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Chapter 4: Russia

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> "The only way to kill piracy in Russia is strong copyright law with stern penalties and government resolve to enforce that law."
>
> – *Jack Valenti, president of the Motion Picture Association of America*[1]

Introduction

Since 2000, Russia has held an unshakeable spot on the USTR's Special 301 "Priority Watch List," backed by industry claims of billions lost to US companies in software, music, and film piracy. For 2008, the IIPA reported US$2.3 billion in losses in business software alone. Had the motion picture, music, and entertainment software industry groups reported, the total would almost certainly have exceeded $3 billion. The only country with higher reported losses was China, where the IIPA cited some $3 billion in software losses in the same year (IIPA 2009).[2]

Despite these numbers, quantitative reporting on Russia has fallen off sharply in the past several years, with the Motion Picture Association of America (MPAA) dropping out after 2005, the Entertainment Software Association (ESA) after 2006, and the Recording Industry Association of America (RIAA) after 2008. With the recognition by the Business Software Alliance (BSA) in 2010 that its "losses" are better characterized as "the commercial value of unlicensed software," there is no longer any current industry reporting of piracy losses in Russia.

Reported rates of piracy in Russian media markets (as opposed to monetary losses) generally decreased throughout the 1995–2009 period, with sharper drops after 2006—a period of stepped-up Russian enforcement. For reasons discussed later in this chapter, it is unclear to us whether these trendlines reflect real differences in the availability of pirated goods. The size of the Russian market for all types of media goods except recorded music increased dramatically over the past decade, making higher total quantities of pirated goods and lower overall rates a plausible combination, and one validated by our experience with Russian consumers. Russian sources in enforcement, for their part, generally share these doubts. But the reported decreases

1 See Arvedlund (2004).

2 In 2009, in a flagging economy, reported software losses in Russia dipped to $1.86 billion. Losses in China remained stable, at just over $3 billion (IIPA 2010).

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have played an important role in the domestic politics of enforcement and above all in the US-Russia dialogue as evidence of Russian compliance with US demands.

Lobbying by US copyright interests has made piracy a source of continuous tension in US-Russian relations over the past decade—at times placing it on diplomatic par with global security issues such as nuclear proliferation. Russian government attitudes toward this pressure have varied, with conspicuous efforts to comply with US demands emerging in 2005–7 as the prospects for Russian accession to the World Trade Organization (WTO) seemed to grow closer. A bilateral Russia-US agreement on trade and IP (intellectual property) enforcement was signed in November 2006 and set in motion a wide array of changes to Russian law, enforcement practices, and—ultimately—the organization of piracy, in which a relatively formalized pirate retail sector gave way to a range of more informal and less visible channels.

Domestic pressure for stronger enforcement also grew in the period, as Russian software and movie interests, especially, emerged from the economic turbulence of the late 1990s and began pushing for stronger local controls. As elsewhere, these local conversations have been shaped by (and fed back into) the wider context of international copyright lobbying, but they also are indicative of new locally grounded debates over the costs and benefits of enforcement. In our view, the experience of the past four to five years suggests that these domestic Russian conversations will have more impact on enforcement efforts than the USTR or other external forces—if not always at the level of state policies, then at the level of the actual practices of enforcement and the margins accorded piracy in Russian business and consumer life. A primary goal of this chapter is to contribute to that conversation.

IIPA reports continue to provide the dominant account of piracy in Russia, however, and debates tend to be framed by its claims and those of affiliated groups. In part, this dominance reflects the very effective use of the

reports by Western-affiliated industry groups active in enforcement lobbying, notably the Russian Anti-Piracy Organization (RAPO) in film, the BSA in software, and the International Federation of the Phonographic Industry (IFPI) in music. In part, this discursive power simply reflects the lack of alternatives: as in other countries, the same industry affiliates provide the only broad-based infrastructure for research and reporting on piracy. Although local political interests have, on several occasions, challenged perceived overreach by the police and industry groups, this opposition has not articulated a clear alternative account and has produced little independent research or data.

The picture that emerges from IIPA and other industry research follows, for the most part, the well-established IIPA template for high-piracy countries. Failures of Russian political will, popular ignorance of the law, insufficient deterrents, corruption, and inadequate police powers all figure prominently and repeatedly in the reports of the past five years. Although our work lends support to some of these accusations, this narrative of failure provides a very incomplete perspective on the wider social, political, and economic contexts of piracy in Russia. Most important, it does very little to explain the prevalence and persistence of piracy in Russia despite more than a decade of international pressure, institutional growth, policy change, and expanded enforcement efforts.

Like the other contributions to this report, our account of media piracy in Russia emphasizes the relationship between pirate and legal media markets. As elsewhere, the dominance of domestic media markets by multinational companies means that media prices remain high and the variety of available goods low. As elsewhere, the growth of domestic media markets in the past decade is largely a function of rising incomes in major cities (in the case of film, matched by rising prices)—not of efforts by multinational companies to compete on price. (The Russian music market, with its unusually large percentage of locally owned labels and

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Acronyms and Abbreviations

CPP	comparative purchasing power
CRM	collective rights management
DRM	digital rights management
IP	intellectual property
IP address	Internet protocol address
ISP	Internet service provider
IT	information technology
P2P	peer-to-peer
BSA	Business Software Alliance
ESA	Entertainment Software Association
IFPI	International Federation of the Phonographic Industry
IIPA	International Intellectual Property Alliance
MPAA	Motion Picture Association of America
RIAA	Recording Industry Association of America
TRIPS	Agreement on Trade-Related Aspects of Intellectual Property Rights
USTR	Office of the United States Trade Representative
WTO	World Trade Organization

Acronyms and Abbreviations

This chapter preserves the original Russian-language system of acronyms and abbreviations through transliteration.

Department K	computer crime unit, Ministry of the Interior
FAS	Antitrust Service
FSB	Federal Security Bureau
FTS	Federal Customs Service
MILITIA	Department of Public Safety, also known as municipal police
MVD	Ministry of the Interior
NFPP	National Federation of Phonogram Producers
NPD	Nonprofit Partnership of Distributors
NP PPP	Nonprofit Partnership of Software Suppliers
OBEP	Department of Economic Crimes, Ministry of the Interior
Prokatura	Prosecutor's Office
RAO	Russian Author's Society
RAPO	Russian Anti-Piracy Organization
RARE	Restricted Access Regime Enterprise
RFA	Equal Rights Phonographic Alliance
ROSP	Russian Association of Allied Rights
VOIS	Russian Organization for Intellectual Property

close ties to the live-performance market, offers a partial exception, visible in lower CD prices.) Recurrently, our study suggests that the strongest competition on price and services in Russia takes place in the pirate market—in the optical disc channel, on the Internet, and in the various quasi-legal ventures that have exploited confusion around Russian copyright licensing laws. As in other middle-income and low-income countries, Russia's pirate market provides the only truly mass market for recorded media and often the only source of any kind for niche-market goods, such as non-Hollywood foreign films.

In key respects, Russia is also an outlier in our work. Many of the most common features of pirate markets—selective enforcement, conflicting official action on piracy, and inadequate domestic licensing regimes, to cite a few—are extravagantly present in Russia and represent virtual limit cases in this study. The chapter explores, for example, how operating fully within the licensed economy is a luxury reserved for large, well-capitalized businesses and how the capture and use of enforcement resources by those businesses conveys competitive advantages—tracking with and reinforcing influence and size.

It explores the surreal history of copyright licensing in Russia, which deserves a study of its own. Where other national licensing regimes for music or film are merely inefficient, leading to high prices and limited availability of goods in the legal market, the Russian media market is the product of a wild proliferation of licenses, of counterfeit licenses, and—most significantly—of licensing authorities, with the result that licensing has largely ceased to be a viable means of distinguishing licit from illicit goods. Efforts to address this through the consolidation of licensing authority in groups like the Russian Author's Society (RAO) have, so far, produced hyperactive rights enforcement and a massive (some would say, indiscriminate) expansion of rights claims and litigation but nothing yet resembling a transparent, credible basis for artist royalties.

Perhaps the most striking feature of Russian pirate markets, however, is the evidence of state protection of pirate optical disc production. A number of industry and government sources have drawn attention to the role of Restricted Access Regime Enterprise (RARE) sites—such as military industrial facilities and nuclear power plants under the protection of state security forces—as hosts of pirate production lines. Factories on such sites also are among the major "legal" suppliers of discs in Russia and contribute, in particular, to a DVD pirate market saturated by the "above-quota" production of high-quality discs. While the RARE sites have been targeted for closure in recent years by the Russian government—with some success according to industry sources—the larger web of police and security-service protection for the major factories appears to be mostly intact.

Conversely, we see no evidence of ties between pirate networks and broader "organized-crime syndicates" or the so-called ethnic mafia often alleged to dominate Russian black markets. Such allegations are relatively common in online forums and it would be surprising, in our view, if opportunistic connections between piracy and other forms of criminal activity were absent from the Russian market. But we have seen no evidence of systematic relationships and believe such activity to be, at most, peripheral to the larger dynamics of Russian piracy.

In 2006–7, Russian law enforcement agencies conducted a major crackdown on pirate producers and retailers, leading to praise from both domestic and foreign government officials and industry groups. But in an environment in which the major producers enjoyed relative immunity, the crackdown had a perverse outcome. It was, by most accounts, successful in sweeping out the most exposed middle-tier producers and retail vendors of pirated CDs and DVDs. But in so doing it consolidated the power of the large, protected factories and—above all—sheltered them from the mid- and low-level competition that has collapsed prices for pirated optical discs in many other countries. One consequence is that pirate disc prices in Russia remain unusually high—averaging $4–$6 for a high-quality DVD. In countries where cheap burners and raw materials have led to extensive small-scale, low-end competition among producers, DVD prices have fallen to $1–$2 at retail and often lower at wholesale and in the least formalized sectors of the market.[3]

The crackdown and its aftermath also provide evidence of the increasingly complex balance of forces that shapes the politics of IP and enforcement in Russia. Although the crackdown and related changes to Russian law have been framed by the IIPA and other international stakeholders as responses to US pressure—notably in the context of Russian efforts to join the WTO—a domestic reading is also possible in which local rights holders played the critical role in supporting the crackdown and later in limiting it as business-class discomfort with the raids grew. The two views are not irreconcilable, but the latter is largely invisible in the international arena. Over the past half decade, we see evidence of growing autonomy in Russian approaches to IP policy and enforcement, shaped by struggles between domestic stakeholders and by calculations of domestic costs and benefits.

3 See the India, Mexico, and Bolivia chapters in this report.

From the perspective of Russian consumers concerned above all with access to media, these cost-benefit calculations are relatively simple and unambiguously favor piracy. Our work finds near-universal participation by Russian consumers in the pirate economy, differentiated mostly by the frequency of pirated purchases or downloads and the degree of (mostly inconsequential) ambivalence toward the practice. Piracy, our work suggests, is not just a drain on the cultural economy in Russia—*it is one of the primary forms of that economy* and is woven into a wide range of licit practices, forms of enterprise, and patterns of consumer behavior. Much of what follows is an effort to understand enforcement in relation to this other side of piracy, this feature of everyday life in Russia.

A Brief History of Piracy in Russia

Since the transition from socialism in 1991, there have been three distinct phases in the organization of Russian piracy:

- An initial period, running from 1991 to roughly 1999, characterized by (1) the widespread smuggling of optical discs from other countries into Russia (especially from the former Eastern-bloc countries), (2) weak law enforcement, and (3) generally low public awareness of IP law. Cassettes—audio and video—were the first generation of pirate goods, complemented in the mid-1990s by increasing numbers of CDs. These markets grew and, by the late 1990s, had become widely embedded in small and medium scale retail. Enforcement was minimal in this context: criminal charges and civil lawsuits were rare, successful convictions rarer, and penalties negligible.

- A second period, running from the late 1990s to 2006, marked by a shift toward domestic production as manufacturing costs dropped and by the growth of a relatively diverse pirate economy with low barriers of entry and a wide range of producers, distributors, and vendors. A mixed international and domestic enforcement lobby also began to take shape in this period, resulting in several rounds of changes to IP law and the reorganization of enforcement operations, but with little visible impact on street piracy.

- A third period marked by (1) the emergence of much stronger cooperation between industry groups and the state, (2) a resulting sharp increase in enforcement pressure against local vendors and distributors, and (3) the growth of the Internet as a competitor to the pirate optical disc channel.

In the first years of the post-socialist era, the Russian government worked to build a free market economy by creating legal institutions based on US and European norms. Western-style intellectual property law was part of this first round of legal reform. When Russia passed its Copyright Statute in 1993, it closely followed the standards set by the Berne and Rome Conventions for the protection of author's rights and the range of neighboring rights in

performance, recording, and broadcast. This included, notably, the concept of "transferable" copyright separate from the inalienable "moral" rights of a creator over his or her work—a distinction that remains important in Russian legal and popular understanding of intellectual property.

Despite these legal innovations, the concept of unauthorized copying as an illegal activity was slow to emerge in Russian public life. The unauthorized recording, sharing, and gifting of cassettes had been common behavior in Russia, especially in regard to the Western cultural goods that official censorship kept out of legal reach of Soviet audiences.[4] Such practices continued well after the fall of the Soviet Union, fostered by the lack of developed legal markets. When pirated CDs and video cassettes flooded into Russia after the transition, they were perceived by most Russians as the market—neither legal nor illegal but simply available, part of the consumer surplus promised by capitalism.

The first organized "pirate" networks emerged to meet this demand. Illegal copying on an industrial scale began in the early 1990s, as formerly state-run optical disc factories across the region lost their primary buyers and turned to production for the black market. Because of Soviet-era decisions about the placement of optical disc factories, much of this production took place outside Russia, in the former socialist countries of the Council for Mutual Economic Assistance (COMECON). Factories in Bulgaria and the Ukraine, in particular, became major suppliers of pirated CDs and later DVDs to the emerging Russian market (and to other Eastern and Western European markets). Discs from Bulgaria were transported in large quantities by truck across the southern border of Russia, often disguised as industrial waste to avoid customs. Piracy in this period was embedded in these wider regional networks and their complicated supply chains, which started with the acquisition of original CDs and film prints from Western distributors. According to several experts interviewed for this report, studio originals, not cruder "camcordered" copies, were the standard for pirated new movie releases. Because the optical disc factories were among the last high-tech industries to be built under socialist rule, the quality and quantity of output throughout the 1990s was generally high.

On the enforcement side, the 1990s were, by most accounts, a period of impunity for pirates in Russia. Although both the IFPI and the MPAA had active enforcement efforts underway by the mid-1990s, with numerous raids and seizures of infringing goods, the first successful prosecution for optical disc smuggling came only in 2001, in the so-called Bulgarian case.

The Bulgarian case was the first trial for music piracy in Russia—so named because it centered on CD shipments intercepted en route from Bulgarian CD factories. The case was the first to reveal the complexity of the international pirate trade in Russia but was otherwise notable mostly for its glacial pace. The investigation began in 1995. Two years passed before initial arrests were made in 1997. Court proceedings took another four years before guilty verdicts were handed down in 2001. The leader of the ring was sentenced to three years in prison, but because he had been detained throughout the period of investigation, his

4 Unauthorized translations of Western texts nonetheless circulated in the Soviet Union, sometimes widely, as part of larger samizdat (self-publishing) networks.

sentence was considered served. Despite the conviction, the Bulgarian case became a symbol in enforcement circles of the futility of investigating and prosecuting copyright infringement under current Russian law. In the words of one of the investigators, "one piracy case equals three unsolved murders" (Vitaliev 1996).

From 1997 on, the IIPA treated these issues as failures of Russian policy, political will, and training—views visible in its annual Special 301 criticisms of Russian officials for failure to prioritize anti-piracy efforts. But the ineffectiveness of copyright enforcement is difficult to disentangle from the broader problems of institutional development and state power in Russia in the 1990s. New state institutions were fragile and slow to assimilate the vast array of new laws, norms, and procedures created only a few years before. Ongoing fiscal crises—the most severe in 1998—limited the capacity of the Russian state to effectively perform many of its regulatory and law enforcement roles. And the rapid, disorganized privatization of state enterprises—largely abetted by US interests—created massive economic dislocation in which lines between legal and illegal business were often impossible to draw. In this context, the introduction of fully formed international intellectual property norms into Russian society was a predictable failure.

The Bulgarian case remained a point of reference for industry demands for expedited legal procedures, stronger customs controls, and other measures designed to strengthen enforcement (many of which would be implemented in later revisions to the criminal code). In practice, however, the case also closed the door on the period in which the cross-border smuggling of optical discs was the major vector for piracy. As CD/DVD burners became less costly and more portable, pirate production became predominantly domestic and more diverse in location and scale. Small and medium-sized production lines mushroomed in Russian cities, supplementing the large-scale state-licensed factories that pumped out a mix of licensed goods and above-quota pirated copies. The retail side also grew and diversified as small and medium-sized stores sold both licensed and unlicensed goods and as specialty stores emerged to address the chronic deficiencies of the legal market. By the early 2000s, transnational networks had ceased to play an important role in supplying Russian pirate markets. The supply chain for pirated discs had become mostly national.

Russian government interest in accession to the WTO combined with growing pressure from domestic and international copyright interests began to alter this landscape as the decade advanced. Executive and legislative action on several levels introduced changes to Russian IP law and enforcement practices, with enforcement-friendly revisions to the criminal code passed in 2004 and 2007 and a major overhaul of the civil code passed in 2006. As in other countries, efforts were made to streamline enforcement authority and strengthen coordination among the many government agencies involved in anti-piracy efforts. Responsibility for enforcement was consolidated around a handful of agencies and specialized units, including the Department of Economic Crimes, the Militia (or municipal police), and the Ministry of the Interior's

"Department K" computer crime unit. Public-private and nonprofit partnerships quickly became the norm in these contexts and continue to play a large role in directing enforcement efforts.

The outcome of these developments was the enforcement push in 2006–7, in which police eliminated many of the small and medium-sized producers, distributors, and vendors of optical discs, but which—according to our interviews with enforcement agents—also reconsolidated production around large, politically protected plants. The enforcement push raised the cost of buying off the police and other law enforcement agencies, strongly favoring the largest-scale and best-connected players. The cartel-like behavior of these enterprises kept optical disc prices in Russia unusually high, with prices of $5 for a high-quality DVD still common. Although prices at the low end of the market have fallen (for example, for homemade compilations), there has been no general collapse of pricing to near the marginal cost of the media, as we have seen in other countries when copying technologies flooded the marketplace.

This centralized model has come under increasing pressure since 2007, though not primarily from the police. In 2004, 675,000 Russians had a broadband connection. By 2007, that number was 4.8 million. By 2009, there were 10.6 million broadband subscribers, with 14 million projected for 2010 (Dorozhin 2007; Kwon 2010). Russians are rapidly joining the global online community, and our limited evidence suggests that they have followed their Eastern European neighbors in embracing peer-to-peer (P2P) services as their primary broadband applications—representing up to 70% of bandwidth utilization according to recent measurements at several Eastern European ISPs (Schulze and Mochalski 2009). Russian authorities, moreover, have been slow to act against companies that have exploited ambiguities in licensing rules to offer their own low-cost online-distribution services. The well-known case of AllofMP3, a Russian website that sold nominally licensed music at $0.01 per megabyte, was a prominent example. The commercial profile of the site made it a major annoyance to international copyright organizations and a regular subject of IIPA and USTR complaints. Although the website was eventually shut down in 2008 after a lengthy legal battle and political intervention, it spawned various clones that continue to operate.

