Testimony of

Robert Holleyman II

May 25, 2005

Testimony of Robert Holleyman
President and CEO
Business Software Alliance
Before the
Senate Intellectual Property Subcommittee
May 25, 2005

Good afternoon. My name is Robert Holleyman. I am the President and CEO of the Business Software Alliance. The Business Software Alliance is an association of the
world's leading software companies and their key hardware partners. BSA's members create approximately 90% of the office productivity software in use in the U.S. and
around the world.

I thank the subcommittee for the opportunity to testify here today. The theft of intellectual property, commonly known as "piracy", is a matter of great concern to the
business software industry. Piracy costs the industry billions of dollars in lost revenues each year. It reduces investment in creativity and innovation. And it harms national economies including our own.

In my testimony, I intend to give a brief overview of the contributions that the business software industry has made and continues to make to the global economy and to
describe how piracy has undermined those contributions. I will next describe the evolving challenges the software industry faces with respect to piracy and explain the
steps industry is taking to address these challenges. I will outline the challenges we face in two particularly difficult markets: China and Russia. Finally, I will summarize the lessons that we have learned regarding how best to end piracy both here at home and abroad.

First, though, let me begin by thanking the members of the subcommittee for hosting this hearing. BSA and each of its member companies commend you for recognizing the
software industry's important contributions to the global economy and the serious threat posed to the industry by software piracy.

Software Industry Contributions and the Impact of Piracy

1 The Business Software Alliance (www.bsa.org) is the foremost organization dedicated to promoting a safe and legal digital world. BSA is the voice of the world's commercial software industry and its hardware partners before governments and in the international marketplace. Its members represent one of the fastest growing industries in the world. BSA programs foster technology innovation through education and policy initiatives that promote copyright protection, cyber security, trade and e-commerce. BSA members include Adobe, Apple, Autodesk, Avid, Bentley Systems, Borland, Cadence Design Systems, Cisco Systems, CNC Software/Mastercam, Dell, Entrust, HP, IBM, Intel, Internet Security Systems, Macromedia, McAfee, Microsoft, PTC, RSA Security, SAP, SolidWorks, Sybase, Symantec, The MathWorks, UGS and VERITAS Software.

Information technology has changed the world in which we live. It has made us more efficient, more productive and more creative. Software has been at the heart of this technology revolution. Software facilitates the dissemination of knowledge, drives global communication and promotes continued innovation. It helps us to solve problems and generate new ideas, gives us the power to create and to collaborate and fosters self-expression in a range of spheres.

The information technology sector, driven by the software industry, has also proven to be a remarkable engine for global economic growth. According to a 2003 survey on

the economic impact of piracy by IDC, a major IT research firm, the IT sector employs more than nine million people worldwide in high-wage, skilled jobs, raises more than $700 billion in taxes annually and contributes nearly a trillion dollars each year to global economic prosperity. Between 1996 and 2002, the IT sector grew 26%, creating 2.6 million new jobs and adding a cumulative $6 trillion to economies around the world. Each year, the packaged software sector alone contributes in excess of $180 billion to the global economy.

While these numbers testify to the economic force of the software industry, this sector has yet to reach its full economic potential. This is due, in large part, to piracy. In 2004 we measured the global piracy rate at 35%. In many countries the piracy rate exceeded 75%, reaching highs of 90% or more in some markets. Although piracy levels in the U.S. historically have been low as compared to other countries, the figure is far from negligible. In 2004 the U.S. piracy rate was 21%. More than one in every five copies of business software in use in this country today is stolen. There are few industries that could endure theft of its products at this level.

Piracy inflicts significant financial harm on U.S. software companies. Piracy in the U.S. alone cost the software industry almost $6.6 billion in 2004. Worldwide, piracy led to estimated losses of over $32 billion. Publishers invest hundreds of millions of dollars every year and immeasurable amounts of creativity in designing, writing and bringing new products to market. They depend upon the revenue they receive from those products to obtain a return on their investment and to fund the development of new products. Piracy undermines this model.

Of course, the impact of piracy extends beyond lost sales. Pirates steal jobs and tax revenues as well as intellectual property. The IDC economic impact survey cited above found, as a general rule, that there is an inverse relationship between software piracy rates and the size of the IT sector as a share of the gross domestic product. As piracy is reduced, the software sector grows. This creates a ripple effect that stimulates other parts of the IT sector and of the economy overall. The equation is a basic one: the lower the piracy rate, the larger the IT sector and the greater the benefits. Putting this into real numbers, the IDC survey concludes that a 10 point reduction in the global piracy rate over four years could deliver 1.5 million new jobs, $64 billion in taxes and $400 billion in new economic growth. In North America alone, benefits would include 145,000 new jobs, $150 billion in additional economic growth and more than $24 billion in tax revenues.

