



June 21, 2007

VIA E-MAIL: FR0711@USTR.EOP.GOV

Ms. Marideth J. Sandler
Executive Director
Generalized System of Preferences (GSP) Program
Office of the U.S. Trade Representative
600 17th Street, NW, Room 403
Washington, D.C. 20508

Re: Russia GSP IPR Review Case: 018-CP-05

To the GSP Subcommittee:

The International Intellectual Property Alliance (IIPA) and its member associations take this opportunity to reiterate our request that the United States government immediately suspend Russia's eligibility for any duty-free trade benefits that it enjoys under the Generalized System of Preferences (GSP) program, due to Russia's failure to provide adequate and effective protection to U.S. copyrights, including its failure to comply with U.S.-Russia IPR Bilateral Agreement of November 19, 2006.

Our request today repeats identical requests we made in our February 12, 2007 Special 301 submission (attached) as well as our numerous (March, June and July) 2006 letters to the GSP Subcommittee. We have provided the interagency with several updates on the lack of progress being made in Russia on continuing rampant piracy, ineffective copyright enforcement, and the numerous legal deficiencies in the Russian IPR regime. See, for example, the attached "Fact Sheet" which details that Russia is currently failing to comply with many IPR Bilateral Agreement obligations. There simply is no justification for continuing to give trade benefits to a country which fails to comply with the basic terms of the GSP trade program.

Sincerely,

Eric J. Schwartz on behalf of IIPA

INTERNATIONAL INTELLECTUAL PROPERTY ALLIANCE

2007 SPECIAL 301 REPORT

RUSSIAN FEDERATION

Special 301 Recommendation: IIPA recommends that the Russian Federation be retained on the Priority Watch List and that the U.S. Government also undertake an Out of Cycle Review (“OCR”) in 2007 to carefully monitor Russia’s progress on enforcement and necessary legal reforms.¹

IIPA makes this recommendation in light of the recent signing of the 2006 U.S.-Russia IPR Bilateral Agreement under which Russia committed to taking actions (most of them by June 1, 2007) with respect to the issues that have given rise to prior IIPA requests for the designation of Russia as a Priority Foreign Country and the removal of Russia’s GSP benefits. IIPA recommends that the OCR review should commence immediately after June 1; this provides Russia an opportunity to implement its IPR protection and enforcement obligations as stipulated in the IPR Bilateral Agreement. If after the OCR review, the U.S. Government determines that Russia has not made significant progress fulfilling its obligations, then IIPA recommends that the U.S. Government should designate Russia as a Priority Foreign Country and should immediately suspend Russia’s entitlement under the GSP program. Further, since violations of trade agreements are subject to mandatory retaliation, the U.S. Government should also initiate an investigation that will lead to the imposition of trade sanctions as contemplated under Section 301 of U.S. trade law. Conversely, if Russia has met all of its obligations, then the U.S. Government should consider removing Russia from the Priority Watch List.

EXECUTIVE SUMMARY

On November 19, 2006 the Governments of Russia and the United States entered into a IPR Bilateral Agreement (“Side Letter”) in the context of Russia’s efforts to accede to the WTO; it was signed by Russian Minister Gref and Ambassador Schwab.² According to the Side Letter, U.S. support for Russia’s entry into the World Trade Organization (WTO) is now conditioned on meaningful copyright law enforcement with specific obligations that Russia must take to reduce piracy “on a priority basis” as well as requirements to adopt the laws necessary to accomplish this goal. The IIPA recommends an OCR to ensure that Russia accomplishes the specific Side Letter obligations by the specified deadlines (many in mid-2007), and also that it meets its obligations under other existing bilateral and multilateral commitments. Russia needs to comply with its obligations and make appreciable progress on enforcement to continue to enjoy existing trade preferences, such as duty-free benefits (GSP), and in order to accede to the WTO.

At present Russia’s current copyright piracy problem remains one of the worst of any country in the world, resulting in losses of over \$2 billion in 2006. Piracy levels of all copyright

¹ For more details on Russia’s Special 301 history, see IIPA’s “History” appendix to filing at <http://www.iipa.com/pdf/2007SPECIAL301HISTORICALSUMMARY.pdf>. Please also see previous years’ reports at <http://www.iipa.com/countryreports.html>.

² The text of this Side Letter, known formally as the U.S.-Russia Bilateral Market Access Agreement on Intellectual Property Rights, is available at http://www.ustr.gov/Trade_Sectors/Intellectual_Property/Russia/Section_Index.html.

materials – motion pictures, records and musical compositions, business and entertainment software, and books – range from a low of about 65% to a high of 83%. These levels are unacceptable for a country and economy of the size and sophistication of Russia. Moreover, exports of infringing products from Russia – which have been forensically identified in over 27 countries – are eroding the copyright industry’s legitimate businesses in third country markets.

In 2006, there was some enforcement progress to report, particularly with respect to raids and inspections of some of the optical disc plants. But, the situation has not materially improved due to the continued lack of criminal prosecutions and sentences, and the absence of a sufficiently effective regime to prevent the production of illegal optical discs at Russia’s numerous plants. In 2006, the Russian Government reported that it ran an increasing number of “raids” and “inspections” on the optical disc plants, even more than in 2005. However, few of these “raids” were surprise inspections and some were undertaken without the cooperation of rightholders. Much more needs to be done in 2007 for Russia to meet its bilateral obligations under the Side Letter, including undertaking real surprise inspections with rightholder cooperation at all of the plants and, in order to be effective, adopting more detailed licensing provisions (required by June 1, 2007). There are three components to effective optical disc enforcement, in addition to the need to adopt a comprehensive and effective licensing regime: (1) all of the plants involved in the manufacture of illegal material must be closed; (2) plant operators of such plants must be convicted and sentenced; and (3) the machinery used to conduct this piracy must be detained and sealed as evidence, and then seized and destroyed, regardless of the ownership of the machinery.

In 1996, when the IIPA first brought the optical disc (“OD”) piracy problem to the attention of the U.S. and Russian governments, there were 2 plants; in 2005, there were 47. This figure grew to 54 optical disc plants last year, but has now decreased to 53 due to a consolidation of two of the plants. While it is clear that many of these plants are producing illegal material for export, the lack of a comprehensive and effective inspection and enforcement system, makes it hard to precisely determine this figure. The Side Letter, obligates the Russian Government to address this problem with specific on-the-ground enforcement steps and legislative actions -- by June 1, 2007. As the Side Letter notes (listing OD piracy as a priority), Russia is committed to addressing the problem, inter alia, “[w]ith the objective of permanently closing down operations of plants that engage in [the] production of optical discs and other optical media containing pirated and counterfeit material.”

The aggregate number of criminal enforcement actions (raids and convictions) by the Russian police did increase in 2006, with the business software sector seeing a 300% increase in such actions. The significant increase in sales experienced by some in the business software sector may be attributable, in part, to this increase in enforcement activity.

Additionally, there were positive steps undertaken to improve the IPR legal regime. For example, the Criminal Procedure Code was amended in 2006 to allow Russian police (in addition to prosecutors, as it was previously limited) to initiate criminal investigations of IPR infringements.

Second, legislation was introduced (and is expected to be adopted and in force in 2007), to establish higher penalties for copyright infringements -- of up to six years imprisonment, and by re-classifying copyright infringements as a “grave crime.” Once adopted, this would allow Russian law enforcement authorities to use a wide spectrum of investigative measures which are not possible for the current classification of copyright as a “medium gravity” crime.

Also, on June 19, 2006, the Supreme Court of the Russian Federation passed a resolution of the Plenum of the Supreme Court that clarifies the practices courts must follow when applying civil procedures in copyright infringement matters.

Major legal reforms (i.e., the enactment of a comprehensive Civil Code, Part IV on IPR) were adopted in 2006. However, the practical result of the Civil Code reform is that it will more than likely cause confusion among practitioners and the courts and will actually weaken, not strengthen, existing protections. Some of the Civil Code provisions did improve existing legal protections. But, it is unfortunate that the Russian government and parliament focused almost all of their attention in 2006 on replacing the existing (and mostly sufficient) copyright law with a new Civil Code, Part IV (a substitute for all IPR laws). This diverted attention and resources from the much more important need to undertake effective enforcement and to change procedural enforcement measures. In fact, in 2006, the most significant IPR enforcement matters showed little appreciable signs of improvement: (1) optical disc piracy remains unacceptably high; (2) criminal enforcement, especially against optical disc piracy, is weak overall, non-deterrent, and certainly not directed against plant operators and organized crime syndicates, which it must be to be effective; and, (3) Internet piracy of movies, music, videogames and books is growing, with blatant pirates using Russian-based servers (an otherwise simple target for enforcement), for example, allofmp3.com, operating with impunity.

Enforcement Steps Required by the Side Letter for 2007: Russia has agreed in the Side Letter to make copyright enforcement an IPR priority, especially against illegal optical media plants, and to improve overall enforcement. For years, IIPA has provided a list of the critical steps that the Russian Government could take to effectively confront its optical disc and other critical piracy problems. IIPA supports the inclusion of many of these steps as binding commitments of the Russian Government in the Side Letter.

