

# INTERNATIONAL INTELLECTUAL PROPERTY ALLIANCE

## 2007 SPECIAL 301 REPORT

### CANADA

**Special 301 Recommendation:** IIPA recommends that Canada be elevated to the Special 301 Priority Watch List in 2007.

## **EXECUTIVE SUMMARY**

Canada's long tenure on the USTR Watch List seems to have had no discernible effect on its copyright policy. Almost alone among developed economies in the OECD, Canada has taken no steps toward modernizing its copyright law to meet the new global minimum standards of the WIPO Internet Treaties, which Canada signed a decade ago. Its enforcement record also falls far short of what should be expected of our neighbor and largest trading partner. Pirates have taken advantage of the gaps in Canadian law to make it a leading exporter, both of camcordered masters that feed audio-visual piracy worldwide, and of devices – illegal in most global markets besides Canada – that are intended to circumvent technological protection measures used by the publishers of entertainment software. Canada lacks effective border controls on pirated products, and most of its other enforcement efforts suffer from insufficient resources and a lack of deterrent impact. To underscore U.S. insistence that Canada take action to address the serious piracy problem it has allowed to develop just across our border, and that it bring its outmoded laws up to contemporary international standards, IIPA recommends that Canada be elevated to the Priority Watch List in 2007.

## **Actions Which the Canadian Government Should Take in 2007:**

### **Copyright Law Reform**

- Enact legislation bringing Canada into full compliance with the WIPO "Internet" Treaties (WIPO Copyright Treaty [WCT] and WIPO Performances and Phonograms Treaty [WPPT])
- Create strong legal incentives for Internet Service Providers (ISPs) to cooperate with copyright owners in combating online piracy
- Amend the Copyright Act to clarify the scope of the private copying exception for sound recordings
- Amend the Copyright Act to clarify that illicit file-sharing services are a violation because they authorize infringement
- Amend the Criminal Code to make unauthorized camcording an indictable offense

### **Enforcement**

- Make legislative, regulatory or administrative changes necessary to empower customs officials to make *ex officio* seizures of counterfeit and pirate product at the border
- Increase resources devoted to anti-piracy enforcement both at the border and within Canada

- Direct the RCMP, CBSA, and Crown prosecutors to give high priority to intellectual property rights enforcement, including against retail piracy and imports of pirated products, and to seek imposition of prison sentences for material infringements

<b>CANADA</b>				
<b>Estimated Trade Losses Due to Copyright Piracy</b>				
<b>(in millions of U.S. dollars)</b>				
<b>and Levels of Piracy: 2005-2006<sup>1</sup></b>				
<b>INDUSTRY</b>	<b>2006</b>		<b>2005</b>	
	<b>Loss</b>	<b>Level</b>	<b>Loss</b>	<b>Level</b>
<b>Records &amp; Music</b>	NA	NA	NA	NA
<b>Business Software<sup>2</sup></b>	551.0	34%	491.0	33%
<b>Motion Pictures</b>	NA	NA	118.0	8%
<b>Entertainment Software</b>	NA	NA	NA	NA
<b>Books</b>	NA	NA	NA	NA
<b>TOTALS</b>	<b>551.0</b>		<b>609.0</b>	

## **COPYRIGHT LEGAL REFORM AND RELATED ISSUES**

Canada remains far behind virtually all its peers in the industrialized world with respect to its efforts to bring its copyright laws up to date with the realities of the global digital networked environment. Indeed, even most of the major developing countries have progressed further and faster than Canada in meeting this challenge. Although the new Canadian government that took office in March 2006 expressed its commitment to modernization of Canada's copyright laws, to date it has not even released a draft of legislation.

The globally accepted benchmark for modern copyright legislation can be found in the WIPO "Internet" Treaties, the WIPO Copyright Treaty (WCT) and the WIPO Performances and Phonograms Treaty (WPPT). Although Canada was one of the original signatories to the WCT and WPPT a decade ago, Canadian copyright law remains far out of compliance with the standards set in these treaties. The previous government unveiled legislation (Bill C-60) in 2005 that, while positive in some respects, fell far short of meeting the WCT and WPPT benchmarks. While we continue to urge the current government to jettison the approach taken by Bill C-60, in favor of legislation more consistent with international norms for nations that have already implemented these treaties, the direction Canadian copyright reform will take remains unknown.

