

# CORPORATE GOVERNANCE IN UKRAINE

## 1. General information related to the state of corporate legislation

The level of corporate relationships regulation in Ukraine cannot be estimated as perfect and efficient. When most of the CIS-states have adopted the new Civil Codes and have established or considerably modified specialized legislation on joint stock companies, Ukraine still has to be contented with the Civil Code adopted in 1963, and the Law “On Economic companies” adopted on September 19, 1992 makes the fundament for corporate legislation in Ukraine. And though this legislative act has undergone through introduction of numerous amendments, those related to corporate governance inclusive, the Law has obviously lost some of its regulative functions and presently requires global reconsideration.

In June, 2000 the Supreme Council Of Ukraine has adopted in the second reading the Draft Civil Code of Ukraine and currently the preparatory activities for its third reading are being implemented; the Draft Law of Ukraine “On Joint Stock Companies” has been submitted for consideration to the Supreme Council.

These documents stipulate the legal basis for organization and operations of entrepreneurial subjects as entities being regulated by the private law; they also provide the details of peculiarities characteristic only for the joint stock companies. Though the Draft Law of Ukraine “On Joint Stock Companies” can not yet be considered as perfect and gives rise to many censorious remarks, Ukraine has come to realize the necessity of introduction of the key reforms in the corporate legislation in the whole and of the institute of corporate governance in particular.

## 2. Securing protection of shareholders’ rights

Ukrainian legislation regulating the procedure for implementation of entrepreneurial activities in the whole and corporate legislation in particular does not contain any notion that could be analogical to the American notion of *merger of companies*. Ukrainian legislation does not put forth any requirements to the joint stock companies or to their management to be followed in case of merger, it does not establish any additional mechanism and protection measures to be applied to protect the shareholders of the merged company.

In contrast to the shareholder-related legislation of other states, the right of a shareholder not to agree when the decision on merger of his company is being adopted is absent in the current Ukrainian legislation.

The blank spaces in the Ukrainian legislation are preconditioned by some objective reasons: practically, no mergers of joint stock companies by their competitors or by other subjects has ever occurred in Ukrainian stock market, which can be explained by the capital structure.

Presently, Ukrainian stock market has not been developed sufficiently enough, and circulation of securities occurs in negligible volume. More than 2/3 of the total number of Ukrainian joint stock companies have been established in the form of closed joint stock companies, shares of which, in accordance with Article 25 of the Law of Ukraine “On Economic companies”, cannot be bought and sold in the market.

The constitutive documents of joint stock companies often stipulate the duty for a shareholder willing to sell his shares to propose these shares to the company or to other shareholders and only in case of expressed refusal of the company or that of the other

shareholders he is able to alienate his shares in favor of outsiders. This limitation gives rise to doubts related to its being legal, but with the help of establishment of the priority right of shareholders or company to redeem their own shares it is possible to prevent losing control over the company when the considerable block of shares belongs to the same person.

Antimonopoly legislation of Ukraine contains some limitations related to acquiring of share holdings.

Unlike the countries having developed corporate legislation, Ukraine has not established the legal procedure for operations with insider information. Persons, who in accordance with American legislation are recognized as *insiders* (managers, directors, owners of more than 10% shares), do not bear any additional responsibilities related to disclosure of information on share holdings and are not limited in their rights related to share holding.

Shareholders' rights protection is realized mostly under the court procedures in accordance with Article 124 of Ukrainian Constitution.

As it can be seen from the analysis of the court practices, most actions are related to recognition of the decisions of the general shareholders meetings as invalid and to dividends payment. Such actions are usually brought against the company by single shareholders.

The mechanism for *bringing collective actions*, developed in the legislations of other countries, in particular, in the USA, is not stipulated in Ukrainian corporate legislation, as well as the shareholders' right to bring such actions.

Apart from the court procedure, legislation related to regulation of securities market stipulates the possibility for the shareholders to appeal to Securities Stock Market State Committee. So, only for the period of the year of 1999, the Committee has received for consideration approximately 10.000 letters, appeals and claims from physical persons and professional market participants related to violation of their rights and legal interests. Violation of requirements related to personal notification of shareholders on convening the general shareholders meeting, falsification of general shareholders meetings' resolutions are among the most typical violations of legislation on the part of the issuers of securities.

It goes without saying, the court procedures shall become the main method (form) of shareholders' rights protection.

Corporate legislation in Ukraine does not differentiate the amount of shareholders' rights in respect to the number of shares they hold. All the shareholders are entitled with equal rights and duties. The difference is only in the number of shareholders' votes at the general shareholders' meetings. It depends on the number of shares the shareholder owns and on the opportunity to participate in the meeting that depends on the type of shares (common or privileged shares).

Taking these premises as the basis, Article 10 of the Law of Ukraine "On Economic companies" stipulates the right of the company participant to obtain information on company activities irrespective of the number of shares he holds.

There is no specific norm regulating the shareholders' right to appeal to the court with the action against joint stock company management in the legislation of Ukraine. Therefore, any shareholder whose proprietary rights and legal interests are violated has the right to bring an appeal against management of a joint stock company. This right does not depend on the number of share he owns.

