

**Ukraine: A Strategy to Seek Elimination of US Trade  
Sanctions and to Attract Additional FDI through Improvement  
of the IPR Protection Regime**

MASTER'S PROJECT

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## **Scenario**

For the purpose of this project, I am assuming the role of a consultant to the Ukrainian Association of Manufacturers and Entrepreneurs (UAME).

The intended audience of the project is the top management of the Association and representatives from corporate members.

## **Issue**

Since 2001 trade relations between the United States and Ukraine have deteriorated dramatically. The main reason for such deterioration is the dissatisfaction of the US government with the progress of development of the intellectual property rights (IPR) protection regime in Ukraine. In March 2001, Ukraine was designated a Priority Foreign Country under Section 182 ("Special 301") of the US Trade Act of 1974, as amended. In August 2001, Ukraine lost its Generalized System of Preferences (GSP) beneficiary status. In January 2002, the US imposed prohibitive tariffs on Ukrainian exports worth \$75 million. Not only do the trade sanctions have an adverse effect on Ukraine's economy, but they also create a poor image of the country thus blocking FDI inflows and threatening the country's accession to the World Trade Organization (WTO).

## **Executive Summary**

An inadequate IPR protection regime in Ukraine primarily affects US music and movie industries, or at least these are the two industries that have been the most vocal in expressing their concerns. Therefore, this project, both in its analytical and strategy parts, focuses on IPR issues as they relate to these industries.

This project consists of eight sections. The Background section focuses on the development of diplomatic relations between Ukraine and the US in general, and trade relations in particular. The Legal Analysis section looks at the development of the legal framework for IPR protection in Ukraine and analyzes the conformity of this framework with international norms as they are presented in the World Intellectual Property Organization (WIPO) Conventions and WTO TRIPS Agreement. On the other hand, this section also looks at the US Generalized System of Preferences (GSP) and Section 182 ("Special 301") of the US Trade Act of 1974, as amended, to determine the legal basis for removing trade benefits from and imposing trade sanctions on Ukraine due to its IPR violations.

The Diplomatic Relations Analysis section looks beyond the scope of trade relations between the two countries by examining how deteriorating trade relations fit the broader picture of US-Ukraine worsening diplomatic relations. In addition, a long-term goal of Ukraine to accede to the WTO and the US position on Ukraine's accession are analyzed here.

The Public Policy Analysis section analyzes the challenges that Ukraine faces in its attempts to enforce adequate IPR protection in the country without aggravating such problems as unemployment and cultural and economic development.

The Public Opinion Analysis section analyzes the public opinions of Ukrainians about intellectual property rights and the challenges that may arise during an effort to sway these opinions.

The Political Analysis section looks at both the US and Ukrainian stakeholders and tries to determine their interests in the issue of IPR protection in Ukraine and how it affects them.

The Economic Analysis section estimates the effect of lost GSP benefits and increased tariffs on Ukraine's exports to the US. An attempt is made to estimate the negative impact of trade sanctions on metallurgical, chemical, and footwear industries, the three Ukrainian industries that export the most to the US.

The Strategy section provides recommendations, goals and objectives of the UAME as well as strategic steps and the timeline for the UAME to achieve these objectives.

## **Background**

**US-Ukraine Diplomatic Relations: Development.** Ukraine became an independent nation state on August 24, 1991, and was recognized as such by the United States of America on December 25, 1991. Since then the US has viewed Ukraine as its strategic ally, "a vital buffer between Russia and the West" [1].

At that point, good diplomatic relations between the two countries were based on the US government support for economic, political and social reforms that the government of Ukraine was determined to implement. The relations further improved with Ukraine's decision to become a non-nuclear weapons state in 1994 and transfer nuclear weapons left on its territory after the split-up of the Soviet Union to Russia. Under the Cooperative Reduction (also called Nunn-Lugar) Program, Ukraine received hundreds of millions of dollars in aid to dismantle its nuclear arsenals [2].

To assist Ukraine in its development and transition to a market economy, the US provided financial aid through various channels. The US State Department Background Note identifies some of the most significant ones.

In October 1992, the Freedom for Russia and Emerging Eurasian Democracies and Open Markets (FREEDOM) Support Act (FSA) was enacted. US assistance "to support Ukraine's transition to a market economy... has focused primarily on economic restructuring, development of the private sector, and energy-sector reform. US assistance priorities for Ukraine have included enterprise development, deregulation,

macroeconomic reform, civil society development, community-based programs and nuclear safety” [2]. In January 1994 President Clinton announced establishment of the Western NIS Enterprise Fund (WNISEF) to promote development of the private sector in Belarus, Moldova and Ukraine. In 1999 alone, the Fund provided financing to 22 companies in the amount of \$74 million [2].

Assistance to Ukraine in the areas of democratic and social sector development has been primarily administered through the United States Agency for International Development (USAID). Support has been provided for “programs on participatory political systems, independent media, rule of law, local governance, and civil society, as well as a wide range of exchanges and training” [2]. Additional training and technical assistance is channeled to “Ukrainian institutions and government agencies on reforms of health care financing and delivery of medical services” [2]. Extensive humanitarian assistance to targeted groups of Ukrainian society has also been provided over the course of the years.

These and many other US assistance programs made Ukraine the fourth largest recipient of US aid [3]. However, diplomatic relations between the US and Ukraine has undergone a dramatic change during the last two years. The analysis and implications of this change are provided in the Political Analysis section of this project.

**US-Ukraine Trade Relations: Development.** Trade Relations between the United States and Ukraine are governed by the “Agreement of Trade Relations between the United States of America and Ukraine,” which took effect on June 18, 1992. Under the agreement, both countries granted one another Most Favored Nation (MFN) treatment. Article VIII of the Agreement provides for protection of intellectual property rights by requiring the parties to the Agreement to enact and implement adequate IPR protection laws.

The following table summarizes US-Ukraine trade flows from 1998 to 2001.

**Table 1. Trade flows between the US and Ukraine, in US\$ million**

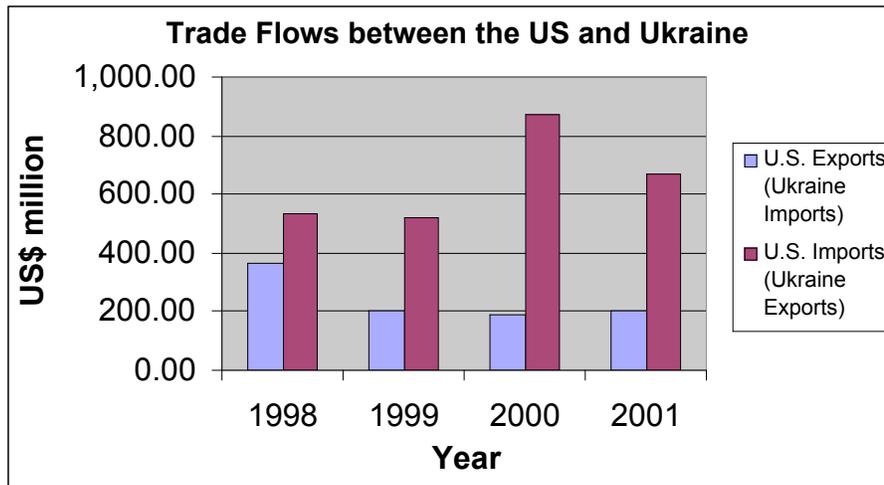
	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>
<b>US Exports (Ukraine Imports)</b>	367.55	204.22	186.18	205.14
<b>US Imports (Ukraine Exports)</b>	530.69	517.79	872.99	670.05
<b>Total Trade Turnover</b>	<b>898.24</b>	<b>722.01</b>	<b>1059.17</b>	<b>875.19</b>

**Source: US Census Bureau, Foreign Trade Division, Data Dissemination Branch.**

The trend for trade flows between the two countries has been such that Ukraine’s exports to the US have grown by 26% while Ukraine’s imports from the US have declined by 44%. This trend in the direction of trade flows led to Ukraine’s inability to maintain trade surplus with the US for every year from 1998 to 2001. The graphical representation of the trade flows between the two countries is presented below in Chart 1.

According to the recent Fact Sheet on Ukraine, prepared by the Business Information Service for the Newly Independent States (BISNIS) of the US Department of Commerce, US Exports to Ukraine in 2001 primarily consisted of “steam turbines, generators, other industrial machinery; charitable items, donated medicinal and pharmaceutical products; tobacco; optics, medic and surgical instruments; computer components, office machine parts; centrifuge filters; sound generating equipment; radio and telecommunication equipment; commercial trucks, passenger cars, auto parts; organic cleaning chemicals; books, magazines; tube, pipe, and seamless steel items; plastic plates, sheets, film items; aircraft parts and components; and synthetic textiles” [4].

**Chart 1. Trade Flows between the US and Ukraine**



US imports from Ukraine in 2001 were mainly composed of “iron and steel products such as pig iron or non-alloy steel, bars, rods, and irregular coil...; inorganic chemicals, and rare earth metals, woven apparel, aluminum, spacecraft, launch vehicles, powered aircraft, salt, sulfur, earth and stone, and cement” [4].

As of October 1, 2002, the US has remained the leading source of foreign direct investment (FDI) with \$843.4 million invested. This represents 17.1% of total FDI in Ukraine since 1992, which The State Committee of Statistics of Ukraine estimates at \$4,923.1 million [5]. Unfortunately, FDI inflow to Ukraine is far below its potential level, primarily due to administrative corruption. US Foreign Commercial Service 2002 Country Commercial Guide on Ukraine notes that “growth in FDI in Ukraine has been very slow, and remains insignificantly small for a country of nearly 50 million people with the resource base and economic potential of Ukraine. In comparison, foreign direct investment in Poland since 1991 has been about \$40 billion, of which more than \$6 billion stems from American investors. Foreign direct investment in Hungary has been over \$20 billion during the same period, despite the fact that Hungary’s population is only a fifth the size of Ukraine’s” [6]. It is obvious that Ukraine can offer a lot of opportunities for US investors, but those opportunities have been underutilized so far.

**US-Ukraine Diplomatic Relations: Current State of Affairs.** Unfortunately, the negative trend in the US-Ukraine trade relations matches the recent negative trend in overall US-Ukraine diplomatic relations. The US has long been dissatisfied with the high level of corruption in Ukraine. According to the 2002 Corruption Perception Index (CPI), published by Transparency International, Ukraine ranked 85<sup>th</sup> out of 102 countries with the score of 2.4 (with the highest score of 9.7 by Finland, meaning the least corrupt country; and the lowest score of 1.2 by Bangladesh, meaning the most corrupt country) [7]. The international community, and the US in particular, is increasingly dissatisfied with the state capture corruption in Ukraine. US Foreign Commercial Service 2002 Country Commercial Guide for Ukraine quotes the World Bank's definition of state capture corruption as "occurring when politically influential individuals or groups use their power to appropriate for themselves sections of the economy." The Guide further describes state capture corruption in Ukraine, "where a group commonly referred to as 'oligarchs' control a significant portion of the economy, particularly in the spheres of mass media, energy and heavy industries such as steel and chemicals. Many of these oligarchs enjoy immunity from prosecution thanks to their seats in the Rada (parliament)" [6].

US dissatisfaction with Ukraine's corruption reached yet another level after a so-called "cassette scandal," when the former presidential bodyguard, Mykola Melnichenko, released the secretly recorded conversations of President Kuchma with his subordinates. On one of the tapes, "he [President Kuchma] is apparently heard telling a government minister to 'deal with' a troublesome journalist, Georgiy Gongadze" [10]. According to the U.S State Department Spokesman Richard Boucher, as quoted in Washington Times, on another tape "Ukrainian President Leonid Kuchma is heard approving the clandestine sale of 'Kolchuga' early warning system to Iraq, and we believe this recording to be authentic" [13].

With the Ukrainian President facing such serious accusations, Ukraine becomes more isolated from the US As BBC News Online observes, "top-level US-Ukrainian meetings were a regular occurrence until the tapes were leaked, then they were abruptly stopped" [10]. Something else that was "abruptly stopped" following allegations of the Ukrainian President's approval of the sale to Iraq was "approximately \$54 million in aid for government, legal and regulatory reform" [13]. Under the circumstances, it is obvious that US foreign policy towards Ukraine is not focused on trade sanctions, which makes it more difficult for Ukraine to communicate improvements in its IPR protection regime to the US. With US government aid cut, it will also be more difficult for Ukraine to achieve such improvements. A more detailed analysis of US diplomatic relations with Ukraine is provided in the US-Ukraine Diplomatic Relations Analysis of the project.

**US-Ukraine Trade Relations: Current State of Affairs.** US Copyright industries have long complained about IPR violations taking place in Ukraine. One of the press releases of the United State's Trade Representative (USTR) noted that "Ukraine is the largest producer and exporter of pirated optical media products in Europe, according to US recording industries" [11]. The International Intellectual Property Alliance estimated losses to just three of its members due to copyright violations in optical media production

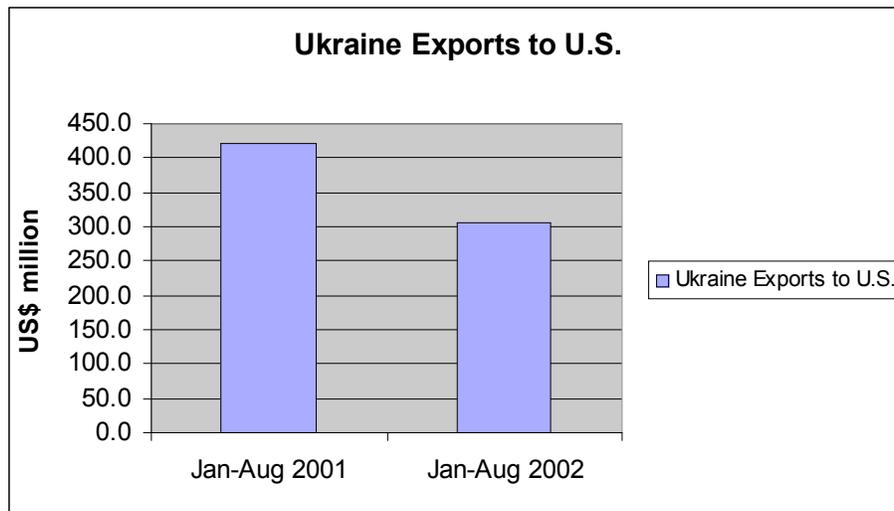
in Ukraine at \$216.8 million in 2000: “the Recording Industry [Association] of America (RIAA) estimated \$160 million in losses; the Motion Picture Association of America (MPAA) estimated \$40 million in losses; and the Business Software Alliance (BSA) estimated its US company losses were \$16.8 million in 2000” [9, p.6].

Even though the \$216.8 million figure is quite high, it is less than 0.05% of the US core copyright industries production in 2000. According to the IIPA, “the core copyright industries accounted for \$457.2 billion in value added to the US economy, or approximately 4.9% of the Gross Domestic Product (GDP) in 1999” [8].

