

INTERNATIONAL INTELLECTUAL PROPERTY ALLIANCE

2006 SPECIAL 301 REPORT

UKRAINE

EXECUTIVE SUMMARY¹

Special 301 Recommendation: Effective on January 23, 2006, at the conclusion of an out-of-cycle review by the U.S. Government, Ukraine was placed on the Priority Watch List. IIPA recommends that Ukraine remain on the Special 301 Priority Watch List.

In 2005, Ukraine adopted significant amendments to its optical disc laws to improve its enforcement regime. This was a major accomplishment by the Government of Ukraine and IIPA applauds the addition of this important tool in the enforcement regime. In addition, the Ukraine Government agreed to participate cooperatively with the copyright industries in Ukraine on enforcement—including the commencement of joint surprise plant inspections. If implemented properly, these changes will regulate the legal production and distribution of optical media material in Ukraine. IIPA strongly urges the Government of Ukraine to fulfill its obligations and remain vigilant on its pledges of cooperative enforcement in order to improve on-the-ground efforts.

The adoption of amendments to the optical disc law (effective August 2, 2005), a key legislative reform, was a crucial step toward Ukraine's implementation of the 2000 Joint Action Plan which was agreed upon by the Governments of Ukraine and the United States. There are still improvements in Ukraine's enforcement regime that the Government of Ukraine must immediately undertake to ensure proper implementation of the new laws. These include: the adoption of regular surprise plant inspections; the creation of an "evidence repository" of sample copies of all productions runs of master stampers and finished disc produced in Ukraine; and the proper prosecution and imposition of deterrent sentences against commercial pirates of optical disc and other copyright materials. If these steps are taken, Ukraine will come a long way toward improving its copyright enforcement regime for the betterment of the local economy and the protection of domestic and foreign copyright owners. Proper implementation will ensure that the production and export of pirate optical media product cannot be resumed and that other key enforcement steps, that remain unfulfilled, are addressed. We firmly believe that, when fully implemented, the adoption of an effective copyright enforcement regime in Ukraine will benefit not only U.S. copyright owners, but also the government and people of Ukraine, by encouraging foreign investment and growth within the Ukrainian copyright industry.

A major "missing" component of the Ukraine enforcement regime has been the absence of effective criminal prosecutions and deterrent sentencing, especially against large-scale pirate operations (involving music, film, and/or entertainment software). This, coupled with ineffective border enforcement, invites wide-scale commercial piracy operations to continue in Ukraine or to work in conjunction with operations in neighboring countries, such as Russia. The Government of Ukraine must turn its attention to effective criminal enforcement. In our view, these improvements

¹ For more details on Ukraine's Special 301 history, see IIPA's "History" appendix to this filing at <http://www.iipa.com/pdf/2006SPEC301HISTORICALSUMMARY.pdf>. Please also see previous years' reports at <http://www.iipa.com/countryreports.html>.

are also necessary for Ukraine to fully comply with the TRIPS obligations of the World Trade Organization.

Actions That the Government of Ukraine Needs to Undertake

In order to provide more effective enforcement, we recommend that the Ukrainian Government take the following steps:

First, the Government of Ukraine must: (a) fully and completely inspect the optical disc plants, including surprise inspections with copyright right holder cooperation; (b) close plants that have been found to be involved in illegal production (in breach of the licensing rules and/or the copyright law); (c) seize and destroy illegal material, including the materials and equipment used in the course of illegal production (plus the spare parts and pieces of equipment); (d) properly monitor the importation of raw materials (optical-grade polycarbonate) used in the production of optical disc media; and (e) properly license new plants and/or lines at existing plants (for example, the Rostok plant which received new lines without proper review), including requiring the adoption of SID Codes. In addition, criminal cases and convictions against illegal plant operators and others involved in commercial piracy must follow proper plant inspections.

There are two optical media disc plants in operation that are the subject of detailed complaints from the recording industry (IFPI). Unfortunately, the relevant authorities in Ukraine, specifically the State Department for Intellectual Property (SDIP) and its State Inspectors, have to date failed to take meaningful and decisive action on the basis of these complaints. Despite the fact that the complaints reported large-scale illegal production, neither of the plants nor their owners/managers has faced criminal investigation, let alone prosecution. In fact, both plants are still in full operation. Note, however, that pursuant to a Ukrainian forensic report, which supported IFPI's findings of illegal production, SDIP fined one of the plants (CD Master) for illegal production of a music disc by a U.S. artist. The fine was subsequently overturned by the Kiev Commercial Court, on appeal from the plant. One of the complaints dates from 2004. The Government of Ukraine could have taken action against the plant in question under the old optical disc regime but it failed to act under that law, and has not made any progress since the adoption of the new law either. Passage of the new optical media disc law is not a substitute for enforcement.