Many Internet service providers, for their part, offer low-cost or free music- and movie-download services as part of their subscription packages—not all of them legal. Nearly all observers attribute the persistence of these quasi-legal businesses to the legal thicket around licensing in Russia, which has permitted extensive manipulation of the rules by local groups and limited judicial recourse by rights holders. The shift toward online distribution has also introduced a lag in law and policing strategies, marked by a lack of effective criminal procedures for commercial online infringement. Such lags also have an important geographical component, with bandwidth, income, policing, and judicial experience concentrated in the capital cities.

Disaggregating Piracy by Sector

In Russia, as in the other countries documented in this report, changes in the organization of piracy and enforcement are part of a wider evolution of media markets and patterns of media access. Overall, legal media markets in Russia have expanded dramatically in the last decade, fueled by rising middle-class incomes and the growth (and global integration) of the Russian film and software industries. The market for recorded music has been in decline since 2004 but largely in sync with the global fall of the CD format.

The rapid growth of the last decade, however, occurred against a backdrop of economic crisis in the 1990s. Present-day media markets remain very small for a country of 145 million—some $220 million for recorded music (IFPI 2009) and $830 million at the box office in 2008 (Berezin and Leontieva 2009)—and highly concentrated in the capital cities of Moscow and St. Petersburg.[5] Per capita spending on music, film, and software is still a fraction that of Western markets, and the prices of a number of signature media goods have dramatically risen—notably movie tickets, which doubled in price between 2004 and 2008 (Berezin and Leontieva 2009).

These market shifts also have important social dimensions. The rebirth of the film market, in particular, also represented a transformation of that market from a massively popular and accessible form of entertainment in the Soviet era to a luxury good largely confined to the urban middle and upper classes. In the late Soviet period, Russians averaged sixteen theatrical visits per year (Padunov 2010), more than triple the US average. By the mid-1990s, that number had fallen to 0.25 visits per capita. In 2008, after a decade of growth, it was 0.83 per capita.

Movies

Between 1991 and 2008, the Russian film industry underwent a near-total collapse, restructuring, and revitalization. Prior to perestroika, Soviet censorship kept Western film and television largely out of reach of Soviet citizens, with the predictable effect of vastly increasing the status of such goods. Economic liberalization released this pent-up demand but provided it few licit outlets. Informal, privately run movie theatres multiplied rapidly, often consisting of little more than conference rooms with video projectors. *Rocky, The Terminator, 9½ Weeks*, and other iconic Western movies were publicly shown for the first time in such theatres. Nearly all this exhibition was based on pirated video cassettes. As home players became more common, rental businesses based on pirated stock also emerged.

Broadcasters also engaged widely in pirate exhibition. Following the privatization of the state TV channels, new station owners routinely broadcasted foreign movies without permission. This practice angered the MPAA, but it had little direct recourse: although foreign rights were

5 Moscow collects 35% of box office receipts, and St. Petersburg 8%–12% (Anufrieva 2008).

legally recognized, there was no infrastructure for enforcing them. US movie studios responded with a boycott of Russia in 1992–93, which ended with the passage of a new copyright law.

The transition also inaugurated a period of rapid decline for the domestic movie market as public financing for Russian producers and exhibitors disappeared. Annual feature film production dropped from roughly three hundred in the early 1990s to only fifty by 1995. Signs of renewed investment in production and exhibition began to appear in the capitals in the second half of the 1990s. The first Western-style multiplex opened in Moscow in 1996. By 1998, film distribution companies had taken the lead in renovating dilapidated movie theatres.

By the early 2000s, Russians had returned in significant numbers to movie theatres, and theatrical exhibition has continued to grow. The Russian hit *Night Watch* topped the box office charts in 2006, with $30 million in revenues. *Pirates of the Caribbean: At World's End* earned $31 million in 2007. 2008 set new records in (post-Soviet) attendance, with over 120 million tickets sold and $830 million in revenues. *Avatar* passed the $100-million mark five weeks after its release at the end of 2009. Despite the renewal of the domestic industry, Hollywood dominates the Russian box office, accounting for over 80% of theatrical revenues in the last decade.

Music

Throughout the 1990s and even into the early 2000s, the vast majority of Russians used record and cassette players to play recorded music, with piracy largely confined to the latter market. Although the IFPI and the IIPA repeatedly raised concerns about cassette piracy in Russia in the mid-1990s—citing what were almost certainly little more than rough guesses of losses—the market was inconsequential in size and, by Western standards, technologically obsolete. In 1997, only 2% of Russians owned CD players, and the major labels were in no rush to see this change. The international labels working in Russia—at the time, EMI, Sony, BMG, Polygram, and Warner—licensed only cassette rights, not CD rights, to their Russian partners and generally viewed the Russian market as unprofitable.

The music market nonetheless grew rapidly in the early 2000s, fueled by rising urban middle-class incomes and the widespread adoption of the CD. According to the IFPI, the wholesale market peaked at $342 million in 2004 (the high point for CD sales in most countries). Since then, sales have hovered at lower annual levels of around $220 million—still primarily based on CD sales but complemented by an emerging (but for now, tiny) legal digital sector geared toward the Russian cell-phone market. Although the Russian music market is miniscule compared to the United States, Japan, and the United Kingdom, it is still the twelfth largest national market.

Most of the music purchased in Russia is local repertoire—over 70% by most estimates, and higher in the provinces. Unlike most countries, where the four global majors (EMI, Sony Music Entertainment, the Universal Music Group, and Warner Music Group) typically control 80%–85% of the market, the Russian market is dominated by forty to fifty independent local

labels. As a relatively formal concert market emerged from the black market in recent years, local labels also took on primary roles as promoters (Alekseeva 2008).

By all accounts, the licit market for music is smaller than the pirate market—and very likely much smaller. In 2006, the IFPI estimated the rate of physical piracy at 67% of the total Russian market (IFPI 2006). Its conventional estimate of digital piracy, also from 2006, is 95%. Because the IFPI shares no details about its research methods, we place no particular confidence in these numbers. But we do think them plausible, and indeed the intervening years have likely shifted the balance further toward the high end as digital technologies have become more widespread.

Software

The skilled and highly educated Russian IT community emerged from the Soviet period with great expectations for the transition to capitalism. These hopes were widely shared: one of the earliest acts of the Russian Duma was the passage of a law granting IP protection to software products and databases (1992).

In the early 1990s, several different operating systems competed on the Russian software market, but as elsewhere, pirated copies of MS-DOS and—soon—Microsoft Windows quickly won out. As new versions of Windows were released, new pirated versions entered into circulation, leaving Microsoft with the dominant position in the Russian operating-system market. The adoption of business tools followed a similar pattern, with Microsoft, Adobe, Corel, Autodesk, and other companies holding commanding positions by the mid-1990s in a thoroughly pirated software market. In 1995, the BSA estimated that 94% of business software in Russia was pirated.

Throughout the 1990s, however, the software market—both legal and illegal—was tiny. Computer adoption in Russian businesses and households was still negligible. By 2000, only 6% of households had personal computers, with the vast majority concentrated in a few large cities (Abraham and Vershinskaya 2001). But economic stability and falling computer prices after 1999 combined to produce a very rapid transition. By 2004, 20% of households had computers (Tapalina 2006); by 2009, 49% had them (Ministry of Communications 2009).[6]

Despite the availability of pirated foreign software, software sales also grew dramatically, climbing to $2.6 billion in 2003 and an estimated $10 billion in 2007. Russian software companies benefited greatly from this expansion. The sector recorded 30%–40% annual growth and emerged as the third-largest destination country for "offshore" programming services after China and India. The current leaders in the market include Russian firms such as 1C Company,

6 We have seen widely varying estimates of computer adoption in Russia, leading us to approach this subject with caution. The commonly used replacement rate of one-third of systems per year almost certainly doesn't describe the situation in Russia. Many computers purchased for business purposes end up in Russian homes, either directly or after they have been retired from office use. Boston Consulting Group recently put the total number of PCs in Russia at 45 million, representing an overall 32% penetration rate (Boston Consulting Group 2010).

Kaspersky Lab, and Center of Financial Technologies—all of which specialize in tools for Russian businesses. In the boom year of 2007, 1C's sales increased by over 90%, driven by its popular accounting suite, a global-hit World War II flight simulator, and other foreign-licensed games distributed in the Russian market. Overall, however, the relative position of Russian vendors has eroded as transnationals like Microsoft and Adobe increase their presence in the Russian market (RosBusinessConsulting 2008).

This growth has given Russian software companies a voice in enforcement policy and led to some local research interventions that push beyond and, in some respects, challenge the BSA narrative about marginal improvements in Russian business software compliance. The RosBusinessConsulting review suggests that software piracy was only 25%–30% in the corporate sector in 2006—a far cry from the BSA figure of 80% for the market overall. We have no opinion on the accuracy of this number and note the skepticism of at least one consulted expert. But a significantly lower figure for the corporate sector is reconcilable with the BSA findings. Large businesses are usually the most compliant organizations due to their pricing leverage with vendors, generally sophisticated IT-management practices, and vulnerability to enforcement if piracy becomes too flagrant. Such factors contribute to the differential treatment of big and small business discussed later in this chapter.

Enter the Internet

Inevitably, pirate media markets are shaped by the available consumer infrastructure for audio and video consumption. Today, DVD players are the primary playback devices in Russia, offering backward compatibility with CDs and—increasingly—forward compatibility with MP3 and MP4 files. As in other middle-income countries, this is a very recent development: in 2004, only 6% of Russian households owned a DVD player. By 2007, that number had risen to 51%. According to a 2008 Screen Digest report, twenty-eight million Russian households had a DVD player in 2008, giving Russia the largest installed base in Europe. The growth of DVD piracy, in the past half decade, is both a response to and a driver of this process of adoption.

Music has weaker ties to optical disc media than film, due to the wide range of different storage and playback devices. Sales of digital audio players, for example, doubled annually in the latter half of the decade. The small size of digital audio files facilitates downloading, sharing in bulk, and the amassing of large music collections at moderate cost. Our survey work on media habits[7] indicated that few younger Russian listeners treat CDs as the elements of a personal music collection. Instead, individual listening and collecting is satisfied mostly through digital files that are downloaded or shared among friends. The CD retains a role, however, as a status object in some contexts, notably for gifts.

The geographic distribution of wealth and services also shapes patterns of use. Access to broadband remains very uneven in Russia, with Moscow and St. Petersburg well ahead of

7 "Consumers of DVDs" survey conducted for this report by the Evolution Marketing Center in Irkutsk in November and December 2008. The project coordinator was K. Titaev.

other Russian cities. Uncapped, relatively affordable broadband services became available in St. Petersburg only in 2007. White-collar families, especially those with older children in the household, are the primary early adopters, replicating adoption trends for other consumer technologies. In our interviews, members of this group clearly indicated a shift away from DVDs—pirated or otherwise—as the medium of choice for film/video consumption. It was also clear from interviews that access to pirated media is not just a consequence of broadband adoption but an important driver of it. Given the high costs of media, low local incomes, and underdevelopment of other digital services in Russia, P2P is a strong value leader among broadband applications.

As in other countries with rapidly growing broadband infrastructures, Russian P2P activity is directed primarily at top-tier international sites—a list that in 2009 included The Pirate Bay, Demonoid.com, and Mininova. But a large local P2P community has also emerged in the past several years, consisting of around fifty BitTorrent trackers that specialize in Russian-language content and a wide variety of niche genres. The eight largest BitTorrent trackers in Russia counted almost eight million total registered users in late 2009 (not counting overlap between them). These larger sites typically index a wide range of materials, from movies to local TV, games, music, books, educational materials, pornography, and subtitled versions of foreign media in all those categories.

The largest site, Torrents.ru, specializes in film and TV. Our analysis of the geographic distribution of users of Torrents.ru suggests that the site serves a broad regional and diasporic Russian-speaking population, with almost half the users with resolvable IP (Internet protocol) addresses located outside Russia.[8] In addition to providing access to a much wider range of media for Russian broadband users, sites like Torrents.ru also clearly provide local Russian-language media for those living abroad. Torrents.ru's domain name was suspended in early 2010 by authorities, allegedly at the behest of software companies Autodesk and 1C. As with many enforcement actions, the attempt to shut the site down resulted in its relocation outside Russia—in this case to an ISP registered in the Bahamas (enigmax 2010a).

How Piracy Works

Media piracy in Russia has many determinants, ranging from the high price of licit goods relative to local incomes, to police crackdowns on retail vendors, to the failure of licensing regimes to provide much variety in Russian music, film, and software markets. Among these factors, price and income are fundamental. Although Russia is usually described as a middle-income country, GDP (gross domestic product) per capita is around $9,000 and median annual

8 On the basis of a data crawl of Torrents.ru's user index, we identified 156,487 registered users residing in Russia and 70,087, in descending order, in the Ukraine, Germany, Latvia, Moldova, Lithuania, Estonia, Israel, the United States, Kazakhstan, and Belarus. The IP addresses of 98,168 registered users were not resolvable at this level.

income remains under $5,000.[9] Full-price licit CDs and DVDs, especially for foreign music and film, cost between $10 and $25 and consequently have a very small market share (according to IFPI sources, full-price CDs account for only 10%–12% of the market). The large pirated optical disc market and, increasingly, the large-scale culture of online and digital piracy cannot be understood outside this price-income mismatch.

The limited selection of media goods offered by the legal market is another crucial determinant. Most Western film and music, for example, is simply unavailable through legal retail channels, with the range of goods falling off still further in the provinces. This situation is by no means unique to Russia but rather reflects global business models in which incentives to compete on price and services in emerging economies stay low. In Russia, this problem is exacerbated by two additional factors: (1) the unparalleled complexity of the licensing environment and (2) the assumption of risk by retailers in the media-distribution chain.

In Russia, the costs associated with unsold stock are borne by the retailer, not the distributor. This assumption of risk has consequences for the availability of media at the retail level: it pushes retailers toward low-risk, well-established, well-marketed products that are less likely to leave them with unsold stock and correspondingly away from more specialized or lesser-known music and film; and it creates incentives to stock much cheaper unlicensed goods, which can often be purchased wholesale at prices of from $0.30 to $1.

The police crackdown in 2006 changed these calculations. First and foremost, it became more dangerous to stock pirated goods, leading many vendors to exit the business. Distribution shifted toward less vulnerable retail networks, including anonymous chains and mobile street vendors. Higher up the distribution chain, complex warehousing networks emerged that separated pirate production and distribution, minimizing risk to distributors.

In turn, this less formalized trade has come under pressure from Internet-based distribution, in the form of both file sharing networks and well-known, nominally "licensed" Russian download sites like AllofMP3 and its successors. Although relatively few Russians possess the combination of broadband service, a modern computer, and digital playback and storage devices that enables full participation in the digital media economy, such infrastructure is growing rapidly and represents a clear challenge to the current organization of both legal and pirate media markets.

Licenses Everywhere

Most debates about piracy and enforcement presuppose the existence of clear distinctions between licit and illicit goods. The IIPA's assertion of $2–3 billion or more in annual losses in Russia since 2003 draws a bright line on this issue. But such distinctions can be complicated on the ground and are uniquely complex in Russia, where the copyright economy has been—

9 These are nominal GDP per capita figures appropriate for the comparison of fixed-price goods like DVDs. GDP is often reported in terms of "purchasing power parity," or PPP, reflecting the relatively lower prices of goods and services in many countries. Russian GDP per capita in PPP terms has fluctuated between $15,000 and $16,000.

and to a considerable extent, still is—mediated by overlapping licensing regimes that govern relationships among creators, publishers, distributors, vendors of media goods, and makers of audiovisual equipment. There have been several efforts to consolidate licensing procedures in the past decade, but the results have been either modest or counterproductive. The situation remains, by most accounts, a mess.

As elsewhere, responsibility for licensing individual works for production and distribution resides first with rights holders and then, under certain circumstances, with collective rights management (CRM) organizations. These collect royalties for airplay, performance, and other use of works; distribute the money to rights holders; and otherwise act to protect artists' interests. In Russia, this scenario was complicated by three provisions of the Copyright Statute of 1993: (1) the law allowed an unlimited number of collective rights management societies; (2) these societies were allowed to represent authors in absentia, without specific contracts to do so; and (3) they were allowed to manage a wide and underspecified range of neighboring rights.

The situation allowed for extensive gaming and abuse. In several cases, publishers and distributors registered as CRM societies and began publishing and distributing work—often without the consent of the rights holders. Nonpayment of fees and royalties was a recurring problem in this context and became the basis of mobilization and lobbying by the IFPI and the RIAA.

AllofMP3 was the best-known exploiter of these loopholes. The Russian web portal sold music online to international audiences at prices far below international norms, realizing a modest profit of $11–14 million annually (Golovanov 2008:2). Mediaservice, the parent company, obtained its licenses from two legally licensed Russian CRM organizations. The legitimacy of these licenses was challenged in 2004 by the IFPI and the RIAA under Article 146 of the Criminal Code. The owner of AllofMP3, Denis Kvasov, was charged with criminal infringement but was later acquitted in 2007 for lack of evidence of actual illegal activity. Under continuing pressure from the IFPI and US groups, the Russian government closed AllofMP3 in 2007, but clones of the site soon opened and continue to operate (although on a much smaller scale).

Reform in 2008 introduced a process of state accreditation of CRM groups, with the aim of consolidating authority around a single society in each of the main domains of culture and entertainment. Henceforth, only the accredited societies would be able to represent authors and rights holders without formal contracts. The law was not retroactive, however, and several of the CRM societies in existence before 2008 continued to operate.

In the copyright area, the Russian Author's Society won accreditation and became the de facto government-backed monopoly. Arguably, this consolidation traded one set of problems for another. The RAO has been repeatedly criticized for a lack of transparency and for failure

to deliver collected funds to musicians—all charges vehemently denied by the RAO's deputy director, Oleg Patrin. The organization keeps 30% of its gross licensing revenues[10] and has grown rapidly since 2006, increasing its proceeds from 1.5 billion rubles (approximately $50 million) in 2007 to 2.2 billion ($70 million) in 2008. The RAO charges concert organizers 5% of their proceeds and 3% of the box office take at movie theatres for "the public performance of music used in films" (Goncharova and Pushkarskaya 2009).

The RAO has made a particular habit of targeting concert promoters found skirting this tax (as in many other countries, live performance is the only high-growth sector of the music business in Russia). In 2008, the RAO attracted attention by suing Yug-Art, a concert organizer, for the "unauthorized public performance" of Deep Purple songs by Deep Purple during its Russian tour. The RAO won an award of 450,000 rubles ($15,000, or $1,000 per song), affirming the principle that all performance revenues must pass through the RAO. In March 2010, the RAO sued a World War II veterans' choir for performing patriotic Soviet songs at a free concert in Samara without signing a licensing agreement (enigmax 2010b). This event provoked a minor uproar in the Russian Parliament and may signal more organized pushback against the RAO's maximalist stance on performance rights.

