



UKRAINE

TECHNICAL ASSISTANCE REPORT—ENHANCING THE POWERS AND INDEPENDENCE OF THE NATIONAL SECURITIES AND STOCK MARKET COMMISSION

October 2015

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ENHANCING THE POWERS AND INDEPENDENCE OF THE NATIONAL SECURITIES AND STOCK MARKET COMMISSION

Eija Holttinen (Mission Chief)
Phyllis J. Cela and Malcolm Rodgers (External Experts)

October 2015

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GLOSSARY

EU	European Union
FSAP	Financial Sector Assessment Program
IOSCO	International Organization of Securities Commissions
MCM	Monetary and Capital Markets Department of the IMF
MMOU	Multilateral Memorandum of Understanding
MoF	Ministry of Finance
MoJ	Ministry of Justice
MOU	Memorandum of Understanding
NBU	National Bank of Ukraine
NSSMC	National Securities and Stock Market Commission
SRO	Self-Regulatory Organization
SRS	State Regulatory Service
TA	Technical Assistance

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 the period July 13–24, 2015. The mission members included Ms. Eija Holttinen (mission chief) and Ms. Phyllis J. Cela and Mr. Malcolm Rodgers (MCM experts).

The mission's main task was to assess the sufficiency of the NSSMC's operational and financial independence, accountability, and investigative, enforcement and international cooperation powers, and advise on changes needed to enhance the Ukrainian framework's compliance with the International Organization of Securities Commissions' (IOSCO) Objectives and Principles of Securities Regulation (IOSCO Principles).

The mission met with Chairman Timur Khromaev and other senior officials of the NSSMC. Meetings were also held with the Head of the Higher Economic Court Bogdan Lvov, Head of the Verkhovna Rada Committee on Financial Policy and Banking Sergiy Rubalka, First Deputy Governor of the National Bank of Ukraine (NBU) Oleksandr Pysaruk, Deputy Minister of Finance Roman Kachur, Deputy Minister of Justice for State Enforcement Service Sergiy Shkliar, Head of the State Regulatory Service (SRS) Ksenia Liapina, as well as other senior officials of these organizations. The mission also met senior officials of the Administration of the President of Ukraine, Higher Administrative Court, Prosecutor General's Office, Ministry of Justice, Ministry of Interior, and Security Service as well as representatives of self-regulatory organizations, market participants, and law firms. The mission would like to express its appreciation to Ukrainian authorities and other stakeholders for providing their senior officials' valuable time for in-depth discussions with the mission.

EXECUTIVE SUMMARY

The NSSMC faces significant challenges in its role as the regulator of the Ukrainian securities market. Market activity has been shrinking over the past few years, but misconduct—such as issuance and trading of “fictitious” securities—prevails. At the same time, the authorities have committed to an ambitious Program of Financial Market Development of Ukraine until 2020, which also incorporates the implementation of European Union (EU) legislation in line with the Association Agreement. Dealing with these challenges requires resources, powers, and ability to take effective regulatory, supervisory and enforcement action.

As a member of the international securities regulatory community, the NSSMC is expected to cooperate with and provide assistance to its international peers. However, at the moment it is unable to commit to these reciprocal arrangements due to significant gaps in its investigation, enforcement and international cooperation powers. Having these powers is a precondition of being accepted as a signatory to the IOSCO Multilateral Memorandum of Understanding (MMOU). Key changes needed relate to enhancing the NSSMC’s ability to conduct investigations of and demand information from any legal or natural person, have access to and share information otherwise restricted by secrecy laws, assist foreign authorities even without an apparent violation of the Ukrainian securities laws, as well as maintain the confidentiality of information exchanged under the MMOU.

The NSSMC’s operational independence falls short of the expectations for an independent regulator. The most significant constraints have been imposed on the NSSMC’s inspection activities. The moratoria on on-site inspections, one of which still remains in place, the constraints on the frequency and length of inspections, and the requirement to seek approval of an external authority for certain inspections are in sharp contrast with the standards set by IOSCO. Certain elements of the rulemaking process, in particular the degree of discretion provided to the Ministry of Justice (MoJ) in assessing the compliance of the NSSMC regulations before registering them, may also undermine the NSSMC’s operational independence. These shortcomings should be addressed. To balance such enhanced independence, it is recommended that the NSSMC be subject to explicit requirements to prepare an annual report to the President and the Verkhovna Rada (Parliament) and to give reasons to parties affected by its regulatory, supervisory and enforcement decisions.

Ensuring the sufficiency and stability of the NSSMC’s funding in the current macroeconomic and fiscal environment is challenging. Given the broader financial stability risks arising from potentially inadequate securities regulation and supervision, the current constraints on the NSSMC’s financial independence raise concerns. The civil service remuneration rules make it difficult for the NSSMC to gain and retain experienced staff and the lack of funding for technology investment undermines the efficiency of its supervisory

activities. Moving to self-funding through administrative service charges and annual supervisory fees paid by regulated entities has the potential to address the funding challenges, and serious consideration should be given to it. However, it is not recommended that revenue from administrative sanctions be used as a funding source due to the conflict of interest this would create. Appropriate governance arrangements on setting the remuneration of the Chairman and Commissioners would also be required.

Table 1. Summary of Main Recommendations

Recommendation	Timeframe
<p>Amend legislation to enable the NSSMC to sign the IOSCO MMOU by:</p> <ul style="list-style-type: none"> • Providing the NSSMC with the: <ul style="list-style-type: none"> • Power to conduct investigations of and demand information from any legal or natural person; • Access to and ability to share information restricted by secrecy laws; and • Ability to assist foreign authorities even without an apparent violation of the Ukrainian securities laws. • Protecting the confidentiality of information exchanged under the MMOU. 	End-February 2016
<p>Amend legislation to enhance the NSSMC's operational independence by:</p> <ul style="list-style-type: none"> • Removing the constraints on the NSSMC's ability to plan and conduct inspections; • Removing the external approval requirements for the NSSMC's rulemaking; and • Providing appropriate legal protections to the NSSMC and its Chairman, Commissioners and staff. <p>In parallel, formalize the accountability arrangements for the NSSMC.</p>	End-February 2016
<p>Enhance the sufficiency and stability of the NSSMC's funding by amending the existing budget process and related legislation, especially with a view to:</p> <ul style="list-style-type: none"> • Removing constraints on the NSSMC's ability to remunerate employees appropriately; and • Enabling the NSSMC to make adequate investment in technology. 	End-February 2016

I. INTRODUCTION

1. **The NSSMC is the state agency responsible for the regulation of the Ukrainian securities market.** The main law regulating its governance and responsibilities is the Law on State Regulation of Securities Market (Law on State Regulation). Various sectoral laws, such as the Law on Securities and Stock Market, regulate the provision of specific services in the market. The NSSMC has a Chairman and up to 6 Commissioners; however currently only the Chairman and 4 Commissioners have been appointed. Out of the 460 staff positions, 321 are based in Kyiv and 139 in the regional offices. A number of staff positions are currently vacant.
2. **The NSSMC is a member of IOSCO, and is therefore expected to strive to comply with the IOSCO Principles.** IOSCO Principles set out the requirements and expectations on an effective securities regulatory and supervisory framework. The IMF and World Bank use IOSCO Principles as a benchmark in their Financial Sector Assessment Program (FSAP).
3. **IOSCO Principles require a securities regulator to have comprehensive inspection, investigation and enforcement powers, and the ability to use these powers to assist its foreign counterparts.** A regulator without sufficient investigation and enforcement powers cannot be accepted as a signatory to the IOSCO MMOU, which is an understanding among its signatories on consultation, cooperation, and exchange of information for purposes of enforcing securities regulation. At the time of the mission IOSCO had 105 signatory and 24 non-signatory members, with the NSSMC being among the non-signatory members.
4. **Operational independence, stable and adequate funding, and the appropriate accountability of the securities regulator are key building blocks of a sound regulatory system.** Independence requires the ability to operate independently of sectoral or political interest and to undertake regulatory measures and enforcement actions without external (political or commercial) interference. A stable source of funding is critical, because operational independence can be compromised if funding can be curtailed by external action. The ability of the regulator to act independently is enhanced by adequate legal protection for the regulator and its staff in the exercise of their functions. At the same time, independence has to be balanced with appropriate accountability.
5. **The mission's work built on an analysis of the key laws and regulations that relate to the functions, powers and independence of the NSSMC.** The complexity of the legal framework and lack of complete, up to date translations of certain key laws posed challenges on the mission's ability to ensure complete understanding of the framework applicable to the NSSMC. Appendix I includes a list of the laws that the mission used as a basis of its work.