Second, retail piracy in markets and in the streets—especially at big outdoor markets, such as the Petrovka Market in Kiev, which doubled in size in 2005, and the Radio Market in Kiev, as well as at street stalls and kiosks—has unfortunately not seen any significant decrease. The Government of Ukraine did a good job of reducing such piracy, temporarily, for the May 21, 2005 Eurovision event in Kiev – so it is clear that this type of activity can be undertaken if it is made a priority of the government. Indeed, the Government of Ukraine has demonstrated that it can effectively prevent retail piracy when the political will and resources are allocated to this problem. However, the open availability of pirated materials has once again reached previous levels as Ukrainian law enforcement has failed to clamp down on street and market piracy on an on-going basis.

Third, the Ukrainian Ministry of Science and Education should issue written and irrevocable instructions to the licensing body to automatically suspend an operating license and seal the relevant production facilities if and when it is presented with forensic evidence of breach by a given optical disc plant of the licensing rules (including copyright infringement). We recommend that this suspension should endure for at least the duration of an in-depth investigation into

infringing behavior, and the possible subsequent criminal or administrative investigation, even if this evidence is presented by a private sector representative organization.

Fourth, we recommend that the appointed department within the Ministry of the Interior which carries out forensic expertise in cases of copyright crime should receive appropriate training and assistance to improve its working methods and expertise.² Its handling of, for example, the CD Master case shows that there is much room for improvement, including how pieces of crucial evidence are physically handled (for example, forensic investigation of optical discs requires the delicate treatment of relatively fragile objects).

Fifth, the Government of Ukraine should provide the specialized intellectual property rights unit within the customs service with the mandate, and operational competence, as well as sufficient resources to act (*ex officio*) against intellectual property rights crimes. This step is necessary for effective enforcement at the border. In sum, the Government of Ukraine must move away from creating yet another bureaucratic entity at the central headquarters and instead devote more resources and show more willingness to effectively enforce intellectual property rights crimes at the border. It should be highlighted that these specialized customs units be instructed and trained to focus on illegal shipments and smuggling of pirated product, rather than the creation of massive bureaucratic hurdles for legitimate importations.

Sixth, the Government of Ukraine should take affirmative steps to stop on-line piracy. Websites offering pirate material continue to thrive in Ukraine, with the support of local Internet service providers. Internet service providers must be liable for allowing illegal material to reside on their servers, or for inducing the distribution of illegal materials by third parties, and they must act to block rampant Internet piracy.

COPYRIGHT ENFORCEMENT

The bill of amendments to the optical disc law and related enforcement legislation (which was adopted in the RADA on July 6, and entered into force on August 2, 2005) included many critical elements to secure better enforcement of illegal product, and to encourage an open market for legal product. The law's provisions included: (1) clear mandates for surprise inspections; (2) the licensing of the production of matrices (two mandatory copies of each production run/order for the licensing authorities) used to produce optical discs; (3) improved criminal sanctions for violations; and (4) the abolishment of a requirement for SID (source identification) coding for imported finished product (discs being imported into Ukraine).

More recently, CD-R production piracy by organized criminal syndicates continues to flourish because of Ukraine's weak criminal enforcement regime.

It is clear that over the past few years, optical disc production has slowed in Ukraine, at least for most industries. For the entertainment software industry, production (mostly involving CD-R material) appears to have increased as have exports of pirated entertainment software products on optical media. In 2005, optical disc production capacity increased with the arrival of two new plants in Odessa and Kiev, respectively (the recently installed new lines in Ukraine add an

² One positive step worth noting was the government's establishment of a specialized unit for intellectual property rights crimes within the Economic Crime Division in the Ministry of the Interior. This unit has the exclusive authority to deal with intellectual property rights crimes. In addition, the General Prosecutor reconstituted economic crime status to criminal violations of author's and neighboring rights.

additional capacity of up to 40 million discs per year, as well as new mastering equipment). This is why proper implementation of an effective enforcement regime is so critical.

Recent shortcomings have meant that: (1) most inspections of the plants have lacked the required element of surprise (and have instead consisted of pre-raid information leaks where plants have ample time to sanitize their premises); (2) mastering codes have been issued to plants that have no mastering facilities, thus allowing facilities to produce masters and engraving codes without any oversight by the copyright owners; and (3) key enforcement tools (the use of production samples) that could aid in the detective work for uncovering illegal activity have been held back by the agency responsible for optical media licensing, the State Department for Intellectual Property (SDIP). Rightholders' organizations should get access to production samples of optical discs via SDIP so that they can properly conduct anti-piracy investigations.

In December 2005, the Government of Ukraine pledged to participate in an "Enforcement Cooperation Group" with copyright owners—hosting regular meetings to coordinate enforcement and to share information and expertise. This is a step in the right direction. But, more important are regular surprise inspections and stepped up activity (raids and seizures) against organized crime operations. The Government of Ukraine has indicated its willingness to improve its enforcement while IIPA and its members await actual implementation of these plans—these must include frequent (monthly) surprise inspections jointly undertaken by right holders and government enforcement agents, coupled with 24-hour security measures at the plants, and the maintenance of a comprehensive evidentiary database of samples, polycarbonate usage, production and sales statistics and the like. When, during an inspection, machinery is claimed to be temporarily inoperable, a subsequent surprise inspection must be arranged to obtain exemplars from that plant.

