



UKRAINE

TECHNICAL ASSISTANCE REPORT—REGULATION OF MARKET ABUSE AND ISSUER DISCLOSURE REQUIREMENTS

July 2016

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REGULATION OF MARKET ABUSE AND ISSUER DISCLOSURE REQUIREMENTS

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July 2016

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GLOSSARY

CSMAD	Directive on Criminal Sanctions on Market Abuse (Directive 2014/57/EU)
EU	European Union
GAAP	Generally Accepted Accounting Principles
IFRS	International Financial Reporting Standards
IOSCO	International Organization of Securities Commissions
JSC	Joint Stock Company
MAR	Market Abuse Regulation (Regulation 2014/596/EU)
MCM	Monetary and Capital Markets Department of the IMF
MEDT	Ministry of Economic Development and Trade
MiFID	Markets in Financial Instruments Directive (Directive 2004/39/EC, as amended)
MMOU	Multilateral Memorandum of Understanding
MTF	Multilateral Trading Facility
NBU	National Bank of Ukraine
NSSMC	National Securities and Stock Market Commission
OTC	Over-the-counter
PD	Prospectus Directive (Directive 2003/71/EC, as amended)
PR	Prospectus Regulation (Regulation (EC) No 809/2004, as amended)
RM	Regulated Market
SRO	Self-Regulatory Organization
TA	Technical Assistance
TD	Transparency Directive (Directive 2004/109/EC, as amended)

PREFACE

At the request of the National Securities and Stock Market Commission (NSSMC), a Monetary and Capital Markets Department (MCM) technical assistance (TA) mission visited Kyiv, Ukraine during January 11–22, 2016 and April 6–19, 2016. The mission was executed within the framework of the Government of Canada-funded, IMF-administered Technical Assistance Project. The mission members included Ms. Eija Holttinen (mission chief) and Mr. Ville Kajala and Mr. Sebastian de Schmidt (MCM experts).

The mission advised the Ukrainian authorities on the changes needed to align the Ukrainian legislative and regulatory framework on market abuse and issuer disclosure requirements with the relevant international standards, taking into account the European Union (EU) Market Abuse Regulation (MAR), the Directive on Criminal Sanctions on Market Abuse (CSMAD), as well as the Prospectus (PD) and Transparency Directives (TD).

The mission met with Chairman Timur Khromaev and other senior officials of the NSSMC. Meetings were also held with senior officials of the National Bank of Ukraine (NBU), Supreme Court, Ministry of Economic Development and Trade (MEDT), Ministry of Internal Affairs, and State Enforcement Service as well as representatives of market participants. The mission would like to express its appreciation to Ukrainian authorities and market participants for providing their senior officials' valuable time for in-depth discussions with the mission.

EXECUTIVE SUMMARY

The Ukrainian regulatory framework for market abuse and issuer disclosure requirements has significant gaps, whose impact is compounded by the NSSMC's lack of sufficient supervisory, investigative, and enforcement powers. This has contributed to overall lack of transparency and widespread misconduct in the market, including through issuance and trading of “fictitious” securities. To address the current challenges, the Ukrainian legislation needs to be aligned with the international standards to provide the NSSMC with sufficient means to require enhanced disclosures and combat market abuse. With this objective, the NSSMC has prepared draft proposals to amend the Ukrainian legislation in these two areas, taking into account the relevant EU legislation.

The legislative challenges in the two areas are different. The new issuer disclosure requirements have to build on, but over time also appropriately transition away from the unconventional scope of application of the current requirements. This transition will take time. In contrast, the new market abuse legislation can largely be built from scratch. While this has a number of benefits, implementing advanced reporting and disclosure requirements will require the NSSMC and market participants to adopt new systems and procedures. In both areas, the draft laws are well advanced in aligning the Ukrainian framework with the EU legislation, but additional work is needed on some details. The role of securities legislation in determining the disclosure requirements for non-listed banks and state-owned enterprises also has to be agreed on with the other relevant authorities.

In addition to technical changes, the draft laws are intended to introduce a significant change in the NSSMC's and criminal authorities' enforcement powers. The draft amendments follow on the changes proposed in the draft Independence Law, and largely build on the requirements of EU legislation. However, there is still a need to ensure that the powers are appropriately designed to fit the broader Ukrainian legal framework, in particular in the criminal side. Where responsibilities overlap, it is important that authorities agree on the most appropriate division of responsibilities and collaboration. Completion of such inter-authority consultation is essential before proceeding with the legislative proposals.

To be effective, the new legislation will have to work in a coherent manner with the other pending initiatives. This includes the Independence Law, the Law on Regulated Markets and Derivatives and other possible future legislative initiatives. It is therefore important that the schedule and order of submitting the laws to the Parliament will be carefully planned to avoid gaps and inconsistencies in the new framework.

Table 1. Summary of Main Recommendations

Recommendation	Timeframe
Issuer disclosure requirements	
NSSMC to make a final decision on the disclosure requirements it will propose to be applied to various type of issuers	End-July 2016
NSSMC to consult all relevant authorities (at least the NBU and MEDT) on the draft legislative proposals implementing the PD, TD, and MAR disclosure requirements	End-September 2016
NSSMC to revise the draft legislative proposals to incorporate the above decision, the comments of other authorities and this advice	End-November 2016
Market abuse	
NSSMC to consult all relevant authorities on the draft legislative proposals <ul style="list-style-type: none"> • At least the criminal authorities and the Supreme Court on those implementing the CSMAD and related amendments • At least the NBU on those implementing the MAR powers and sanctions in relation to banks 	End-September 2016
NSSMC to revise the draft legislative proposals to incorporate the comments of other authorities and this advice	End-November 2016
Legislative process	
NSSMC to ensure consistency between the pending Independence Law and Law on Regulated Markets and Derivatives and the new draft laws implementing the PD, TD, and MAR	End-November 2016
NSSMC to incorporate the changes related to implementing the PD, TD, and MAR into one legislative proposal so that all changes will be discussed and will enter into force at the same time	
Powers and sanctions	
Authorities to ensure that the enhanced powers for the NSSMC will be adopted as proposed in the draft Independence Law reviewed by the MCM July 2015 mission	End-September 2016
Authorities to ensure that appropriate administrative and criminal sanctioning powers will be included in the legislative proposals	End-November 2016
NSSMC regulations and procedures	
NSSMC to finalize the necessary draft regulations implementing the PD, TD, and MAR provisions not covered by the draft laws and initiate market participant consultation	End-June 2017
NSSMC to adopt appropriate administrative procedures for taking the new administrative measures and sanctions	End-November 2017
Future amendments	
Follow the development of the EU Level 1 and Level 2 legislation and adjust the Ukrainian framework, as appropriate	As needed
Consider adjusting the requirements for admission to trading on multilateral trading facilities (MTFs), in particular if a significant number of issuers will be subject to trading only on an MTF	At the latest when implementing relevant EU legislation

I. INTRODUCTION

1. The primary objective of the ongoing MCM TA to the NSSMC is to enhance the Ukrainian securities regulatory framework's compliance with the international standards.

Previous MCM TA missions have advised the Ukrainian authorities on how to enhance the powers and independence of the NSSMC in line with the International Organization of Securities Commissions (IOSCO) Objectives and Principles of Securities Regulation (IOSCO Principles). At the request of the NSSMC, this report focuses on advising the Ukrainian authorities on how to improve the quality of Ukrainian securities legislation in selected priority areas. These relate to enhancements to issuer disclosure requirements and to the introduction of a more robust framework to prohibit market abuse and provide the authorities with appropriate tools and powers to enforce compliance with disclosure requirements and detect and sanction market abuse. The findings and recommendations of the report are based on the review of the draft legislative proposals prepared by the NSSMC.¹

2. Ukraine has an Association Agreement with the EU requiring it to implement relevant EU legislation by the end of 2020. That includes legislation on market abuse and issuer disclosure requirements. The primary EU legislation covering these areas consists of the PD, TD, MAR, and CSMAD. This so called "Level 1" framework is complemented by a range of "Level 2" measures. A list and hyperlinks to the relevant EU legislation are included in Appendix I.

3. Existing Ukrainian legislation has significant gaps compared to the IOSCO Principles and EU legislation. In order to develop a concrete framework for closing these gaps and at the same time advising the Ukrainian authorities on how to prepare for complying with the EU requirements, the mission has based its advice on legislative changes not only on the IOSCO Principles, but also on the relevant EU legislation. The current review has been limited to the substantive provisions of the EU legislation. It is recommended that the Ukrainian authorities address the provisions relating to the operation of the EU internal market at a later stage.

4. Requirements deviating from the EU legislation have been proposed in certain cases.

This applies where the EU requirements do not necessarily ensure full compliance with the IOSCO Principles when applied to the particular circumstances of the Ukrainian market. This has also been done where the mission considered that the level of market development in Ukraine justified deviations from the current EU requirements before transitioning to the full EU framework.

¹ The mission reviewed the following versions of the draft legislative proposals: changes implementing the PD ("PD law") dated April 5, 2016; changes implementing the TD ("TD law") dated April 1, 2016; and changes implementing the MAR and CSMAD ("MAR law") dated April 1, 2016.