Article 23 of the Law of Ukraine "On Economic companies" (parts 5, 6) stipulates the following:

- company management bodies officers are responsible for damage caused to the company by them in accordance with the current legislation of Ukraine;
- officers shall be liable for divulge of commercial secrets and confidential information, as it is stipulated in the current legislation of Ukraine and in the constitutive documents of the company.

In accordance with point “g” of Article 41 of the same Law, adoption of the decisions related to calling management officers of the company to material responsibility shall be in the competence of general shareholders’ meeting.

When solving the problems related to responsibility of company officers for damage caused to the company by them, it is necessary to start from relationships the officer is in with the company. If those relationships are labor relationships, the liability shall be considered in accordance with the norms of labor legislation; in particular, in accordance with the Code of Labor legislation of Ukraine, which regulates the procedure for calling the employees to material account. If the company officer does not have labor relationships with the company (for instance, he is a member of the board of directors or of the audit committee), the provisions of the Civil Code shall be applied to him (Article 440).

Responsibility of management members (if these persons have labor relationships with the company) may be limited in accordance with Labor legislation.

### **3. Corporate governance bodies**

In accordance with the Law of Ukraine “On Economic Companies” (Articles 41, 46, 47, 49), general shareholders’ meetings, joint stock company council (board of directors), management and the audit committee belong to the bodies of corporate governance.

General shareholders’ meeting is recognized as the supreme body of joint stock company having practically unlimited competence, for the company charter may refer other issues to the competence of general shareholders’ meeting except for those stipulated in Article 41 of the Law.

Amendments introduced to the Law “On Economic companies” in 1997 determine the circle of aspects comprising exclusive competence of general shareholders meetings and these issues cannot be delegated for consideration and resolution to other bodies of joint stock companies.

Board of directors that can be elected in the joint stock company, and election is the mandatory for companies the number of shareholders in which exceed 50 persons, shall represent the interests of the shareholders in the period between the holding the general shareholders’ meetings. The main function of the board of directors is to secure control over the activities of executive body (management). In accordance with the company’s charter, the board of directors may be delegated with some functions referred to as the competence of general shareholders’ meetings (except for those referred to as exclusive competence of general shareholders’ meetings).

Company charter may also stipulate exclusive competence for the board of directors. Alongside with this, the range of these issues is not stipulated on the level of legislation. Issues referred to exclusive competence of the board of directors by company charter may not be delegated for consideration to executive body (management).

As it is stipulated in Article 47 of the Law of Ukraine “On Economic companies”, management is the executive body of a joint stock company that implements the guidance of its current activities. An executive body can have other name, which shall be stipulated in the company charter.

Management shall solve all the issues of company’s activities, except for those that belong to the competence of general shareholders’ meeting and the board of directors. General shareholders’ meetings can adopt decisions on transfer of the part of the rights

that belong to them to the competence of management, except for those issues, which comprise the exclusive competence of general shareholders' meetings.

The Law of Ukraine "On Economic companies" defines the main principles of formation for the corporate governance bodies.

All shareholders, irrespective of the quantity and type of shares they hold, are entitled with the right to participate in the general shareholders' meetings. Voting at general shareholders' meeting is realized in accordance with the principle: one share – one vote. Members of management holding no company shares may participate in the general shareholders' meetings with the right of deliberative vote.

The board of directors shall be elected from among the shareholders at the general shareholders' meeting. Representatives of trade union or of some other body authorized by the working collective and having concluded collective agreement on the behalf of the working collective may participate in the work of the board of directors with the right of deliberative vote.

Not only shareholders, but also persons having labor relationships with the company may become chief executive officer and members of management as the executive body of the company.

The audit committee of a joint stock company implements control over the financial and economic activities of management and shall be elected from among shareholders of the company. The members of the audit committee are entitled with the right to participate in the meetings of management with the right of deliberative vote.

Ukrainian legislation excludes the possibility of combining participation in the activities of company governance bodies for certain persons. The members of the board of directors cannot be members of executive body or of the audit committee (Article 46 of the Law); neither management members, nor the members of the board of directors as well as any other company officers cannot be members of the audit committee (Article 49 of the Law).

Functions, competence and organizational principles of activities for the bodies of corporate governance of the company are just outlined in the general form in the Law of Ukraine "On Economic companies". As a rule, these aspects find their detailed reflection in internal bylaws of the companies: in by-law on the general shareholders' meeting, on the board of directors, on management, on the audit committee. As these documents are adopted within the company and by the company and possess local characteristics, realization of corporate governance functions in them is stipulated with considerable deviations and differences.

Taking into consideration the necessity to unify the corporate governance institute in the whole as well as unification of its particular mechanisms, the Draft Law of Ukraine "On Joint stock companies" stipulates detailed regulation of competence of the general shareholders' meetings, their functions and procedures for their convening and holding, as well as participation of shareholders in them. Section IV of the Draft Law entitled "General shareholders' meetings" comprises 18 articles in contrast to 5 articles available in the current Law. Exclusive competence of general shareholders' meetings is intended for considerable expansion: it shall have 28 points, as stipulated in the Draft Law, instead of 4 points stipulated in the current legislation.

Special sections shall regulate the status of the company council. Section VIII of the Draft Law entitled "The Board of directors of the company" comprises 7 articles in contrast to one article available in the current Law. Section IX "Company executive body" comprises 4 articles and stipulates the existence of both collegial (management, directorate) and sole executive body (director, general director).

