Roberts (1994)	• Maintain extensive network with state authorities, lawyers and private investigation agencies • Consumer education against piracy
Seadle (2006)	• Litigation and compensation • Consumer Education against piracy
Papadopoulos (2004)	• Lobby government for tightening enforcement • Reduce price differential between original and pirated products • Distribute as widely as possible • Offer price discounts, especially by monopoly distributors
Kitching and Blackburn (1999)	• SMEs maintain trust-based relationship with suppliers and distributors • SMEs threaten infringers for litigation • SMEs adapts out-of-court settlement with/without compensation
Yang et al. (2004)	• Proactive approaches: - Budweiser Strategy: sophisticated technology - Contractual Surveillance: Tight contractual obligation - Coca-cola Strategy: Penetration pricing - Microsoft Strategy: Constant monitoring of market • Networking approaches: - DuPont Strategy: Persuasive reapplication - MU Strategy: Maintain network with other companies - Government Hand: Maintain network with state authorities - Consumer Campaign: Education against piracy • Defensive approaches: - Commercial Settlement: Seek compensation - Acquiring Strategy: Acquiring infringing company and converting to licensee.
Wang, et al. (2005)	• Educating consumers on - how to identify fake products - consequence of piracy on society and economy - purchasing fake products have ethical dilemma as well
Phau et al. (2001)	• Consumer education
Prendergast et al. (2002)	• Focus on product quality than price based competition. • Introduce holograms, magnetic codes, and special links to enable consumers to differentiate fake from original. • To educate customers of real distributors, consequences of piracy. • Motivate distributors to contain original products • Restrict distribution at pirated prone locations. • Promoting the embarrassment of getting caught with pirated products.
Tan (2002)	• Promoting the embarrassment that producing/selling/buying infringed product can cause
Ang et al. (2001)	• Consumer education

Grand Smart being a local company it is relatively smaller than large MNCs like Disney, Microsoft in terms of resource and power and hence can be categorized as SME. This raises the question whether these anti-piracy strategies are applicable for smaller local companies as well. Therefore, the paper aims to compare anti-piracy strategies of Disney and Grand Smart within the frameworks of Yang et al. (2004) and Kitching and Blackburn (1999).

4. Comparative analysis of anti-piracy strategies: Disney vs. Grand Smart

To combat with slavish-copying and licensing-overrun, Disney has introduced 3D-holographic label, which is supplied by themselves to licensees to put on every consumer goods (Lim, 2005). This technological solution to piracy reflects that they are complying with 'Budweiser Strategy'. However, this strategy may not threaten proficient infringers. Consequently, Disney's Head of Consumer Products commented, "The holograms are incredibly difficult to copy but I'm hesitant to say anything's impossible in China" (Lee, 2006). Hence, they require application of other strategies as well. Therefore, they comply with 'Microsoft Strategy', though not as extensively as Microsoft , through maintaining close contact with retailers to monitor their activities and also through making licensees conduct market inspections on behalf of Disney (AP, 2005). Moreover, to prevent licensing-overrun and IP-leakage by licensees, they ensure tight contractual relationship with them which reflect application of 'Contractual Surveillance' strategy. Before entering into any collaboration they analyse the biography of potential partners to identify any record of infringement (Walt Disney, 2009). Furthermore, to motivate licensees and maintain long-term trust relationship with them, Disney rewards licensees' loyal efforts and thus reduces possibility of unfaithful activities by them. For instance, Walt-Disney provided Grand Smart, for their valued service Asia-Pacific's Licensee of the Year Award in 1995, 2003 and 2004 (Grand Smart, 2009). Another proactive strategy of the company is to make their products available on as many different platforms as possible. They make their content locally relevant and available to as many people as possible (Staggs, Bird, Cheung, Jain, & Ozkan, 2007). Hence, in China, Disney is expanding from more than 4,000 retail corners currently to 6,000 by 2009, most of which are directed by licensees in China (Swanson, 2007).

Besides above proactive approaches, Disney has adapted some networking approaches. Disney maintains extensive network with Hong-Kong Customs and mainland Chinese authorities to ensure support from them. Recently, Customs has conducted raid in Dongmen Market, Shenzen, China, where fake Disney products are usually sold (AP, 2005). Chinese governments' recent proposal to open Disneyland in Mainland has given bargaining power to Disney which also ensured more support from state authorities (Lee, 2006). This strategy also creates publicity and awareness against piracy and simultaneously, complements creating brand awareness which is also Disney's current strategic vision in China (Walt Disney, 2005). However, maintaining such relationship is bureaucratic and time-consuming. Another networking approach of Disney includes adaptation of 'MU Strategy'. Consequently, Disney is a member of Quality Brands Protection Committee (QBPC) which cooperatively works with Chinese government to ensure IP protection to its member MNCs (QBPC, 2009).

Disney's anti-piracy strategies mainly reflect proactive rather than reactive/defensive approaches presented in Yang et al. (2004). Actually, seeking compensation for damage from small pirates will add little value to this entertainment giant's finance. Another defensive approach that is 'Acquisition Strategy' might also not appeared viable option for Disney as it requires huge investment.