6. **This report is comprised of three main sections.** Section II describes the legislative and regulatory changes that are needed for the NSSMC to gain the necessary powers to comply with the requirements for signatories of the IOSCO MMOU. Section III discusses measures needed to enhance the NSSMC's operational independence, while Section IV focuses on the NSSMC's funding. Both Sections III and IV suggest some enhancements to the NSSMC's accountability that would be appropriate in light of any enhanced operational and financial independence.

II. PROVIDING THE NSSMC WITH SUFFICIENT POWERS

A. Background

7. **The NSSMC has submitted several versions of its MMOU application to IOSCO, but has not completed the process.** The original application was submitted in February 2013, which the NSSMC has amended twice (October 2013 and May 2015). IOSCO's review of the May 2015 application is ongoing. The past questions from IOSCO have focused on the same areas as those identified by the mission where the NSSMC still lacks the powers required to comply with the MMOU requirements.

8. **The NSSMC is among the shrinking number of IOSCO members that are not signatories to the IOSCO MMOU because of a lack of key enforcement and cooperation powers.** This means that any formal assessment would identify significant gaps in the Ukrainian system's compliance with the IOSCO Principles.

B. Findings and Recommendations

9. **The mission conducted a detailed assessment of the Ukrainian framework's compliance against the IOSCO MMOU requirements.** A detailed description of the analysis and its findings is included in Appendix II.

10. **The NSSMC lacks important powers to comply with the IOSCO MMOU requirements.** The mission advised the NSSMC on areas where the Ukrainian framework does not comply with the IOSCO requirements. The principal findings include that the NSSMC lacks comprehensive investigation powers, is unable to access and share bank records, is unable to assist foreign regulators where the NSSMC does not have a regulatory interest in the subject matter of a request, and is unable to protect the confidentiality of information obtained under the MMOU. Addressing these gaps requires legislative changes.

Legislative changes needed and recommended

11. **The Ukrainian legislation needs to be amended to provide the NSSMC with additional powers that would:**

- Empower it to conduct investigations to require any legal or natural person, whether regulated or unregulated, to provide information and documents:
 - To determine compliance with Ukrainian securities laws; and
 - To assist foreign regulators under cooperation arrangements.
- Permit it to have access to and share with other regulators information that is “restricted” under various Ukrainian laws, including information subject to bank secrecy or “professional secrecy” and personal data; and
- Provide it with the ability to assist foreign authorities even without an apparent violation of the Ukrainian securities laws.

12. The additional confidentiality requirements necessary to protect information exchanged under the MMOU would:

- Deem information (including requests for assistance) obtained from a foreign authority to be confidential information.
- Protect the confidentiality of information obtained under the MMOU against legally enforceable demands of any private party or public body without prior approval of the foreign authority. Under the MMOU, exceptions are permitted for demands from courts and criminal authorities related to criminal investigations and prosecutions of securities related violations.
- Prohibit current and former NSSMC employees from disclosing confidential information obtained under the MMOU, except as permitted in the MMOU.

13. In addition to the above necessary powers, the NSSMC would benefit from reinstatement of certain inspection powers. In particular, the NSSMC’s authority to seize documents on a temporary basis during inspections of regulated entities, as provided under the Law on State Regulation, should be restored.

Regulatory changes needed

14. The NSSMC itself can take certain measures to enhance compliance with the MMOU requirements. This relates in particular to making additions to its recordkeeping requirements that apply to regulated firms and ensuring that its MMOU application includes all the necessary information (see Appendix II). Preparing a complete application would expedite the screening of the application by IOSCO.

III. NSSMC'S OPERATIONAL INDEPENDENCE AND ACCOUNTABILITY

A. Background

15. **The legal basis for the NSSMC's governance and responsibilities is set out in the Law on State Regulation.** Article 5 makes the NSSMC responsible for regulation of the securities market. Article 6 deals with the status and general accountability of the NSSMC to government, the appointment and removal from office of the Chairman and Commissioners, the status of Commission members and NSSMC staff, and governance arrangements including the role of the Chairman. In particular, under Article 6:

- The NSSMC is established as a state collegial body subordinated to the President of Ukraine and that reports to the Verkhovna Rada of Ukraine.
- The NSSMC as a collegial body consists of the Chairman and six Commissioners.
- The Chairman and Commissioners are appointed and may be dismissed by the President of Ukraine through the issue of a presidential decree.
- The Chairman and Commissioners are appointed for a term of six years, and may hold office for no more than two successive terms.
- The NSSMC's Chairman, Commissioners, managerial staff and specialists are civil servants.
- The schedule of positions and salaries of the NSSMC is approved by the Chairman with the consent of the Ukraine Ministry of Finance.
- The maximum number of employees is approved by the President of Ukraine.

16. **A number of specific topics are relevant in considering the extent to which the Ukrainian system meets the standards of operational independence required by the IOSCO Principles.** These are NSSMC rulemaking, control over the NSSMC's use of its inspection powers, and protections for Commission members and NSSMC staff. The current arrangements and their legal basis are described in detail in Appendix III.

17. **Operational independence has to be balanced with adequate accountability mechanisms that apply to the NSSMC.** This relates, for example, to procedural protections available to those adversely affected by NSSMC supervisory decisions. The current accountability arrangements are described in Appendix V.

B. Findings and Recommendations

18. **The system in Ukraine has challenges in meeting in full all the IOSCO Principles relating to operational independence.** In contrast, the related accountability arrangements are broadly appropriate.

NSSMC rulemaking

19. **NSSMC rulemaking is subject to controls that relate both to the process used for the making of rules, and also some aspects of the substance of the rules.** These controls are exercised by various state bodies, most importantly the SRS and MoJ.

20. **The Law on State Regulatory Policy in the Area of Business Activity (Law on State Regulatory Policy) and the Law on Licensing of Economic Activities (Law on Licensing) require the involvement of the SRS in the making of some NSSMC rules.** The legislation is designed to ensure that regulators follow proper processes, such as consultation and the analysis of the need for a proposed rule. An obligation of this kind is not inconsistent with IOSCO Principles. It is required of securities regulators in some jurisdictions and followed by many others even where there is no requirement to do so. The role that the SRS plays in monitoring compliance with these obligations is less common, especially in relation to the power it appears to have under the new Law on Licensing to refuse to approve the making of NSSMC rules.

21. **All NSSMC rules of a general character must be reviewed and registered by the MoJ before they become effective.** The key issue for consideration is whether the MoJ review involves reviewing the regulator's judgment as to what is necessary from the point of view of securities regulatory policy, or is confined to evaluating the legal effectiveness of a proposed rule. There appears to be scope under the current arrangements for the MoJ to substitute its view of what securities regulatory policy requires for that of the regulator. This undermines the ability of the NSSMC to make regulatory decisions on matters in which it has unique expertise, and adversely impacts its independence.

22. **In contrast, the NBU is subject to much more limited controls on its rule-making activities.** The NBU is not subject to the obligation to obtain MoJ registration of its regulatory acts, including those applying to banking regulation and supervision. However, some NBU regulatory acts are subject to the procedural requirements set out in the Law on State Regulatory Policy (see Article 3). These include regulatory acts relating to the conduct of banking transactions, payment and settlement systems, and the licensing of banks. By contrast, NBU regulatory acts relating to banking regulation and supervision are not subject to the Law on State Regulatory Policy.

23. **Two alternative draft laws relating to the independence of the NSSMC aim at addressing these challenges.** A summary of the draft laws is included in Appendix VI. A draft Law on Independent Regulators of Ukraine (draft Law on Independent Regulators) and a draft Law on Amendments to Some Legal Acts Regarding Implementation of IOSCO Principles Concerning Functioning of Stock Market Regulator (draft NSSMC Independence Law) remove the obligation of the NSSMC to comply with the process obligations for rulemaking imposed by the Law on State Regulatory Policy and the Law on Licensing. The

effect of this would be that the NSSMC would have to comply with Article 6 of the Law on State Regulation, which requires consultation about proposed rules, but it would not be obliged to prepare an analysis of the regulatory effect, including costs, of proposed rules (as currently required by Article 8 of the Law on State Regulatory Policy). Removal of an obligation to conduct an analysis of regulatory effect may raise questions about compliance with IOSCO Principles for regulatory processes (see IOSCO Principle 4, and especially Key Question 2(c) of the Assessment Methodology), if the NSSMC does not have a legal obligation to carry out such an analysis, or does not adopt a policy of doing so as a matter of practice.