In the whole, the Draft Law "On Joint stock companies" keeps loyal to traditional for Ukrainian corporate governance distribution of functions and competence among the corporate governance bodies.

General shareholders' meetings are considered as supreme company bodies. The board of directors is the company body implementing general guidance, control over the operations of the executive body and protection of shareholders' rights. The Draft Law stipulates a considerable amount of issues to be referred to the exclusive competence of the board of directors. At the same time the Draft Law preserves the institution of competence delegated from the general shareholders' meetings.

Taking into consideration the fact that the Draft Law stipulates for the board of directors not only control over the activities of executive body, but also implementation of general guidance of company's operations, one could make a general conclusion that the role of the board of directors in implementation of corporate governance functions has increased. The executive (collegial and sole) body preserves its competence on governance of the current activities of the company. The executive body is accountable to the general shareholders' meeting and to the board of directors and its role is to implement their resolutions.

The current legislation of Ukraine does not contain any limitations on issues related to quantitative composition of the board of directors or management. The question about the quantity of the board of directors or management members is solved by the general shareholders' meeting and the number of members of the bodies in question depends on the size of the company. As a rule, the number of members of the board of directors in big companies (joint stock companies) ranges from 5 to 12 persons.

Open joint stock companies organized through the process of privatization of big and middle-sized state owned enterprises, those that have undergone through the process of corporatization included, have considerable peculiarities. For enterprises in question special procedure for organization and activities was established on the level of legislation. In accordance with Provisions "On Board of directors" approved by the Resolution of the Cabinet of Ministers of Ukraine as of July 19, 1993 # 556, it is stipulated that in open joint stock companies organized on the basis of the property of state enterprises whose shares had been the objects owned by the state, boards of directors are organized on mandatory basis and shall comprise the representatives of state privatization bodies, branch ministries having interest in the company activities, Antimonopoly Committee, bank institutions and working collective. The quantitative composition of the board of directors was determined by this principal basis.

So, the board of directors of NJSC "Neftegas Ukrainy" (Ukraine Oil and Gas) comprises 11 persons, that of NJSC "Ugol Ukrainy" (Ukraine Coal) – 8 persons, Sberbank (savings bank) – 10 persons.

The board of directors composed in accordance with this principle preserves its competence till the first general shareholders' meeting, which shall be held after more than 60% of shares are sold in the process of privatization.

Any other limitations imposed by legislation related to the quantitative and personal composition for both the board of directors and management are not stipulated in the current Ukrainian legislation.

Though the current Ukrainian legislation does not impose any limits related to the possibility of participation of the same persons in activities of the board of directors of different companies, this practice (especially relevant for the members of executive bodies whose members are as a rule hired) cannot be recognized as widely spread.

Alongside with this, the appearance of big strategic investors in Ukrainian market who possess the control over the companies forms the new trends in corporate governance functions implementation. In some cases commercial banks or other big creditors require participation of their representatives in corporate governance bodies apart from paying off the debtor liabilities. However, these are only cases regulated on the basis of individual agreements and they are not stipulated on the level of legislation.

Management as the executive body of a joint stock company shall be accountable before the board of directors and general shareholders' meetings (and, afterwards, before all the shareholders) for the guidance of current activities of the company.

As far as the duties related to taking into consideration the interests of small shareholders, they are outlined in general and do not find any detailed reflection in provisions regulating the activities of the board of directors or management.

So, the shareholders who in the aggregate hold more than 10% of shares have the following rights:

- to appoint their own representatives in order to control implementation of shareholders' registration for participation in the general shareholders' meetings;
- to introduce their proposals related to inclusion of the issues into the agenda of the general shareholders' meeting;
- to demand for convening extraordinary general shareholders' meeting.

These aspects practically settle the possibilities to protect the minor shareholders' interests stipulated in the current legislation of Ukraine.

Chief executive officer and members of the executive body (management), the chairman and the members of the board of directors as well as the chairman of the audit committee are recognized as the officers of joint stock company.

Officers are subject to civil and legal (material) responsibility stipulated in the current legislation of Ukraine and for administrative and criminal responsibility in accordance with the generally applied practices for violations of the law committed by them.

General shareholders' meeting is entitled with the competence to call the officers of the joint stock company to material responsibility.

Application of measures of administrative and criminal prosecution for commitment administrative offence and crimes on the part of the officers of joint stock companies belongs to the competence of respective state bodies. Specific administrative or criminal responsibility for violation of the corporate legislation is not stipulated in the current Ukrainian legislation.

Calling to disciplinary and material responsibility of joint stock companies officers cannot be recognized as a widely spread practice in Ukraine, as this, firstly, is preconditioned by the imperfection of the civil and labor legislation in Ukraine. As it has already been stressed, no new Civil Code and new Code of Labor Laws have been adopted in Ukraine yet, which would take into account the modern requirements of the market economy.

Application of the contract form conclusion with management members in labor relationships within the joint stock companies cannot be recognized as the widespread practice either. The current Ukrainian legislation contains considerable limitations related to this aspect.

As the board of directors is elected exclusively from among the company shareholders, and the outside persons may be appointed to be the members of management on the basis of labor contract, the problem of insiders and outsiders is solved by this method in Ukraine.