Reducing piracy delivers indirect benefits as well. Society benefits from new technological innovations. Consumers benefit from more choices and greater competition. Internet users benefit from new ways of communication and expanded creative content made available online. And national economies benefit from enhanced productivity leading to higher standards of living.

Piracy: Defining the Problem

In its simplest terms, "software piracy" generally refers to the reproduction or distribution of copyrighted software programs without the consent of the copyright holder. In most countries around the world, the law makes clear that when a person copies or distributes software, they must have authorization from the copyright holder through a license agreement or otherwise, unless the copyright law provides a specific exception for such activity. Otherwise, such activities constitute piracy.

Piracy of software can take several forms:

? Organizational end-user piracy

The business software industry's worst piracy problem traditionally has involved its primary users - large and small corporate, government and other enterprises ? that pirate our members' products by making additional copies of software for their own internal usage without authorization. We commonly refer to this activity as "organizational end-user piracy".

? Counterfeiting

Counterfeit software, often packaged to appear nearly identical to the genuine article, continues to pose a serious problem for BSA's members. Over the past several years,

BSA has seen a dramatic increase in the amount of high quality counterfeit software imported into the U.S. from overseas, especially from Asia. Compilation CD-ROMs containing a large selection of software published by different companies also pose a problem. Although compilation CDs do not exactly replicate the packaging of genuine software, unsophisticated consumers are often led to believe that they are legitimate promotional products.

? Internet piracy

The Internet is the future of global communication and commerce. It creates tremendous opportunities for faster, more efficient and more cost-effective distribution of information, products and services across the globe. Unfortunately, the emergence of the Internet also has added a new dimension to software piracy by permitting electronic sales and transmission of illegal software on a global scale. Today, computer users can and do download infringing copies of BSA members' products from hundreds of thousands of locations on the Internet all over the world.

? Industry Efforts against Piracy

The Business Software Alliance and its individual members devote significant financial and human resources to preventing piracy worldwide. Our efforts are multi-faceted. First, 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. Among other resources, we provide school curricula to promote responsible internet behavior among students, and guides and technologies that assist end-users in ensuring that their installed software is adequately licensed. We likewise offer tips to consumers so that they can be confident that the software they acquire on-line is legitimate.

Second, we work closely with national and international bodies to encourage adoption of laws that strengthen copyright protection and promote an environment in which the software industry can continue to innovate.

Finally, where appropriate, BSA undertakes enforcement actions against those involved in the unlawful use, distribution or sale of its members' software. On the Internet, for example, BSA conducts a far-reaching "notice and takedown" program. BSA's members have also filed suit against individuals offering pirated software for free download and over auction sites. BSA also engages in civil litigation against corporate end-users who are using our members' products without authorization.

Of course, technology plays a role in protecting intellectual property rights as well. Content owners must take responsibility to ensure that their works are not easily subject to theft, rather than rely wholly on others to protect their intellectual property. Accordingly, BSA's members have invested hundreds of millions of dollars and thousands of engineering hours in developing technologies to protect content and intellectual property. Our companies have worked diligently, voluntarily and cooperatively with content providers and consumer electronics companies to create systems that will foster the legitimate distribution of digital content. Experience clearly demonstrates, however, that there is no silver bullet technological solution that will solve the problem of piracy. Nor are government mandates the answer. Technology develops most effectively in response to market forces; government mandates would stifle innovation and retard progress.

Piracy Abroad

Last year, the worldwide rate of personal computer (PC) software piracy decreased by one percentage point to 35 percent. This occurred despite an influx of new PC users from high piracy market sectors -- consumer and small business -- and the increasing availability of unlicensed software on Internet peer-to-peer (P2P) file-sharing sites. That's the good news.

Unfortunately, the total value of pirated software worldwide actually increased, despite the modest decline in the piracy rate. This was a result of the fact that the global PC software industry grew over six percent and the U.S. dollar fell by more than six percent against the world's other currencies. In 2004, the world spent more than $59 billion for commercial packaged PC software. Yet, software worth over $90 billion

was actually installed. For every two dollars' worth of software purchased legitimately, one dollar's worth was obtained illegally.

The software industry suffers piracy losses in countries all over the globe. Two of these stand out for having very high piracy rates, combined with high PC penetration and large potential markets: China and Russia. These countries should both be tremendous opportunities for our industry. Their potential as software markets - and, indeed as software suppliers, will remain largely unfulfilled until they bring the piracy situation under control.