Although the loss due to IPR violations in Ukraine constitutes such a small percentage of US copyright industries' output, these industries were able to successfully exercise their power and influence as a lobbying group to convince the USTR to take serious actions against Ukraine. Dissatisfied with Ukraine's legal framework for IPR protection, on March 12, 2001 the USTR identified Ukraine as a Priority Foreign Country under Section 182 (“Special 301”) of the Trade Act of 1974, as amended. On August 7<sup>th</sup>, 2001 Ukraine lost its GSP beneficiary status [11]. Effective January 23, 2002 the USTR imposed 100% *ad valorem* tariffs on imports from Ukraine worth \$75 million [15\*]. US trade sanctions primarily targeted Ukraine's mineral and chemical industries (imports under Harmonized Tariff Schedule (HTS) categories 27, 28 and 32 comprised over 35% of all US imports from Ukraine in 2001) [19]. US revocation of Ukraine's GSP beneficiary status has also injured Ukrainian steel exporters as they now face recent tariffs of up to 30% on steel products. US actions seriously jeopardize Ukraine's chances to maintain its economic development with its more developed neighbors, such as Poland, Latvia, Lithuania, Estonia and Czech Republic, who hope to accede to the EU in 2004, yet for the time being remain US GSP beneficiaries and, therefore, continue to enjoy duty-free treatment of their exports [12].

Not surprisingly, following revocation of GSP beneficiary status and imposition of sanctions, Ukraine's total exports to the US have decreased by 27% from \$421.3 million in January-August 2001 to \$304.5 million in January-August 2002 [19].

A detailed analysis of the US trade sanctions on Ukraine's exports to the US is provided in the Economic Analysis section of this project.

**Chart 2. Ukraine's Exports to the US.**

### **Legal Analysis**

The Legal Analysis section of this project is a very important one, as it is the deficiencies of Ukraine's legal framework for protecting intellectual property rights that caused the US trade sanctions. It is worth noting at the beginning of the analysis that experts believe that Ukraine has been quite successful in taking decisive steps to bring its IPR legal framework closer to international standards: "Ukraine has come a long way in its efforts to establish a sound, long-term legal basis for IPR protection, and has achieved unprecedented progress compared to other CIS countries" [28].

#### **Ukraine's Domestic Legislation**

**Constitution of Ukraine.** New Constitution of Ukraine was adopted by Ukrainian Parliament on June 28, 1996. Article 54 of the Constitution provides for the protection of intellectual property rights and prohibits violation of these rights. The article reads:

- Citizens are guaranteed the freedom of literary, artistic, scientific and technical creativity, protection of intellectual property, their copyrights, moral and material interests that arise with regard to various types of intellectual activity.
- Every citizen has the right to the results of his or her intellectual, creative activity; no one shall use or distribute them without his or her consent, with the exceptions established by law.

Having such an article in the Constitution of Ukraine is essential as the article establishes the legal concept of intellectual property and the rights to it in the document that is the basis of the entire legal framework of the country.

US trade sanctions and international pressure on Ukraine to improve its IPR regime have recently brought about significant positive additions and changes in Ukraine's legal framework. Among the most important ones are:

1. Amendments to the Law of Ukraine “On Copyright and Neighboring Rights.”
2. Law of Ukraine “On the Specifics of the Government Regulation of the Activity of the Subjects of Economic Activity Associated with the Manufacture, Export and Import of Laser-Readable Discs.”
3. Addition of Article 203<sup>1</sup> to the Criminal Code of Ukraine.
4. Addition of Article 164<sup>13</sup> to the Administrative Violations Code of Ukraine.
5. Amendment of Article 116-1 of the Customs Code of Ukraine, which increased penalties for violations of IPR as they relate to import and export.

**Law of Ukraine “On Copyright and Neighboring Rights”.** Original Law of Ukraine “On Copyright and Neighboring Rights” was adopted by Ukrainian Parliament in 1994. However, under the pressure coming from the international community and mainly the US, the Law was significantly amended and received a new wording on July 11, 2001. This Law further defines the concepts of intellectual property rights, copyright, neighboring rights, and right holders.

Main concerns of the international IPR community were addressed in the following articles. Article 15 establishes protection of proprietary rights of an Author. Paragraph 1 reads:

The Proprietary rights of an author (or other copyright holder) shall include:

- a) the exclusive right to use a work;
- b) the exclusive right to allow or prohibit the use of a work by other persons.

Paragraph 3 further explains:

The exclusive right of an author (or other copyright holder) to allow or prohibit the use of a work by other persons shall entitle him to allow or prohibit:

- 1) reproduction of works;
- 2) public performance and broadcast of works;
- 3) public demonstration and public display;
- ...
- 11) import of specimens of a work [20].

Thus, Article 15 establishes legal protection of essentially all proprietary rights of authors. Article 18 addresses protection of computer software as literary works and reads:

Computer software shall be protected as literary works. Such a protection shall cover computer software irrespective of the method or form of its expression [20].

Article 39 establishes legal protection of performers' proprietary rights (neighboring rights). Article 40 addresses concerns of international copyright industries and establishes protection for proprietary rights of manufacturers of sound and video recordings. Article 40 (1) reads:

The proprietary rights of manufacturers of phonograms and manufacturers of videograms shall include their exclusive right to use their phonograms, videograms and the exclusive right to permit or prohibit other persons from taking the following actions:

- a) reproduction (direct and (or) indirect) of their phonograms and videograms in any form and by any method;
- b) distribution among the public of phonograms, videograms and specimens thereof through first sale or other title transfer;
- c) commercial rental of phonograms, videograms and specimen thereof, even after they have been distributed by a manufacturer of a phonogram or videogram with their permission... [20]

Article 50 is quite important as it defines copyright and neighboring rights infringements that provide a basis for legal action. In particular, subparagraphs b and e read:

- b) piracy in the sphere of copyright and (or) neighboring rights – publication, reproduction, importation into the customs territory of Ukraine, exportation from the customs territory of Ukraine, and distribution of counterfeit specimens of works (including computer software and databases), phonograms, videograms and broadcast organization programs;
- e) actions that pose a threat of infringement or copyright and (or) neighboring rights [20].

Article 52 specifies what remedies may be sought by copyright or neighboring right holders in case their rights are infringed. Article 52, paragraph 1 reads:

In case of a violation, by any person, of a copyright and (or) neighboring rights... or for the creation of threat of unlawful use of objects of copyright and (or) neighboring rights... persons holding copyright and (or) neighboring rights shall have the right:

- b) to lodge claims with a court of law (arbitrazh court) requiring renewal of the infringed rights and (or) the termination of actions infringing copyright and (or) neighboring rights or posing a threat of their violation;
- d) to lodge claims requiring reimbursement of losses (material damage), including lost profit, or collection of the income derived by the infringer as a result of his violation of copyright and (or) neighboring rights, or payment of compensation;
- f) to participate in the inspection of the production premises, storage facilities, technological processes and business operations relating to the production of specimens of works, phonograms and videograms with respect to which there are grounds to suspect violation or threat of violation of copyright and (or) neighboring rights... [20]

The Law of Ukraine “On Copyright and Neighboring Rights,” as was mentioned above, is considered a significant step forward in improving Ukraine’s legal framework

for IPR protection. The Law protects the rights of copyright and neighboring right holders by clearly specifying their rights, actions that are considered right violations and the protective measures available to right holders in case their rights are infringed. This is a very important step for Ukraine's legal framework, taking into account the relatively young age of IPR concept in Ukraine, even though this Law does not specify the government involvement in copyright and neighboring rights protection. The deficiency of the Law is that while the copyright holder is given the right to sue copyright violators, under this Law it is the responsibility of the copyright holder to monitor and identify violators. Most international treaties on IPR to which Ukraine is a party require governments to be actively involved in monitoring, identifying and preventing IPR infringements. This deficiency was addressed in a later Law, discussed below.

**Law of Ukraine “On the Specifics of the Government Regulation of the Activity of Subjects of Economic Activity Associated with the Manufacture, Export and Import of Laser-Readable Discs.”** This Law, also referred to as “Optical Disc Law,” was adopted by Ukrainian Parliament on January 17, 2002. It addresses some of the concerns of US copyright industries regarding lack of government involvement in optical media production. Before analyzing it further, it is worth noting a deficiency that stems from the very title of the Law. While the Law regulates production, export and import of optical media, it incidentally or deliberately ignores distribution. This is a severe deficiency and is a step back from the previously analyzed Law “on Copyright and Neighboring Rights” which, in its definition of piracy in the area of copyright and neighboring rights includes the word “distribution” (Article 50 (b)). Distribution is a major component of piratical activities and should be effectively regulated by this Law. An amendment to the title, text and the scope of application of the Law should be made, which should include the word “distribution” in addition to “manufacture, export and import.”

The Law establishes the regulatory system for the government of Ukraine to enforce copyright and neighboring rights, to monitor, identify and prevent copyright infringements. Article 3(1) provides that

Manufacture of laser-readable discs shall be carried out by subjects of economic activity only if they have a license for this activity [21].

Article 4 requires that

A manufacturer that shall have obtained a license to manufacture laser-readable discs shall:

- e) manufacture laser-readable discs containing objects of copyright and/or neighboring rights only with the authorization of persons holding copyright or neighboring rights [21].

Article 4(2) provides for the right of copyright and neighboring right holders to obtain official information from the licensing body, which “shall provide a written

response to any inquiry concerning the manufacture, export and import of laser-readable discs containing the respective objects of copyright and/or neighboring rights” [21].

Article 6 allows for “unscheduled (surprise) inspections... [to] be conducted without prior notice to the subject of economic activity, also upon a written application to the licensing body from the holders of copyright and/or neighboring rights concerning the violation of their rights” [21].

Article 7 and 9 identify some of the measures that may be taken to terminate copyright violations. Subparagraphs 1,2,3 and 4 of Article 9(1) read:

- 1) the restriction or temporary suspension of the operations of subjects of economic activity...
- 2) the cancellation of the license to manufacture, export or import laser-readable discs, or to export or import equipment or raw materials for their manufacture, for a repeat violation of the licensing conditions prescribed by this Law. The manufacturer, exporter or importer may obtain a new license authorizing the respective type of activity no earlier than one year after the date of the adoption of the licensing body’s resolution canceling the previous license;
- 3) the suspension of the license to manufacture, export or import laser-readable discs... in the event of discovery of... not following the licensing body’s requirement that a violation be terminated within one month after the date on which the violation was revealed.
- 4) The sealing and/or taking into protective custody of the laser-readable discs manufactured or imported, or of those exported, in violation of the requirements of this Law, or of equipment and raw materials for their manufacture not meeting the requirements of this Law [21].

Based on these provisions, it is obvious that the dissatisfaction of US copyright industries with the fact that “the law allows convicted plant operators to be reissued a license, and delays the suspension of licenses even in cases of clear violations” [9, p.9] is well grounded. However, it is not clear what the IIPA bases its claims on that “surprise inspections are permitted only after compliance with cumbersome and timely procedures that will eviscerate their effectiveness” [9, p.9]. The only requirement for a surprise inspection under the Law is a written application to the licensing body, as specified by Article 6(2) quoted above, which is not by itself “a cumbersome and timely procedure.” Even if such procedures are lengthy in practice, it is rather a problem of implementation of the Law and not the Law itself.

Another point of dissatisfaction of IIPA with the Law is that “it also does not allow for either the effective securing of evidence or the seizure of equipment and discs during plant visits” [9, p. 9]. Article 9 (4) allows that, so the problem must lie with the concept of “effectiveness.”

In fact, it is an interesting point of how IIPA ties problems with implementation of the legislation with the legislation itself. Below is a quote from the 2002 Special 301

Report on Ukraine prepared by the IIPA that summarizes its concerns with the Optical Disc Law: “they [the Optical Disc Law and Implementing Decree] 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” [9, p.2]. While criticizing Ukraine’s progress in developing its IPR legal framework, IIPA in the same report states that “in 2001, customs authorities began to take some action, seizing several thousand CDs” [9, p. 3]; “Ukraine made progress in 2001 by finally correcting this problem for both works and sound recordings” [9, p. 3]; “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” [9, p. 5]. Finally, IIPA admits that “in 2000 losses to the music industry were estimated at \$200 million; in 2001, the estimated losses were \$170 million” [9, p. 3]. It turns out that Ukraine did make progress in developing its IPR protection regime and reduced losses to the US music industry by 15% in just one year. Yet, “IIPA recommends that in 2002 Ukraine be retained as a Priority Foreign Country (PFC)” [9, p.1].

**Article 203<sup>1</sup> of the Criminal Code of Ukraine** The US copyright industries have expressed a strong dissatisfaction with the fact that Ukraine’s legal framework provides for inadequate criminal prosecution for IPR violations. Article 203<sup>1</sup> was added to the Criminal Code of Ukraine when the Optical Disc Law was adopted on January 17, 2002 and reads:

The violation of legislation regulating the manufacture, export, and import of laser-readable discs, export, import of equipment or raw materials for their manufacture, if significant amounts are involved in these actions –  
Shall be punishable by imprisonment for a period of up to 5 years [21].

As was mentioned in the quote above, IIPA regarded this article as a positive step. However, it argued that the *significant amounts* “threshold... remains cloudy and this is a bar to the use of the provisions” [9, p.5]. It is worth noting that the threshold is not that “cloudy.” Information about Ukraine’s minimum tax-free income is readily available on the Internet and right now is UAH 17 (or app. \$3.5) [22]. With three thousand times of that, the threshold is at app. \$10,000. The average price of a pirated CD in Ukraine is \$2 [23]. Therefore, in order to face imprisonment, a copyright violator needs to produce 5000 CDs. IIPA estimated that in early 2001 Ukraine had at least five known CD plants capable of producing over 70 million discs a year” [9, p. 2]. Since the argument of IIPA is that “with an ineffective law now in place, these plants could restart their operation... [9, p. 3], a 5-year imprisonment term for producing 5000 illegal CDs out of 70 million, or 0.007%, does not really look like “a bar” at all.

While IIPA is analyzed in a greater detail in the Political analysis section, it is worth noting here that this organization is a “watchdog” for industries that depend on intellectual property. If there were no violations of IPR, IIPA would have nothing to do. Obviously, this organization tries to portray any violation it discovers in as gloomy a light as possible. While it is important to pay attention to the IIPA due to its significant

influence on the US executive branch, more effort should be devoted to consistent policies aimed at further improvement of IPR law enforcement in Ukraine.

### **Ukraine's International Obligations**

**US-Ukraine Bilateral Trade Agreement** Ukraine's trade relations with the US are regulated by the "Agreement on Trade Relations between the United States of America and Ukraine" that was signed on May 6, 2002 and entered into force on June 23, 1992. Provisions on protection of intellectual property rights are specified in Article VIII. Article VIII(1) reads:

- a) ensure in accordance with the provisions of internal legislation, protection and implementation of intellectual property rights, including copyright on literary, scientific and artistic works including computer programs and databases...
- b) ensure that their international commitments in the field of intellectual property are honored... [24].

Article VIII(2) requires that in order for the Parties

To provide adequate and effective protection and enforcement of intellectual property rights, each Party agrees to submit, to their respective legislative bodies, the draft laws necessary to carry out the obligations of this Article and to exert their best efforts to enact and implement these laws" [24].