With such a record, most CRM organizations enjoy low levels of participation and high levels of distrust from rights holders. In 2008, the RAO's coverage of public performance spaces was estimated at only 10%–12% of the total market.[11] Such numbers reflect, to be sure, the difficulty of establishing a consistent and credible framework for performance rights in a country that had historically ignored them but it also reveals clear frustration with the RAO's maximalist view of IP rights and hyperactive, indiscriminate practices of litigation. Many popular musicians now waive their performance rights altogether in order to avoid the RAO.

The RAO's efforts to expand have also created problems. In 2008, RAO associates launched the Russian Organization for Intellectual Property (VOIS) in a bid to become the accredited organization for "neighboring rights," such as those granted to broadcasters or producers. Concerns about the VOIS's lack of transparency regarding royalties and governance, however, led many producers to back a separate group in the accreditation process, the Equal Rights Phonographic Alliance (RFA). By all accounts, the political jockeying for accreditation was intense. The RFA's general director, Vadim Botnaruk, was assassinated during this period, although clear motives for the crime were never established. Ultimately, the VOIS won accreditation in 2009. The RFA continues to operate, however, grandfathered under the 2008 law, and is still the preferred organization of many foreign CRM societies.

The rights management situation remains unresolved in key respects. Other organizations, such as the Russian Association of Allied Rights (ROSP), are vying for accreditation to

10 See RAO's official website at http://www.rp-union.ru/en/docs/.

11 Interview with IFPI Russia staff.

collect royalties in still other areas. Control over licenses for manufacturers and importers of audiovisual equipment and blank media is one of the prizes, estimated to be worth $50–100 million annually.

Other types of licenses add to the confusion. In addition to the CRM societies, numerous anti-piracy organizations conduct their own "licensing" of the products of their members, often in the form of stamps of approval or authenticity placed on the goods. Such forms of authentication have no legal power but are intended to help signal legitimacy to retailers and consumers.

Regional and local authorities also issue an array of licenses to commercial vendors, from street vendors to large national chains. These allow trade in CDs and DVDs but in practice have no bearing on whether the products sold are legal. One interesting and controversial variation is the "regional license" (*regionalka*), which authorizes the distribution and sale of media goods at reduced prices (and often reduced quality) within a particular geographical region. Regional licenses have become a common strategy used by Russian distributors to lower prices outside the core Moscow and St. Petersburg markets.

Legal, Grey, and Illegal

Inevitably, the overlapping licensing regimes introduce a wide variety of opportunities for abuse. Different kinds of licenses define different types of illegality beyond the simple infringement of copyright, including violations of the authorized format (CD, DVD, streaming audio or video), the number of authorized copies, the permitted geographical boundaries of distribution, and so on. From the perspective of producers, these diverse violations are part of the larger repertoire of piracy in Russia. They are all sources of rights-holder losses and differ mostly in terms of their legal remedies.

From the perspective of consumers and—arguably—retailers, however, the same range of practices describes a spectrum of white, grey, and black goods—not a dichotomy. From this perspective, not all violations are equal, nor is the legality or illegality of most goods clearly marked or unambiguous. Rather, consumers make efforts to relate differences in perceived legality to differences in perceived quality, with the highest-quality, fully legitimate goods at the top of the hierarchy and the lowest-quality, informally produced goods at the bottom. The language of white, black, and variations on grey circulates explicitly in this context, though by no means consistently with regard to set practices. We provisionally distinguish five "shades" at work in this consumer logic:

1. *White* goods exhibit all the attributes of legal production, including high-quality packaging and printing and, above all, high prices, which can range from 350 to 800 rubles ($14–

$32[12]). These are typically sold in large, specialized music-video stores as well as major department stores and supermarkets.

2. *Light-grey* goods are legally produced but involve other practices whose legality or fairness may be in dispute—notably in the case of the parallel importation of CDs or DVDs into Russia, which can contravene trade laws or geographical licensing restrictions.[13]
3. *Grey* goods, such as above-quota CDs or DVDs, are identical to the legal versions but of dubious origin, signaled by their lower prices (150–250 rubles; $6–$10). Their paths lead primarily to specialized small and medium-sized stores, lower-end supermarket chains, and kiosks.
4. *Dark-grey* goods are factory produced but generally lower quality and visibly unlicensed or under-licensed. Unauthorized song compilations and film collections are prime examples. Such discs are commonly sold at kiosks, by street vendors, and in open-air markets, at 100–120 rubles ($4–$5).
5. *Black* goods are burnt on home computers or produced by small-scale cottage operations. In many cases, these are copies of other pirated copies or burned to disc from downloads. Such pirated media is found at open-air markets and costs from 10 to 100 rubles ($0.40–$4).

Many other genres also circulate in the lower tiers of the retail ladder, including concert bootlegs, self-help videos, evangelical sermons, and pornography. The legal status of these goods is harder to assign as they include a great deal of amateur and non-commercial productions.

Stamps and Stickers

On the street, determining the degree of legality of media goods is often impossible, even for experts. Our interviews suggested that neither shop assistants nor law enforcement officers involved in inspecting retail outlets for counterfeit goods can reliably distinguish legal and illegal copies. Nor, for that matter, can the growing strata of customers willing to pay a premium for legal goods. In practice, people rely first on price as a signal of legal status and second on their

12 Prices are cited at the summer 2008 exchange rate of roughly 25 rubles to the US dollar, when this first phase of work was conducted. Changes in exchange rates can have a dramatic impact on these cross-currency comparisons (by October 2010, the rate stood at around 31 rubles to the dollar), though less on local affordability.

13 The status of such imports is a matter of some legal dispute in Russia. The RAPO and other anti-piracy organizations have challenged its legality, but a number of companies operate openly as importers. Here the legal question is not copyright infringement but, rather, the extent to which the imported goods comply with trade agreements and whether customs are paid. The discounted price of many imported goods often permits vendors to undercut locally produced and licensed goods. See also Olimpieva, Pachenkov, and Gordy (2007).

tacit knowledge of what constitutes a legal (or almost-legal) copy. A regime of authenticating stickers and stamps placed on the goods themselves has emerged to guide this process but has itself become so byzantine and extensively counterfeited that it only adds to the confusion.

Many rights-holding or rights-issuing authorities attempt to validate products with specially designed stamps or stickers. These serve as signals to consumers of (ostensible) authenticity, but they have no legal authority and are not required by law. Because there are many rights-holder groups and rights-granting authorities, discs can be marked with a wide variety of stamps and stickers—and even multiple stickers. Some carry as many as five. As the chief of the St. Petersburg branch of the RAPO put it:

> RAPO CHIEF: Each copyright holder puts his sticker however he wants to: "I want to protect my property in this way, and so I better put a sticker on."
>
> INTERVIEWER: So the sticker, in general, means nothing?
>
> RAPO CHIEF: In general, it means absolutely nothing.

Representatives of the IFPI-backed recording industry association NFPP (National Federation of Phonogram Producers) reported better luck, but only when the sticker program was actively supported by law enforcement.

Naturally, stamps and stickers are also widely copied and fraudulently applied to pirated goods. In 2003, sixteen of the largest Russian music distributors created a private-public partnership called the Nonprofit Partnership of Distributors (NPD), which promptly issued its own sticker of authenticity.[14] The executive director of the partnership explained to us that, today, the stamp itself needs protection. Even the complex holographic design does not deter counterfeiters:

> We have a stamp and it has many protection features, but it is now also forged. It has the serial number. It has a hologram. It has every possible watermark. So it has a lot of protection. But we are pirated. Our stamp itself is pirated!

Interviews with consumers and music store personnel made it clear that no one can explain the meaning of the different stamps and stickers in any detail. Recognition has not been aided by changes in appearance: the NPD's sticker, for example, "has changed many times" and has existed, in its current form, for "maybe the last four years."[15]

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14 In its early days, the NPD was itself dogged by accusations of involvement in the distribution of pirated CDs.

15 NPD representative to the regions, in a round-table discussion, Moscow, June 2008.

Such confusion in the marketplace leads to indifference to the licensing system. Many stamps are assumed to be fraudulent. Worse, some stamps signal side-deals between the state, private enforcers, and commercial interests that are little more than protection rackets. Several retail-shop owners described these as "pseudo-licenses." Most were aware of a case in St. Petersburg from mid-2005 in which a so-called association of retailers used such licenses to expand their control of the music market. The association struck a deal with the local police to raid only those shops whose products lacked its stamps.

Nonetheless, the NPD and other rights groups have launched several efforts to educate consumers about the differences between legal and illegal optical discs. The key attributes of pirated discs, the NPD suggested on its website in 2005, are:

1. There is no NPD sticker on the cover, or the sticker has been forged.
2. There is a fake holographic stamp on the cover, or an imitation of a stamp has been made of a light-reflecting material.
3. The cover has apparent signs of scanning (copying) from the original. E.g., on close scrutiny the disc reveals that: the picture on the cover consists of separate points having regular geometrical shapes (square, rectangle, rhomb, and hexagon) or horizontal and/or vertical lines; and/or the contrast and color spectrum do not correspond to the original colors (for instance, the prevalence of one color in the picture, i.e., blue)

. . .

5. The data appear in small print or are blurred or unreadable.
6. There are no indicators of author's rights or copyright—i.e., the Latin letters ©.

. . .

9. There is no logo of the issuing company on the cover.
10. There is no information in Russian on the cover.
11. More than one audio collection or several albums by the same performer are present on a CD.
12. The disc case indicates that the disc is a CD-R or DVD-R format.

(NPD 2005)

Despite obvious problems related to the use of stickers, many pirated goods are, of course, easily identifiable. Most of the attributes listed by the NPD are clear giveaways: faded colors, blurred pictures, and grammatical mistakes mark the pirate origins of a disc. Curved, uneven, or scratched discs are more likely to be pirated. Street markets and kiosks, especially, are full of pirated discs that make no serious effort to hide their origins. The high end, in contrast, presents serious problems of identification. Although it can be easy to spot an undisguised pirated disc, it has become extremely difficult—even for enforcement officers—to verify a legal copy. In the higher tiers of the Russian media market, licit and pirated discs come from the same assembly lines and are identical.

The Social Organization of Production

According to estimates by the RAPO, the majority of pirated DVDs are produced above-quota at licensed factories.[16] As of 2009, the RAPO believed that there were at least fifty such factories running extra shifts or, in some cases, additional production lines. There are obvious advantages to this method: the oversupply is impossible to distinguish from the authorized production run, greatly complicating enforcement. As the executive director of the NPD put it:

> Before lunch they produce according to the terms of their license, and after lunch they do the pirated run [*piratka*]. And who can tell which they are printing at this very moment—legal or pirated?

Capital-investment and technological requirements at this level are high—as are the quality standards. An industrial replication line can cost $2 million. Production also involves the printing of high-quality jackets and other insert materials, as well as packaging. Output can be massive—as many as 450,000 discs per month per production line. Large plants may have as many as twenty to thirty such lines. When a factory is operating illegally or above quota, it also installs crushers—special machines for destroying the pirated discs in the event of a police raid.

Large-scale production is often broken into stages, with each stage conducted in a separate location. A typical division of labor separates the replication of discs, the printing of accompanying materials, box assembly, packaging, and transportation. This division of functions often results in the delivery of disassembled products to retailers, allowing producers and distributors to shift costs further toward the retail end of the commodity chain.

Smaller production lines played a major role in Russian optical disc piracy earlier in the decade. Built around multipurpose "recording machines," often compact enough to fit in single offices, such lines usually combine the different stages of the production process, from disc burning to the printing of covers and inserts. The quality of output from these operations is typically lower than from the major plants—especially in regard to printing and packaging—but so, too, is the capital investment: dedicated burners on this scale cost, on average, $40,000, allowing pirates to quickly recover their initial investment. The lower cost also means that abandoning the machine in the event of a police raid is less likely to represent an irrecoverable loss. Unlike the major factory production lines, such machines are generally clandestine and unregistered. Production is flexible, fast, and consumer oriented.

Discs burned in homes or small shops on personal computers are also widely available, especially in open-air markets. These generally cater to the poorer strata of the urban population and show little concern for packaging. Vendor stock, in such contexts, is often

16 According to IFPI sources, above-quota production has never been much of an issue for CDs, which are typically produced on dedicated pirate production lines.

Flooding the Market

According to sources in enforcement, above-quota production is routinely several times larger than the licensed production run, ensuring that the vast majority of copies in circulation are pirated. RAPO estimates regarding several popular films from 2001 to 2004 (well before the DVD boom in Russia) suggest the scale of the practice:

> *Harry Potter and the Philosopher's Stone* (2001). Legal issue: 120,000. Illegal issue: 350,000.
>
> *The Matrix Reloaded* (2003). Legal issue: 200,000. Illegal issue: 500,000.
>
> *Shrek 2* (2004). Legal issue: 220,000. Illegal issue: 450,000. (Vershinen 2008)

Such estimates were generally based on extrapolations of estimates of volume from key points of retail sale—methods that have proved highly approximate. The IIPA in 2010 reported that some seventy million pirated DVDs were produced in Russia in the previous year—apparently applying the older MPAA technique for modeling the pirate DVD market based on the difference between the size of the licit market and estimates of the total production capacity of Russian DVD factories. According to IFPI sources, most current industry estimates are based on the assumption that factories run at 60%–70% capacity. As the chief of the St. Petersburg branch of the RAPO observed, the central fact is that:

> There are too many plants, too many production lines, while the real demand for legal DVDs is not as large. Legitimate orders don't pay for this many production lines.

supplemented by back catalogs of film and music titles that can be either ordered or burned on demand. Homemade discs can also be found in specialty stores, such as those specializing in rare film or music. Sales personnel in such stores often have networks of trusted clients whom they assist in finding and burning particular albums, compilations, or movies. Such services are inexpensive—usually the cost of the blank disc plus a markup of 20–40 rubles ($0.80–$1.60).

Consolidated Production after the Crackdown

A different pirate economy emerged from the crackdown in 2006 and 2007. Where the older model was characterized by relatively decentralized production and a wide range of retail types, the new model consists primarily of centralized, politically protected manufacturers and, at the local levels, an increasingly informal retail sector marked by shifting legal ownership, greater anonymity of distribution and retail outlets, and growing reliance on street vending by illegal migrants and the working poor.

The crackdown took the sharpest toll, by most accounts, on the middle and lower tiers of producers and retailers.[17] Among the large production facilities, the crackdown produced consolidation and restructuring, with protection from the police and other enforcement authorities becoming the critical differentiator. As large manufacturing facilities have become more dependent on state protection, the mix of protection strategies has shifted. Manufacturing has moved away from open facilities into "closed" sites with private or sometimes public security. The most overt forms of protection involve placement in military facilities beyond the authority of the conventional police:

> INTERVIEWER: I was told that almost every pirate factory now sits on the premises of another factory, where there are multiple security checkpoints . . .
>
> ENFORCEMENT AGENT: In "PO boxes"—that's what we call them. . . . An ordinary plant can be inspected by city police, and regional police can raid it too. Now, a PO box is classified and has its own security service. No one goes there, not even the FSB [Federal Security Bureau], without a permit.

PO Boxes are production lines located on military bases or other premises run by state security services (also known as Restricted Access Regime Enterprise, or RARE, sites). Estimates of the number of these plants have varied over the years, and they are not, in and of themselves, illegal. In 2005, the Russian government put the number at eighteen of the forty-seven registered optical disc plants in Russia. These were allegedly responsible for a large portion of the above-quota production that saturates Russian markets.

Foreign complaints about the RARE sites were a contributing factor to the 2006–7 crackdown, and by most measures the government responded. By 2008, the number of RARE sites used for optical disc production had reportedly fallen to four (IIPA 2010, 2009). A Ministry of the Interior (MVD) police unit called the Eighth Directorate was given the responsibility of policing the RARE sites, but its effectiveness remains a subject of dispute. Confidence in the Eighth Directorate among some industry sources is low, fed by rumors of corruption of the directorate's staff. Criminal investigations have only occasionally resulted in the revocation of licenses, and only a handful of low-level employees of such facilities have been prosecuted.

Less substantiated rumors about state involvement also circulate widely. An owner of a record label in St. Petersburg told us about a plant that used illegal prison labor:

> Some years ago a production facility was raided inside [Prison X]. It shows what a remarkable system we have here. . . . Someone in Prison X, who is very powerful, well connected, and clever about networking, bought an optical disc production line.

17 Small-scale production now plays a relatively small role in the Russian pirate economy, though the situation is dynamic and the IIPA, for its part, has recently begun to signal the reemergence of small production lines as a result of government pressure against some of the larger factories (IIPA 2010).

Defending the Release Window

In the film business, the primary goal of enforcement is to delay pirate access to a high-quality copy during the initial release or exhibition window—the period in which a film makes most of its profits. Rapid, widespread distribution of films is both the key to capitalizing on this window and the challenge to maintaining control of copies. In Russia, the transfer from distributors to movie theatres is a particularly vulnerable step in the distribution chain. Typically, 35mm film reels leave Moscow-based distributors two to three days in advance of a movie release. Reaching more remote locations can take as long as ten days. This is often more than enough time for a detour to a specially equipped studio where pirates can produce a high-quality DVD master.

Providing early access to pirate copies of such films is lucrative, fetching between $10,000 and $40,000 according to our sources. Such copies also quickly appear online—although at this stage it is in the pirate's interest to limit competing channels of distribution. For obvious reasons, studios are most upset by pirate releases that precede the official release (although evidence for a strong substitution effect vis-à-vis box office receipts, even for pre-release films, is weak). The next generation of digital film projectors is designed to address this vulnerability in the distribution chain by downloading encrypted satellite feeds of movies directly to the theatre (Vershinen 2008). Among the advantages from an enforcement perspective is that such downloads can be watermarked, giving police a means to trace digital copies back to their source. In 2008, there were 91 digital screens in Russia, out of a total of 1,800 (Berezin and Leontieva 2009).

> It isn't a cheap line—it costs, probably, one hundred thousand dollars. And decided to install everything in the prison, where the people doing the work don't cost much. In the raid, some millions of discs were confiscated, including one and a half million copies of my discs . . . There was a trial, but nobody was convicted, everybody got away in some way.

The Russian media publish similar stories. One account described the use of psychiatric patients for assembling boxes for pirated video:

> [Assembling boxes] proved to be such mindless work that vile entrepreneurs organized a packaging line in a psychiatric clinic. The final products were distributed from there to warehouses across the country. (Vershinen 2008)

Not all our sources credited these examples, and it is quite possible that some of them are urban legends. But sources did consistently corroborate reports about the wider role of state security agencies and the military in large-scale pirate disc production. Such matters are, for obvious reasons, extremely difficult to investigate, and we did not substantiate them independently.

The crackdown also provides a context for one of the unique features of the Russian pirate market: its high prices. In Russia, $5 for a high-quality DVD is typical, and the price of high-end pirated discs has actually slightly increased in recent years. Pirate prices can even equal or exceed the price of certain categories of licensed DVDs, such as region-specific regionalka, which often involve compromises in quality or features. No other country documented in this report comes close to maintaining this degree of price stability. Elsewhere, the proliferation of low-cost burners and the growth of Internet distribution has radically reduced pirate disc prices—generally to between $1 and $2 at retail for a high-quality copy, and often much less at wholesale. At the high end in other countries examined here, such as in the tourist-priced flea markets of Johannesburg or Rio de Janeiro, prices rarely exceed $3.50.