In particular, the Side Letter requires the Russian Government to:

1. Address the optical disc problem, with the objective of permanently closing down illegal plants, by:

A. Conducting “repeated, unannounced inspections” of all known OD plants. “Such inspections will take place regularly, without prior notice, and at any time, day or night. If evidence of unauthorized production of optical media bearing content protected by copyright or related rights on a commercial scale is found, criminal proceedings will be initiated.” Russia will then be required to “[c]ontinue to conduct actions to find and shut down unlicensed plants producing optical media bearing content protected by copyright or related rights.”

B. Conducting actions to “find and inspect warehouses” storing pirate product, including the seizure and retention for evidence of illegal copies, as well as initiating “investigations to determine the owner, distributor, and manufacturer of such goods and prosecutions of these persons and enterprises” including “criminal proceedings...in cases of piracy or counterfeiting on a commercial scale.”

C. “Ensur[ing] that facilities on the territory of government-controlled military-industrial [i.e., RARE] sites are not leased or otherwise made available to companies producing optical media bearing content protected by copyright or related rights and immediately take action to terminate any existing leases.”

D. Enacting legislation (by June 1, 2007) to “strengthen the licensing regime for optical media plants” including “grounds to deny applications for licenses and to suspend, and then immediately seek revocation by a court of, licenses of persons whose production premises are found to be manufacturing pirated product; enhanced recordkeeping requirements; and government monitoring of production.” This legislation must ensure that “each licensee will verify that the customers for whom it produces optical media bearing content protected by copyright or related rights have authorization from all relevant right holders” and that “licensees mark optical media with data that identifies the licensee and the license number” and “that licensees use additional markings, such as source identification codes.”

E. Ensuring that grounds to deny, suspend or “immediately seek revocation by a court of a license” include: violations of “any licensing condition,” and that by June 1, 2007 legislation will include a provision that “licenses will be denied to persons who have previously had a license revoked by a court for infringement of any license requirement, such as violation of copyright or related rights.”

2. Address the need for effective criminal enforcement, focusing in particular on piracy “committed for purposes of commercial advantage or private financial gain” by referring “to the Supreme Court of the Russian Federation a proposal for it to pass a resolution of the Plenum of the Supreme Court” to clarify for the courts their practices so that they impose stiff penalties for IPR violations, and requiring that judges “take into account the high degree of public harm from such infringement.”

3. Address the need for effective border enforcement by “significantly increas[ing] the percentage of export shipments inspected” and to provide information to “appropriate authorities for investigation and prosecution.” Also, the government will seek to enact legislation (by June 1, 2007) “strengthening Customs officials’ authority to take actions *ex officio* with respect to suspected exports and imports of pirated or counterfeit goods” and “encourage Customs officials to use such authority.”

4. Address the need to combat the growing threat of Internet piracy “with the objective of shutting down websites that permit illegal distribution of content protected by copyright or related rights” (and especially for websites whose servers are situated in Russia (which in a footnote specifically says “[s]uch as allofmp3.com”) by:

A. Taking actions “against the operation of websites...that promote illegal distribution of content protected by copyright or related rights, such as phonograms (sound recordings).”

B. “[I]nvestigat[ing] and prosecut[ing] companies that illegally distribute objects of copyright or related rights on the Internet.”

C. Enacting by June 1, 2007, legislative amendments to “provide that collecting societies may act only on behalf of right holders that explicitly authorize such action” and the “provisions needed to implement the World Intellectual Property Organization (WIPO) Copyright Treaty [WCT] and WIPO Performances and Phonograms Treaty (WPPT).”

5. Adopt legislation to “fully implement the TRIPs Agreement and other IPR-related international agreements” to which the United States and Russia are already parties (as

well as to “fully implementing the WCT and WPPT”). Ensure that any legislative, regulatory or other measures made prior to accession, i.e. Part IV of the Civil Code, will not “result in a lesser degree of consistency than exists on this date” (November 19, 2006) with the TRIPs Agreement or any other international IPR agreement to which the U.S. and Russia are parties.

6. Ensure on-going dialog and work to implement the obligations above through a Bilateral Working Group, as well as to provide appropriate training to Russian enforcement officials.

The summary of these six Side Letter obligations illustrates the important enforcement actions that Russia must undertake in 2007 (most by June 1). Note that even though the Side Letter has the status of an international agreement under U.S. and Russian law, as of February 1, 2007 (almost two and a half months after its signing), it still not been published in the Russian language in Russia, nor is it available in either English or Russian on any Russian Government website; it is only available in English on the USTR website.

The IIPA continues to recommend several enforcement steps without which Russia will not be able to meet its performance requirements under the 2006 Side Letter. These include:

1. Making certain that the optical disc licensing regime includes: (a) stricter controls on the importation of polycarbonate and machinery; (b) mandatory seizure and destruction of machinery used to produce pirate materials (regardless of the ownership of the machinery, and the relationship of the “owner” of the machinery to the infringement); and (c) the introduction of criminal penalties for the owners of such plants. Plant inspections must be undertaken regularly and exemplars tested jointly with rightholders. In addition, any plant licensing regime should extend in scope to the operators of telecine machines and mastering laboratories used to pirate audiovisual works;

2. Announcing from the office of the President, that fighting copyright piracy is a priority for the country and law enforcement authorities, and instructing the Inter-Ministerial Commission, headed by the First Deputy Prime Minister, to deliver reports every three months to the President on what steps have been taken to address the problem. Also, it is imperative to establish a central coordinating body for law enforcement authorities with wide powers, derived directly from the President, to combine the efforts of the Economic Crime Police, Department K (the New Technologies Police), and the Police of Street Order;

3. Adopting in the Supreme Court a decree setting forth sentencing guidelines for judges — advising the courts to impose deterrent penal sanctions as provided under the penal code as amended (Article 146) for all copyright violations, including Internet piracy as well as providing guidelines for the application of substantive copyright law in criminal processes (such as, a presumption of ownership). We also recommend amending Article 146 to a minimum penalty of six years, not the current penalty of five years (since only penalties of six or more years are treated as “serious” crimes) and that legal entities be included as subjects of criminal liability (a bill to amend Art. 146 accordingly is under consideration in the Duma);

4. Using the existing authority to take down websites offering infringing copyright materials, against, not only allofmp3.com (music), but also websites such as, www.threedollardvd.com, alltunews.com, mp3search.ru, www.dvd-box.ru (films/music), <http://ebook-mega-store.com> and related sites (books), www.stalevar.com (business software), www.cdcheap.com (business software) and criminally prosecute those responsible, including

unauthorized collecting societies (such as ROMS, FAIR, and FOSP) that purport to grant licenses for rights that they do not possess, as well as introducing ISP liability in civil and criminal cases;

5. Using the improved border enforcement authority to stop the import of machinery used to produce illegal product in addition to the export of large shipments of that product abroad;

6. Initiating investigations into and criminal prosecutions of organized criminal syndicates that control piracy operations in Russia (including operations that export pirate material to markets outside Russia);

7. Encouraging the Economic Police (including the Anti-Fraud Department) to substantially increase the number of anti-piracy raids, especially against large scale targets, and to extend their actions to the distribution networks supplying illegal street sellers as well as to bring more cases to the prosecutors; and

8. Taking action to undo the situation in St. Petersburg, where legitimate video and DVD markets have been effectively lost due to the activities of a collective management organization known as the Association of Collective Management of Authors' Rights which falsely claims to represent MPA member companies and which, incredibly, enjoys the support and protection of local officials, and requires (in violation of federal law) the application of a pirate hologram on all products sold with its license. Similar organizations have proliferated in Russia, including MAS (Interregional Authors Partnership), ROSA, and MO UIPKO (Interregional Union for Collective Management of Rights).

9. Developing effective measures to criminalize the camcording of motion pictures in theaters, since these are the primary source for illegal DVDs.

In 2004, Russia adopted important law reforms to bring its laws into compliance with the 1992 Bilateral NTR Trade Agreement and the Berne Convention – most in the copyright law. Unfortunately, in 2006, Russia decided to completely overhaul its IPR regime by adoption of the Civil Code and the repeal of the copyright law. As noted, there are now gaps in the IPR enforcement regime both in the Civil Code and elsewhere pertaining to enforcement, that Russia needs to address to come into compliance with the IPR Side Letter, including further updating the Criminal Code, the Criminal Procedure Code, and Administrative Code (as detailed in this and prior reports). Amendments to the Code of Administrative Misdemeanors adopted in 2005, entered into force in January 2006.

RUSSIAN FEDERATION
Estimated Trade Losses Due to Copyright Piracy
(in millions of U.S. dollars)
and Levels of Piracy: 2002-2006³

INDUSTRY	2006		2005		2004		2003		2002	
	Loss	Level								
Motion Pictures ⁴	NA	NA	266.0	81%	275.0	80%	275.0	75%	250.0	80%
Sound Recordings & Musical Compositions	423.0	65%	475.9	67%	411.9	66%	405.0	64%	371.9	66%
Business Software ⁵	1433.0	83%	894.0	83%	800.0	87%	704.0	87%	370.0	89%
Entertainment Software ⁵	282.1	72%	223.9	82%	255.8	73%	NA	80%	NA	90%
Books	42.0	NA	42.0	NA	42.0	NA	40.0	NA	40.0	NA
TOTALS	2180.1		1901.8		1784.7		1424.0		1031.9	

COPYRIGHT ENFORCEMENT IN RUSSIA

Illegal Optical Media Production and Distribution

By no later than June 1, 2007, the Russian Government has committed to making significant improvements in the manner in which it addresses the problem of illegal optical disc plants, including permanently closing down plants containing pirate material. As of January 1, there were 53 known optical disc plants licensed in Russia to manufacture and distribute products (including music CDs, DVDs, videogames, and VCDs); this includes 2 CD-R and DVD-R production facilities. However, of this number, only 42 plants (plus six mastering facilities, that do not need licensing under current law) were in operation on January 1. Of the total number of optical disc plants, at least 24 have been confirmed to be producing pirate product.

