

Testimony of Joseph Papovich
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Before the
United States House of Representative
Committee on Government Reform
September 23, 2004

Mr. Chairman, Ranking Member and other Members of the Committee, I appreciate the opportunity to testify today about intellectual property piracy.

I am Senior Vice President International for the Recording Industry Association of America, the trade group that represents the U.S. recording industry. RIAA's mission is to foster a business and legal climate that supports and promotes our members' creative and financial vitality. Our members are the record companies that comprise the most vibrant national music industry in the world. RIAA members create, manufacture and/or distribute approximately 90% of all legitimate sound recordings produced and sold in the United States. Prior to obtaining my current position, I served for 21 years in the Office of the U.S. Trade Representative. From 1994 until 2003, I led USTR's intellectual property efforts. So I am familiar with the subject of today's hearing from industry's and government's perspective.

Music is the world's universal form of communication. It touches every person of every culture on the globe to the tune of \$32 billion annually, and the U.S. recording industry accounts for more than one-third of that world market. Our members create employment for thousands of people, including singers, musicians, producers, sound engineers, record promoters and retail salespersons, to name only a few.

The importance of the U.S. recording industry, and intellectual property protection, to the U.S. economy

An important part of our nation's competitive strength lies in the creation of knowledge-intensive intellectual property-based goods and services. This is one of those economic activities that Americans do better than the people of any other nation. The "core" U.S. copyright industries account for more than five per cent of US GDP. The foreign sales and exports of U.S. copyright industries were nearly \$90 billion in 2001, an amount greater than almost any other industry sector, including automobiles and auto parts, agriculture and aircraft.

Therefore, international markets are vital to our companies and our creative talent. Exports and other foreign sales account for over fifty percent of the revenues of the US record industry. This strong export base sustains American jobs.

In this respect, the protection of our intellectual property rights abroad is vital to promoting America's competitive advantages in world commerce. As our trade deficit has soared, we call upon Congress to consider more closely the relationship between our widening trade and current account deficits and copyright piracy and to take steps to enable us to more effectively protect our intellectual property rights and to sell our products at home and abroad.

In a sense, the intellectual property of the United States is like a warehouse of ideas and creativity. For people to walk in and steal them is no more tolerable than theft of physical goods. And the sale of our recordings abroad makes a major contribution to America's current account balances. Each and every sale of a pirated product abroad that substitutes for the sale of a legitimate American product increases our current account deficit. As a result, Americans employed in competitive industries like ours are denied financial benefits that should have occurred but did not.

The Effect of Music Piracy

The piracy of music is almost as old as the music industry itself, but historically it was difficult for the criminal to reproduce copies as good as the real thing. Now with the advent of digital recordings criminals can reproduce perfect copies of any recording. There is massive manufacture and traffic of illegal CDs, both in the form of molded CDs that are produced in large plants, and increasingly CD-R's produced on blank optical discs with readily available computer CD-R burners

The illegal music trade is feeding the profits of international organized crime syndicates who are involved in drugs, money-laundering and other criminal activities. Music piracy is costing governments hundreds of millions of dollars in tax revenues.

In 2003, pirates sold 1.7 billion units of recorded music; worth an estimated \$4.5 billion—at pirate prices. Pirated optical discs accounted for 1.1 billion of these. Globally, 2 in 5 recordings are pirate copies. Total optical disc manufacturing capacity (video / audio CDs, CD-ROMs and DVD) – stands at well over 40 billion units, having quadrupled in the past five years and greatly exceeds legitimate demand. This creates a business environment ripe for exploitation by criminal syndicates, often shielded by governments hostile or indifferent to our interests. Given that pirate operations have few or none of the overhead costs associated with genuine production, the profit margins are incredible.

The battle against intellectual property theft must be unrelenting. Digital technology and internet piracy have greatly exacerbated our problems. Our country must employ every

tool at its disposal, including the critically important leverage provided by international trade agreements.