When Canada signed the WCT and WPPT a decade ago, it pledged support for treaties that were designed to respond to what were then new technologies. Notably, as a crucial element to foster the healthy development of e-commerce in copyrighted materials, these

<sup>1</sup> The methodology used by IIPA member associations to calculate these estimated piracy levels and losses is described in IIPA's 2007 Special 301 submission at <http://www.iipa.com/pdf/2007spec301methodology.pdf>. For information on the history of Canada under Special 301 review, see Appendix D at <http://www.iipa.com/pdf/2007SPEC301USTRHISTORY.pdf> and Appendix E at <http://www.iipa.com/pdf/2007SPEC301HISTORICALSUMMARY.pdf> of this submission.

<sup>2</sup> BSA's 2006 statistics are preliminary. They represent the U.S. publishers' share of software piracy losses in Canada, and follow the methodology compiled in the Third Annual BSA/IDC Global Software Piracy Study (May 2006), available at <http://www.bsa.org/globalstudy/>. These figures cover, in addition to business applications software, computer applications such as operating systems, consumer applications such as PC gaming, personal finance, and reference software. BSA's 2005 piracy statistics were preliminary at the time of IIPA's February 13, 2006 Special 301 filing; the 2005 data was revised and posted on the IIPA website in September 2006 (see <http://www.iipa.com/statistics.html>), and the 2005 revisions are reflected above.

treaties obligated adhering countries to enact effective legal regimes to protect technological measures used by copyright owners to control access to and copying of their works. While nearly every other OECD country either has met this obligation or is well on the way to doing so, Canadian law remains hopelessly outdated in this area. IIPA urges Canada to fulfill its pledge by enacting laws that deal with technological protection measures (TPMs) in a manner that fully complies with the WCT and WPPT. This means legislation that:

- comprehensively protects TPMs, both in so far as they manage access to copyright works and in their use to prevent unauthorized copying and the exercise of other exclusive rights;
- outlaws trafficking in devices aimed at circumventing TPMs, or providing circumvention services, and defines violations without imposing onerous intent requirements;
- defines exceptions or defenses with care, so as to avoid the creation of a market for circumvention devices or services; and
- provides strong civil and criminal remedies for violations.

Canada's failure to provide legal protection for TPMs is not a mere theoretical lapse: it has already had concrete consequences. In the absence of strong prohibitions to the contrary, Canada now finds itself one of the world's epicenters of the manufacture and export of important categories of tools aimed at circumventing TPMs – so-called "modification chips" and similar devices that enable pirated and counterfeit video games to be played on videogame consoles. Highly organized international crime groups have rushed into the gap left by Canada's outmoded copyright law and now use the country as a springboard from which to undermine legitimate markets in the United States, the United Kingdom, Australia and elsewhere, through the export of circumvention devices. It is long past time for Canada to put into place the legal tools that will enable it to put a stop to this increasing pollution of the markets of its trading partners.

Copyright reform legislation in Canada is also needed to counter the growing problem of Internet piracy. It can best do so by conditioning liability limitations for Internet Service Providers (ISPs) on affirmative cooperation with copyright owners in combating online infringements. As recommended by the Supreme Court of Canada in *SOCAN v. CAIP*, legislation should also provide a true "notice and takedown" system that offers an expeditious means of shutting off access to infringing online activity, rather than confining itself to the mere "notice and notice" regime of Bill C-60. While an obligation for an ISP to forward notices from copyright owners to end-users would be a useful supplement to a system that gives ISPs strong incentives to "take down" infringing materials, it is no substitute for it.

New legislation must also address the scope of the private copying exception for sound recordings. While IIPA hopes that further judicial interpretation of Canada's current law will more clearly establish that the private copying exception applies only to individuals who make copies for their own use, a legislative amendment is also required to clarify that the exception applies only to copies of non-infringing recordings owned by the person who makes the copies. Any broader application of the private copy exception would raise serious questions about Canadian compliance with its WTO TRIPS obligations.