II. CHALLENGES IN DEVELOPING THE NEW LEGISLATION

A. Existing Framework

5. **In some areas, the Ukrainian market structure and practices differ significantly from those in developed markets.** In the focus areas of the mission, the key differences relate firstly to the mandatory listing requirement for all public joint stock companies (JSCs). The second notable difference is that private placements currently require essentially the same type of prospectus as public offers, and issuers that have only made a private placement are subject to certain periodic and ad hoc disclosure requirements. A summary of the existing requirements is in Appendix II. International standards and EU legislation are based on imposing disclosure requirements on issuers that have made a public offer or whose securities are admitted to trading on an exchange (regulated market). This difference of approach makes designing an appropriate future model for the Ukrainian market very challenging.

B. Ongoing Legislative Reform

6. **Previous MCM missions have provided advice on the powers the NSSMC would need to have to comply with the requirements for the signatories of the IOSCO Multilateral Memorandum of Understanding (MMOU).** Shortly after the April mission, some parts of the draft Law on Amending Some Legal Acts on Implementing IOSCO Principles on the Functioning of the Securities Regulator (“Independence Law”) reviewed by the MCM July 2015 mission were submitted to the Verkhovna Rada. However, these parts do not include the provisions due to enhance the NSSMC’s supervisory, investigative and enforcement powers, which would also help ensure the Ukrainian legislation’s compliance with the PD, TD, and MAR requirements for the powers of the competent authority.

7. **Another challenge relates to the ongoing implementation of legislation that will in principle require all public JSCs to comply with strict exchange listing and corporate governance requirements or convert their legal form to private JSCs or limited liability companies.** The NSSMC’s original objective was that this requirement would lead to a significant drop in the number of listed companies (to only about 15). However, the NSSMC has since revised its thinking and now intends to propose that, in addition to exchanges², securities of public JSCs that do not meet the listing (admission to trading on a regulated market (RM)) criteria could be admitted to trading on EU type MTFs operated by exchanges (market operators). The current legislation does not recognize MTFs, neither are references to them incorporated in the draft Law on Regulated Markets and Derivatives.³ The draft PD, TD, and MAR laws reviewed by the mission did not yet include the NSSMC’s emerging thinking on the regulation of MTFs. As a result, the mission has not been able to complete the detailed review of the draft PD, TD, and MAR laws as originally intended.

² Under the proposed Law on Regulated Markets and Derivatives, the reference to EU type RMs replaces the reference to stock exchanges.

³ MCM has not assisted the NSSMC in drafting the proposal on the Law on Regulated Markets and Derivatives. The proposed law was approved in the first reading in the Verkhovna Rada on March 31, 2016.

8. **The draft laws reviewed by the mission did not yet include sufficient details on the disclosure requirements planned to be applied to various categories of issuers.** The mission discussed various options with the NSSMC, and the model preferred by the NSSMC that the mission used as a basis for its further work is summarized in Tables 2 and 3. The key design principles of the model are:

- The current Tier 1 and Tier 2 listings would correspond to admission to trading on an RM.
- Only those public JSCs that are admitted to trading on an RM and/or that make a public offer of securities after the entry into force of the new requirements will be subject to the new enhanced disclosure requirements intended to comply with the PD and TD. For issuers that have made a public offer of securities, the same requirements apply independent of whether their securities have been admitted to trading on an RM or MTF.
- Those public JSCs that do not convert to private JSCs but do not make any new public offers after the entry into force of the new prospectus requirements will be required to be admitted to trading on an MTF operated by an exchange (market operator), but can continue to comply with the existing disclosure requirements during a transitional period. By the end of the transitional period (before converging to the EU Markets in Financial Instruments Directive (MiFID) requirements), the NSSMC will have to determine what kind of disclosure requirements it will require MTF operators to have for issuers whose securities are admitted to trading only on an MTF.
- The issuers that have only made private placements would remain subject to the existing disclosure requirements.

Table 2. Disclosure Requirements in Relation to Issuers of Shares

	Shares admitted to trading on an RM (public JSCs only)	Public offer after entry into force of the PD law (public JSCs only)¹	No public offer after entry into force of the PD law (public JSCs² and private JSCs)
Prospectus requirements	Compliant with EU legislation	Compliant with EU legislation	Decision of placement for private placements ³
Annual financial information	Compliant with EU legislation	Same as for shares admitted to trading on an RM ⁴	Currently existing regime
Quarterly financial information	Compliant with EU legislation	Same as for shares admitted to trading on an RM ⁴	No ⁵
Major shareholding notifications	Compliant with EU legislation	Same as for shares admitted to trading on an RM ⁴	Public JSCs: Same as for shares admitted to trading on an RM Private JSCs: Currently existing regime
Disclosure of ad hoc/inside information	Compliant with EU legislation	Same as for shares admitted to trading on an RM ⁴	Currently existing regime (if admitted to trading on the issuer's application)
Source: NSSMC			
¹ Private JSCs wishing to make a public offer of shares would have to convert to public JSCs. Shares of a public JSC that has made a public offer would have to be admitted to trading on an RM or MTF.			
² Public JSCs that are not compliant with the requirements for admission to trading on an RM and/or that are in the process of converting to private JSCs within the transitional period provided in the Law on Joint Stock Companies. Shares of such public JSCs would have to be admitted to trading on an MTF.			
³ As currently proposed in the draft PD Law.			
⁴ EU legislation only applies to issuers with securities admitted to trading on an RM. IOSCO Principles also apply to issuers that have made a public offer of securities.			
⁵ Except for financial institutions and companies with state ownership interest of at least 25 percent.			

Table 3. Disclosure Requirements in Relation to Issuers of Non-Equity Securities

	Securities admitted to trading on an RM	Public offer after entry into force of the PD law	No public offer after entry into force of the PD law¹
Prospectus requirements	Compliant with EU legislation	Compliant with EU legislation	Decision of placement for private placements ²
Annual financial information	Compliant with EU legislation	Same as for securities admitted to trading on an RM ³	Currently existing regime
Quarterly financial information	Compliant with EU legislation	Same as for securities admitted to trading on an RM	No ⁴
Major shareholding notifications	N/A	N/A	N/A
Disclosure of ad hoc/inside information	Compliant with EU legislation	Same as for securities admitted to trading on an RM	Currently existing regime
Source: NSSMC			
¹ Including legacy issuers not compliant with the requirements for admission to trading on an RM.			
² As currently proposed in the draft PD Law.			
³ EU legislation only applies to issuers with securities admitted to trading on an RM. IOSCO Principles also apply to issuers that have made a public offer of securities.			
⁴ Except for financial institutions and companies with state ownership interest of at least 25 percent.			

C. Recommendations

9. **The NSSMC has made rapid progress in designing the new legislative framework, but it is important to ensure that the new laws will form a coherent framework.** The Law on Regulated Markets and Derivatives that is already being discussed at the Verkhovna Rada and the PD, TD, and MAR laws are closely interlinked. For this reason, the mission recommends that:

- The NSSMC makes a final decision on the regulatory framework applicable to each type of issuer identified in Tables 2 and 3. Before finalizing the legislative proposal, the NSSMC is strongly encouraged to consult the NBU and other relevant authorities, in particular those responsible for state-owned enterprises (such as the MEDT).
- The NSSMC makes the proposal for changes to the Law on Regulated Markets and Derivatives permitting MTFs and waits for the approval of that law.
- The NSSMC consolidates the draft PD, TD, and MAR laws into one legislative proposal, with the intention that all changes enter into force at the same time. This is important because many of the provisions in the laws are interlinked and have to enter into force at the same time for the framework to reach its full effect.

III. ISSUER DISCLOSURE REQUIREMENTS

A. Issuer Initial Disclosure Requirements

Findings

10. **The current initial disclosure requirements do not comply with IOSCO Principle 16 or the key provisions of the PD.** IOSCO Principle 16 requires full, accurate, and timely disclosure of financial results, risk and other information which is material to investors' decisions. Art. 5(1) of the PD requires the prospectus to contain all information which, according to the particular nature of the issuer and of the securities offered to the public or admitted to trading on an RM, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses, and prospects of the issuer and of any guarantor, and of the rights attaching to such securities. This information must be presented in an easily analyzable and comprehensible form.

11. **Significant deficiencies relate to all of the above requirements.** NSSMC regulation No 1073 does not require the issuer to present an operating and financial review or a management report containing an analysis of the development of the issuer's business. Disclosure of financial information is limited in all prospectuses to balance sheets and profit and loss statements and excludes cash flow statements and notes to the financial statements. Financial information is required to be disclosed only for the latest full financial year and the latest quarterly period. Risk disclosures are limited to risks relating to the issuer and do not cover the risks relating to the securities or potential guarantor. As a result, the information required to be disclosed in connection with a securities offering does not allow prospective investors to make an informed assessment of the characteristics and risks of the issuer and the securities on the basis of information required to be published in a prospectus.

12. **There is no efficient regime for supplementing the prospectus.** The Law on Securities and Stock Market does not permit the issuer to make changes to the prospectus once the subscription period for the securities has started. Art. 16 of the PD requires a supplement to the prospectus to be prepared in certain cases to ensure that potential investors have sufficient and up-to-date information to support their investment decision.⁴ In case of public offers, publication of a supplement also triggers a right for investors to withdraw their acceptances in case they have agreed to purchase or subscribe for the securities before the supplement is published.