RIAA's 2004 Overall Priority Issues and Countries

Our priority countries are the biggest markets for pirate CDs--Russia, Brazil, Mexico and China. The emergence of commercial scale CD-R piracy is localizing pirate production, and forcing a change in anti-piracy strategies away from exclusively trying to control production and towards control of consumption (i.e. the offer for sale of pirate products in the marketplace). In addition, the rapid growth of the internet and personal CD-R burning as mechanisms for the unauthorized distribution of recorded music, is having the same impact as commercial piracy even though the individual actor may not be acting with any profit incentive, or possessing what one would ordinarily think of as "criminal intent."

In sum, we need more attention and resources dedicated to enforcement, both in the physical and on-line environments.

With respect to physical piracy, we need:

1. Adoption of optical disc regulations (requiring the use of source identifier—known as “SID” codes—in territories producing large quantities of pirate discs, or where the production capacity vastly exceeds legitimate needs--e.g. Russia, Thailand, Pakistan, Indonesia;
2. To ensure that criminal penalties are adequate in law and implemented in practice to serve as a deterrent in light of the fact that any fine, no matter what size, can be absorbed as a cost of doing business;
3. To amend criminal laws to make copyright offenses cognizable under organized crime and criminal conspiracy provisions, thus giving governments better investigative tools and resources in order to fight organized piracy;
4. To criminalize the provision of raw materials in furtherance of piracy; and
5. To ensure that law enforcement officials have “ex officio” authority to seize any infringing materials, and that they are directed to seize, without complaint from the copyright owner, any materials that are offered for sale. (This is necessary in light of the practical inability to control piracy by focusing exclusively on the suppression of illegal production--efforts need to be diversified to include market control).

With respect to on-line piracy, we need:

1. To secure ratification and implementation of the WIPO Copyright Internet Treaties to ensure that adequate rights are established online;

2. To ensure that ISP's are required by law to engage in reasonable business practices with respect to the detention and removal of infringing files, or by preventing access to their networks on the part of known infringers;
3. To amend criminal laws so that they apply to internet "piracy"--both by ensuring the application of principles of vicarious liability and contributory infringement, and most importantly by applying criminal penalties to acts undertaken WITHOUT any commercial purpose when they are done on a commercial scale, like making materials available through the internet as was done in the US via the Net Act; and
4. To increase the ability of law enforcement agencies from different countries to cooperate with each other in multi-territorial cases, including by securing broad adherence to the Cybercrime Convention.

Recording Industry Actions to address Piracy

Through our international affiliate, the International Federation of Phonographic Industries, or "IFPI", the recording industry maintains a global anti-piracy team of investigators and analysts, made up largely of ex-law enforcement personnel who develop civil litigation and work with law enforcement personnel in pursuit of criminal prosecutions. We also have an active online anti-piracy program. We work in close collaboration with governments, police forces and customs departments worldwide.

We are engaged in extensive educational efforts, designed to increase public understanding of the value of intellectual property and to improve overall awareness of copyright laws, on a global basis.

We work closely with national and international bodies to encourage adoption of laws that strengthen copyright protection and promote an environment in which our industry can continue to innovate.

Record quantities of discs and equipment were seized in 2003. An estimated 56 million pirate music discs—up from 13 million in 2001—were seized, while seizures of all formats, including cassettes and music DVDs, totaled 64 million units. The vast majority of seizures were in South East Asia and Latin America.

Enforcement actions are being concentrated at the source of pirate operations where we aim to confiscate manufacturing equipment and not merely pirate product, thereby imposing more significant "costs" to pirate operations. In 2003, our industry seized over 12,000 CD "stampers"—the master copy used to press illicit CDs. This is six times the number seized in 2002. There was also a substantial increase in the number of CD-R burners seized—nearly 15,000 in 2003 compared to just 5,000 in 2002.

Forensic analysis

We maintain a unique forensics laboratory at the IFPI headquarters in London that traces the manufacturing source of pirate CDs through microscopic examination and measurement. This has helped link infringing discs to source factories and resulted in many raids on suspect plants worldwide. This in turn encouraged several governments including Malaysia, Poland, Bulgaria and Russia to establish their own forensic programs.

