

INTERNATIONAL INTELLECTUAL PROPERTY ALLIANCE

2002 SPECIAL 301 REPORT

UKRAINE

EXECUTIVE SUMMARY¹

On March 12, 2001, Ambassador Zoellick designated Ukraine as a Priority Foreign Country (PFC) for its failure to implement the Joint Action Plan agreed to by then-President Clinton and President Kuchma in Kiev on June 1, 2000. The designation in March commenced a formal investigation of the IPR protection and enforcement failures in Ukraine, consistent with Special 301 legal requirements. On December 20, 2001 that formal investigation ended and the U.S. government announced the imposition of trade sanctions amounting to \$75 million, effective on January 23, 2002, as the result of the continued and complete failure on the part of the government of Ukraine to meet its obligations under the Joint Action Plan, namely to properly regulate optical media production and to engage in effective enforcement of copyright law in Ukraine. The imposition of sanctions in January 2002 were in addition to the complete withdrawal of trade benefits to Ukraine under the Generalized System of Preferences program; that suspension was announced on August 10, 2001, effective August 24, 2001.

On January 17, 2002, the Ukraine Parliament (Rada) adopted a severely deficient law that was intended to regulate optical media production and distribution (Optical Disc Licensing Bill #8278-1). This law, signed by President Kuchma on February 7, 2002, has many significant shortcomings and will likely not permit effective regulation of the production and distribution of illegal optical media discs as required by the Joint Action Plan. It is unfortunate that, after working with the copyright industries for two years to craft an effective bill consistent with international standards and experience, the Ukraine Parliament chose to adopt a watered-down version that falls far short of the proper implementation called for in the Joint Action Plan. The U.S. government properly reacted to that bill calling it an insufficient measure and refusing to forestall the trade sanctions or to re-institute the GSP benefits.

In sum, Ukraine has not adopted an effective optical media regulatory regime and failed to implement the Joint Action Plan by providing adequate and effective copyright protection and enforcement. For these reasons, IIPA recommends that in 2002 Ukraine be retained as a Priority Foreign Country (PFC).

The optical media law is only one part of an overall weak legal regime in Ukraine. That law, coupled with the absence of any meaningful enforcement activity by the government, has resulted in a climate that, during the course of 1999 to 2000, made Ukraine the largest producer and exporter of illegal optical media discs (CDs, CD-ROMs, DVDs) in Central and Eastern Europe. During 2001, heeding close international governmental scrutiny and media attention, some of the existing plants either suspended their operations or moved them to neighboring countries – namely Russia and Belarus.

¹ For more details on Ukraine's Special 301 history, see IIPA's "History" appendix to this filing.

While the current plant production (and capacity) is below the levels reported in early 2001, the illegal distribution network remains and the environment is still ripe for Ukrainian producers of illegal material to quickly ramp up to the once high levels of illegal production. Furthermore, because of the overall weak enforcement regime, especially at the borders, pirate inventory continues to be shipped from Ukraine, and other pirate product is transshipped throughout, to other countries in Eastern and Central Europe.

Without the adoption of an effective optical media law and without the implementation of a legal infrastructure that can effectively police against large-scale commercial piracy, Ukrainian plants could, at any time, easily restart illegal operations back up to the capacity they had in 2000 and 2001. That is why Ukraine remains a major threat to the growth of legitimate markets domestically and in the region. Ukraine also has failed to use its criminal code to crack down on the organized crime syndicates distributing material in and out of Ukraine, and has failed to properly police its borders that permit this wide-scale shipment and transshipment of these materials.

The key to Ukraine's success will be how quickly it can get itself back on track to adopt and implement the effective laws it pledged to adopt in June 2000. On June 5, 2000, Ukraine formally announced the Action Plan in a joint statement issued by then-President Clinton and Ukrainian President Kuchma. The Action Plan was meant to combat the unauthorized production and export of optical media products in Ukraine. In that joint statement, the government of Ukraine announced its commitment to implement the plan by November 1, 2000. Now, 16 months after the agreed to enactment date, that plan remains a well-intentioned but unimplemented scheme.

The Action Plan consists of three parts: (1) to close the plants, seize illegal material, and only to reopen the plants when there is a legal licensing scheme in place; (2) to adopt proper optical media production and distribution regulations, including identification (SID) coding and the monitoring of raw material and manufacturing equipment, as well as of exports of product; and (3) to significantly improve the copyright law and to introduce other legal reforms, including criminal and administrative penalties, necessary to implement a modern copyright regime.

The optical media law adopted in January 2002 (Optical Disc Licensing Bill #8278-1) is deficient in a number of key areas. An Implementing Decree signed on January 30, 2002 has not directly improved the prospect for effective optical media regulation and does not address the deficiencies of the Optical Disc Law. To name just a few of the many deficiencies: the Optical Disc Law (and Decree) do not cover all of the equipment used in the production of (illegal) discs, especially the matrices used in the manufacturing process; they leave room for manipulation of the use of international identification practices (unique identifiers); they do not effectively regulate the issuance, suspension, or revocation of a license for plants producing or distributing discs; they fail to provide for effective means to seize equipment and discs; and they do not permit effective or proper inspections of the plants. So unfortunately, Ukraine has still not implemented the Action Plan in the first two key parts detailed above. Even with this new law and the late-January Decree, the production and distribution of illegal optical media discs can continue without effective enforcement.

In early 2001, the problem of optical media production consisted of at least five known CD plants capable of producing over 70 million discs a year, which was more than Bulgaria produced at the height of its capacity. Currently the plant capacity is limited to at least two operating plants,

but with several other plants still in Ukraine having suspended operations. Unfortunately, with an ineffective law now in place, these plants could restart their operations without effective enforcement by the copyright industries. In 2000 losses to the music industry were estimated at \$200 million; in 2001, the estimated losses were \$170 million, reflecting the plant migration and suspension.

The plants in Ukraine mostly produce illegal musical CDs, as well as business and entertainment software CD-ROMs. More recently in late 2001, one of the plants began to produce blank CDs and then orchestrated other underground reproduction facilities to press music on those CDs (at so-called "CD-R plants"); the original plant then completes the piracy of these recordings by printing and inserting the disc's art work for final sale into the illegal marketplace.