New legislation should also clarify liability under Canadian law for illicit peer-to-peer (P2P) services. In contrast to the international trend, exemplified by successful lawsuits in Australia, Korea, Taiwan and the U.S. against P2P services that were facilitating massive

worldwide infringement, recent Canadian case law on liability for authorizing infringement raises questions as to whether a comparable enterprise would be found liable under Canadian law. The Copyright Act should be amended to enable rights holders to obtain effective remedies against those who in the Internet context knowingly facilitate infringements (such as P2P service providers and distributors of file sharing software who offer services or software knowing that their actions will likely result in infringement), or who encourage, induce or materially contribute to the infringement.<sup>3</sup>

Bill C-60 contained several positive features, notably the specification of an exclusive right of "making available," and a new section banning dissemination or public performance of a copy of a sound recording made under the private copying exception. These should be brought forward in new copyright reform legislation. On the other hand, Bill C-60 also included flawed proposals in the area of educational and library exceptions, such as an ill-defined new exception for use of a work in a "lesson, text or examination" in educational settings, and a provision authorizing interlibrary distribution of digital copies, that would have had a significant detrimental impact on publishers of scientific, technical and medical materials in particular. These should be carefully re-examined. The Canadian government should ensure that any legislative proposals it makes on educational and library exceptions to copyright can pass muster with its existing and anticipated international obligations, and that they provide ample room for market solutions.

Finally, along with reform of Canada's substantive copyright law, legislative changes are necessary, though not alone sufficient, for Canada to begin to remedy its serious deficits in copyright enforcement (discussed in more detail in the next section). Among other critical changes, the Canadian Border Services Agency (CBSA) must be given the independent authority it currently lacks to act *ex officio* against any suspected pirate or counterfeit imports; and unauthorized camcording of films in Canadian theaters must be made an indictable criminal offense through an amendment to Canada's Criminal Code.

## **COPYRIGHT PIRACY AND ENFORCEMENT**

There is no doubt that the piracy problem within Canada is getting worse, not better. Canadian piracy is also a serious problem for markets in other countries, including the U.S. For example, Canada is becoming notorious as one of the world's leading sources for "mod chips" and other videogame circumvention devices, and for the camcorded master copies for digital audio-visual piracy.

Pirate and counterfeit videogame products continue to flow into and out of Canadian territory. Pirate games are manufactured throughout the country, notably in Vancouver/Richmond, Calgary, Toronto/Markham, and Montreal. Much of the pirate product in the market continues to flow in from Asia across Canada's porous borders. Disturbingly, Quebec, Ontario and British Columbia have become havens for the manufacturers and

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<sup>3</sup> Bill C-60 failed to address this problem, and would in fact have exacerbated it, because it would have provided sweeping safe harbors to network service providers without creating any incentives for them to cooperate with copyright owners to deal with copyright infringements that take place in the digital network environment. In particular, it would have immunized service providers against liability even when they had actual knowledge of infringement and the power to restrict or prevent it, until an independent court order was obtained; would also have sheltered P2P file sharing services that contribute to massive infringement; and would have prevented rights holders from even obtaining injunctions against service providers whose services are used to facilitate infringement. Such an approach failed to comply with the mandate of the WIPO Internet Treaties that national law "permit effective action against any act of infringement of rights covered by this Treaty."

distributors of devices that bypass TPMs that entertainment software publishers use to protect their product from piracy. “Mod chips” for videogame consoles such as the Sony PlayStation 2, Microsoft Xbox and Nintendo GameCube are made in Canada, both for domestic consumption and for export to the United States, Europe and parts of southeast Asia. Other devices, such as the “Flash ROM Linker” that enables piracy of games designed for play on the Nintendo console, are assembled in Canada for distribution both domestically and internationally. Burned pirate optical discs are manufactured in “micro-replication facilities,” often located in private residences, and are then distributed either in local retail markets or via Internet websites maintained by the pirates. However, much of the thriving activity in importation, manufacturing and distribution of pirate entertainment software products and circumvention devices appears to be controlled by organized crime rings, such as the Hells Angels in Quebec, and the Big Circle Boys in Ontario and British Columbia.