13. **The Ukrainian framework does not make a distinction between the prospectus requirements for public offers and private placements.** Essentially the same kind of prospectus is required for both public offers and private placements without exemptions. For public offers, the prospectus has to be published whereas for private placements it is sufficient to make it available to investors subject to the offer. There is no separate requirement for a prospectus when securities are sought to be admitted to trading. IOSCO Principle 16 applies to public offers and admissions to trading. Art. 3(1) and 3(3) of the PD require a prospectus to be published whenever securities are offered to the public or admitted to trading on an RM, subject to the exemptions provided in the PD.

14. **The NSSMC is required to register the securities issue and the prospectus, and the process focuses on compliance with the legal requirements.** The process of issuing securities is regulated in a very detailed manner in the Law on Securities and Stock Market and related NSSMC regulations. The rules set out a mandatory order for steps and decisions to be taken by the issuer. The NSSMC process focuses more on confirming that the legal requirements for the registration of the securities issue are met rather than on scrutinizing the information to be disclosed to investors in the prospectus. Art. 2(1)(q) of the PD sets the criteria for the approval of a prospectus. The competent authority has to scrutinize the completeness of the prospectus, including the consistency and comprehensibility of the information given. The PD does not regulate the registration procedures for securities issues, but limits the powers of the host member state competent authorities to apply a registration requirement.⁵

15. **As currently drafted, the Law on Securities and Stock Market can limit the future development of new types of instruments.** The law is prescriptive in that it defines the types and categories of securities that may be issued in Ukraine. The approach used does not easily allow introducing new types of securities to the market, as any new type of security would first have to be defined in the law. PD disclosure requirements are applicable to any type of transferable security within its scope. Due to the openness of the PD and MiFID definitions of transferable securities and the limitations on the powers of the host member state competent authorities (see above), the ultimate transposition of the PD passporting rules may require adjustments to the current approach.

⁴ Art. 16 requires that every new factor, material mistake or inaccuracy relating to the information included in a prospectus that can affect the assessment of the securities and that arises or is identified between the approval of the prospectus and the final closing of the offer to the public or commencement of trading on an RM (whichever occurs later), must be mentioned in a supplement to the prospectus.

⁵ Registration of an increase of share capital is required by the EU company law Directives. However, Art. 17(1) of the PD prohibits the competent authorities of the host member states to undertake any approval or administrative procedures relating to prospectuses. Once the PD passporting rules are implemented in Ukraine, the registration requirement cannot be extended to offers where Ukraine is the host member state.

NSSMC draft legislative proposals

16. **The NSSMC has drafted legislative proposals to address the above findings and to start to converge the Ukrainian legislation towards the IOSCO Principles and the PD.** The key draft amendments relate to:

- Introducing an obligation to draw up a prospectus for public offers and admissions to trading on an RM and exemptions from such obligation (with the objective of complying with Art. 3 of the PD).
- Abolishing the obligation to draw up a prospectus for private placements. Private placements will however continue to have to be registered with the NSSMC.
- Introducing general requirements for the structure and content of a prospectus (with the objective of complying with Art. 5 of the PD).
- Amending the provisions relating to the approval and publication of prospectuses (with the objective of complying with Art. 13 and 14 of the PD).
- Introducing a regime for supplementing the prospectus (with the objective of complying with Art. 16 of the PD).

17. **The NSSMC has also identified a need to develop conduct of business rules and market practices in relation to primary markets.** The identified areas of improvement include the book-building and subscription processes and the allotment procedures. While making recommendations on these is outside the scope of the mission, the mission agrees with the need to improve the market practices.

Recommendations

18. **The suggested legislative changes appropriately address the key requirements of the IOSCO Principles and the PD.** The mission reviewed the draft legislation provided by the NSSMC and considers that the proposed amendments to the Civil Code, the Law on Securities and Stock Market, the Law on State Regulation of Securities Market, the Law on Joint Stock Companies, and the Law on Advertising address the key deficiencies in a satisfactory manner.

19. **However, further amendments to the draft legislation and existing NSSMC regulations and issuance of new regulations are required to address the details of the IOSCO Principles and the PD.** For example, the detailed content requirements for prospectuses set in the NSSMC regulations have to be amended to comply with the Level 2 Prospectus Regulation (PR) and its annexes. The mission suggests that the NSSMC addresses the following issues by amending the draft legislation or existing NSSMC regulations or by new NSSMC regulations.

- The NSSMC should conceptually separate prospectus approval from the registration procedure for securities issues and, following the separation, ensure consistent terminology⁶ throughout the provisions.

⁶ Especially the consistent use of terms public offer, admission to trading on an RM, issuer, offeror and person asking for admission to trading on an RM.

- The NSSMC should ensure that the proposed legislation adequately addresses the liability issues relating to the prospectus disclosures (to comply with Art. 6 of the PD).
- The NSSMC should ensure that all the exemptions from the requirements to publish a prospectus are covered by the regime (Art. 1, 3 and 4 of the PD).
- The NSSMC should introduce detailed disclosure requirements for prospectuses of shares, debt securities and derivative securities in line with the PR and its annexes.
- The NSSMC should ensure that the detailed rules on the format of prospectuses are in line with the PR.
- The NSSMC should introduce rules for incorporation by reference in compliance with Art. 11 of the PD and the PR.
- The NSSMC should ensure that the language regime meets the needs of the Ukrainian market and is sufficiently aligned with Art. 19 of the PD.

20. **The proposed transitional provision regarding share offerings of private JSCs is not compatible with the PD.** The provision allows a private JSC to offer its shares through a private placement to less than 150 non-qualified investors and to its existing shareholders until January 1, 2018. Art. 3 of the PD exempts offers to less than 150 natural or legal persons, other than qualified investors. This amount also includes existing shareholders. However, given the current market structure and the NSSMC's strategic objective to reduce the number of public JSCs, the mission agrees that the proposed short transitional period is appropriate to enable public JSCs to transform to private JSCs.

21. **The NSSMC should follow the EU legislative developments.** The European Commission has published a proposal for a new Level 1 Prospectus Regulation that would replace the PD. While the key principles of the proposed regulation are in line with the PD, a number of changes to the existing regime have been proposed. Discussions on the proposal are currently ongoing both in the European Parliament and in the Council. As the final content of the regulation cannot be anticipated at this stage, the NSSMC should follow the EU regulatory developments and adjust the Ukrainian framework, as appropriate.

B. Issuer Periodic Disclosure Requirements

Findings

22. **The requirements on the content of the periodic financial reports do not comply with IOSCO Principle 16 or the TD.** IOSCO Principle 16 requires full, accurate and timely disclosure of financial results, risk and other information which is material to investors' decisions. Art. 4 of the TD requires an annual financial report to contain a management report⁷ that includes, inter alia, a fair review of the development and performance of the company's business and financial position as well as a description of its principal risks and the uncertainties that it faces. Art. 5 of the TD requires a half-yearly report to contain an interim management report that includes at least an indication of

⁷ The management report has to be drawn up in accordance with Art. 19 or 29 of the EU Accounting Directive (2013/34/EU) that has replaced the fourth and seventh EU Company Law Directives (78/660/EEC and 83/349/EEC) referred to in Art. 4(5) of the TD.

important events that have occurred during the first six months of the financial year, and their impact on the condensed set of financial statements, together with a description of the principal risks and uncertainties for the remaining 6 months of the financial year. For issuers of shares, the interim management report must also include major related party transactions.

23. The requirements for annual and quarterly reports set out in the Law on Securities and Stock Market fall short of the above requirements. Information required to be disclosed in the annual report covers, inter alia, annual financial statements and audit report, basic information on the issuer and its management, information on the issuer's securities and business activities, as well as information on the approval of significant transactions and related party transactions. Information to be disclosed in the quarterly reports is to a large extent similar to that required to be included in the annual reports.

24. The applicable accounting standards depend on the legal form of the company, which is not compliant with the TD. Public JSCs are required to draw up their financial statements in accordance with the International Financial Reporting Standards (IFRS). With the exception of financial institutions, private JSCs and limited liability companies are allowed to prepare their financial statements following the Ukrainian Generally Accepted Accounting Principles (GAAP) even if they have made a public placement of non-equity securities and those securities are admitted to trading on a stock exchange. EU legislation⁸ requires the use of IFRS in the consolidated accounts of an issuer. The member states have discretion to extend the requirement for IFRS accounts also to issuers that are not required to prepare consolidated accounts or to the annual accounts of the parent company.