24. **Supervision of the NSSMC’s rulemaking by the SRS does not raise significant independence questions.** This is because it is focused on compliance with process obligations rather than the specific technical content of proposed rules.

25. **The breadth of the criteria used by the MoJ and its power to refuse registration raise potential independence issues under the IOSCO Principles.** In addition, the practice of industry participants of making comments directly to the MoJ as well as (or instead of) to the NSSMC is undesirable. Removal of the obligation to register NSSMC regulations with the MoJ, as is proposed in the draft Law on Independent Regulators and the draft NSSMC Independence Law, would remove these problems. This would treat securities rules made by the NSSMC in the same manner as banking supervision rules made by the NBU that do not require MoJ registration to enter into force, and thereby reinforce the NSSMC’s operational independence.

NSSMC inspections

26. **The NSSMC like other state licensing authorities in Ukraine has been subject to moratoria prohibiting it from carrying out inspections of regulated entities.** The mission has been informed that the temporary moratorium applicable to all inspections that was in force during the period January 1–June 30, 2015 expired at the end of June. Another moratorium that applies under the Tax Code to inspections of entities whose yearly revenue is UAH 20 million or less continues to be in force. A proposal has been submitted to Verkhovna Rada to exempt the NSSMC from this moratorium.

27. **The Law on on Basic Principles of State Supervision (Control) in the Sphere of Economic Activity (Law on State Supervision) and the Law on Licensing impose limits on the NSSMC’s ability to carry out inspections both on a routine basis (scheduled inspections) and on an ad hoc basis (unscheduled inspections).** The NSSMC is required to have a publicly disclosed plan for scheduled inspections and can only carry out one scheduled inspection on a regulated entity each year; and unscheduled inspections can only be carried out for reasons specified in the legislation. Some types of unscheduled inspections require the approval of the Expert and Appellate Board and the SRS before they can be

undertaken. The NBU is not subject to the limitations on inspections that apply to the NSSMC under the Law on State Supervision as that law does not apply to the NBU. This approach is in line with the operational independence requirements for financial sector regulators set by the relevant international standards.

28. **These limits are not consistent with the IOSCO Principles which envisage a regulator having discretion on when and how it can use its inspection powers, limited only by the terms of the securities legislation.** The limits on this discretion in the Ukrainian legislation mean that the NSSMC is not fully independent in its ability to make decisions about the use of its powers. The draft laws bring the regime more into line with IOSCO expectations as they remove the limits on the NSSMC's use of its inspection powers and eliminate the SRS supervision and Expert and Appellate Board appeal mechanisms.

Protection of the NSSMC Commission members and staff

29. **The power of the President to remove the NSSMC Chairman or Commissioners does not appear to be limited as required by the IOSCO Principles.**¹ The removal power does not appear to be confined to the circumstances listed in Article 6 of the Law on State Regulation (set out in Appendix III), and may be exercised for other reasons or even without cause. The law should be clarified to require that the Chairman or a Commissioner can be removed only for the reasons enumerated. In addition, it would be desirable to add a requirement, found in many other jurisdictions, that a decision to remove a Chairman or Commissioner from office must set out the reasons for the dismissal, and a notice including these reasons must be provided to the person affected, and made public.

30. **There are no specific provisions in legislation providing legal protection to the NSSMC, and its Chairman, Commissioners and staff for the bona fide discharge of their governmental, regulatory and administrative functions and powers.** Such protection is required by the IOSCO Assessment Methodology, and ensures that the regulator, Commission members, and staff can carry out their functions without the threat of liability for proper performance of their duties.²

31. **To comply with the IOSCO Principles, measures to ensure adequate protection for Commission members and staff should be introduced.** Both draft independence laws address the issues raised above. They make explicit that the NSSMC Chairman and Commissioners can be removed from office only for the reasons specified in the legislation. They also provide protection for Commission members and staff by providing that, if there is

¹ In particular, see Key Question 5 under Principle 2 of the Assessment Methodology.

² See Key Question 4 under Principle 2.

a court challenge to an official's actions, the NSSMC rather than the individual is to be the respondent. Nonetheless, to bring the regime fully into line with IOSCO Principles, the legislation should be further strengthened by providing explicit immunity for the NSSMC, its Chairman, Commissioners, and staff for acts and decisions taken in the good faith discharge of the NSSMC's functions and powers. The NSSMC should also consider providing indemnification for legal costs if an individual Commission member or staff member is sued in a personal capacity for the good faith discharge of their functions.

Accountability

32. **The current arrangements for the accountability of the NSSMC to the government and Verkhovna Rada are relatively informal.** However, they appear to be effective in practice.

33. **The NSSMC is transparent in its operations and decision making.** There are specific legislative requirements that require transparency. In addition, the NSSMC has a policy of using its website to communicate with the market and the public, and of providing information about the regulatory framework and Commission decisions. It also voluntarily prepares and publishes an annual report.

34. **Current NSSMC procedures create a generally adequate framework for due process in decision making.** The NSSMC is not subject to a comprehensive legislative obligation to give written reasons for its material decisions or to give affected persons the opportunity to make representations before decisions adverse to them are made. However, it has adopted and makes publicly available procedures obliging it to provide reasons for its regulatory decisions and giving in relevant circumstances affected parties the right to make representations before decisions adverse to them are made.

35. **Sufficient possibilities to appeal exist.** Court review is available for all decisions of the NSSMC and other avenues of appeal are also open in relation to some decisions. There is evidence that rights of appeal against NSSMC decisions are actively exercised. In 2013-2014, Administrative Courts of first instance dealt with more than 3,600 cases in which the NSSMC was either plaintiff or defendant, many involving appeals against NSSMC sanction decisions.

36. **The accountability framework for the NSSMC under the current legislation does not raise any significant issues for compliance with the IOSCO Principles.** The draft independence laws do not make any additions to the accountability framework other than by requiring the NSSMC's use of resources to be audited by an independent non-government auditor.

37. **Nonetheless, if either of the draft independence laws were to be proceeded with, consideration should be given to clarifying and strengthening the accountability of the NSSMC by:**

- Making it mandatory for the NSSMC to provide an annual report to the President and Verkhovna Rada;
- Permitting the President to specify matters that must be covered in that report, provided this does not require the disclosure of confidential or commercially sensitive information; and
- Creating a general obligation for the NSSMC to give reasons for its regulatory and supervisory decisions, and to give legal and natural persons adversely affected by its decisions the right to make representations before final decisions are made.

IV. NSSMC'S FINANCIAL INDEPENDENCE AND ACCOUNTABILITY

A. Background

38. **Funding of the NSSMC and bodies established by it to fulfil its functions is provided from the State budget of Ukraine (Article 18 of the Law on State Regulation).** Preparation of the NSSMC's budget takes place as part of the government-wide budget process. The Cabinet of Ministers makes decisions on the budget in September each year. When main government priorities are determined, the Ministry of Finance (MoF) provides each agency of the government with an indication of the proposed allocation to that agency. Agencies then undertake planning in light of that information, and have the opportunity to request changes to proposed allocations. Once the budget has been finalized, there are limits (described in Appendix IV) on the NSSMC's ability to reallocate funds between activities.

39. **The NSSMC's approved budget has remained relatively stable over the last 5 years, taking into account the decline in market activity.** The budgets for 2014 and 2015 fiscal years saw a reduction of a little over 12 percent from fiscal year 2013. Approved staff numbers have reduced significantly. Reductions in staff numbers have been achieved through the closure of regional offices and the absorption of some functions into the central office, where numbers have increased. Further details are provided in Appendix IV.

40. **Staff salaries and on-costs account for between 88 and 90 percent of the NSSMC budget over the last 3 years.** There is no budget provision for capital expenditure or expenditure on IT systems.

B. Findings and Recommendations

41. **It is difficult to draw firm conclusions about the required level of NSSMC's funding, especially in light of the fact that the market has been shrinking over recent years.** At the same time, significant problems have emerged in the market such as those

relating to “fictitious securities.” These problems place additional demands on the NSSMC and appear to be testing its ability to respond in a timely and effective way.