Even with the suspension or closure of some of the plants and the migration of others into third countries, the overproduction of years past was so huge that back-catalog material continues to flood other countries, completing disrupting the already vulnerable markets throughout Central and Eastern Europe (including the Commonwealth of Independent States, C.I.S.), as well as established markets in Western Europe and the Middle East. Plenty of previously produced material also is still being stored in or distributed through Ukraine. Illegal discs produced in Ukraine have been seized by police in the following 16 countries: Romania, Hungary, Poland, Bulgaria, Peru, United Kingdom, Finland, Germany, Italy, Lithuania, Moldova, the Slovak Republic, Greece, Israel, New Zealand and the United States. The recording industry reports seizures made by their own local representatives in a number of additional countries. This is evidence of the wide-scale disruptive effect of the Ukraine optical media production and distribution problem.

As IIPA reported last year, audio CDs and software CD-ROMs are not the only materials being reproduced and distributed in Ukraine. Audiovisual VCDs have also been the subject of piracy; in one case in April 2000, over 11,000 VCDs made in Ukraine were seized by the motion picture anti-piracy organization in Bulgaria.

In 2001, customs authorities began to take some action, seizing several thousand CDs. However there still has not been the promised follow-up to these seizures with the commencement of criminal investigations and convictions. Much more needs to be done by customs authorities in order to stop the trafficking of material into and out of Ukraine by seizure and confiscation and by application of the criminal laws. In addition, in a step backwards, an onerous customs registration system was adopted by a decree in May 2001.

It was only in February 2000 that Ukraine even began to protect foreign sound recordings, as a result of its accession to the Geneva Phonograms Convention. That was a positive step. A further positive step was the passage of copyright law amendments effective in September 2001, including finally fixing the protection for older (pre-existing) works and sound recordings.

Until passage of the copyright law amendments in July 2001 (effective date September 5, 2001), foreign sound recordings released prior to February 18, 2000, and works published prior to May 27, 1973 (the date of adherence to the Universal Copyright Convention) were unprotected in Ukraine. Ukraine made progress in 2001 by finally correcting this problem for both works and sound recordings. Now, in order to create legitimate markets for music and motion picture materials, Ukraine police will have to properly implement the 2001 law to rid the marketplace of back-catalog material that has flooded the market (along with optical media products) because of the past and present legal and enforcement deficiencies.

In addition to the optical media regulations, other major legal reforms are needed to provide effective protection and enforcement for works and sound recordings. Criminal code amendments were adopted by the Parliament in April 2001 and went into force on September 1, 2001. These amendments fixed one problem – applying the criminal penalties for the first time, to neighboring rights violations; but the code was not amended to remove the “substantial material harm” threshold that will continue to act as a bar to the effectiveness of the criminal provisions.

Ukraine still must also amend its criminal procedure code, its customs code, and its administrative/regulatory code to effectively address systematic violations of copyright and neighboring rights laws, including amendments to correct all of the shortcomings in the optical media production provisions. Ukraine must make these changes (and fix its overall enforcement scheme) in order to comply with the World Trade Organization TRIPs Agreement for its eventual accession. The current package of legislative proposals under discussion in Ukraine in the context of WTO accession falls short of bringing the intellectual property protection regime into compliance with TRIPs, and are not likely to lead to improvements in the overall enforcement situation on the ground.

On May 6, 1992, Ukraine signed a bilateral trade agreement with the U.S. that entered into force on June 23, 1992. That agreement included wide-ranging commitments for Ukraine to enact and enforce modern laws protecting intellectual property rights and to provide effective enforcement. In exchange, the U.S. granted Ukraine Most Favored Nation (MFN), now Normal Trade Relations (NTR), treatment; the Ukrainian deadline for meeting the IPR obligations was December 31, 1993. In December 1993, Ukraine did enact a new law on copyright and neighboring rights (this law was significantly amended in July 2001, effective September 5, 2001).

On October 25, 1995, Ukraine adhered to the Berne Convention (Paris Act); Ukraine also adhered to the Universal Copyright Convention on December 25, 1991 but acknowledged their successor status to the Soviet Union’s membership in the U.C.C., effective May 27, 1973. On February 18, 2000, Ukraine adhered to the Geneva Phonograms Convention. All of these acts were obligations, even if some were undertaken belatedly, to comply with the bilateral agreement.

During the seven years that Ukraine, slowly and only in piece-meal fashion, implemented the bilateral IPR obligations with its legal reforms, it became a “safe haven” for an increasing number of pirate manufacturers of musical recordings, business and entertainment software, and, more recently, audiovisual material. A combination of legal reform and enforcement deficiencies created conditions ripe for piracy: Until 2000, foreign sound recordings weren’t protected at all; older material including pre-1973 works and pre-1995 sound recordings were unprotected until September 2001, thereby undercutting any marketplace for newer material; the optical media plants continue to operate freely and without effective control mechanisms – the new law has yet to be put into force (and given its deficiencies there are low expectations that it can be in any way effective); organized criminal syndicates continue to distribute material in and out of Ukraine with impunity; there are no administrative sanctions being imposed, and the new criminal sanctions have not yet been put to use, nor are there any aggressive on-the-ground enforcement activities to deter piracy. Until these problems are fixed and there is an operational system of deterrent criminal enforcement, pirated products will continue to flood Ukraine and the region, and the Ukraine marketplace for legitimate sound recording and works will not get itself established.

The failure to provide effective enforcement is a breach of the U.S. trade agreement (and any eventual World Trade Organization accession). Criminal sanctions do exist for violations of copyright pertaining to works and neighboring rights and were, for the most part, improved by amendments effective in 2001. However, they have not deterred commercial piracy for two reasons: (1) the penalties have a “significant material harm” threshold that remains cloudy and this is a bar to the use of the provisions; and (2) simply, the criminal sanctions (old or new) have yet to be used to convict anyone in a copyright or neighboring rights case. These provisions must be used against the criminal syndicates involved in wide-scale piracy of recorded music as a first step.

To be more effective, the criminal code must be amended to remove or clarify (and set at a low level) the “significant material harm” threshold. The criminal procedure code also must be amended to provide police the authority to act *ex officio* to initiate criminal intellectual property cases.

