

Ukrainian capital and commodity markets: enhancement to regulator's powers and other regulatory developments

12 June 2024

On 27 April 2024 the Law of Ukraine "On Amendments to the Law of Ukraine "On State Regulation of Capital Markets and Organised Commodity Markets" and Certain Other Statutory Acts of Ukraine Concerning Regulation and Supervision of Capital Markets and Organised Commodity Markets" (the "Law") came into effect.

As claimed by the Law's authors, the primary aim of the Law is to frame an effective regulatory system for the Ukrainian capital market by, inter alia, expanding the powers of the regulator, the National Securities and Stock Market Commission (the "Commission") and vesting it with broad authority to investigate offences on capital markets, amending the financing of its functions, and enhancing the rules for market abuse prevention.

While there are arguments in support of this Law, as a necessary regulatory framework for the development of the national capital market in accordance with the IOSCO requirements and its alignment with the EU laws, there are those that criticise the Law. The latter particularly relate to the transformation of the Commission into a de-facto law-enforcement authority with unprecedented discretionary powers. In this article, we will set these debates aside and focus on the most important aspects of the Law.

1 Commission: extended authorities

The Law introduces substantial modifications to the Law of Ukraine "On State Regulation of Capital Markets and Organised Commodity Markets" dated 30 June 1996 no.448/96-BP (the "Regulation Law") and the Law of Ukraine "On Capital Markets and Organised Commodity Markets" dated 23 February 2006 no.3480-IV (the "Markets Law") as it pertains to the expansion of the Commission's authorities.

Notably, the Commission will among other things:.

- "**clarify the list of actions**" that may be conducted exclusively on condition of obtaining a license for the relevant activities on capital markets or organised commodity markets, or a respective certificate from the relevant register. Furthermore, the Law grants the Commission the power to determine the rules for the combination of activities on capital markets and organised commodity markets, which are now regulated by statutory acts (i.e., the laws of Ukraine adopted by the Parliament) and will be determined by the Commission's regulations.
- decide on **whether financial instruments and/or so-called civil rights objects (i.e. assets or instruments) belong to securities**.

In this regard, it is worth noting that the Law amends the definition of "security" (please see below more details) by excluding certain key features of securities and thus making this definition rather broad. This

Wolf Theiss

gives the Commission room for interpretation as to whether an instrument can be referred to as a security with all applicable regulatory requirements.

- **conduct inspections and investigations** on capital markets or organised commodity markets (please see further details below). Compared to the audits that the Commission is authorised to conduct under effective regulations, the Law generally arms the Commission with greater capacity and authority during the inspection process;
- have **more extended tools of influence on market players**, such as requesting the dismissal of persons with managerial functions. It will be also able to suspend measures that are taken by market participants to increase sales of financial instruments and the distribution of information regarding financial instruments that is unrelated to advertising (the Law does not specify any grounds for such suspension and one can expect it in the future regulations of the Commission).

As a general observation, the Commission has obtained discretion to decide on and adopt regulations involving a broad list of matters. Moreover, in addition to the above-mentioned determination of licensed activities, securities, and combination of activities, the Commission will set fees for its administrative services, additional requirements for professional participants and the right to suspend the licences of professional participants.

2 New definition of security

The Law introduced a new definition of security defining it as a document (electronic document) that certifies the property [ownership] and other rights of its owner, arising as a result of one or more transactions (issuance or execution of a security) and having monetary value. In addition, the Law abandons Article 196 of the Civil Code of Ukraine, setting forth that the mandatory requisites of a security are that it be established by law and that an instrument cannot be considered as a security if it fails to meet the specified requisites and form.

However, it is presently not clear whether such requisites will be established by the Commission's regulations rather than by statutory acts or if the Commission will develop some other criteria for referring to an instrument as a security. The new definition seems to be too broad and a bit puzzling. Unfortunately, the explanatory note behind the Law omits shedding light on the reason for having it this way.

In this regard, one cannot ignore another definition of a security that has been recently brought to law by amending Article 194 of the Civil Code of Ukraine. Namely, the Law of Ukraine "On Agrarian Notes" dated 22 February 2024, no. 3586-IX (the "Agrarian Notes Law") provides for a more extended and self-sufficient definition of a security, which is still conditioned by statutory law¹.