This Committee should be aware that the recording industry is not sitting back and waiting for others to act. We are investing millions of dollars around the world to protect our products, but we are battling forces far beyond our ability, acting alone, to solve. First, government corruption in many other countries denies us any possibility of criminal or civil justice. In addition, and perhaps as part of this, there is a well-established link between piracy, organized crime, and even international terrorism which uses music piracy to divert huge sums of money to other criminal enterprises. Recent testimony by a Mafia boss from Forcella, Naples (February, 2003), clearly illustrated that the Mafia are directly involved in the production and distribution of pirate music, carving up the territory between various gangs and paying a share of profits to 'godfathers'.

The Importance of the U.S. Government to our industry

America's music composers, performers and producers could not survive in the battle against piracy, domestic and international, but for the absolutely critical and splendid assistance that we have received over the past 15 years from the United States Government, Executive and Legislative branches—Republican and Democrat.

We rely heavily upon our government for our very survival in combating the plague of music piracy. The U.S. Government does more than any other government in protecting its nation's intellectual property, and does so with vigor and determination, albeit with limited resources.

Since the passage of the 1988 Omnibus Trade and Competitiveness Act, intellectual property issues have been an integral part of our country's international trade agenda. When it comes to U.S. Government efforts in this regard, it all starts at the Office of the U.S. Trade Representative. USTR develops, coordinates and implements our nation's trade policy. With its small but highly dedicated staff of only 200 individuals, USTR provides leadership and negotiating expertise in nearly all trade policy areas.

It is in the context of the massive size and scope of our nation's international trade activity that we look for help in protecting our nation's creative wealth. Of course, USTR is not tasked with doing all these things alone. Its mission is to develop, coordinate and implement our nation's trade policy in conjunction with other relevant and highly interested agencies, including the Departments of State, Justice, the FBI, the Department of Homeland Security—particularly Bureau of Customs and Border Protection, and the Department of Commerce and, within Commerce, the U.S. Patent and Trademark Office, as well as the Copyright Office in the Library of Congress.

Ultimately, helping us battle piracy abroad requires the involvement of these and other agencies of the U.S. Government, including the Ambassadors and officers in many of our embassies abroad.

Existing Tools for Addressing International Piracy Problems

Congress has already provided several “tools” for our government to use in helping us better protect our intellectual property abroad, many of which are well described in the GAO Report that is the subject of today’s hearing.

Special 301: This is an extremely important tool to us. This annual review and report, mandated by the 1988 amendments to the Trade Act of 1974, requires USTR, with the active assistance of these other agencies, to identify foreign countries that deny adequate and effective protection of intellectual property rights or fair and equitable market access for U.S. persons that rely on intellectual property protection.

This annual review is an outstanding tool for leveraging other countries into making needed improvements to their intellectual property laws and/or enforcement. It also serves as the mechanism for the executive branch to set its annual agenda for how it will address intellectual property matters in our bilateral, regional and multilateral trade relationships, and how it will allocate its resources in combating intellectual property problems globally.

USTR and the other agencies do a very good job with the limited resources available to them, but there is little doubt that this program would be more effective if there were additional resources. For example, an extremely effective aspect of Special 301 is conducting “out-of-cycle” reviews of selected countries over the course of the year, and other less structured but intensive bilateral engagement. Otherwise, some countries conduct a flurry of activity prior to April 30 in order to avoid an undesirable designation in the report, then turn a blind eye to piracy once the report is issued. This can be remedied by re-visiting the most problematic countries over the course of the year by announcing that they will be reviewed again after a certain number of months. However, limited resources at several agencies, including at USTR, have limited the utilization of the very effective tool of out-of-cycle reviews.

“GSP” Trade Benefits: Another important tool in our trade policy arsenal is the conditioning of the grant of duty-free importation to developing countries under the Generalized System of Preferences (GSP) on adequate and effective intellectual property protection in such countries. The law authorizes the President to suspend or revoke all or part of a country’s GSP benefits if he determines that it denies adequate and effective intellectual property protection to U.S. right-holders. In the past, suspension of such benefits has been an extremely effective tool in achieving meaningful IPR improvements in these countries. We have pending petitions to suspend GSP benefits for Russia, Brazil, and other countries. An important decision regarding Brazil is due at the end of September. We hope the Administration will act upon our petitions, unless of course these countries make meaningful and sustained progress prior to this date.