25. In most cases, interim reports are required to be prepared on a quarterly basis. Pursuant to NSSMC regulation No 2826, the following issuers are subject to a quarterly reporting requirement: (i) companies where the state ownership is at least 25 percent; (ii) issuers that have made a public placement of securities; and (iii) issuers whose securities are listed. IOSCO Principle 16 requires disclosure of interim financial information at least on a semi-annual basis. Art. 5 of the TD requires publication of half-yearly financial information. Art. 3 of the TD allows member states to require publication of quarterly financial information, subject to certain preconditions.⁹

26. Disclosure deadlines are compliant with the TD. An annual report has to be published by April 30 of the year following the reporting year (which is always a calendar year), i.e., 4 months after the end of the financial year. Pursuant to NSSMC regulation No. 2826, quarterly reports have to be published not later than the twenty-fifth of the month following the reporting quarter. IOSCO Principle 16 requires timely disclosure without specifying the reporting deadlines. Art. 4 of the TD

⁸ Art. 4(3) and 5(3) of the TD and the EU IAS Regulation ((EC) No 1606/2002).

⁹ The additional periodic financial information required (i) must not constitute a disproportionate financial burden in the member state concerned, in particular for small and medium-sized issuers; and (ii) its content must be proportionate to the factors that contribute to the investors' investment decisions in the member state concerned. These preconditions are not applicable to issuers that are financial institutions. Moreover, before imposing the issuers a requirement to publish additional periodic financial information, member states are required to assess both whether such additional requirements may lead to an excessive focus on the issuers' short-term results and performance and whether they may impact negatively on the ability of small and medium-sized issuers to have access to the regulated markets.

sets a four month deadline for the publication of an annual financial report. Art. 5 of the TD requires that a half-yearly financial report is published as soon as possible after the relevant period, but at the latest 3 months thereafter.

27. **The quality of audits varies significantly.** High quality and independent audit is a key element in safeguarding the reliability of financial information. One common theme arising from meetings with the Ukrainian authorities and market participants was the concern over quality of audits and lack of independent and effective audit oversight in Ukraine. IOSCO Principles 19–21 require adequate level of audit oversight, independence of auditors from the issuers subject to their audit, and audit standards of a high and internationally acceptable quality.

NSSMC draft legislative proposals

28. **The NSSMC has drafted legislative proposals to address the above findings and to start to converge the Ukrainian legislation towards the IOSCO Principles and the TD.** The key draft amendments relate to:

- Introducing detailed content requirements for management reports (with the objective of complying with Art. 4(5) of the TD and related EU Accounting Directive).
- Introducing detailed content requirements for interim management reports (with the objective of complying with Art. 5(4) of the TD).
- Introducing a requirement to include in the annual and interim financial reports a responsibility statement by persons responsible for preparing the report (with the objective of complying with Art. 4(2)(c) and 5(2)(c) of the TD).
- Introducing disclosure requirements on payments made to governments by issuers active in the extractive or logging industries (with the objective of complying with Art. 6 of the TD).

29. **The NSSMC is planning to apply the new provisions to a broader group of issuers than required under the TD.** The plan is to apply the requirements to all issuers that have securities admitted to trading on an RM and to issuers that have made a public offer of securities after the entry into force of the PD law. The NSSMC also plans to create a transitional regime for issuers that were public JSCs on May 1, 2016 but do not meet the enhanced listing criteria. The transitional regime would basically maintain the existing disclosure requirements for those companies (see Table 1).

Recommendations

30. **The suggested legislative changes appropriately address the key requirements of the IOSCO Principles and the TD.** The mission reviewed the draft legislation provided by the NSSMC and considers that the proposed amendments to the Law on Securities and Stock Market, Law on Joint Stock Companies, Law on State Regulation of Securities Market, and Law on Audit Activity address the key deficiencies in a satisfactory manner.

31. **However, further amendments to the draft legislation and to the existing NSSMC regulations are required to address the details of the IOSCO Principles and the TD.** The mission

suggests that the NSSMC addresses the following issues through amendments to the proposed legislation and/or existing NSSMC regulations.

- The NSSMC should ensure that all issuers that have securities admitted to trading on an RM or that have made a public offer of securities are covered by the requirement to draw up at least their consolidated annual and interim financial statements in accordance with the IFRS. Currently the requirement only applies to the annual and interim financial statements of public JSCs.
- The NSSMC should ensure that the proposed legislation adequately addresses the liability issues relating to the disclosure of periodic reports (to comply with Art. 7 of the TD).
- The NSSMC should amend its regulations to comply with Articles 3, 4, and 12 of the TD implementing Directive (2007/14/EC).¹⁰

32. **The mission considers that the quarterly financial reporting requirement should be maintained at this stage despite the TD presumption for half-yearly reporting.** This is important due to the current deficiencies in the ad hoc reporting requirements (see below), and the need to ensure sufficient level of transparency and to facilitate the strengthening of confidence towards the functioning of financial markets. However, once the proposed periodic and ad hoc reporting requirements have been in operation for some time, it is recommended that the NSSMC reviews the operation of the regime and considers whether moving to apply the TD presumption of half-yearly reporting frequency would be appropriate at least for certain categories of issuers, such as issuers of non-equity securities.

33. **The proposed scope of application of the new legislation is in line with the IOSCO Principles and the EU legislation.** However, a situation where a significant number of issuers were subject to trading only on an MTF without their own application would be unusual. Adjustments to the framework may also be needed to ensure compliance with the MiFID requirements for admission to trading on an MTF.

34. **The mission also urges the NSSMC to continue its efforts to promote the establishment of an effective and independent audit oversight body.**

C. Issuer Ad Hoc Disclosure Requirements

Findings

35. **There are significant deficiencies in the current ad hoc disclosure requirements, which make them non-compliant with the IOSCO Principles and the MAR.** IOSCO Principle 16 requires full, accurate and timely disclosure of information which is material to investors' decisions.

¹⁰ Art. 3 stipulates the minimum content for non-consolidated interim financial statements for issuers using national GAAP. Art. 4 defines the minimum information on related party transactions for interim management reports. Art. 12 sets the minimum standards for dissemination of regulated information.

Art. 17 of the MAR requires the issuer to disclose inside information¹¹ as soon as possible in a manner which enables fast access and complete, correct and timely assessment of the information by the public. The issuer is allowed to delay disclosure of inside information at its own responsibility provided the following conditions are met: (i) immediate disclosure is likely to prejudice the legitimate interests of the issuer; (ii) delay of disclosure is not likely to mislead the public; and (iii) the issuer is able to ensure the confidentiality of the information.

36. **The Law on Securities and Stock Market does not contain any general requirement for the issuer to disclose information which is material to investors' decisions.** Instead, the law imposes an ad hoc disclosure requirement on certain events or decisions relating to the issuer or its securities. The list of events and decisions prescribed by the law is exhaustive and there are no exemptions from the disclosure requirement. The requirements for the content of the ad hoc disclosures are set by a NSSMC regulation. The information required by the regulation does not enable complete, correct and timely assessment of the information by investors. The ad hoc disclosure requirement covers all types of issuers, including issuers who have only made a private placement of securities and have no securities admitted to trading.

NSSMC draft legislative proposals

37. **The NSSMC has drafted legislative proposals to address the above findings and to start to converge the Ukrainian legislation towards the IOSCO Principles and the MAR.** The key draft amendments relate to introducing a requirement to disclose inside information as soon as possible and a possibility to delay disclosure of inside information under certain conditions and on the issuer's own liability (with the objective of complying with Art. 17 of the MAR).

38. **As for the periodic disclosure requirements, the NSSMC is planning to apply the new provisions to a broader group of issuers than required under the TD.** The scope of application of the new framework is planned to be the same as that described above in paragraph 29.

Recommendations

39. **The suggested legislative changes appropriately address the requirements of the IOSCO Principles and the key MAR requirements for disclosure of inside information.** The mission reviewed the draft legislation provided by the NSSMC and considers that the proposed amendments to the Law on Securities and Stock Market and the Law on State Regulation of Securities Market address the key deficiencies in a satisfactory manner.

40. **However, further amendments to the draft legislation and to the existing NSSMC regulations are required to address the details of the MAR.** The mission suggests that the NSSMC

¹¹ MAR definition of inside information is in Art. 7(1)(a). Inside information in relation to issuers and financial instruments has been defined as information of a precise nature, which has not been made public, relating, directly or indirectly, to one or more issuers or to one or more financial instruments, and which, if it were made public, would be likely to have a significant effect on the prices of those financial instruments or on the price of related derivative financial instruments.

addresses the following issues through amendments to the proposed legislation and/or existing NSSMC regulations.

- The NSSMC should ensure that the scope of the provision covers issuers covered by the MAR and emission allowance market participants (if applicable) and is also otherwise in line with the MAR.
- The NSSMC should aim to reduce overlaps of the provisions relating to disclosure of inside information and ad hoc information.
- The NSSMC should amend its regulations to comply with the relevant MAR implementing technical standards.

D. Dissemination of Regulated Information

Findings

41. **The current method for disclosure of periodic reports and ad hoc information does not comply with the TD or MAR.** Art. 21 of the TD requires that regulated information is published in a manner ensuring fast access to such information on a non-discriminatory basis. The dissemination media to be used should be such that they can be reasonably relied upon for the effective dissemination of regulated information throughout the EU. Art. 17(1) of the MAR requires inside information to be published in a manner ensuring fast access and complete, correct, and timely assessment of the information by the public.