It is worth noting that the Agreement provides little specification on what the legal framework for IPR protection should be, placing more emphasis on the enforcement – "adequate and effective protection of intellectual property rights." The Agreement also recognizes the right of each Party to establish its own regulatory framework for IPR protection. The only International Convention to which the Parties are required to adhere is the Berne Convention for the Protection of Literary and Artistic Works (Article VIII, 2(a)), which Ukraine joined on October 25, 1995. The Agreement also requires the Parties to confirm their commitments under the Paris Convention for the Protection of Industrial Property (March 30, 1883, revised July 14, 1967) and the Universal Copyright Convention of September 6, 1952 (Article VIII, 1(b)). Ukraine was a Party to these Conventions as a successor state to the USSR.

**World Intellectual Property Organization (WIPO) Conventions.** Ukraine is Party to most WIPO Conventions. As for specifically copyright and neighboring rights, as of June 12, 2002 Ukraine became party to the following WIPO Conventions:

1. The Berne Convention for the Protection of Literary and Artistic Works (adhered on October 25, 1995);
2. The Geneva Convention for the Protection of Producers of Phonograms against Unauthorized Duplication of Their Phonograms (adhered on February 18, 2000);

3. WIPO Copyright Treaty (joined on March 6, 2002);
4. WIPO Performances and Phonograms Treaty (adhered on May 20, 2002);
5. The Rome Convention for the Protection of the Performers, Producers of Phonograms and Broadcasting Organizations (adhered on June 12, 2002).

It is worth noting before starting the analysis of the Conventions that most of the Ukrainian legislation has a provision that if domestic legislation conflicts with the international agreements to which Ukraine is a party, provisions of the international agreements prevail. Thus, even if some of the provisions of the Conventions may not be included in the domestic legislation per se, they are still part of the domestic legal system of Ukraine.

This Analysis focuses on the Berne Convention, the Geneva Convention and the Rome Convention. WIPO Copyright Treaty and WIPO Performances and Phonograms Treaty, while significantly expanding on the rights of copyright and neighboring right holders, are primarily based on the three conventions mentioned above.

#### The Berne Convention for the Protection of Literary and Artistic Works

Ukraine joined the Berne Convention on October 25, 1995, which was subsequently ratified by Ukrainian Parliament.

The Convention mostly defines the variety of creative works eligible for protection. It is rather vague as to the specific ways of how the protection shall be granted. Article 9, paragraph 1 provides:

Authors of literary and artistic works protected by this Convention shall have the exclusive right of authorizing the reproduction of these works, in any manner or form.

Article 16, paragraph 1 reads:

Infringing copies of a work shall be liable to seizure in any country of the Union where the work enjoys legal protection [25].

#### Convention for the Protection of Producers of Phonograms against Unauthorized Duplication of Their Phonograms

Provisions of the Geneva Phonograms Convention became effective in Ukraine on February 18, 2000. The Geneva Convention is somewhat clearer about subjects of protection and enforcement means of such protection. Article 2 provides:

Each Contracting State shall protect producers of phonograms who are nationals of other Contracting States against the making of duplicates without the consent of the producer and against importation of such duplicates, provided that any such making or importation is for the purpose of distribution of such duplicates to the public.

Article 3 continues:

The means by which this Convention is implemented shall be a matter for the domestic law for each Contracting State and shall include one or more of the following: protection by means of the grant of a copyright or other specific right; protection by means of the law relating to unfair competition; protection by means of penal sanctions [26].

The objective of these two Conventions, which were a relatively early undertaking of the international community to protect intellectual property rights, was apparently to establish relative concepts and an international legal framework for such protection. Specific issues about enforcement were addressed in later Conventions, when it became more and more obvious that even an advanced legal framework may not work if there is lack of law enforcement.

#### The Rome Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations

The Rome Convention is one of the most recent conventions that Ukraine joined (June 12, 2002). Article 7 of the Convention specifies the kind of protection that should be provided to performers. Article 7(1) reads:

The protection provided for performers by this Convention shall include the possibility of preventing:

- a) the broadcasting and the communication to the public, without their consent, of their performance...
- b) the fixation, without their consent, of their unfixed performance;
- c) the reproduction, without their consent, of a fixation of their performance:
  - (i) if the original fixation itself was made without their consent;
  - (ii) if the reproduction is made for purposes different from those for which the performers gave their consent...

Article 10 establishes protection for producers of phonograms (neighboring right holders) and reads:

Producers of phonograms shall enjoy the right to authorize or prohibit the direct or indirect reproduction of their phonograms [27].

Some experts admit that “these positive developments [Ukraine’s adherence to WIPO Conventions and Treaties], complimentary to the progressive changes in the national legislation, brought Ukraine very close to TRIPS compliance in the legislative field” [29]. It is a good place, therefore, to analyze some of the provisions of the WTO TRIPS Agreement.

**WTO TRIPS Agreement (Agreement on Trade-Related Aspects of Intellectual Property Rights)**

Ukraine is not a member of the WTO, but expresses a strong desire to join and is in the process of bilateral negotiations with current Members of the Organization. Ukraine's accession group was established on 17 December 1994.

Experts attribute "Ukraine's failure to stop massive optical media piracy... to the lack of success... in establishing a strict and effective regulatory regime of government control over the manufacture and distribution of optical media, and the lack of enforcement of whatever control exists at present..." [28].

For the purposes of this project, therefore, this analysis will focus on Part III of the TRIPS Agreement – "Enforcement of Intellectual Property Rights." Article 41(1) reads:

Members shall ensure that enforcement procedures as specified in this part are available under their law so as to permit effective action against any act of infringement of intellectual property rights covered by this Agreement, including expeditious remedies to prevent infringements and remedies which constitute a deterrent to further infringements.

Ukraine may have a problem with this Article because of such concepts as "effective action" and "expeditious remedies." The definition of these concepts is very subjective. It is very hard, if not impossible, to achieve a 0% piracy rate or 100% IPR law enforcement. It is important to understand that "effectiveness" and "expedition" are a function of resources available to the government. It is no secret that Ukraine experiences a severe lack thereof. In this regard, it is important to analyze Article 41(5), which reads:

It is understood that this Part does not create any obligations to put in place a judicial system for the enforcement of intellectual property rights distinct from that for the enforcement of law in general, nor does it affect the capacity of Members to enforce their law in general. Nothing in this Part creates any obligation with respect to the distribution of resources as between the enforcement of intellectual property rights and the enforcement of the law in general.

In this regard, it is worth noting that Ukraine's enforcement of laws in general is weak. This in part can be explained by high corruption levels as discussed above. Limited resources at the disposal of the law enforcement authorities (customs, police) and judicial authorities cause lack of "effectiveness" and "expedition." This Article should be used by Ukraine in its accession process as an argument in support of the fact that Ukraine's government needs additional assistance to improve its law enforcement regime. Also, progress in improvement of the IPR protection regime rather than the final result should play a determinative role in the accession process.

Further, Article 42 provides that

Members shall make available to right holders civil judicial procedures concerning the enforcement of any intellectual property covered by this Agreement.

Article 44 (1) maintains that

The judicial authorities shall have the authority to order a party to desist from an infringement...

Article 45 reads

The judicial authorities shall have the authority to order the infringer to pay the right holder damages adequate to compensate for the injury the right holder has suffered because of an infringement of that person's intellectual property right by an infringer who knowingly, or with reasonable grounds to know, engaged in infringing activity.

Article 46 reads

In order to create an effective deterrent to infringement, the judicial authorities shall have the authority to order that goods that they have found to be infringing be, without compensation of any sort, disposed of outside of the channels of commerce... or... destroyed.

At this point it is worth noting that these provisions have already been incorporated into Ukraine's domestic legal framework for IPR protection as discussed above.

Another article that deserves special attention is Article 61, which talks about criminal procedures and reads:

Members shall provide for criminal procedures and penalties to be applied at least in cases of willful trademark counterfeiting or copyright piracy on a commercial scale... Members may provide for criminal procedures and penalties to be applied in other cases of infringement of intellectual property rights, in particular where they are committed willfully and on a commercial scale [29].

According to this Article, "a commercial scale" is a basis for criminal prosecution. A parallel can be made here with Article 203<sup>1</sup> of the Criminal Code of Ukraine, which establishes a "significant amount" requirement. Although heavily criticized by the US copyright industries as discussed above, a "significant amount" requirement distinguishes a commercial scale piracy (currently app. \$10,000) and is, therefore, in compliance with the TRIPS agreement.

To summarize this analysis, Ukraine in fact brought its legislative framework significantly closer to compliance with the TRIPS Agreement. The major problem that still remains, however, is enforcement of IPR laws. Some options that Ukraine has in order to improve its IPR law enforcement and the means to implement them will be discussed in the Strategy section.

## US GSP and “Special 301” Provisions

### US Generalized System of Preferences (GSP)

“The Generalized System of Preferences (GSP) program of the United States provides unilateral, non-reciprocal, preferential duty-free entry for over 4,650 articles from approximately 140 countries and territories for the purpose of aiding their economic development through preferential market access. The GSP program was instituted on January 1, 1976, and authorized under Title V of the Trade Act of 1974” [30].

Regarding IPR protection, Section 502 (c) of Title V of the Trade Act of 1974, as amended, provides:

In determining whether to designate any country as a beneficiary developing country under this title, the President shall take into account –

(5) the extent to which such country is providing adequate and effective protection of intellectual property rights.

In regards to withdrawal, suspension, or limitation of country designation, subsection 502(d)(1) maintains:

The President may withdraw, suspend, or limit the application of the duty-free treatment accorded under this title with respect to any country. In taking any action under this subsection, the President shall consider the factors set forth in Section 501 and subsection (c) of this section [31].

Thus, this title gives US Government the right to unilaterally provide or withdraw preferential treatment of developing countries. In our case, the US Government, in accordance with subsection 502(d)(1), withdrew duty-free treatment of Ukrainian exports for Ukraine’s failure to ensure IPR protection. It is worth noting, however, that it is solely at the US Government’s discretion to determine to what extent “adequate and effective” IPR protection is sufficient in order for the country to qualify for GSP benefits. This is a very powerful tool that the US may and does use to exert influence over some of the developing countries.

### US “Special 301” Section

In 1998, US Congress created “Special 301” when it passed the Omnibus Trade and Competitiveness Act of 1988, which added section 182 to title I of the Trade Act of 1974.

Section 182 (“Special 301”), subsection (a) requires the USTR to identify:

- (1) those foreign countries that –
  - (A) deny adequate and effective protection of intellectual property rights...
- (2) those foreign countries identified under paragraph (1) that are determined by the Trade Representative to be priority foreign countries.

Section 182, subsection (b) provides:

- (1) In identifying priority foreign countries under subsection (a)(2), the Trade Representative shall only identify those foreign countries –
  - (A) that have the most onerous or egregious acts, policies, or practices that -
    - (i) deny adequate and effective intellectual property rights...
    - (B) whose acts, policies, or practices described in subparagraph (A) have the greatest adverse impact (actual or potential) on the relevant United States products.

Like GSP, “Special 301” uses the notion of “adequate and effective” IPR protection. It also introduces the notion of “the most onerous or egregious acts,” determination of the extent of which is once again at the full discretion of the US Government.

Finally, Section 301 (a) of Chapter 1 of title III of the 1974 Trade Act provides:

- If the United States Trade Representative determines... that –
- (A) the rights of the United States under any trade agreement are being denied, or
  - (B) an act, policy, or practice of a foreign country -
    - (i) violates, or is inconsistent with, the provisions of, or otherwise denies benefits to the United States under, any trade agreement, or
    - (ii) is unjustifiable and burdens or restricts United States Commerce;
- the Trade Representative shall take action authorized under subsection (c)...

Subsection (c) further reads:

- (1) For the purposes of carrying out the provisions of subsection (a)... the Trade Representative is authorized to –
  - (A) suspend, withdraw, or prevent the application of, benefits of trade agreement concessions to carry out a trade agreement with the country referred to in such subsection;
  - (B) impose duties or other import restrictions on the goods of, and, notwithstanding any other provision of law, fees or restrictions on the services of, such foreign country for such time as the Trade Representative determines appropriate... [32].

Having imposed trade sanctions against Ukraine, the USTR has acted within the scope of Section 301. In our case US sanctions against Ukraine can be justified due to Ukraine’s breach of the bilateral trade agreement (failure to comply with Article VIII (2) to provide “Adequate and effective protection and enforcement of intellectual property rights”). What is hard to justify is the US’ unilateral determination of thresholds after which sanctions can be imposed. Absence of such clear limits can theoretically allow the US to deviate from the Most Favored Nation treatment depending on its foreign policy objectives, as will be discussed below in the US-Ukraine Diplomatic Relations Analysis section.

In conclusion, it follows that the real problem with the IPR enforcement regime in Ukraine lies not with an inadequate legal framework, which in fact has generally been brought into compliance with international norms, but with law enforcement. Lack of political will, corruption and bribery are certainly inhibiting proper IPR law enforcement. However, one of the primary reasons for a poor IPR protection regime is lack of resources that the Ukrainian government can devote to this problem. As a result, the issue of technical assistance from developed countries in the area of IPR should be extensively explored by the Ukrainian government.

### **US-Ukraine Diplomatic Relations Analysis**

As was briefly discussed in the Background Section of the project, overall diplomatic relations between the US and Ukraine went from the one end of the spectrum to the other during the last ten years: “the darling of US policy among the former Soviet States during the 1990s, Ukraine’s relations with the United States are looking more and more like those with its neighbor Belarus – Europe’s most isolated country...” [1].

There are several reasons for such a dramatic change in the U.S-Ukraine relations, and the most important ones seem to be:

1. US dissatisfaction with Ukraine’s political regime (high corruption levels, President Kuchma, control over the media);
2. Shift in the US foreign policy priorities away from the region;
3. Alleged arms sales to Iraq.

#### **US Dissatisfaction with Ukraine’s Political Regime**

As was discussed in the Background Section, starting in late 1992 – early 1993 the US has provided millions of US dollars in assistance for political, democratic and social development. However, despite US efforts and Ukraine’s commitments to such development, little success was achieved.

Despite all the assistance for government reforms, Ukraine remained one of the most corrupt countries in the world. According to the 2002 Corruption Perception Index (CPI), published by the German-based NGO Transparency International, Ukraine ranked 85<sup>th</sup> out of 102 countries with the score of 2.4 (with the highest score of 9.7 by Finland, meaning the least corrupt country; and the lowest score of 1.2 by Bangladesh, meaning the most corrupt country) [7].

State capture corruption is considered the most detrimental to the country’s development process. State capture corruption in Ukraine can be characterized as such “where a group of commonly referred to as ‘oligarchs’ control a significant portion of the economy, particularly in the spheres of mass media, energy and heavy industries such as steel and chemicals. Many of these oligarchs enjoy immunity from prosecution thanks to their seats in the Rada (parliament)” [6]. Some of the Ukrainian media even connected

US trade sanctions, which, as will be analyzed below, primarily targeted chemical, mineral and metallurgical industries, with the US desire to “shake” the oligarchs. They argued that “the Americans deliberately chose the chemical and metallurgical industries as targets for sanctions in order to reduce the profits of the oligarchs before the [parliamentary] elections” [33].

A so-called “cassette scandal” gave another spin to the US’ dissatisfaction with Ukraine’s political regime. A former bodyguard of President Leonid Kuchma, Mykola Melnichenko, released secretly recorded conversations between Kuchma and his subordinates. On one of the tapes, the President allegedly orders a murder of a troublesome journalist Georgiy Gongadze.