Ukraine remains a major transshipment point and a storage facility for illegal discs produced in Russia and elsewhere because of very poor border enforcement. Pirate CDs and DVDs dominate the market in Ukraine and are sold in markets, kiosks and street stalls; one example is the Petrovka Market in Kiev, which has close to 300 stalls openly selling pirate material.

Ukraine is obligated to provide effective monitoring of plant production and the licensing of new lines of production. In June 2000, the Joint Action Plan was announced in a joint statement issued by then-President Clinton and then-President Kuchma aimed at optical disc piracy enforcement. The Joint Action Plan consisted of three parts: (1) to close the illegal optical disc plants, to seize illegal material, and only to reopen the plants when there was 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 improve significantly the copyright law and to introduce other legal reforms, including criminal and administrative penalties, necessary to implement a modern copyright regime.

As noted, there are four steps that the Government of Ukraine must undertake to complete its implementation for proper optical disc production and distribution regulation. These are steps that the government is either not currently doing or not doing properly: (1) effective surprise plant inspections—the only means of effective plant production enforcement; (2) the issuance of SID codes upon proper verification at the time of issuance (with comprehensive and in-depth follow-up inspections and maintenance of codes on all equipment and molds and mirror blocks); (3) monitoring of equipment used at the plants in operation to make certain that source identification (SID) codes are in fact properly engraved on molds, matrices and all relevant equipment used in

the production of optical discs; and (4) creation of a database by the enforcement authorities to establish a complete and detailed inventory of the equipment used in the production of optical discs at the licensed plants.

It is estimated by the recording industry (the International Federation of the Phonographic Industry, IFPI) that the current total production capacity of optical media material is around 90 million units per year. The estimated demand for legitimate CDs in Ukraine is still less than one quarter of this total.

Three plants were inspected once each with IFPI and state inspectors present in 2005: the Rostok, ZMS Prod and Amitron plants. The CD Master plant was inspected twice with IFPI and state inspectors present. Two other plants, Media Park and Odyssey Disc (which opened in 2005 with a total capacity of at least 7.5 million discs per year), were inspected by Ukrainian officials in 2005, but these were undertaken in the absence of copyright owners (IFPI). However, both were separately visited by IFPI. The Government of Ukraine reports that, as of December, it was commencing “weekly” inspections of all the plants, but there was no indication that these would all be surprise inspections, which are necessary for effective enforcement. IFPI responded favorably to the government’s invitation to join the government in all of its future inspections. However, there have been to date no actual invitations to join inspections since that announcement. In fact, plant inspections have taken place without IFPI or other rightholders present. In addition, IFPI encourages the government to be more open and cooperative with the forensic evidence that it acquires during inspections. The failure of SDIP to disclose to the rightholders the evidence SDIP has obtained, and the conclusions it has reached, based on past raids has been a stumbling block to effective plant enforcement.

One misstep that has undercut effective enforcement was the adoption of the controversial Hologram Sticker law in 2000. The inconsistent and haphazard implementation of the Ukrainian hologram system (administered by the government) is seriously harming the interests of the legitimate copyright owners while it permits suspect companies to receive thousands of holograms for foreign releases (music, film, entertainment software) for which they have no licenses despite objections from the legitimate licensees. These holograms are ultimately found in the market on pirate products. The copyright industries are trying to compete against the pirates, even pricing their products lower (\$5 to \$7 per CD, for example; DVDs are \$20 compared to the pirate price of \$4) and printing materials in Cyrillic for local distribution. However, legitimate rightholders cannot compete against the pirates without effective enforcement by the Ukraine Government to stop piracy, and to stop the misuse of the hologram system. IIPA understands that SDIP is considering new regulations, which if adopted, are intended to prevent the fraudulent issuance of holograms.

Holograms stickers are frequently issued on the basis of false contracts, which are rarely verified. In such instances, pirate products are *de facto* authorized by the state for distribution. Such materials cannot be seized by law enforcement officials. Practice shows that one out of every two products seized is labeled with a false hologram (either counterfeit or with a reprinted title). In light of this, it is obvious that the hologram program is totally ineffective.

Entertainment software companies, among others, are experiencing problems with the hologram stickering program. An ESA member company reports that the stickering program is highly ineffective, as pirates are clearly able to obtain these stickers to affix to their pirated products. Though the SDIP has apparently agreed to stop issuing stickers or “control marks” for games that have the English titles or a direct translation of the title of that company’s products, it remains difficult to prevent the issuance of a sticker to a pirate that merely adopts a slight variation

in the title.³ The same company reports that though it only entered the market last year, it found that over 70 labels/stickers had already been issued for its entertainment software products—all to pirates selling illegal versions of their games. In addition, the pirates appear to have convinced the government that labels or stickers should be issued on a “genre” basis rather than just on a single title basis. This “genre” rather than per title labeling means that a slew of entertainment software gets the labels all at once, rather than having to meet the more rigorous application (and proof) requirements for a label for each particular title. With the widespread use of false documents to obtain “genre” stickers, pirates are not only obtaining these stickers, but are getting a toehold in the unauthorized distribution network within Ukraine and in neighboring countries.