The Agrarian Notes Law will become effective on 1 January 2025, while the provisions of the Markets Law amending the definition of a security have already come into effect. The existing confusion seems to be the result of an omission by the lawmakers rather than an intention to have the definition of security changed twice in one year. Nevertheless, one may only guess at which of those definitions will ultimately survive.

3 Authorised persons of the Commission

The Law introduces an institute of authorised persons of the Commission ("authorised persons") who are defined as the officers of the Commission and are authorised to perform the following functions on capital markets and organised commodity markets: (i) carrying out inspections, (ii) conducting investigations, (iii) supporting and presenting cases that are reviewed by the Commission, (iv) considering cases of breach of applicable legislation.

¹ The Agrarian Notes Law introduces the following definition: "A security as an object of civil rights, which form of existence is established by law, certifies a monetary or other property right, determines the relationship between the issuer of the security (the person who executed the security) and the person who has rights to the security, provides for the fulfilment of obligations for such a security, as well as the possibility of transferring rights to a security and rights attached to a security to other persons or limiting such possibility in the cases and in the manner prescribed by law."

The authorised persons will be powerful players and basically independent. This follows from the provisions of the Law setting forth that an authorised person shall not be obligated to provide any explanations regarding, among other things, the subject of an inspection or an investigation, except for providing explanations during the course of criminal proceedings and litigation.

4 Inspections and investigations

The Law supplements the Regulatory Law with detailed rules for the off-site and on-site inspections by the Commission and extends a list of persons that can be subject to inspections. Notably, this list has been updated with such new categories as investors in financial instruments, applicants for the obtainment of a license of a professional participant and authorisation of information services provider on capital markets and organised commodity markets. So far, only the actual holders of the license/authorisation can be subject to the audit by the Commission.

As already mentioned, inspections will now be conducted by authorised persons who will exercise greater powers. An inspection will result in a draft report, which should be shared first with a person under inspection for any comments, objections, or suggestions that must be considered by the authorised person and either reflected in the report or rejected with grounds for the rejection.

In addition, after the completion of the inspection, the Commission may take additional measures, such as (i) requesting an inspected person to take certain actions, (ii) referring inspection documentation to the state enforcement authorities, other state or local authorities, (iii) referring these documents to the authorised person for the purpose of supporting the case or for conducting an investigation, and (iv) sending documentation to foreign capital markets regulators. However, the Commission has quite a deferred deadline of one year to take these measures following the completion of the inspection.

While the above-mentioned provisions on the inspections by the Commission have become effective, the procedures for conducting inspections and the consideration of the inspection report, the issuance of related rulings by the Commission and the form of the inspection report and other documents, must still be elaborated on in the regulations of the Commission.

Starting on **1 January 2026**, the Commission will be empowered with **investigatory functions** on capital markets and regulated commodity markets. There are grounds for the launch of an investigation in the Law; some of these, "*potential breach*" and "*reasonable suspicion of breach*" of applicable legislation, stand out as vague and uncertain. Investigations will be conducted by authorised person(s) and must be completed within 18 months. This term can be extended for another year.

While conducting an investigation, an authorised person is vested with powers that are very similar to the powers and functions of an investigator in criminal proceedings. They include:

- accessing the premises of capital market participants as well as professional participants of organised commodity markets, and based on a court ruling, the premises of any legal entity or individual;
- accessing the information and telecommunications systems, documents, objects etc. concerning the subject – matter of an investigation;
- requesting any information concerning the subject-matter of an investigation including restricted access information (apart from advocate secrecy);
- conducting a survey of individuals (including witnesses) and using video, photo, audio recordings in the course of a survey;
- upon the approval of the Head of Commission - requesting that the court to seize property including financial instruments and funds;
- suspending the performance of agreements on capital markets, further requesting the same from the court; and

- suspending the entry of amendments to the depository accounting system with respect to the securities of a specific owner.

The respective provisions on investigations require the Commission to adopt a number of by-laws, inter alia, regulating the process of decision-making by the Commission in terms of launching an investigation, the adoption of rules required in the course of investigation, etc.

5 Breaches of legislation; Penalties

Similarly, as provided in the effective laws, a violation of law must be recorded and documented in the form of a detailed act of violation. The Law amends this procedure as well as provides the requirements to the act, which is now the responsibility of a specially designated authorised person of the Commission, who is responsible for supporting the case.