Moreover, the Side Letter requires Russia to specifically address the problem of the plants located on government owned or leased property. These plants on former military bases are known as “Russian State (owned) Restricted Access Regime Enterprises” (RARE) – there are currently 8 such optical disc plants. As of March 2005, Ministry of Interior officials and State

³ The methodology used by IIPA member associations to calculate these estimated piracy levels and losses is described in IIPA’s 2007 Special 301 submission, and is available on the IIPA website at www.iipa.com/pdf/2007spec301methodology.pdf.

⁴ MPAA’s trade loss estimates and piracy levels for 2006 are not yet available. However, such numbers will become available later in the year and, as for 2005, will be based on a methodology that analyzes physical or “hard” goods and Internet piracy. For a description of the new methodology, please see Appendix B of this report. As the 2006 loss numbers and piracy levels become available, they will be posted on the IIPA website, <http://www.iipa.com>.

⁵ BSA’s 2006 statistics are preliminary. They represent the U.S. publishers’ share of software piracy losses in Canada, and follow the methodology compiled in the Third Annual BSA/IDC Global Software Piracy Study (May 2006), available at <http://www.bsa.org/globalstudy/>. These figures cover, in addition to business applications software, computer applications such as operating systems, consumer applications such as PC gaming, personal finance, and reference software. BSA’s 2005 piracy statistics were preliminary at the time of IIPA’s February 13, 2006 Special 301 filing; the 2005 data was revised and posted on the IIPA website in September 2006 (see <http://www.iipa.com/statistics.html>), and the 2005 revisions (if any) are reflected above.

⁶ ESA’s reported dollar figures reflect the value of pirate product present in the marketplace as distinguished from definitive industry “losses.” The methodology used by the ESA is further described in Appendix B of this report.

Trade Inspectors were granted the authority to have 24-hour access to RARE facilities in order to conduct plant raids (which are otherwise off-limits to local enforcement authorities). MOI officials can, but to date have not used their full authority to undertake effective surprise inspections, including the seizure of illegal material and the closure of illegal plants. In September 2006, the Russian Government acknowledged (on national television) that at least 5 of these RARE plants were engaged in illegal production of optical discs; they further reported that the directors of those plants were dismissed – but, to date there have been no additional reports about any prosecutions of those directors. In the Side Letter, the Russian Government agreed to inspect all of these plants, to close the illegal ones, and to end existing and deny new leases to these plants.

The 53 optical disc plants have a total plant capacity of 455 million CDs and DVDs per year (with an estimated actual production of between 150 and 200 million discs per year). There are estimated to be a total of 130 lines (including the 6 mastering facilities), with 71 lines dedicated to DVD production, up from 34 less than two years ago. The local legitimate market is significantly less than this figure. For example, it is estimated that the current demand for legitimate DVDs is about 10 million discs per year but that Russian plants are now manufacturing between 80 and 100 million DVDs per year for export to markets outside of Russia (with markets in Bulgaria, Czech Republic, Estonia, Finland, Germany, Hungary, Israel, Poland, Romania, Turkey, Ukraine and the United Kingdom being negatively impacted, in particular). According to the recording industry, fewer than 85 million legitimate CDs were sold in Russia in 2006.

In 2006, the Russian Government continued to take raids against some of the plants – certainly a positive step, but merely a first step. The government has indicated that it has conducted “inspections” of all the known plants (i.e., license inspections) in 2006. As a result of these visits according to the official government statistics, licenses at 8 plants were temporarily suspended by the Ministry of Culture (i.e., the Federal Licensing Service – Rosokhrankultura), 6 plants had their licenses withdrawn, and 4 others voluntarily returned their licenses (although the Rosokhrankultura website notes the agency made only 14 license checks, suspending 3 licenses and cancelling 3 licenses). While this is certainly encouraging, it has done little to stem the production and distribution of pirate discs, and illustrates the need for comprehensive legal measures and effective enforcement techniques. In 2006, there were, to our knowledge, 8 criminal cases initiated against (7 different) optical disc plants.

After plant “raids” the Russian government has declared some of the plants to be “clean.” This “cleanliness” should not be misinterpreted; it likely resulted because many visits were not surprise inspections. We applaud the increase in plant inspection activity—an increase that led to the seizure of increased quantities of piratical goods. But taken in context, these raids are not sufficient to address the escalating piracy problem. For example, it is reported that over 10 million DVDs were seized in the first nine months of 2006 (although, as noted, the motion picture industry reported that as many as 80 to 100 million discs were produced for export alone during the year).

The end results of the 2006 raids are telling, and underscore the significant amount of work Russia must undertake to address the piracy problem as well as to meet the Side Letter’s (and other pre-existing bilateral and multilateral) obligations. It would appear that almost all of the optical disc plants that were raided in the last three years remain in operation after those raids. For example, last year we reported on a raid of the Roff Plant in Odinstovo, near Moscow. At the time of the raid (November 2005), the plant’s license was suspended while a criminal prosecution proceeded. This was the first such suspension by Roskhankultura and several other

suspensions were announced in early 2006. However, although its license remains suspended, forensics evidence indicates the plant is continuing to replicate illegal (DVD) discs. Roskhankultura has been notified of this activity. This illustrates the problem--plants remain in operation even after raids, illegal material continues to be seized after an initial raid, and even, in many cases, operating licenses are not suspended by Roskhankultura. The Side Letter calls for significant improvements in plant regulations, and, among other important steps, requires the Russian authorities to "permanently close" illegal plants and to criminally prosecute the plant operators.

The ongoing piracy problem has continued in large measure, because the plant owners have, for years, remained unscathed by the criminal justice system. For example, a plant in Tver, Media Systems, was raided and though the director of the plant was arrested, the owner was not. Action against the plant owners is an essential element in combating OD piracy, and requires political willpower by the enforcement agencies. In short, a few plant employees, but no plant operators, have been convicted after over 10 years of optical disc piracy problems, and, even the prosecution of employees is usually accomplished only after extensive delays in the investigations and by the imposition of suspended sentences.

There have been a few exceptions: in December 2006, two plant employees operating in Rostov-on-Don were sentenced under Article 146(3) of the Criminal Code to four years and six months of actual imprisonment (and fined \$15,000). This is the toughest copyright-related sentencing ever assessed in Russia for copyright infringement. It resulted because these were the defendants' second convictions (their previous sentences had been suspended), so automatic prison sentences were imposed -- although the length of the sentences was surprising. On October 25, 2006, RAPO participated in a proceeding that resulted in the successful criminal prosecution of the director of the Simplex Disc DVD plant. The defendant was given a suspended two-year prison sentence and the plant's license was revoked. The court agreed to damages of 22 million rubles (US\$815,000) to be paid to RAPO's members (although this can only be secured through a subsequent enforcement proceeding). Another exception occurred in June 2002 when the Disc Press MSK plant (raided in 1999) was finally closed and a Zelenograd court handed down four-year prison sentences to two operators of the plant.

The more typical case is that of the Synograph plant, raided in October 2000. There was a four-year criminal investigation aimed at the director of the plant. The plant long-ago changed its name and remained in operation; in 2006, after years of delay, a lower court finally heard a criminal case against the former plant director. Although he was convicted and sentenced, the director was ultimately acquitted by an appeals court.

In addition to raids and criminal actions, rightholders have brought civil law suits against the plants directly; these actions are summarized in the Civil Enforcement section below.

As the Side Letter requires, Russia must undertake vigorous criminal enforcement against the plants and, in particular, the plant operators (and not, as has been suggested in the past, leave this enforcement to private party action). According to the Entertainment Software Association (ESA), Russian organized crime syndicate pirates of videogame material are so well entrenched that they "label" their product. Russian produced pirated entertainment software products are also localized into Russian and, in some instances, the language of the country to which the pirate exports are destined (for instance, Poland). Pirated videogames produced in Russia have been found in neighboring Eastern European countries, and as far away as Israel. The Motion Picture Association (MPA) reports that DVDs are being locally produced in seven or

eight foreign languages, not including Russian, indicating that the organized crime syndicates are producing these DVDs strictly for export. The music industry reports that Russian produced CDs have been found in many of these same countries – over 27 in all.

Since 2004, plant licensing authority has rested with the federal service known by the acronym FSCLMM — Federal Service for Supervising Compliance with Laws Regarding Mass Communications and the Protection of Cultural Heritage. The FSCLMM (also known as Rosokhrankultura) is a part of the Ministry of Culture. However, Rosokhrankultura has responsibility only for the licensing of optical disc plants that produce music or DVDs, not computer software (according to Federal Law No. 80-FZ “On Licensing of Certain Types of Activities”). Separately, copyright policy is vested in the Ministry of Culture and the Ministry of Education and Science. The Federal Service on Intellectual Property (Rospatent) is now in charge of industrial property and trademarks.