In October 2002, Ukrainian journalists formed their first independent union to fight growing government censorship. The formation of the union came just a few weeks after many journalists were forbidden to provide news coverage of the street protests on the second anniversary of Gongadze’s disappearance. Ukrainian journalists explain government censorship by the fact that “major media outlets are merely sideline businesses for a few oligarchs who are economically and politically dependent on President Kuchma, and thus subject to government interference on content issues”; “managers simply order reporters not to run news items if they have received telephone calls from President Kuchma’s office” [34]. Under the circumstances, the frustration of the US State Department is understandable - all the assistance and hard work to promote Ukraine’s democracy and government reform produced little results. As Steven Pifer, US Deputy Assistance Secretary of State and former US Ambassador to Ukraine described it, “what we have here now in particular is a crisis of confidence at the senior level” [4].

Apparently, US diplomats would like to see the regime change in Ukraine. However, this is unlikely to happen before the next presidential election in 2004. Despite relatively frequent protests against Kuchma on the streets of Kiev, the President of Ukraine has made it clear that he would not give up his power. Taking into account that it will not be long before the next election, opponents of the current political regime (who are usually proponents of closer integration of Ukraine with Western countries) should concentrate their efforts on supporting presidential candidates who are more Western-oriented. If businesses are more active in this process, they have a better chance to see the President who will be aware of and more responsive to their problems and needs.

### Shift of US Foreign Policy Priorities

After the split-up of the Soviet Union, the foreign policy priorities of the US were clearly focused on Eastern Europe. The US was interested in ensuring the safety of Soviet nuclear weapons and extensively assisted such countries as Ukraine, Belarus, and Kazakhstan to become non-nuclear states. To secure US interests in the region, US foreign policy makers chose Ukraine as a “buffer” between NATO countries and Russia, which kept nuclear weapons and continued to remain quite influential in the region.

After September 11, 2001 US interests turned away from Central and Eastern Europe. The war on terrorism and countries of the “axis of evil” became new foreign

policy objectives for the US. A recent development has been US aspirations to go after Iraq. As Fiona Hill, who is an expert on the former Soviet Union with the Brookings Institution summarized, "the priorities for the United States now are in the Middle East and Central and South Asia, rather than in Europe. In that regard, Ukraine's strategic importance as a bulwark between NATO and Russia seems to be diminished" [1].

There is not that much that Ukraine can do about this shift of US foreign policy priorities. Ukraine could certainly express its support for US efforts in the war on terrorism and to disarm Iraq, but it seems to have lost momentum as Russia did so first. With Russia and the US becoming close allies there simply seems to be little need for the "buffer" any more. On the whole, such a shift in foreign policy priorities is usually an exogenous factor that is unlikely to be influenced by a third country like Ukraine. However, Ukraine did find a way to do so in this case, not by reversing the effects of this shift, however, but by further aggravating them.

### Alleged Arms Sales to Iraq

On another tape, released by Mykola Melnichenko, there is a recording of the Ukrainian president allegedly approving of a sale of an early warning radar system "Kolchuga" to Iraq. In late September 2002, US State Department announced that the recording is believed to be authentic. In light of the current US foreign policy towards Iraq, such allegations are detrimental to US-Ukraine relations and have already led to suspension of about \$55 million in US aid for government and legal reforms in Ukraine.

The government of Ukraine denied the sale. In his statement, President Kuchma said that "Ukraine is prepared to make available all information, and it is open to inspections by competent authorized international organizations, including US experts" [13]. As far as the authenticity of the recordings is concerned, Ukrainian officials declared that "they checked the copies of the tapes and had concluded that they were altered" [4].

These allegations caused significant damage to the US-Ukraine relations. Also, their timing could not have been worse, as the US is leading an international effort to disarm Iraq. It will take time to reverse this damage. Fortunately, the US seems to associate alleged arms sales directly with president Kuchma and his immediate staff. Consequently, if a reform-oriented President is elected, there is a fair chance that US-Ukrainian relations will improve.

### Russian Argument

With the isolation from the West, President Kuchma turned to Russia, which apparently is more receptive to him. Having extensive influence over Belarus and aspiring to restore its influence in Ukraine, Russia has been supportive of the shift in Ukraine's foreign policy priorities away from the US.

What are Ukraine's interests in closer relations with Russia? No country likes to be isolated, and Ukraine is no exception. Formerly close ties with Eastern European countries, for example with Poland, are becoming weaker, with Poland soon becoming a member of the EU and Ukraine moving in the opposite direction – away from the West. There are strong pro-Western and pro-Russian political forces in Ukraine, but isolationist forces, even if they exist, are much weaker. Therefore, Kuchma turns to Russia, as it is better to have some domestic support than no support at all. Apart from strong economic interests, Ukraine turns to Russia with hopes that Russia will be able to shield it from the now "hostile" West.

Russia's interest in Ukraine is not new. In fact, it has been the same for several centuries – to maintain political and economic influence over the country and utilize its strategic location in the center of Europe. Right after the split-up of the Soviet Union, Russia found Ukraine distancing itself from their mutual historical ties and moving towards the West. Economic and political pressure on Ukraine did not help much – Ukraine was enjoying large amounts of various aid packages from the US and EU and seemed to cope quite well without much dependence on Russia.

Russia itself is interested in integrating with the industrialized nations and realizing all the potential benefits that such integration can bring. When Ukraine fell into disfavor, Russia, on the other hand, found itself in a quite favorable position: US interests in the region were unlikely to decline substantially, assistance and FDI should continue to flow, but the lion's share of them, originally meant for Ukraine, now may as well go to Russia.

Apparently, Ukraine made a strategic mistake. Instead of being at the forefront in integrating with Europe, Ukraine turned to Russia. Russia, on the other hand, is now in the lead of the "race to the West," leaving Ukraine far behind. With Russia on its way to Western integration and Eastern European countries approaching membership in the EU, Ukraine faces the fate of Belarus, which is isolation.

### **US Trade Sanctions on Ukraine**

US trade sanctions came after years of both cooperation with and pressure on Ukraine to improve its IPR protection climate. News reports indicate that “the dispute over the theft of intellectual property by Ukrainian firms is long-running. Washington has suggested strict legislation against the production of counterfeit CDs, but Ukraine’s parliament, the Rada, has repeatedly rejected US suggestions” [35]. As USTR’s press release announcing trade sanctions said, “for over two years, the United States has been urging Ukraine to take measures to stop this piracy and prevent its recurrence. Despite the commitments Ukraine made as part of the June 2000 US-Ukraine Joint Action Plan to Combat Optical Media Piracy in Ukraine, the Ukrainian Government has failed to end the piracy... In a final effort to achieve compliance, the United States extended this deadline based on promises of parliamentary action. Now that the parliament has failed to act effectively, the United States has no choice but to impose sanctions” [15].

The failure to act effectively on behalf of Ukrainian parliament refers to its passing the Optical Media Piracy Law, analyzed in the Legal Analysis section of this project. The IFPI (International Federation of the Phonographic Industry) “called the bill ‘ineffective’ and ‘highly flawed’” [35]. In his testimony to the Senate Foreign Relations Committee, Allan Larson, the Undersecretary of State for Economic, Business, and Agricultural Affairs, said: “We worked very hard. For example, on Ukraine. I pushed them several times, talked with their trade ministers, their finance ministers, and we thought for a time that we had begun to turn around this problem of piracy. But they (Ukrainian officials) didn’t persist in turning around, and so we were quick to... [take] back a significant amount of trade benefits” [36].

US trade sanctions do not only mean forgone trade benefits for Ukraine. US officials at different levels have repeatedly stated that an inadequate IPR protection regime and the resulting trade sanctions will have a direct impact on Ukraine’s chances to accede to the WTO. As Maria Jovanovich, a spokeswoman for the US ambassador to Ukraine stated, “this question also goes to the heart of Ukraine’s integration into Europe and into the global community – for example, into the World Trade Organization and a closer association with the European Union” [35].

The USTR has also made it clear that “Ukraine will need to improve its IPR regime – both with respect to legislation and enforcement – in order to meet the requirements of the WTO TRIPS agreement, which the United States and other WTO members insist upon as one of the preconditions for Ukraine to join the WTO” [37]. Following the imposition of trade sanctions, the USTR further emphasized that “the World Trade Organization also places a high priority on protecting intellectual property. Given Ukraine’s aspirations to enhance its economic relationship with the United States and eventually join the WTO, it is in its interest to move with dispatch to adopt measures that will help curtail the pirating of intellectual property” [15].

### **Recent Developments**

At the time this project is being finalized, the war in Iraq is underway, and, there has been a positive development in the US-Ukraine diplomatic relations. President Kuchma decided to deploy an NBC (nuclear-biological-chemical) battalion to Kuwait. This decision has received a warm welcome from the US. In fact, the US Ambassador to Ukraine Carlos Pascual announced that Ukraine’s decision “will have a positive impact on Ukraine’s entry to the WTO.” [46] This statement clearly demonstrates the strong connection that the US maintains between its foreign policy and international trade objectives. It remains to be seen whether this decision by President Kuchma, which was supported by Verkhovna Rada, will improve the prior damage caused to Ukraine’s international image. However, it is certainly a step in the right direction for Ukraine.

Both trade sanctions, alleged arms sales to Iraq and oppression of mass media have led to an extremely poor image of Ukraine in the international community. Addressing the problem of IPR violations without addressing the problem of poor international image and diplomatic relations with the US will be much less effective than

addressing all of these issues simultaneously. Successes in intellectual property rights enforcement need to be communicated along with other positive steps that Ukraine takes on its way to economic, political and democratic development. Certain steps that Ukraine may take to improve its international image will be presented in the Strategy part of this project. In conclusion, it is important to emphasize that Ukraine needs to be consistent in its pursuit of closer international integration with the West and better international image.

### **Public Policy Analysis**

The following quote presents a fair picture of one of the policy issues that the Ukrainian government faces in its attempts to curb IPR violations in the country: “What is the difference between two recordings of the song by Canadian pop singer Nelly Furtado ‘Turn Out the Lights’? On the street of the Ukrainian capital, Kyiv, the difference is about \$14. The one record is a legally manufactured compact disc that sells for around \$16. The other is a pirate CD made in Ukraine and sold openly in kiosks and street markets throughout the country for about \$2. The difference in price between the legitimate CD and the pirated copy represents around half the average monthly salary for most Ukrainians. For them, there is no question about whether to buy the legitimate or illicit version of a product. The illicit version is the only one they can afford” [23].

The government faces two major policy issues in its attempts to deal with IPR violations:

1. How to maintain and increase public access to foreign technology and entertainment in Ukraine;
2. How to avoid negative effects of stricter IPR enforcement on unemployment;
3. How to encourage and promote Ukrainian culture and language.

For many small and even medium-sized businesses in Ukraine the cost of licensed software may be unbearable. Most of home PC users are not able to afford it at all. Even those businesses that can afford to install licensed software may not be able to afford the cost of software upgrades as technology changes so fast.

Pirated music, movies and game software are a major source of entertainment for Ukrainians. Pirated copies are extremely popular as such copies are the only ones that average people can afford. Historically, food and entertainment have been the main forces abating social unrest. This may not be exactly the case in modern society, but listening to music, watching movies or playing computer games most likely diverts some people from going to the streets to protest against the current political regime.

When the government of a country has difficulty taking care of its people, the least it can do is to not interfere when people take care of themselves. This seems to partially explain the insignificant efforts that Ukraine's government has made to curtail copyright piracy in the country. As far as public access to foreign technology and entertainment is concerned, it seems the Ukrainian government's current policy is the policy of “non-interference.” Whether or not such a policy is beneficial for Ukrainian society is questionable. The poor IPR enforcement regime hinders FDI and the transfer of

“legitimate” and often more advanced technology to Ukraine. There is a similar situation with foreign entertainment products. Pirated movies, for example, are often of extremely poor quality and, therefore, rarely satisfy the public.

Instead of pursuing this policy of “non-interference,” the government should establish public policies aimed at educating the public about long-term benefits of a sound IPR regime and access to advanced technology and quality entertainment that will come with such a regime. Certain steps that the government can take to pursue a public education policy on IPR issues will be discussed in the Strategy section of the project.

Although a sad reality, distribution of pirate CDs on the streets of Ukraine does provide income for a large number of people, especially young people. Some reports describe how illicit CDs are distributed in Ukraine: “in a sprawling outdoor market in northern Kiev, teenagers are setting up booth after booth, each stocked with illicit CDs” [39]; “fight your way through the early April bustle of Kiev’s outdoor markets and you’ll come across all sorts of local treats. There are pickled cucumbers, warm Easter breads and fresh hot copies of Windows 2000. Everywhere you look, young guys in leather jackets hawk Madonna’s Music from portable tables” [38].

**Picture 2.**



Source: Mykola Lazarenko, *The Day*

The income of distributors is usually minimum, often not exceeding \$2-\$4 a day, which equals the price of 1 or 2 illegal CDs. A lot of them are quite happy with the pay: it is next to impossible to find a decent job for young people in Ukraine. Elimination of pirated CDs will leave thousands of them unemployed, and is likely to increase the crime rate, as well as the rates of drug and alcohol use.

Wiping out pirated software will be a significant blow to numerous small computer assembly companies, as computers and software are complementary goods. With the price of a licensed Microsoft® Office software package being almost half of the price of the computer, a lot of small computer assembly companies will simply go out of business. In addition, without pirated movies thousands of small movie rental places will have to close down. All this will not only aggravate an unemployment problem, but also will significantly reduce government tax revenues and increase unemployment benefits payouts.

The unemployment situation in Ukraine is worsening. As of November 2002, the official unemployment rate was at 3.6% [40]. Unofficial estimates of unemployment in

Ukraine are often much higher. Some estimates in 2000 put the unemployment rate as high as 35-40%. And over 30% of all unemployed were under 28 years old [41, p. 27]. Such a discrepancy between official and unofficial data is explained by the so-called “hidden unemployment,” when people “are on forced long-term leave, or work one or two days a week” [41, p.27].

**Picture 3.**



**Source:** *National Security and Defense No 2, 2000*

The current public policy of the Ukrainian government with regards to potential increase in unemployment due to a stricter IPR enforcement regime also seems to be that of ‘non-interference.’ Instead, policies aimed at creating more jobs for young people and educational policies should take priority, for example, to train young people on job-hunting techniques and to encourage them to be more active and persistent as well as patient when looking for a job.

Another public policy problem that the government of Ukraine faces is how to promote Ukrainian language and culture. Unfortunately, this is the area that usually receives the lowest priority when it comes to funding. Going to a theater becomes less and less popular due to abundant TV soap operas. Unfortunately, many people cannot afford the price of a theater ticket. To make matters worse, the Eastern, predominantly Russian-speaking, part of Ukraine, has failed to fully implement some language policies put forth by the government (using Ukrainian as an official language in business, government, and educational sectors).

The most successful Ukrainian performers leave Ukraine to work in Russia. Even though they mostly do so due to the fact that the Russian entertainment industry is more advanced, part of the reason is that Russia makes much more effort to combat CD and audiotape piracy. In Ukraine, performers receive very small royalties, as their legally produced CDs cannot compete with pirated ones. Talented performers who leave for Russia often sing in Russian to have a larger audience, which is detrimental to Ukrainian culture.