The Business Software Alliance (BSA) also reports that the hologram stickering system is acting as a hurdle to legitimate businesses and has become an effective marketing tool for the pirates it was intended to thwart.

In 2003 the Ukrainian Ministry of Education and Science passed an “order” requiring the SDIP to organize a voluntary registry for software manufacturers and distributors in Ukraine. This registry was intended to contain the names of software manufacturers/distributors, data about their registration, location, and contact details as well as information about management, type of business activity and a short description of all software products manufactured/distributed. Under the order, all software manufacturers/distributors can obtain a certificate to verify their registration. For a fee, SDIP will provide users with information from this registry about a particular software manufacturer/distributor. The registry was intended to improve a level of copyright protection for computer programs and databases, as well as to provide information to the public regarding software manufacturers, distributors and licensing information. However, the BSA reports that the registry, to date, has not fulfilled its intended function to distinguish legal software manufacturers/distributors from illegal ones.

Broadcast television piracy also remains a major problem for the motion picture industry, especially with regard to regional broadcasts. There is also a large number of cable operators who transmit pirate and other product without authorization.

The business software industry (BSA) reports that there were some changes regarding software copyright enforcement in 2005. Specifically, Internet-based piracy increased, in particular, the resale of software in violation of licensing agreements (for example, software was obtained using privileged licenses for definite users and then resold to the public on the Internet). One company reported significant increases in sales of legal software products following the legislative improvements of the past few years. The company also reported that the numbers of new PCs sold with legal operating systems preinstalled (versus illegal operating systems hard disk loaded) has grown much faster than the PC market, indicating that at least this form of piracy may be decreasing.

Ineffective Criminal and Border Enforcement

Two additional key enforcement tools are needed: (1) efforts targeted at the criminal syndicates (and administrative remedies directed against smaller scale activities); and (2) strong border enforcement measures to stop the export and transshipment of illegal optical media.

³ As one example: the game “Need for Speed: Most Wanted” was issued a sticker, but the word “speed” was translated into Russian while the rest of the label was in English.

Criminal Enforcement

The copyright industries report that there have been some welcome raids conducted over the past year, but not enough action has been directed at large-scale commercial piracy. Further, there are too few deterrent prosecutions or sentences by the courts, which are often burdened by long delays. Also, there are still too few administrative actions against stores, kiosks and other street piracy. With some notable exceptions, virtually all of the reports of activity in 2004 and 2005 were directed against sellers and small-scale distributors, with the criminal gangs involved in organized large-scale piracy remaining largely unscathed.

In fact, as a result of the too-high threshold for criminal prosecution (i.e., material damage amounting to at least UAH 26,200/US\$5,210), most cases result in administrative actions. IPR-related offenses are hampered by procedural problems such as the use of expert evidence, and instead need to have clear sets of rules guiding procedure.

Provisions do exist in the Ukrainian criminal code (e.g., Article 28) to prosecute organized groups or criminal organizations, including those engaged in IPR offenses, but to date they have not been used for this purpose. The entertainment software industry notes that both Russian and Ukrainian organized criminal syndicates control distribution of pirated video game products in the country through their local affiliates, and are not being prosecuted under the criminal laws. In fact, pirated entertainment software products often bear the “marks” or “logos” of the criminal syndicate producing and distributing particular pirated product. The business software industry (BSA) reports that the criminal code is (albeit rarely) being applied to smaller groups of collaborating pirates, such as two individuals selling illegal software in a store. But overall, the criminal laws are not being more broadly applied to large-scale organizations, as is necessary to stem the levels of piracy.

The motion picture industry reports that over the last two years, there have been some encouraging signs of increased and geographically wider police activity, both in Kiev and elsewhere, against the retail sale and distribution of pirate products. For example, in April 2005 a massive operation called “Intellect,” with participation of many government departments and public anti-piracy organizations, resulted in the seizure of 217,724 pirate items valued at an estimated US\$600,000: 98,343 optical discs (DVDs, CD-Rs and CDs), 28,214 VHS cassettes and 91,167 audio cassettes. Administrative Code sanctions were applied against 1,014 individuals. Separate raids resulted in the seizure of significant quantities of pirate products and the discovery of CD-R/VHS duplicating laboratories.