Until recently, the Russian Government used (2002) reproduction and licensing regulations to provide licenses for replication facilities for optical discs and analog tapes. Changes were made in 2006 to the regulations. The regulations allow for unannounced inspections of replication plants and for the suspension, as well as the initiation of the cancellation, of operating licenses of facilities found to be in breach of the regulations (Article 13). Thus, Rosokhrankultura issues and checks licenses, and can suspend a license, but not close a plant, absent a court order. The revised Licensing Regulations (2006) foresee only one visit every five years to each plant, absent information about piracy at a plant. Making matters more confusing, inspection authority has been divided between two Culture Ministry bodies-- Rospechat (regular plant visits) and Rosokhrankultura (license suspensions). Unfortunately, in late 2006, Rosokhrankultura, in a few instances, inspected plants and collected exemplars, without rightholder participation or knowledge. Inspections should be increased in frequency and intensity, and should also take place on a surprise basis. A high level of cooperation with rightholders is critical to the success of this program, as is the collection of exemplars (and sharing information with rightholders about them) to facilitate the effective forensic examination of discs found in the marketplace.

Another major shortcoming is the lack of deterrent criminal penalties for such violations and the inability to seize and confiscate the equipment used for pirate production. One continuing loophole that the pirates have exploited is that the equipment is leased by one party, and the plant owned by another – this allows the leasing party to seek a return of its equipment when a plant is raided because Article 81 of the Criminal Procedure Code bars confiscation of such leased equipment. It is expected that these deficiencies will be corrected by new regulations and legislation, as well as more effective plant enforcement activities, all of which are (June 1) requirements of the Side Letter.

As noted, according to special regulations adopted by the Ministry of Interior (MOI) in 2005, MOI officers have the right to 24-hour access to all “restricted access” (RARE) facilities for the purpose of conducting raids on optical disc plants located on these restricted access (RARE) properties. The full scope of MOI’s authority remains unclear, however. As required by the Side Letter, Russia must now use whatever authority it possesses to suspend the operations of these enterprises involved in piracy, and to seize piratical goods and the machinery used to manufacture them pending a (court) order for destruction. Further, Rosokhrankultura must suspend plant licenses immediately upon presentation of evidence of piratical activity, and, the courts must act promptly to issue license revocation orders thereafter.

The business software industry reports that in 2006, optical disc piracy remained at the same level as in 2005. While the quantity of channel raids (including those against vendors/shops of burned discs) significantly increased, the business software industry reports only one raid conducted against an optical disc plant in 2005, and none in 2006. Under the current optical disc regulations, the reproduction of software on optical discs is not even subject to licensing (only audio and video works are covered). Amendments to correct this deficiency were proposed by the Ministry of Culture in April 2005, but have yet to be adopted.

In short, the existing laws and regulations pertaining to plant licensing fall far short of IIPA's model optical disc legislation (provided to the Government of Russia), and is demonstrably inadequate — evidenced by the fact that the existence of these regulations has done little to stem, or even slow, the production of pirate discs in the country's optical disc facilities. Until better provisions exist (as required by the Side Letter), however, the existing laws must be utilized to the fullest extent possible. Any new optical disc licensing regime must, among other things, include mandatory SID codes as well as the regulation of the importation of optical grade polycarbonates used in the production of optical media.

Raids and Seizures in 2006

As noted, in 2006, although all of the plants were “visited” (albeit, not surprise inspected) by the government, there were only 8 criminal actions taken against individuals in seven of the optical disc plants. There were also many raids and the seizure of illegal materials, some involving the plants, according to Russian Government reports and the copyright industries.

In 2006, the recording industry was involved in 486 raids throughout the country. The raids resulted in the seizure of 2.57 million CDs, 113,776 (burned) CD-Rs, 189 stampers and 106,623 cassettes. In addition, during those raids, more than 5 million DVDs were seized (which included 130,000 music DVDs). The recording industry also reported that in 2006 it participated in raids of five suspected illegal optical disc plants. In four instances, the prosecutors initiated a criminal investigation. The recording industry is hopeful that in 2007, there will be further criminal proceedings brought against plant operators in the 19 cases of plant raids undertaken between 2004 and 2006 but for which no criminal actions have yet proceeded. Another positive outcome in 2007 would be the securing and removal by the police of the manufacturing lines at plants that have been raided (as happened in September 2006 against the Media Systems plant). This has, unfortunately, not been a regular occurrence.

In 2006, the motion picture industry's anti-piracy organization RAPO participated in twelve raids on suspected illegal DVD plants, including various plants in Tver, Zelenograd, Saint Petersburg, Moscow and elsewhere in the Moscow region. The motion picture industry reported that a total of 16 million DVDs were seized in 2006. RAPO and the police raided 15 warehouses in 6 cities (St. Petersburg, Tver, Kazan, Rostov, Samara and Mitishy), yielding a total of 9.68 million pirate discs.

In October 2005, a plant in Kazan, Tatarstan, located on a RARE facility, was raided. Although a case against the director of the plant (Laser Style) was commenced, it was closed due to a lack of evidence. In a second case in 2005 in Kazan, also against a RARE facility plant, a case against a plant director was closed due to a grant of amnesty. The plant in Tver that was also raided in December 2005 was found to have 5 unlicensed DVD lines and over 21,000 pirate DVDs. The lines were sealed by the local Economic Crime Police. The investigation is continuing and the plant director (but not the plant owner) is in prison awaiting the investigation to conclude.

Here are some recent examples of successful raids undertaken by RAPO and the Russian government: in Tver, a raid was run on the Media Systems plant in October 2006 in which 7 DVD lines were disabled and placed into a Moscow police storage facility. The plant director (but unfortunately, not the plant owner) was arrested and an investigation is ongoing. In November 2006, an optical disc plant and a warehouse in Kazan (another RARE facility) was raided. During the raid, moulds, a printer, 208 stampers and approximately 20,000 pirate DVDs were seized from the plant, and over 1 million pirate DVDs were seized from the warehouse. As a result of the plant and warehouse raid, two criminal cases have been initiated by the local prosecutor. In another raid, this time in Samara in late November 2006, a warehouse (in a block of apartments) was raided by the Criminal Investigation Department (and RAPO); over 1.5 million pirate discs, most of them DVDs, were seized. There were reports that the Samara warehouse belongs to a local company “Soyuz” whose warehouses were raided in September 2005 yielding over 3 million illegal discs. In November 2006, in Mytishchi, near Moscow, the Interior Ministry police (with RAPO cooperation) raided a warehouse and seized more than 500,000 pirate DVDs, 90% were pre-release titles (of MPA member companies), the rest were Russian pre-release titles. In December 2006, in St. Petersburg, the Economic Crime Police (DOI) along with RAPO raided a warehouse seizing 180,000 pirate DVDs; a criminal case was initiated.

In 2004, to address retail piracy, the Government of Russia adopted a legal ban on the street sales of audio and audiovisual products, for example, at kiosks, especially in Moscow. This did result, at least in the short term, in a significant reduction in the availability of pirated home video entertainment, especially on the streets of Moscow. The music industry reports that street sales are no longer a major problem, but market piracy is — for example, in markets such as in Tsaritsino. Absent, third party liability, action against the market operators is hard to effectively enforce. The motion picture industry reports very differently, that the street sale ban has been irregularly enforced and DVDs remain widely available. Piracy of DVDs in retail outlets such as in supermarkets (large and small), specialty shops, and large kiosks, is rampant. In Moscow alone, there are approximately 1,500 kiosks, shops and trading places (some in supermarkets) that sell only pirate DVD product. Such piracy can be eradicated: for instance, during a U.S. Government delegation meeting in Moscow with Russian officials in late January 2007, virtually all pirate product disappeared from shops, kiosks, and markets (or the stores were closed). On February 5, following the U.S. delegation’s departure, pirate product returned to these establishments. This clearly demonstrates that the Russian Government can effectively act against the pirate market when it chooses to do so.

Retail cases have resulted in some administrative fines, but these are generally of a *de minimis* nature. In 2006, amendments were considered but never adopted to expand the scope of the kiosk and street sale ban to (business and entertainment) software and databases; we recommend its immediate enactment.

The pattern of successful raids without prosecutions (with a few exceptions) is a recurring problem. It is estimated that about half of the pirated product seized in raids in Russia finds its way back into shops and kiosks. The Government of Russia must put a stop to these practices.

In 2006, as in other years, large-scale Ministry of Interior operations were undertaken, for example, one during the G-8 Summit in St. Petersburg, which resulted in police raids at numerous markets. In another operation (named Set), Department K officials acted against counterfeit products distribution and products in several regions — in Orenburg, Severdlovsk, Tomsk, Krasnoyarsk, Kazan, Tver, Gorno-Altaysk City, Penza City, Surgut City, and Kemerovo,

among others. These operations resulted in numerous raids at markets, shops, vendors, and warehouses, and the seizure of pirate audiovisual and software products.

The Business Software Alliance (BSA) reports that in November 2005, a hard disk loader was sentenced to one year of actual imprisonment and fine of \$900; and, in September 2006, there was a conviction in a CD-R case, with a sentencing of one year of actual imprisonment. BSA also reports that there has been progress in a case arising from a November 2005 raid by Economic Crime Police of Moscow on the Unitekhnoplast Ltd. plant located in Lobnya. In that raid, the police seized a number of CD stampers, moulds for CD replication and counterfeit CDs, including some containing illegal Microsoft software. Preliminary damages were estimated at over \$70 million. A criminal case was initiated in December 2005, with the first criminal hearing scheduled for February 2007.