In addition, Ukraine does not have an effective customs code to deter piracy at the border; neither recently adopted amendments, nor the recently proposed (further) changes fix the loopholes and difficulties facing effective border enforcement. These failures permit illegal material to flow freely into and out of Ukraine. The customs code must be amended to permit *ex officio* border enforcement actions; border enforcement action needs to be effective and must be carried out in cooperation with rightsholders.

Equally important as Ukraine’s other legal reform failures is the failure to take the steps necessary to properly enforce its copyright laws with police, prosecutor and judicial action to deter commercial piracy. The improvements in the enforcement legal regime of Ukraine – to the criminal, criminal procedure, civil, administrative, and customs codes – and the implementation of on-the-ground enforcement are necessary for compliance with the bilateral trade agreement and for Ukraine’s accession to the World Trade Organization.

IIPA GSP PETITION AND PARTICIPATION IN THE PFC INVESTIGATION AND DETERMINATION HEARINGS IN 2001

The IIPA’s GSP Petition and Testimony at the U.S. Government’s PFC Investigatory Hearing Detailed Ukraine Practices That Result in Huge Industry Losses

As a result of its NTR status, Ukraine is qualified to be a beneficiary under the Generalized System of Preferences (GSP) program, a U.S. trade program which offers preferential trade benefits to eligible countries; that is, duty-free status for certain imports.

In order to qualify for such unilaterally granted trade preferences, the U.S. Trade Representative must be satisfied that the country meets certain discretionary criteria, including that it provides “adequate and effective protection of intellectual property rights . . .” This includes that a country is providing adequate and effective protection and enforcement of copyright and neighboring rights. Ukraine has not been fulfilling the statutory obligations of GSP. In fact, at the same time that Ukraine was causing millions of dollars of losses to the U.S. due to piracy, it was

enjoying trade benefits worth close to \$40 million without duty, or over 4.6% of its total imports into the U.S. in 2000.

As a result of this situation (under similar circumstances in 1999), IIPA filed a petition with the U.S. government on June 16, 1999 to request the suspension or withdrawal of Ukraine's GSP benefits. That petition was accepted on February 14, 2000 and public hearings were held on May 12, 2000.

At the same time as the GSP investigation was underway by the U.S. government, Ambassador Zoellick on March 12, 2001 designated Ukraine as a Priority Foreign Country. The PFC investigation moved on a parallel track with the GSP case. Public hearings were held on April 27, 2001 with IIPA testifying and filing voluminous written material in support of its petition. In the filings, the IIPA identified the losses to its members resulting from Ukraine's acts, policies and practices. The IIPA estimated that these losses (from just three of its members with available statistical information) was \$216.8 million in 2000—that is, but for the Ukrainian piratical practices, \$216.8 million would have been repatriated back into the U.S. economy.

The IIPA estimates were as follows: the Recording Industry of America (RIAA) estimated \$160 million in losses; the Motion Picture Association of America (MPAA) estimated \$40 million in losses; and the Business Software Alliance (BSA) estimated its U.S. company losses were \$16.8 million in 2000. The other members of the IIPA, namely the Association of American Publishers (AAP), the American Film Marketing Association (AFMA), the Interactive Digital Software Association (IDSA), and the National Music Publishers Association (NMPA) did not have loss figures available. However, these industries were then and continue to be hurt by piracy in Ukraine and the failure of the government of Ukraine to deter piracy. To illustrate, the illegal optical media discs seized by authorities in Ukraine and in the other 16 countries where these Ukraine discs have been illegally distributed, contain unauthorized recorded music (RIAA), audiovisual material (MPAA and AFMA), underlying musical compositions (NMPA), business software (BSA), entertainment software (IDSA), and literary material (AAP). The PFC investigation figures of \$216.8 million are losses to American repertoire that resulted from Ukraine's practices anywhere in the world. So, for example, the arrest of individuals in London (in December 2000) with illegal discs of the Beatles album #1 produced in Ukraine was not counted in the PFC investigation losses because that is British, not U.S., repertoire.

On August 10, 2001 the U.S. government, satisfied by the evidence presented about the ineffective Ukraine legal and enforcement regime, announced it was suspending all of the GSP benefits to Ukraine, effective August 24, 2001. If retained for a full year, this would result in roughly \$40 million in losses to Ukraine judging by the last year when GSP benefit figures were available (2000), as noted above.

On December 20, 2001 the formal PFC investigation ended and the U.S. government announced the imposition of trade sanctions amounting to \$75 million, effective on January 23, 2002.

The GSP benefit withdrawal and PFC trade sanctions are the result of Ukraine's complete failure to meet its obligations under the Joint Action Plan to provide for an adequate and effective copyright protection and enforcement regime in Ukraine. These steps by the U.S. government were fully supported by IIPA. It remains the hope of the IIPA that these harsh steps undertaken by

the U.S. government in 2001 and early 2002 of withdrawing and suspending trade benefits and imposing trade sanctions will act as a call to action for the Ukraine government to take the positive steps laid out in the Joint Action Plan in 2000 to eradicate the optical media production and distribution problem and to develop an effective copyright legal and enforcement regime. If undertaken properly, this will encourage investment for the benefit of U.S. and other foreign investors, as well as for Ukrainian authors, producers, and copyright industries.

COPYRIGHT PIRACY

The Need to Regulate Optical Media Production in Ukraine, and to Control the Export of Illegal Material in the Region

The absence of optical media regulation and criminal enforcement provisions allowed Ukrainian plants to become a major source of the production, distribution and export of illegal optical disc media (CDs containing musical works, audiovisual VCDs, and CD-ROMs containing entertainment and business software). Even with the current plant production slow-down, the past practices have left a flood of illegal optical media product in Ukraine and the export of millions of pirate CDs throughout Eastern, Central and Western Europe over the past several years. The current inability to properly regulate means that production of even more unauthorized material is a looming threat that can be restarted at any time.