A March 2005 raid by the Economic Crime Police, with the cooperation of the IFPI/MPA Kiev office, resulted in the seizure of 63 CD-R/DVD-R burners and thousands of blank and recorded CD-Rs (music, video, and games) and inlays. The raided lab was one of the suppliers of illegal product to wholesalers in Kiev and in other regions of Ukraine, and had previously been raided in 2004 but remained operational because of lack of evidence. Another raid by the same groups in May on a warehouse belonging to one of the biggest distributors of pirate optical discs in the Lugansk region netted over 53,000 pirate DVDs, over 43,000 CDs and over 16,000 inlays. Unfortunately, a similar raid undertaken a year earlier, in which about 100,000 DVDs and CDs were seized, was not followed by a criminal prosecution because the pirate had the support of the former regional administration.

Among other raids in 2005 were one in Kiev targeted against street vendors, pirate warehouses, and CD-R labs that resulted in the seizure of over 14,600 pirate DVDs and some 29,000 pirate CDs; one on a large pirate distribution warehouse in Khmel'nitsk city that resulted in

the seizure of 773 DVDs and 6,820 CDs, together with hundreds of VCDs and discs containing MP3s and software; and one on a warehouse in Lugansk that resulted in the seizure of 58,236 DVDs and 24,616 CDs imported from Russia.

It is common, unfortunately, for cases to end without deterrent penalties, and worse, for pirates to petition the court successfully to have illegal products returned to them. Here are two such examples. The first resulted from a final ruling on November 10, 2005 (*In re: Zhovtnevyi*) in the district court of Lugansk City. An Article 176 Criminal Code violation was dismissed and amnesty granted to the defendant, and pirated product consisting of 41,543 CDs and 45,785 DVDs (that was seized by the police) was returned to the defendant as his “personal” property. All claims by the rightholders for damages were dismissed. In the second example (*In re: Dzerzhinsky*) in the district court of Kharkiv City on December 12, 2005, a criminal proceeding under Article 203(1) of the Criminal Code (pertaining to the illegal distribution of optical discs) was dismissed and pirate product consisting of 6,200 DVDs and 800 CDs was returned to the defendant.

Border Enforcement

Ukraine has also failed to properly police its borders, which has resulted in wide-scale shipment from and transshipment of these materials through Ukraine, to other countries in Eastern and Central Europe—including Poland, Hungary, Lithuania, Romania and Slovakia, and other countries such as Israel. In fact, border enforcement is probably the weakest link in Ukraine’s enforcement regime, as it allows large-scale smuggling operations to move pirate product mainly produced in Russia into Ukraine for the local market or for shipment to other countries. The common trade regime among Russia, Ukraine, and Belarus will only exacerbate the border enforcement problems, putting additional pressure on neighboring countries. There have been some minor seizures by customs authorities of CDs and other materials over the past few years, but cooperation has been spotty and the activity has not been nearly enough to stem the flow.

One lingering border problem supposed to have been fixed in August 2005 has not been implemented yet. The 2005 optical disc law made it clear that SID coding for imported finished product (discs being imported into Ukraine) was not required. But, in January 2006, there have been complaints that border officials are preventing the importation of finished CDs without SID codes. The Government of Ukraine must properly implement this new law immediately.

The IFPI and MPA report that Ukrainian customs officials have demonstrated better cooperation for enforcement of IPR crimes at the border than in previous years. But, overall, much more needs to be done to improve border enforcement to the extent needed to have a real impact on cross-border trade in pirated goods. The Ukraine Government must devote more resources and show more willingness to enforce IPR crimes at the border. The motion picture industry (MPA), for example, reports that a lingering major piracy problem as a result of poor border enforcement remains the influx of pirated DVDs from Russia.

Customs officials were granted *ex officio* authority to properly conduct enforcement investigations (in amendments to the Customs Code effective January 1, 2004). With this *ex officio* authority customs officials can seize illegal material at the border without a court order. The police and other enforcement officials also reportedly have equivalent *ex officio* authority, but in practice they still depend on right holder complaints to commence investigations—this needs to be corrected. Without proper implementation of this clear authority on the part of police and border officials, and without proper confiscation of pirate materials (which IIPA understands can only constitutionally be undertaken by the courts), the problems will continue to worsen. Waiting for the

right holders to file complaints in each instance given the widespread scope of the illegal activity is a recipe for failure. Also, a statutory deficiency still exists because the Customs Code narrowed sanctions to only those activities meeting a “commercial purpose” threshold, which hampers effective enforcement (especially against the widespread cross-border suitcase trade in pirated goods).

Other Enforcement Issues

Article 203(1) of the Criminal Code was modified as part of the amendments adopted in August 2005. It is now no longer necessary for right holders to file complaints before the police can initiate criminal actions. Without proper implementation of this clear authority on the part of police and border officials, and without proper confiscation of pirate materials (which we understand can only constitutionally be undertaken by the courts), the problems will continue to worsen. Also, a statutory deficiency still exists because the Customs Code narrowed sanctions to only those activities meeting a “commercial purpose” threshold, which hampers effective enforcement (especially against the widespread cross-border suitcase trade in pirated goods).