Our conclusion is that relatively successful Russian enforcement in the lower tiers of the supply chain has afforded the large producers a degree of control over supply and, consequently, pricing. Such market power is very likely temporary. Industrial-scale disc production plays a diminishing role in the larger, digital pirate economy, and it is hard to see how high prices will survive the spread of broadband and digital storage, which are already showing signs of circumventing the optical disc supply chain. In this respect, the digital transition in Russia may have an unusual upside in putting the large, state-protected pirates out of business.

Geography

As we have noted throughout this report, the globalization of media industries has not produced a unified global market for copyrighted goods. Although copyright is an international system in which rights established in one country must be honored in another, the licensing system for copyrighted goods is nation-based and requires producers and distributors in each country to separately license foreign goods for distribution. The vast majority of media goods for the Russian market—including Hollywood movies and international pop albums—are consequently produced under license in Russia. There is very little direct importation of media goods from foreign producers, although movie and music industry groups have complained vociferously about the legal loopholes that enable a small, legal import trade in discounted foreign CDs and DVDs.

The relevant geography of both licit and illicit production is thus a Russian one. Among illicit producers, reports suggest that small- to medium-scale producers are present in most cities (the Ministry of the Interior singles out Kazan, Rostov-on-Don, Samara, and Novosibirsk for attention). But most of our interviews described a concentration of industrial-scale production around Moscow and St. Petersburg, tracking broader patterns of growth in high-tech industry, media markets, and income. Several informants indicated further that, in the post-crackdown era, Moscow has become dominant in terms of both the volume and variety of its production and the extent of its regional networks.

Pirate production is also geographically marked within cities. St. Petersburg, like many Russian municipalities, is not only a post-communist but also a post-industrial city. The

Garbage Firms

A variety of business ownership patterns have emerged to meet the two requirements of the pirate optical disc market: maintaining economies of scale while minimizing exposure to raids. In one common strategy, legal, registered firms act as commercial landlords for smaller illegal businesses (generally known as "garbage firms" in Russian). The garbage firms are registered to fictitious owners but, in practice, belong to the landlord. In the event of police raids, the garbage firm can be thrown off without jeopardizing the parent firm—whence its name.

Syndicates are another organizational response in which a group of firms operate as a single enterprise but without legal contractual agreements. Capital and other material resources are shared, but liability is not. In the event of a raid, police can generally only charge the targeted firm, minimizing losses to the larger operation.

former Soviet heavy and high-tech manufacturing sector is both highly developed and very underutilized. Such declining enterprises are the principle sites of large-scale illegal production. In St. Petersburg, they are typically located at the periphery of the city, following the Soviet pattern of industrial development.[18] Smaller production lines and the "warehouse printing plants" described in the next section, in contrast, do not require large premises and are, consequently, more geographically dispersed throughout the city.

The Social Organization of Distribution

The ease of manipulating licensing regimes, notably via above-quota production, is one of the chief reasons why piracy is so difficult to prosecute in Russia: it is often impossible to distinguish legal from illegal copies. The organization of the distribution chain also presents challenges, however, and more so in the wake of the 2006–7 crackdown as pirate intermediaries change their business practices to minimize risk.

Warehouses

Throughout the late 1990s and early 2000s, large pirate manufacturers usually found it advantageous to concentrate production services within single sites, ranging from the illegal acquisition of originals to production, printing, packaging, and storage. From these production centers, the product would be distributed to smaller warehouses, sometimes called "studios" in reference to their size. Increased police action beginning in 2006 resulted in the closure of several major manufacturing lines and increased risk for producers who stored above-license goods in their facilities. Pirate manufacturers responded by creating networks of specialized

18 A notable exception is the Kirov Factory, one of the oldest and largest industrial plants in St. Petersburg, which is situated in the city center. This plant was raided by police in 2008.

warehouses that separated production from storage and distribution. According to the RAPO and other sources, one-stop shops are now rare.

A RAPO expert interviewed in our study estimated that there are roughly a thousand warehouses in Russia that distribute pirated products to retail (we found a comparable number listed on Russian-language online forums discussing piracy). Based on assessments by both retailers and the RAPO, St. Petersburg, in 2008, had three or four large optical disc plants making both pirated and legal discs, five to ten large warehouses, and about seventy small warehouses through which different white- and grey-market goods were processed.

The multiplication of warehouses permits a high degree of compartmentalization for firms engaged simultaneously in licit and illicit activity. A single owner may control multiple warehouses, with some dealing in licensed goods while others distribute pirated materials, often in close spatial proximity. This separation provides some protection against losses in the event of a raid.

Personal referrals and long-term partnerships between distributors and retailers also play important roles in the distribution chain. Most suppliers, we were told, cultivate relationships with small networks of retailers and protect them from competitors—indeed suppliers compete for retailers rather than consumers. These relationships reinforce security, help suppliers gauge demand and, above all, lower the likelihood of overproduction, which can ruin profit margins.

Different types of vendors have different structural positions in these distribution networks. Vendors who trade from portable stalls acquire stock from the nearest small warehouse (it may be a rented apartment or a commercial structure) and generally carry it with them. Fixed-location retail shops, as a rule, employ delivery services and have designated personnel for managing stock. Large chains often have their own warehouses to which they transport goods by train or truck. Because of the growing concentration of production, more and more product is now ordered through catalogs sourced to suppliers in Moscow or St. Petersburg.

Working outside this mixed licit-illicit economy is difficult and requires substantial investment in managing both the production and the distribution chain. Leading Russian software companies such as Soyuz and 1C, which do have sufficient scale and resources, control their inventory by purchasing directly from licit producers and by operating their own warehouses. Few smaller businesses have this capacity—or incentive structure.

The Deformalization of Retail

The organization of retail in Russian media markets has changed dramatically over the past decade as piracy and, later, stepped-up local enforcement altered the profitability of retail sales and the cost of entry into recorded media markets. In the formative 1995–2000 period of the St. Petersburg media market, music and video businesses invested heavily in retail store branding. Businesses openly sold an array of pirated and licensed goods and competed for consumer attention. The size of the legal market was small, and enforcement was infrequent—or easily bought off. As the pirate media market grew and raids by different enforcement

agencies became more common, market strategies changed. Today, firms trading in music and video are structured to meet the pressure of law enforcement, rather than consumer demand. Stores with pirated goods generally prefer anonymity and generic names, exemplified by the common "CD/DVD" signs that hang from storefronts.

Several informants put the total music/video retail market in St. Petersburg at seven hundred to a thousand "stationary selling points," including established music/video chains, independent music/video stores and kiosks, the day stalls of street vendors, and stalls at weekend open-air markets. The 2009 St. Petersburg Yellow Pages listed sixty "branded" CD/DVD media chains in the city—that is, stores that have a distinctive name under which they formally register their activities, such as Titanik or Nastroyenie. In addition, there are some thirty generic CD/DVD chains. Although indistinguishable from one another by name, their ownership structure varies, with some registered to individuals and others grouped into larger corporate chains.

The shift toward anonymity, mobility, and flexibility in the retail sale of pirated goods is strongest at the level of kiosks and day stalls, which are generally found near train and subway stations and in other high-traffic locations. Foot vendors have also become more common, operating mainly in subway trains. Such vendors are almost always part of larger networks with centralized suppliers and are mainly preoccupied with avoiding the police. The riskiness of the business favors rapid turnover and low prices, which allows for smaller losses in the event of an arrest or raid. The cycle of investment is short, and profit margins are modest. The cheaper categories of pirated music and video are essential to business operations at this level.

Municipal efforts to regulate and occasionally ban these forms of informal trade have proved successful in temporarily disrupting and—in a few cases—destroying street markets, but the broader effect, by most accounts, has simply been the further deformalization of the street trade. As a sales assistant at a specialized music and movie store in St. Petersburg explained:

> Organized pirate markets, large networks, were destroyed [by the police] and became disorganized. Now there are Uzbeks with tables, Tadjiks with tables. Earlier these were stalls with cash registers. Now they don't have them. Everything can be purchased. Everything can be found in the city.

Rather than wiping the pirate trade out, this source argued further, prohibition has stripped it of its last vestiges of formality and transparency, pushing it completely underground and opening it to more harmful and illegal trade and labor practices.

The crackdown of 2006–7 and changes in policy at the local level have also altered this dynamic by substantially increasing the cost of protection. In 2005, according to informants, the cost of maintaining a busy trading spot near a metro station in Moscow was $5,000–$7,000 per month, mostly in rent and bribes to the police and other controlling agencies. Such businesses could generate $4,500–$6,500 a month in profit. Today the margins are much

smaller. Maintenance costs—including bribes—are now closer to $10,000 per month, making profitability uncertain for all but the highest-volume vendors. By most accounts, these changes have been less dramatic in provincial cities and towns, where the enforcement push was less intense and sustained and where paying off the police remains cheaper.

The retail market for optical discs continues to bifurcate. Informants generally agreed that the ratio of licensed to unlicensed goods on sale correlates with the size and "formality" of the business. Large retail chains sell a higher proportion of licensed/legal products, while informal businesses tend toward 100% pirated goods. This market structure presents challenges for vendors who want to "go legal." None of the vendors we interviewed believed that licit sales alone provide a viable model for small and medium-sized businesses. Our interviews found a strong desire to legalize among such vendors but also sharp constraints from competition with the lowest-priced street vendors. As one owner of a middle-sized, medium-priced music shop in St. Petersburg argued:

> SHOP OWNER: Say a store sells licensed products, but as soon as you step out you see twenty tents that sell pirated stuff, at half the price. Well, try to be competitive there!
>
> INTERVIEWER: Selling licensed products is more profitable for you?
>
> SHOP OWNER: For us, having fewer problems is more profitable. And as a way to avoid problems, licensed product is of course better. But how can you switch to licensed stuff if there are small stores, tents, kiosks, in the subway and around it, who beat you down with the price? Thank God, all trade was banned in the subway two years ago. I mean, not only from the subway but from everywhere, and it has affected the license situation in a good way. Because why would someone need licensed discs if they have already bought unlicensed ones, and for half-price?

Piracy is less a choice, in this context, than an economic survival strategy for both parties, and it creates predictable tensions between shop owners and street vendors.

The presence of larger chains selling (by all appearances) exclusively legal goods suggests that the important differentiator is not a conventional notion of formal versus informal organization but rather the scale of operations. As one informant suggested, fully legal media retailing in the Russian market is a "luxury business" because of low rates of return and long investment cycles. Only well-capitalized companies with profit centers in other areas can afford to "play by the rules." The recently established music chain Nastroyeniye (Russian for "ambiance") is an example. Nastroyeniye is known for legal, high-quality media goods.It is also a product of corporate diversification strategies,[19] rather than growth from within the vendor

19 In this case, of a large St. Petersburg-based (but with branches nationwide) gambling business called

market. This was an important distinction in the eyes of several informants, who viewed the combination of high enforcement and high media prices as a structural advantage for big business and a guarantee of a persistent—if increasingly impoverished—low-end pirate sector.

Vendors and distributors of pirate media are acutely aware of the changes that have come with deformalization. Several characterized them as "hurting the consumer." Some talk about the diminishing quality and variety of pirated goods in the marketplace. Many of what were perceived to be the "best" warehouses in St. Petersburg, in the sense of providing quick access to a wide variety of music and film, were closed in the 2006–7 crackdown.

Consumption

In interviews, enforcement officers often blame the consumer for piracy, citing lack of respect for intellectual property laws, lack of knowledge or confusion about what constitutes piracy, and a general indifference to the moral dimension of piracy in favor of the obvious economic advantages. Our work—involving a survey of DVD consumers in Irkutsk, a focus group in St. Petersburg, and analysis of online discussion groups—suggests that Russian consumers bring a great deal of discrimination to the purchasing of pirated goods and that their moral calculus is more complex than a simple account of ignorance, greed, and theft accommodates. Moral discourse is hardly absent, but it often targets corporate dominance of the media markets and US pressure on Russia in making judgments about fairness and legitimacy in the actions of both pirate and licit producers.[20]

"Piracy," in this context, is a broad concept covering a shifting array of activities, which ordinary Russian consumers often only label on the spot in their interactions with media markets. "Media pirates" are favorably distinguished, notably, from "counterfeiters" who pass off fakes at original prices. Other forms of illegal copying, even when of poor quality, are accepted, and some are routinely praised. Neutral and positive attitudes toward illicit media goods, their trade, and the groups involved in it are strong among Russian consumers. Rather than morally indifferent, Russians are highly sensitive to the political issues surrounding piracy—just not the ones industry stakeholders would like.

The Socioeconomics of Consumption

Our work indicates that the vast majority of Russian consumers are active participants in the pirate economy, whether through the purchase of unlicensed CDs or DVDs or—increasingly—through the downloading and sharing of digital files.[21] Inevitably, differences in these practices

Volcano, which sought out new investments after gambling restrictions came into effect in the city.

20 Russia may be unique in having such positions become the basis of advertising campaigns themselves, as one informant described in the case of AllofMP3.

21 A recent survey commissioned by the International Chamber of Commerce put this number at 89% of the population, with software only slightly behind at 80% (BASCAP/StrategyOne 2009).

are shaped by age, socioeconomic status, and associated variations in purchasing power, access to technology, and cultural capital.

In our survey of three hundred DVD consumers conducted in Irkutsk in December 2008 with the Evolution Marketing Center, college students were the most active viewers of pirated movies and—as elsewhere—lead the way in the shift from optical disc purchases to downloaded or otherwise shared digital files. Personal computers, university-based Internet connections, and—increasingly—home broadband connections are relatively common in this group. Although our survey recruitment method likely oversampled those with high Internet skills, the frequency of reported downloading still surprised us: some 50% of those surveyed reported downloading at least three films or videos per week. Among the larger pool with access to broadband connections, respondents reported downloading, on average, ten albums a month and five to ten films. Despite this shift, the overwhelming majority of consumers in our sample still buy discs from pirate vendors—and among lower-income consumers, almost exclusively so.

Opinions about the importance of purchasing a licensed disc or paying for a download varied. Students led the way in general disregard for licensing: only 17% described it as "very important" or "important" (the other options were "not very important" and "not at all important"). Blue-collar and white-collar workers accorded licensing more importance: 45% and 50%, respectively, for the two categories combined. When asked how much they would pay for a legal DVD, blue-collar workers indicated a maximum average price point of around 140 rubles (about $5.60), and white-collar workers 165 rubles (about $6.60), with students falling in the middle. All these averages are well below the price of licensed DVDs ($14–$20), providing an indicator of the pricing mismatch in Russian media markets.

Lower-income families are, predictably, the most sensitive to price and gravitate toward the low end of the price/quality spectrum of pirated goods. White-collar consumers are at least potentially "swing consumers" motivated by the implied quality of the licensed disc or legal download. And although they still describe legal CDs and DVDs as overpriced, they do occasionally buy them. More generally, they furnish the market for perfect above-quota copies, which sell at a higher price than the low-end pirated goods. Our research strongly suggests that the struggle between pirates and legal distributors is primarily a struggle for this new middle class, which can be "tipped" into the licensed market under the right circumstances.

Patterns of Consumption

In nearly all cases, respondents drew attention to the complex set of decision points that could override the price barrier. Most often, these were contexts in which the quality or the social function of the purchase was at a premium. Several respondents observed that it was poor form to give pirated copies as gifts, making gift-giving a significant motivator for purchasing licensed CDs.

Our focus group also revealed strong "sampling effects" from downloading in some

contexts, in which the discovery of music or movies through pirate sources led to the purchase of licensed CDs or DVDs.[22] Such purchases generally occurred in the context of collecting. High-quality CDs remain the gold standard in many music collections, and the supplemental materials packaged with a licensed CD provide added value for those with broader interests in music culture. Some respondents also reported purchasing DVDs after sampling downloaded versions—again in contexts where collecting was a primary interest.

Sampling via pirated goods mitigates the problem of poor signaling in cultural markets. Because consumers generally buy cultural goods with only limited information about their likely satisfaction, many of their choices turn out to be wrong. In a context of high prices relative to local incomes, bad choices are especially costly, and the consumption of licensed music and movies remains an expensive hobby. The licit media market in Russia offers few ways to lower these costs of casual cultural consumption. Notably, piracy occupies the place of low-cost movie rental services, which are virtually absent from the Russian market.

Implicitly or explicitly, every person interviewed expected the quality of a pirated CD or DVD to be lower than that of an original, and occasionally so poor that discs may need to be returned. But quality, many respondents made clear, refers to more than the fidelity of the recording. For the majority of Russian families who don't own sophisticated TV and sound systems, properties such as screen resolution, surround sound, and other high-end differentiators in the US and European markets do not greatly matter. The first measure of quality is basic playability. Next come obvious distinctions between poor camcordered copies of new films and DVD-quality prints. Quality also frequently refers to the print materials that accompany the disc, including its inserts and cover. For regular consumers, low-end and low-priced pirated discs are generally purchased in locations near one's home or workplace, where they can be returned if they prove unsatisfactory.

Comparative Purchasing Power

Our findings suggest that piracy in Russia is—first and foremost—a failure of the legal market to price goods at affordable levels. The comparison of GDP per capita in Russia to the prices for legal and pirated CDs and DVDs provides ample evidence of this disconnect. The problem is sharpest with respect to the international goods that dominate Russian markets—notably film and software. As in other countries, international licensing models allow for only modest retail-price discrimination. International CDs, DVDs, and nearly all software at retail are sold—with occasional exceptions—at Western prices, leading to huge differentials in the cost of goods relative to local incomes.

Like a number of other high-piracy countries, Russia has seen a handful of experiments with lower pricing of media goods, including efforts by Columbia Tristar and Warner Brothers to create a "mass model" in 2003–4 by cutting DVD prices to $10 and $15 respectively

22 The group was too small to derive quantitative estimates of this effect.

How to Watch *Night Watch*

"From my point of view, a competitive-price policy can be quite effective. For example, ORT-Video, an official distributor of the latest Russian box office hit *Nochnoi Dozor* [Night Watch], carried out an experiment by reducing the price of licensed DVD copies of the movie. The price was set at almost the same level as that for illegally duplicated copies. As a result, the official sales of the movie soared, while the number of bootleg DVDs dropped to a trifling 2%. Around three hundred licensed movies are being distributed in DVD format on the basis of the same pricing. A few of them are foreign-made. It is mostly the movies that were already shown in many theatres across Russia; therefore the market demand is steady.

Some of those DVDs are on sale in my stores. I pay a reasonable price when I buy them wholesale, and they are officially licensed products so no brushes with the law are expected. Moreover, lately the legal distributors have started releasing movies on DVD much faster than before. In the past a movie would be available on DVD only two or three months after it was officially released in Russia. Nowadays the delay lasts a month at the longest. These latest developments significantly hamper the illegal trade of the pirates. My message to those who are trying to fight piracy is the following: we are not die-hard perpetrators; we are businessmen trying to succeed in the competitive business environment. Therefore, the market mechanisms should be used for putting an end to piracy."
–*A retailer in Veliky Novgorod* (*Pravda* 2005)

(Arvedlund 2004); a more significant effort by Russian film distributor ORT-Video, which briefly released its catalog at lower price levels; and the low-priced regionalka licensing of DVDs in the provinces. Software companies like Microsoft have experimented with lower-cost, stripped-down versions of their products, such as Windows XP Starter Edition, which limited multitasking and networking features. But these efforts have been controversial, short lived, and largely unsuccessful at making a dent in the pirate market. Modest price drops and lower-quality options may boost sales at the margin but are clearly not compelling alternatives to the pirate market for most Russians.