In early 2001, it was estimated by the recording industry (International Federation of the Phonographic Industry, IFPI) that the production capacity of optical media material was around 70 million units per year. The demand for legitimate CDs in Ukraine is still approximately 5 million units. In late 2000/early 2001, initial reports of the closure of some of the plants by the Government of Ukraine turned out to be false when it was discovered that previously government-inspected and supposedly "closed" plants were still in operation. So it was the case that until the second half of 2001, at least five plants (identified in last year's report) continued to produce predominantly pirate product. In a September 2001 *Kyiv Post* article, a Ukraine government minister announced that four of the five plants had been closed, but acknowledged that the closure was not permanent, and that some of the plant lines may have been exported to other countries.

At present, the IFPI reports that one of the five plants reported on last year has suspended all or part of its operations and moved its production lines to Belarus and Russia. Of the remaining three (known) CD plants in Ukraine, one is cooperating with the international recording industry on establishing proper identification coding and production operations. However, one of the remaining (known) plants in Kiev has transformed its illegal CD production and now makes "legal" blank recordable CDs but orchestrates that legal production with the sale of these CD-Rs to CD-burning establishments. The plant further coordinates this activity with the illegal production of artwork which is collated with the disc and then sold in Ukraine and/or shipped abroad. As noted, the other plants that suspended their operations could, at any time, restart and expand their illegal production lines. Now that a weak optical media law is in place, this becomes a very real threat and one that will only be "legitimized" by the implementation of this law. In the meantime, illegal discs of music, software (business and entertainment) and audiovisual material (VCDs) are prevalent

at street kiosks and widely distributed by commercial enterprises for distribution in Russia and other C.I.S. countries as well as other parts of Eastern and Western Europe.

In May 2001, the Ukrainian government finally agreed to direct the General Prosecutor's Office to collect the wealth of evidence (including forensic tests) submitted by the copyright industries of the massive piratical activity by the Ukraine CD plants, and to commence a criminal investigation of the illegal plant activity. On January 31, 2002, after eight months, the Prosecutor's Office announced that it was terminating that investigation because of a lack of sufficient evidence of any violations of the law. So, the plant operators will not be prosecuted by the criminal laws even though the plants have been producing and distributing more illegal material than those in any other country in Europe and have been doing so for years. On this point, there is no dispute since optical media regulation was the basis of the Joint Action Plan, and the Ukraine government has openly acknowledged plant piracy.

The Action Plan originally announced by the Ukraine and U.S. governments in June 2000 was intended to properly and completely address this problem by taking the steps necessary to regulate optical disc plants, and by improving border enforcement to contain the problem within the borders of Ukraine. Proper optical media regulation in Ukraine would consist of: (1) instituting plant licensing, SID code and optical media regulations and penalties for noncompliance that include the closing of offending plants; and (2) appointment of the proper agencies and officials, as was done in Bulgaria, with the authority to undertake this enforcement effort and responsibility for putting these regulations in place.

The Action Plan, consistent with what the copyright industries have requested in the Ukraine and in other countries, would require Ukraine to immediately stop production of the illegal material and to set up plant monitoring procedures, like those established in Bulgaria in 1998, to regulate the production, distribution and export of optical media. Such regulations include provisions to close plants that are caught illegally producing copyrighted material; to seize infringing product and machinery; to introduce criminal liability for the individuals infringing these regulations; and to monitor the importation of raw materials (optical-grade polycarbonate) used in the production of CDs, DVDs and CD-ROMs (and other optical disc media). All of the plants would be required under the Action Plan to adopt source identification (SID) codes to deter plants from infringing production of optical discs.

The history of copyright enforcement in Ukraine the past few years has unfortunately consisted of a series of missteps, undercutting effective enforcement. Distribution, including the import, export, wholesale and retail trade of audio and audiovisual products, could have been properly regulated by Presidential Decree # 491 of May 20, 1998. At the time, IIPA welcomed adoption of the decree as a positive step against piracy, but unfortunately, the decree was never implemented. Instead, on March 23, 2000, the Parliament adopted the Ukraine Law on Distribution of Copies of Audiovisual Works and Phonograms (the "Hologram Sticker" law); it was signed into law on November 15, 2000. That law was not aimed at and does not achieve improvements in copyright enforcement against CD plants. Adopted over the objections of the copyright industries, that law is not an alternative to plant licensing regulations, and it remains unclear whether the law actually, or only effectively, repealed the 1998 Decree, but it clearly ended any hope of proper implementation of the 1998 provisions.

The controversial Hologram Sticker law was finally implemented effective January 1, 2001. As predicted, the Hologram Sticker law proved itself to be open to abuse and fraud. To make

matters worse, the law completely exempted exports, the real problem with overproduction in Ukraine; and it exempted manufacturers, the real source of the problem. It established an unworkable administrative burden on legitimate businesses and kept legal product from the market, thus permitting more pirate material to flourish in the vacuum. The Hologram Sticker law was not repealed by the January 2002 Optical Disc Law.

After almost two years of debate, the Ukraine Parliament adopted Optical Disc Licensing Bill #8278-1 on January 17, 2002 as its response to the Joint Action Plan. That law which was signed by President Kuchma on February 7, 2002, goes into effect 60 days after its official publication.

In fact, the Optical Disc Licensing Bill has numerous flaws that will likely prevent it from effectively stopping piracy in the production and distribution of optical media discs. The experience of the copyright industries in many countries other than Ukraine has shown that there are at least six basic features of an effective optical media regulatory scheme.

To be effective, an optical disc plant law must (1) require plants to obtain a business license to commence production; (2) establish a basis for regulators to deny, suspend and revoke the license upon evidence of illegal activity; (3) require import and export licenses and transparent searches of these licenses; these licenses must cover the goods (discs) and machinery and equipment (including the raw materials) used in the production of optical discs; (4) require the plants to apply internationally recognized identifiers on the goods and machinery, to keep records of production and distribution licenses, and to cooperate with the police upon inspection; (5) require plant inspections and in particular, "surprise" plant visits, including means for the rightholder organizations to participate in such plant visits, to obtain evidence and forensic tests, and access the plant's records; and (6) require a comprehensive list of enforcement procedures, remedies, sanctions, powers granted to authorized officers, including the powers to seize equipment and discs during plant visits.