In contrast, for Grand Smart, conducting business mainly as licensee, it is critical to comply with anti-piracy strategies of licensors. For instance, they put holograms, supplied by Disney, Mattel, on respective consumer goods (Grand Smart, 2009) and thus comply with licensors' 'Budweiser Strategy'. Moreover, on behalf of Disney they arrange frequent inspections to local markets and report counterfeiting activities to Disney (AP, 2005) and thus comply with Disney's 'Microsoft Strategy'. Apart from this, all other anti-piracy strategies of Grand Smart are mainly informal. For instance, unlike Disney they may not maintain extensive network with government but ensure trust-relationship with retailers to prevent infringement activities in their distribution network (Grand Smart, 2009). Moreover, to maintain harmonious relationship with Disney they are committed to offer valued service. Such motive emphasise their intention to avoid occurrence of licensing-overrun or IP-leakage, which is proved through the awards presented by Disney to them. Figure-2 reflects the comparative analysis of both companies' anti-piracy strategies.

5. Conclusion

5.1. Key Findings

Findings of comparative analysis reflect that Disney adopted a combination of proactive and network approaches involving more than one strategy from each category. Proactive approaches include introducing 3D-holographic label to prevent both third-party copying and licensing-overrun and monitoring of market using licensees to identify infringement. Moreover, they use tight contract and harness long-term relationship with licensees to prevent licensing-overrun. Disney's networking approaches include maintaining network with government and membership of QBPC to maintain network with other victim MNCs. Contrarily, apart from complying with licensors' formal strategies, Grand Smart, being local company with less resource and power, mainly relies on trust-based relationship with licensors and distributors to avoid licensing-overrun and prevent infringement respectively. This strategy also complements Chinese culture where trust or Guanji is highly valued in case of business (Yang, 2005).

5.2. Recommendations

The literature review suggests that Chinese consumers lack awareness about the consequence of piracy and believe that sellers are only responsible for piracy not consumers. This stresses the importance of educating them about the impact of piracy on society and economy and also about the fact that encouraging piracy has ethical dilemma as well. Notably, Disney does not emphasise consumer campaigning in China. Previously, Chinese governments' restriction on set-up of foreign channels prevented Disney to reach mass-market which is essential for such campaign. However, recently, government approved 49% ownership of Chinese TV firms by foreign channels (Buck, 2004). Disney can utilise these Channels, viewed by 475million households (Walt Disney, 2005), to create awareness against purchase of fake Disney products. Moreover, using fear-appeal, as suggested in Prendergast et al. (2002), they can promote the embarrassment that may cause if consumers get caught purchasing or using pirated products. Such campaign will ensure brand awareness which may further encourage consumers to buy original products. Moreover, instead of acquisition or seeking compensation Disney, as defensive strategy, can make infringers apologise publicly which is perceived as highly insulting in Chinese society and thus discourage infringement.

5.3. Managerial implications

This paper shows that to protect valuable brands from pirates and sustain in China, depending merely on law and enforcement is not enough rather managers of MNCs should proactively develop anti-piracy strategies. Local companies, especially those who mainly depend on licensing, should also apply some sort of formal and/or informal strategic solutions to eradicate piracy.

5.4. Limitations and further research direction

The findings of this paper are not based on empirical evidence and thus have limited validity and reliability. Indeed, studies consisting empirical data on this issue are scarce indicating the need for further research. Moreover, as per the literature review most researchers studied anti-piracy strategies of large organizations or multinational corporations. Researches reflecting the same for small and medium sized local companies are limited and those reflecting comparison of MNCs and SMEs are even rare. Therefore, this could be another area for further study.

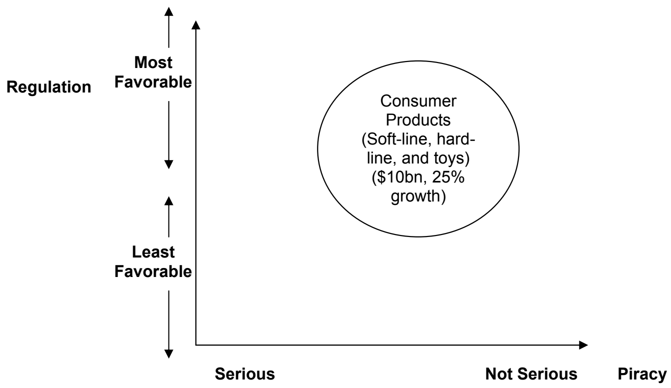

Figure-1: Risk of consumer products of Disney in China
Source: The Walt Disney (2005), p.7