In addition to enforcement against hard copy piracy, Ukraine enforcement officials must also begin actions against on-line piracy. It is estimated that there are over 400 ISPs in Ukraine and that over 150 of these support sites offering pirate DVDs (for on average US\$10).

In 2005, the recording industry continued to suffer from pirate optical disc (including CD-R) distribution with estimated piracy levels at around 60% for international repertoire, and losses estimated at \$30 million (including losses from the export of pirate product from Ukraine).

Pirate films continue to appear in Ukrainian kiosks within weeks of their U.S. theatrical release. Street kiosks sell pirate optical discs off the spindle and package them on the spot. Video retail stores stock pirate product, including pre-release material that is available within days of U.S. theatrical release.

Pirated entertainment software products continue to be exported from and through Ukraine (from Russia). ESA member companies report that optical discs containing pirated entertainment software are now being produced in Ukraine for sale both locally and for export. Several thousand pirated video game products, sourced from the Ukraine, have been seized in foreign countries (including Israel and Lithuania). There have also been some shipments to the U.S. which though of some regularity, are always in low quantities – an apparently deliberate move by the pirates to avoid detection as well as enforcement action. Many are shipped with fake documentation claiming that the shipper has the appropriate licenses for the products shipped. The pirated video games also bear the “marks” or “logos” of the pirate operation which is producing and distributing the pirated games. It appears that both Ukrainian and Russian syndicates are operating in the country, and have adopted the practice of “branding” their pirated products. Forensics identification information indicates that these pirate entertainment software discs are being made in well known factories in Ukraine.

BSA reports (and appreciates) good cooperation with the State Department of Intellectual Property (SDIP) in improving IPR awareness (helping legitimate sales), and reducing software piracy rates. SDIP has coordinated special IPR events including press briefings, practical training programs for law enforcement and other government officials, and projects regarding needed legislative amendments.

The Ukraine law enforcement officials reported the following: in 2005, there was a total of 483 criminal IPR cases opened (compared with 455 in 2004, and 374 cases in 2003). Of these, 298 cases were Article 176 cases (52%). The figures for 2004 and 2003 were 311 and 297 cases, respectively. There were 115 Article 203(1) cases involving the illegal circulation of optical discs—new provisions adopted in July 2005. These involved music, video and software games.

Further, the SDIP reported the Government of Ukraine seized a total of 850,000 items in 2005, compared with 600,000 in 2004 and 300,000 in 2003. A total of 100,000 items were destroyed in 2005, compared with 70,000 and 80,000 respectively in 2004 and 2003. There were 5,100 administrative cases undertaken in 2005, compared with 4,300 in 2004 and 2,000 in 2003.

The Tax Police seized a total of 280,000 items (including 60,000 discs) in 2005. In 2004, they seized 340,000 items (including 150,000 discs); in 2003, they seized 200,000 (including just 5,000 discs). The Customs authorities reported 350,000 discs seized compared with 100,000 in 2004 and just 34,411 in 2003. The State Inspectors (in all 16 regions) reported 400,000 discs and tapes seized, 100,000 destroyed, 450 administrative protocols, and 100 criminal cases opened. The figures for 2004 were 270,000 items seized, 40,000 destroyed, 390 administrative protocols, and 58 criminal cases opened. In 2003, the figures were 50,000 items seized, 25,000 destroyed, 110 administrative protocols, and 40 criminal cases opened.

The business software industry (BSA) reports significant improvements in its relations with the Ministry of Internal Affairs, in addition to good national police cooperation, although relationships with local police departments remained the same. The sum total of activities included 165 police raids; 112 criminal proceedings; 53 administrative proceedings; and 20 civil proceedings. In most cases raids were taken *ex officio* by the police. Most police enforcement activities were directed against CD pirates. Other forms of piracy were almost “untouchable”—IIPA and BSA urge the police to broaden their focus from CD piracy actions to include actions against PC manufacturers and corporate end-users. Last, the police must act not only against small resellers and end-users but against organized crime operations. One note of success was the sweeps that began in July 2005 against stalls in a well known flea market (making it difficult today to find pirated CDs, especially including Microsoft® business software at this and other flea markets in the largest cities). At present, there does not appear to be much pirated business software material (on CDs) in retail chains.

History of GSP Petition

As a result of Ukraine’s serious optical disc piracy problem, the IIPA filed a petition on June 16, 1999 to request the withdrawal or suspension of Ukraine’s GSP benefits. That petition was accepted by the U.S. Government on February 14, 2000; in support of that petition IIPA testified at a public hearing on May 12, 2000. The U.S. Government suspended Ukraine’s GSP benefits on August 24, 2001. On August 8, 2005, the IIPA requested that the suspension remain in place (i.e., that the automatic 4-year sunset provisions not take effect) in a letter to Mr. William Burris, Chairman, Section 301 Committee.