The Ukraine Optical Disc Law of January 2002 falls short of these key features. In addition, there is now a patchwork of conflicting laws (including the General Licensing Law), decrees, and regulations. This will only cause confusion when the OD Law is finally implemented.

On its face, the Optical Disc (OD) Law has several deficiencies. The OD Law does not properly regulate all of the equipment used in the production of (illegal) discs, in particular it essentially does not cover the matrices used in the manufacturing process and keeps some of the important records and licensing information out of reach from investigators seeking information on possible illegal activity. It leaves loopholes in the requirement that Ukrainian plants comply with the international identification practices, namely SID coding, in all production facilities; nor are the plant operators required to keep sample copies of the discs; all of this evidentiary and coding information is essential to identify the source of the illegal material. The OD Law does not effectively regulate the issuance, denial, suspension, or revocation of a license for plants producing or distributing discs—the law allows convicted plant operators to be reissued a license, and delays the suspension of licenses even in cases of clear violations. The OD Law does not permit effective or proper inspections of the plants – for example, surprise inspections are permitted only after compliance with cumbersome and timely procedures that will eviscerate their effectiveness; it also does not allow for either the effective securing of evidence or the seizure of equipment and discs during plant visits. The OD Law contains loopholes for import and export of some of the tools (matrices and manufacturing equipment) essential to produce discs. Finally, the liability for

violators is too limited—with low minimum penalties; no provisions for confiscation or destruction of discs, material or equipment; weak administrative penalties; and weak criminal penalties (a high threshold will bar use of the criminal penalties in many cases).

Overall, the OD Law needs significant improvement before it can be enforced in a way to bring meaningful protection and enforcement in Ukraine. Already, there is disagreement among Ukraine experts as to how this law will be implemented; the January 31, 2002 Decree, according to some experts, could be used to improve the plant inspection deficiencies in the law, while other experts disagree. Many in the Ukraine Parliament and government worked closely with the copyright industries for two years crafting legislation that incorporated the experience of industry experts in other countries (such as Bulgaria) to create the proper legal framework to regulate the plants and to rid Ukraine of the influence of organized criminal syndicates in the plant production businesses. Instead, in the end, Ukraine unfortunately chose to enact a weakened bill that will likely prove ineffective.

Last, there is one additional lingering issue preventing effective enforcement in Ukraine. In 1999, the Ukraine Copyright Agency (SCAU) was closed and then reorganized into a much weaker structure. The government of Ukraine never clarified the authority and role of the Ukraine Copyright Agency vis-à-vis other government agencies, including its role, if any, in verifying the legality of the issuance of certificates for import, export, and the wholesale and retail trade of copyright material. The Copyright Agency, in essence an authors' collecting society, and the State Department on Intellectual Property are not equipped to monitor and close down plants that are engaged in piratical activity. That should be left to the economic police authorities in an enforcement-based agency within the government.

COPYRIGHT LAW, CIVIL CODE, AND OTHER LEGAL REFORMS

Amendments to the Copyright Act and Related Enforcement Laws Were Adopted; Need for Proper Implementation

In 2001, two important pieces of the Ukraine legal regime were amended. The Copyright Law of 2001 (effective September 5, 2001) significantly revised the Copyright Law of 1993. Also, the Criminal Code was amended on April 25, 2001, effective September 1, 2001. In addition, Ukraine made very positive steps to modernize its legal regime by acceding to and implementing (at least in part) the two WIPO Internet treaties in 2001. Still, important pieces of Ukraine's legal regime remain to be adopted—most importantly, the criminal procedure code, the customs code, and key administrative remedies. A lingering fear is that adoption of a new civil code with extensive IPR provisions will undermine the copyright law and its enforcement.

Until 2001, the legislative deficiencies in Ukraine included the lack of: (1) protection for sound recordings created before February 18, 2000 and for works created prior to May 27, 1973, as required by the Berne Convention and WTO/TRIPS; (2) full national treatment of neighboring right holders with regard to rights and remedies; (3) optical media plant regulations to stem the commercial-scale pirate production of CDs, CD-ROMs and DVDs; (4) criminal penalties and procedures and administrative regulations to deter commercial piracy; (5) customs code amendments to grant clear *ex officio* authority to customs officials to seize suspected illegal material at the border; and (6) civil *ex parte* search procedures necessary for effective end-user

piracy actions (and required by WTO/TRIPS). In 2001, Ukraine fixed item 1 above, the protection for pre-existing works and sound recordings; and, it amended the criminal penalties provisions (item 4 above) making some improvements, though additional changes are still necessary.

In the 1992 bilateral trade agreement with the United States, Ukraine acknowledged its successor status to the Soviet Union's adherence to the Universal Copyright Convention, effective May 27, 1973. This confirmed that the point of attachment for copyright relations between the United States and Ukraine existed from this date forward at least for works (but likely not including sound recordings). The 1992 agreement also stipulated a bilateral obligation of both countries to provide a full retroactive term of protection to each other's works on the date when both countries became members of the Berne Convention in accordance with Article 18 of Berne (this is also a WTO/TRIPS obligation). All during this time, the United States has unilaterally provided full retroactive protection for all Ukrainian works and sound recordings; that protection was extended from a term of 75 years to a term of 95 years in amendments adopted by the Congress in 1998.

Following the breakup of the Soviet Union, the Ukraine Parliament passed a law on Copyright and Neighboring Rights on December 23, 1993, which came into force on February 23, 1994. That law was closely modeled on the Russian Federation's 1993 copyright law. Separate legislation and regulations on broadcasting were later adopted.

In October 25, 1995, when Ukraine adhered to the Berne Convention, its instrument of accession included a declaration stating that it would *not* apply Berne's Article 18 obligations to protect pre-existing foreign works in Ukraine. Ukraine's decision not to grant protection to pre-existing U.S. copyrighted works (prior to May 1973) was incompatible with its bilateral trade agreement with the U.S., as well as with Ukraine's Berne Article 18 and national treatment obligations.

On February 18, 2000, Ukraine adhered to the Geneva Phonograms Convention, also an obligation of the bilateral trade agreement. However, the copyright law of 1993 did not provide protection for pre-existing sound recordings. That created an intolerable situation for the recording industry. By waiting almost seven years to join Geneva Phonograms, Ukraine permitted an explosive growth of illegal cassette tape and optical media disc piracy of foreign musical recordings to flourish. And by excluding pre-existing sound recordings, Ukraine held itself out as a safe haven for back-catalog pirates.