42. Despite these uncertainties, it is possible to draw some conclusions about the structural environment in which the NSSMC operates:

- The civil service remuneration rules which apply to the NSSMC are highly likely to be having an adverse effect on its ability to attract and retain suitably experienced and skilled staff, especially those with the market knowledge and understanding needed to make the NSSMC an effective regulator.
- There is a high probability that the lack of funding for investment in technology currently impedes the NSSMC’s ability to receive, analyze and act on information efficiently and effectively. Securities markets are technology intensive industries and their regulators need adequate levels of technology resources to do their jobs well. Over time, a continuing lack of appropriate technology has increasingly adverse consequences for both effectiveness and efficiency.
- Lack of funds that can be allocated for non-staff costs related to the NSSMC’s enforcement activities, such as costs of enforcing Commission decisions, is likely to be lessening the deterrent effect of monetary sanctions imposed by the NSSMC. For example, unless the NSSMC has a sufficient budget to enable it to seek court orders to collect monetary penalties, the impact of the sanctioning process is undermined.

43. The comments above apply to the position of the NSSMC now and in light of current market circumstances. If the NSSMC is to make an effective contribution to the ambitious program for the development of the Ukraine financial sector until 2020, there will be further demands on its resources and organizational expertise.

44. If the problems identified above cannot be adequately dealt with under the NSSMC’s current funding and structural arrangements, consideration should be given to alternative funding methods. To be fully effective, the NSSMC needs to be able to attract and retain suitably qualified staff, and to do so it must be able to remunerate them appropriately. In addition, investment in technology and systems is required to enhance the NSSMC’s capacity to effectively supervise markets and market participants, as is the ability to enforce the legislation effectively. If competing priorities for the state budget make this impossible to achieve under the current framework, alternatives such as creating a source of self-funding for all or some of the NSSMC’s funding needs should be explored.

45. Both independence laws propose a shift from government budget funding of the NSSMC to funding provided by administrative service charges, fees paid by regulated entities, and revenue from administrative sanctions. This would shift the cost of regulation of the markets from the state to market participants and users. Currently,

participants in the market pay only fees for administrative services and this revenue goes to the government, not the NSSMC.

46. **The IOSCO Principles are neutral on the question of whether regulators should be government funded or self funded.** The focus in the Principles is on the stability and continuity of funding sources (Principle 2); and whether funding is adequate to permit the regulator to fulfil its responsibilities, whether the regulator is able to affect the operational allocation of resources, and whether resource levels take into account the need to attract and retain experienced and skilled staff (Principle 3).

47. **Nonetheless, the trend internationally has over time been toward self funding of securities regulators, and many regulators (including European ones), operate on this basis.** In many jurisdictions, the revenue structure is similar to that proposed in the draft independence laws: a combination of fees for decisions involving the issue of licenses and permissions and registration; and an annual levy on regulated entities. Some jurisdictions also impose levies on market transactions, such as on new issues of securities or secondary market trading.

48. **The NSSMC has done preliminary modelling of the levels of administrative service charges and annual supervisory fees that could be collected under the self-funded framework proposed in the draft independence laws.** Conservative assumptions have been used to take into account the impact of the imposition of supervisory fees on markets and market participants. For example, it is assumed that fees on market transactions will result in a fall in trading volumes of 45 percent for both the regulated markets and OTC markets. It is also assumed that as a result of the imposition in 2015 of minimum capital requirements on market participants, a large number will exit the market and their trading activity will not be taken up by remaining or new market participants. For administrative service charges, the model assumes existing administrative fees will stay at the current level except for a rise in the maximum cap of the securities issuance fee. The model does not assume that revenue from financial penalties will go to the NSSMC.

49. **Using these assumptions, the modeling shows a total revenue of UAH 238 million.** This would be composed of revenue from administrative service charges of almost UAH 55 million and annual supervisory fees of UAH 183 million. That is around 5.7 times larger than the current NSSMC budget. Even if annual supervisory fees were to be set at a lower level than the NSSMC modeling assumes and the budget increase were smaller, the self funding model proposed in the draft independence laws would be a first step in overcoming many of the problems identified in the analysis of the current arrangements against IOSCO Principles. If self-funding were to be adopted, consideration would also need to be given on the need to build reserves over time and on the treatment of possible “extra” funding accumulated once sufficient reserves have been built.

50. **If the proposed method of funding the NSSMC were to be adopted, the ability of the NSSMC to utilize additional funding effectively would depend on removing existing constraints.** In particular, the current requirement that staff classification and remuneration be tied to civil service rules; the limited ability of the NSSMC to invest in appropriate technologies; and its limited ability to support its enforcement activities would need to be addressed.

Administrative sanctions

51. **The proposal included in both draft laws that the monetary penalties imposed by the NSSMC should comprise a revenue source raises difficult questions.** For a regulator to benefit directly and financially from the imposition of penalties that it decides upon creates a serious conflict of interest, and is likely to undermine confidence in the sanctioning system. More broadly, it creates potentially undesirable incentives for regulators to pursue cases on the basis of the likelihood of sanctions being paid, rather than on other possibly more important factors. If the proposed funding model is proceeded with, monetary penalties should be removed as a source of the NSSMC's revenue. In some jurisdictions, fines and administrative penalties (or some portion of them) are used to help fund stand-alone investor compensation schemes, or investor education initiatives undertaken by third parties. These functions are not performed by the regulator and therefore do not give rise to a conflict of interest problem.

Setting the remuneration of the Chairman and Commissioners

52. **The draft NSSMC independence law provides that the remuneration of the Chairman and Commissioners is determined by the NSSMC Chairman.** This would take place "within the limits of the outlays designated in the [NSSMC's] budget." If this means that, provided the Chairman's decision does not result in the NSSMC overspending its budget, he or she is free to determine his/her own remuneration and that of fellow Commissioners, it is undesirable from a governance perspective. There are two reasons:

- It is undesirable in principle for a public official such as the Chairman to determine his or her own remuneration.
- In a collegiate body where all members participate equally in decision making, it is undesirable that the remuneration of members of the body is set by one of their number.

53. **A better approach to the governance on the setting of remuneration would be for the determination to be made independently of those affected by the decision.** This could be done, for example, by the budget council making the decision as part of the annual budget process as proposed in the draft law on Independent Regulators or by reference to an objectively determined benchmark. In both cases, it is important that the remuneration

ensures the ability to attract Commission members with sufficient qualifications and professional standing. Publication of the Commission members' salaries may also be considered to enhance transparency.

APPENDIX I. TRANSLATED LAWS AVAILABLE TO THE MISSION

The mission had the unofficial translations of the following laws at its disposal during the mission:

- Law of Ukraine on State Regulation of Securities Market in Ukraine (as at May 20, 2015);
- Law of Ukraine on Securities and Stock Market (as at June 2, 2015);
- Law of Ukraine on the Depository System of Ukraine (as at July 6, 2012);
- Law of Ukraine on Information (as at July 3, 2012);
- Law of Ukraine on Public Information Access (as at January 13, 2011);
- Law of Ukraine on Financial Services and State Regulation of Financial Markets (as at December 15, 2005);
- Law of Ukraine on Banks and Banking Activity (as at June 24, 2015);
- Articles 1, 3, 8, 9, 10 and 21 of the Law of Ukraine on Principles of State Regulatory Policy in the Area of Business Activity (as at July 4, 2015);
- Law of Ukraine on Basic Principles of the State Supervision (Control) in the Sphere of Economic Activity (as at December 28, 2014); and
- Articles 4, 5, 13 and 19 of the Law of Ukraine on Licensing Types of Business Activities (as at March 2, 2015)

APPENDIX II. ANALYSIS OF THE NSSMC’S ABILITY TO COMPLY WITH THE IOSCO MMOU REQUIREMENTS

The following analyzes the NSSMC’s investigation, enforcement and international cooperation powers to identify gaps in its ability to comply with the IOSCO MMOU requirements and the corresponding IOSCO Principles 10–12 relating to enforcement and Principles 13–15 relating to cooperation. The analysis is based i) on a limited review of Ukrainian laws and regulations concerning the NSSMC’s ability to obtain information about securities related violations, and obtain and share information with foreign securities regulators under the MMOU; and ii) detailed discussions with key NSSMC staff and public and private NSSMC counterparties.

The analysis considers each question in the MMOU questionnaire, summarizes the gaps identified, and discusses how the recommended amendments to the laws and regulations would address the gaps in the NSSMC’s powers. The mission used the draft IOSCO Law³ prepared by the NSSMC staff as a basis of its work and proposed additional amendments where the original draft did not fully address the gaps identified. The analysis below also gives guidance to the NSSMC on the information to be included in its MMOU application to enhance the likelihood that IOSCO will be satisfied that it has sufficient information to assess the application.