More radical measures by Russian distributors to compete at pirate prices, for their part, have not been sustained. Reduced-functionality software has fared similarly—pushed into use in some institutional-licensing contexts but not viable in the retail market, where full-featured pirate versions provide better value. As a result, international prices have remained the norm for DVDs, international music, and retail software. The notable exception to this rule is the local music business, which is independent of the majors and consequently less bound by international licensing regimes and pricing norms. In contrast to the movie and software businesses, Russian music labels often compete with pirate pricing—generally in the hope of building audiences for more lucrative live performances.

There is no single price for pirated goods, but rather a price range reflecting differences in the point of sale, perceived quality, and popularity, among other factors. The price differential between licensed and pirated goods also widely varies but is especially stark in the DVD and

retail software markets. A licensed international hit movie or album is commonly priced at between 350 and 450 rubles ($14–$18 in 2008–9), with certain titles priced as high as 800 Rubles ($32). Albums published by local labels—representing an unusually large 80% of the total Russian market according to the IFPI (2009)—are almost always significantly lower in price, ranging from 150 to 200 Rubles ($6–$8). Business software at retail, such as Microsoft's Office suite or Adobe's Creative Suite, is priced at Western levels.[23]

High-quality pirated CDs and DVDs, in contrast, generally range between 100 and 150 rubles ($4–$6). Compilation discs—whether the popular collections of ten to twelve films or software packages combining twenty to thirty commercial programs—undercut even this price level and often run as little as 50–100 Rubles ($2–$4).

What do these prices mean to most Russians? Russian GDP per capita is roughly $9,000 in nominal US dollar terms (IMF 2009), representing a little under one-fifth the US GDP per capita. Median Russian income is under $5,000, with higher earners disproportionately concentrated in Moscow and St. Petersburg.

Even in a context of high pirate prices (in comparison to other countries), the market-creating role of piracy is obvious. The price of a high-quality pirated CD or DVD in Russia is comparable to the price of a legal disc in the United States, relative to per capita GDP. The pirate market, in effect, is the only mass market in Russia for audiovisual goods. For software, the discrepancy is much larger. In our street survey of pirate prices in St. Petersburg, we found no stand-alone copies of major productivity software or games but many large pirated software compilations, which retail for a couple dollars depending on the contents. According to Microsoft, software piracy is still prevalent in established retail—present in 25% of software-selling stores overall and up to 70% in more remote regions of Russia (Microsoft Russia 2010). Much of this sector, our sources indicate, has simply moved to non-commercial distribution online.

This general pattern of pricing for legal media (see table 4.1) is consistent with our findings in other countries. The film market is highly integrated at the global level and maintains strongly uniform pricing for DVDs. $14–15 is the floor for DVD pricing in most countries, regardless

23 Our interviews—though not our fieldwork—revealed noise in the price data for some of these categories of goods that we were unable to fully resolve. Microsoft representatives, for example, criticized our use of retail prices for small businesses, on the grounds that Microsoft offers small-business discounts (analogous to the lower-priced volume licenses that Microsoft negotiates with many large institutions). Although our sample is by no means representative, none of the business owners interviewed for this report were aware of or took advantage of such programs. From their perspective, the market is split between the high-price retail sector and the low-price pirate sector. There are a number of possible reasons for this, ranging from inadequate investment in licensing programs by vendors (completing markets under such circumstances requires significant local investment) to reluctance on the part of small-business owners to formalize their businesses except when absolutely necessary. These explanations are not mutually exclusive. Our description, in any event, is consistent with the 68%–80% rate of piracy in the software market reported by the BSA over the past five years. Similar issues complicate music pricing at the periphery of our account, including the release of lower-priced cover albums of international hits and short-lived experiments by the major labels with lower domestic pricing.

Table 4.1 Legal and Pirate Prices, 2008-9

Movies

	Legal Price ($)	CPP Price	Pirate Price	Pirate CPP Price
The Dark Knight (2008)	$15	$75	$5	$25
The Inhabited Island (Обитаемый остров, 2008)	$15	$75	$5	$25
Compilations (10–12 films)	—	—	$4	$20

Music

Coldplay: Viva la Vida (2008)	$11	$55	$5	$25
Dima Bilan: Against the Rules (2008)	$8.50	$42	$5	$25
Krematorium: Amsterdam (2008)	$6.50	$32.50	$5.75	$ 28.75

Business Software

Microsoft Windows Vista Home Premium	$260	$1300	–	–
Microsoft Office Small Business 2007 (for Windows)	$500	$2500	–	–
Adobe Photoshop CS4 Extended	$999	$5000	–	–

Entertainment Software

Grand Theft Auto IV, PC (2008)	$20	$100	–	–
Mario Kart, Wii (2008)	$50	$250	–	–

The "legal price" is a widely available retail price for the good in Russia. The CPP, or comparative purchasing power, price is the hypothetical price of the good in the United States if it represented the same percentage of US per capita GDP. "Pirate price" and "pirate CPP price" apply the same principles to the pirate market.

Source: *Authors.*

of the origins of the film. Russian hits like *The Inhabited Island* (2008) retail at the same price as Hollywood hits like *The Dark Knight* (2008). The music market is more complex and shows prices ranging from international hits like Coldplay's *Viva la Vida* at the high end, to regional favorites like Dima Bilan's *Against the Rules* in the middle, to local hits like Krematorium's *Amsterdam*, which is sold slightly above the price of high-end pirated goods. The dominance of Russian music labels in the market and the strong promotional function of CD sales clearly impact pricing. Business and entertainment software, in contrast, show no price discrimination to speak of at the retail level (although as in other countries, institutional markets are generally served through lower-priced volume licensing).

Author and Copyright

Author's rights and the commercial features of copyright are distinct issues in Russian copyright law and—our work suggests—in the minds of many Russian consumers when invited to explain how media commodities and media markets work. In our interviews, sympathy for artists and authors was usually strong. Sympathy for the business culture responsible for the commercialization of cultural work was usually nonexistent. Justifications of piracy generally occupied the space between the two.

> They usually buy the right for distributing a film, and it has no relationship to the author himself. It has no impact on the author that I buy an unlicensed disc. We are talking about author's rights and about licensed discs as if they're all in the same terms. These are two different things! (23-year-old male, St. Petersburg focus group)

Several focus group members offered accurate descriptions of copyright, author's rights, and the transfer of rights associated with commercial production—though knowledge of the details of copyright law was infrequent overall. Much more common was the general belief that culture is, fundamentally, a common heritage, a "public domain" that should be accessible to all. When pushed to clarify these positions and reconcile them with existing copyright law, many respondents argued for more limited rights of commercial exploitation. The duration of copyright protection seventy years beyond the death of the author (in Russian law) proved particularly unpopular: "Why should [an artist's] successors own what he created? In my view, after the author's death, his work should belong to everyone, to the society" (41-year-old male, St. Petersburg focus group—higher education, high income, employed in marketing).

Respondent attitudes toward piracy generally combined this bias toward access with broader cynicism about business practices and business culture—both licit and illicit. Although all participants were aware that the sale of pirated optical discs was illegal, few framed this as an important moral dilemma, and none condemned the practice. Some expressed approval of pirate vendors. Several described piracy as occupying an empty niche in Russian cultural markets and pirates as business people who had moved in to fill it. Several reserved their disapproval for the "counterfeiters" who pass off fakes at the full licit price, in distinction from

"media pirates" who deal openly in pirated material or who seed content on peer-to-peer websites.

> My attitude toward pirates is neutral. When I find a pirated copy of something I have been looking for for a long time, I feel happy that there are people in this business who help me to fulfill my needs. I feel rather positively toward them. (24-year-old male, St. Petersburg focus group—student)

Any qualms about dealing with the black market disappeared when the subject turned to Internet access. Free downloads on the Internet, and P2P file sharing networks in particular, garnered unambiguous praise from the majority of respondents. Central to this approval was the absence of a profit motive and the resulting lack of consumer implication in the corrupt—and corrupting—wider business culture. In our study, P2P proved to be a very powerful focal point for Russian attitudes toward piracy, combining a self-interested economic rationale with a moral framework that nearly always trumped the claims of rights holders.

Counterfeiting

In Russia, the terms for piracy (*piratka*) and counterfeiting (*kontrafakt*) are used interchangeably in industry and media representations of copyright infringement (a term that, in contrast, is almost never used). Traditionally, however, piracy and counterfeiting refer to distinct phenomena: piracy to the unauthorized copying of the content of expressive works; counterfeiting to the unauthorized application of brand names to cheap copies of goods—often with the implication of consumer fraud. The former violates copyright and the latter trademark.

Where consumers generally treat piracy as a neutral phenomenon, subject to only limited moral censure, the term *kontrafakt* has stronger negative associations with health and safety risks—especially in connection with fraudulent pharmaceutical and alcohol products. As we discuss in chapter 1 of this report, our collective work finds piracy and counterfeiting to be largely disconnected phenomena at the global level. Efforts to precisely duplicate the packaging and presentation of licit discs are rare and, on the Internet, irrelevant. Cross-border smuggling—the basis of the counterfeit-goods trade—has been largely replaced by a mix of local production and Internet distribution.

In Russia, however, the central role of above-quota production in licensed factories creates a zone of overlap between the two phenomena—albeit in ways that erase notions of substandard quality. The place accorded to this type of counterfeiting in Russia is unique in this report. And yet we are hard pressed to find evidence of widespread fraud. In our findings, Russian consumers show remarkably little confusion about what they're paying for—indeed the complex negotiation of price versus perceived quality is popularly understood as a Russian specialty, grounded in the long-standing role of black markets in the distribution of luxury goods (Dolgin 2006).

In cases where the copy is above-quota or otherwise exact, it makes little sense to speak of fraud: the consumer gets exactly what he or she expects. More often, the choice to purchase unlicensed goods reflects a deliberate compromise. Consumers weigh price against perceived quality, not against perceived origins. Discontent with pirated goods, in this context, arises when the paid price is seen as higher than the received quality. Such negotiations shape the spectrum of pirated goods available in Russian markets. There is, for example, a large market for low-quality pirated products offered at low prices, with the corresponding risk assumed by the buyer.

Intentional deceit of consumers is, of course, far from unknown. There are a variety of ways in which packaging can mislead with regard to quality or content, and it isn't difficult to find such products in the retail markets of St. Petersburg or Moscow. But deceptive practices in the pirate market are mitigated by the important role of return customers in many vending contexts—and the resulting importance of trust. Pirate vendors often have a strong customer-service ethos that includes the exchange or return of defective or deceptive discs. Such services often go well beyond what is available in the licit market. As one of St. Petersburg's major music stores makes clear: "Licensed discs are not subject to exchange or return."

It seems likely to us that the deformalization of pirate retail in Russia will put pressure on this service-oriented model. As pirate distribution leaves the sphere of the (however informally) regulated market, connections between vendors and customers become weaker, and more opportunities for outright fraud arise.

Local Effects

The moral calculus around piracy often has strong patriotic overtones. US pressure on the Russian government related to IP and trade issues is widely viewed by consumers as commercial imperialism—a form of aggression rather than an assertion of universally shared rights. The intellectual property of foreign corporations, in this context, circulates at a moral discount and raises fewer concerns about the impact of piracy.

Many of our informants believed, in this context, that domestically produced Russian music and film are pirated less voraciously than foreign material. Although empirical evidence is thin, we see both social and economic factors supporting such a claim. First and foremost is the issue of cost: the economics of licensing in Russia create a strongly bifurcated market for Russian and foreign music. The costs of licensing and producing Russian music are significantly lower than for foreign acts, and the resulting discs are sold at prices much closer to those of their pirated competition. It is far easier for consumers to make the "right" choice when legal CDs cost $6–$8, while pirated copies cost $4–$5. The price of a foreign-licensed CD, in comparison, averages $12 and can go as high as $30. The market for such goods is accordingly tiny, and the range of goods available is very limited.

Our findings also point toward a more tentative distinction between local and non-local artists within Russia. Music retailers in St. Petersburg described a loose system of obligations in

which social ties among musicians, producers, record companies, and retailers anchor norms of respect for local commercial products. "No one wants to hurt one's own," said one retailer. Informants described several cases in which representatives of St. Petersburg-based record labels personally reproached music store owners for pirating local bands, and others in which music producers and bandleaders made the rounds before album releases to urge music store owners to refuse pirated products.

The view that local musicians are sheltered from illegal copying was not universally shared, however. As one representative of an anti-piracy organization put it: "They write on the Internet that 'we do not pirate Russians.' Come on, everybody is pirated!"

The Economic Function of Piracy

For obvious reasons, industry research and lobbying paint piracy as a drain on the Russian economy and emphasize losses to copyright holders. The BSA's estimate of total software losses in Russia topped $4.2 billion in 2008 (BSA/IDC 2009). Creative reframings of piracy's effects have also become common in this context. The BSA now produces annual estimates of the number of jobs that would be created in return for small reductions in software piracy. But this account of piracy as a pure loss to the economy is misleading. Piracy is not just a drain on the media economy in Russia—it is a fundamental part of the media economy, deeply woven into a wide range of licit practices and forms of enterprise. The direction of claimed losses also matters greatly. From the perspective of the Russian economy, losses to international rights holders are, strictly speaking, gains for Russian businesses and consumers. Losses to Russian copyright holders, in contrast, represent a more complex reallocation within the Russian economy, in which money is not "lost" but spent in other ways. For countries that import more IP than they export, like Russia, this balance of exchange may be strongly positive.[24]

Even within law enforcement agencies and anti-piracy organizations, views about the impact of media piracy on Russian society vary. Strong negative judgments equating piracy with theft are, of course, commonplace. But so too are alternative accounts, offered less in support than in explanation of piracy. The roles of the informal economy in Russia as a source of additional jobs and second incomes and—in cultural terms—as a support infrastructure for cultural diversity figure prominently in these accounts. These roles are especially strong outside Moscow and St. Petersburg, where the commercial media infrastructure remains very underdeveloped.

Survival in the Informal Economy

Media piracy is attractive to workers in the low-end retail economy because it affords relatively high profit margins compared to other types of trade. According to our interviews with vendors

24 See the analysis of economic gains and losses, including BSA/IDC job-creation estimates, in chapter 1.

and store owners, the retail markup for licensed media goods runs approximately 80%–150% for CDs, 80%–200% for DVDs, and 40%–60% for the fading LP market. Unlicensed goods, in contrast, generally carry a 200%–300% markup (over significantly lower wholesale prices). For street vendors further down the economic ladder, other incentives come into play: the informal sector provides jobs to social groups with little access to legal employment—especially the urban poor, migrant laborers, and students. In most other regards, the street vending of CDs or DVDs is comparable to selling other commodities, such as food and clothes, but yields higher incomes.

The informal economy in St. Petersburg is organized around several different types of commerce, ranging from transient vending in subway stations, to more organized sales in open-air flea markets, to established retail shops. By our estimate, there were between 150 and 200 subway vendors in St. Petersburg in 2008–9. Most work from foldable card tables, which can be set up and packed away quickly. Vendors at different stations are almost always part of a larger distribution chain run by a single owner, who takes most of the profits. A vendor typically receives 10% of sales in salary. Our research indicated that a hired vendor typically earns between 500 and 1000 rubles per day ($20–$40), or approximately $450–$900 per month. This is between 78% and 157% of the median income in St. Petersburg (Regnum News 2008). It is also significantly higher than other segments of the street economy. Footwear vendors working at marketplaces around subway stations, by comparison, earn an average of 500 rubles ($20) during the same nine- to ten-hour workday. With an estimated profit of $10–15 million generated annually in the city by pirate street vending, some $1–1.5 million ends up as household income for those employed in the sector.

The sale of pirated goods is thus a relative privilege for people who would otherwise be—at best—part of St. Petersburg's working poor. Roughly 10% of the city's population qualifies as poor by Russian standards. The median monthly income in 2008 was 19,000 rubles, or $770, while the estimated minimum subsistence level is 4,900 rubles, or almost $200 (City Statistics Bureau 2008). For the many families in this category, the additional income from piracy is often the difference between simple poverty and destitution, as one working family member usually supports anywhere between two and four non-working members. The trade in pirated goods has one important further advantage: it is relatively socially acceptable and does not carry the kind of stigma associated with the drug trade, prostitution, or other forms of criminality (Ovcharova and Popova 2005:15, 28, 35).

Well-known open-air markets like Gorbushka in Moscow and Yunona in St. Petersburg play prominent roles in this wider economy of secondhand, grey-market, counterfeit, and pirated goods. But they are not unique. Almost every open-air market in Russia includes trade in software, music and video CDs, and DVDs—all of which are likely to be pirated. Most trade in the cheapest variety of pirated goods—the products of "cottage-industry" production. Used CDs, DVDs, and video cassettes are also common. Some vendors carry more conventional high-end pirated stock purchased from larger suppliers. The prices of CDs and DVDs in these

markets are significantly lower than in subway stalls: 50 rubles ($2), as opposed to 100–150 rubles ($4–$6), for a DVD. In these circumstances, a single vendor generally sells between one hundred and two hundred discs over the weekends in which the markets operate, making a 5- to 10-ruble profit ($0.20–$0.40) on each disc. Total profits may range between 1,000 and 2,000 rubles ($40–$80) per weekend. The less-organized, part-time structure of the work in such marketplaces means that many of the vendors are industrial and service workers trying to supplement their incomes. One of our informants was a travel agent who organized trips abroad for Russian tourists.

The Small-Business Dilemma

Software is critical infrastructure for most businesses, from basic productivity tools to the more specialized software packages needed as businesses move up the value chain. As in the retail-sales sector, however, operating with fully licensed software in Russia is often a privilege of size. Because software is generally priced at or near Western levels, it represents a disproportionate and often prohibitive investment for small businesses and start-up companies. Although open-source software tools can provide much of the same functionality for free, low rates of open-source adoption and—in some areas—inferior open-source alternatives impose costs on use, especially when commercial software operates as a de facto standard.

Given the choice between free open-source options and free pirated commercial software, Russian businesses almost always opt for the latter. The downstream consequences for the Russian economy—or for any other economy, to the best of our knowledge—have never been adequately calculated.[25] But there is little doubt that pirated software is both an enabler of economic activity and an obstacle to wider open-source adoption.

The role of pirated software as infrastructure for emerging software companies is an open secret in the globalized software industry—sufficiently so that the Romanian president, Traian Basescu, publicly thanked Bill Gates in 2007 for the role that pirated Microsoft software played in IT development in Romania (Reuters 2007). Although Russian firms like 1C and Kaspersky Lab are now large enough and integrated enough into the global software economy to make them domestic advocates of IP enforcement, the economics of small software firms still virtually dictate the use of pirated software.

The price of licensed software for a firm working with professional multimedia tools, such as Flash, can start at roughly $2,000 per employee and rise quickly from there.[26] Software licensing costs can easily represent the largest portion of investment in a new web or design business. Few start-up firms have sufficient capital or prospects for return business to warrant such investment, especially in a context where "free" pirated alternatives are widely available. The owner of a start-up media-production firm in St. Petersburg put it this way:

25 See chapter 1 for a discussion of why BSA claims on this subject should be discounted.

26 A typical professional software setup could include the Adobe Creative Suite 5 Master Collection ($2,500) and more basic Microsoft Windows, Microsoft Office, and productivity tools ranging up to $1,000.