Fortunately, there was good news in 2001 on this issue. As part of the Action Plan, Ukraine had agreed to correct this deficiency with amendments to the copyright law for both works and sound recordings. In the September 5, 2001 Copyright Law amendments, Ukraine added provisions intended to fully comply with its obligations to grant pre-existing foreign works and sound recordings protection if they are less than 50 years old. Although these provisions provide a shorter term of protection than the protection afforded by the United States to Ukraine works and sound recordings, it is a vast improvement from the pre-2001 situation. Also, although the intention of the drafters was clear, the actual provisions are difficult to understand especially for material that was never protected in Ukraine such as sound recordings (pre-February 2000) and for nonrenewed U.S. works (covered under the pre-1978 U.S. copyright laws). However, numerous Ukraine copyright law experts and government officials assured the IIPA and U.S. government officials during talks in 2001 that the provisions in the September 2001 Copyright Law do provide full 50-year "retroactive" protection for works and sound recordings, and that that will be the outcome when the provisions are put to use by Ukraine enforcement officials or the courts.

Another major legal shortcoming in Ukraine has been the lack of effective criminal penalties to deter piracy. In the Soviet era, identical criminal sanctions for copyright infringement were a part of the criminal codes in each of the republics of U.S.S.R. In April 2001, the Ukraine Parliament adopted amendments to the criminal code, including a new Article 176 applicable to infringement of copyright and neighboring rights. The adoption of this provision applicable to protect infringements involving producers of sound recordings or performers was a step in the right direction, closing a gaping loophole in the old law. Unfortunately, the new provisions deleted an interim law with tougher five-year penalties and reverted to sanctions that provide for up to two years' imprisonment and fines ranging from 100 to 400 times the minimum wage (roughly U.S. \$2,000 to \$8,000) for copyright and neighboring rights violations. These fines can multiply up to 200 to 800 times the minimum wage for repeat offenders, and up to 500 to 1000 times the minimum wage in certain instances (for officials abusing their "official positions").

One major shortcoming of the criminal code provisions that remains after the September 2001 amendments is that the penalties can only be imposed for "substantial material damage" – this is a standard that creates an unwarranted threshold for copyright piracy. This provision creates two problems: (1) it sets a threshold that is too high; and (2) the threshold will be impossible to prove with the certainty necessary for criminal proceedings. The law should have been (and now needs to be) amended to include a low and clear threshold to instigate a criminal action—IIPA recommends a threshold no higher than 50 times the minimum daily wage. Not only would this help to identify criminal infringing acts for prosecutors, but it would provide critical guidance for the police when they are conducting initial raids and need to assess, in a particular situation, whether a case should be brought under the criminal code or the administrative code. In any case, none of the existing or new penalties have ever been applied in any copyright or neighboring rights case, so they are not being used to deter commercial piracy as they could.

As part of the Action Plan, Ukraine agreed not only to enact a criminal penalties bill, but also appropriate administrative remedies to deter piracy. These administrative remedies must be properly implemented alongside available and properly implemented criminal penalties at levels sufficient to deter piracy for effective copyright protection, as well as to meet any future WTO/TRIPS obligations.

With respect to criminal procedures, police should be able to act *ex officio*, and to initiate an intellectual property criminal case for further investigation and submission to the court, including the authority to hold confiscated products and equipment for use at trial. Ukrainian criminal procedures currently require rightholders to file complaints to initiate actions. Prosecutors, not the police, are responsible for initiating infringement cases. Enforcement would be significantly improved if the police were afforded *ex officio* authority to initiate cases without any formal complaint of the copyright owner. None of this is currently permissible under the existing criminal procedures code. The current criminal procedure code must therefore be amended to grant this authority as soon as possible in 2002.

Ukraine still does not have an effective customs code to deter piracy at the border. Neither recently adopted amendments nor newly proposed ones properly amend the loopholes and deficiencies in the current border enforcement scheme. These failures permit illegal material to flow freely into and out of Ukraine. The customs code must be amended to make border enforcement effective as soon as possible in 2002.

Amendments to the Civil Code (Chapter IV) pertaining to copyright continued to circulate for another year for consideration by the parliament. For many years, IIPA has urged that this draft law not be passed because it is a dangerous development jeopardizing effective application of the Copyright Act, and would be in breach of the bilateral trade agreement. It is also a development not unique to Ukraine, as it has been considered in several countries of the C.I.S., including the Russian Federation, as part of the comprehensive reform of the civil codes of these nations.

In Ukraine, as in other countries in the C.I.S., the efforts to revise the civil code will result in the addition into that code of new copyright provisions inconsistent with Berne, WTO/TRIPS, and the bilateral trade agreement. Efforts to so revise the civil code in Ukraine should be opposed. In December 2001, the latest draft of Chapter IV of the Civil Code had been reduced to 14 articles. This is an improvement over earlier drafts that contained over 140 articles (and then 50 in a subsequent draft), many which would have undercut the copyright law. However, even the shorted version with 14 articles is confusing and could overlap the copyright provisions; and, because it makes reference to over 90 other laws this could make it obsolete if and when any of the other laws referred to are amended. IIPA continues to urge that the civil code Chapter IV should not be adopted, certainly not in a manner that would in any way weaken the copyright law or its enforcement.

In 2001, Ukraine officials reported to IIPA that the Ministry of Education agreed with the U.S. and European software industries to adopt a "legal" software program, in other words a software asset management program for the educational sector, to ensure that Ukrainian schools used only licensed software. In exchange, the software industries agreed to provide their software at special rates for use in Ukrainian schools. The agreement will be implemented by June 2002. However, the software industry reported that a government-wide program to this effect was not finalized in 2001. That was disappointing to the software industries. The business software industry has been trying to convince the Ukraine government for a number of years to adopt a software asset management decree—to get the government ministries to use legal copies of business software—but so far, without success.