After Ukraine’s adoption of the optical disc law in August 2005, the U.S. Government announced on August 31, 2005 that it was terminating the 100% *ad valorem* duties that had been in place since January 2002 on Ukrainian exports. It then announced an out-of-cycle review in October 2005, which concluded in January 2006. Effective on January 23, 2006, the U.S. Government announced that it was lowering the designation of Ukraine from a Priority Foreign

Country to placement on the Priority Watch List; coupled with that designation, the U.S. Government also announced, effective on January 23rd, the reinstatement of GSP benefits for Ukraine.

LEGAL REFORMS

A history of the key legal reforms made by Ukraine in the past few years is available on the IIPA website at <http://www.iipa.com>.

The key missing legal reforms needed for effective enforcement (and TRIPS compliance) are: (1) amendments to the criminal procedure code; (2) amendments to the customs code (the customs code revision, effective January 1, 2004, did not repeal the restrictive “commercial purpose” threshold or the onerous registration and fee requirements for IP-related materials); and (3) the addition of key administrative remedies. The law of 2003 included in the Civil Procedure and Commercial Procedure Codes *ex parte* search provisions necessary for effective end-user (software) piracy actions. In 2004, the Highest Commercial Court of Ukraine adopted recommendations to implement these procedures. However, practical difficulties remain, most critically, the inability of the authorized enforcement agency (the state executive service) to actually undertake *ex parte* searches in spite of the new civil procedure code (since the civil code does not apply to administrative remedies).

Copyright Law: The Copyright Law of 2001 fixed a major deficiency of the old law, namely, the protection for pre-existing works and sound recordings. Several problematic provisions in the 2001 law were never corrected, such as Article 43.3; this provision permits the over-regulation and consolidation of power into government collecting rights societies. The Ukrainian Cabinet of Ministers has, under this provision, adopted fixed tariffs for the broadcasting of sound recordings, which totally undermines the right of phonogram producers to freely negotiate their fees with users. Article 43.3 of the Copyright Act should be deleted and the tariff decision by the Council of Ministers should be withdrawn. Collective management should be a private, not a government, enterprise; legal entities and foreign rightholders should be permitted to be members on their own in Ukrainian collecting rights societies. In addition, as noted below, Ukraine must further revise the Copyright Law to fully comply with the digital treaties in order to properly protect the production and dissemination of materials on digital networks.

The Government of Ukraine is currently considering major copyright law reform. The current draft bill, prepared for Inter-Ministerial review, over-regulates the collective management of rights and includes unwarranted government intervention in the exploitation of copyrights, to mention two of the many shortcomings of this draft bill. The Government of Ukraine should consult with right holders and international copyright experts before moving forward with this legislation, to simplify the provisions and to ultimately make its law compatible with international norms and business practices.

Criminal Code and Criminal Procedure Code: The criminal code was completely revised in 2001, and further revised in 2003. Article 176 now provides sanctions including fines ranging from 200 to 1000 minimum tax-free incomes, approximately US\$640 to US\$3,200, (up from 100 to 400 times), or correctional labor for a term of up to two years, or imprisonment for a term of up to two years with confiscation of infringing material. The threshold for criminal liability is met when material damage caused by an infringement equals or exceeds 200 minimum tax-free incomes (i.e., “substantial material damage”). The sanctions provide an increase for repeat offenders and cases where the material damage equals or exceeds 1,000 minimum tax-free incomes (i.e., “very substantial material damage”), such as for officials abusing their “official positions.” In those cases

finances can reach up to 1,000 to 2,000 times the minimum tax-free incomes (previously it was 500 to 1,000 times), which is the equivalent of US\$3,200 to \$6,400; the term of imprisonment ranges from two up to five years. A new system for the twice-a-year calculation of minimum tax-free incomes entered into force in January 2004, applicable to the Article 176 provisions. In 2005, the minimum monthly wage was UAH 262 (US\$49.31) for purposes of the threshold calculation applied to actual fines; however, the minimum tax-free income of UAH 17 (US\$3.20) is also applied in other calculations (making it very confusing to apply). The criminal code provisions sanction both copyright and neighboring rights violations.

In general, the criminal penalties can only be imposed for “substantial material damage,” which creates a threshold that is too high to commence a criminal copyright piracy case. Before January 2004 the threshold was UAH 3,400 (US\$640). But the thresholds rose as follows: in November 2004, the threshold was UAH 14,220 (US\$2,676) and on January 2005, it rose to not less than UAH 26,200 (US\$4,931). This year, it will rise to UAH 45,120 (approximately US\$8,492). If the value of seized illegal product is below the threshold there is no criminal responsibility, only administrative fines (usually very minor). Obviously, there has been a substantial increase in the threshold for activities to qualify as a crime, which is a problem for two reasons: (1) the level is too high (and getting higher); and (2) it is a very difficult threshold to prove with the certainty necessary for criminal proceedings. Activities that fall below the threshold can be sanctioned by the much weaker administrative offenses code. Even though these are far short of deterrent sanctions, if properly implemented and prosecuted, those penalties can provide some relief for certain low-level offenses. In sum, the criminal code needs to be amended to provide a lower and clearer threshold to instigate a criminal action. IIPA recommends a threshold no higher than the equivalent of 50 times the minimum daily wage or some other low and clear threshold. Not only would this help to identify criminal infringing acts for prosecutors, it would also 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. Amendments to consider lowering the threshold were considered but never adopted in November 2005. IIPA urges the government to reconsider this issue in 2006.