Promoting Ukrainian culture given available funding is quite a complicated task. The government should fully support public policies that may have an indirect positive effect on the country’s cultural development. Therefore, supporting a public awareness campaign about the potential benefits of an enhanced IPR protection regime in Ukraine should be an objective that the government follows.

These policy issues that the government of Ukraine faces are indeed important ones. And not exercising an extra effort to curb IPR violations--that is, pursuing “non-interference” public policy--may be an easy way to address these issues. However, the long-term damage that an ineffective IPR protection regime inflicts on the economy and society of Ukraine outweighs short-term benefits, because the ineffective IPR protection regime:

1. Supports low value-added industries (copying pirated CDs and videos does not add much value or require high skills);
2. Impedes domestic technological and cultural development (for example, software developers are not encouraged to work on the development of new software as they are unlikely to receive royalties; Ukrainian musicians leave to work in Russia);
3. Prevents FDI and, consequently, economic growth (foreign investors are not interested to invest in a country where their patents, trademarks or copyrights are violated).

The next section discusses the views that the Ukrainian public has taken on these issues.

### **Public Opinion Analysis**

To effectively analyze current public opinion on IPR protection in Ukraine, it is helpful to determine what drives public opinion in general. Ukraine has been considered a country with a relatively low social awareness of and interest in politics – there is generally lack of public debate, Ukrainians usually do not discuss politics in their families, at work or during social gatherings. As a result, public opinion is mostly shaped and driven by mass media. Therefore, to sway public opinion one way or the other, it is often sufficient to put out a couple of newspaper articles and TV news reports. No wonder that interest groups who have a stake in keeping the IPR enforcement measures at their current level are the most vocal ones. These interest groups try to bring aboard as much support as possible – they know what they have to lose and try to shield themselves from IPR enforcement measures with public support.

In mass media there are arguments addressing both public policy issues discussed above: 1) access to technology and entertainment for Ukrainian society and 2) effects of stricter IPR enforcement on Ukrainian economy and unemployment situation.

The poor economic and social situation often justifies the argument of many producers of illicit CDs that they do what they do with the needs of Ukrainian society in mind. As some of the reports indicate, “the CD manufacturers [in Ukraine] argue that American industry is more interested in stifling competition than protecting copyright, and they paint themselves as Robin Hood figures, protecting the poor Ukrainian consumer against high prices set by the Microsoft monopoly and a music industry that’s being investigated on two continents for price-fixing” [38].

The international recording industry argues that owners of CD manufacturing plants successfully utilize public opinion and lobby the parliament to pass weak and ineffective laws. As Eugene Kornychuk, a former advisor to Kuchma on copyright issues observes, "The pirates are very active in the parliament when they are trying to postpone drafts of new legislation. They complain they are Ukrainian companies that pay taxes and have employees that they will have to fire" [38]. Back in 2001, Igor Eichenwald, head of operations at "Bolidisc," a Kiev-based CD manufacturing plant, gave another explanation of US dissatisfaction with the piracy level in Ukraine: "We are potential competitors. That is what the Americans are afraid of" [38]. Due to increased international pressure, Bolidisc, however, has recently had to move its operations to Belarus and change its name [35].

Many members of parliament side with public opinion and view these arguments as legitimate, arguing that CD manufacturing is an infant industry and needs protection. One of the co-sponsors of the highly criticized Optical Media Licensing Law, discussed in the Legal Analysis section, Mykhailo Pavlovsky, argues that "by passing this law, we have demonstrated that Ukraine has its own views... I don't condemn the United States. They are working correctly in the interest of their people. We should work properly in the interest of our nation and our manufacturers" [23].

Another quite legitimate argument that enjoys great support from the public is that the US recording industry and the USTR fail to recognize the positive development of Ukraine's IPR protection climate. Despite the fact that CD piracy flourishes in many other countries in the world, the US decided to make Ukraine a "scapegoat," because the US cannot sanction other countries for political reasons. As Oleg Purik, director of Rostok CD plant put it, "America is a very powerful country able to solve its internal problems at the expense of other countries. Although plants that manufacture cheap CDs can be found in China, Russia, Bulgaria and Taiwan, sanctions are planned only against Ukraine. The USA just needs boys to beat up. It's a pity that our country can't offer any resistance" [39]. As follows from IFPI statements, such arguments do not lack ground.

An article by Radio Free Europe / Radio Liberty quotes some statements by Stefan Krawczyk, the IFPI's regional director for Eastern Europe, who admits that "the real production bases remain Ukraine, Russia, Bulgaria, Belarus, and possible Poland and Czech Republic" [35]. Krawczyk continues: "After Ukraine, I would say the spotlight in terms of industrial CD piracy would go to Russia... Up to a year ago, there was already large-scale piracy in Russia, but it mostly remained inside the Russian market. And they now have clearly taken over the role that Ukraine used to play" [35]. Another country, which, according to Krawczyk, causes concerns to the international recording industry, is Bulgaria: "Bulgaria, or Bulgarian entrepreneurs I should say, have been taking advantage of all this attention on Ukraine to start building up CD capacity again. And they are certainly also again involved in pirate production" [35]. And this is not all, as Krawczyk says, "if you look at pure pirate production, I would also include the former Yugoslav [republics] – Yugoslavia as such, Bosnia, Montenegro, [Macedonia]... They are having a very big impact on the market there, which is almost 100 percent pirate" [35].

Disappointment of both Ukrainian public and government at the supposedly unfair US treatment of Ukraine is understandable: trade sanctions are imposed solely on Ukraine and its chances for WTO accession are significantly weakened. At the same time, other 'pirate' countries remain unaffected. Moreover, Bulgaria, Bosnia and Macedonia, whose piracy levels are not that far off from that of Ukraine, are up for the EU accession.

The solution to the negative public opinion problem is not difficult at all: public opinion can be influenced using the same methods that were used to initially shape it, which is by using mass media. For example, the international recording industry blames the ignorance of Ukrainian society about intellectual property for the piracy problem in the country. As Andrey Dakhovskyy, owner of Ukrainian records, a Ukrainian distributor of Universal Records puts it, "under the communist regime everything was for the community. For 70 years there was no respect for intellectual property. People do not understand what it is. It's like trying to sell air" [38]. By educating the public, by presenting contrary arguments to the ones put forth by opponents of IPR enforcement efforts, supporters of Ukraine's closer integration with the US will be able to influence public opinion. By demonstrating that the ineffective IPR regime actually impedes economic development of Ukraine in the long run, proponents of more effective IPR enforcement should be successful in having the public favor further IPR reforms.

### **Political Analysis**

#### **Ukraine's Political System**

Ukraine is a parliamentary-presidential republic. The head of the state is the President, the head of the government is the Prime Minister, and the Speaker leads the Parliament.

The current President of Ukraine is Leonid Kuchma, who is in his second term and whose time in office expires in 2004. Kuchma came to power in 1994, when he won early presidential elections over Leonid Kravchuk, the first President of Ukraine. There are 24 regions in Ukraine, where the President appoints Governors, and the Autonomous Republic of the Crimea.

The Prime Minister (currently Mr. Victor Yanukovich) is recommended by the President and approved by the Parliament. The executive powers of the Prime Minister are quite extensive. The Prime Minister heads the Cabinet of Ministers of Ukraine. The Ukrainian Parliament has the power to remove the Prime Minister.

The Speaker of the Parliament (Verkhovna Rada) is currently Mr. Vladimir Litvin. Verkhovna Rada of Ukraine is a single chamber legislative body, primarily dominated by three political forces: right-wing (nationalist and pro-reform interests), centrists (business interests) and left-wing (Communist and Socialist parties). The President has the power to dismiss the Parliament.

Therefore, the two most powerful people in the executive branch, having the ultimate oversight of the implementation of governmental policies, are the President and Prime Minister. Their support, or at least absence of their opposition, is essential to improving the IPR protection regime in Ukraine. Therefore, the phrase “the government of Ukraine” used in the Strategy section of this Project refers to the President of Ukraine, the Prime Minister and governmental agencies responsible for various aspects of IPR law enforcement (the Ministry of Internal Affairs, State Customs Service and State Department of Intellectual Property. This Section further analyzes various stakeholder groups in the issue of IPR protection in Ukraine.

### Ukrainian Stakeholders

Among Ukrainian stakeholders, several groups may be distinguished: business and political interests directly affected by trade sanctions and interests in favor of closer integration with the West; interests that benefit directly from poor IPR protection or are pro-Russian and anti-Western oriented; interests that experience a direct negative effect of inadequate IPR law enforcement; and, finally, groups that have mixed interests.

Business and Political Interests Directly Affected by Trade Sanctions and Interests in Favor of Ukraine's Closer Integration with the West. This group of stakeholders includes Ukraine's export industries against which trade sanctions were imposed, other export-oriented industries, and business and political interests looking forward to closer integration with and more FDI inflows (tourism sector, for example) from the West.

The three industries with most exports to the US are metallurgical, chemical, and textile and footwear industries. These are the three industries that are hurt the most by the US trade sanctions. The impact of the sanctions on these industries is analyzed in the Economic Analysis of the project. These industries should be interested in having the trade sanctions lifted and improving Ukraine trade relations with the US. The sanctions have reduced their exports, which in turn caused output and employment reduction. In addition, their access to the US market has either been blocked or significantly reduced.

The three largest enterprises in the metallurgical sector are:

1. Krivorozhstal;
2. Mariupol Metallurgical Combine;
3. Azovstal'.

The three largest enterprises in the chemical sector are:

1. Odessa State Port Plant;
2. AZOT, Severodonetsk;
3. AZOT, Cherkassy.

The three largest textile and footwear enterprises are:

1. Vozko, Voznesensk;
2. Teksterno, Ternopol';
3. Demitekst, Poltava.

Industries directly affected by US trade sanctions pressure their representatives in Ukrainian parliament to do whatever it takes to ensure that the US trade sanctions are lifted. This is only possible with a more effective enforcement of IPR laws. Even though the legislative branch has less influence over the executive branch in Ukraine than in the US, members of parliament still oversee the work of the executive branch and can provide their input into how effective or ineffective the government is in fighting IPR violations.

Metallurgical, chemical, and textile and footwear industries also have their respective labor unions: the Trade Union of Workers of Metallurgical and Mining Industry of Ukraine, the Trade Union of Workers of Chemical and Petrochemical Sectors of Industry of Ukraine; and the Trade Union of Workers of Textile and Light Industry of Ukraine. These labor unions are unhappy about the sanctions as they directly affect an unemployment problem. Labor unions in Ukraine, however, are relatively weak and do not have much influence on the government, parliament, or even the management of their enterprises. Labor unions in Ukraine need to become more involved in politics. By being more vocal in expressing their interests and concerns, labor unions will have a greater chance to be heard and perceived as a strong force. While labor unions may be allies in an effort for a greater integration with the Western countries, businesses need to be careful so that not to give labor unions too much power.

Export-oriented industries generally favor closer international integration as such integration opens new markets for them. There are also a lot of enterprises in Ukraine that seek more financing in the form of foreign direct investment (FDI). These enterprises often understand, or otherwise need to be informed, that additional FDI inflows are only possible if Ukraine enforces its IPR laws and foreign investors feel safe that their trademarks, copyrights and patents are duly protected. Export-oriented enterprises and enterprises seeking FDI are potential allies in an effort to influence the government of Ukraine to bring about better enforcement of IPR laws and Ukraine's closer international integration.

In Ukraine, a lot of businesses, especially large ones, have strong ties with politicians whom they can effectively influence. Such relations are rarely made public, so it is often hard for outsiders to identify specific politicians and enterprises whose interests they represent. However, in the issue of Ukraine's closer integration with Western countries, pro-Western and pro-Russian interests can often be connected with specific regions of the country.

Pro-Western business and political interests are primarily concentrated in Kiev and Odessa regions and in the Western part of Ukraine. Kiev is the capital and has the strongest connections with the Western world out of all the regions of Ukraine. International organizations, embassies of foreign countries and multinational corporations

often first establish themselves in Kiev. The capital also attracts human resources with the best education and experience in a wide range of professions. Due to the much greater exposure to the West that Kiev has compared to other regions of Ukraine, business and political interests here have a better understanding of potential benefits that both the capital and the entire country will have with westernization and, therefore, should support it. Pro-Western interests in Kiev have the benefit of being closer to central government and, therefore, have a better ability to interact with and influence governmental agencies in charge of IPR protection.

Business and political interests representing the Odessa region should also support closer international integration of Ukraine. The Odessa region has Ukraine's largest ports which process a huge portion of Ukraine trade flows. Closer international integration will result in more trade and, consequently, more business for the Odessa region.

The western part of Ukraine has historical and cultural ties with the countries of Eastern Europe and opposes the pro-Russian direction that President Kuchma has taken. Business and political interests in this part of the country have always supported closer integration of Ukraine with the West and are very likely to continue to do so. Interest groups in this part of Ukraine are more nationalist and strongly advocate sustainable growth of Ukraine's economy, better standards of living for Ukrainian people and reduction of Ukraine's economic dependence on Russia. Business and political interests in Western Ukraine are much more interested in seeing Ukraine as a respectful member of the international community than their counterparts from the East.

Generally, however, pro-Western political forces are at a disadvantage now due to the pro-Russian president and majority of the government. The situation may change depending on the upcoming presidential elections in 2004 and members of the coalition should make an extra effort to ensure that the next President of Ukraine is more Western-oriented.

Business Interests Directly Affected by Lack of IPR Enforcement. This group includes distributors of the US, European and Russian recording industries as well as Ukrainian CD and video manufacturing companies that are willing to and capable of producing and marketing licensed products. They are interested in an improved IPR protection regime, because it will lead to a larger market share for their products and, therefore, more sales, revenues and profits. This group is generally pro-Western. Ukrainian distributors of the US recording industry are the most active of this group, perhaps because US recording companies (for example, Universal Records, represented in Ukraine by Ukrainian Records, and Sony Music Entertainment) are losing out the most and have much more resources to pursue IPR protection improvements in Ukraine than, for example, the Russian recording industry.

Other stakeholders in this group include Ukrainian performers and software developers. These are the people who actually create and invent, and they experience the damage from lack of IPR enforcement first hand. Unfortunately, a lot of software developers look for work overseas where there are more opportunities for them and their

work is duly compensated. As a result, Ukraine loses valuable human resources that may contribute to its technological development.

The most successful Ukrainian performers leave Ukraine to work in Russia. Even though they mostly do so due to the fact that the Russian entertainment industry is more advanced, part of the reason is that Russia makes much more effort to combat CD and audiotape piracy. In Ukraine, performers receive very small royalties, as their legally produced CDs cannot compete with pirated ones. Talented performers who leave for Russia often sing in Russian to have a larger audience, which, as mentioned, is detrimental to Ukrainian culture.

Other stakeholders in this group are movie theaters (for example, a nation-wide chain of "Movie Palaces"), widely broadcast national and regional TV and radio channels (Inter, 1+1, ICTV), and large music and movie retailers.

Movie theaters in Ukraine show licensed movies and, therefore, often have difficulty competing with pirated videotapes and DVDs. Even though more and more people prefer to watch new releases with a quality translation on a big screen, revenues of movie theaters are much lower than they would be if copyright laws were effectively enforced.