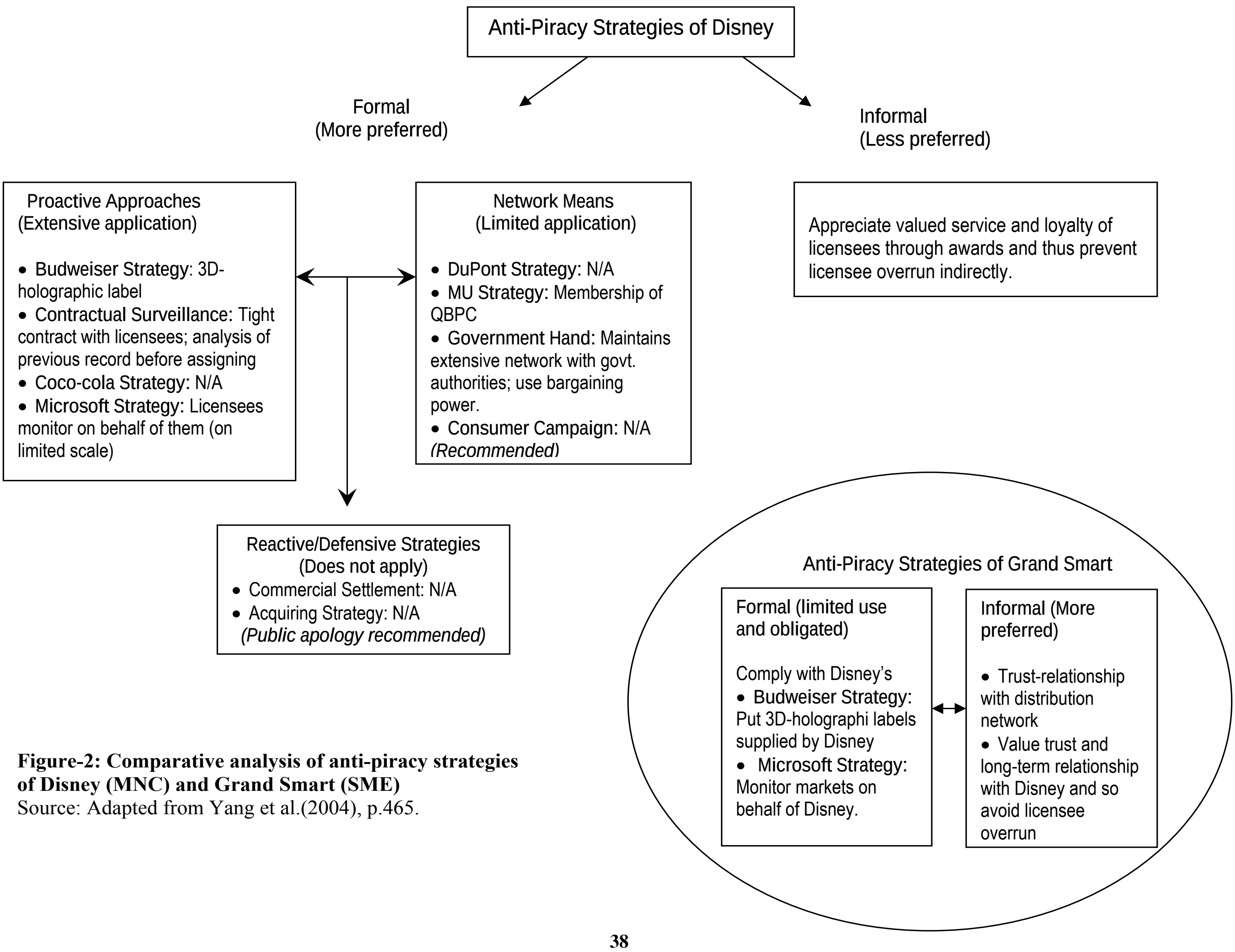

Figure-2: Comparative analysis of anti-piracy strategies of Disney (MNC) and Grand Smart (SME)
Source: Adapted from Yang et al.(2004), p.465.

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Notes

Grand Smart is also licensee of other international entertainment companies like, Mattel, Warner Brothers etc (Grand Smart, 2009).

For instance, Article-56 of Trademark Law of China stipulates that innocent infringer shall not receive punishment but does not define the term 'innocent-infringer'. Such gap can give opportunity to infringers to use as self-defence.

Article-53 stipulates that in case of any valid complain of infringement, the administrative authority will stop any infringing act, destroy the infringed goods and machineries used for their production. It also states that parties shall first try to solve the dispute through consultation and if failed, can file litigation (Trademark Law of People's Republic of China).

In China, Microsoft continuously identifies companies those use pirated software and managed to convert all the pirate companies into license-holding customers. In one case, it compelled the offending company to take out advertisements in Chinese newspapers admitting it was using pirated software, but was now using the genuine article (McKinsey, 2003).

The QBPC, which held its official Chinese launch on March 2, 2000, is registered under the China Association of Enterprises with Foreign Investment (CAEFI). The QBPC is comprised of more than 140 multinational companies concerned with the impact of counterfeiting and membership continues to grow. The QBPC mission is 'to work cooperatively with the Chinese Central and local governments, local industry, and other organizations to make positive contributions to intellectual property protection in the People's Republic of China.' (QBPC, 2009)

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