Participation of independent members in the activities of the board of directors is stipulated only for state joint stock companies.

Making decisions on the amount of remuneration to be paid to company officers, to the officers of its subsidiaries, affiliates and representative offices is referred to the competence of general shareholders meeting.

Special regulations related to remuneration to be paid to members of the board of directors, management members and other company officers are stipulated in the company by-laws. The information on the amount of remuneration mentioned is not published.

The current legislation of Ukraine does not stipulate mandatory organization of specialized committees on internal audit and remunerations paid to the management. As a rule, this information belongs to the closed information.

In accordance with the valid Law of Ukraine “on Economic companies” a joint stock company shall be accountable on its liabilities only with the company’s property.

Shareholders are accountable on the company’s obligations only to the extent of shares hold by them. Hired employees (managers) are not accountable on the external company liabilities.

Neither legislation, nor court practices do not stipulate cases of receding from the principle of limited liability for joint stock companies and their shareholders.

These rules are stipulated in the perspective: in the Draft Civil Code of Ukraine and in the Draft Law “On Joint stock companies”. The Drafts mentioned are also oriented towards general principles of corporate governance and stipulate certain guarantees for protection of shareholders’ rights. They also provide with branched details related to competence and activities of all the links of corporate governance.

As it has already been mentioned, the level of corporate governance regulation in Ukraine legs far behind even of that established in the neighboring CIS-countries: Russia, Kazakhstan, Georgia and others.

Provisions “On self-regulated organization on securities market (the Order of Securities Stock Market State Committee of Ukraine as of 11.11.1997 #45) have been adopted in Ukraine. However, the infrastructure of Ukrainian stock market has not yet been formed completely, so these organizations have not been playing an important part in regulation of relationships within the stock and corporate market and do not come as the alternative bodies yet.

Though recently there has been a trend towards activization of discussion on corporate governance problems, and holding of conferences, roundtables, training seminars testify for it, the general level of corporate culture in Ukraine cannot be called efficient yet.

There have come no proposals related to establishment of the rules of the corporate governance. This situation is preconditioned by the fact that the mechanisms of financial market have not been functioning in Ukraine properly yet, and the fact that the shares are owned by mass investor is explained only by privatization processes.

#### **4. Information disclosure and transparency**

Internal and external reporting is stipulated for Ukrainian joint stock companies in accordance with the current legislation of Ukraine.

Reporting of the executive body (management) at the annual general shareholders’ meeting may be related to the internal reporting of joint stock company. It shall be complimented with the mandatory conclusions of the audit committee on the results of financial and economic activities of management.

In accordance with Article 18 of the Law of Ukraine “On Economic companies” a joint stock company shall maintain book-keeping records, make and submit financial reporting in accordance with the general requirements of the current legislation mandatory for all the subjects of entrepreneurial activities.

Statistics reporting operating with monetary equivalent is based upon the data of accounting reporting and shall be submitted in the established volume to the state statistics bodies.

General requirements to maintaining accounting records and to maintaining of records related to financial reporting are determined in the Law of Ukraine “On book-keeping and financial reporting in Ukraine” adopted on 16.07. 1999.

In accordance with Article 14 of the Law, enterprises shall submit quarterly and annual financial reporting to bodies to the sphere of governance of which they belong, to labor

collectives upon their request, to the owners (founders) in accordance with the constituent documents, if otherwise is not stipulated in the Law. Financial reporting is forwarded to the bodies of executive power and to other users in accordance with the current legislation. The Cabinet of Ministers of Ukraine establishes the term of financial reporting submission.

Alongside with this, financial reporting of the companies shall not be considered as commercial secrecy information except for cases stipulated in the legislation.

Open joint stock companies, enterprises issuing bonds, trust companies, currency and stock exchanges, investment funds, investment companies, credit associations, non-state pension funds, insurance companies and other financial institutions shall promulgate their annual financial reporting and consolidated reporting through publication in the periodical press or distribution in the form of sole printed issues no later than on the 1<sup>st</sup> of June of the year following the year of reporting.

In case the company is liquidated, liquidation committee makes a liquidation balance sheet and in cases stipulated in the current legislation of Ukraine publishes it within the term of 45 days.

Control over observing the legislative provisions on book-keeping and financial reporting in Ukraine is implemented by respective competent bodies within the limits of their powers stipulated in the current Ukrainian legislation in accordance with Article 15 of the Law under analysis.

The standards of book-keeping and financial reporting for Ukrainian enterprises were approved by Ukraine Ministry of Finance in the Orders # 87 as of 31. 03. 1999, #137 as of 28. 05. 1999, #242 as of 18. 10. 1999, # 246 as of 20. 10. 1999, # 237 as of 08. 10. 1999, #20 as of 31. 01. 2000 and # 290 as of 29. 11. 1999.

Though these standards have been developed in order to adjust the procedure for keeping financial reporting to the needs of the market economy, one cannot but state that this goal has been achieved. The process of implementation of the market standards of financial reporting faces considerable complications preconditioned by insufficient level of personnel training and inadequate technical and information basis development in this sphere.