National and large regional TV stations and radio channels are in a similar situation. They cannot broadcast pirated material, but often do not have sufficient resources to purchase broadcast rights for newer "blockbuster" music and movies. As a result, they have to broadcast cheaper but older and less popular content. Large TV stations and radio channels often lose their audiences, and therefore, advertising revenues to their smaller counterparts who can sometimes get away with broadcasting pirated content due to less attention being paid to them by regulatory agencies.

Large movie and music retailers face fierce competition from street vendors and small kiosks. Due to a greater visibility of business practices of large retailers, they often cannot sell pirated music and movies, while street vendors and small kiosks can. Since the price of pirated material is so much cheaper, large retailers lose customers and profits.

Stakeholders in this category have a few options. First of all, all of them should try to influence the government to make more effort in fighting IPR violations. In addition, TV and radio stations can effectively influence public opinion by running commercials and hosting talk shows to educate the public about the negative effects of IPR violations on the Ukrainian economy, jobs and the standard of living. Distributors of the US, European and Russian recording and movie industries can run heavily advertised promotion campaigns in an attempt to get a greater market share by delivering quality products to customers at discounted prices. A majority of consumers in Ukraine do not have access to quality products due to their high prices, but once they get a feel for quality, some of them are likely to switch to licensed CDs, DVDs, audio- and videotapes. Movie theaters and large movie and music retailers can incorporate both techniques: they can both run IPR awareness campaigns (posters in stores and movie theaters, and

infomercials prior to showing a film in the movie theaters) and cooperate with distributors on discounting tickets, CDs, DVDs, or tapes. These options will be discussed in a greater detail in the Strategy section of this project.

Pro-Russian and generally anti-Western business and political interests are heavily concentrated in the Eastern part of Ukraine (Donetsk, Dnepropetrovsk and Kharkov regions) primarily due to this region's proximity to Russia and strong historic, economic and cultural ties with Russia. The eastern part of Ukraine has many heavy industries (metallurgical, chemical, machine building), which conduct a significant part of their business with Russia. The decision of the US to impose sanctions on the products of metallurgical and chemical industries, therefore, may be explained by the fact that the US was interested in hitting pro-Russian interests and avoiding damaging pro-Western interests. While business and political interests from Eastern Ukraine generally disfavor closer integration with Western countries, some of them may still become potential allies in an effort to reduce IPR violations and have the US trade sanctions lifted (see the section on interest groups directly affected by US trade sanctions above).

Interest groups opposing Ukraine's closer international integration also include Ukrainian industries that currently enjoy lack of competition and, therefore, can charge higher prices and make more profit. Closer international integration of Ukraine will undoubtedly make this country's economy more open. These industries will not only face competition from international manufacturers and service providers, but more FDI inflows will promote creation of domestic competitors as well. Telecommunications and financial services are among those sectors particularly not fond of foreign direct investment because of a growing demand for their products which would ultimately result in much more business opportunities provided that there was still lack of competition. It is worth noting, however, that even though some industries that enjoy lack of competition may oppose the opening of Ukraine's economy which will follow the country's closer international integration, they may also be interested in stronger intellectual property rights protection.

Interest groups directly benefiting from poor IPR law enforcement in Ukraine certainly include enterprises manufacturing pirated CDs, DVDs, and audio- and videotapes, distributors and exporters of pirated products, as well as political forces both within the government and parliament of Ukraine that support them. Intellectual property is one of the pillars of Western society and IPR violators naturally have anti-Western feelings. With the US putting pressure on Ukrainian government to better enforce IPR laws, the very existence of enterprises engaged in music and movie piracy is at stake. The more effective an IPR enforcement regime in Ukraine becomes, the fewer CDs, DVDs and tapes that will be manufactured in violation of copyright and neighboring rights. Consequently, revenues and profits of manufacturers and distributors will plummet and many of them will go out of business. The primary interest of this stakeholder group is to postpone improvement of the IPR regime in the country for as long as possible by lobbying legislators and bribing law enforcement agencies.

Local radio channels and TV stations broadcasting pirated material are also in this group of stakeholders. They enjoy larger audiences and greater advertising revenues due to the fact that they often broadcast popular “blockbuster” content for which they do not pay. A stronger IPR protection regime, which the US presses for, will reduce the popularity and, consequently, revenues of small TV stations and radio channels, which they certainly do not favor.

Stakeholders that have mixed interests. Government of Ukraine, law-enforcement agencies, and Ukrainian public have mixed interests in the problem of ineffective IPR protection regime in Ukraine.

The government of Ukraine has mixed interests due to the variety of policy issues that its ministries and departments face. Within the Ukrainian government, there are several departments that are interested in strong relations with the United States and in having US trade sanctions lifted. The two ministries that are responsible for Ukraine's international relations are the Ministry of Foreign Affairs (Minister – Mr. Anatoliy Zlenko) and the Ministry of Economy and European Integration (Minister – Mr. Valeriy Khoroshkovsky).

The primary area of responsibility of Ukraine's Ministry of Foreign Affairs (MFA) is establishing and maintaining diplomatic relations between Ukraine and other nation states. MFA also coordinates Ukraine's consular, cultural, and political relations. One of the responsibilities and interests of the ministry is to improve the poor international image of Ukraine. The Ministry of Foreign Affairs is also interested in improving Ukraine's relations with the United States.

The Ministry of Economy and European Integration of Ukraine is responsible for the country's economic development and its closer integration with Europe. Joining the WTO and the European Union is among the top foreign policy priorities for Ukraine, and the Ministry's responsibility is to ensure that economic goals and policies of Ukraine are in line with those established for the countries that seek accession. Since Ukraine's ineffective IPR protection regime is in the way of the country's international integration, the Ministry is interested in improving it. The Ministry is also interested in having US trade sanctions lifted as they have a negative impact on the economy of Ukraine.

Another governmental agency that has a stake in the issue of IPR protection is the State Department of Intellectual Property (Head – Mr. Mykola Paladiy), which is a division of the Ministry of Education and Science of Ukraine and is responsible for designing and implementing national IPR policies. The title of the Department suggests broad enforcement powers, which is not the case. The main responsibility of the Department is to ensure normative and institutional development of intellectual property issues in Ukraine.

The Ministry of Labor and Social Policy of Ukraine may not fully support strong IPR enforcement in the short run, as stronger IPR enforcement will result in job losses, especially for younger people involved in distribution channels. The officials in the Ministry need to be made aware, unless they already are, of the long-term benefits for the

unemployment situation that a stronger IPR enforcement and subsequent FDI inflows can bring.

The Ministry of Internal Affairs (MIA) and the State Customs Service of Ukraine are the two primary government agencies responsible for enforcement of IPR laws in Ukraine. MIA is responsible for enforcing IPR protection laws within the territory of Ukraine (manufacture and distribution), while the Customs Service oversees export and import of optical media, equipment for their production, and raw materials. These law enforcement agencies have mixed interests within themselves. On the one hand, they should be interested in enforcing IPR laws as it makes them look as if they were efficiently and successfully performing their duties. On the other hand, these agencies are struggling with high corruption levels. Customs and police officers are bribed by IPR violators to disregard piracy and counterfeiting. Officers who accept bribes are naturally interested in the continued flow of bribes. In addition, since illegal IPR-related goods distribution channels keep a lot of young people away from alcohol, drugs and crime, law enforcement agencies may want to maintain status quo to keep their work load from increasing.

The Ukrainian public is a stakeholder group with mixed interests in the issue of IPR protection as consumers of music and movie products. As discussed above, Ukrainians generally are not well educated about copyright issues. However, most of them understand that improvement in the IPR protection regime will lead to better quality, but much more expensive CDs and videos. Therefore, within the society there are at least two groups: those who want better quality products and those who want cheaper products. The first group is likely to support improvement of the IPR protection regime, while the second group is likely to oppose it. Effective educational, advertising and promotion campaigns advocating stronger IPR protection while reducing high prices of quality IPR-related products should increase the first group in size, while reducing the second one.

### US Stakeholders in Support of Trade Sanctions

The two most important stakeholders in support of the US trade sanctions against Ukraine are the USTR and the US copyright industries, primarily represented by the Motion Picture Association of America (MPAA), Business Software Alliance (BSA) and the Recording Industry Association of America (RIAA). The interests of the RIAA are represented internationally by the International Federation of the Phonographic Industry (IFPI).

### US Copyright Industries, IFPI

Since the US recording and movie industries are the largest in the world, they are the most vocal in expressing their concerns about international copyright piracy, which directly affects their revenues and, therefore, profits.

However, piracy, which denies royalties to the US copyright industries, is not the only issue that concerns them. Another problem is lost market share. It is clear that highly priced CDs, videos and DVDs cannot compete in the markets of low-income developing countries. However, pirate optical media produced in Ukraine is often directed to higher-income countries of Central and Western Europe, where lower-priced pirate CDs take over part of the legitimate CD market.

Therefore, the interest of the US copyright industries is to move forcefully to eliminate international copyright piracy. Since it is the responsibility of the governments to enforce laws in their respective countries, US copyright industries work hard to pressure governments to engage in proper enforcement practices. The easiest way to exercise such pressure is through the US government, the USTR in particular.

IFPI is an international recording industry association, headquartered in London, UK. The main mandate of IFPI is to fight piracy. The key people in the IFPI with whom the coalition should work closely are Jay Berman, chairman and CEO, and Stefan Krawczyk, regional director for Eastern Europe.

It should be noted that these associations (IFPI, MPAA, BSA and RIAA) are member-driven. They have a distinct interest – to keep their members satisfied with their work. Therefore, associations may exaggerate certain facts or dramatize certain violations to help them look successful in identifying and addressing IPR violations. A poor image of Ukraine gives associations momentum and additional leverage to press the US government (USTR) to maintain Ukraine as a priority foreign country and keep the trade sanctions in place.

## USTR

The “Special 301,” discussed in the Legal Analysis section of this project, requires the USTR to identify the countries that deny adequate protection of intellectual property rights.

Most pressure on the USTR comes from the US copyright industries. However, the USTR also has to report to US Congress annually on the results of his work in the IPR area. The interest of the USTR is to effectively carry out his responsibilities and to reduce the pressures coming from these two sources by acting decisively against IPR violations across the world. On the other hand, the USTR is interested in promoting good trade relations between the US and other countries, including Ukraine. USTR is interested, therefore, in supporting Ukraine's efforts for a more effective IPR protection regime so that trade sanctions can be lifted and US-Ukraine trade relations can be improved.

## US Stakeholders in Support of Stronger US-Ukraine Relations

A large portion of the interested parties in the US would like to see US-Ukraine relations strengthen. These are the Congressional Ukrainian Caucus, NGOs and business

organizations. They are often connected to the Ukrainian Diaspora, which is quite large and active in promoting Ukraine's interests. It should be noted up front that US supporters of closer ties with Ukraine are not in a favorable position right now due to Ukraine's poor international image. With a more negative attitude in the US towards Ukraine, it is harder for these organizations to press the US government for closer US-Ukraine diplomatic and trade relations or more assistance and aid. Improving Ukraine's image in both diplomatic and trade areas will make it easier for these organizations to focus on specific issues that are in the way of even closer relations between Ukraine and the US.

### **Congressional Ukrainian Caucus**

The Congressional Ukrainian Caucus in the US Congress unites representatives who support stronger relations between the US and Ukraine, and deeper integration of Ukraine into the international community. According to the Ukrainian Congress Committee of America (UCCA), the Caucus consists of some 30 members of Congress [42]. The most active members are Rep. Bob Shaffer, Rep. Marcy Kaptur, Rep. Kurt Weldon, and Rep. Maurice Hinchey, who apparently have large pro-Ukraine constituents and want to respond to their concerns about worsening US-Ukraine diplomatic and trade relations.

It is very important for the government of Ukraine to cooperate with the Congressional Ukrainian Caucus to promote democratic, legal and economic reforms in the country. One of the first priorities of the Caucus, in cooperation with the UCCA, is "Ukraine's graduation from the Jackson-Vanik amendment, which would afford it a permanent most-favored-nation (MFN) trade status, thus boosting trade between Ukraine and the United States" [42].

### **Non-government Organizations**

One of the most active NGOs advocating closer US-Ukraine relations is The Ukrainian Congress Committee of America, Inc. (UCCA). UCCA was established in 1940 and today unites over 20 Ukrainian organizations and over 75 branches throughout the United States. UCCA's offices are located in New York City, Washington DC, and Kiev, Ukraine.

Another quite active NGO is the US-Ukraine Foundation (USUF), which was established in 1991 to facilitate democratic development, encourage free market reform, and enhance human rights in Ukraine. As USUF's web site states, the organization "is dedicated to strengthening the mutual objectives of both nations while advancing Ukraine as a cornerstone of regional stability and as a full partner in the community of nations."

These NGOs depend on the support and donations they get from interested parties. Therefore, they are interested in responding to the concerns of such parties as effectively as possible. UCCA and USUF should be involved in the coalition effort to improve trade relations between the US and Ukraine as they can benefit the coalition by influencing the US government and bringing publicity to the coalition effort. On the other hand, these

NGOs will also benefit from being a part of the coalition, as they will be actively involved in improving US-Ukraine relations, which should satisfy the parties who support them and possibly increase such support.

### **Business Sector**

While the Congressional Ukrainian Caucus and NGOs are primarily involved in the democratic, educational and political side of the US-Ukraine relations, the business sector is actively engaged in promoting trade and investment ties between the two countries. An umbrella organization promoting business relations between the US and Ukraine is the US Chamber of Commerce.

The Europe & Eurasia Business Committee (EBC) of the US Chamber of Commerce is responsible for promoting US business interests the Newly Independent States, including Ukraine. Through the EBC, US member companies can influence US commercial policy and access key decision-makers in the United States and in the region. The American Chamber of Commerce in Ukraine was established in June 1992. Its main tasks are to support its members who operate in Ukraine and to promote new trade and investment relations between the US and Ukraine.

The US Chamber of Commerce is an influential force that should be fully employed by the coalition. The Chamber is a member-driven organization and is interested in larger and stronger membership. By ensuring that business interests of its pro-Ukrainian members are effectively promoted, the Chamber will ensure the support and continued membership from such interests.

Some other organizations that are involved in promoting US-Ukraine business relations, although to a lesser extent, are the Ukraine-US Business Council, the Russian-Ukrainian Legal Group and the US-Ukraine Digital Alliance (USUDA). The Ukraine-US Business Council represents more than thirty major US corporations doing business in Ukraine. The Council serves as a major liaison between business and the Governments of Ukraine and the US. The main objective of the Council is to improve business conditions in Ukraine for US investors. The Russian-Ukrainian Legal Group, headquartered in Washington, DC, provides legal support to international corporations engaged in business and investment activity in Ukraine and other CIS countries. USUDA was established in June 2002 to promote and support Ukraine's transition to an economy that provides for effective and widespread use of information technology.

These organizations need to communicate their interests to the USTR more effectively. As was just mentioned, USTR's main objective is to promote trade and investment between the US and foreign countries. Strongly expressed concerns about the fact that US trade sanctions damage US business interests will give USTR more leverage to counter numerous complaints by associations representing IPR-dependent industries.