Continued High Piracy Levels and Other Problems

The piracy levels and dollar losses in Russia are very high for an economy as well developed as the Russian market. These high piracy levels cost the Russian economy millions of dollars in lost jobs and lost taxes. In a study undertaken by the software industry (BSA/IDC Study, December 2005), it was estimated that if levels of piracy could be reduced by 10 points, it would add \$23.5 billion to the Russian economy and create 33,700 new jobs — more jobs than are currently employed in Russia's hardware, software, and services sector combined. It would also generate \$15 billion in local industry revenues and \$823 million in tax revenues.

The motion picture industry reports very high piracy rates for DVDs. Foreign producers have worked to quickly get legitimate locally replicated DVDs into the Russian market and to lower the prices of legitimate product. However, development of the home entertainment market, as well as further growth in other markets, have been stymied by rampant piracy. The 2005 Russian home video revenue total was less than the total five years ago. Home video revenues represent just 4% of the total Russian market, as compared to nearly 50% of the global media market. Moreover, telecine copying of theatrical prints for online piracy is a major problem in Russia. (Telecine is the copying of theatrical prints into other formats, including digital, which can then be uploaded onto the Internet). Since 2004, 60 movies have been pirated using Russian prints as the source, and investigations have revealed 22 telecine machines in Moscow alone. Camcording from local theaters and Internet piracy, with such active websites as DVDAvenue.tv and www.film-dvd.ru, are also problems.

The recording industry reports that the closure of the former Gorbushka market resulted in the migration of illegal sales to other sites (although there have been improvements at one such site -- the Rubin Trade Center, known as La-La Park). The market problems are especially bad on the outskirts of Moscow, for example, at Tsaritsinio. Piracy levels remain very high (at 65%), as well as CD piracy (over 65%), despite major raiding activity and the expenditure of major resources by IFPI. Overall losses in the recording industry were \$423 million in 2006. This figure represents physical copy losses; in 2005, the figure was \$450 million. The drop from 2005 can be attributed to a migration of piracy to the Internet.

The level of piracy for entertainment software is 72% of the market. Russian syndicates continue to be involved in a significant portion of the production and distribution of PlayStation® and PlayStation2® videogames and personal computer games. While the majority of pirated video game product in Russia is replicated domestically, pirated products replicated in Ukraine are also entering the market. The criminal syndicates involved in factory replication of pirated entertainment software also localize and customize the pirated products not only for the Russian

market, but also for markets such as Poland. At least one company (“Hobbydisc”) openly replicates and self-brands pirated versions of legitimate entertainment software titles. Although its products have been successfully removed from legitimate distributors’ inventory, it is still widely present in the Gorbushka market (and while there have been improvements at Gorbushka, additional anti-piracy work there is critical). The growth of other replacement pirate markets on the outskirts of Moscow is also of concern to the industry.

Although pirated entertainment software products continue to be available in Moscow and other larger cities, the entertainment software industry reports that the areas where pirated product is available on a commercial basis is narrowing. Many of the kiosks that used to sell pirated entertainment software products within Moscow have been removed, and it is rare to find pirated video games in larger retail chains. Most of the illegal product is found in flea markets (and there are estimated to be 50,000 such markets nationwide) and street vendor stalls. However, piracy remains rampant in other key cities such as St. Petersburg and Vladivostok. Piracy at Internet cafés continues to be problematic; there are approximately 6,000 cafés in the country with less than 5% licensed.

Pirate syndicates continue to run illegal distribution networks not only in Russia but also in the surrounding countries to which Russian-sourced pirated products are exported. It is widely believed that Russian groups are involved in the distribution of pirated entertainment software products in many Eastern European countries, including the markets in Poland and Latvia. Given these circumstances, it is imperative that the Russian Government initiate investigations into and criminal prosecutions against such piracy operations. In addition, the government must also improve border enforcement measures to address the export of Russian-produced pirated video games. With the majority of pirated product in Russia being domestically replicated, for both the local and export market, export controls or at least a robust inspection regime is critical to stemming the flood of pirated video games (on optical media) emanating from the country.

Book piracy, both in hard copy and in the digital realm, continues to cause significant harm to the publishing industry in Russia. While bestsellers were the target of the pirates in the past, popular items for pirates now also include an array of reference works and textbooks, increasingly a large market in Russia as the penetration of English-language materials in the market grows. Unlicensed imports of pirated reprints from neighboring countries, and pirated reference books and medical texts, still abound. Illegal commercial photocopying is also a problem, especially in the academic sector. In addition, the “hidden print run” and “overrun” problems remain, where printers of legitimate editions deliver additional unauthorized copies to unauthorized distributors before delivering books to legitimate publishers.

Most importantly, publishers are also experiencing a significant increase in Internet piracy, in the form of unlicensed electronic files. Thousands of academic and professional textbooks and reference books as well as fiction bestsellers are widely available for download on websites in Russia, or for purchase as unlicensed ebooks. These websites, run by Russian entities and hosted on Russian ISPs, are operating without any interference from Russian authorities. Sites such as the “ebook” family of sites (<http://ebook-mega-store.com>, <http://ebooknetstore.com>, <http://download-ebook.org>, <http://ebookscollections.com>, <http://www.ebooknetstore.biz> and <http://www.ebooknetstore.info>) and others such as <http://www.avaxhome.ru>, <http://www.demonoid.com> among many others, are sure to stunt the growth of the book market in Russia. The Association of American Publishers (AAP) estimates losses in Russia in 2006 at \$42 million.

Criminal Enforcement

The criminal enforcement system in Russia remains the weak link in the Russian copyright regime, resulting in the extraordinarily high piracy levels and trade losses. In 2003, the Criminal Code was improved, and cooperation with law enforcement on the ground has, as a result, been enhanced. However, significant problems continue, including delays in completing criminal investigations, failure to address major targets, and a judiciary that has failed to recognize the severity of the problem, and which therefore fails to deal with copyright offenses in a severe enough manner to provide deterrence. Although the Criminal Code was improved, enforcement continues to be hampered by a lack of uniform guidelines for police, prosecutors and judges.

Changes of the Russian Criminal Procedure Code, which entered into force in 2006, allowing Russian police to initiate criminal cases of copyright infringement, have had a positive impact on Russian police activities, as reflected in a sharp increase in the number of police raids. A change to the Russian Criminal Code, introduced in 2006 and expected to be finally adopted in 2007, would re-categorize copyright infringement as a “serious” crime. This too, will have a positive effect on enforcement.

Over the past five years, less than one-third of the criminal cases were heard by the courts, with the other two-thirds being dismissed for a variety of reasons. There has been a recent improvement in the number of cases initiated by prosecutors as well as an increase in the number of such cases brought to court. According to Ministry of Interior and the Prosecutor’s Office statistics, the Russian authorities initiated 4,001 criminal cases for copyright infringement in the first half of 2006 (compared to 2,924 in all of 2005); 2,298 cases were sent to criminal courts in that time period (compared to 2,195 in all of 2005); and, the Russian courts convicted 3,400 individuals in the first 11 months of 2006 under Article 146 of the Criminal Code (compared to 1,450 in all of 2005). Despite these improvements, the sentences imposed by the courts remain woefully non-deterrent; for example, the motion picture industry (RAPO) was only able to secure the imprisonment of five offenders in all of 2006 (and none for pirate DVD replication). A total of only 6 offenders were jailed in 2006.

The criminal enterprises are increasingly turning to the Internet as a means of distributing their counterfeit products. The business software industry reports that there is a persistent problem of counterfeit software promoted and sold all over the world using Intranets (which are difficult to police), as well as via unsolicited e-mail advertisements (spam) and mail-order services. The absence of clear methodologies for police and investigators to collect evidence and prosecute Internet crimes is a major stumbling block, as well as the lack of jurisprudence regarding ISP liability. The business software industry recommends that the Interior Ministry and the Prosecutor’s Office publish detailed methodologies on how to collect and fix (especially electronic) evidence pertaining to IPR crimes committed on the Internet. They further recommend that these cases be referred to Department K (high tech) at the Ministry of Internal Affairs. IIPA understands that in October 2006 Department K made internal recommendations to its police to target end-user piracy with warning letters to companies which could be used (if ignored) to show criminal intent. While well intended, this initiative may backfire as it will give warning to business in advance of any raids. To overcome the lack of experience by investigators and prosecutors, the business software industry continued its extensive training programs in Russia.

Internet piracy is growing, and remains virtually untouched by the Russian enforcement authorities. For example, the world’s largest server-based pirate music website – allofmp3.com

– remains in operation even after two on-going criminal investigations (including a criminal case pending for more than 8 months), and a singling out of this pirate for closure by the Russian Government in the Side Letter. The Russian law is clear (and has been confirmed by the Russian Government) that this type of piracy is illegal, and now as required by the Side Letter, that the Russian authorities will close pirate websites down permanently. In addition, the role of unauthorized collecting societies must be curtailed – which is required in the Side Letter (by June 1, 2007). ROMS and FAIR, in particular, have continued their illegal practice of issuing licenses for the Internet distribution of sound recordings owned by RIAA members (and underlying compositions owned by NMPA members), despite the fact that ROMS and FAIR have no rights to do so. Other rogue collecting societies have followed ROMS' example (including the distribution of sound recordings and musical compositions), including FAIR as well as FOSP. There are dozens of sites offering infringing copyright materials of films and music (such as www.threedollardvd.com, www.dvd-box.ru and others noted above) and books (such as the ebook websites noted above) that also need to be criminally investigated, closed down, and prosecuted.