The problem of unauthorized camcording of films in Canadian theaters is now nearing crisis levels. MPAA analysis of counterfeit copies of recently released movies on DVD seized throughout the world reveals that more than 90 percent can be sourced back to theatrical camcording. As of August 2006, MPAA had documented 179 member company titles that had been stolen in this manner since 2004, providing the source copies for pirate DVDs discovered in the markets of 46 other countries on every inhabited continent. In 2006, 20-25 percent of camcorded masters worldwide were sourced to Canada. Through sophisticated pirate replication and distribution networks, DVDs produced from camcorded masters are on the street literally within hours: for instance, pirate DVDs of *Poseidon* were being sold a mere 13 hours after the film’s theatrical debut in Canada.<sup>4</sup> The number of titles affected is consistently trending upwards, and the problem is national in scope; theaters from Nova Scotia to British Columbia have been identified as sites of unauthorized camcording, although the worst problem is in Montreal.

The estimated piracy rate for business software in Canada of 33% far exceeds that of the U.S. or of most Western European countries. Servers at universities continue to act as digital storage facilities for large quantities of pirate intellectual property, including, games, music and movies. In the United Kingdom and Germany, the number of regular buyers of legal downloads of music now exceeds the number of regular unauthorized file-swappers.<sup>5</sup> In Canada, by contrast, unauthorized file-swapping swamps legal sales of digital music on the order of 100 to 1.<sup>6</sup> According to the OECD, Canada has the highest per capita incidence of unauthorized file-swapping in the world.<sup>7</sup> In short, Internet piracy appears to be on the increase in Canada, aided by the uncertain legal environment and serious shortfalls in enforcement.

These realities point to serious deficiencies in enforcement against piracy. Much of the problem is attributable to the inaction of Canada’s government on law reform. For instance, Canada has become a leading global source of camcorded pirate master copies of films because there is no federal criminal prohibition against unauthorized camcording in movie theaters unless it can be established that it is for commercial purposes. Because of this gap in the law, neither Canada’s federal law enforcement agency (the Royal Canadian Mounted Police [RCMP]) nor local authorities will take action against the practice. Remarkably, one theater owner who sought assistance from law enforcement was told that the only reason the police

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<sup>4</sup> MacDonald, “Pirates of the Canadians,” *Globe & Mail*, Jan. 13, 2007.

<sup>5</sup> International Federation of Phonographic Industries (IFPI), *Digital Music Report 2006* (Jan. 2006), p. 15.

<sup>6</sup> IFPI, *The Recording Industry 2006 Piracy Report* (July 2006), p. 11.

<sup>7</sup> Organization for Economic Cooperation and Development, “Digital Broadband Content: Music,” Dec. 13, 2005, p. 75, <http://www.oecd.org/dataoecd/13/2/34995041.pdf>.

would attend the theater was to arrest the theater owner if he tried either to confiscate the recording equipment or detain the person operating it. Making unauthorized camcording an indictable criminal offense is the indispensable first step toward cracking down on this serious problem.

Similarly, Canada's outmoded copyright law contains no criminal prohibitions on the manufacture or distribution of devices (such as mod chips and the like) whose only plausible use is to circumvent technological protection measures used by copyright owners to fight piracy. Consequently, although both RCMP and local authorities are well aware of the organized criminal groups in Canada who dominate trade in these circumvention devices, they are powerless to act against them. Only when Canada's copyright law is modernized to include clear criminal prohibitions against this activity will Canadian law enforcement even have the legal authority to enforce against mod chip manufacturers, distributors and exporters. Until then, rather than attacking the problem at its source, the burden of combating this activity is unfairly shifted to law enforcement in the countries to whose markets these devices are being exported, and whose governments (unlike Canada's) have already stepped up to the problem by adopting laws to enable implementation of the WIPO Internet Treaties.