## **Economic and Commercial Analysis**

### **FDI in Ukraine**

One of the most valuable benefits to the economy of Ukraine, and one of the most obvious ones, that will result from an enhanced IPR protection regime is a significant increase in FDI inflows. Foreign direct investment is generally considered by developing countries more preferable than domestic investment due to a number of reasons, among them are:

1. Technology spillover effect;
2. Management expertise;
3. Additional financial resources coming into a country;
4. Strengthening of the local currency.

Some of the variables that affect the country's attractiveness to foreign investors are:

1. Population;
2. GDP growth;
3. Law Enforcement and Corruption;
4. Tax regime;
5. Literacy rate, etc.

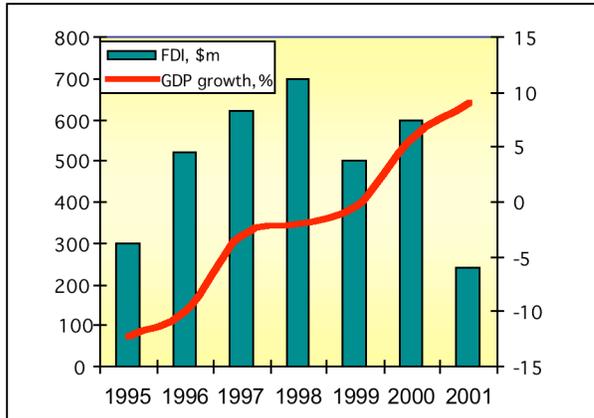
This analysis attempts to illustrate how an inadequate IPR protection regime may affect FDI by explaining the relationship between FDI inflows, GDP growth and the size of the population.

Chart 3 illustrates the relationship between GDP growth and FDI that has been established empirically: the larger the economy of the country grows, the more foreign investment comes in. In other words, the larger becomes the pie, the larger piece you will get, and, therefore, more people will want a piece of it. The Chart below shows that for Ukraine, from 1995 to 2000 the relationship between FDI inflows and GDP growth was generally positively correlated. However, from 2000 to 2001 we see that the relationship becomes negatively correlated: as the economy of Ukraine grows, FDI inflows actually decrease! What this implies is that at this point some other variables influencing FDI have become so much stronger, that they actually reversed the existing relationship between FDI and GDP growth for Ukraine. The year 2000 is when Ukraine's IPR violations reached their peak and the US started to actively push the Ukrainian government to take some measures to amend the problem.

If we look at some other countries in Eastern Europe (Russia, Poland and the Czech Republic), we clearly see that these countries were able to attract much more FDI inflows with even lower GDP growth (Chart 4 and table below). Poland, for example, was able to attract \$5.7 billion in FDI despite the fact that its GDP only grew by 1% in 2001. Russia attracted three times more FDI than Ukraine, even though its GDP growth was almost half that of Ukraine. If we account for the difference in the population size

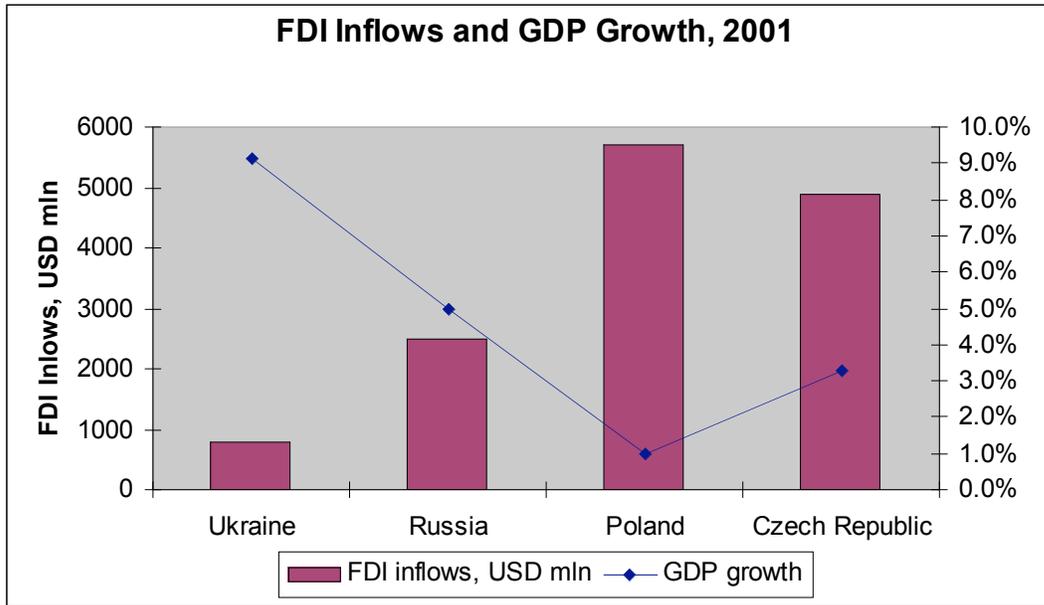
between the two countries (Russia's population is nearly three times more than that of Ukraine), we see that Russia was able to attract roughly the same amount of GDP per capita, despite the fact that its GDP growth was almost half of that of Ukraine. This may be explained by the fact that Russia's IPR enforcement regime is stronger than that of Ukraine.

**Chart 3. Ukraine: GDP growth and FDI Dynamics, 1995 - 2001**



Source: Ukrainian Economic Trends, Jan. 2002

**Chart 4.**



Source: Worldbank Economic Indicators, 2001.

2001	Ukraine	Russia	Poland	Czech Republic
<b>FDI inflows, USD mln</b>	792	2,500	5,700	4,900
<b>GDP growth</b>	9.1%	5.0%	1.0%	3.3%
<b>Population, mln</b>	49.1	144.8	38.6	10.2
<b>GDP per capita, USD</b>	\$16.13	\$17.27	\$147.67	\$480.39

If we compare FDI inflows per capita of Poland and Czech Republic and account for the differences in GDP growth between these two countries, we see that the FDI

inflows per capita per percentage point in Poland and Czech Republic are roughly the same (Poland: \$147.67, Czech Republic:  $\$480.39 / 3.3\% = \$145.57$ ). Indeed, these two countries have approximately the same, but lower level of copyright piracy than Ukraine or Russia.

It follows from this simple analysis that Ukraine has a huge potential in attracting more FDI, but this potential is severely underutilized. While it can be argued that there are other variables that may affect the problem of low FDI inflows to Ukraine, an inadequate IPR protection regime must be somewhere at the top of the list.

### **Negative Effect on Ukrainian Industries**

This section analyzes the impact of suspended GSP benefits and imposed trade sanctions on Ukraine's economy. Ukraine's exports to the US are analyzed during two periods:

1. January – August 2001 (before GSP benefits were suspended on August 7<sup>th</sup>, 2001 and trade sanctions were imposed on January 23, 2002);
2. January – August 2002 (the same period, but after suspension of GSP benefits and imposition of the sanctions).

According to the USITC [19], during January-August 2001 (period 1) exports of just 3 industries (metallurgical, chemical, and footwear) comprised more than 73% of total Ukraine's exports to the US and were distributed as shown below. For the purpose of the project, the following methodology has been used:

1. Only categories with exports of more than 1% of total exports are included in the analysis);
2. Categories that are not included in either the "GSP Imports – 2000. Top Duty Free Items from Ukraine" [43] or "List of Products of Ukraine Subject to Increased Duties" [44] are not included in the analysis.

**Table 2. Exports by Metallurgical, Chemical and Footwear Industries During Period 1**

#### **Metallurgical Industry**

<b>HTS Category</b>	<b>Imports in million USD</b>	<b>% of total Imports from Ukraine</b>
<b>72.</b> – Iron and Steel	\$78.3	18.585%
<b>76.</b> – Aluminum and articles thereof	\$20.1	4.771%
<b>73.</b> – Articles of Iron and Steel	\$6.3	1.495%
<b>Total for Metallurgical Industry</b>	<b>\$104.7</b>	<b>24.851%</b>

#### **Chemical Industry**

<b>HTS Category</b>	<b>Imports in million USD</b>	<b>% of total Imports from Ukraine</b>
<b>28.</b> – Inorganic chemicals; organic and inorganic compounds of precious metals, of rare-earth metals, of	\$136.9	32.494%

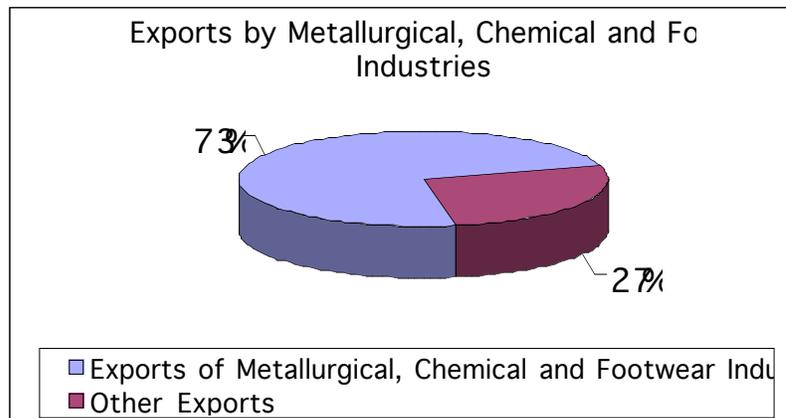
radioactive elements or of isotopes		
<b>27.</b> – Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	\$14.5	3.442%
<b>31.</b> – Fertilizers	\$21.4	5.079%
<b>32.</b> – Tanning or dyeing extracts; tannins and derivatives; dyes, pigments and other coloring matter; paints and varnishes; putty and other mastics; inks	\$11.4	2.706%
<b>35.</b> – Albuminoidal substances; modified starches; glues; enzymes	\$5.0	1.186%
<b>29.</b> – Organic chemicals	\$7.3	1.732%
<b>Total for Chemical Industry</b>	<b>\$196.5</b>	<b>46.639%</b>

### Footwear Industry

HTS Category	Imports in million USD	% of total Imports from Ukraine
<b>64.</b> – Footwear, gaiters and the like; parts of such articles	\$7.0	1.661%
<b>Total for Footwear Industry</b>	<b>\$7.0</b>	<b>1.661%</b>

<b>Total for Metallurgical, Chemical, and Footwear Industries</b>	<b>\$308.2</b>	<b>73.151%</b>
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Chart 3. Exports by Metallurgical, Chemical, and Footwear Industries to the US



According to the USITC [19], during January – August 2002 (period 2) exports in the categories above changed as follows:

**Table 3. Changes in Exports by Metallurgical, Chemical, and Footwear Industries due to Suspension of GSP benefits and Imposition of Trade Sanctions**  
**Metallurgical Industry**

HTS Category	Imports in million USD (period 1)	Imports in million USD (period 2)	% change
<b>72.</b> – Iron and Steel	\$78.3	\$86.1	+9.961%

<b>76.</b> – Aluminum and articles thereof	\$20.1	\$0	-100%
<b>73.</b> – Articles of Iron and Steel	\$6.3	\$11.3	+79.365%
<b>Total for Metallurgical Industry</b>	<b>\$104.7</b>	<b>\$97.4</b>	<b>-6.972</b>

#### Chemical Industry

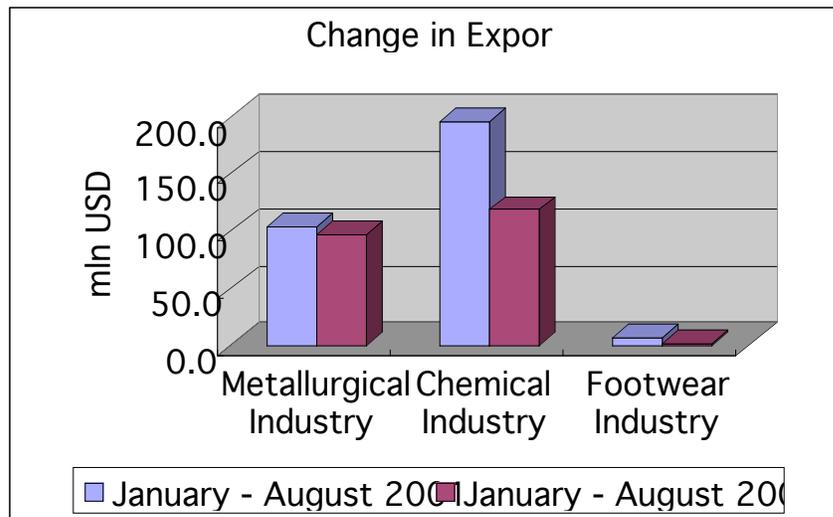
HTS Category	Imports in million USD (period 1)	Imports in million USD (period 2)	% change
<b>28.</b> – Inorganic chemicals; organic and inorganic compounds of precious metals, of rear-earth metals, of radioactive elements or of isotopes	\$136.9	\$40.7	-70.270%
<b>27.</b> – Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	\$14.5	\$68.1	369.655%
<b>31.</b> – Fertilizers	\$21.4	\$1.4	-93.458%
<b>32.</b> – Tanning or dyeing extracts; tannins and derivatives; dyes, pigments and other coloring matter; paints and varnishes; putty and other mastics; inks	\$11.4	\$4.0	-64.912%
<b>35.</b> – Albuminoidal substances; modified starches; glues; enzymes	\$5.0	\$4.1	-18%
<b>29.</b> – Organic chemicals	\$7.3	\$0.5	-93.150%
<b>Total for Chemical Industry</b>	<b>\$196.5</b>	<b>\$118.8</b>	<b>-39.542%</b>

#### Footwear Industry

HTS Category	Imports in million USD (period 1)	Imports in million USD (period 2)	% change
<b>64.</b> – Footwear, gaiters and the like; parts of such articles	\$7.0	\$1.8	-74.285%
<b>Total for Footwear Industry</b>	<b>\$7.0</b>	<b>\$1.8</b>	<b>-74.285%</b>

<b>Total for Metallurgical, Chemical, and Footwear Industries</b>	<b>\$308.2</b>	<b>\$218.0</b>	<b>-29.266%</b>
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**Chart 3. Change in Ukraine’s Exports to the US (Period 1 vs. Period 2)**



By analyzing the information about the total output and employment in each of the three industries, it is possible to derive the Employment Requirement Coefficient (ERC), which determines how much output one worker can produce in each of the three industries. Table Ukraine’s Ministry of Industrial Policy provides the following data for total output and employment in metallurgical, chemical and light (textile, apparel and footwear) industries [45]. The following methodology has been used to analyze the data:

1. The exchange rate of 1 USD = 5.3 UAH has been used to convert the data to US Dollar figures;
2. Equivalent of full-time employment is analyzed;
3. The data for total output is provided for January – July 2002. To arrive at the ERC that determines how much output one worker can produce *per year*, total output for 7 months is divided by 7 to arrive at the total monthly output, and multiplied by 12 to arrive at the yearly total output.
4. Output and employment is provided for light industry, which includes textile and apparel in addition to footwear. It is assumed that ERC for the entire light industry will be a fair representation of the ERC for the footwear industry.