The analysis of financial reporting standards gives ground for general conclusions. In the whole, they provide the shareholders with the opportunity to obtain complete and all-embracing information on the state of financial and economic activities of joint stock companies. At the same time, the channels through which the information reaches the persons it is intended for are not sufficiently branched and worked out, and the addressees of the information, as a rule, do not show any real interest in its receiving.

**Reporting to taxation bodies** comprises, primarily, submission of tax declarations by legal entities.

This type of reporting is implemented on the basis of:

- the Law of Ukraine “On Taxation and income of enterprises” as of 28.12.1991;
- the Law of Ukraine “On Value added tax” as of 03.04.1997;
- the Decree of the Cabinet of Ministers of Ukraine “On excise tax” as of 26.12. 1992;
- the Decree of the Cabinet of Ministers of Ukraine “On local taxes and duties” as of 20.05. 1993;
- the Law of Ukraine “On payment for land” as of 03.07.1992, and other legislative acts.

**Reporting to Securities Stock Market State Committee (SSMSC)** is stipulated taking into consideration the fact that SSMSC is the body implementing state regulation of the issuers’ activities as well as the activities of other securities market participants, joint stock companies inclusive.



Securities Stock Market State Committee (SSMSC) in accordance with the Laws of Ukraine “on State regulation of securities market in Ukraine”, “On Securities and stock exchange”, “On Economic Companies”, “On Book-keeping and financial reporting” has defined the terms and procedures for provision of regular and specific information by joint stock companies.

In particular, the Resolution of SSMSC as of 17.01. 2000 #3 approved **“Provisions on submission of regular information by joint stock companies and enterprises issuing bonds”**. The Provisions define the structure, list, form, terms and procedure for submission of regular information by joint stock companies and enterprises issuing bonds.

The Provisions determine the requirements to the report, which shall comprise the following sections:

- General information on the issuer;
- Information on the issuer’s securities;
- Business description;
- Information on proprietary state and financial and economics activities of the issuer.

Information on internal and external markets where the issuer’s securities are traded (exchange market, organizationally registered off-exchange securities markets), as well as the information on submitted applications or on intentions related to submission of applications for access to the exchange (organized markets) shall be included into the section “Information on the issuer’s securities”. If the dates of inclusion of the securities into the list and their participation in the trades are known, they shall be specified.

**“Business description”** section shall include the following information relevant for the period under review in the derived form:

- compressed information on the history of the enterprise, the significant stages of its formation;
- information on the organization structure of the issuer, of its subsidiaries, affiliates and representative offices with indication of identification, actual location, role and forecasts of development, on changes in the organization structure;
- description of the adopted accounting policies (method for calculation of depreciation, stock costs, accounting and estimation of finance investments and the like);
- information on basic types of products/services manufactured/provided by the issuer, the production forecast for certain goods or provision with services; dependence on the seasonal variations; information on main markets of sales and major clients; on the channels for sale of products/services and on methods of sales applied by the issuer; on raw material sources, their accessibility and price dynamics; information on specifics and state of development of the branch of industry the issuer belongs to, the level of new technologies implementation, new goods produced; information on competition in the branch of industry the issuer belongs to, on specific features of products/services of the issuer compared to the products/services of the competitors;
- information on considerable problems influencing the operations of the issuer; the degree of dependence on legislative or economic limitations;
- information on the facts of fine and compensation payments for violation of the current legislation of Ukraine;
- description of policies adopted in respect to financing activities of the issuer, sufficiency of the working capital for the enterprise’s current needs, possible ways of liquidity in accordance with the estimates provided by the issuer’s experts;
- information on the price of concluded but not yet executed contracts/agreements valid for the end of the period under review (general conclusions) and on profits expected after execution of the contracts/agreements mentioned;

- forecasts and plans for at least a year on the activities of the issuer (related to production expansion, modernization, financial state improvement, description of considerable factors able to impact the activities of the issuer in future); description of the issuer's policies related to research and development, with specification of the amount of research and development costs for the year under review;
- other information that may be relevant for the investor in order to enable him to estimate the financial state and results of activities of the issuer.

Provided that the information on results and analysis of maintaining economic activities for the previous three years is supplied, this information may be attached to the report as the analytical reference in the derivative form.

The section **“Information on proprietary state and financial and economic activities of the issuer”** shall specify, except for other relevant information, data on fixed assets owned or used by the issuer (with specification of the terms and conditions of fixed assets disposal (on basic groups), the degrees of their wearing and disposal, as they precondition considerable changes in fixed assets cost, as well as information on all the limitations related to disposal of property by the issuer).

Besides, the following documents shall be submitted: Enterprise balance sheet, Financial results report, Cash flow report, Owned capital report and notes to the reports mentioned; Securities issue, sale and circulation report.

Audit conclusions in the written form shall be attached to annual financial reporting.

The report shall be attached with the copies of general shareholders' meetings for the period under review, which dealt with solving the issues related to the exclusive competence of general shareholders' meeting.

If the issuer due to objective reasons cannot specify some kind of information required in the Provisions mentioned above, he shall specify the reasons for non-submission of mandatory information in the respective report attachment.

The issuer shall bear responsibility for failure to submit, untimely submission or submission of inadequate information deliberately in accordance with the Law of Ukraine “On State regulation of securities market in Ukraine”.

The procedure for submission of **specific information** by the issuers was determined by SSMSC in the respective **“Provisions on submission of specific information by joint stock companies and enterprises issuing bonds”** approved by the Resolution of SSMSC as of 17.01. 2000 #5.