A third anti-piracy battlefield where Canadian government inaction has effectively handcuffed its law enforcement agencies is at the border. Canadian customs officers in the CBSA lack statutory authority to seize even obviously counterfeit products as they enter Canada. Unless a court order has been previously obtained<sup>8</sup>, only the RCMP can carry out an *ex officio* seizure, and coordination between the two agencies is generally not effective. As a result, virtually no seizures at the border have occurred, and Canada's borders are effectively wide open to imports of pirate CDs, DVDs or videogames and other infringing materials. CBSA must be given independent authority to act against any suspected pirate or counterfeit imports. Although the Canadian government has acknowledged this deficiency and has been studying the issue for years, it has failed to introduce the necessary legislative changes. It is long past time for the Canadian government to identify which statutes, regulations or policies must be amended in order to confer meaningful *ex officio* authority on border enforcement agencies, and to act promptly to institute the needed changes.

The same deficiencies that undercut enforcement efforts in Canadian movie theaters, at "mod chip" factories, and at the border also hamper attempts by copyright owners or law enforcement to combat piracy on the Internet. Though the online piracy problem is pervasive and growing, Canadian law lacks the fundamental legal tools for addressing it. Notably absent are clear legal incentives for network operators to cooperate in anti-piracy efforts, whether through a notice and takedown system such as the regime that has been in place in the U.S. since 1998, or through the use of liability doctrines to encourage network operators to take more proactive steps to detect and deal with pirate activity online. Until Canada adopts a modernized legal regime that includes such incentives, prospects for progress against online piracy will remain dim.

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<sup>8</sup> Court orders, however, can only be obtained upon the filing of an application by the right holder, supported by affidavit evidence, including information regarding the identity of the importer, exporter or vendor; country of origin or export; quantity and value of the infringing goods; estimated date of arrival in Canada; mode of importation; identity of the ship, train or truck used to transport the infringing goods, and (if available) the serial number of the container in which these goods may be found. In many instances, a right holder will not have access to this information and the necessity of obtaining the court order is itself unduly burdensome and not designed to prevent pirated and counterfeit imports from entering the country.

However, not all enforcement problems in Canada can be traced to deficiencies in the law. Even when pirate activity is clearly illegal, Canada's response to it all too often falls short. While Canadian authorities may say that combating copyright piracy is an important objective, their actions – in terms of priority setting, resources, training, and the outcome of prosecutions – suggest the contrary. Piracy is a serious problem in Canada, but the evidence is that the Canadian government is not taking it seriously.

In its Special 301 announcement last April, USTR called for more anti-piracy resources and training to be provided both to CBSA and to domestic law enforcement officials. This has not happened. Both CBSA and RCMP remain short of dedicated resources – including manpower and data and intelligence management – to address Canada's growing piracy problems. CBSA officials also lack training in identification of pirate imports; while training by the private sector has been offered, and some law enforcement agencies have responded positively, CBSA personnel have rarely been made available for training. Nor is there progress to report on interagency cooperation, another problem flagged by USTR last year. The existing arrangement under which CBSA can refer cases to the RCMP through designated RCMP liaison officers is unwieldy and impractical.

The continued prevalence of pirate product in Canada's retail market indicates another enforcement shortcoming: the RCMP's long-standing reluctance to target retail piracy. Its record of cooperation with right holders to attack piracy is spotty at best. Examples of unwillingness to share information, reluctance to disclose the inventory of pirate entertainment software product seized, and insistence on formalities such as Canadian copyright registration are all too common. Although the RCMP has now listed intellectual property crimes among its top stated priorities, its actions too often belie this label. Under the Justice/RCMP Copyright Enforcement Policy, RCMP still will not take action against retail outlets engaged in piracy, except in exceptional cases in which it is shown that the target is a repeat offender. The Enforcement Policy does not account for the reality that as technology constantly advances, the "retailers" now use ordinary computer equipment to become mass manufacturers, producing literally hundreds of thousands of pirated DVDs, CDs, software and video games. Not surprisingly, the retail piracy problem in communities such as Vancouver, Montreal, Edmonton, Calgary and Greater Toronto continues to worsen. While there have been some important successes – for instance, RCMP criminal actions have been critical in the near-total suppression of the pirate retail videogame market in Quebec City – on the whole the Canadian law enforcement commitment to enforcement against retail piracy is inconsistent and generally under-resourced.