> We can cover all the office costs for four months for this amount—rent, phone, bank service, taxes . . . What part of turnover is this? Well, it's hard to say—the turnover is not stable at all, as is typical for any small firm. There's just no free money we can take out of the business and invest in software.

The logic is much the same in other software-dependent businesses, such as printing. Margins on print jobs are invariably thin, and such businesses rarely begin on sound financial footing. Software costs per employee or seat can easily run $3,000,[27] and a business with any significant volume would need multiple seats.

While incentives run strongly toward pirated software for small businesses, such choices involve a measure of risk. Small businesses are often visible and potentially vulnerable to police and private investigators. The ability to effectively manage software licenses is itself a luxury of size. Maintaining accurate licensing records for multiple versions of different software tools, over years and across machines, is challenging for firms that lack well-run, professional IT departments and puts even well-intentioned software purchasers at risk. Large corporations, in contrast, are better able to absorb software-licensing costs and, importantly, cut deals with software vendors and defend themselves against charges of infringement—factors that, in turn, make them less likely to be raided. Enforcement tends to fall hardest, consequently, on small businesses, where a raid or a fine can be fatal.

As in the retail sector, consequently, the price differential between licit and pirate media shapes the larger opportunity structures of business in Russia. Because only large, well-capitalized companies can afford to operate consistently within the licit economy, enforcement campaigns confer de facto commercial advantages on those firms by making competition and innovation from below more costly and precarious. Although large businesses would describe the pressure to remain licit as an additional cost, the history of the last fifteen years in Russia is unambiguously one of oligopoly—of self-perpetuating commercial advantage for the largest players. IP enforcement, perhaps unavoidably, has become part of that dynamic.

The Cultural Function of Piracy

The poverty of legal supply is a key to understanding the cultural function of pirate markets. With the exception of international hit albums, most foreign music is not legally available in Russia—even in St. Petersburg, Russia's second-largest media market. Provincial markets are even more poorly served. Legal distributors generally do not stock niche genres or artists that fall below a perceived threshold of international popularity. Manufacturers make similar choices due to the high costs of licensing foreign work.

27 A printer would need to buy three to four programs per seat: commonly a lower-end Adobe Creative Suite 5 bundle ($1,800) and the usual Microsoft packages and productivity tools.

The growth of chain stores, centralized production and distribution, and police pressure on smaller retailers are both contributing causes and symptoms of this problem. All work to diminish the role of customer relationships in the retail business. Local feedback loops from customer to retailer to distributor to manufacturer are much less frequent in the new era of large diversified chains—and indeed have become a signature of "unlicensed" retail and production. The market advantage of pirate vendors is thus one not only of price but also of greater proximity to consumer demand and greater freedom to innovate with compilations, mash-ups, and other alternative formats to meet that demand. The greater diversity of content within the pirate market is particularly important to groups who feel strongly connected to international cultural conversations—especially the educated, mostly urban Russian intelligentsia, for whom access to a wide variety of cultural goods is a condition of cultural participation.

Interviews with older St. Petersburg residents reveal a consistent set of observations about piracy's place in the transition from communism. The social consciousness of many educated Russians in the communist era was formed through the consumption of censored Western cultural goods—typically available through the black market and other clandestine networks (Baker 1999). The end of communist censorship unleashed enormous pent-up demand for such works. A wide variety of books, films, and music came to market, but at prices that were prohibitive for all but a few Russians. Piracy—first of books and cassettes, and more recently of discs and digital files—became the main remedy for this problem.

Specialty Stores

To a significant extent, this cultural diversity role in Russian cities has been filled by specialty music/video stores, which often deal in niche film genres and music subcultures. Because legal manufacturers and distributors in Russia cannot efficiently license and produce for small markets, specialty stores deal mostly in pirated goods. Often they are the only suppliers for whole categories of music and film.

The management of such shops often involves a mix of business and vocation. In our research, shop owners recurrently emphasized their sense of contributing to the education of the Russian audience. Such considerations did not obviate moral concerns about piracy but did generally overcome them.

> As for the moral side of things, yes, there is nothing good in the violation of somebody's rights. There is nothing to be proud about. But I am doing this not in order to make mega-profits; I am doing this because I think that people in this country, in this city, should have access to good music and good films. I will not become rich doing this, that's for sure. But people will get access to these things. (Owner of a well-known St. Petersburg specialty music/video store)

In 2009, there were a handful of specialty shops in St. Petersburg that sold music and film and two or three more that specialized in video only. The social roles these shops play go well beyond the traditional functions of the media retail business. They anchor local communities of music and film collectors and serve a broader enthusiast culture, stocking vinyl records and secondary literature, organizing film showings, and—perhaps most important—promoting local and lesser-known artists. Several of the stores have libraries of MP3 and MP4 files, which can be made into compilations and burned on demand. The dialogue between customers and retailers shapes both the stock of goods and the services offered.

New market niches can be—and often are—created through these customer relationships, and store owners and staff sometimes play an important part in building audiences:

> Yes. I understand that they are pirates. But I also understand that if I don't take a step toward these pirates myself, the listener who is interested in electronica will never learn about the Frans label or the existence of the Violet project, which combines electronica with psychedelia. No Russian magazine will write about this project. And if one day someone wants to organize a concert by Violet, no one would come—or only those few people who either downloaded it from the Internet or bought it from me. (Manager of a St. Petersburg specialty music store)

This manager also views her role as one of integrating Russia into the wider global market for live performance:

> I am thinking about the day when the group Sunn comes to Russia. In order for them to come, I need to prepare the ground, the audience. So that when I come to a promoter and say, "Let's bring Greg Anderson to Russia," I have an answer when he asks me, "Will it pay?" Every promoter has to know whether it will pay. And for that I prepare my audiences.

Because major legal distributors rarely go beyond a narrow stock of international hits, international music scenes in Russia have been built largely around pirate networks.

For specialty store staff, maintaining this loop between taste-building, promotion, and consumer demand in Russia is not easy. One popular independent music store in St. Petersburg works on a regular basis with three warehouses, all of which furnish a mix of licensed and unlicensed CDs and DVDs. The important differentiator, for store owners, is not the license but rather the quality of the service: the range of titles available, the frequency with which they are updated, and the speed with which stock is delivered to the store. Store staff work, especially, to ensure that they stock titles reviewed in international music publications like the *Wire*, which are increasingly accessible online. Suppliers, for their part, routinely frustrate retailers by not updating their offerings with enough frequency. As the same specialty store

manager emphasized, "I tell them, if you guys are pirates, at least make sure you bring in new music!"

In our interviews, music producers and musicians expressed ambivalence toward this promotional function. Although many viewed piracy as "theft," a majority also understood that piracy helps build audiences for live shows and can provide an indicator of popularity. As one record promoter argued:

> Nowadays pirates don't pirate anything and everything, thank God. They need to make money. So when I see one of my projects pirated, it means it's good. I have become popular. My promotion has worked well in this project. Pogudin, The King and the Clown, The Pilot, and Night Snipers became popular, yes. Pirates pirated them, and I am very proud of it.

Expanding the Market

The market for cultural goods extends far beyond the available licensed material. Pirate production—and sometimes non-commercial production—fills the gap. Documentaries and educational programming, to take two popular genres, almost never appear in licensed form, yet pirated British and American World War II documentaries and military history videos are commonplace in the pirate market. Meditation and yoga videos, self-help audiobooks, language courses, and religious sermons ranging from Orthodox Christianity to Buddhism to Pentecostalism also circulate widely. Although the commercial media in these contexts is clearly pirated, other material—especially religious media—is often produced without express commercial purposes. Circulation, rather than sales, is the primary goal, with the informal marketplace providing the infrastructure.

The pirate market's close connection to consumers sometimes results in product innovation, occasionally to a degree that produces original and valuable new work. Unauthorized subtitling and even dubbing of foreign material into Russian is a prominent example. A trader at St. Petersburg's open-air market Udel'naya described the phenomenon:

> Well, they shoot it on video in a movie theatre and then translate the dialogue. There is a special site, Kvadrat Malevicha, where you can find all kinds of Western TV series, like *Lost* and so on. They offer all the popular Western serials that are not aired in our country at all or only with a big delay. The site translates these series [into Russian] at their own audio studio—yes, they do have their own studio for translation.

The intersection of Russian-language film-dubbing traditions and cheap sound-mixing technologies has also given rise to a popular genre of alternative voiceovers, pioneered by Dmitri Puchkov (a.k.a. "Goblin"). Many of these alternative dubs are serious efforts to improve

the translation of colloquial language. Others are "funny translations" that make satire out of the original material. Goblin's satirical edits of the *Lord of the Rings* films, *The Matrix*, and *Star Wars: Episode I* have been enormously popular and led to the inevitable dual-track DVDs. The same trader noted:

> Recently pirates began to issue films which can switch from "normal" translation to "funny Goblin" and back. The movies have both soundtracks. This is a very popular format in the market now.

Film compilations and "greatest-hits" music compilations populate much of the middle and lower tiers of the pirate market. Although some of these are pirated versions of authorized greatest-hits albums, many are original compilations released by pirate producers. Many have additional tracks or favor songs that became popular in the Russian market. The general decline of the album format also plays a role, as pirates respond to consumer preferences for cherry-picking hits and avoiding filler. Film compilation DVDs—often grouped by genre, actor, or theme—are almost always original pirate productions.

Reproducing the Intelligentsia

Ten years after the transition from communism, German Gref, the minister of economic development, offered a bleak assessment of Russian cultural institutions: the physical plants of theatres, museums, and other infrastructure for culture were in severe decline; the cultural and informational isolation of many regions of Russia was on the rise; and wages among employees in the cultural sector were falling. As a result, he argued, Russia was playing a diminishing role in global cultural production (Gref 2000). The groups hardest hit by this decline were public employees in schools, universities, orchestras, museums, and other cultural and educational institutions—the core of the Russian intelligentsia. Plummeting incomes and the rising costs of cultural and educational goods made this class of educated urbanites a natural consumer of pirated media. The superior diversity of the pirate marketplace, especially for non-mainstream and foreign imports, solidified this relationship.

In interviews, members of this loose class displayed strikingly favorable attitudes toward pirated goods. Several called piracy their "rescue" or "salvation." What they typically meant was that piracy provided their only access to the world of non-blockbuster media goods—independent music, art-house films, and much Western media. Such access is not a luxury for members of this group, but in many cases the basis of their professional activities as musicians, writers, editors, and producers. Piracy—not the licit market—enables them to participate in the international cultural arena. Consequently, it is also the condition of their survival and renewal as a professional class. As one St. Petersburg film critic and college teacher explained:

> Libraries are so impoverished. I cannot find anything reasonably recent in them—anything that came out after 1985. And if I only watched films released in our movie

> theatres, I would have to quit my job. I would not know what to write about! Thanks to pirates, I can download books I need. And what would magazines cover if people like me couldn't see movies that I know get released over there?

Such views are commonplace in Russia and reinforce a basic finding of this report: pirate distribution plays an important role not only in relation to access and consumption in the media economy, but also production. Below the top income strata in Russia and other emerging markets, the globalization of media culture passes largely through pirated goods.

Law and Enforcement

For several years after the demise of the Soviet Union in 1991, authorities worked to build the legal institutions considered necessary for a modern market economy, including the first Western-style intellectual property laws. The enactment of the laws On the Legal Protection of Computer Software and Information (1992) and On Author's Right and Neighboring Rights (1993) culminated several years of work initiated prior to the transition on adapting European IP norms to the Russian context. Consistent with most interpretations of the Berne Convention, copyright in the new law was described as a private right, with provisions for criminal penalties limited to cases of commercial infringement. Criminal provisions were also written into the Statute on Programs Protection, covering the illegal commercial copying of software. Through 1997, the older Criminal Code provided for up to two years of forced labor and/or a fine in such cases, but the statute was very rarely applied (Golavonov 2008).

After 1992, responsibility for IP enforcement was assigned to the new Russian police agencies, including the MVD (the Ministry of the Interior) and the FSB (the Federal Security Bureau). A variety of non-governmental anti-piracy organizations also soon emerged to ensure that foreign (and over time, domestic) rights-holder interests played a role in guiding enforcement efforts.

The new legal institutions—and law enforcement in general—were nonetheless very weak in this period. Diminished financing and dwindling ranks left the police internally disorganized and short of basic resources. The social and economic turmoil occasioned by the rapid, disruptive transition from communism sent rates of violent crime skyrocketing and allowed for the emergence of powerful organized-crime organizations that co-opted law enforcement and operated with general impunity, especially in regard to non-violent "property crimes." Although the IIPA and other industry groups complained loudly about piracy throughout the 1990s, and particularly about the ineffectiveness of Russian law enforcement, these complaints found little political traction in a context of wider problems of public order and weakness of

the rule of law.[28]

The consolidation of a new legal, civil, and economic order did not happen overnight and suffered notable setbacks, including a major economic crisis in 1998. The process of revision of the legal foundations of the new Russian state continued through the early 2000s. With respect to IP policy, an important new factor was the emergence of a domestic IP lobby, built on the recovering film industry and the emerging software industry and closely integrated with and advised by Western companies. This lobby began to push for stronger enforcement efforts and an end to the impunity of pirate activity.

The new enforcement advocates pushed for changes to law, law enforcement, and judicial process. Lawyers who represented plaintiffs in piracy suits in the 1995–2000 period, in particular, had had overwhelmingly negative experiences with the courts and strongly favored efforts to streamline police and court procedures. The lack of coordination among law enforcement agencies was also a major hindrance. Cases were often split among several agencies and frequently slowed or ground to a halt when those agencies could not effectively coordinate the different stages of investigations. The penalties at the end of the process were rarely dissuasive and generally thought to be futile. A common saying among lawyers and prosecutors at the time was that "one piracy case equals three unsolved murders"—a reference to the waste of material and administrative resources associated with copyright infringement cases. For much of the legal community, strengthening the laws against piracy was a pragmatic solution to the wider set of inefficiencies produced by IP laws. For law enforcement, which rarely viewed IP cases as a high priority, the streamlining of case procedures promised to free them to do more of the other things they considered important.

High-level meetings between government and industry were held in 2001 and 2002 and led to the creation of an interagency commission devoted to coordinating IP policy and enforcement efforts.[29] The first major legislative reform took place in 2003, with the amendment of Article 146 of the Criminal Code. The revised Article 146 granted police ex officio powers to launch investigations and make arrests, sped up criminal prosecution, and increased the penalties and other remedies available under the law. This effort, in turn, paved the way for the development of sweeping new IP legislation, known as Part IV of the Civil Code.

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28 Court statistics indicate that charges against pirate distributors and vendors were nonetheless filed with some frequency in the period, often for violations of fair competition rather than piracy. Few of these cases went to trial, however, and industry actors, in general, were slow to make use of the civil remedies available in Russian law. The first civil complaint for software piracy, filed by the software company 1C against another company, Nais, went to trial in 1995 and led to the first successful sentences against software "pirates." The Bulgarian case, described earlier in this chapter, went to trial in 1997 (Vitaliev 1996).

29 The commission was chaired initially by Prime Ministers Kasyanov and Fradkov and later by future president Dmitry Medvedev, whose main interest was the development of Russia's IT sector.

Part IV was intended to unify Russian IP law and bring it into full compliance with international IP agreements, including the Berne Convention (in anticipation of WTO accession) and the World Intellectual Property Organization's Internet Treaties. It was also intended to solve a number of long-standing problems in the IP rights arena, such as the chaotic situation in collective rights management. Although the end result achieved many of these goals, not everything went as planned. When a draft bill emerged in 2006, it was widely criticized on both form and substance by industry stakeholders, local IP practitioners, and foreign government officials. The omnibus approach was controversial—viewed as both hard to implement and hard to change. Industry stakeholders also resisted what they viewed as steps back from TRIPS (Agreement on Trade-Related Aspects of Intellectual Property Rights) and TRIPS+ standards, particularly in regard to private copying, secondary liability, and technical protection measures in the digital environment, on which the bill was vague or silent.[30]

When it became clear that rights-holder groups could not kill the bill, they mobilized to change it. Several rounds of debate and revision followed, with the final compromise mostly ratifying the strong interpretations of TRIPS promoted by rights-holder groups. Part IV entered into force on January 1, 2008, superseding all previous law governing IP protection. Elements of the legislation are still being implemented, including the 2010 passage of a 1% levy on blank media and audiovisual equipment as a means of counterbalancing the law's relatively broad allowance for private copies.[31]

Russian efforts to join the World Trade Organization played an important role in the evolution of these IP reforms. WTO rules require that prospective members secure the agreement of major trading partners prior to entry—a requirement that gave the United States a de facto veto over Russian admission.[32] As Russian economic and political stability appeared to bring prospects for admission closer, pressure grew for stronger cooperation on enforcement.

In 2006, following several rounds of talks about trade and IP protection, the United States and Russia signed a Bilateral Market Access Agreement that focused on expanding Russian enforcement efforts. In the wake of the agreement, the government launched the major crackdown on piracy described earlier in this chapter. The Duma also raised penalties for piracy, making damages greater than 250,000 rubles ($10,000) punishable by up to six years in prison. Although Part IV says nothing about how to establish damages, Russian courts have followed the industry practice of using retail prices to value pirated goods, thereby expanding the range of offenses subject to the highest penalties.

30 On these changes and the broader arc of IP reform in Russia, see Mamlyuk (2010), Budylin and Osipova (2007), and Golavonov (2008).

31 Among other things, the measure will pour an estimated $100 million per year into yet another opaque collective rights management organization, called the Russian Union of Rightsholders, led by film-maker Nikita Mikhalkov (Russian Law Online 2010).

32 It was widely expected that WTO member-state Georgia would be the stalking horse for the actual veto, with support from the United States and probably the European Union.

But by most accounts, this momentum was not sustained. Since 2008, Russian enthusiasm for WTO accession has faded—and with it much of the incentive to implement additional US requirements on enforcement. From the perspective of the Russian government, dialogue with the United States involved a continuously shifting set of goalposts, with agreement to one set of demands only producing more stringent demands. Lack of progress on issues unrelated to copyright, such as Russian requests to the United States to repeal the Jackson-Vanick Amendment (a Cold War provision linking tariffs on Soviet-produced goods to emigration policy), created additional sources of tension.

Plans for further changes to Part IV of the Civil Code slowed dramatically in this context, with little movement on the TRIPS+ enforcement standards demanded by the USTR and international rights-holder groups. The absence of clear provisions for secondary liability for Internet service providers (and other web-based services) in cases of online infringement has been one of the touchstones of this debate. Although Russia officially acceded to the WIPO Internet Treaties in 2009, the emergence of a strong Russian ISP lobby in the past few years and the apparent reluctance of the administration to undertake a separate law on Internet regulation has kept this issue off the legislative agenda. The adoption of US-style "notice and takedown" procedures for infringing online content, in particular, remains unlikely for the foreseeable future.

Governmental Actors

Within the executive branch, four agencies have primary responsibility for IP enforcement: the Ministry of the Interior (MVD), the Prosecutor's Office (Prokuratura),[33] the Federal Security Bureau (FSB), and the Federal Customs Service (FTS). Each has its own investigative functions and the right to initiate criminal proceedings for copyright infringement, and each now conducts investigations ex officio—without the traditional need for a complaint filed by the rights holder(s). Prior to 2006, the MVD played a relatively minor role in the investigation of copyright infringement. It was considered a weak and easily corrupted organization, with limited experience in investigating IP crimes. With the amendment of Article 151 of the Criminal Code in 2006, both the MVD and the Prosecutor's Office became more central and active in enforcement efforts. By most accounts, the MVD's weaknesses in enforcement have been addressed or at least minimized through collaboration with anti-piracy organizations, which now guide and advise its operations.