In certain cases, which are to be determined by the Commission, an alleged wrongdoer will receive a draft of the act recording the violation along with a draft of a settlement agreement from the authorised person. Therefore, the Law introduces a kind of settlement procedure at this stage whereby the person in question for whom the act has been drawn up may provide comments, objections and suggestions to the act, as well as propose their own settlement terms by submitting a draft agreement.

The Law substantially expands the corrective measures that the Commission will be empowered to apply for the breach of legislation. Apart from financial sanctions, it may withdraw or suspend the licence/authorisation issued by the Commission and may apply public warnings, prohibitions against conducting transactions in financial instruments, compensation of damages to the investors, prohibitions against participating in trading and against performing managerial functions in a capital market participant, etc.

While applying these measures, the Law requires the Commission to consider a variety of factors such as: the severity and duration of the violation, the financial standing of the wrongdoer and the possible consequences caused by the application of sanctions, as well as damages to third parties caused by the violation, other violations of legislation within the last 10 years, cooperation with the Commission, etc.

The ranges of financial sanctions (fines) and the number of violations for which these sanctions could apply, as introduced by the Law, are among its most debatable provisions. These ranges are determined rather broadly (e.g., "from UAH 20 mln to UAH 30 mln" or "up to 81 mln but not exceeding 10% of the total annual turnover of a legal entity").

The provision on financial sanctions will come into effect on 1 January 2026 and the amounts will be subject to a gradually increasing reduction factor until 1 January 2030. Prior to 1 January 2026, the Commission will apply financial penalties envisaged by the transitional provisions of the Law based on reduced rates and for a limited number of violations. When it comes to individuals, most of these penalties will apply after introducing the respective amendments to the Code on Administrative Offences of Ukraine.

6 Regulatory contributions

The Law provides for a new mechanism and new sources of financing for the Commission. A novelty in the national law is the so-called regulatory contributions payable by professional participants and certified market players of capital markets and organised commodity markets that hold a respective licence/authorisation as of 1 January of a respective year. These regulatory contributions are linked to the minimum living wage of the employable population and depend on a specific activity. Basically, two rates are provided, which currently amount to UAH 45,420 and UAH 227,100. They must be paid to a special fund of the State Budget of Ukraine annually by 1 July.

Failure to make a regulatory contribution will be subject to forced collection by the state execution authority and financial sanctions.

The entry into force of these provisions is linked to the enactment of amendments to the Budget Code of Ukraine related to the Commission's functions.

7 Other regulatory developments

There are a number of other fundamental regulatory developments introduced by the Law that are worth noting, including:

- Enhancement of corporate governance rules for professional participants of capital markets, including requirements and procedures for a conflict-of-interest disclosure, its prevention and settlement, notification to the regulator of market abuse or misbehaviour.
- Updated and extended rules for self-regulatory organisations of professional participants of capital markets.
- More extended rules on market abuse prevention including more enhanced requirements related to insider trading such as the disclosure of insider information and insiders, insider deals, etc.
- Rules, procedures and authorities of the Commission in the course of international cooperation with international organisations, market regulators and their associations.
- Introduction of the notion of whistle-blowers with regard to capital markets and organised commodity markets, with the relevant procedures, rights and protection measures.

8 Further steps

The new regulatory framework will come into force in stages over the next few years. During this time, apart from the further development and adoption of by-laws by the Commission, which are necessary for the implementation of the Law, the regulator and market players will simultaneously undergo the transformation and adaptation to a new regulatory set-up.

One of the main difficulties of this process is the fact that the Law does not simply introduce the new rules but rather changes the principles and approaches to regulation and enforcement in capital markets and organised commodity markets dramatically. It is quite clear that the success of this entire undertaking will largely depend on the quality of regulations, which are yet to be developed by the Commission, and their ability to ensure transparency and be premised on the balance of interests and risks.

Wolf Theiss is one of the leading European law firms in Central, Eastern and South-Eastern Europe with a focus on international business law. With more than 390 lawyers in 13 countries, over 80% of the firm's work involves cross-border representation of international clients. Combining expertise in law and business, Wolf Theiss develops innovative solutions that integrate legal, financial and business know-how.

For more information, please contact:



Oksana Volynets
Senior Associate

E oksana.volynets@wolftheiss.com

T +38 044 3 777 508