The TRIPS Agreement in the WTO: An important multilateral tool is active U.S. Government participation in the World Trade Organization's Agreement on Trade-Related Intellectual Property Rights, or the "TRIPS Agreement. All 146 members of the WTO are obligated to provide and enforce minimum standards of intellectual property protection to all the other members. If they fail to do so, the WTO provides an effective dispute resolution process that provides with imposition of trade sanctions against countries that fail to comply with TRIPS obligations. The TRIPS Agreement, which came into effect in 1995, ensured that scores of countries adopted and committed to enforce fairly modern, substantive copyright laws. This was a tremendous achievement. Monitoring full implementation of the TRIPS Agreement, and aggressive use of WTO dispute settlement against non-compliance, remains a top priority for our association and our members.

The WIPO Digital Treaties: Digital technology, much of which came onto the market after the TRIPS Agreement came into effect, has brought many changes and challenges to international trade and perhaps none more so than with respect to the protection of intellectual property rights. In this new digital environment, entertainment products, legitimate and pirated, can be transmitted across the internet in perfect digital form from one corner of the globe to another in a matter of seconds. Revolutionary new technologies of this nature sometimes demand that new rules be included in the agreements that govern trade between nations.

Two significant treaties to this effect were concluded at the World Intellectual Property Organization in 1996. Ratification and implementation of these treaties is a high priority for our organization. We are pleased that our government has made achieving ratification of these treaties an important element of its bilateral intellectual property agenda.

Bilateral Trade Agreements: The Administration's ambitious agenda to negotiate bilateral free trade agreements has proven to be an excellent mechanism for achieving legally-binding bilateral obligations from certain trading partners to ensure that digitized content and transmissions are correctly and adequately provided full copyright protection. The FTAs negotiated thus far with Jordan, Singapore, Chile, Australia, Morocco, Bahrain and five Central American countries and the Dominican Republic under the CAFTA address this urgent need. We look forward to significant improvements in addressing rampant copyright piracy in such countries as Thailand, Colombia, Bolivia and Peru, in ongoing FTA negotiations. The FTA negotiating process is the best avenue currently available to us for ensuring that these important digital copyright issues are adequately addressed. We praise USTR, Commerce, PTO, the U.S. Copyright Office and other agencies for doing so and congratulate them for achieving significant results in these negotiations.

The record industry is currently confronting a piracy situation, both on and off line, that requires the significant revision of laws, and it is necessary to address these in a time sensitive manner or we risk further declines in US revenue and jobs. As a consequence, we fully endorse negotiations undertaken on a bilateral, and occasionally regional, basis.

This is extremely time and resource consuming—but absolutely necessary if we are to preserve the US economic competitiveness created by American ingenuity, know how, and creativity. We thus strongly support the negotiation of free trade agreements to introduce laws and practices consistent with the needs of today’s business world, and trust that reforms achieved in this manner will ultimately lead to global solutions.

We also obviously have major music piracy problems in countries with which the U.S. Government is not negotiating free trade agreements. China, Russia, Taiwan, Brazil, and Pakistan are particularly egregious examples, but there are many others. It thus is critically important that the U.S. Government have adequate resources to actively press these countries using the tools already granted by Congress. The U.S.-China Joint Commission on Commerce and Trade concluded this past April included potentially significant new commitments by China in this regard. But significant follow-up efforts are required to ensure that China lives up to these commitments.

Technical Assistance and Training: In an effort to promote the protection of intellectual property rights (IPR) worldwide, the Department has approved six projects to provide urgently needed training, programs and equipment to better protect American intellectual property. These projects are the first tranche of \$2.5 million to be spent on IPR training to help protect intellectual property overseas. The State Department’s Bureau of International Narcotics and Law Enforcement Affairs and the Bureau of Economic and Business Affairs selected the projects after conferring with industry, other Federal agencies, our overseas missions, and Congress. The second tranche of funding for the balance of the \$2.5 million will be announced and obligated before the end of this fiscal year. The first six projects are for Paraguay, Thailand, The Asia-Pacific Cooperation Forum, the Association of South East Asian Nations, Mexico, and the Central American Free Trade Agreement partner countries. We strongly support this program, and believe that it is essential for the US to help to build the capacity of governments to meet the variety of challenges that they confront in addressing criminal copyright enforcement.