The MVD is itself composed of many individual departments, each specializing in a different domain of criminal activity and type of enforcement. The OBEP (the Department of Economic Crimes) targets pirate production and distribution networks. Department K, the MVD's computer crime unit, specializes in Internet crime and, in theory, bears responsibility for prosecuting copyright violations on the Internet—though in practice such action has been

33 Roughly speaking, the Prokuratura in Russia combines functions that in the United States are assigned to the Office of the Attorney General, Congressional investigating committees, grand juries, and public prosecutors.

infrequent. The Department of Public Safety (a.k.a. the Militia) has jurisdiction over street vendors, including the trade in pirated discs.

The Federal Security Bureau has plays a variety of roles in IP protection efforts, initially due to its jurisdiction in contraband cases, but more recently under the pretext that the unregulated financial flows associated with piracy represent a threat to national security (a standard that would include most Russian businesses if applied consistently). In practice, it also acts as an occasional check on the other agencies and has prosecuted cases of corruption in the MVD.

The role of Customs in copyright enforcement has declined significantly since the 1990s, when smuggling of pirated optical discs into Russia was widespread. Pirated discs, in this earlier period, came principally from former members of the Soviet bloc—especially Bulgaria and the Ukraine. Once optical disc manufacturing technology became less capital intensive and more mobile, a local pirate manufacturing base developed that obviated the need for most high-risk smuggling operations. With the decline in this form of physical distribution, Customs is now preoccupied with other types of illegal and counterfeit smuggled goods, including pharmaceuticals, textiles, electronics, and industrial products.

Other agencies play more specialized or occasional roles. The Ministry of Culture and the Russian Cultural Protection Agency together license and administer the activities of the collective rights groups and have been involved in the controversies surrounding AllofMP3 and now the RAO. The Federal Anti-Monopoly Bureau plays a periodic enforcement role when a case turns on "unfair competition" or related anti-competitive business practices. The Ministry of Mass Communication has responsibility for Internet regulation, including laws governing e-commerce and the liability of ISPs, hosting services, and other services for infringement. It also licenses optical disc plants. Other ministries and organizations participate in more specific contexts, such as the Ministry of Economic Development, which is negotiating Russia's entry to the WTO and bears responsibility for Russian compliance with international IP norms.

Non-governmental Actors

Numerous non-governmental organizations also take part in enforcement efforts, but six are preeminent in this area: the Russian Anti-Piracy Organization (RAPO), the Nonprofit Partnership of Distributors (NPD), the Nonprofit Partnership of Software Suppliers (NP PPP), the National Federation of Phonogram Producers (NFPP), the local affiliate of the BSA, and the local branch of the IFPI. These organizations specialize in different areas of enforcement: the RAPO oversees film and video compliance; the NFPP, the NPD, and the IFPI handle sound recordings and music; and the NP PPP and the BSA monitor the distribution and use of computer software.

The RAPO was created in 1997 by US studios and film distributors seeking better representation of their interests in Russia. American studios continue to provide the RAPO's core funding, although Russian films co-produced with US studios are also covered through the organization. In addition to Moscow and St. Petersburg, the RAPO has offices and

representatives in a number of provincial cities, as well as its own investigative staff, which works closely with the state police. Until 2004, these investigative networks provided the basis for the MPAA's "supply-side" estimates of pirated disc sales in Russia, which hovered between 80% and 90% of the total market throughout the late 1990s and early 2000s.[34] In recent years, the RAPO has focused on investigations targeting large warehouses and optical disc manufacturing, but several informants described a new shift toward disc sales and—inevitably—Internet monitoring.

The most influential industry group is the NP PPP, which represents major domestic and international software companies, including Microsoft, Adobe, Borland, Symantec, and Autodesk. This international membership substantially overlaps with that of the BSA, leading to many shared interests. Unlike the BSA, the organization also represents virtually all the domestic software suppliers—a constituency that gives NP PPP considerable access to government officials. As a result, the NP PPP is not perceived only as a representative of foreign technology interests but also of the growing domestic software industry and, consequently, as a credible voice for domestic business interests.

The NPD is similar in structure to the NP PPP but focused on the music market. Founded in 2003, it coordinates lobbying and enforcement efforts for the eight largest music distributors in Russia. The NFPP is an IFPI-sponsored competitor and maintains close relationships with international organizations and labels.

Despite efforts in the past decade to routinize coordination and cooperation, relations between law enforcement and industry are complicated. Interests in the enforcement area have become too complex and diverse for simple implementation of industry directives of the kind favored by the IIPA and the BSA. In our research, representatives on both sides of these partnerships characterized the relationships as "cautious." Industry groups are routinely dissatisfied with the scale and effectiveness of police efforts. The RAPO has issued numerous complaints about the unwillingness of local police to raid businesses identified as pirates. NPD representatives described how local precincts offer protection—or "roofs" in Russian argot—to markets or retailers for a modest fee ($300–$500) and how regional representatives to the Duma have blocked NPD efforts to mobilize police to raid markets where they have discovered illegal sales. By the same token, when local businesses feel harassed by aggressive enforcement tactics, they have become much quicker to involve local political authorities and to pursue appeals within the industry groups.

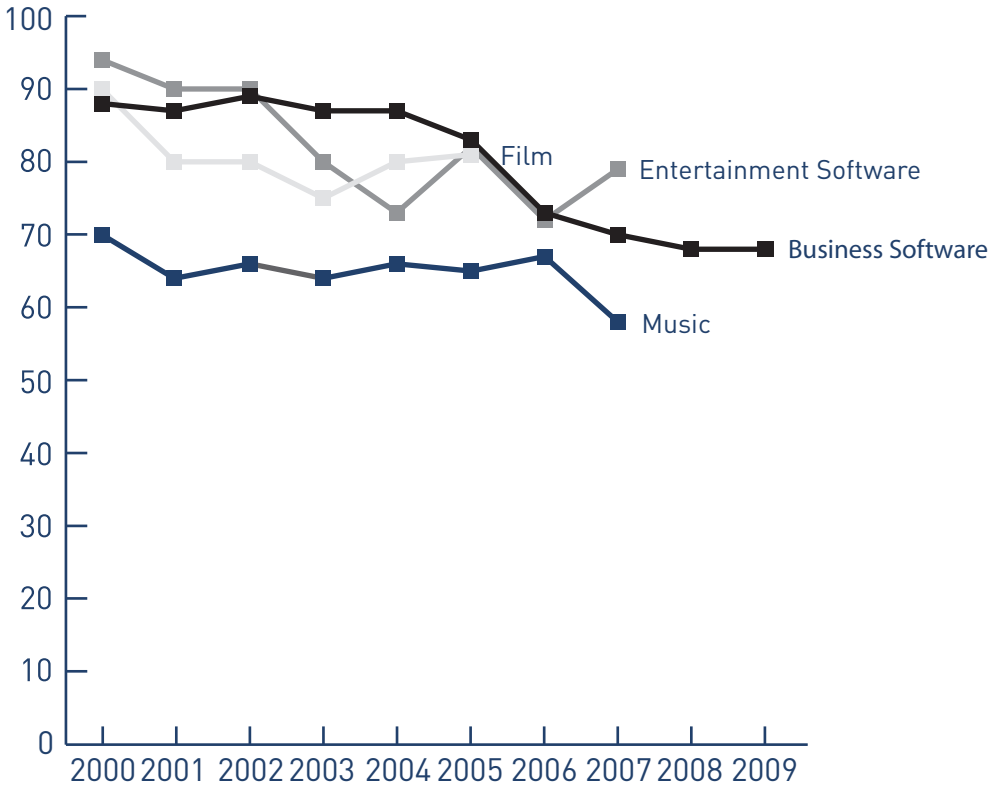
The Effectiveness of Enforcement

There is considerable debate about the effectiveness of IP enforcement efforts in Russia, especially in the wake of the 2006–7 crackdown. Without question, the crackdown hurt

34 In 2005, the MPAA switched to a consumer-survey method, which estimated the rate of piracy at 81% (MPAA 2005). The MPAA has not conducted a follow-up study.

the more exposed categories of manufacturers, distributors, and retailers and produced a reconfiguration of production and distribution—centralizing the former and breaking up the latter into less formalized channels. Industry reported measurable drop-offs in piracy in the software and music categories in 2007–8. The RAPO, in particular, claimed a 40% fall in DVD piracy in the major St. Petersburg and Moscow street markets, where enforcement actions were concentrated.[35]

Figure 4.1 Estimated Share of Pirated Products in Russian Markets, 2000–9



Source: Authors based on IIPA data, 2001-2010.

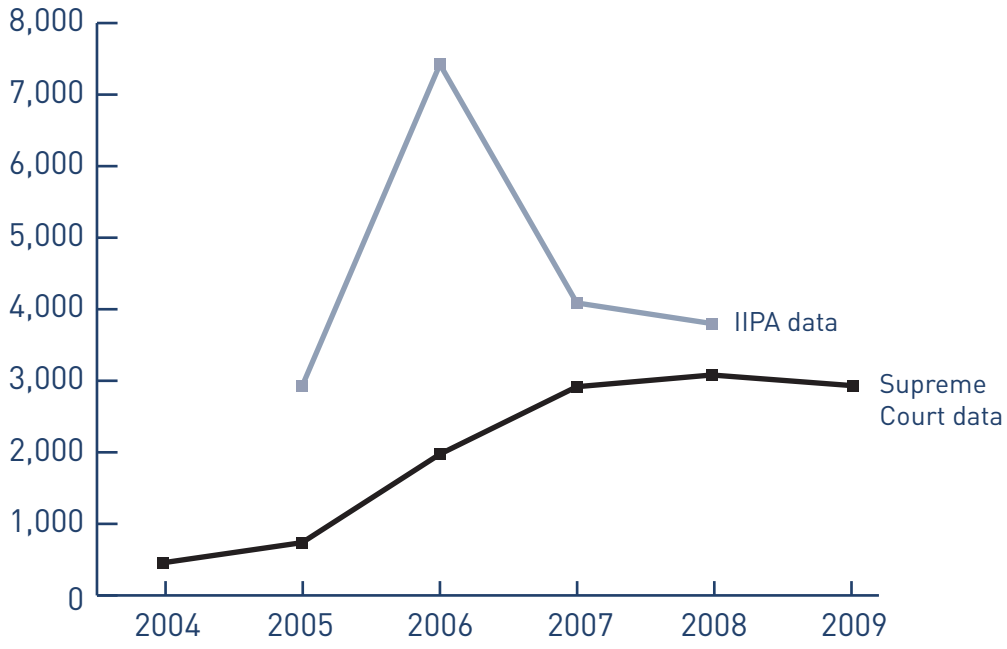
These numbers fit within the broader industry account of modest decline in the rates of piracy in the Russian market (see figure 4.1). Policy change and stepped-up police efforts are central to this account, but organizational changes within law enforcement are also commonly credited. Despite ongoing tensions, many of the enforcement personnel we interviewed testified to the improvement of cooperation between industry and law enforcement and to improvement, in particular, in the skills of investigators and prosecutors. As an NP PPP representative observed: "We learned how to successfully combat piracy in its traditional form," where traditional refers to the optical disc retail trade.

35 Interview with RAPO staff.

In Russia, as in other countries, the effectiveness of enforcement tends to be measured in terms of the scale of street operations, seizures, and resulting penalties or convictions. As in other countries, this practice has been lopsided, with very large numbers of raids and seizures producing a much smaller collection of suspended sentences, fines, and occasional prison terms. Although the IIPA and other rights-holder groups have complained vociferously about the poor record of the courts in Russia, we argue throughout this report that this is not a defect of the national enforcement regime, strictly speaking, but rather the global norm, in which raids scale much more easily than due process and in which courts have remained relatively indifferent to the view that street piracy, especially, constitutes a serious economic crime.

Although this was clearly the case in Russia through 2005, the crackdown in 2006–7 inaugurated a higher level of enforcement and judicial activism. Raids, arrests, and criminal charges increased dramatically, drawing on the streamlined evidentiary and court procedures implemented in 2003. The Russian Supreme Court, which tracks convictions under different articles, reported a sharp increase in criminal copyright convictions under Article 146, from 429 in 2004 to 2,740 by 2007, with numbers holding roughly steady since then. The IIPA, it is worth noting, misreports this data, appearing to conflate different data sets for reported crimes and individuals charged rather than actual convictions (see figure 4.2). This would be a minor point except that the IIPA uses it to overemphasize the magnitude both of the crackdown and of the alleged drop-off in Russian enforcement after 2007—warning repeatedly against the "recent trend of diminished enforcement activity" (IIPA 2010).

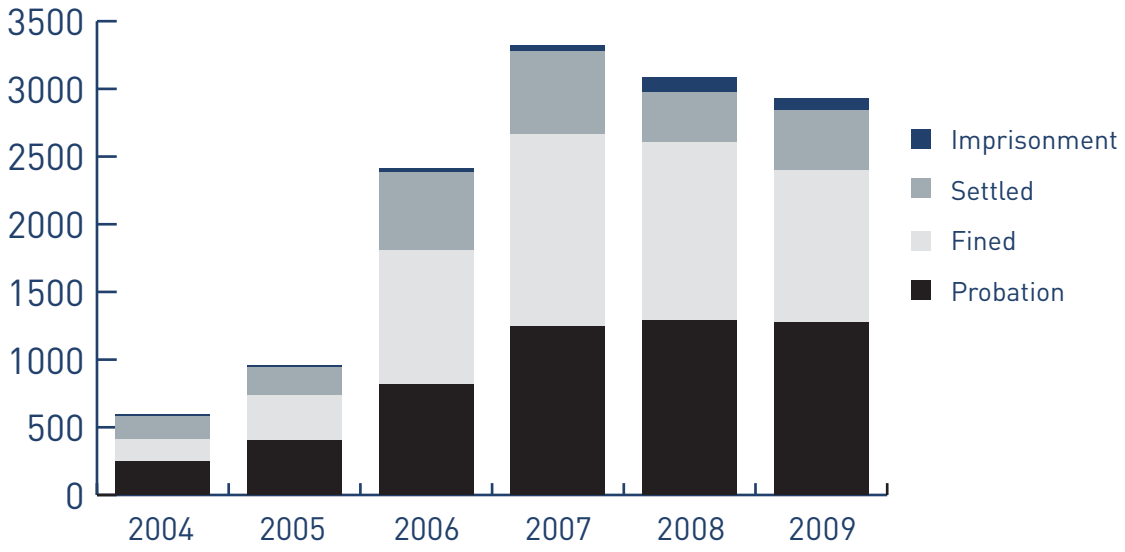
Figure 4.2 Criminal Copyright Convictions in Russia, 2004–9



Source: Authors based on IIPA (2006-2010) and Russian Supreme Court data.

Nonetheless, the crackdown was intense. A seven-month campaign in 2007 netted some 4,300 copyright violations discovered through raids, with reportedly 2,000 persons charged and 2 billion rubles ($80 million) recovered through fines and other forms of compensation (Levashov 2007). In the course of a single week-long national police sweep during the campaign, the Ministry of the Interior reported 29,670 "actions"—a fairly astonishing number that produced only 73 criminal cases. Despite the new status of most acts of street and retail piracy as "serious crimes," nearly all these convictions resulted in suspended sentences or small fines (see figure 4.3).

Figure 4.3 Russia: Number and Types of Sentences, 2004–8



Source: Authors based on Russian Supreme Court data.

What the crackdown meant for the wider prevalence of pirated goods is less clear. Prior to 2007, estimated losses in film and entertainment software showed remarkable—and even implausible—stability, given the dramatic increases in the installed base of DVD players and computers. MPAA losses were pegged at $250 million between 1999 and 2002 and increased only slightly to $266 million by 2005. The ESA reported $240 million in entertainment software losses in 1998 and $282 million in 2006.[36]

Only the RIAA and the BSA reported sharp upward trends in losses in the period. According to the RIAA, music and sound-recording losses to US rights holders tripled, from $170 million in 1998 to a peak of $475 million in 2005. The BSA is a special case: BSA estimates for business software losses fell throughout the late 1990s and early 2000s, dropping from $196 million in 1998 to $93 million in 2002. In 2003, however, the BSA expanded the range of software it

36 For a detailed account of industry reporting, see chapter 1.

includes in its studies to cover Microsoft Windows and a variety of consumer products and games. This change reset the baseline for losses, producing a claim of $1.1 billion lost in 2004. Estimated losses then climbed steadily, reaching $4.2 billion by 2008.

By the time of the crackdown in 2006–7, only the BSA and the RIAA were compiling new annual piracy numbers in Russia.[37] In 2007, both reported dips in absolute losses and estimated rates of piracy. The RIAA's findings took place within a largely static market for CDs in Russia, which has averaged $200–230 million per year at wholesale since 2003 (IFPI 2009).[38] The BSA's estimates were made against the backdrop of rapid 30%–40% annual growth in the Russian software market.

Given the pressure on retailers and the focus on institutional compliance, evidence for declining piracy in some sectors of the software market is relatively strong. The BSA's reports are loosely corroborated, for example, by Microsoft's survey of software retailers, which found in 2010 that only 25% sold pirated software—a rate that Microsoft represented as a clear sign of progress (Microsoft Russia 2010). When the software association NP PPP surveyed its 281 institutional members in 2008, 40% perceived a decline in the illicit retail sector represented by small businesses, street vendors, and subway vendors. A decrease in "pre-installment" of pirated operating systems was observed by 45%, with most of the rest citing "no change." When asked about Internet piracy, 44% of members signaled "no change"—a surprising number given the frequency of reports of the growth of Internet piracy.[39] In our view, the declining BSA numbers describe a bifurcated market, in which negotiated volume licenses produce higher rates of compliance among large institutional actors, while consumers and small businesses continue to pirate at very high levels due to the lack of low-cost retail alternatives.

Evidence for change in other markets is more equivocal. The Russian Guild for Development of the Audio and Video Trade—an organization that includes street vendors and almost certainly pirate vendors—estimated that the rate of pirated goods in Russian media markets was stable between 2006 and 2009. In spite of the recent economic crisis, the average retail price for non-licensed CDs and DVDs has remained roughly the same—between 100 and 150 rubles—suggesting no significant change in supply.

Some sectors also have financial incentives to overestimate piracy, complicating evaluations of enforcement. According to one informant, the padding of both box office numbers and piracy estimates is common in the Russian film industry as a strategy for boosting the perceived popularity of films. Such estimates, which the informant described as routinely inflated by $1–1.5 million at the box office, create leverage for studios as they negotiate over subsequent DVD and home video release rights, as well as for further rounds of investment. When film

37 The MPAA conducted its most recent survey in 2005, the ESA in 2006.

38 With the exception of a banner year in 2004, according to the IFPI. Russian reporting of record sales has always been considered unreliable.