Ukraine was not a signatory to either of the two new WIPO Internet treaties when these were completed in 1996. But on September 20, 2001, the Ukraine Parliament ratified legislation to accede to both of the treaties – the WIPO Copyright Treaty (WCT) and the WIPO Performances and Phonogram Treaty (WPPT). On November 29, 2001 Ukraine deposited its instruments of accession to both treaties with the WIPO (on March 6, 2002 the WCT will go into force and it is expected that sometime later in 2002, the WPPT will also enter into force once 30 countries have acceded to).

The Copyright Law of 2001 also included amendments to implement these treaties. These actions by Ukraine, if properly enforced, are intended to protect against Internet and other forms of digital piracy, and should help with the development of electronic commerce in Ukraine. This is an important step for Ukraine and the other C.I.S. members since accession and implementation provisions were agreed to by the Interparliamentary Assembly of the Member States of the Commonwealth of Independent States (C.I.S.) in December 2000 in St. Petersburg as a way to modernize the copyright and neighboring rights laws of countries in the region. In fact, these resolutions and recommendations were agreed to by all 12 members states of the C.I.S., working in conjunction with officials from the WIPO.

ENFORCEMENT

Until the Action Plan is fully implemented, the enforcement situation for the copyright industries will continue to be a failure. The inadequate enforcement regime has, for many years, been preventing entry by the U.S. creative industries into the country, and stifling the development of local copyright industries. Without the passage of an effective optical media law and the other key enforcement tools (such as strong customs laws), there is no way to stop the illegal optical media production and distribution, or to combat the failures at the border to stop or even slow the exporting or transshipment of that material, not to mention the failures of the police or judicial bodies to crack down on commercial pirates, much less on retail-level activities.

The Ukraine enforcement problem is twofold. First, there are extremely high levels of piracy of all copyrighted products – music, sound recordings, business applications software, interactive entertainment software (on all platforms, CDs and cartridges), motion pictures, videos, television programming, and books and journals, throughout Ukraine. Second, levels of piracy in the entire region will not get better until the Ukrainian government fully implements the Action Plan and imposes strict monitoring of the illegal optical disc media production facilities in Ukraine, steps up its border enforcement, and imposes criminal penalties aimed at the commercial pirates, especially the criminal syndicates, that are producing, distributing, and transshipping materials into, through, and out of Ukraine, mostly for foreign consumption.

In the first six months of 2001, Ukraine law enforcement officials reported that officers had inspected around 11,000 shops, businesses and warehouses and seized 217,000 videotapes, 166,000 audiotapes and 183,000 CDs. All told over UAH 5 million (US\$939,700) worth of material was confiscated. There were no reports of the final disposition of the material confiscated, such as its destruction and/or the conviction and sentencing of any offender of the IPR laws. Instead, the Ukraine government said that 44 criminal investigations were commenced in the first six months of 2001 compared with 19 criminal cases instigated in all of 2000. In addition, the police reported a “major raid” against the Petrivka CD market in late January 2002, seizing about 13,000 CDs, videotapes, and software CD-ROM discs, according to a Ukraine news report. It was reported as the “first large crack-down on street vendors of illegal CDs in the last few years.”

The copyright industries reported the following enforcement statistics in 2001:

The Business Software Alliance (BSA) reported 61 raids conducted; 49 cases were commenced; two defendants were convicted; four were acquitted or dismissed, and there are 43 cases pending. There was one case that resulted in a jail sentence; one resulted in a suspended prison term. But unfortunately, in the only two cases involving business software that commenced in 2001 that led to a conviction in the court of first instance, both of these cases have been appealed by the defendants so neither of the software sentences have actually been served to date according to IIPA’s information. There were only two cases in which a criminal fine was imposed.

The International Federation of the Phonographic Industry (IFPI) and the Recording Industry Association of America (RIAA) reported that there were 116 cases commenced under the criminal code (Art. 176), of which 90 involved music piracy. The industry reported that the new criminal code provisions actually created obstacles to the investigation of copyright crimes that were not present under the old provision (Art. 136). Many of the criminal cases resulted in the confiscation

of the products and some fines (the amounts were not available). None of the cases resulted in prison sentences; many of the cases never went to trial, but were dismissed.

Under the administrative code violations, the IFPI and RIAA reported that there were 3,542 registered cases, most involving the sale of copyrighted product without hologram stickers (and about 60% of these were CDs and audiovisual material cases). The administrative penalties meted out for these violations were not reported.

MPA reported a single case in which a pirate received a suspended (five year) sentence.

In all, the copyright industries reported that the Economic Police seized 135,248 videocassettes; 104,080 audiocassettes; and 77,271 CDs in 2001. In total, the Economic Police, the Tax Police and other agencies seized 1 million items, but only a small percentage of these were destroyed.

IFPI and RIAA report that Ukraine is still the second largest music market after Russia in the C.I.S. The recording industry reports that piracy of international repertoire is estimated to be at least 85%. The total value of pirate sales, including exported CDs, is estimated at some \$170 million.

Ukraine continued to export millions of pirate CDs in 2001. These include not only declared exports of product, but also many thousands of smuggled shipments as well. Police inspectors reported (in one newspaper account in October 2001) that one quarter of the material they inspected was pirate and that they seized 21,000 items through October 2001. The industry reported that the formation of a special IP unit in the Economic Crimes Department in the Ministry of Internal Affairs has led to an increase in the quantity of police raids; however, these raids have not focused on the large distributors, but rather on the small retailers. This has not deterred piracy. Further, there were almost no customs seizures conducted on the Ukrainian-Russian border where illegal traffic is the most active, and little or no import/export activity anywhere aimed at optical disc piracy. This compares sharply with effective customs seizures in neighboring countries such as Poland, on goods leaving Ukraine. In sum, the lack of effective police and customs activity means that pirate production continues to damage not only the Ukrainian market, but also other markets in the region, as well as in the EU.

To add to the severity of the problem, Ukrainian CD plants and their related distribution companies offer their entire illegal catalog of recordings for sale via the Internet. These companies have no licenses from any music publishers or sound recording producers to replicate this material.