? China

Despite repeated commitments, legal reforms, episodic crackdowns against retail piracy and the personal intervention of Vice Premier Wu, China's market is awash with pirate and counterfeit copies of practically anything that is worth pirating or counterfeiting. Nine out of every ten copies of software installed on PCs in China last year were

pirated, representing a loss to the U.S. software industry of about $3.6 billion. This, of course, is not a complete picture of the harm caused by piracy in China, since China is also the world's leading producer and exporter of counterfeit software. Piracy on such a massive scale has significant ramifications for the U.S. software industry and our national economy.

Rampant piracy has effectively stalled growth in U.S. software exports to China, despite China's escalating use of computer and software technologies. Consider that in 1996 China was the sixth largest market for personal computers and the 26th largest for software; it is now the second largest market for personal computers but still only the 25th largest market for software. This growing gap between hardware and software sales is the inevitable consequence of a market that does not respect intellectual property rights or reward the significant investment required to develop and market innovative software products.

China's failure to protect and enforce intellectual property rights has also hindered its ability to grow a domestic software industry (a problem that China is attempting to cure through protectionist and discriminatory industrial policies). According to 2003 report by the market research firm IDC, a ten percent reduction in piracy could help the Chinese IT sector grow nearly fourfold in four years.

Two key reasons for China's failure to make significant inroads into software piracy are deficient IPR laws and an enforcement regime that is not deterrent.

The WTO TRIPs agreement requires China to criminalize copyright piracy on a commercial scale, including enterprise end use piracy of computer software. Unfortunately, end user piracy is not regarded as a crime in China, so there has never been a criminal prosecution of this activity.

TRIPs also requires enforcement of intellectual property rights to be deterrent in practice. Through a combination of inadequate dedication of resources and lack of significant penalties for piracy, China's enforcement regime simply does not deter piracy.

As the U.S. government works implements its strategy for addressing the piracy problem in China, BSA urges the government to demand the following four improvements to China's IPR regime:

Extend criminal liability to enterprise end user piracy. The relevant provisions of China's criminal code - Articles 217 and 218 - do not treat corporate end user piracy as a criminal offense, despite its devastating effect on software industry revenues and growth. China's failure to extend criminal remedies to enterprise end user piracy violates its WTO-TRIPS obligations and should be rectified immediately.

Reduce and clarify criminal thresholds. In late December, the Supreme People's Court and Supreme People's Procuratorate released amended Interpretations of Articles 217 and 218 of the criminal code which lower the thresholds for establishing a criminal copyright violation. Unfortunately the thresholds are still too high, particularly because the phrase "illegal income" is unclear and in certain cases (e.g., enterprise end user piracy) may be difficult to prove.

Increase administrative resources and penalties. Administrative enforcement

actions against software piracy can be brought by the National Copyright
6
Administration of China (NCAC) and local Copyright Administrations (CAs). In our experience, however, neither the NCAC nor the local CAs has the resources or interest to exercise this authority. When administrative actions are taken, fines are rarely issued and the outcome is rarely publicized. The end result is that administrative actions provide virtually no deterrent value.

Legalize the government sector and state-owned enterprises (S0Es). BSA and its member companies are heartened by China's commitments to legalize software use within the public sector, which represents China's largest consumer of software. These policies should also extend to SOEs. The assurances on government legalization will be of limited value, however, if China proceeds with its proposal to impose severe restrictions on procurement of software from non-Chinese suppliers.

All of these steps are necessary to address unacceptable software piracy rates in China that cost the U.S. software industry billions of dollars in lost exports and stifle the development of a domestic software industry. No single step is sufficient on its own. The goal, of course, is to increase the legitimate market for software in China, to the benefit of all suppliers, Chinese and foreign. Ultimately, China's success or failure on this issue must be measured against that goal, not against the completion of any particular step along the way. To this end, we are working to develop new benchmarks to measure progress on this issue.

? Russia

At 87%, Russia's software piracy rate is only a three points lower than that in China, and has not improved over the past several years. Russia has adopted a number of legal reforms over the past several years and it is our hope that, once they come fully into force, they will lead to improvements in the marketplace.

In 2003, the Russian criminal code was amended to clarify the previously ambiguous standard for triggering a criminal infringement case. In 2004 Russia adopted copyright law amendments that, in addition to extending protection to certain pre-existing works and sound recordings, implement a number of provisions of the WIPO Internet Treaties. This amendment included the creation of an exclusive right of making available, which will be critical to enforcement against Internet piracy once it goes into effect in September 2006.

The piracy situation on the ground in Russia is mixed. Our companies that engage in channel enforcement have reported that they are receiving cooperation from Russian law enforcement authorities, and are achieving some successes. There is little enforcement against end-user piracy in Russia, but we are working in Russia to change that.