42. **The current framework does not include a dissemination (“push”) requirement.** Annual, quarterly and ad hoc reports are published on the website of the issuer, filed with the NSSMC and its public database, and published in an official newspaper. Pursuant to NSSMC regulation No. 2826, ad hoc information has to be filed in the NSSMC’s public database within one working day after the date of the action, published on the website of the issuer and in an official newspaper within five working days, and submitted to the NSSMC within seven working days. While electronic publication on the website of the issuers and in the NSSMC public database allow for fast access to the information, both employ a “pull” method for receiving information. This means that an investor or news media wishing to access the information has to visit the website of the issuer or the NSSMC database to retrieve the information. The TD and MAR require that information is also actively disseminated employing “push” methods, i.e., methods capable of disseminating information to as wide a public as possible and as close to simultaneously as possible throughout the EU. In practice, this is achieved by feeding information to various newsfeeds that investors and news media have subscribed to.

NSSMC draft legislative proposals

43. **The NSSMC has drafted legislative proposals to address the above findings and to start to converge the Ukrainian legislation towards the IOSCO Principles and the TD and MAR.** The NSSMC proposes to delete from the Law on Securities and Stock Market the requirement to publish periodic and ad hoc information in an official newspaper. However, otherwise the mission’s review of the draft legislation provided by the NSSMC concluded that the draft legislation does not yet

include sufficient requirements for the dissemination methods to comply with the TD and MAR requirements.

Recommendations

44. **Further amendments to the draft legislation and to the existing NSSMC regulations are required to address the details of the TD and MAR.** The mission suggests that the NSSMC introduces the requirement to use “push” methods for dissemination of regulated information to ensure fast access to the information and to fully comply with Art. 21 of the TD, Art. 12 of the TD implementing Directive, and Art. 7(1) of the MAR. This may also imply the need to align the scope of regulated information with the scope of the TD definition.

E. Major Shareholding Notifications

Findings

45. **There are currently no disclosure requirements for shareholders acquiring or disposing a significant proportion of voting rights or financial instruments, which is not in compliance with the IOSCO Principles or the TD.** IOSCO Principle 16 requires full, accurate and timely disclosure of information which is material to investors’ decisions. This includes information about those who have a significant interest in the issuer or who seek control of an issuer. Art. 9 and 10 of the TD require shareholders and other natural and legal persons to notify their holdings when they acquire or dispose voting rights where the proportion of holdings reaches, exceeds or falls below the thresholds of 5, 10, 15, 20, 25, 30, 50, or 75 percent. Art. 13 of the TD extends the notification requirement to financial instruments entitling to acquire shares already issued and to any other financial instruments with a similar economic effect. The notification must be made to the issuer and the competent authority. The member states have discretion as to whether the notification is made public by the issuer or the competent authority.

46. **Certain very limited information on shareholders is currently available through other means.** The Law on Securities and Stock Market allows an issuer to request information on its shareholders from the central securities depository. However, the information is provided on a legal entity basis and not aggregated to cover all holdings within the shareholder’s sphere of control (indirect holdings). The information received through the central securities depository does not cover information on shareholders’ voting agreements either.

NSSMC draft legislative proposals

47. **The NSSMC has drafted legislative proposals to address the above findings and to start to converge the Ukrainian legislation towards the IOSCO Principles and the TD.** The key draft amendments relate to:

- Introducing a requirement for shareholders and other natural and legal persons to notify their holdings reaching or crossing a notification threshold (with the objective of complying with Art. 9 and 10 of the TD).

- Introducing exemptions from the notification obligation (with the objective of complying with Art. 9 and 12 of the TD).

48. **As for the periodic and ad hoc disclosure requirements, the NSSMC is planning to apply the new provisions to a broader group of issuers than required under the TD.** The scope of application of the new framework would be the same as that described above in paragraph 29.

Recommendations

49. **The suggested legislative changes appropriately address the requirements of the IOSCO Principles and the key provisions of the TD.** The mission reviewed the draft legislation provided by the NSSMC and considers that the proposed amendments to the Law on Securities and Stock Market, Law on Joint Stock Companies, and Law on State Regulation of Securities Market address the key deficiencies in a satisfactory manner.

50. **However, further amendments to the draft legislation and the existing NSSMC regulations are required to address the details of the TD.** The mission suggests that the NSSMC addresses the following issues through amendments to the proposed legislation and the existing NSSMC regulations:

- The NSSMC should amend the draft legislation to exempt the NBU from the notification obligation when the latter carries out its functions as a monetary authority (with the objective of complying with Art. 11 of the TD).
- The NSSMC should ensure that the disaggregation rules for the parent companies of fund management companies and investment firms providing individual portfolio management are in compliance with Art. 12(4) and (5) of the TD as well as Art. 10 of the TD implementing Directive.
- The NSSMC should amend its regulations to comply with Art. 5-11 of the TD implementing Directive¹² and the technical standards on major holdings (Regulation (EU) 2015/761).¹³

¹² Art. 5, 6 and 10 define additional criteria for application of certain exemptions from the TD major shareholding notification requirement. Art. 7 stipulates the obligation for competent authorities to publish a calendar of trading days. Art. 8 clarifies the persons subject to the obligation to notify holding of voting rights. Art. 9 defines when a shareholder is deemed to have learned about acquisition, disposal or possibility to exercise voting rights. Art. 11 defines minimum information to be required in a notification of financial instruments under TD Art. 13.

¹³ The technical standards relate to aggregation of holdings, treatment of financial instruments referenced to a basket or an index, and the determination of 'delta-adjustment' for financial instruments providing exclusively for a cash settlement.

IV. MARKET ABUSE

A. Prohibition of Market Abuse

Findings

51. **The scope of the current market abuse prohibition does not comply with the key provisions of the MAR.** While the Law on Securities and Stock Market and the Law on State Regulation of Securities Market prohibit market manipulation and unlawful use of inside information, the scope of the prohibitions does not comply with the MAR requirements. Deficiencies relate both to the requirements applicable to insider dealing and disclosure of inside information and market manipulation.

52. **While the current legislation includes a definition of inside information and prohibits the use of inside information, some key provisions are missing.** Art. 14 of the MAR prohibits a person from (i) engaging or attempting to engage in insider dealing; (ii) recommending that another person engages in insider dealing or inducing another person to engage in insider dealing; and (c) unlawfully disclosing inside information. Similar prohibition is included in Art. 45 of the Law on Securities and Stock Market, but the prohibition does not cover attempts to engage in insider dealing or use of inside information to cancel or amend an order.

53. **The current legislation does not provide any exemptions from the insider dealing prohibition.** MAR provides such exemptions for trading in the issuer's own shares in buy-back programs and trading related to stabilization (Art. 5 MAR), market soundings (Art. 11 MAR)¹⁴ and legitimate behavior (Art. 9 MAR).¹⁵

54. **There is currently no obligation for issuers to draw up a list of all persons who have access to inside information (insider lists).** Insider lists are an important tool when regulators investigate possible misuse of inside information, as such lists help identify the persons who had access to inside information and the date on which they gained access.

55. **The current prohibition of market manipulation has some shortcomings compared to the MAR requirements.** Art. 15 of the MAR prohibits a person from engaging in or attempting to engage in market manipulation. Art. 12 of the MAR describes which activities are considered to be market manipulation. The main deficiencies related to the prohibition of market manipulation included in Art. 10-1 of the Law on State Regulation of Securities Market are:

- The prohibition of market manipulation only applies to financial instruments.

¹⁴ Market soundings are interactions between the seller of financial instruments and one or more potential investors, prior to the announcement of a transaction, to gauge the interest of potential investors in a possible transaction and its pricing, size and structuring.

¹⁵ Legitimate behavior may include, for example, recognizing the role of market makers when they act in the legitimate capacity of providing market liquidity.

- The current legislation does not include a prohibition against attempting to engage in market manipulation.
- The prohibition relating to market manipulation through the dissemination of information only refers to dissemination of “false” information.¹⁶
- While the current law includes an exemption for certain actions,¹⁷ it does not provide an exemption for buy-back programs.

NSSMC draft legislative proposals

56. The NSSMC has drafted legislative proposals to address the above findings and to start to converge the Ukrainian legislation towards the MAR. Regarding the use of inside information and unlawful disclosure of inside information the key draft amendments relate to:

- Including the use of inside information by cancelling or modifying an order in the definition of insider transactions (with the objective of complying with Art. 8(1) of the MAR).
- Defining the term “information that would have a significant effect on the price” as information that an investor would most likely use as a basis for making his/her investment decisions (with the objective of complying with Art. 7(4) of the MAR).
- Requiring issuers and other entities acting in the interest or on behalf of issuers to compile insider lists (with the objective of complying with Art. 18 of the MAR).
- Including an exemption for “market sounding” (with the objective of complying with Art. 11 of the MAR).
- Introducing a detailed framework for share buy-back programs and stabilization of financial instruments (with the objective of complying with Art. 5 of the MAR; this exemption would also apply for the prohibition of market manipulation).

57. With regard to the prohibition of market manipulation the key draft amendments relate to:

- Expanding the scope of the prohibition of market manipulation (with the objective of complying with Art. 2 of the MAR).¹⁸
- Prohibiting an attempt to manipulate the market (with the objective of complying with Art. 15 of the MAR).