Another missing element in the criminal code (or copyright law) is a provision that makes the possession for commercial purpose of illegal copies of works or sound recordings a criminal offense; the Government of Ukraine should introduce and push for the passage of such a provision.

The Criminal Procedure Code must also be fixed in law and practice so that police can act *ex officio* to initiate criminal intellectual property cases. Ukrainian criminal procedures in practice (although not required by the code) currently require right holders to file complaints to initiate actions. This acts as a bottleneck to successful enforcement. The procedure code should be changed so that police initiate intellectual property criminal cases and investigations for submission to the court; it must also be clear that the police (as they sometimes do in software cases) have the authority to hold confiscated products and equipment for use at trial.

WIPO Digital Treaties: In 2001, Ukraine acceded to the two digital treaties—the WIPO Copyright Treaty (WCT) and the WIPO Performances and Phonogram Treaty (WPPT). The Copyright Law of 2001 included amendments intended to implement these treaties. Unfortunately, the amendments fell short of complete and effective implementation, especially with regard to technological protection measures (requiring proof of “intentional” circumvention, which could prove a major impediment to protection). Ukraine needs to fully implement the treaties with amendments to its copyright law.

Administrative Remedies: As part of the Joint Action Plan in 2000, Ukraine agreed to adopt and implement appropriate administrative remedies to deter piracy as well to enact criminal penalties. IIPA understands that the proper remedies exist but are not being used effectively to remove the business licenses of infringing retail stores, kiosks, and other smaller scale pirates. Administrative remedies must be properly implemented alongside available and properly implemented criminal penalties at levels sufficient to deter piracy.

Customs Code: The Customs Code of Ukraine (Law No. 92-IV, “On Amending the Customs Code of Ukraine”) entered into force on January 1, 2004. It provides clear *ex officio* authority (Art. 257) to customs officials to seize suspected illegal material at the border, thus closing a major legal loophole in the enforcement regime of Ukraine. Unfortunately, the new Customs Code narrowed the sanctions (permissible under the old code) to those meeting a “commercial purpose” threshold; this limits the effectiveness of the new code. In addition, the notification and registration requirements, and the fees were not repealed by the new law. They should be abolished; these provisions act as a bar to effective border enforcement action by causing a confusing maze of unnecessary regulation.

Civil Code: A new civil code came into force on January 1, 2004—Chapter IV of the Civil Code (Intellectual Property Rights) contains 90 articles in total, 15 in the section on copyright, and 8 pertaining to neighboring rights. Most of the copyright and neighboring rights provisions duplicate provisions in the Copyright Law of 2001, setting up the possibility of confusion, especially for judges who need to provide effective IPR enforcement. IIPA had urged that civil code reform exclude anything but passing reference to copyright and neighboring rights because of fears that duplicate provisions would jeopardize effective application of the copyright law (and breach the bilateral trade agreement). Experts in Ukraine report that the 2004 civil code provisions, since they duplicate the copyright law ones and do not contradict them, will not weaken implementation or enforcement of the copyright law. IIPA urges the enforcement agencies and the judiciary in Ukraine to rely on the copyright law, not the Civil Code Chapter IV, for effective enforcement.

Dubbing Law: Amendments to a draft media law have been introduced in the Parliament that would call for mandatory dubbing in Ukrainian for films shown in cinemas and on television. If these, or similar, amendments were to be adopted, they would have a significant impact on audiovisual market development, particularly for MPA member companies and other foreign companies in the Ukraine.

Government Software Asset Management: In September 2003, the Cabinet of Ministers of the Ukrainian Government passed a regulation establishing procedures for the use of software in government agencies. It provides (among other things) for government institutions to use properly licensed and legally held software, and prohibits public servants from installing, using, or copying software without prior consultation with a responsible system administrator. In March 2004, the government issued a new regulation to implement legalization. It assigned all procurement authority for software products to a single entity, SDIP, in order to try to eliminate the use of pirated software products in the public sector. BSA reported substantial progress and cooperation on the legalization of government software in 2005. These encouraging efforts by the Government of Ukraine provide a positive example for the private sector. In addition to the software legalization program, the government created separate budgets for legalization funds in the state budget for various government agencies; this plan was approved by the Ukrainian Parliament. Separately, the BSA reported similar developments in the commercial sector. For example, the Association of Ukrainian Banks created a special program for software legalization to reduce the level of unlicensed software use within the financial sector.

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