The Provisions contain the notion of specific information, which is defined as information on changes in financial and economic as well as governance activities of securities issuer, which have occurred and influence the value of securities or the amount of income on them.

In particular, the following information is referred to specific:

- 1) information on changes of rights for securities, which shall include:
  - information on adoption of a decision on changes of rights for the owners of securities by general shareholders' meeting. The information shall specify the case of the matter taken as the ground for introduction of changes mentioned. The date when the general shareholders' meeting adopted the respective resolution shall be considered the date of the event;
  - information on adoption of the decision on redemption of its own shares by the company. The date when the general shareholders' meeting adopted the resolution on redemption of shares shall be considered the date of the event;
- 2) information on changes in the personal composition of issuer's officers: information on appointment and dismissal of issuer's officers, on appointment and dismissal of the chief

- accountant of the issuer, if he/she does not belong to the executive body (management). The date when the resolution was adopted shall be considered the date of the event;
- 3) information on sequestration of the bank accounts of the issuer. Description of the events related to sequestration or release of sequestration of any bank accounts of the issuer shall be submitted. The date when the issuer received the copy of respective decision shall be considered as the date of the event;
  - 4) information on the start of readjustment activities (implementation of complex measures aimed at improving the financial state of the issuer). The date of adoption of a decision on readjustment shall be considered the date of the event (start of readjustment activities). The date of adoption of resolution on bringing the action on bankruptcy by arbitration court shall be considered the date of bringing the action on bankruptcy;
  - 5) information on restructuring of the issuer: information on adoption of a decision on merger, affiliation, split-off, segregation, transformation of the issuer by the general shareholders' meeting of the issuer. The date when the general shareholders' meeting adopted the respective resolution shall be considered the date of the event;
  - 6) information on suspension or cessation of the issuer's activities:
    - information on the suspension of the validity of the issuer's license (permit) for implementation of activities and on renewal of its validity. Information on licenses (permits) for implementation of professional activities in the field of securities market shall be published but not submitted to the Committee. The date when the copy of the respective decision from the body that issued the license was received shall be considered the date of the event;
    - information on cessation of the issuer's activities in accordance with the decision of the general shareholders' meeting of the issuer or on liquidation of the issuer in accordance with court decision (Appendix 9). The date of adoption of the respective decision by the general shareholders' meeting of the issuer or the date when the copy of court (arbitration court) decision was received shall be considered the date of the event;
  - 7) information on demolition of property of the issuer due to emergency. The information shall specify the fact of demolition of at least 10% of the property (the sum of assets in accordance with the balance sheet as of the beginning of the year under review) of the issuer. The date of property demolition shall be considered the date of the event;
  - 8) information on advancing a claim to the issuer for the amount exceeding 10% of the charter capital of the issuer or the sum of fixed and turnover assets of the issuer. The date when the issuer received the copy of claim application shall be considered the date of the event;
  - 9) information on receiving a credit or information on issue of securities for the sum that exceeds 50% of the charter capital or of the sum of fixed and turnover assets of the issuer:
    - information on receiving the credit for the sum that exceeds 50% of the charter capital or of the sum of fixed and turnover assets of the issuer. The date when the assets or material values were received shall be considered the date of the event;
    - information on adoption of a decision on issue of securities for the amount that exceeds 50% of the charter capital or of the sum of fixed and turnover assets of the issuer. The date when the general shareholders' meeting of the issuer adopted the respective decision shall be considered the date of the event.

Within two working days after the date of the respective event the issuer shall present (with courier or by mail) the notification to Securities stock Market State Committee. Notification shall be secured in electronic and hard copy forms.

Within the week from the moment of submission of notification by the issuer or the moment SSMSC received the notification by mail specific information on the issuer shall be placed on official web page of SSMSC.

The issuers shall publish specific information (in notification or text format) in one of the official press bodies of the stock exchange where the issuer's securities are listed no later than the term stipulated in the current legislation of Ukraine. The issuer shall submit a sample of the issue of the press body with the information published within 10 days after the information is published.

If the issuer publishes inadequate specific information, it shall immediately notify of it Securities Stock Market State Committee and take measures on introducing corrections into the information within two working days (adequate specific information shall be secured for publishing), and in case if publishing inadequate specific information is the fault of the publisher, measures shall be taken in order to secure publishing corrected information.

The Provisions also define the grounds and terms on liability of the issuers related to provision with specific information. In accordance with them, if the issuer cannot specify some part of information referred to specific and required in the Provisions mentioned due to objective reasons, a note "The data are absent" (or "0") is entered into the respective article, and the issuer shall specify the reasons of absence of mandatory information in the explanatory notes attached to the information.

The issuer shall bear responsibility for failure to submit, untimely submission or submission of inadequate information deliberately in accordance with the Law of Ukraine "On State regulation of securities market in Ukraine".

The Law of Ukraine "**On Audit activities**" adopted on April 22, 1993 stipulates the regulatory basis for implementation of audit activities in Ukraine. The Law shall be applied to all subjects of economic activities, irrespective of forms of ownership and types of activities, as well to state executive bodies.

Audit activities shall include organizational and methodological provisions of audit, practical implementation of audit controls (audits) as well as provision with other audit services.