39 The remainder were roughly equally divided between "increase," "decrease," and "no basis for making the judgment." From an unpublished NP PPP study shared with the researchers.

executives talk about the impact of pirate distribution on new films, the rule of thumb is to cite a 20%–25% estimated loss in box office receipts. Thus the director general of the RAPO, Konstantin Zamchenkov, estimated that the Russian blockbuster *The Irony of Fate 2* lost $10 million when high-quality copies became available shortly after its release (overall, the film made $50 million). Twentieth Century Fox estimated losses to piracy for the same film at $12 million (Vershinen 2008). The basis for these estimates is unclear. In a business with a 10:1 failure ratio, no one—including the studios—understands the alchemy of hits or can accurately forecast results. For nearly a decade, all new films have been pirated within a few days of the initial theatrical release, if not earlier. Whatever the impact on specific films, this phenomenon has not prevented Russian box office receipts from growing over 300% between 2004 and 2008.

For our part, the focus on indicators of success in and around the enforcement effort risks missing the larger point: with a partial exception for the institutional software market, piracy remains ubiquitous in Russia. We see no evidence that this situation has been altered in any significant way by either the changes in law or the crackdown on retail. None of our focus group respondents expressed any difficulty acquiring pirated goods, and our street surveys, conducted in 2008 and 2009—revealed ample and generally undisguised opportunities to purchase discs. Moreover, we see little evidence that industry methods can reliably track small year-to-year changes in the wider prevalence of pirated goods—especially at the consumer level. Industry research methods—including the comparatively solid BSA rates model—introduce too many points of uncertainty, from an inability to measure the scale of digital distribution, to conflicting estimates of the size of licit retail markets. Consumer surveys allow measurement across the different forms and modes of piracy but introduce survey and self-reporting biases when asking consumers about illegal behavior. Because these surveys and underlying data are not made public, their results cannot be evaluated or, in our view, trusted.

Most enforcement personnel, in our experience, are aware of these limitations and do not greatly trouble themselves about such margins of error. Several indicated that slight reported increases or decreases were shaped as much by perceptions of the enforcement effort and the politics around it as by the situation on the ground. Given industry and Russian government interest in managing perceptions of piracy, such skepticism seems warranted.

Selective Enforcement

Debates about effectiveness also tend to obscure the other side of enforcement in Russia: its capture by politically connected actors. Rather than serving (or failing) all parts of the copyright sector equally, enforcement is a scarce resource that confers competitive advantages in the marketplace. Some of these advantages are relatively subtle, as when large firms enjoy more influence with police or prosecutors than small firms. One company's protection, in such contexts, is often another's exposure. But others are cruder and run the gamut from commissioned prosecutions and harassment of competitors to more elaborate forms of extortion and corporate raiding (*reiderstvo*). Such problems are by no means limited to IP rights

in Russia, but the mix of corruptible institutions, near-universal legal jeopardy, and scarce actual enforcement creates fertile ground for them.[40]

Much of the practice of capture is public and even celebrated in the form of partnerships between rights-holder groups and law enforcement. Here, domestic interests often trump international ones. Our limited data suggests that national actors generally have greater capacity to mobilize the state than the multinationals. Among the 207 indictments for software piracy initiated by the NP PPP between 2002 and 2008, for example, some 126 were on behalf of the Moscow-based software company and retailer 1C, predominantly in relation to infringement of 1C's widely used accounting suite. Microsoft, in the same period, was the plaintiff in 21 cases. The Russian software companies Konsul'tant and Garant-Service (equivalent to the American legal-research platforms LexisNexis and Westlaw) appear third and fourth on the list, with 9 cases each.

Several domestic film companies have also been successful in mobilizing the police to suppress the pirate DVD distribution of particular films prior to their theatrical release. Such was the case, notably, for the Russian hits *Night Watch* (2004), *Day Watch* (2006), and *The Irony of Fate 2* (2007). Not every film benefits from special police protection. A representative of Channel One, the Russian TV broadcasting corporation that distributed *The Irony of Fate 2,* said in regard to street piracy:

> We simply scared them off. We asked the OBEP to pass the word that our reaction [to pirated copies] will be harsh . . . Our access to "administrative resources" undoubtedly helped. They would be unlikely to listen to anyone smaller than us. (Vershinin 2008)

"Administrative resources," in Russian business parlance, means connections to municipal, regional, or in this case, federal officials. Predictably, such resources are not evenly distributed but track with—and reinforce—influence and size. Large companies, such as Mosfilm or The First, have much more leverage with officials than smaller companies, which translates into better protection for their films.

There are also more aggressive uses of enforcement. Among the St. Petersburg retailers interviewed for this report, the OKO-505 case was a well-known example of anti-piracy enforcement as a form of corporate raiding. OKO ("the eye") was a St. Petersburg-based collective rights management organization established by Dmitry Mikhalchenko, a powerful local businessman involved in the privatization and redevelopment of municipal property. Structured as a public-private partnership, OKO enjoyed the support of the governor and had close ties to the regional police. In 2006, OKO initiated raids against 505, one of the most

40 Firestone (2010) describes the wide variety of abuses that have become common in such contexts, including the practice of "intellectual property squatting," or fraudulent registering of trademarks and patents in order to set up a civil suit or criminal charges against the rights holder. Astafiev (2009) notes that the MVD initiated 350 investigations of corporate raiding in 2005. See also Rigi (2010).

The Total Checkup

The director of the St. Petersburg branch of a Moscow-based insurance company described an MVD-directed police raid in summer 2008, triggered by a complaint by a frustrated client who had had an insurance claim denied. The complaint led to what in Russia is called a "total checkup," in which police investigate all aspects of a business's activity. When a review of the company's accounting practices turned up no inconsistencies, police asked company representatives to produce evidence that software on the office computers was licensed. Because the office's equipment was purchased and serviced from Moscow, no such documentation was available onsite. The police confiscated the computers until proof of the licensing status of their copies of Microsoft Windows could be acquired from their Moscow headquarters. No charges were filed during the investigation; nor—according to the office director—was the seizure of the equipment accompanied by proper paperwork. These procedural problems eventually led to the closure of the investigation without charges. But for two weeks the company was paralyzed and could not provide services to its clients. Beyond the initial disruption, the experience has also affected the firm's business practices: the company is now much more careful to avoid conflicts with clients.

popular local music/video retail chains. All fifteen of 505's shops were closed for three days, and most of its stock was confiscated. The public-relations director of 505, Alena Kondrikova, acknowledged that a substantial portion of the media sold at 505 was unlicensed, but it was widely understood that the same was true of other large retail chains such as Titanik, Desyatka, and Aisberg, which remained in business.

The logic of OKO's selective targeting began to emerge in press reports and online forums. OKO pressured music and movie retailers to become paid members of the organization, with the strong implication that this would exempt their operations from police harassment. Some retailers consented; others, like 505, did not. On this basis, 505 filed a complaint with the Antitrust Service (FAS), but as with many raiding investigations the case was not pursued and 505 eventually went out of business (Russian Antitrust Service 2006).

Business Community Pushback

The ramp up of investigations and raids during 2006–7 amplified these problems and produced a powerful reaction in the Russian business community. As a growing number of businesses were disrupted by police raids, software-licensing investigations, and other forms of pressure, IP enforcement began to be identified with police corruption and business takeovers rather than the protection of rights. Shakedowns were common in these contexts, and even under the best of circumstances, police raids could paralyze businesses for days before a case was cleared up or dropped. Pressure to turn in "adequate" statistics on enforcement led to spikes of

activity during enforcement reporting periods, with licensed goods—according to enforcement sources—representing up to 30% of seizures.

By 2007, police overreach had become a regular focus of local and federal-level economic summits and soon produced a revised approach to enforcement. Now president, Dmitri Medvedev took the side of harassed business owners, stating, in December 2008, that businesses should not be "terrorized" by the police. In 2009, Vladimir Putin, now prime minister, claimed that most police inspections of businesses were commercially motivated and had "no obvious justification" (Firestone 2010; Beroev 2009). Pushback had become the government position: in early 2009, the Duma passed a new law limiting police inspections of businesses to once every three years.

Not surprisingly, rights-holder groups reacted very unfavorably to these developments, with the IIPA in particular describing the new restrictions as a retreat from the 2006 bilateral agreement with the United States. Recent government investigations of Microsoft and other leading international companies may be further evidence of a divergence of foreign IP interests from the perceived interests of the Russian business community. Although it is hard to attribute coordinated intent to the range of actors operating within this space, the Russian government appears increasingly comfortable with a strong and self-interested position on behalf of its business community. As in other contexts, enforcement policy needs to be seen as a product of this balance of forces.

The Ponosov Case

The politics of selective enforcement, software piracy, and Russian technology policy came together unexpectedly in May 2006, when a police raid on a primary school in rural Perm found that twelve of the school's twenty new computers were operating with unlicensed copies of Microsoft Windows. In November 2006, these findings were transferred to the local court, and the principal of the school, Aleksandr Ponosov, was arrested on suspicion of piracy. Initially, Ponosov was charged with approximately $10,000 in damages to Microsoft—a sum that also exposed him to up to five years in prison. Ponosov pleaded not guilty.

Between 2006 and 2008, the case underwent seven hearings and appeals, demonstrating in the process the difficulty of reconciling the harsh terms of the law with the utterly commonplace use of pirated software. Initially, the presiding judge found Ponosov guilty of infringement but rejected the damage claims. Although Ponosov was set free without penalty, he appealed the ruling. A subsequent hearing imposed a fine of $380 on the vendor who sold the computers—though the question of where the software had been installed remained a point of contention. At a further hearing in May 2007, Ponosov was pronounced guilty and fined 5,000 rubles ($190). Again, Ponosov appealed—both to the regional court and to the Russian Supreme Court. The regional court turned down the appeal, but the Supreme Court recognized it as valid and sent the case back for retrial. This step initiated a series of legal victories for Ponosov. In December 2008, he was pronounced not guilty and awarded legal costs. In July 2009, he was awarded compensation for defamation.

In the course of the prosecution, Ponosov attracted some remarkable public support. In February 2007, former president Mikhail Gorbachev and Duma deputy Aleksandr Lebed sent an open letter to Bill Gates calling on him to intervene to get the charges dropped. Microsoft, for its part, saw a public-relations disaster in the making, and its Russia office publicly disavowed the actions of the regional Prosecutor's Office. Microsoft's intervention, however, was both late and ineffective. Because the case was being prosecuted as a criminal matter, not a civil one, the injured party could not withdraw the charges. The prosecutors dug in.

The number of Ponosov supporters continued to grow. The Federal Agency on Press and Mass Communications of Russia (Rospechat) offered to pay the claimed damages, asserting that "it is implausible to consider a teacher in a rural middle school a major media pirate in our country" (NTV 2007). The Minister of Education of the Perm region also weighed in on Ponosov's side, as did Posonov's students, who picketed the court building during the hearings. Support also came from then president Vladimir Putin, who, when asked about the case at a February 2007 press conference, offered that prosecuting all pirates "under the same blanket" was wrong: Ponosov may have been guilty of buying computers with unlicensed software, but "threatening him with prison is complete nonsense, simply ridiculous" (Putin 2007).

Ponosov himself reacted to the experience by becoming a vocal advocate for free software. Together with former Duma deputy Viktor Alksnis, he founded the Center for Free Technology in 2008, which promotes the development and distribution of free software in Russia. Posonov's own school (from which he has retired) now runs Linux.

Ponosov's troubled prosecution brought the ubiquity of unlicensed software in Russian schools (and by extension, in state institutions) into the open and recast it as a policy, rather than an enforcement, issue. Given the level of political involvement in the case, something now had to be done. The Ponosov case had become a catalyst for technology-policy change at the federal level.

The case highlighted not only the problem of an unlicensed governmental sector but also the difficulty of resolving it at the lower levels of the state administration. A national policy for transitioning state offices to licensed software was proposed as a way forward.

Mass retroactive licensing was discussed but quickly dismissed as prohibitively expensive due to the quantity of unlicensed software in use. The government then tried to cut a deal with commercial vendors. Intense lobbying by domestic and international software interests resulted in the creation of the First Aid program, designed to fund software licensing in Russian schools. Initially, the NP PPP, which represented all the major suppliers of software to the Russian market, was to receive a $200 million contract to purchase licensed commercial software for Russian schools. (The budget for open-source solutions under First Aid, announced later, was around $20 million.) Senior Russian officials, including Dmitri Medvedev, began negotiations with major international software companies, including Microsoft and IBM, for discounts on their products. The stated goal was "100% license purity in Russian schools."

But First Aid quickly ran into trouble with the Ministries of Economic Development and Finance over its "high cost." The Russian leadership pivoted again and convened a meeting with

leaders in the Russian IT community—including those working with open-source software—to chart a more economical solution. The new strategy involved a mix of commercial and open-source solutions deployed in three-year pilot programs in three regions of Russia, with plans for expansion into the wider national education system and possibly into other governmental sectors. Pushed by Ponosov and Alksnis, Linux played a role in these programs but not an exclusive one. A wide range of commercial software, including products by Microsoft, Adobe, Corel, and other US firms, were included in the discounted package of software deployed in the pilot programs. Microsoft agreed to include Windows Vista in this package at a 95% discount off the retail price, suggesting the degree of its commitment to the Russian market when open-source alternatives are seriously in play.

The war of maneuver with Microsoft and other vendors continues. In June 2009, the FAS opened an antitrust investigation of Microsoft for its withdrawal of Windows XP from the Russian market—and closed it three months later without filing charges. In March of 2010, Microsoft agreed to provide free copies of Windows 7 to 54,000 Russian schools, with licenses set to expire at the end of 2010. This date also marks the scheduled end of the First Aid program, when license negotiation and the possibility of more widespread open-source adoption will presumably be back on the table.

State Capture

In September 2010, the New York Times published a story on the Russian government's use of software piracy investigations as a means of harassing political activists and journalists (Levy 2010b). The piece establishes a pattern of government raids and criminal charges against opposition actors, going back several years. It also establishes a pattern of complicity by Microsoft's local representatives in these efforts.

As in other cases, raids lead to the seizure of computers, the disruption of work, and a wide array of follow-up criminal charges if unlicensed software is found, including fines and the possibility of long prison terms. Because Microsoft and other software vendors have insisted on using the retail value of software when pursuing criminal charges, a handful of pirated copies can quickly push users into felony territory.

With BSA estimates of piracy in Russia at around 68% of the market—and with the actual rate almost certainly higher in the small-business and nonprofit sector—exposure to felony prosecution is thus the norm in Russia. Complex licensing and arbitrary compliance standards make claims of innocence—such as those advanced by the environmental activist group Baikal in the New York Times story—difficult to establish and dependent on the integrity of the police. In an effort to head off a public-relations fiasco, Microsoft announced a blanket license to activist groups and media outlets in Russia—shielding them from this type of harassment (Levy 2010a).

At one level, of course, these cases have little to do with piracy. Software enforcement is a convenient tool in wider campaigns of political harassment. But the larger matrix of

enforcement in Russia—the sharp criminalization and highly selective enforcement of commonplace behavior—makes abuse inevitable. The blanket-licensing solution sidesteps this wider problem but also sets up Microsoft as an arbiter of civil liberties in Russia. When the blanket license expires in 2012, Microsoft will determine whether the political climate warrants its renewal.

Conclusion

Like other countries documented in this report, Russia is in the midst of a transition from optical disc piracy to digital file piracy, conducted largely but by no means exclusively via the Internet. The consumer infrastructure around optical discs, however, is still more developed than the Internet counterpart, and it will be several years before broadband connections, digital playback and storage devices, and recent-vintage computers supplant the optical disc channel for most Russians. Russia will, in the meantime, continue to face the problems chronic to small media markets dominated by multinational companies: licit market growth will be tied to slowly rising local incomes rather than to rapidly dropping technology prices. As we argue throughout this report, this is a recipe for continued high rates of consumer piracy.

In all the countries examined in this report, price competition and service innovation come primarily from competition among domestically owned media industries. The multinationals, our work suggests, simply do not have the incentives to offer significant price cuts in low- and middle-income markets, for fear that these will impact pricing in their larger, more profitable markets. In the software sector especially, piracy assists this policy by providing the vendors a form of de facto price discrimination that generates positive network effects for commercial products, while locking out "free" open-source alternatives. The Ponosov case suggests the complexity behind this balancing act—as well as the pragmatism of the Russian government in angling for advantageous deals with multinationals. The government's strong stated commitment to open source appears to be just one part of this larger strategy of hedging and dealmaking.

In this context, it seems entirely possible that both licit and illicit media markets will continue to grow in the next years. The software business is still riding the wave of Russian computer adoption and optimizing the tradeoffs between piracy and enforcement. The record business is already heavily promotional in orientation, rather than vested in retail disc sales. And movie exhibition continues to set records, coming off the near total destruction of the industry in the 1990s.

In Russia, these developments raise familiar questions about the future of media business models. As elsewhere, we would expect this future to involve lower-priced, more convenient forms of legal media access that compete with the pirate market. In our view, the ramp up in enforcement does little to encourage this transition and quite a bit, in contrast, to reinforce the high-price, high-piracy status quo. Related problems with the criminalization of infringement

and the arbitrary application of the law are not unique to Russia but are magnified by the weaknesses of Russian regulation and due process protections. In this context, it is hard not to welcome one short-term outcome of the (still largely pirate-driven) digital transition: the crowding out of state-protected piracy. With that problem headed toward obsolescence, Russians can have a more candid conversation about the costs and benefits of piracy and enforcement and the policies needed to achieve wider access to media.

About the Study

This chapter on Russia combines the efforts of two teams of researchers specialized, respectively, in economic-legal issues and the informal economy. The primary research for the report was conducted by Olga Sezneva, Oleg Pachenkov, Irina Olympieva, Anatoly Kozyrev, and Joe Karaganis. Numerous experts and researchers made additional contributions or provided valuable feedback, including Bodó Balázs, Dmitri Pigorev, Igor Pozhitkov, Maria Haigh, Boris Mamyluk, Kathryn Hendley, and William Pomeranz.

Much of the analysis of the street economy, including enforcement, pricing, availability, and consumer practices, is based on fieldwork in St. Petersburg conducted by Sezneva, Pachenkov, and Olympieva in 2008 and 2009. This work was complemented by some twenty interviews of industry lawyers, judges, and legal scholars and representatives of non-governmental and non-commercial organizations involved in enforcement.

Our broad inquiry into consumer attitudes and values drew on this fieldwork and was complemented by three additional components: a March 2009 focus group with heavy users of unlicensed content in St. Petersburg, a late-2008 survey of three hundred DVD consumers in the city of Irkutsk (conducted by colleagues at the Evolution Marketing Center in Irkutsk), and content-analysis of Russian-language media and online forums.

The analysis of industry and organizational structure and the costs and benefits of copyright enforcement drew on primary interviews, secondary literature, and contributions from our economic and industry research partners, especially Anatoly Kozyrev. A wide array of secondary sources contributed short accounts or expert advice on narrower topics, including pricing, selective enforcement, and other issues.

In order to better understand the shift toward online distribution and its particular Russian inflections, we conducted a data crawl of the Russian BitTorrent site Torrents.ru in March 2009, with the assistance of Bodó Balázs and Dmitri Pigorev.

Key institutional partners in this process included the Social Science Research Council in New York and the Center for International Social Research in St. Petersburg.

Access to sources and confidentiality presented challenges throughout our research. Much of our information about pirate networks, their organizational structure, and above all state involvement came from interviews or media reports. Many statements were off the record.

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