¹⁶ This means that the NSSMC as well as the law enforcement agencies have to prove that the published information clearly has not been truthful. However, manipulation may not only consist of the invention of manifestly false information, but also the willful omission of material facts, as well as the knowingly inaccurate reporting of information. This may be the case if the published information—taken alone—is not “false” but nevertheless leads to a false idea to the investors, for example because the disseminated information is incomplete.

¹⁷ The current exemptions cover those with the aim of supporting the price, demand or offer for financial instruments on the basis of a contract between a stock exchange and an exchange trading participant and those performed by government authorities in relation to the implementation of monetary policy or government debt management policy.

¹⁸ According to the draft legislative proposal the prohibition of market manipulation in Art. 44(2)(1) of the Law on Securities and Stock Market not only applies to financial instruments admitted to trading on an RM (item 1) or for which an application for trading on an RM has been submitted (item 2), but also to financial instruments, the price or value of which depends on or has an effect on the price or value of a financial instrument referred to in items 1) or 2) (item 3). The prohibition also applies to products that are the base asset of the financial instruments envisaged in items 1–3 and financial instruments that affect or could affect the price or volume of trade in products that are a base asset of the financial instruments envisaged in items 1–3. Benchmarks are also explicitly covered.

- Prohibiting not only the dissemination of false but also of misleading information (with the objective of complying with Art. 12(1)(c) of the MAR).

Recommendations

58. **The suggested legislative changes appropriately address the key requirements of the MAR relating to the prohibition of market abuse and the requirement to maintain insider lists.** The mission reviewed the draft legislation provided by the NSSMC and considers that the proposed amendments to the Law on Securities and Stock Market address the key deficiencies in a satisfactory manner.

59. **However, further amendments to the draft legislation and issuance of new NSSMC regulations are required to address the details of the MAR.** The mission suggests that the NSSMC addresses the following issues through amendments to the proposed legislation and/or new NSSMC regulations.

- The NSSMC should add to the scope of the market abuse prohibition financial instruments traded on MTFs to comply with Art. 2(1) of the MAR, since MTFs are currently planned to be included in the scope of the Law on Regulated Markets and Derivatives.
- The NSSMC should define the preconditions and limits of legitimate behavior to comply with Art. 9 of the MAR.
- The NSSMC should determine and publish accepted market practices that are not market manipulation to comply with Art. 13 of the MAR, taking into account the Commission Regulation (EU) 2016/908.
- The NSSMC should define a list of non-exhaustive indicators of manipulative behavior to comply with Annex I of the MAR,¹⁹ taking into account the Commission Regulation (EU) 2016/522.
- The NSSMC should specify the requirements that buy-back programs and stabilization measures must meet to comply with Art. 5 of the MAR, including conditions for trading, restrictions regarding date and volume, disclosure and reporting obligations, and price conditions, taking into the account the Commission Regulation (EU) 2016/1052.
- The NSSMC should determine appropriate arrangements, procedures and record keeping requirements for persons to comply with the requirements of stock market sounding to comply with Art. 11 of the MAR, taking into the account the Commission Regulation (EU) 2016/959 and Commission Regulation (EU) 2016/960.

60. **Some elements can be addressed only once Ukraine will have to reach full compliance with EU legislation according to the Association Agreement.** This includes provisions relating to instruments that do not yet exist in Ukraine (e.g., emission allowances and spot commodity contracts that are not wholesale energy products).

¹⁹ Such indicators should relate to the employment of a fictitious device or any other form of deception or contrivance, and indicators related to false or misleading signals and to price securing.

B. Prevention and Detection of Market Abuse

Findings

61. **The current legislation does not provide effective mechanisms to detect market abuse and therefore neither complies with IOSCO Principle 36 nor with the relevant MAR provisions.** IOSCO Principle 36 requires regulation to be designed to detect and deter manipulation and other unfair trading practices. MAR includes various disclosure and reporting requirements in Art. 16, 19, and 32. Professional stock market participants do not currently need to notify the NSSMC of orders or transactions that could constitute insider dealing and/or market manipulation. The law does not include any provisions aimed to enable market participants, investors or other persons to report actual or potential infringements to the NSSMC. These deficiencies significantly reduce the NSSMC's ability to become aware of potential market abuse and to take appropriate measures. Finally, the current law does not include any obligations for issuers' managers or their associated persons to notify the issuer and the competent authority of their transactions in the issuer's financial instruments or related derivatives (managers' transactions).

NSSMC draft legislative proposals

62. **The NSSMC has drafted legislative proposals to address the above findings and to start to converge the Ukrainian legislation towards the IOSCO Principles and the MAR.** The key draft amendments relate to:

- Requiring stock exchanges to introduce and support the functioning of effective mechanisms, systems and procedures directed at deterring and detecting market abuse and attempted market abuse and requiring professional stock market participants to introduce and support the functioning of effective mechanisms and procedures aimed at detecting suspicious orders or transactions (with the objective of complying with Art. 16 of the MAR).
- Requiring the NSSMC to provide functioning secure communication channels that can be used for reporting of actual and potential violations of the relevant laws (with the objective of complying with Art. 32 of the MAR).
- Introducing a reporting requirement for managers' and their closely related persons' transactions (with the objective of complying with Art. 19 of the MAR).

Recommendations

63. **The suggested legislative changes appropriately address the requirements of the IOSCO Principles and the key provisions of the MAR.** The mission reviewed the draft legislation provided by the NSSMC and considers that the proposed amendments to the Law on Securities and Stock Market and the Law on State Regulation of Securities Market address the key deficiencies in a satisfactory manner.

64. **However, the NSSMC needs to prepare additional regulations to complement the requirements set at the level of law.** This applies especially in relation to regulations to:

- Determine appropriate arrangements, systems, procedures and notification templates to be used by stock exchanges and professional stock market participants to comply with the requirements to report suspicious orders and transactions. It is recommended that the NSSMC takes into the account the Commission Regulation (EU) 2016/957 when preparing this regulation.
- Specify the procedures and arrangements for reporting and following up reports by whistleblowers and the related measures for the protection of persons working under a contract of employment and measures for the protection of personal data.
- Establish the procedure for the notification of managers' transactions, drawing up the list of managers and persons closely associated with them and establishing the circumstances under which the issuer may allow the managers and their closely associated persons to perform transactions during a closed period.

V. POWERS AND SANCTIONS

A. NSSMC Supervisory and Investigative Powers

Findings

65. **The current powers of the NSSMC are not sufficient to comply with the IOSCO Principles and EU legislation.** IOSCO Principle 3 requires that the regulator has adequate powers and the capacity to perform its functions and exercise its powers, and Principle 11 specifies the investigative powers that the regulator should have. Art. 21 of the PD, Art. 24 of the TD and Art. 23 of the MAR stipulate the powers the competent authority should have. These include broad powers to request information, documents and data from any person, including issuers, auditors, shareholders, and persons controlling them or being controlled by them, carry out on-site inspections, require disclosure of information, prohibit or suspend a public offer or trading on an RM, examine that periodic information is drawn up in accordance with the relevant accounting rules, and make public that a legal or natural person (including issuer) is failing to comply with its obligations.

66. **The adoption of the draft Independence Law is intended to address some of the deficiencies in the NSSMC's powers.** The Law on State Regulation of Securities Market currently provides the NSSMC only with the power to conduct inspections and reviews of professional stock market participants as well as of issuers' corporate governance and conduct in the placement and trading of securities. The NSSMC lacks under the current law the power to conduct administrative/civil investigations of issuers, offerors, auditors and other unlicensed entities and persons. Moreover, the NSSMC lacks the power to request information and documents from offerors, auditors and other unlicensed entities and persons. These gaps are proposed to be closed in the draft Independence Law. The NSSMC also lacks supervisory powers towards persons subject to the major shareholding notification obligation.

NSSMC draft legislative proposals

67. **The pending and new draft legislative changes appropriately address the key requirements of the IOSCO Principles and of the PD, TD and MAR relating to the powers of the NSSMC.** The mission reviewed the draft legislation provided by the NSSMC and considers that the proposed amendments to the Law on State Regulation of Securities Market included in the draft Independence Law and the other laws reviewed by the mission make the NSSMC's powers compliant with the IOSCO MMOU requirements and Art. 21 of the PD, Art. 24 of the TD and Art. 23 of the MAR. One of the most significant changes relates to the ability of the NSSMC to conduct investigations, which would be administrative/civil in nature rather than criminal that would remain the prerogative of the law enforcement agencies.

B. Administrative Sanctions and Measures

Findings

68. **The current enforcement measures available to the NSSMC are not sufficient to comply with the IOSCO Principles and EU legislation.** IOSCO Principle 11 requires that the regulator has comprehensive enforcement powers. Art. 25 of the PD, Art. 28 of the TD and Art. 30-31 of the MAR require that appropriate administrative measures can be taken or administrative sanctions can be imposed against the persons responsible, where the legislation has not been complied with.