Audit services may be provided in the form of conduct of audit controls (audits) and provision with expertise services related to them, provision with consultations on the issues of book-keeping, reporting, taxation, analyzing financial and economic activities as well as other types of services related to economic and legal regulation of entrepreneurial activities of the natural and legal entities.

Audit shall be defined as control of public book-keeping reports, accounting, source documents and other information related to financial and economic activities of subjects of economic activities aimed at securing the adequacy of their reporting, accounting, securing that it is complete and corresponds to the current legislation of Ukraine and established standards.

Audit shall be implemented by independent entities (auditors, audit firms) duly authorized by subjects of economic activities.

Audit may be implemented upon the initiative of the subjects of economic activities and in cases stipulated in the current legislation of Ukraine (mandatory audit).

#### **Audit conclusions.**

The Law stipulates the terms for submission of public bookkeeping reporting. In accordance with this Article, public book-keeping reporting shall comprise audit conclusions, balance sheet, income and losses report, other reporting falling within the limits of information that shall not be considered as commercial secret and is determined in the legislation as information to be submitted to the users and for publication.

Alongside with this, **audit conclusions** on adequacy, fullness and correspondence to the current legislation, established norms of balance sheet and other forms of public book keeping reporting maintenance **shall be based on the analysis of considerable amount**

**of information related to the results of financial and economic activities**, examining book keeping reports and documents considered as commercial secret and not intended for publication inclusive.

Disclosure of financial reporting referred to commercial secrecy for audit conduct and provision with other audit services is done by the users of commercial reporting.

Article 8 of the Law outlines the following circle of users of bookkeeping reporting: duly authorized in accordance with the current Ukrainian legislation representatives of state power bodies, legal entities and natural persons interested in the results of economical activities of the audit subjects. Legal entities and natural persons may include: owners and founders of the subject of economic activities, creditors, investors and other legal entities and physical persons, which in accordance with the current legislation of Ukraine are entitled with the right to obtain information contained in book keeping reports.

The users of book keeping reports are entitled with the right to come as the clients on audit conduct and conduct of other audit services, to determine the volume and directions of audit controls within the range of the competence stipulated in the current Ukrainian legislation, constituent documents of the company or respective agreements.

Article 10 of the Law defines cases for mandatory audit conduct. They shall be the following:

- 1) confirmation of adequacy and fullness of the annual balance sheet and reporting of commercial banks, funds, exchanges, associations, cooperative associations, companies and other economic subjects irrespective of the form of ownership and types of activities. Their reporting shall be subject to official promulgation except for state budget institutions and organizations not involved in entrepreneurial activities. Alongside with this, mandatory audit control of the annual balance sheet and reporting of the subjects of economic activities having the annual economic turnover of less than 250 non-taxable minimums shall be held once in three years;
- 2) control of financial state of the founders of commercial banks, enterprises with foreign investments, joint stock companies, holding companies, investment funds, trust companies and other financial intermediaries;
- 3) issuers of securities;
- 4) state enterprises when granting on lease of complex property, in cases of privatization, corporatization and other changes in the form of ownership;
- 5) when bringing an issue on recognizing the enterprise insolvent or bankrupt.

Conduct of audit is considered mandatory also in other cases stipulated in the current legislation of Ukraine.

The manager of the subject of economic activities shall bear responsibility for observing the procedures of bookkeeping stipulated in Ukrainian legislation and for timely and full presentation of book keeping reports to the users and auditors (Article 11 of the Law).

Public book keeping reporting shall be checked by the auditor (audit firm) and can be subject for promulgation within the year following the year under review.

Audit controls do not exclude the possibility of control over compliance with the procedures established in the current legislation of Ukraine and related to taxation on the part of state tax inspections. Control functions may also be implemented by other subjects duly authorized for it in accordance with the current Ukrainian legislation.

In accordance with Article 21 of the Law, audit conclusions shall be made taking into consideration respective norms and standards. They shall contain confirmation or grounded refusal to confirm adequacy, fullness and correspondence to the current Ukrainian legislation related to book keeping of the client.

The procedure for registration of other documents related to the results of provision with audit services is regulated by Ukraine Audit Chamber that takes into account meeting the requirements of the Law mentioned as well as other legislative acts of the current Ukrainian legislation.

The law also determines the duties of the auditors and audit firms. In accordance with Article 8 of the Law, auditors and audit firms shall:

- 1) duly provide with audit services, check the state of bookkeeping and reporting of the client, their adequacy, fullness and correspondence to requirements stipulated in the current legislation and established standards;
- 2) inform the owners, persons authorized by them and clients on revealed drawbacks in book keeping and reporting during audit conduct;
- 3) secure secrecy of information obtained during audit conduct and provision with other audit services. Not to promulgate information subject to commercial secrecy and not to use the information in question in their interests or in the interests of the third parties;
- 4) be accountable before the client for violation of agreement conditions in accordance with the current legislation norms adopted in Ukraine;
- 5) limit their activities to provision with audit services and other types of activities directly related to provision with audit services in the form of consultations, controls and expertise assistance.

Besides, the Law stipulates specific requirements related to audit conduct aimed at securing objective expertise when conducting audit.