According to the Business Software Alliance (BSA), the estimated trade losses due to software piracy in the Commonwealth of Independent States (C.I.S.) other than Russia were \$29.7 million in 2000; the level of piracy was estimated to be 89% in 2000. Figures for 2001 have not yet been finalized. In 2001, the software industry continued to experience exceptionally high levels of pirate product from Ukraine in particular, so a big part of the estimated losses above reflect piracy in Ukraine. There was one reported seizure of mostly computer programs (along with sound recording material and videocassettes) in February 2001; a total of 30,000 optical discs were seized. So, the software industry is vulnerable to the same optical media production and distribution problems that plague the recording and audiovisual industries.

In April 2001, the business software industry began working with the Ukrainian police and prosecutors to undertake the first raids ever against computer shops installing illegal copies of

business software onto the hard disks of computers which are sold to consumers (this is known as HDL reseller piracy). Between April and June 2001, a total of 10 HDL resellers were raided by the police; this was seen as a very encouraging development. However, instead of continuing their focus on these important targets, beginning in the fall of 2001, the police shifted their efforts to easier targets such as small computer clubs and Internet cafes. By the end of 2001, the software industry recorded a total of 61 police raids involving illegal business software; 14 HDL raids; 36 raids of computer clubs or Internet cafes; and 11 raids against small CD-ROM resellers.

In 2001, the business software industry received favorable judgment in two cases, in the court of first instance. On July 23, 2001, the Goloseevskiy District Court sentenced the director of an HDL reseller firm to a suspended imprisonment term of five years (with a three-year probationary period). The defendant was also ordered to pay a \$320 fine and was banned from holding a directorship position in other companies in the future. In a second HDL reseller case decided by the same court on November 29, 2001, two persons from a shop were fined \$640 and sentenced to pay damages to the rightholder (totaling \$11,000). The respective defendants have appealed both cases.

Although the business software industry has had some success with the Ukraine police, prosecutors and the courts, as described above, it is discouraging that in many other cases, strong leads and information provided by right holders to the police resulted in no action being undertaken. To date, all raids conducted by the police were initiated without consulting the right holders. Further, civil litigation remains nonexistent, as a result of the absence of *ex parte* provisions in practice, which makes it impossible for rightholders to collect evidence without police assistance. Disappointingly, ongoing attempts to persuade the government to issue a software asset management decree remained bogged down for another year, and were unsuccessful.

The entertainment software industry (Interactive Digital Software Association, IDSA) is also vulnerable to the same optical media production and distribution problems as the other industries. The IDSA reports that material has been confiscated throughout Eastern and Central Europe that was made illegally in Ukraine, and that material currently or previously produced in Ukraine, is still being widely distributed in the region. As in the music industry, the Ukraine producers created a regional problem with their unregulated production, and now with the distribution and export of material throughout Ukraine, Romania, Poland, the Czech Republic, Hungary, Russia, Belarus and the rest of the countries of the C.I.S. These are region-wide organized criminal operations for the most part.

The Motion Picture Association (MPA) reports that the video piracy rate is over 80%; optical disk piracy is at 99%; and broadcast piracy remains at 95%.

As in prior years, the main piracy problem for the MPA remains rampant video piracy in shops and street kiosks. It is estimated that for all types of audiovisual piracy the levels are over 80%. Pirate films regularly appear in Ukrainian kiosks within weeks of their U.S. theatrical release. Most are back-to-back copies of videos recorded from U.S. cinema screens. Pirate DVDs were also reported seized in at least three raids in 2001, but the details remain unclear, as these investigations are still ongoing. Police lack legislative enforcement tools, and organized criminal groups are believed to be heavily involved. Government stickers created to combat piracy are widely produced and can be easily purchased.

Broadcast television piracy is also widespread. There are three national television stations, two of which are run by Ukrainian State Television and which broadcast original Ukrainian programming and retransmitted Russian signals. There also are many regional channels, which almost exclusively broadcast pirated films. Some of these stations use legitimate U.S. videos to make pirate broadcasts, often broadcasting the U.S. copyright anti-piracy warning at the beginning of those videos. Cable piracy is now an increasing problem.

The Ukrainian Copyright Agency and the National Council for Television and Radio, which have licensing authority over Ukrainian television, have still not been effective. The Ukrainian government should require compliance by broadcasters with copyright laws to obtain and maintain their licenses.

MPA estimates that trade losses in 2001 due to audiovisual piracy in Ukraine remained at \$40 million (unchanged since 1995).

The book industry continues to experience piracy as well, with most of the problem being books illegally printed in the Ukraine for sale in Russia. This includes both overruns of licensed works and the production of unlicensed works, which flow freely into Russia and the other countries in the C.I.S. as the result of lax border enforcement.

One other enforcement tool remains unused. In 1998, the Ukraine government promised to establish an interministerial committee on intellectual property enforcement. In February 2000, the Ukraine government announced that it was finally going to organize this committee. In 2001, the committee finally was organized and met several times, but the copyright industries reported no concrete proposals were issued to effectively deal with IPR crimes, and that there remains a problem of information not being shared among the enforcement agencies. This is unfortunate, because this committee and information sharing by the agencies could be an effective tool in the battle against the spread of pirated material, especially if aimed at the production and distribution of optical disc media.

As already noted, effective enforcement entails not only domestic (internal) enforcement, but proper border enforcement, to stop the flow of goods into and out of Ukraine. This necessitates that Ukrainian authorities coordinate their activities as well as provide customs officials with the proper authority to seize illegal material at the border without a court order, and give police and other enforcement officials the equivalent proper *ex officio* authority. Without this clear authority on the part of police and border officials, piracy will continue to worsen.

In sum, copyright piracy threatens not only foreign investment, but the development of local copyright industries in Ukraine and in the other countries of the C.I.S. This threat must be met by a coordinated legal and enforcement response. All enforcement agencies (that is, the police, prosecutors, judges, customs officials and the ministries of Justice, Interior, and Taxation) should treat commercial copyright infringement as a serious crime, and should use the new criminal code, as well as acquire the proper tools in the criminal procedure, customs, and administrative codes to deal appropriately with the problem. Clear government strategies and lines of authority should be developed. Finally, the training of judges, prosecutors, customs officials, and police should be part of ongoing enforcement efforts once the legal reforms are in place, to develop an effective enforcement regime.