69. **Both the TD and MAR determine the level of fines that competent authorities have to be able to levy for the breach of certain requirements.** In such cases, both the TD and MAR set a minimum level for the maximum fines that differs depending on the type of infringement and whether the breach was conducted by a legal or natural person.²⁰

70. **Competent authorities must also be able to take certain other administrative measures.** The TD requires that for the breach of the requirement for major shareholding notifications, the competent authority must be able to suspend the exercise of voting rights attached to the shares. Art. 30 of the MAR requires the competent authority to have the power to impose administrative measures which include:

- An order requiring the person responsible for the infringement to cease the conduct and to desist from a repetition of that conduct.

²⁰ For legal entities, the maximum level of fines has to amount to:

- TD: at least EUR 10 million or 5 percent of the total (consolidated) annual turnover of a legal entity or twice the amount of the profits gained or losses avoided because of the breach, whichever is higher.
- MAR: at least EUR 15 million or 15 percent of the total (consolidated) annual turnover (for breach of the prohibition of insider dealing, unlawful disclosure of inside information or market manipulation)/at least EUR 2.5 million or 2 percent of the total (consolidated) annual turnover (for breach of the requirement to disclose inside information) or three times the amount of the profits gained or losses avoided because of the infringement, whichever is highest.

For natural persons, the maximum level of fines has to amount to:

- TD: at least EUR 2 million or twice the amount of the profits gained or losses avoided because of the breach, whichever is higher.
- MAR: at least EUR 5 million (for breach of the prohibition of insider dealing, unlawful disclosure of inside information or market manipulation)/at least EUR 1 million (for breach of the requirement to disclose inside information) or three times the amount of the profits gained or losses avoided because of the infringement, whichever is highest.

- The disgorgement of the profits gained or losses avoided due to the infringement insofar as they can be determined.
- A public warning which indicates the person responsible for the infringement and the nature of the infringement.
- Withdrawal or suspension of the authorization of an investment firm.
- In the event of repeated infringements of the prohibition of insider dealing, unlawful disclosure of inside information or market manipulation, a permanent ban of any person from discharging managerial responsibilities within an investment firm or any other natural person who is held responsible for the infringement from exercising management functions in investment firms.

71. **The enforcement powers of the Ukrainian authorities are currently limited, so defining the precise division of responsibilities between the various supervisory authorities has not yet been a priority.** While there are cooperation arrangements between the authorities, so far they have not specifically addressed the use of enforcement powers. Under the EU legislation member states have to designate a single administrative competent authority to exercise the relevant powers and take the relevant administrative sanctions and measures. One competent authority does not however need to undertake all the duties. For example MAR enables the designated competent authority to exercise these powers (i) directly; (ii) in collaboration with other authorities or with the market undertakings; (iii) under its responsibility by delegation to such authorities or market undertakings; or (iv) by application to the competent judicial authorities.

72. **The existing administrative sanctions are not effective, proportionate and dissuasive.** Pursuant to the Law on State Regulation of Securities Market, failure to disclose information, publication of incomplete or misleading information or failure to fulfill the conditions of a prospectus can lead to a fine of up to 1000 minimum tax-free incomes of citizens.²¹ A repeated violation within a year can lead to a fine from 1000 up to 5000 minimum tax-free incomes of citizens. A violation of the prohibition of market manipulation can lead to a fine from 100 up to 500 minimum tax-free incomes of citizens (500 up to 750 minimum tax-free incomes of citizens for violations committed by a group of persons or repeated violations within a year), while a violation of the prohibition of illegal use of inside information can lead to a fine from 500 up to 750 minimum tax-free incomes of citizens.

NSSMC draft legislative proposals

73. **The NSSMC has drafted legislative proposals to address the above findings and to start to converge the Ukrainian legislation towards the IOSCO Principles and the EU legislation.** The key draft amendments relate to:

- Enhancing the sanctioning powers of the NSSMC (with the objective of complying with Art. 25 of the PD, Art. 28-29 of the TD and Art. 30-31 of the MAR). However, with regard to the maximum amount of financial sanctions provided in Art. 11 and 13 of the Law on State Regulation of Securities Market the NSSMC draft proposal includes a transitional provision

²¹ The minimum tax-free income is currently UAH 17.

according to which the maximum fines would be introduced gradually so that they would be 25 percent of the final amount in 2017, 50 percent in 2018 and 75 percent in 2019.

- Assigning the responsibility for imposing all financial sanctions to the NSSMC, whereas the responsibility for taking certain enforcement measures against banks would fall under the responsibility of the NBU, to which the NSSMC would submit documents and information to support the NBU's decision-making.

74. **The NSSMC is also planning to introduce legislative provisions that are neither required by IOSCO Principles nor by MAR.** These proposals relate especially to the introduction of a provision to the Law on State Regulation of Securities Market that would allow the NSSMC to enter into an agreement to settle the consequences of violations of laws concerning the securities market and JSCs.

Recommendations

75. **The suggested legislative changes address the requirements of the IOSCO Principles, PD, TD and MAR on the availability of administrative sanctions and other administrative measures, as well as the TD and MAR requirements for the maximum level of fines.** The suggested gradual implementation of the maximum level of administrative fines would apply until such time as Ukraine will have to reach full compliance with the EU legislation according to the Association Agreement. The mission supports this approach, given that the increase in the maximum fines required by the implementation of the TD and MAR will be significant. However, while the amount of maximum fines is correctly determined in the draft legislation,²² the annual turnover based fines for legal entities should be calculated on a consolidated basis as required by the TD and MAR.

76. **The suggested legislative changes do not include sufficient information on the required collaboration between the NSSMC and the NBU in case banks or their managers or employees will be subject to enforcement actions.** The mission urges the NSSMC to initiate detailed discussions with the NBU on this to ensure that the legislative approach to be taken incorporates the objectives of both authorities in a balanced manner. Guidance on how to design an appropriate model may be sought by referring to the cooperation arrangements made in EU member states that have multiple financial supervisory authorities.

77. **Use of the new powers and sanctions will require changes to the NSSMC's administrative procedures.** It is recommended that the NSSMC pays particular attention to adopting sound administrative procedures to support the efficient, effective and transparent use of its new powers.

²² Based on the current exchange rate.

C. Criminal Sanctions and Proceedings

Findings

78. **The scope of the current criminal sanctions is too narrow and the possible amount of sanctions is not deterrent.** The relevant provisions of the Criminal Code do not comply with the key provisions of the CSMAD. CSMAD requires member states to introduce criminal sanctions at least for serious cases of insider dealing, market manipulation and unlawful disclosure of inside information, when the offenses have been committed with intent. Insider dealing and unlawful disclosure of inside information should be deemed to be serious cases, for example if their impact on the integrity of the market, the actual or potential profit derived or loss avoided, the level of damage caused to the market, or the overall value of the financial instruments traded is high. Other circumstances that may be taken into account are, for instance, whether an offence has been committed within the framework of a criminal organization or whether the person has committed such an offence before. Examples of serious cases of market manipulation include those where the level of alteration of the value of the financial instrument or spot commodity contract or the amount of funds originally used is high or where the manipulation is committed by a person employed or working in the financial sector or in a supervisory or regulatory authority.

79. **With regard to market manipulation the main deficiencies of the current legislation are:**

- The current legislation only provides the possibility to impose fines. Even for serious cases no imprisonment is possible. The maximum amount of fines is limited to 500 minimum tax-free incomes of citizens.
- The scope of application is very limited as the provision only applies to “official stock market participants”. This offers the opportunity for other stock market participants to avoid the danger of criminal prosecution by the use of stooges.

80. **In the case of the prohibition of insider dealing and unlawful disclosure of inside information, the deficiencies relate especially to the following:**

- As for market manipulation, it is only possible to impose fines (500 to 750 minimum tax-free incomes of citizens), not to penalize infringements by imprisonment.
- The scope of application is very limited, as it only applies to certain groups of individuals such as issuer’s officials or persons who have access to inside information due to the performance of their official duties.

NSSMC draft legislative proposals

81. **The NSSMC has drafted legislative proposals to address the above findings and to start to converge the Ukrainian legislation towards CSMAD.** The key draft amendments relate to the introduction of criminal sanctions for specific violations of the prohibition of market abuse (with the

objective of complying with Art. 3-7 of the CSMAD).²³ The maximum terms of imprisonment are in line with those required under CSMAD.

82. **In addition, the NSSMC is planning to propose including additional provisions that are neither required by IOSCO Principles nor by CSMAD.** These proposals relate especially to:

- Extending the penalties applicable under Art. 384 (knowingly false testimony) and Art. 385 of the Criminal Code (refusal to testify) to cases where a person knowingly provides false information under an investigation or inspection conducted by the NSSMC or refuses to provide information to the NSSMC during an inspection or investigation.
- Introducing a provision to Art. 71 of the Criminal Procedure Code that obliges an investigator and prosecutor to engage a representative of the NSSMC as a specialist during criminal market abuse investigations.
- Introducing a provision to Art. 236 of the Criminal Procedure Code that obliges an investigator and prosecutor to request the appointment of a representative of the NSSMC to take part in every search as far as criminal market abuse proceedings are concerned.
- Introducing a provision to Art. 376 of the Criminal Procedure Code according to which a copy of a court decision in a criminal market abuse proceeding must be provided to the NSSMC no later than the next day after the adoption of the decision.
- Introducing a provision to Art. 10 of the Law on State Regulation of Securities Market according to which the NSSMC and law enforcement agencies must exchange with each other information (including information with restricted access) related to criminal investigations as far as criminal market abuse proceedings are concerned.