Questions 1.(a) and (b)– Please identify and explain the general or specific provisions of your laws, rules and regulations that enable you, or a separate governmental body in your jurisdiction, to obtain: (a) contemporaneous records sufficient to reconstruct all securities and derivatives transactions, including records of all funds and assets transferred into and out of bank and brokerage accounts relating to those transactions; and (b) records for securities and derivatives transactions that identify:

1. ***The client;***
 - i. ***Name of the account holder; and***
 - ii. ***Person authorized to transact business;***
2. ***The amount purchased or sold;***
3. ***The time of the transaction;***
4. ***The price of the transaction; and***
5. ***The individual and the bank or broker and brokerage house that handled the transaction.***

³ Law of Ukraine on Amendments to Some Laws of Ukraine on International Cooperation of National Securities and Stock Market Commission

Current NSSMC authority

The NSSMC does not comply with Q.1(a) and (b) largely because it is unable to compel information from unregulated persons (both legal and natural persons). Nevertheless, the NSSMC's recordkeeping and reporting requirements for regulated persons appear to comply with the principal requirements in Q.1(a) and (b).

The NSSMC licenses securities market professional participants, including legal entities that are brokers, dealers, underwriters, asset managers, depository institutions, clearing institutions, and stock exchanges (Law on Securities and Stock Market, Article 21 Item 3, Law on State Regulation, Article 4 Items 1–10). The NSSMC also grants self-regulatory organization (SRO) status to certain associations of professional market participants (Law on Securities and Stock Market, Article 48 Item 2).

The NSSMC has the power to require the production of information from licensees, SROs and issuers through inspections (with certain important limitations) and mandatory requests (Law on State Regulation, Articles 8 and 9). However, under current law, the NSSMC has limited powers to compel information from unregulated legal and natural persons, and cannot obtain bank records. The lack of broad investigation powers could limit the ability of the NSSMC to obtain the information required under the MMOU and trace money flows as required under Q.1(a) and (b).

Restrictions on the NSSMC's inspection powers limit its ability to gather information responsive to Q.1(a) and (b). These restrictions are described in detail in Appendix III. Further, while Article 8 Item 21 of the Law on State Regulation authorizes the NSSMC, as part of an inspection, to "seize" (for a period of 3 days) documents containing information "confirming" securities violations, Article 4 Item 10 of the Law on State Supervision effectively annuls this power by prohibiting the seizure of documents. While it appears that the NSSMC will still have access to such documents during an inspection or upon request, not being able to remove original documents upon discovery could enable the regulated entity to destroy or tamper with evidence. This could undermine the NSSMC's ability to take effective enforcement action.

Bank secrecy laws prohibit the NSSMC from getting information from banks about bank accounts or the names of bank account holders (Law on Banks and Banking Activity, Articles 60–62). While the NSSMC has access to information held by regulated intermediaries about bank accounts that are the direct source of funds for securities accounts, it cannot trace money flows into and out of those bank accounts. Accordingly, the NSSMC would be unable to fully trace money used to fund securities accounts or money that is the proceeds of securities transactions. Thus, the NSSMC would not be able to comply with Q.1(a).

The NSSMC has broad authority to establish recordkeeping requirements for securities transactions (Law on State Regulation, Article 7 Item 12). Securities traders (defined as brokers, dealers, underwriters, securities managers—Law on Securities and Stock Market, Article 17) and

stock exchanges are required to make, and keep for 5 years, records of their securities market activities (Regulation No. 1449, Section 15 Item 6 (for brokers) and Regulation No. 1688, Section VIII Item 9 (for exchanges)). The NSSMC staff advised the mission that the required records permit the NSSMC to reconstruct individual securities transactions, as well as create an audit trail of exchange transactions in a particular security, including information about the securities purchased and sold, the quantity, price, time of transactions, and parties (brokers and clients) involved in the transaction. The mission understands that the name of the individual trader handling a transaction is not required to be kept. The mission has been unable to confirm whether all the data requirements listed in Q.1(a) and (b) are contained in current laws and regulations for all regulated entities due to lack of complete translations.

The NSSMC's reporting requirements for regulated entities enable it to have access to basic transaction information on a routine basis. The NSSMC can require securities market professional participants to regularly report securities transaction data referred to as "administrative data" (Law on State Regulation, Article 7 Item 10). Securities traders are required to report to the NSSMC securities transaction information for both on-exchange and off-exchange transactions. For off-exchange transactions the reporting deadline is within three business days of the transaction (Resolution No. 1283 of July 25, 2012). For on-exchange transactions, stock exchanges are required to report transaction data by 10:00 a.m. the next business day (Resolution No. 1284 of July 25, 2012). The NSSMC also receives administrative data on securities transactions from the central securities depository and depository and clearing institutions.

Exchanges report to the NSSMC administrative data about exchange transactions, which includes: information identifying the security, the regulated entities involved in the transaction and the names of clients, the name of the depository institution, the quantity, the price and the time (to the second) of the transaction (Regulation No. 1284, Separate Notice/Annex of September 25, 2012). For OTC transactions, administrative data is submitted to the NSSMC by securities traders and includes: the security, the date of the transaction, price, quantity of securities purchased or sold, and the securities traders and clients involved in the contract (Regulation No. 1283, Separate Notice/Annex of September 25, 2012). While client identification is considered "administrative" data required to be submitted to the NSSMC, such information is not included in the NSSMC's publicly available data.

The NSSMC can impose modest fines (UAH 17,000 for a first offense and up to UAH 85,000 for violations repeated within a year) against regulated entities and certain of their officials for: failing to submit administrative data, failing to produce information during an inspection or upon request, providing incomplete information, or providing false or misleading information (Law on State Regulation, Article 11 Item 7). According to the NSSMC staff, they routinely impose fines for failing to report administrative data and recordkeeping violations, but the fines have not been effective in deterring violations, because the NSSMC does not have the resources to enforce the fines. While the MMOU screening process does not prescribe a minimum amount for fines related

to recordkeeping and reporting, the Screening Group does expect that fines will be sufficiently robust to meaningfully deter violations.⁴

Powers required to be included in the IOSCO Law to comply with Q.1(a) and (b)

On the basis of the above, the following legislative changes have to be made to enable the NSSMC to comply with the MMOU requirements:

1. Empower the NSSMC to conduct investigations to require any legal or natural person, whether regulated or unregulated, to provide information and documents. Such investigation authority should be broad enough to authorize the NSSMC to conduct investigations of possible Ukrainian securities law violations, as well as conduct investigations on behalf of foreign securities authorities to assist them in matters that are within the scope of bilateral and multilateral information sharing arrangements.
2. Remove the bank secrecy restrictions to enable the NSSMC to have access to bank records, including securities transaction-related fund transfers into and out of bank accounts.

Powers recommended to be included in the IOSCO Law to enhance compliance with Q.1(a) and (b).

1. Remove the ban on “seizing” documents during NSSMC inspections from the Law on State Supervision.

Regulatory changes needed to comply with Q.1(a) and (b)

1. The NSSMC should amend the recordkeeping rules to require that transaction records include the name of the individual trader handling a securities transaction.

Recommendations on amending the MMOU application

Providing the following information in the MMOU application will better enable the Screening Group to evaluate the NSSMC’s compliance:

1. References to the specific recordkeeping requirements (including legal citations and related translations) imposed on regulated entities that cover each of the subsections of Q.1.
2. References to the NSSMC’s powers (including legal citations and related translations) to require regulated and unregulated legal and natural persons to produce information responsive to each of the subsections of Q.1.
3. Justification of the sufficiency of the level of fines that can be imposed in Ukraine.

⁴ See also IOSCO Principle 11, Key Question 2(b).

Question 1.(c) –Please identify and explain the general or specific provisions of your laws, rules and regulations that enable you, or a separate governmental body in your jurisdiction, to obtain information located in your jurisdiction identifying persons who beneficially own or control non-natural persons organized in your jurisdiction.

Current NSSMC authority

The NSSMC does not comply with Q.1(c) because it is unable to obtain information to identify the beneficial owners or controllers of certain legal entities organized in Ukraine.

Under Article 3 Item 4 of the Law on Securities and Stock Market, ownership of securities in bearer form is permitted in Ukraine for certain securities, but not shares of joint stock companies. Under Article 6 Item 3 of the Law on Securities and Stock Market, shares of joint stock companies must be registered and cannot be issued in bearer form. The NSSMC is unable to fully trace beneficial owners of bearer securities because it has limited authority to compel information from unregulated entities and individuals.