The business software industry (BSA) reports a welcome increase in activity by the police against end-user pirates (both private and state-owned companies). In fact, compared with 2005, end-user pirate raids increased 50%-300%, depending on the particular region -- but much more needs to be done, especially in particular problem cities such as St. Petersburg and cities in Siberia. However, only 10%-20% (again, depending on the particular region) of raids resulted in the initiation of criminal cases (although this number too has greatly increased in the past year). The police continue to prefer to target the easier-to-prosecute CD-R pirates over hard-disk loaders or end-user cases. The number cases against hard disk loaders has actually declined, although the market testing conducted by the software industry seems to show that the reluctance on the part of sellers to make blatant offers of illegal software is to a large extent attributable to activities of Russian law enforcement authorities. Many prosecutors are reluctant to bring charges against the managers of companies using unlicensed software in business operations. Court decisions usually result in suspended sentences or small penalties (with more cases being administrative, not criminal, actions).

The business software industry reported the following enforcement statistics for 2006: there were 550 end-user raids and 572 channel raids undertaken. There were 114 criminal actions initiated against end-users (compared with 9 civil actions). Another 288 criminal cases were initiated against channel (distribution) pirates. There was a total of 50 criminal judgments against end-users overall, and 131 against channel pirates.

In spite of a significant increase in overall IPR enforcement activity by the police in 2006, the software industry reported the on-going problems of corruption, political connections, insufficient knowledge and inexperience by investigators and too-high burdens of proof for the overall poor enforcement record, especially criminal enforcement in Russia. As noted, in 2006, the business software industry continued to focus its enforcement activities on the prevention of hard disc loading ("HDL piracy") by computer resellers, and on the illegal use of software by corporate end-users ("end-user piracy"). The industry reported that both channel and end-user cases were conducted with good police cooperation, but that much more sustained action is needed.

In sum, criminal enforcement is hampered by: (1) poor coordination between police and prosecutors; (2) the reluctance of prosecutors to initiate and pursue IPR cases; and (3) the failure of prosecutors to conduct expeditious investigations. The creation of specialized units of

police and prosecutors responsible for combating IPR crime could help alleviate these problems.

Administrative Enforcement

As in past years, retail cases are often handled under administrative machinery, resulting in very small fines. While pirate product is generally confiscated, shop operators are normally not the owners and the latter seldom get caught and fined. As in past years, the recording, business software and motion picture industries report numerous administrative raids. In 2005, amendments to the Administrative Code (in force December 27, 2005) added copyright-related cases. Under the provisions, an administrative investigation is allowed for up to two months (the old provision, was two days), and the statute of limitations was extended to a year; there were also penalty increases — from 30-40 up to 100-200 times the minimum monthly wage. These were long-sought improvements in the Administrative Code.

The business software industry (BSA) reported 23 administrative end-user cases were resolved in 2006 (and another 24 initiated), and 2 additional ones against channel (distribution) pirates (and 7 more were initiated). Over the past few years, the average administrative fine imposed has been about \$150-200 per case. This is viewed by the pirates as a cost of doing business, and is obviously not a deterrent. Market seizures continue to involve the employment of huge resources, since administrative penalties remain totally inadequate to deter piracy over the long term. The recording industry reported that although the law makes liable those who distribute material, the sources and channels of illegal material are rarely pursued. In lieu, most administrative actions against shop owners and sellers require payment of the same average fine (about \$200).

Civil Enforcement

In 2003, the recording industry (IFPI) commenced civil claims against some of the optical disc plants in Russia, seeking damages of millions of dollars, and a prohibition against production of the pirate CD titles named in the suits. This was the first time that civil causes of action were commenced in Russia against optical disc plants. IFPI was pressed to bring civil case by the Russian Government, which was convinced that civil procedures would prove effective. There were a total of 16 IFPI civil claims lodged against two plants. One of the plants settled and the other continued to fight the suit in the courts. Predictably, instead of this course proving effective, the case was bogged down with procedural hurdles, and by the time the court ruled against the plant (and ordered it to pay 500,000 rubles to each plaintiff, or about US\$150,000 total — a fraction of the actual losses) the plant had disbursed all of its assets. The plaintiffs have yet to recover anything from the defendants. As this indicates, civil proceedings are not a successful means to deal with optical disc piracy.

Civil enforcement is generally not effective, and especially not against Internet piracy because: (1) it requires filings with undue evidentiary burdens (such as exhaustive chain of title documents); (2) even successful verdicts are limited to specific titles, rather than a rightholder's catalog of titles; (3) it is virtually useless against criminal syndicates since they are not corporate entities and have no place of business to be properly served. This latter deficiency, especially, must be corrected in 2007. The business software industry (BSA) reported that civil remedies remain inadequate, but that arbitration matters are increasing in number (a total of 9 cases against distributors were initiated in 2006).

Border Enforcement

Russia must significantly improve the lax border enforcement that permits the easy trafficking of illegal material into and out of Russia. Administrative changes were made in 2006 to move the border authority from the Ministry of Finance to the Presidential administration. The Side Letter requires the Government of Russia to direct customs officials to properly address this issue, as well as to fix the major legal flaw by providing border officials with proper and clear *ex officio* authority to commence criminal cases after making an inspection and seizure. Customs officials should be encouraged to consult and coordinate their actions with rightholders' organizations. There are numerous examples of Russian-made material being seized, not by Russian authorities who failed to detect illegal product, but by enforcement authorities in other countries (such as Poland). The music industry reports that Russian-made pirate CDs have been exported to over 27 countries. The entertainment software industry reports that Russian-sourced pirate video games are shipped into Poland, Latvia, Lithuania and Israel.

Russian Government Efforts to Address Piracy

In 2004, the government issued a "Working Plan of the Government Commission for Counteracting Intellectual Property Infringements" (after the 2002 establishment of an Inter-Ministerial Commission headed by the Prime Minister). Unfortunately, the commission has not properly involved rightholders in its activities which is essential if it is going to be successful.

Another impediment to effective enforcement is the fact that jurisdiction for such enforcement is scattered among many government agencies, including those responsible for policy and regulation (i.e., the Ministry of Culture and Mass Communication) and others with limited enforcement authority. Thus, there is no single agency responsible for IPR enforcement, nor a single key policymaker charged with authority to implement a comprehensive enforcement scheme. The newly adopted Civil Code, Part IV will only aggravate this situation. IIPA encourages the U.S. Government to press for clearer accountability on the part of the Russian Government. In the absence of an entity with responsibility for meeting the obligations of the IPR Bilateral Agreement, it is unlikely that compliance will be secured, resulting in delays in Russia's accession to the WTO and the unnecessary (but predictable) escalation of political tension.

GENERALIZED SYSTEM OF PREFERENCES PROGRAM

Even with piracy rates and losses among the highest in the world, Russia continues to receive trade benefits from the U.S. Government. In August 2000 IIPA filed a petition, accepted by the U.S. Government in 2001, to examine whether Russia should continue to be eligible to receive duty-free trade benefits under the Generalized System of Preferences (GSP) program. That petition is still pending; hearings were held in November 2005, October 2003, and March 2001. During the first 11 months of 2006, \$471.3 million worth of Russian goods (or 2.6% of Russia's total exports to the U.S. from January to November) entered the U.S. under the duty-free GSP code. While Russia was receiving these benefits, losses to U.S. industries from copyright piracy in Russia amounted to over \$2 billion. If Russia does not meet its Side Letter obligations by June 1 and does not show significant enforcement improvement, the IIPA recommends that Russia should immediately lose its eligibility for GSP benefits.

DEFICIENCIES IN THE RUSSIAN LEGAL REGIME

Overview of Legal Reforms

On December 19, 2006, President Putin signed into law the Duma's final adoption of Part IV of the Civil Code. This new and extensive law (consisting of 118 copyright articles) is meant to replace the entire existing Russian IPR regime – i.e., the Copyright Law of 1993 (as amended through 2004), as well as the patent and trademark laws. The Civil Code will go into force on January 1, 2008. There are many other steps that will need to be undertaken to tie this complex new law to the other essential IPR related laws, including the Criminal Code, the Criminal Procedure Code, the Administrative Code, and the Customs Code.

The adoption of Part IV was undertaken over the strong objections of the U.S. Government, the European Union, and other governments, as well as the advice of many copyright law experts. First, the Civil Code is very hard to and rarely amended, so the repeal of the copyright law will be replaced (in 2008) with an inflexible law that needs to regulate new as well as developing technologies. Second, there are many deficiencies in the law (summarized below), some even acknowledged by its drafters, which means the current Civil Code does not comply with TRIPs or the WIPO digital treaties, among other concerns. The law is in some instances unclear – a fact not surprising given its breath and the expeditious manner in which it was drafted and adopted without input from copyright experts. The Russian Government has acknowledged in the Side Letter that the Civil Code is not compliant with TRIPs, the WCT or the WPPT, and has agreed to undertake amendments by June 1, 2007. In addition, repeal of the Copyright Law will, it is feared, create confusion about the enforcement of IPR violations via the Criminal Code, the Criminal Procedure Code, the Administrative Code, and the Customs Code.