Recommendations

83. **The suggested legislative changes to the Criminal Code appropriately address the requirements of the CSMAD for the types of criminal sanctions, but further consideration should be given to the definition of a serious case and possible transitional provisions for introducing the planned full fines.** As the proposed criminal sanctions are in all cases linked to a certain “financial impact” of the infringement (“considerable profit”, “large scale loss avoidance” or “significant damage”), the NSSMC should consider introducing additional criteria for “serious cases” that constitute criminal offences. Market integrity can also be significantly harmed by market abuse that does not have a direct financial impact. Such a prerequisite for criminal sanctions may also lead to inappropriate limitations in practice as it may be difficult to assess or prove this financial impact. Therefore it is recommended that the NSSMC continues to discuss the most appropriate definition of a serious case with the criminal enforcement authorities. In addition, in line with the planned approach for the gradual introduction of the maximum administrative fines, it is recommended to

²³ According to Art. 222-1 of the draft Criminal Code a violation of the prohibition of stock market manipulation that leads to a considerable profit or avoidance of loss, or causes essential damage to the legally protected rights or freedoms, individual interests, or state, public, or legal entities’ interests must be punished by a fine from 25 million to 50 million minimum tax-free incomes of citizens or by imprisonment for a period of two to four years. The same penalty range is proposed to apply under Art. 232-1 of the draft Criminal Code for violation of the prohibition on insider transactions. According to Art. 232-1 of the draft Criminal Code, violation of the prohibition of illegal use of inside information can be punished by a fine from 12.5 million to 25 million minimum tax-free incomes of citizens or by imprisonment for a period of up to two years.

consider whether the planned full level of criminal fines could apply only at the same time as the full level of administrative fines would apply.

84. **It is important to ensure that the NSSMC's proposals will form a coherent framework with the existing criminal legislation.** IOSCO Principles and the EU legislation include very limited requirements for criminal sanctions and the powers of the competent authority in criminal proceedings. As a result, the NSSMC is strongly encouraged to engage the criminal enforcement authorities and judicial bodies in further discussions about the proposals to ensure that they will not unnecessarily deviate from the existing criminal enforcement powers and approaches to criminal enforcement proceedings in Ukraine. This applies especially to:

- The compatibility of the amount of fines proposed in Art. 222-1 and 232-1 of the Criminal Code and the amount of other fines permitted under the Criminal Code.
- The compatibility of the definitions of market abuse violations in Art. 222-1 and 232-1 of the Criminal Code with the general requirements for the drafting of the Criminal Code provisions.
- The proposed change to Art. 71 of the Criminal Procedure Code, as in the case of other authorities the current provision only provides a right for criminal authorities to apply for an involvement of a specialist and not an obligation to do so.
- The proposed change to Art. 236 of the Criminal Procedure Code, as in the case of other authorities the current provision only provides a right for investigators or prosecutors to invite experts to participate in the search to obtain assistance on matters requiring specialized knowledge.
- The proposed obligation for courts in Art. 376 of the Criminal Procedure Code to file a copy of a court decision in criminal proceedings involving market abuse to the NSSMC no later than the next day after its adoption, as in other cases a copy of court decisions should only be filed to the parties of criminal proceedings who were absent from the hearing.

Appendix I. Relevant EU Level 1 and 2 Legislation²⁴

Legal instrument	Number	Hyperlink to the text (latest consolidated version where applicable)
Prospectus Directive (PD)		
<i>Level 1</i>		
Directive	2003/71/EC	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:02003L0071-20140523
<i>Level 2</i>		
Regulation	(EC) No 809/2004	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:02004R0809-20160324
Regulation	(EC) No 1569/2007	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:02007R1569-20150101
Regulation	(EU) No 382/2014	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32014R0382
Regulation	(EU) 2016/301	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R0301
Transparency Directive (TD)		
<i>Level 1</i>		
Directive	2004/109/EC	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:02004L0109-20131126
<i>Level 2</i>		
Directive	2007/14/EC	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:02007L0014-20131126
Regulation	(EC) No 1569/2007	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:02007R1569-20150101
Decision	2008/961/EC	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:02008D0961-20150101
Regulation	(EU) 2015/761	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32015R0761
(Regulation)	C(2016) 2887 ¹	http://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2887-EN-F1-1.PDF http://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2887-EN-F1-1-ANNEX-1.PDF
Market Abuse Regulation (MAR) and Directive on Criminal Sanctions on Market Abuse (CSMAD)		
<i>Level 1</i>		
Regulation	(EU) No 596/2014	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32014R0596 ²
Directive	2014/57/EU	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32014L0057
<i>Level 2</i>		
Directive	(EU) 2015/2392	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32015L2392
Regulation	(EU) 2016/347	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R0347

²⁴ Information in this Appendix is up-to-date as of July 15, 2016.

Regulation	(EU) 2016/378	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R0378
Regulation	(EU) 2016/522	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R0522
Regulation	(EU) 2016/523	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R0523
Regulation	(EU) 2016/908	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R0908
Regulation	(EU) 2016/909	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R0909
Regulation	(EU) 2016/957	http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1466756462222&uri=CELEX:32016R0957
Regulation	(EU) 2016/958	http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1466756553611&uri=CELEX:32016R0958
Regulation	(EU) 2016/959	http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1466756602978&uri=CELEX:32016R0959
Regulation	(EU) 2016/960	http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1466756650743&uri=CELEX:32016R0960
Regulation	(EU) 2016/1052	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R1052
Regulation	(EU) 2016/1055	http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R1055
Sources: EUR-Lex, European Commission		
<p>¹ The Commission Delegated Regulation with regard to regulatory technical standards on access to regulated information at Union level has not yet been published in the Official Journal of the EU. It is currently subject to the right of the European Parliament and of the Council to express objections. A hyperlink to the Regulation adopted by the Commission is therefore provided.</p> <p>² Art. 19, 35 and 38 of MAR were amended by Art. 56 of Regulation (EU) 2016/1011 (http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R1011) and Art. 39 of MAR was amended by Art. 2 of Regulation (EU) 2016/1033 (http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32016R1033). These changes have not yet been consolidated to this version.</p>		

Appendix II. Existing Disclosure Requirements

	Public JSC and public offer	Public JSC and private placement	Private JSC and public offer	Private JSC and private placement	LLC and public offer	LLC and private placement
Definition						
Number of shareholders	No limits	No limits	Max. 100, as of May 1, 2016 no limits	Max. 100, as of May 1, 2016 no limits	N/A	N/A
Public offer / prospectus						
Allowed to make a public offer	Yes	N/A	Yes (bonds only)	N/A	Yes (bonds only)	N/A
Allowed to make a private placement	N/A	Yes (shares: max. 100 investors + shareholders; bonds max. 100 investors)	N/A	Yes (max. 100 investors, including shareholders) – Not possible to offer to more than 100 shareholders	N/A	Yes (bonds only, max. 100 investors)
Prospectus requirements	Prospectus to be published	Prospectus to be made available to investors	Prospectus to be published	Prospectus to be made available to investors	Prospectus to be published	Prospectus to be made available to investors
Listing / admission to trading						
Listing (stock exchange register)	Mandatory listing of shares as of May 1, 2016	Mandatory listing of shares as of May 1, 2016	Shares: No Bonds: Yes	Shares: No Bonds: No	Bonds: Yes	Bonds: No
Admission to trading (stock exchange list)	Yes Bonds - issue has to be completed through stock exchange	Yes	Shares: No (except stock exchange auction) Bonds: Yes	Shares: No (except stock exchange auction) Bonds: No	Bonds: Yes	Bonds: No
Periodic reporting						

	Public JSC and public offer	Public JSC and private placement	Private JSC and public offer	Private JSC and private placement	LLC and public offer	LLC and private placement
Quarterly reporting	Yes (if listing)	Yes (if listing)	Yes (bonds or at least 25% state ownership)	No (unless state ownership at least 25%)	Yes	No
Annual reporting	Yes	Yes	Yes	Yes	Yes	Yes
Auditing of annual reports	Yes	Yes	Yes	No	Yes	No
Accounting standards to be used	IFRS	IFRS	Ukrainian GAAP (IFRS for financial institutions)			
Ad hoc reporting						
Ad hoc disclosure obligation	Yes	Yes	Yes	Yes	Yes	Yes
Disclosure of inside information as defined by MAR (if listed/admitted to trading)	N/A	N/A	N/A	N/A	N/A	N/A
Dissemination and storage of information						
Availability on issuer's website	Yes	Yes	Yes	Yes	Yes	Yes
Filing to NSSMC database	Yes	Yes	Yes	Yes	Yes	Yes
Filing to the stock exchange (exchange listed/registered securities)	No	No	No	No	No	No
Publication in official newspaper	Yes	Yes	Yes	Yes	Yes	Yes
Filing with the NSSMC	Yes	Yes	Yes	Yes	Yes	Yes
Major shareholding notifications						
Shareholder's obligation to notify major shareholdings	No	No	No	No	No	No
Source: NSSMC.						