Internet piracy is one piracy challenge in Russia where industry efforts have met with little success in the past few years. The business software industry faces a persistent problem of pirated software promoted and sold all over the world using unsolicited email advertisements (spam) and via mail-order. The spam emails link consumers to slick websites that advertise "OEM versions" software for a fraction of the normal retail price. The prices, however, are high enough to convince some consumers that the offer is legitimate.

These spam e-mails originate from an organization operating under various names: CD Cheap, OEM CD Shop, OEM Software, and other aliases. The spam and scam operation
7
is apparently run by a well-connected, sophisticated Russian criminal network operating in Moscow and in the Sverdlovsk region. In January and February 2004 two police raids and related arrests were carried out in Yekaterinburg, near Sverdlovsk, but the key figures were not touched and there was no noticeable impact on this criminal enterprise. The FBI has opened a case file on this operation and is attempting to work with Russian law enforcement.

BSA urges the U.S. government to use the leverage provided by Russia's WTO accession negotiations to obtain binding commitments in the Working Party report to resolve the range of outstanding IPR problems. The Russian government should begin addressing

these issues immediately, in order remove this continuing irritant from Russo-American trade relations.

The Role of Government

Multilateral and bilateral trade alliances must be fully backed by governments' firm commitment to respect and enforce intellectual property rights within the public and private sectors; to treat the manufacture and sale of counterfeit software as a crime warranting tough enforcement and penalties; and to ensure that its laws and enforcement regimes adequately address all forms of piracy. The Administration and Congress can help promote this commitment to intellectual property protection by:

?? ensuring that governments worldwide fulfill their obligations under the WTO TRIPs Agreement by adopting and implementing laws that provide for effective enforcement against piracy;

?? encouraging implementation of the WIPO Copyright Treaty and strong criminal enforcement of the measures therein; and

?? urging countries to dedicate resources to the investigation and prosecution of piracy in all its forms, as well as to training, technical assistance and mutual cooperation.

? Strong, workable enforcement regimes, as required by TRIPs

While substantive copyright protections are essential to bring piracy rates down, experience has demonstrated that these protections are meaningless without adequate mechanisms to enforce them. The 1994 World Trade Organization Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) provides the framework for such mechanisms.

TRIPs requires that intellectual property rights enforcement regimes meet specific "results-oriented" performance standards. Specifically, each member's enforcement regime must "permit effective action against infringement" and "constitute a deterrent to further infringements." Moreover, enforcement procedures cannot be "unnecessarily complicated or costly," or "entail unreasonable time limits or unwarranted delays." Thus, in assessing TRIPs compliance, it is critical to review and monitor all aspects of a country's enforcement regime, including the adequacy of procedural remedies and penalties, as well as their effectiveness in deterring piracy.

? Full and faithful implementation of the WIPO Copyright Treaty

In direct response to the growing threat of Internet piracy, the international community in 1996 adopted the WIPO Copyright Treaty to ensure protection of copyrighted works in the digital age. Among other measures, the WIPO Treaty (i) makes clear that a copyrighted work can be placed on an interactive network only with the consent of the relevant right holder; (ii) makes clear that the Berne Convention's reproduction right applies to electronic uses of works; (iii) protects all forms of expression of computer programs; and (iv) prohibits "hacking" of technical protections that have been applied to works. These measures ensure that authors' rights will be respected in cyberspace, and are urgently needed on a global basis. While many countries have taken steps toward improving and enforcing laws in this regard, much more remains to be done.

? Dedicated resources to fight piracy

Ending the theft of intellectual property is a low priority in many countries. Piracy investigations are often delegated to law enforcement units with little or no training in intellectual property crime and given local rather than national attention, in competition with many other types of crime for attention and resources. Although copyright crimes often involve cross-border activities, there is frequently a lack of coordination among various countries' law enforcement agencies when investigating and prosecuting pirates. Even where procedures for cross-border coordination do exist, such procedures can be cumbersome and ineffective.

To ensure effective action against piracy, national authorities should establish specialized intellectual property enforcement units at a national rather than local level, who can react quickly and knowledgeably to incidents of IP crime. Better training of law enforcement and the judiciary is equally important, to ensure these bodies are

equipped to deal with these cases. Likewise, better cross-border cooperation among police and other government officials, and improved availability of evidence and judgments for cross-border use, are also essential.

Conclusion

Software contributes profoundly to the world in which we live. It allows us to share, to create and to innovate in ways previously unimaginable. Software-driven productivity strengthens national economies, including our own, and makes them more competitive and more prosperous. Unfortunately, piracy prevents the software industry from realizing its full potential. We urge the U.S. Government and other governments worldwide to help us solve this problem. We thank you for the efforts made to date. Thank you again for the opportunity to testify here today. I look forward to your questions and to continued dialogue on this important topic in future.