Licensed entities (except asset managers) are required to provide beneficial ownership information for persons with a 10 percent or more interest in the entity as a condition of licensing by the NSSMC (Law on Securities and Stock Market, Article 27-1 Part 2 Item 5). The NSSMC staff advised that asset managers only have to disclose two levels of ownership, but not their ultimate beneficial owners. In practice licensees can avoid having to provide beneficial ownership information to the NSSMC by limiting ownership interests to less than 10 percent. However, failure to provide complete ownership information to the NSSMC can be a basis for the NSSMC to revoke a license. Issuers also are required to provide detailed information about their ownership to the NSSMC (Law on Securities and Stock Market, Article 39 Item 2). In addition, anti-money laundering laws apply to bank and brokerage accounts and require NSSMC licensed market participants to follow “know your customer” requirements, which include identification of beneficial owners with interests of 25 percent or more (Anti-Money Laundering Law, Article 5 Part 2, Items 1, 4, Article 6). A new law (Law on Registration of Legal Entities 1701–7 October 14, 2014), not yet in effect, will require identification of beneficial owners of interests of 25 percent or more of all legal entities. The effective date has been postponed until later in 2015. According to staff, the NSSMC will not be able to compel information directly from individuals identified as beneficial owners because of the lack of full scope investigation powers.

Depository institutions maintain records of shareholdings and report administrative data to the NSSMC, including information about direct shareholders owning 10 percent or more of a joint stock company (Law on State Regulation, Article 7 Part 2 Item 10, Law on Depository System, Article 25 Part 1 Item 7). Until the new beneficial owner law is in effect, however, there are no requirements for companies to disclose substantial indirect ownership, unless they are banks.

Powers required to be included in the IOSCO Law to comply with Q.1(c)

To enable the NSSMC to comply with the MMOU requirements, it has to be empowered to conduct investigations to require any legal or natural person, whether regulated or unregulated, to provide information and documents, including beneficial ownership information.

Recommendations on amending the MMOU application

Providing the following information in the MMOU application will better enable the Screening Group to evaluate the NSSMC's compliance:

1. Details about the regulation of bearer securities in Ukraine and the ability of the NSSMC to trace the ownership of such securities. The IOSCO screening process will closely review this information.
2. Information about the new Ukrainian company registration law that will require all legal entities to identify any beneficial owner with a 25 percent or greater interest.

Question 2. –Please identify and explain the general or specific provisions of your laws, rules and regulations that enable you, or a separate governmental body in your jurisdiction, to take or compel a person's statement, or, where permissible, testimony under oath.

Current NSSMC authority

The NSSMC complies with this provision because it can take voluntary statements for its own use and on behalf of a foreign authority under current law. It can obtain written explanations from certain persons as part of its inspection power. Ukrainian securities laws do not explicitly empower the NSSMC to compel oral statements, but the NSSMC staff advised the mission that it requires certain persons related to licensed entities, issuers and SROs to provide oral statements through a variety of provisions granting inspection, licensing, sanctioning and anti-money laundering authority and other similar powers,. The NSSMC does not have the power to require such persons to provide statements under oath, but it can impose sanctions if information provided is false or misleading as discussed under Q.1(a) and (b) above. The NSSMC can also cooperate with criminal authorities that can share witness statements, provided that sharing such information would not adversely affect a criminal investigation (Law on State Regulation, Article 10).

Powers recommended to be included in the IOSCO Law to enhance compliance with Q.2

The IOSCO Law should include a provision that would grant the NSSMC broad enforcement powers to compel testimony and explanations from any legal or natural person, whether the person is regulated or not. Such testimony would not need to be provided under oath. However, it would be essential for the NSSMC to be able to impose fines if a compelled statement were determined to be false or misleading. The NSSMC is currently drafting such a law. The authority to compel testimony should be available for NSSMC investigations of domestic violations and on behalf of foreign authorities under a cooperation arrangement.

Question 3. - Please identify and explain the general or specific provisions of your laws, rules and regulations that enable you to provide to foreign authorities the information referred to in Q.1, Q.2 and Q.3 (information and documents held in the files of the applicant).

Current NSSMC authority

The NSSMC does not fully comply with the requirements of Q.3 because it has limited ability to obtain or share the types of information and records specified in Q.1(a)-(c). In addition, while it is explicitly authorized to cooperate with foreign authorities under reciprocal cooperation arrangements, it is not permitted to share information designated as secret (Law on State Regulation, Article 7 Item 16 and Article 8 Item 25). The NSSMC does not have access to banking information (Law on Banks and Banking Activity, Article 62) and cannot share “personal data” (Law on Information, Article 11).

Article 6 of the Ukrainian Law on Public Information Access establishes three categories of restricted access information: confidential information, secret information and proprietary information. Confidential information is information provided to an authority by a person (individual or legal entity) that the person designates as confidential, subject to certain limitations. The transfer of confidential information, including to a foreign authority, requires the consent of the person. Secret information includes state, professional and banking secrets, pre-trial information, and other secrets under law. Proprietary information includes information in the internal documents of a state authority that relates to the pre-decision making process. The definition of professional secrecy is in Article 1, Item 11 of the Law on Financial Services and State Regulation of Financial Markets. It is information used by state financial services regulators in the performance of their duties that may not be disclosed prior to the decision of such regulators.

Powers required to be included in the IOSCO Law to comply with Q.3

On the basis of the above, the following legislative changes have to be made to enable the NSSMC to comply with the MMOU requirements:

1. Grant the NSSMC access to information currently restricted by bank secrecy laws;
2. Permit the NSSMC to share personal data that is currently restricted under data protection laws;
3. Permit the NSSMC to share “professional secrecy information”; and
4. Empower the NSSMC to conduct investigations to require any legal or natural person, whether regulated or unregulated, to provide information and documents to determine compliance with Ukrainian securities laws or assist foreign regulators under cooperation arrangements.

Recommendations on amending the MMOU application

Providing the following information in the MMOU application will better enable the Screening Group to evaluate the NSSMC's compliance:

1. A clear description of the various restricted information categories that limit it from sharing the information with foreign authorities. The Screening Group will conduct a detailed analysis of these restrictions. Similarly, if the draft IOSCO Law will be enacted, the Screening Group will want to confirm that the new provisions effectively override the current restrictions.
2. A commitment to exercise any discretion that the NSSMC may have under the draft IOSCO Law to grant proper MMOU requests. For example, if the NSSMC can exercise its discretion to share information that is designated as "professional secrecy," it would be expected to do so in response to a proper MMOU request that might specify such information.

Question 4. –Please identify and explain the general or specific provisions of your laws, rules and regulations that enable you to provide information and documents to foreign authorities in response to requests concerning: a) insider dealing, market manipulation, misrepresentation of material information and other fraudulent or manipulative practices relating to securities and derivatives, including solicitation practices, handling of investor funds and customer orders.; b) the registration, issuance, offer, or sale of securities and derivatives and related reporting requirements; c) market intermediaries, including investment and trading advisers who are required to be licensed or registered, collective investment schemes, brokers, dealers, and transfer agents; and d) markets, exchanges, and clearing and settlement entities.

Current NSSMC authority

Based on review of the securities market laws and discussions with the NSSMC staff, it appears that the Ukrainian laws address the various topics in Q.4(a)-(d) and the NSSMC can compel the production of records made and kept by regulated entities. However, the NSSMC does not fully comply with this question for the reasons discussed under Q.3, including that the NSSMC is restricted in its ability to share non-public information with foreign authorities.

Ukrainian laws empower the NSSMC and criminal enforcement authorities (for violations listed under the Criminal Code) to take action for violations of these provisions and to impose sanctions, including fines, although criminal proceedings for securities violations are extremely rare. The NSSMC's authority to sanction regulated entities is comprehensive (Law on State Regulation, Article 8), but its authority over unregulated legal and natural persons is limited.

Powers required to be included in the IOSCO Law to comply with Q.4

The additional powers required under the MMOU are the same as in Q.3.

Recommendations on amending the MMOU application

Providing the following information in the MMOU application will better enable the Screening Group to evaluate the NSSMC's compliance:

- Clearer explanation of the scope of the NSSMC's authority by describing the scope of its regulatory authority in each subject area listed in Q.4.
- Detailed description of how the draft IOSCO Law, if enacted, would override the various restricted information laws that limit the NSSMC from sharing information with foreign authorities.

Question 5. – Please identify and explain the general or specific provisions of your laws, rules and regulations that enable you to provide assistance to a foreign authority, regardless of whether you have an independent interest in the matter.

