

# Legal Regulation of Securities and Stock Market in Ukraine

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In 2007, the main Ukrainian securities exchange, the PFTS, was the second best-performing national securities exchange in the world behind China, with an increase of more than 135% during the year. However, the PFTS fell by 74% in 2008 as the global economic and financial crisis hit Ukrainian companies particularly hard with companies in the mining and metals, energy and chemicals sectors the most severely affected. The PFTS bounced back strongly in 2009, with a gain of more than 83% to the end of September.

Generally, the Ukrainian securities exchanges remain relatively illiquid with only a few local companies listed. They are also relatively lowly capitalised and have no real tradition of market-making. Their development is also hampered by a lack of clear and sufficiently sophisticated legislation to regulate them as well as a lack of proper enforcement of the existing legislation. In addition, legal remedies frequently applied in other countries either do not operate properly or are not available at all in Ukraine.

Currently, the priority tasks for the development of Ukrainian securities exchanges include removing gaps and ambiguities in the Ukrainian securities legislation as well as implementing international standards and generally accepted principles of market practice. This will include amending various legislative acts to make the operation of the Ukrainian securities exchanges more clear and transparent, providing effective protection of securities owners' rights and modernising securities market accounting and trading systems, for example, by implementing modern securities trading technologies. Effective systems of correspondent relations between the Ukrainian and foreign depositories as well as between the Ukrainian depositories themselves need to be established.

## Securities Exchanges

There are currently 10 securities exchanges in Ukraine. As indicated above, the largest securities exchange by market capitalisation in Ukraine is currently the PFTS Stock Exchange which developed from the over-the-counter electronic market trading system PFTS. It has over 850 securities listed (including equity, debt and other securities relating to approximately 580 companies) and a total market capitalisation of approximately USD 25,830 million (as of 25 December 2009). The other nine securities exchanges are individually much smaller by way of total market capitalisation and accounted in aggregate for approximately 51.5% of completed trades on Ukrainian securities exchanges for the first eleven months of 2009.

If at any time any Ukrainian securities exchange ceases to comply with the relevant statutory requirements, the State Commission on Securities and the Stock Market (the Securities Commission) may suspend its operations. Representatives of Ukrainian securities exchanges are obliged to regularly report to the Securities Commission on the securities traders operating on their respective securities exchange and the securities listed on it as well as provide summarised information on completed securities transactions.



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## The Securities Commission

The Securities Commission is the main regulator of the Ukrainian securities market. The Securities Commission is a state authority subordinated to the President of Ukraine and accountable to the *Verkhovna Rada* (the Ukrainian Parliament). It is responsible for developing and implementing uniform state policy on the functioning of the Ukrainian securities market as well as monitoring the compliance of all Ukrainian securities market participants with Ukrainian securities legislation. It has extensive registration, licensing and enforcement powers as well as broad legislative powers to issue regulations, resolutions, recommendations and letters of advice. The Securities Commission has power to apply sanctions against parties that breach securities legislation and these include issuing fines (determined as a fixed amount or as a percentage of the amount obtained illegally) and suspending or revoking the offending party's securities licence.

## Types of Securities and Issuance Procedures

Ukrainian law classifies the securities which can be issued and traded in Ukraine into six groups:

- (i) equity securities (include shares; investment certificates; and certificates of real estate operations funds),
- (ii) debt securities (include corporate, state and municipal bonds; treasury bills; deposit certificates; promissory notes; and bills of exchange),

- (iii) mortgage-backed securities (include mortgage-backed bonds and certificates),
- (iv) privatisation securities,
- (v) derivatives, and
- (vi) commodity-related securities.

Ukrainian securities may be either documentary (certificated) or non-documentary (electronic), and may have bearer, registered or order form. The procedures for issuance, registration and disposal of securities vary depending on their type and form. For example, the procedure for a share issuance requires the issuer to complete approximately 15 steps before being able to complete registration of the shares with the Securities Commission and start trading them. However, the issuance of promissory notes is much simpler as these do not need to be registered with any state authority. To place securities outside Ukraine, Ukrainian issuers, other than the State issuing bonds externally, need to obtain the prior permission of the Securities Commission.

## Licensing of Professional Activities with Securities

All professional activities on Ukrainian stock market are subject to licensing by the Securities Commission and include the following:

- (i) trading in securities (includes brokerage, dealing, underwriting, and securities management),
- (ii) activities of asset management companies,
- (iii) depository activities (include activities of securities registrars, custodians and depositories), and
- (iv) activities of securities exchanges.

Licences may be obtained only by legal entities which meet certain statutory criteria, which include: a minimum amount of charter capital, an appropriate ownership structure, compliance with relevant other licences. Generally, such entities are prohibited from engaging in any business activities besides their licensed professional activities. Licences may be suspended or cancelled if the licensee either ceases to comply with the established criteria or breaches Ukrainian securities legislation.

## Depository System

The depository system of Ukraine has a two-tier structure, an upper tier and a lower tier.

The upper tier comprises the National Depository of Ukraine and other licensed depositories whose main functions are the clearing and processing of settlements under securities transactions.

The National Depository of Ukraine mostly performs administrative functions such as standardising depository accounting procedures and documentation related to securities transactions, codifying securities by assigning an ISIN, and establishing relations with foreign depository institutions.

The Interregional Fund Union (known as MFS) is currently the market leader in depository operations and deals with the majority of securities transactions undertaken in Ukraine. Despite negotiations to merge the National Depository of Ukraine with the Interregional Fund Union, the latter's shareholders decided to merge all their operations with those of the All-Ukrainian Securities Depository. It is expected that this merger will formally complete by early 2010.

The lower tier of the Ukrainian depository system consists of custodians and securities registrars. The custodians are engaged in the custody of securities and servicing the securities transactions on their securities accounts, and the registrars keep registries of registered securities owners.

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Chadbourne has one of the leading Ukrainian law practices. We have a very strong group of Ukrainian and expatriate lawyers with an extensive range of experience in Ukraine, and have worked together as a unified team for 16 years. Our Kiev office includes U.S.-, English- and Ukrainian-qualified attorneys. Our partners are consistently ranked among the top lawyers in Ukraine, and the Kiev office is recognized by legal directories including Chambers Global, Chambers Europe and IFLR1000 as a leading law firm in Ukraine, particularly in the areas of corporate/commercial and banking and finance.

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State authorities exercising control over, and supervising, the national depository system include primarily the Securities Commission, the National Bank of Ukraine and the Ministry of Finance.

## Latest Legislative Developments

Due to the protracted economic and financial crisis and a lack of political consensus, several legislative acts which were expected to be adopted in 2009 to improve the regulation of Ukrainian securities market are still pending. They include new legislative acts on derivatives and on the securities depository accounting system as well as several draft acts aiming to harmonise the existing legislation on the securities and stock markets. On the other hand, important legislative changes have been made to bring existing laws and regulations in compliance with the *On Joint-Stock Companies Act of Ukraine of 17 September 2008, No. 514-VI* that came into force on 30 April 2009, as well as to support securities market participants in meeting the challenges of the current economic and financial crisis.