So, in accordance with Article 24 of the Law, conduct of audit shall be prohibited in the following cases:

- 1) by auditor having direct family relationships with management of the subject of economic activities under control;
- 2) by auditor having personal proprietary interest in the subject of economic activities under control;
- 3) by auditor who is the member of management, founder or owner of the subject of economic activities under control;
- 4) by auditor having employment relationships with the subject of economic activities under control;
- 5) by auditor who is the employee, party in the ownership of subsidiary, affiliate or representative office of the subject of economic activities under control.

Auditor (audit firm) shall bear material and other responsibility, determined in the agreement in accordance with the requirements of the current Ukrainian legislation (Article 25 of the Law) for unduly execution of duties.

The amount of material responsibility of the auditors (audit firms) shall not exceed actual damage caused to the client through their fault.

All the material arguments between the client and the auditor (audit firm) shall be solved in the court.

Besides, in accordance with Article 26 of the Law, the auditor may become subject to application of penalty by Ukraine Audit Chamber. The penalty may come in the form of notice, suspension of certificate and license validity for the term of up to one year or annulment of certificate or license for unduly execution of professional duties.

In accordance with Article 27 of the Law, on the basis of the decision of Ukraine Audit Chamber, penalty in the form of cessation of validity of certificate or license for provision with audit services may be applied to the auditor in the following cases:

- 1) registration of repeated facts of low quality of the audits conducted;
- 2) regular rough violations of the current legislation of Ukraine and established audit norms and standards.

At the same time, Article 30 of the Law stipulates responsibility for the subject of economic activities when audit control is conducted. In accordance with this article, management of the subject of economic activities shall bear personal responsibility for fullness and adequacy of book keeping and other documents presented to the auditor (audit firm) for audit conduct in accordance with the current legislation of Ukraine.

In cases when the facts of provision with inadequate or incomplete book keeping documents are revealed, auditor (audit firm) shall notify of it the client no later than on the day of finishing the control or provision with other services.

In accordance with Article 29 of the Law, subjects of economic activities mentioned in point 1 of Article 10 shall submit audit conclusions and other documents referred to public book keeping reporting to the respective Ukraine tax inspection office within the term of 9 months of the year following the year of reporting.

Audit conclusions shall be submitted to respective tax inspection office within ten days after the audit control is finished. In case of failure to submit or untimely submission of the audit conclusions to respective tax inspection offices caused by the subject of economic activities, the latter shall be subject to application of financial sanctions and administrative penalties stipulated in the current legislation of Ukraine.

In some cases the current legislation of Ukraine stipulates **specific requirements to audit control**.

In particular, Securities Stock Market State Committee adopted “Requirements to audit control of open joint stock companies and enterprises issuing shares (except for commercial banks and institutional investors)” in the Resolution #5 as of 19. 03. 1997. The document mentioned determines the list of questions on the basis of which independent auditors shall confirm that book keeping reports of the open joint stock companies and enterprises issuing bonds is complete and adequate, and form the conclusions on their actual financial state.

As the analysis made testifies, submission of various forms of reporting by joint stock companies and the procedures and terms for audit conduct, mandatory audits included, in Ukraine are regulated with considerable degree of details. However, in practice, state bodies implementing the functions of control, but not shareholders and other persons interested in the corporate sector, use this reporting and results of the audit committee. It can be explained by the fact that financial sector in Ukraine is not sufficiently developed and its mechanisms are on the stage of formation.

As it has already been mentioned, the current Ukrainian legislation does not contain any special provisions related to merger of companies aimed at securing corporate interests’ guarantees. The available norms that determine specific procedures for economic concentration are aimed at securing antimonopoly regulation and make a component part of not corporate, but antimonopoly legislation.

## GENERAL CONCLUSIONS

The Law of Ukraine “On Economic companies” adopted in 1992 does not secure due regulation of corporate relationships and does not facilitate effective corporate governance presently.

It is also worthwhile to mention considerable disproportions in legal regulation of corporations’ activities. On the one hand, legislation related to securing state control over the activities of joint stock companies has being developed dynamically enough, which can be explained by the active position of Securities Stock Market State Committee, on the other hand, development of corporate legislation called to establish the legal framework for relationships inside the corporations is legging far behind.

These problems are considerably deepened and sharpened in relation to the absence of the civil market legislation and incompleteness of administrative and court reform in Ukraine.

Without any exaggeration, the factors mentioned may be considered as serious obstacles on the way of Ukraine to implementation of market reforms, establishment of favorable investment climate and integration into European and international market.

So, the main directions of long-term reformation of Ukrainian legislation can be determined in the following way:

- accomplishment of the court reform and establishment of the framework of independent courts of Ukraine the functioning of which shall secure compliance with legislation, within the corporate sector inclusive;
- implementation of full value administrative reform in the process of which the functions of state regulation and control over entrepreneurial activities shall obtain adequate regulation;
- adoption of new Civil Code of Ukraine to serve as the basic system act of the private law;
- adoption of the Law of Ukraine “On joint stock companies” that would take into consideration all the aspects of joint stock companies’ activities in Ukraine and establish reliable legislative basis for national corporate legislation formation;
- further development and consolidation of legislation related to disclosure of information on corporate activities, provided that it shall be transparent, addressee-oriented and effective in application within the field of corporate governance.



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