In addition, to the Civil Code deficiencies, there are a number of other critical legal reforms that Russia must undertake to improve copyright protection and enforcement, as well as to ensure accession into the World Trade Organization. Since enforcement remains the priority of the copyright industries in 2007, we simply list the legal reforms that are necessary at this time and provide detailed requirements only for the much-needed optical media regulations and the Civil Code deficiencies. Details about the other legal reforms can be found in prior IIPA reports at <http://www.iipa.com/countryreports.html>.

First, a proper optical media law must be adopted to:

- Seize infringing product and machinery, as part of the (unannounced) inspection process, undertaken with the cooperation of rightsholders.
- Require plants to keep meaningful order, production, and delivery records.
- Require plants to adopt source identification (SID) codes so that the source of illegally produced discs can be traced.
- Introduce sanctions (including criminal penalties) for infringing the regulations.
- Control the importation of raw materials (optical grade polycarbonate) used in the production of optical disc media.

The complete details of what is necessary for effective optical media regulation can be found at the IIPA website at <http://www.iipa.com/rbc/2003/2003SPEC301RUSSIA.pdf> on page 14. The Side Letter requires Russia to adopt optical media law reforms by June 1, 2007. IIPA recommends that any plant licensing regime should extend in scope to the operators of telecine machines and mastering laboratories used to pirate audiovisual works. Also, Russia needs to

adopt anti-camcording legislation to facilitate the enforcement and prosecution (with jail sentences of a year or more for first offenses and longer terms for repeat offenders) for those involved in recording films from theater screens to use in pirate products.

Also needed for effective enforcement are:

- Supreme Court guidelines directing that the *ex officio* authority in the Criminal Code and Criminal Procedure Code is properly utilized to commence criminal proceedings; also, amendments are needed to those codes to allow for the confiscation of equipment used to make illegal copyright materials. (The Civil Code in Articles 1252 and 1302 is meant to address this, but: (a) is it not linked to the Criminal Code or Criminal Procedure Code and (b) is flawed – allowing the seized equipment to be sold for state income).
- Amendments to strengthen the implementation of the Code on Administrative Misdemeanors and apply deterrent fines, especially for legal entities and their officers.
- Amendments to the Customs Code to provide the proper *ex officio* seizure authority (the code was last amended effective January 1, 2004). The *ex officio* authority amendments were drafted but never considered in 2006; they are now required by the Side Letter, and must, per that agreement, be adopted by June 1, 2007.
- Amendments to the Civil Code, Part IV to further clarify and ensure the adoption of responsible business practices by collecting societies to avoid abuses that harm right holders' ability to exercise and enforce their own rights. This is also a June 1, 2007 Side Letter requirement.
- Regulations that cover telecine operators (i.e., of film to video machinery) and film mastering labs.
- Introduction and enforcement of anti-camcording legislation that facilitates enforcement; provides for deterrent jail sentences and higher penalties for repeat offenders; and that ensures that anti-camcording measures are not undermined by the private copying exception.

Amendments to the Criminal Code (adopted in 2003) provided *ex officio* authority to allow prosecutors, but not the police, to commence and investigate certain IPR criminal cases. This was a part of the amendments to make prosecution of copyright-related cases a “public” matter, meaning it no longer requires a formal complaint from the right holder, although as a matter of practice such a complaint is still necessary. There was also a corresponding Criminal Procedure Code change to provide enforcement authority both to the police and prosecutors. On July 3, 2006, amendments to Article 151 of the Criminal Procedure Code went into force to enable the police to also have investigative jurisdiction of IPR cases (since the police actually do the investigations and since the prosecutors are often backlogged with other serious crimes). This was a positive step. Separately, IIPA continues to recommend that Article 146 be amended to specify that legal entities can be criminally liable for IPR violations. The Civil Code provides liability for legal entities in Article 1253, and the Administrative Code also provides this liability, but the Criminal Code does not provide criminal liability for these entities.

IIPA has additional recommendations to improve enforcement. First, there needs to be an all-embracing approach to fighting industrial piracy – to implement a comprehensive strategy of criminal prosecutions against the managers and owners of the optical disc plants and other legal entities involved in copyright infringement, as well as to adopt administrative procedures and penalties against legal entities (fines, confiscation of equipment) and deterrent criminal penalties. Second, there needs to be special anti-piracy groups and/or detailed IPR enforcement officers in the LEAs (within the police departments in each city). Third, there must be actions taken to confiscate equipment used for pirate production as evidence (irrespective of its ownership, for example, by third parties) until a court decision is rendered. Fourth, there needs to be a bifurcation of duties on IPR enforcement within the Ministry of the Interior – one directed against physical piracy and a second to combat high-tech crimes, such as Internet piracy. Fifth, there needs to be expertise developed to detect counterfeit products, to provide the necessary measurers for conducting effective, professional, and expeditious investigations of counterfeit products (for example, by using an IPR matrix). Sixth there needs to be provisional measures, to provide broad and unrestricted implementation in conformity with the TRIPs Agreement and as foreseen by Supreme Court’s Plenary resolution of June 19, 2006.

A few other miscellaneous legislative changes are needed: the Criminal Code needs to be amended to ensure that Internet piracy is a crime without regard to the “harm caused” by the infringement, and as noted, there must be criminal sanctions applicable for violations of the licensing regulations for the production of audio or audiovisual materials.

IIPA continues to recommend that the Supreme Court adopt a decree setting forth sentencing guidelines for judges, advising the courts to impose deterrent penalties as provided under the penal code (Article 146), and detailing the application of presumptions of ownership in criminal cases. The Side Letter requires a resolution noting to judges and prosecutors, the importance of the prosecution of IPR crimes and the harms caused to society by these crimes.

A major revision of the Civil Procedure Code (effective 2003) set the rules for initiating and examining civil cases, including disputes pertaining to copyright and neighboring rights infringements. Unfortunately, the code still does not contain the necessary civil *ex parte* search procedures (required by the WTO TRIPs Agreement). These are essential tools for effective enforcement in the software industry. In 2002, a new Arbitration Procedures Code in Article 72 included civil *ex parte* search provisions in a more limited context. In addition, the Plenum of the Supreme Court adopted a resolution regarding the application of civil code provisions to IPR cases. It urged the courts to apply provisional measures in copyright infringement cases and provide general guidelines. However, provisional measures have, in the past, proven ineffective because the courts have applied a very high burden of proof for *ex parte* searches, one that, for example, cannot be met in end-user cases where the evidence of infringement is in the hands of the defendant. The software industry continues to report that these provisions are rarely used and that overall, the procedure remains a difficult and onerous proposition.

The Civil Code, adopted on December 19, 2006, contains several deficiencies. These include two overarching concerns: first, that there are many new and unclear legal terms and definitions (that will likely be unenforceable); and second, that there are administrative law principles throughout the Civil Code that likely cannot be enforced by civil or criminal procedures.

The Civil Code contains many flaws, including: a “three-part” (fair use) test that is too broad, as well as overly broad private and other copying exceptions (Articles 1273 and 1274); a broad exception for the use of computer programs that violates the three-part test (Article

1280(3)); camcording provisions that are negated by a personal use exception (Article 1273(6)); provisions on technological protection measures that are too narrow for treaty compliance, are negated by a “fair use” exception, and which provide no remedy for TPM violations (Article 1299(3)); a too-narrow construction of the protection for temporary copies of computer programs, i.e., only where it is “essential for making available” (Article 1270(1)); the over-regulation of contracts (including registration requirements) in Articles 1232 through 1238; unclear provisions with regard to the protection of pre-existing works (Articles 1281 and 1282); and, similar problems regarding fair use, personal use, TPMs and the overregulation of contracts for neighboring rights (sound recordings) (Articles 1306 through 1309). It is unclear whether the Civil Code provides national treatment, as required by the treaties, for non-exclusive rights (Article 1231). Finally, and perhaps most importantly, steps need to be taken to make certain that essential – treaty required – remedies for IPR infringements found in the Criminal Code, the Criminal Procedure Code, the Administrative Code and the Customs Code will continue to apply in light of the adoption of the new Civil Code and the repeal of the copyright law.

There are several positive features of the Civil Code as well: it purportedly would clarify that collective administration organizations can only operate within the mandates they receive from rightholders (Article 1242); it adds (civil, but not criminal) liability for legal entities at Article 1253; it adds remedies for the seizure and destruction of materials and equipment used in infringements (Article 1252 and 1302), but it negates these remedies with an exception for the sale of materials by the state for “income”; it clearly protects computer programs as “literary works” (Article 1261); it properly provides for the rights of ownership and exploitation of audiovisual works (Articles 1240 and 1263); it provides a clear making available right (Article 1270(11)) consistent with the digital treaties; it provides a private (personal purpose) levy (Article 1245); and, it provides for statutory damages (ranging from 10,000 to 5 million rubles) (Article 1301).

IIPA recommends the introduction into the Civil Code of a clear definition of “Internet Service Provider” and confirmation of clear (third party) liability in civil and criminal law for facilitating Internet piracy, as well as a duty to provide all necessary information to law enforcement agencies in Internet piracy cases.