Department of Justice Initiative: We have been greatly heartened by the Justice Department’s “Operation Fastlink.” Attorney General Ashcroft and his team deserve great credit for this unprecedented 10 country crackdown on the pre-release CD “ripping” groups that make it sport to steal property even before it becomes commercially available. There is real promise to the new Justice Task Force on these matters under the able leadership of David Israelite.

Other Activities: Traditional diplomacy is also very important, bringing the weight to USG power to play quickly when we encounter foreign governments unwilling to enforce their laws against those pirating our products.

Cultural outreach is useful to help empower local cultural communities to lobby for IP protection. Education/technical assistance are also important. Beyond the simple transfer of information and enforcement methods, such training can reinforce links among IPR officials within a region and build working relations between US and foreign law enforcement.

Intelligence gathering/analysis is also increasingly important to deal with the organized criminal element or terrorist financing links associated with international piracy.

Proposals for Reform

First, given the critical nexus between intellectual property piracy and international trade, we propose that Congress elevate the status of international intellectual property protection on our nation's trade policy agenda. Here are our suggestions:

Improving USG's Ability to Measure and Address Countries' Compliance with International Obligations

1. Establish a new USTR office dedicated exclusively to intellectual property matters, led by an Ambassador, "chief negotiator" or at minimum an Assistant U.S. Trade Representative.
 - Increase IPR-dedicated professional staff in this office from the current three to six. Several of these individuals should be dedicated to enforcement-related matters, including with respect to existing multilateral and bilateral agreements.
2. Improve the State Department's capacity in international trade-related anti-piracy and counterfeiting activities.
 - Elevate the State Department Intellectual Property Division in the Economics Bureau to "Office-level" and provide it with sufficient additional resources to enable it to interact effectively with regional offices in the Department and with America's embassies abroad to more effectively address IPR-related concerns as a matter of diplomatic priority.
 - Provide additional and new financial resources for the State Department's Bureau of International Law Enforcement and Narcotics to provide enhanced technical assistance to non-OECD countries in the fight against piracy. Technical assistance should include both the provision of necessary equipment and the training of law enforcement and judicial officers. These resources should be administered in conjunction with the restructured intellectual property office at State as recommended above. The program was funded last year, and we are very encouraged by the early round of grant announcements.

Improving U.S. Law Enforcement's Capabilities to Address Piracy Domestically, Internationally and On-Line

3. Increase funding to the Department of Justice to permit:
 - The appointment of "operational" FBI agents tasked to work on criminal copyright matters in key US missions, notably Russia, Taiwan, Pakistan, Mexico,

Paraguay, China, Thailand, Malaysia and Brazil. Such work should be undertaken in close cooperation with FBI legal attaches to encourage sharing of investigative information and expansion of investigations into organizations' cross-border operations.

- Additional funding to the Department of Justice to ensure that it has increased ability to pursue all forensic analysis necessary to conduct and facilitate a global response to the global problem of on-line piracy.
4. Protecting our nation's borders from pirated imports must remain a critical part of an effective national plan to combat piracy. However, the Bureau of Customs and Border Protection (CBP) is insufficiently staffed to meet this need. Only seven attorneys in CBP's IPR Branch administer CBP's nationwide enforcement effort. As a result, too many cases are not being acted upon quickly enough. The agency could significantly increase its seizures and effectiveness with adoption of amended guidelines permitting more sharing of information with affected US rightholders and providing alternatives to recordation as a means of establishing ownership of rights. However, to utilize this new authority effectively, additional funding should be provided to significantly expand the number of attorneys in CBP's IPR Branch. The IPR Branch should create a special task force aimed at increasing the timeliness, effectiveness and number of IPR civil border seizures. Increased funding should also be provided to assure that the number of U.S. inspectors working in foreign ports is adequate to address intellectual property concerns alongside other important national priorities.