Current NSSMC authority

The NSSMC does not comply with this provision because the NSSMC: is not authorized to make requests of unregulated entities for activities unrelated to violations of Ukrainian securities laws; and can require information from natural persons only when they are certain officials, including certificate holders, of legal entities engaged in activity within the NSSMC's jurisdiction.

The MMOU requires that a signatory be able to assist a foreign authority whether or not the subject matter of the request would constitute a violation of law in the signatory's jurisdiction or is a matter in which the signatory has an interest. The NSSMC's authority to cooperate with foreign authorities is limited to providing information on the operation of the Ukrainian securities market and regulated entities, provided that the information does not contain restricted information (Law on State Regulation, Article 8 Item 25 and Decree on National Stock Market Commission, Article 6 Item 47). Legal and natural persons located in Ukraine that are engaged in wrongdoing in foreign securities markets or possess information about such wrongdoing would be beyond the reach of the NSSMC's information gathering authority.

Broad investigation powers would enable the NSSMC to get information from any person in Ukraine, who might, for example, be defrauding foreign securities market investors, manipulating prices of securities on foreign markets or funneling the proceeds of insider trading on a foreign market into a bank account in Ukraine. Correspondingly, the NSSMC would be able to achieve the same benefits in its cross-border cases, including being able to trace foreign beneficial owners and money flows through bank accounts of entities engaged in wrongdoing in the Ukrainian securities markets. The NSSMC would be able to share such information received under the MMOU with criminal authorities in Ukraine in securities related matters, or with the consent of foreign MMOU signatories in other criminal cases.

Powers required to be included in the IOSCO Law to comply with Q.5

The additional powers required under the MMOU are the same as in Q.3.

Recommendations on amending the MMOU application

If the draft IOSCO Law will be enacted and grant the NSSMC broad investigation powers, the NSSMC should explain in its MMOU application how it will be able to assist a foreign authority, even if the information requested does not relate to trading on the Ukrainian securities market or potential violations of Ukrainian securities laws.

Question 6. – Please identify and explain the general or specific provisions of your laws, rules and regulations that require maintenance of the information and documents identified in Q.1(a)–(c) (including the period of time for which such information or documents are required to be maintained).

The analysis under Q.1(a)–(c) generally describes the recordkeeping and reporting requirements under Ukrainian securities laws, including the time period for maintenance of required records. The limitations of the NSSMC’s authority identified in those discussions and the legislative changes and amendments to the MMOU application are also relevant here.

Question 7. – Please identify and explain any domestic secrecy or blocking laws, rules and regulations that relate to the collection for, or provision to, foreign authorities of the information in Q.1, 2, and 3(e).

Ukrainian secrecy and blocking laws are extensive and effectively block the NSSMC from sharing non-public information. The analysis under Q.3 describes the particular secrecy and blocking provisions that limit the NSSMC’s information sharing authority. The draft IOSCO Law, as written, will remove those restrictions to enable the NSSMC to comply with the requirements of the MMOU: 1) access to bank records; 2) ability to share personal data; 3) ability to share other restricted information, including internal NSSMC information, and information submitted by persons to the NSSMC that such persons designate as confidential.

Powers required to be included in the IOSCO Law to comply with Q.7

On the basis of the above, a legislative change to override restrictions on sharing various types of restricted information, including bank records, personal data and professional secrecy information has to be made to enable the NSSMC to comply with the MMOU requirements.

Recommendations on amending the MMOU application

Same as for Q.3.

Question 8. – Please identify and explain any specific or general provisions of your laws, rules and regulations which restrict or limit the following uses by foreign authorities of information and documents identified in Q.1(a)–(c), Q.2, and Q.3(e) provided by you: (a) for the purpose of ensuring compliance with (including investigation of potential violations of) laws and regulations related to Q.4(a)–(d); and (b) for the purpose of conducting a civil or administrative

enforcement proceeding, assisting in a self-regulatory organization’s surveillance or enforcement activities or assisting in a criminal prosecution.

The NSSMC advised the mission that there are no Ukrainian legal provisions that would restrict the use of information shared with foreign regulators for the purposes specified in Q.8, which is based on Paragraph 10(a) of the MMOU. This is likely to be the case because, under current law, the NSSMC has limited ability to share non-public information. If the draft IOSCO Law were enacted, it would permit the NSSMC to share information that is considered “restricted” under Ukrainian laws, e.g., bank records and confidential information. To be compliant with the MMOU requirements, the draft law also would have to permit foreign authorities to use “restricted” information as provided in Q.8.

The analysis in Q.3 addresses the impact of the “restricted” information provisions on compliance with the MMOU requirements. The legislative changes and amendments to the MMOU application identified in Q.3 are also applicable to Q.8.

Question 9. – Please identify and explain any specific or general provisions of your laws, rules and regulations that provide for the confidentiality of: (a) requests for assistance made to you by foreign authorities, the contents of such requests, and any matters arising under such requests, including consultations between or among the authorities, and unsolicited assistance; and (b) documents and information received from foreign authorities.

Current NSSMC authority

The issue of confidential treatment is assessed by the Screening Group in several contexts. First, information provided to a signatory has to be kept confidential. Confidentiality must apply to the content of the request, all correspondence and consultations concerning the request, and information and documents shared in response to a request. Second, signatories must ensure that they will use information provided under the MMOU only for the specific purposes listed in Paragraph 10(a) of the MMOU (essentially, in securities related administrative, civil and criminal proceedings), unless they have the prior approval of the requested authority. Third, signatories must be able to impose effective sanctions against current and former employees who breach the confidentiality restrictions. And, finally, signatories must be able to resist demands of third parties, both public and private, to get access to confidential MMOU information. If a signatory receives a legally enforceable demand it must notify the foreign authority that provided the information and assert privileges to try to resist complying with the demand. Exceptions can be made for demands from courts and criminal authorities related to securities related violations.

The NSSMC does not comply with these confidentiality requirements. Based on review of Ukrainian information laws and discussions with the NSSMC staff, there do not appear to be any specific provisions that would protect the confidentiality of information obtained from a foreign authority in accordance with the MMOU. The presumption under Ukrainian information laws is that all information in the possession of authorities is public unless it falls into one of the

categories of restricted information (Law on Public Information Access, Article 1). Because the mission is not aware of any provision that explicitly deems information from foreign authorities to be restricted, there would be no guarantees that the NSSMC could protect confidential information received under the MMOU, as required by Q.9.

However, NSSMC employees are required by law to maintain the confidentiality of restricted information. Breaches can result in sanctions including dismissal. NSSMC staff advised the mission that some disclosures could result in criminal sanctions (Criminal Code, Article 182).

Powers required to be included in the IOSCO Law to comply with Q.9

On the basis of the above, the following legislative changes have to be made to enable the NSSMC to comply with the MMOU requirements:

1. Deem information (including requests for assistance) obtained from a foreign authority to be confidential information. Use of such information would have to be limited as provided in Paragraph 10(a) of the MMOU—any other use would require the prior approval of the foreign authority.
2. Protect MMOU information from demands of any third party—both public and private—without prior approval of the foreign authority. Exceptions can be made for demands of courts and criminal authorities related to investigations and prosecutions of securities-related violations.
3. Prohibit current and former NSSMC employees from disclosing information obtained under the MMOU—except as permitted in the MMOU.

Recommendations on amending the MMOU application

Providing the following information in the MMOU application will better enable the Screening Group to evaluate the NSSMC's compliance:

1. Detailed description of the new confidentiality provisions in the IOSCO Law, if it is enacted, including the sanctions that can be imposed on both current and former NSSMC Commission members and staff for breaches of confidentiality.
2. Confirmation that demands for MMOU information by third parties, including public bodies and private persons, can be resisted. The NSSMC should explain the procedure it will follow to deny such requests unless it gets prior approval from the foreign authority.

APPENDIX III. NSSMC OPERATIONAL INDEPENDENCE

NSSMC rulemaking

Article 8 paragraph 13 of the Law on State Regulation gives the NSSMC a general power to prepare and approve mandatory rules (normative acts) on matters within its jurisdiction.⁵ Specific legislation administered by the NSSMC, notably the Law on Securities and Stock Market, also contains many instances where it is envisaged that the regulatory framework will be completed by NSSMC rulemaking.⁶

NSSMC rules are adopted by a decision of the Commission. In practice, a proposed rule may be considered by a meeting of the Commission on at least two or three occasions. Proposed rules must be published for industry and public comment as required either by Article 9 of the Law on State Regulatory Policy or by Article 6 of the Law on State Regulation. There are five NSSMC Committees each chaired by a Commission member and comprised of “members” who are NSSMC staff and “participants” who are representatives of SROs, exchanges, the central securities depository, investment, legal and audit firms and independent experts. The relevant committee reviews proposed NSSMC rules and provides formal advice for consideration by the Commission.