**Table 4. Employment Requirement Coefficient for Metallurgical, Chemical and Light (Footwear) Industries**

Industry	Output Jan-Jul 2002 (USD)	Yearly output (USD)	Employment (Workers)	ERC (\$ / Worker)
Metallurgical	4,304,500,000	7,379,142,857	287,252	25,688
Chemical	657,400,000	1,126,971,428	96,327	11,699
Light	67,600,000	115,885,714	41,614	2,784

Having the value for ERC for the three industries, it is possible to assess the impact on employment in these industries caused by suspension of GSP benefits and the imposition of trade sanctions by the US. Reduced exports will cause reduction in the

output provided the exports are not diverted to other markets. The results are provided in Table 5.

**Table 5. Impact on Employment in Metallurgical, Chemical, and Footwear Industries due to Suspension of GSP Benefits and Imposition of Trade Sanctions**

Industry	Exports in Period I (USD)	Exports in Period II (USD)	Change (USD)	ERC (\$ / worker)	Change in # of jobs
Metallurgical	104,700,000	97,400,000	7,300,000	25,688	- 284
Chemical	196,500,000	118,800,000	77,700,000	11,699	- 6,642
Footwear	7,000,000	1,800,000	5,200,000	2,784	-1,868
<b>Total Jobs Lost</b>					<b>8,794</b>

This analysis shows that suspension of GSP benefits and imposition of trade sanctions by the US caused a loss of nearly 9,000 jobs in the Ukrainian economy, with most jobs lost in the chemical industry.

In conclusion, it should be noted that any numbers obtained in evaluating the potential increase in FDI or estimation of the negative effect of US trade sanctions can only be considered a rough approximation of what the real results may be. For example, a steady growth in FDI in Ukraine may trigger foreign investor confidence in the country, and FDI inflows may turn out significantly higher than predicted. Also, estimates of losses to Ukraine's economy may be significantly understated due to negative spillover effects into other industries, which are extremely hard to estimate. However, even these rough estimates provide a relatively clear picture of the potential benefits of an effective IPR protection regime and the negative effects of the lack thereof.

### Strategy

In the analytical sections of this project the conclusions have been made that in order to improve the IPR protection regime, have US trade sanctions lifted and GSP benefits restored, Ukraine's objectives should be to:

1. Improve IPR law enforcement;
2. Educate Ukrainians about the damage of music and movie piracy to the cultural and technological development of Ukraine, as well as its economic growth;
3. Improve Ukraine's international image.

Although these objectives are within the domain of the central government of Ukraine (perhaps with the exception of educating the public), it is in the UAME's interest to ensure that the above objectives are effectively and expeditiously implemented. To

achieve this, the UAME should start with building of the “Coalition Against Copyright Piracy.”

### **Coalition Building**

The UAME efforts to bring about a more effective IPR law enforcement and all the potential benefits listed above will be more successful and will have much more leverage if these efforts are united with the efforts of other stakeholders with similar interests. These stakeholders include (see the Political Analysis section for a discussion of stakeholders):

1. In Ukraine – business interests directly affected by US trade sanctions, business and political interests in favor of Ukraine’s closer integration with the West, and stakeholders directly affected by lack of IPR enforcement;
2. In the US – business, NGO and political interest groups in favor of closer US-Ukraine diplomatic, trade and economic relations.

The UAME should establish and lead the new “Coalition against Copyright Piracy”. To bring interested parties into the coalition, explanatory letters should be sent to prospective members (a sample letter is provided in Appendix 2), and discussion meetings should be organized. The UAME should also hold a press conference to bring news coverage to the establishment of the Coalition and its progress (a sample press release is provided in Appendix 3).

Potentially, the efforts of the Coalition may face some distrust from Ukrainian stakeholders with strong nationalist or pro-Russian interests due to the presence of US interest groups in the Coalition. These concerns may be addressed by advancing the argument that it is entirely up to the USTR whether or not to lift trade sanctions against Ukraine, and US supporters of the Coalition, being familiar with the intricacies of the interaction with the US government will be an invaluable asset to the Coalition and a great help to Ukrainian government in its efforts to communicate the results of the improved IPR law enforcement measures. Pro-Russian business interests that may not be clearly interested in Ukraine’s closer integration with the West need to be advised about the benefits of having expanded access to markets beyond Russia (for example, diversification of export markets leads to a reduced risk of exports volatility).

US business stakeholders interested in the Eastern European region need to be educated about potential business opportunities arising from Ukraine’s beneficial geographic location in the middle of Europe-- a market of nearly 50 million people and stable economic growth. Participation in bilateral business events organized by the US and Ukrainian embassies, US Chamber of Commerce or Ukraine’s Trade Mission to the US will be a good forum to achieve this.

The final goals of the Coalition should be:

1. Elimination of US trade sanctions and restoration of US GSP benefits for Ukraine;
2. Better access to international markets for Ukrainian enterprises;
3. Increase in FDI inflows and creation of additional jobs;
4. Enhanced technological and cultural development in Ukraine;
5. Greater chances for Ukraine's expeditious accession to the WTO.

More detailed arguments about the potential benefits to the UAME and Ukraine in general are provided in the sample White Paper of the UAME (Appendix 4). In order to achieve these goals, the Coalition should concentrate its efforts on two areas:

1. Close cooperation with the government of Ukraine to ensure that appropriate measures are developed to achieve the Coalition goals;
2. Media and public awareness campaign.

### **Cooperation with the Government and Public Awareness Campaign**

As mentioned above, the Coalition needs to work closely with relevant agencies of the Ukrainian government (see the Political Analysis section) to ensure that effective governmental policies are established and followed in the following three areas:

1. IPR law enforcement;
2. Public education campaign about the damage of piracy of music and movies to the cultural and economic development of the country;
3. Improvement of Ukraine's international image.

With the exception of the public education campaign, only the Ukrainian government can work in these three areas. While the coalition certainly cannot dictate to the government what to do, it can make certain recommendations and use its leverage to exercise pressure on the government to implement these recommendations. Alternatively, the Coalition can pressure the government to seek its opinion and recommendations if the government were to develop different policies.

### **Improve IPR Enforcement**

As was concluded in the Legal Analysis section of the project, Ukraine's legal framework for IPR is generally in compliance with international norms, and the reason for an inadequate IPR protection regime is lack of law enforcement.

One of the reasons for poor law enforcement in Ukraine (not only as it relates to IPR) is lack of resources and funds to pay for enforcement mechanisms. While the government should try its best to improve IPR law enforcement with the resources it has at its disposal, it should also seek technical assistance from developed countries that are interested in the enhancement of the IPR protection regime in Ukraine (the US and EU). The need for technical assistance in order to improve IPR law enforcement should be clearly communicated to these countries.

The UAME should make the following recommendations to the government of Ukraine:

1. The Ukrainian government should resume its efforts to bring about stronger IPR law enforcement by creating a special copyright anti-piracy police unit, which should not be subordinated to regular police authorities, but linked directly to the Cabinet of Ministers to avoid multiple levels of bureaucracy. This anti-piracy unit should have ultimate jurisdiction over IPR-related cases and have the right to conduct unannounced inspections of production facilities; seize counterfeited products and equipment used for their manufacture until there is a court ruling to permanently close down the facilities and destroy seized products; arrest manufacturers and distributors of pirated products, and inspect distribution channels (stores, kiosks and street vendors) to intercept pirated products.

While it may seem an expensive endeavor at the outset, it does not have to be. Even a relatively small unit can achieve its objectives, which should be to send a message to copyright violators, media, the Ukrainian public, US copyright industries and the USTR that copyright piracy in Ukraine will no longer be tolerated. Officers should be selected on the basis of a strong record of merit and integrity and should be motivated to maintain strong performance. A compensation package for the unit officers should be higher than that of regular police authorities to discourage corruption and bribe taking. The package may have a non-monetary component to it that may be attractive for some officers such as a business trip to a foreign county for training (funding for which should be sought from the US and EU as part of the technical assistance package to the Ukrainian government).

2. The Ukrainian government should also make an extra effort to educate judges in the area of trademark and copyright violations. The problem of insufficient number of judges can be addressed by having specially trained judges specialize only in IPR-related cases. Furthermore, such cases may be considered in a city or regional court instead of a district court to avoid dispersion of cases and risk of a case being considered by a judge without experience in intellectual property rights. Judges should be selected for special training and specialization in IPR-related cases on the basis of a strong record of merit and performance. An attractive compensation package should be developed for judges concentrating on IPR-related cases to discourage corruption and bribes. Part of a compensation package may be a business trip to a foreign country for training.

3. Investigations and trial of IPR-related cases should be fully transparent and open to the extent permitted by law. In fact, as many cases as possible should be made public and be covered by the media to effectively convey the message to the violators, Ukrainian public and foreign copyright industries and governments that copyright violations in Ukraine will not be tolerated and will be prosecuted to the fullest extent permitted by law. Such publicity will serve two objectives. Firstly, it will act as a deterrent to future IPR violations. Secondly, it will communicate to the stakeholders in the issue that significant progress is being made in Ukraine's IPR protection regime.

### **Educate the Public about the Damage Caused to Ukrainian Culture and Economy**

This objective should be implemented both by the government (State Department of Intellectual Property, a division of the Ministry of Education and Science of Ukraine) and the Coalition to show the Ukrainian public that improving the IPR enforcement regime is a consolidated effort. The Ministry of Education and Science has direct access to the majority of consumers of the illicit videos and CDs, who are often either high school or university students. The State Department of Intellectual Property should organize lectures at educational institutions or young men and women's organizations to educate young people about the damage being done by copyright piracy to Ukraine's economy and culture. A direct link between piracy today and their future should be established and clearly communicated. Such issues as unemployment, economic growth, cultural and technological development of Ukraine should be quite appealing to young Ukrainians.

In addition, the Ministry of Education and Science should join the Coalition efforts in running a public awareness campaign. This should include TV commercials and newspaper ads (for example, in such popular nation-wide newspapers as "Fakty i Kommentarii", "Kievskie Vedomosti"), increased media coverage of prosecution and trial of IPR-related cases, anti-piracy entertainment events, and talk shows with popular Ukrainian performers. While TV commercials and newspaper ads will have to be paid for, the Coalition should employ its influence over some of the major newspapers and seek extended media coverage for the Coalition efforts free of charge. An example of an article that may appear in Ukrainian newspapers following the creation of the Coalition is provided in Appendix 5.

Anti-piracy business interests in Ukraine should be quite instrumental in shaping the success of the public awareness campaign. Nation-wide TV channels (Inter, 1+1, ICTV) and radio stations have access to a majority of Ukrainian consumers and can influence their public opinion on IPR issues by bringing publicity to the government's IPR enforcement efforts. Distributors of the US, European and Russian recording and movie industries should run heavily publicized promotion campaigns about delivering quality products to consumers at discounted prices. Once again, the coordinated effort of these industries should become news by itself due to the wide consumer appeal, so such promotion campaigns should not require paid advertising. As part of the campaign, movie theaters and large movie retailers can incorporate both techniques: they can both run IPR awareness campaigns (posters in stores and movie theaters, infomercials prior to shows in movie theaters) and cooperate with distributors on discounting tickets, CDs, DVDs, or tapes. Exchange booths may be set up to exchange a certain number of pirated CDs or videos for a licensed, high quality equivalent. While short-term expenses on the public awareness campaign may seem high, anti-piracy oriented businesses are likely to understand the long-term benefits resulting from such consolidated anti-piracy efforts.

Ukrainian performers with the support of the Coalition should organize an anti-piracy concert tour around Ukraine. They can cooperate with law enforcement agencies

to have illicit CDs and videos destroyed as part of the concert program, as it was done in Russia when bulldozers crushed thousands of pirated products in front of the stage for everyone to see. These events should be widely broadcast to reach even larger audiences.

### **Improving Ukraine's International Image**

This effort by the Ukrainian government should be made not only in the area of IPR protection, but preferably in other areas as well (for example, administrative and economic reforms, democratic development). The Ukrainian government has some options that it can pursue to achieve this goal.

As mentioned above, by making IPR-related prosecutions and court trials transparent, the government can send a strong message to the international community that it is serious in its intentions to curb IPR violations in the country. Joining the business community in a public awareness campaign will demonstrate the possibility of success that cooperation between business and government interests can potentially have in various areas.

The Ukrainian government can closely work with foreign governments and take advantage of their experience and expertise in areas such as democratic development, economic and administrative reforms, and proper governance. In the area of IPR protection, for example, the government can work with the US government through both the Ukrainian Embassy in Washington, DC and the US Embassy in Kiev. The Ukrainian Embassy to the US can hold regular briefings or organize business lunches with the US recording and movie industry associations (RIAA and MPAA) to communicate the results of Ukraine's IPR protection regime and seek their recommendations and expertise. Some of the measures and steps recommended by the US copyright industries may not be acceptable to Ukraine, at least in the short run. However, by making the associations part of the development of Ukraine's IPR regime, Ukraine's government can obtain the support of these associations, or at least reduce industry associations' objections to the government of Ukraine's efforts to convince the USTR to have trade sanctions lifted and the GSP benefits restored.

Close work with the USTR on the issue of IPR protection in Ukraine is something that Ukraine's Embassy in Washington, DC should consider one of its priorities. It is the responsibility of the USTR to review the state of IPR protection in countries around the world annually, and it is the USTR who has the authority to impose and lift trade sanctions. The Embassy of Ukraine should provide as much information on the progress of IPR enforcement in Ukraine as possible. As the USTR annual Special 301 Report is preceded by a period of public comments, in support of closer cooperation with Ukraine, US business interests can be extremely instrumental in influencing the USTR's decision and counteracting negative pressure coming from the US copyright industries. This opportunity should be utilized by the Coalition to the fullest extent. Another source of information for the USTR on IPR-related issues in Ukraine is the US Embassy in Kiev. Therefore, the Ukrainian government needs to maintain close contacts with the US

embassy and ensure that it provides timely and sufficient information about the progress of IPR protection.

Another available measure for the government to improve Ukraine's international image is to periodically place articles about major political, economic and democratic developments in Ukraine in newspapers read widely in political circles, such as the Financial Times and the Economist. These newspapers readily cover negative developments in Ukraine, but positive ones often remain unnoticed. Articles that the Ukrainian government should place in these newspapers need to emphasize good things that happen in the country and educate the international community about them. The Ukrainian government should attempt to place as many of these articles as possible for free, in the form of editorials or op-ed pieces. However, if these attempts are not successful, paid articles should be considered. An example of the article that aims at improving Ukraine's international image and may appear in international media is given in Appendix 6.

Yet another measure that the government may take to improve Ukraine's international image is to make available well-known representatives from academia and public advocacy groups for international media and academic events. If Ukraine's government encourages these people to actively interact with their international counterparts, voice their concerns and share their opinions, even though they may sometimes be negative towards the government, the international community will perceive Ukraine as a democratic country that, even though it has some problems, is not ashamed to admit them.

### **Conclusion**

The success of the Strategy depends on how coordinated and strong the efforts of all the parties to the Coalition are. The recommendation for the UAME is to seek the broad support for the "Coalition against Copyright Piracy" and ensure effective cooperation between business stakeholders and the government. The approximate budget for the UAME is given in Appendix 7. The Coalition efforts will be successful if it achieves the following goals within the proposed timeline (see Appendix 7):

1. Have US trade sanctions lifted and GSP benefits restored;
2. Increase FDI inflows to Ukraine;
3. Raise public awareness about the damage of copyright piracy to Ukraine's economic, cultural and technological development;
4. Expedite Ukraine's accession to the WTO.

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