In December 2005, the Code on Administrative Misdemeanors was amended (consistent with IIPA recommendations). The amendments: (1) extended the timetable for pre-action investigation from two days to two months; (2) extended the statutory limitations to one year (from two months); and (3) increased the penalties for administrative violations of copyrights and related rights (from 30-40 up to 100-200 times the minimum monthly wage).

IIPA continues to note that the development of legitimate markets is harmed by the high taxation system on video rentals. Since 2002, a 24% profit tax on revenue from video rentals, along with other “vice” activities such as gambling, has been in effect. This tax is very high (although an improvement from the previous 70% rate). The Government of Russia felt that lowering the tax to 24% would help the video market’s growth in Russia, but the lingering high rate combined with the growth of DVD piracy has, for the most part, overwhelmed the legitimate market for rentals.

In addition, customs authorities in Russia assess duties on the royalty value of imported audiovisual materials (such as television master tapes, DVDs, etc.), rather than solely on the physical value of the material. This is contrary to prevailing international and European legal practice. While a new Customs Code entered into effect in 2004, the Law on Customs Tariffs,

which underlies the royalty-included valuation, remains intact. Customs duties which are assessed on potential royalties serve as a form of double taxation, since royalties are also subject to withholding, income, value-added, and remittance taxes, and are a barrier to further growth of the legitimate Russian audiovisual market in favor of the illegitimate operators who do not pay any taxes at all.

FACT SHEET: U.S. – RUSSIA BILATERAL AGREEMENT (NOVEMBER 2006)

On November 19, 2006 the Governments of Russia and the United States entered into a IPR Bilateral Agreement (“Side Letter”) in the context of Russia’s efforts to accede to the WTO; it was signed by Russian Minister Gref and Ambassador Schwab.¹ According to the Side Letter, U.S. support for Russia’s entry into the World Trade Organization (WTO) is conditioned on meaningful copyright law enforcement with specific obligations that Russia must take to reduce piracy “on a priority basis” as well as requirements to adopt the laws necessary to accomplish this goal.

Enforcement Steps Required by the Side Letter for 2007: Russia agreed in the Side Letter to make copyright enforcement an IPR priority, especially against illegal optical media plants, and to improve overall enforcement. In particular, the Side Letter requires the Russian Government to:

1. Address the optical disc problem, with the objective of permanently closing down illegal plants, by:

A. Conducting “repeated, unannounced inspections” of all known OD plants. “Such inspections will take place regularly, without prior notice, and at any time, day or night. If evidence of unauthorized production of optical media bearing content protected by copyright or related rights on a commercial scale is found, criminal proceedings will be initiated.” Russia will then be required to “[c]ontinue to conduct actions to find and shut down unlicensed plants producing optical media bearing content protected by copyright or related rights.” **Russia has not met this obligation. To date in 2007, according to IIPA’s information, Russian authorities have inspected only five out of an estimated 50 manufacturing facilities. We further understand that one plant, operating without a license, was closed. Both the optical disc plant licensing authority (Rosokhrankultura) and the Economic Crime Department of the Ministry of Interior are, at present, short staffed and under reorganization.**

B. Conducting actions to “find and inspect warehouses” storing pirate product, including the seizure and retention for evidence of illegal copies, as well as initiating “investigations to determine the owner, distributor, and manufacturer of such goods and prosecutions of these persons and enterprises” including “criminal proceedings...in cases of piracy or counterfeiting on a commercial scale.” **Russia has undertaken some warehouse and optical disc plant raids. However, the Russian courts have not imposed deterrent sentences against the owners or operators of warehouses and optical disc plants. In fact, in most instances, such cases cannot be initiated because of the inability to identify the relevant “owner.”**

C. “Ensuring that facilities on the territory of government-controlled military-industrial [i.e., RARE] sites are not leased or otherwise made available to companies producing optical media bearing content protected by copyright or related rights and immediately take action to terminate any existing leases.” **Russia has not met this obligation. IIPA understands that the Russian Government plans not to renew leases for these facilities when they expire, but this is a far cry from the Agreement’s commitment to “take immediate action” to stop these entities from being used in furtherance of piracy.**

D. Enacting legislation (by June 1, 2007) to “strengthen the licensing regime for optical media plants” including “grounds to deny applications for licenses and to suspend, and then immediately seek revocation by a court of, licenses of persons whose production premises are found to be manufacturing pirated product; enhanced recordkeeping requirements; and government monitoring of production.” This legislation must ensure that “each licensee will verify

¹ The text of this Side Letter, known formally as the U.S.-Russia Bilateral Market Access Agreement on Intellectual Property Rights, is available at http://www.ustr.gov/Trade_Sectors/Intellectual_Property/Russia/Section_Index.html.

that the customers for whom it produces optical media bearing content protected by copyright or related rights have authorization from all relevant right holders” and that “licensees mark optical media with data that identifies the licensee and the license number” and “that licensees use additional markings, such as source identification codes.” **Russia has not met this obligation. This obligation is key to addressing many of the current optical disc piracy problems – both the manufacturing and distribution of pirate material – and was supposed to be accomplished by June 1. There is no known timetable in the Russian Government to meet this obligation.**

E. Ensuring that grounds to deny, suspend or “immediately seek revocation by a court of a license” include violations of “any licensing condition,” and that by June 1, 2007 legislation will include a provision that “licenses will be denied to persons who have previously had a license revoked by a court for infringement of any license requirement, such as violation of copyright or related rights.” **Russia has not met this obligation. Rosokhrankultura has, to its credit, tried to apply such measures in a de facto manner, but the absence of clear statutory authority is limiting its success.**

2. Address the need for effective criminal enforcement, focusing in particular on piracy “committed for purposes of commercial advantage or private financial gain” by referring “to the Supreme Court of the Russian Federation a proposal for it to pass a resolution of the Plenum of the Supreme Court” to clarify for the courts their practices so that they impose stiff penalties for IPR violations, and requiring that judges “take into account the high degree of public harm from such infringement.” **Russia did adopt a resolution on April 29, 2007 (the US government and IIPA are awaiting an official translation).**

3. Address the need for effective border enforcement by “significantly increas[ing] the percentage of export shipments inspected” and to provide information to “appropriate authorities for investigation and prosecution.” Also, the government will seek to enact legislation (by June 1, 2007) “strengthening Customs officials’ authority to take actions *ex officio* with respect to suspected exports and imports of pirated or counterfeit goods” and “encourage Customs officials to use such authority.” **Russian Customs authorities are regularly conducting inspections, but the obligation for legislative reform has not been met. The continued availability of Russian manufactured illegal discs is evidence of the need for better enforcement.**

4. Address the need to combat the growing threat of Internet piracy “with the objective of shutting down websites that permit illegal distribution of content protected by copyright or related rights” (and especially for websites whose servers are situated in Russia (which in a footnote specifically says “[s]uch as allofmp3.com”) by:

A. Taking actions “against the operation of websites...that promote illegal distribution of content protected by copyright or related rights, such as phonograms (sound recordings).” **Russia has not met this obligation. The most notorious website (even noted in the Agreement), allofmp3.com, continues to operate, pirating U.S. and other foreign material with impunity. Despite the initiation of a number of criminal cases, allofmp3.com, and unauthorized collecting societies like ROMS and FAIR continue to grant “licenses” for content they neither own nor are permitted to license.**

B. “[I]nvestigat[ing] and prosecut[ing] companies that illegally distribute objects of copyright or related rights on the Internet.” **Russia has not met this obligation. Six months after this obligation, IIPA is unaware of a single case that has been initiated by Russian authorities against an Internet pirate.**

C. Enacting by June 1, 2007, legislative amendments to “provide that collecting societies may act only on behalf of right holders that explicitly authorize such action” and the “provisions needed to implement the World Intellectual Property Organization (WIPO) Copyright Treaty [WCT] and WIPO Performances and Phonograms Treaty (WPPT).” **Russia has not met this**

obligation. One change adopted by the Civil Code, Part IV, would clarify that collecting societies may only operate with a mandate from rightholders; but this legislation does not go into force until January 1, 2008. There are many other WIPO treaty obligations that Russia must meet – detailed in IIPA’s Special 301 filing in February – including properly protecting technological protection measures (TPMs), narrowing the scope of exceptions to protect rightholders, and providing effective enforcement provisions.

5. Adopt legislation to “fully implement the TRIPs Agreement and other IPR-related international agreements” to which the United States and Russia are already parties (as well as to “fully implementing the WCT and WPPT”). Ensure that any legislative, regulatory or other measures made prior to accession, i.e. Part IV of the Civil Code, will not “result in a lesser degree of consistency than exists on this date” (November 19, 2006) with the TRIPs Agreement or any other international IPR agreement to which the U.S. and Russia are parties. **Russia has not met this obligation. The details of the TRIPs deficiencies are provided in the IIPA’s Special 301 filing, but include especially the need to provide effective enforcement remedies.**

6. Ensure on-going dialog and work to implement the obligations above through a Bilateral Working Group, as well as to provide appropriate training to Russian enforcement officials. **The U.S.- Russia Working Group meets quarterly.**

The summary of these six Side Letter obligations illustrates the important enforcement actions that Russia must undertake in 2007 (most by June 1). Note that the Side Letter has the status of an international agreement under U.S. and Russian law.