The same problems extend to prosecutors and courts in Canada. Few resources are dedicated to prosecutions of piracy cases; prosecutors generally lack specialized training and (apparently) any interest in obtaining it; and too many judges seem to deprecate the seriousness of copyright piracy. The result is that those few pirates who are criminally prosecuted generally escape any meaningful punishment. An illustrative example is the story of Chui Lau, a well known owner/operator of a pirate retail store in Richmond, British Columbia, who pled guilty to over eighty counts of criminal copyright infringement over a three year period beginning in 2003, as a result of a series of raids in which equipment for manufacturing counterfeit DVDs was seized, along with a large quantity of pirate product. Despite being charged on three separate occasions, the total punishment Mr., Lau received for his repeat offenses was a fine of C\$11,000 (US\$9400) and an order to remain in his residence from 11pm to 7am for 12 months. Even the RCMP acknowledges that the penalties for engaging in copyright piracy in Canada – usually insignificant fines – remain simply insufficient to deter people from engaging in this highly profitable and relatively risk-free crime.

The light penalties also encourage recidivism. As the RCMP concluded in recent policy assessments of Canada's rampant piracy problem: "Counterfeiters have stated to police they will continue to sell counterfeit goods because the deterrents offer no incentive. ... Minimal sentences and low fines offer little incentive for law enforcement to pursue this issue more vigorously, and every incentive for criminals to continue pirating copyrighted goods."<sup>9</sup> A notable example involves a Markham, Ontario pirate video game retailer: "Fun Desk," located at Pacific Mall and owned by Ka Man Chan. In April 2005, RCMP officials raided "Fun Desk" and seized thousands of pirate video game optical discs, mod chips and other counterfeit game devices. Chan pled guilty to six offenses and was sentenced to pay a fine of C\$67,000 (US\$57,175). Clearly that sentence did not deter Chan. After being sentenced, he purchased two new stores at Pacific Mall, "Xtreme Video Entertainment Inc." and "Genesis Video Games," where he, again, sold pirate video game optical discs and other circumvention devices. RCMP officials also found Chan to be manufacturing much of the infringing products from his home, a short distance away from Pacific Mall. In July 2006, Chan was arrested and charged with over twenty counts of infringing on copyrighted works. Such recidivism will continue so long as the penalties imposed for piracy amount simply to a cost of doing business for the pirates.

USTR should press the Canadian government to initiate and adequately fund a coordinated federal law enforcement effort against copyright piracy. This should include a nationwide program to crack down on the importation of pirate goods at all major Canadian points of entry. Raids and seizures against retail targets, as well as against the manufacturers of pirate products, must be stepped up, and unnecessary roadblocks to enforcement eliminated (such as the informal requirement in cities such as Vancouver, Montreal and Toronto that retail targets must receive a formal "cease and desist" notice from a right holder before any raid will be considered). Since the availability of pirated products will not be reduced without criminal prosecutions against infringers and the imposition of deterrent sentences, Crown counsel should be encouraged to take on more copyright infringement cases, and be provided with the training and other support needed to fully prosecute them. Canadian courts should be looked to for more consistent deterrent sentences, including jail time for piracy cases. Canadian authorities should be encouraged to accord a high priority – in practice, not just in rhetoric – to the serious piracy problems within their country, and to devote adequate resources to the investigation and prosecution of these cases.

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<sup>9</sup> RCMP, "An Assessment of Commercial Scale Criminal Copyright Piracy and Trade-mark Counterfeiting in Canada", 2000. See also, RCMP, "A strategic intelligence assessment of Intellectual Property Crime in Canada", 2004; RCMP, "Intellectual Property Crime in Canada – Hazardous and Costly", 2005.