NSSMC rulemaking must comply with rules of process established by the Law on State Regulatory Policy and, for rules relating to licensing, with the Law on Licensing; and with the requirement that, to be effective, rules must be registered by the Ministry of Justice (MoJ).

Law on State Regulatory Policy

The Law on State Regulatory Policy applies to government agencies, and sets standards that apply to the making of “regulatory acts.” Regulatory acts are defined in broad terms in Article 1 of the Law to include any measure containing requirements of general application that governs business or economic relations, or administrative relations between government regulatory bodies and business entities. Any agency proposing to make a regulatory act of this kind must:

- Carry out an analysis of the regulatory effect of the proposed act that covers specified matters, including the costs associated with compliance, and provide a reasoned justification for adoption of the measure (Article 8); and
- Publish the proposed act and seek public and industry comment on it (Article 9).

By Article 3 of the Law on State Regulatory Policy, these obligations do not apply to the NSSMC with the exception of rules (regulatory acts) made in respect of 18 matters referred to in the Article. Examples of NSSMC functions that are subject to these obligations include: granting,

⁵ See also paragraph 3 of Article 6 of Presidential Decree No 1063/2011 (as amended).

⁶ See also numerous examples in Presidential Decree No 1063/2011 (as amended).

suspending or cancelling of licenses for professional market participants; registration of rules relating to the operation of organized securities and derivatives markets; establishing procedures for a commercial bank obtaining a license for depository, clearing and settlement services; establishing requirements for entities acting as asset managers or collective investment institutions; and establishing requirements relating to advertisements in the securities market.

Compliance with obligations imposed on regulatory authorities by the Law on State Regulatory Policy is monitored by a specially authorized body, the SRS. Proposed regulatory acts must be submitted to the SRS for “coordination” (Article 21). If the body proposing the regulatory act is part of the central executive of government, it is prohibited from adopting the regulatory act if required procedures were not followed or the SRS makes a decision to refuse to coordinate the act (Article 25). The position for independent regulators, including the NSSMC, is somewhat different and the role played by the SRS is generally advisory only. However, as a matter of practice the MoJ requires the NSSMC to provide it with a copy of the SRS’s letter of advice as part of the material supplied when the NSSMC seeks to have a regulatory act registered, and therefore the MoJ is able to verify that the SRS is satisfied that the procedural requirements have been met.

The situation is different with respect to the NSSMC’s regulatory acts relating to licensing. Article 4 of the Law on Licensing makes the SRS responsible for approving draft normative and legal acts adopted by licensing authorities. This appears to mean that the NSSMC’s rulemaking on licensing issues is subject to the SRS’s approval, although because of the newness of the legislation this has not yet been tested in practice.

The SRS must make its coordination decision within one month of the regulatory authority submitting the draft regulatory act and supporting material (Article 21). If the form of a regulatory act changes during the process of its development, it must again be submitted to the SRS for coordination.

Once adopted, a regulatory act must be published in the *Ofitsiyny Visnyk* (Official Herald) and in the newspaper *Uriadovy Kurier* (Government Courier) (Article 12); and the adopting regulatory body must track and report publicly on its continuing regulatory effectiveness (Article 10).

The requirements of the law on State Regulatory Policy apply to the NBU in respect of regulatory decisions (such as those relating to the adoption of rules of conduct for banking transactions) specified in Article 3 of the Law on State Regulatory Policy. The Law on Licensing does not apply to the procedures for issuing, renewing or revoking licenses for banking activities carried out under the Law on Banks and Banking Activities (Article 2 of the Law on Licensing).

Ministry of Justice approval

Article 6 of the Law on State Regulation requires regulatory acts of the NSSMC to be registered by the MoJ.⁷ An act must be registered to be effective. This requirement reflects government policy established in the 1990s that all regulations adopted by a government authority should be registered by the MoJ.

A decree of the Minister of Justice (No 34/5, April 12, 2005 as amended) sets out the criteria used by the MoJ to assess proposed regulatory acts (Article 4.2). They include:

- Compliance with the Constitution and other current legislation of Ukraine;
- Whether the drafting meets norms for technical quality;
- The power of the regulator to adopt the regulatory act;
- The quality, relevance and timeliness of the act; and
- Possible positive and negative consequences of the act.

In addition, the MoJ review is to be conducted with the assistance of the department of anti-corruption policy if regulatory acts contain rules relating to: citizens' procedural rights and responsibilities; the provision of administrative services; competitive (tender) procedures; public procurement; granting discretionary powers to state authorities, local governments, or their officials; or the financing of political parties and election campaigns.

Proposed regulatory acts of the NSSMC need to go through this process if they are acts of general application. The MoJ must generally make a decision within 15 working days of receiving a proposed act, although the period can be extended for an additional 10 working days. In practice, the MoJ sometimes makes its decision in less than the statutory time period.

As a result of an amendment to the Law on the National Bank of Ukraine in 2014, regulatory acts of the NBU are no longer subject to a requirement that they be registered by the MoJ.

In practice, industry participants and associations often make comments on a proposed regulatory act directly to the MoJ, sometimes as an alternative to providing them to the NSSMC during the public consultation process. The MoJ may take comments of this kind into account when it reviews a proposed regulatory act.

If the form of a regulatory act changes after it has been submitted to the MoJ for review, it needs to be re-submitted for review and registration.

⁷ Note also Article 13 of Presidential Decree No 1063/2011 (as amended):

Decisions of the NSSMC that are legal regulatory acts are to be officially registered following legally established procedure.

Control over NSSMC's use of its inspection powers

The Law on State Regulation gives the NSSMC a broad power to conduct audits and inspections of regulated entities and issuers (Article 8.9; see also Article 6.51 of Presidential Decree No. 1063/2011 as amended). However, its ability to use this power is limited, in some circumstances, by legislation that applies to the NSSMC as well as other government regulatory authorities.

Law on State Supervision

The Law on State Supervision of 2007 (as later amended) contains detailed requirements relating to inspections carried out by regulatory authorities. These include:

- Requirements for regulators to prepare, approve and publish an annual or quarterly plan of scheduled inspection activities, including the identity of entities to be inspected (Article 5.1). Such plans are approved by the SRS in its role as the central executive body responsible for implementation of state policy in this area (Article 9-1);
- A prohibition on carrying out more than one scheduled inspection on a regulated entity each year (Article 5.1);
- A requirement for regulators to prepare and make public a report on their inspection activities each year (Article 5.3);
- Limits on the purposes for which unscheduled inspections can be undertaken (Article 6). Such inspections can only be undertaken:
 - At the request of the regulated entity;
 - To detect and confirm unreliable information provided in statutory reports submitted by the regulated entity;
 - To verify compliance by the regulated entity with remedial orders issued as a result of a scheduled inspection;
 - In response to a reasoned appeal (complaint) by a natural person that their legitimate rights have been violated by a regulated entity. An inspection on these grounds must be approved by the SRS;
 - Failure of the regulated entity to submit statutory reports within the prescribed period without valid reasons and written explanations; and
 - In relation to an accident, death or occupational disease that was associated with the activity of the regulated entity.
- A requirement that during an unscheduled inspection only the issue that was the reason for the inspection can be examined.

The SRS plays a supervisory role over authorities' compliance with the requirements of this legislation and can, for example, carry out an inspection of a regulatory agency to ensure it is complying with the requirements of the legislation (Article 9–1).

The Law on State Supervision applies to all NSSMC inspection activities, such as inspections of licensed market participants and issuers.

By virtue of Article 2 of the Law on State Supervision, the law does not apply to bank supervision and therefore does not apply to the NBU in its capacity as the bank supervisory authority.

Law on Licensing

The Law came into force in June 2015. It applies to government agencies that perform licensing functions, including independent regulators such as the NSSMC. However, in cases where specific provisions of the legislation administered by the NSSMC deal with the same topics as the Law on Licensing, those specific provisions apply and the operation of the corresponding provisions of the Law on Licensing is excluded (for example in relation to documents an applicant for a license must submit). Notwithstanding this general rule, Article 4 of the Law on State Regulation specifically applies Articles 13 and 19 of the Law on Licensing to the NSSMC. Provisions of the Law on Licensing that affect the operation of the licensing regime administered by the NSSMC include:

- Provisions giving the dedicated agency on licensing matters (in practice the SRS), responsibility, among other things, for supervising compliance by authorities with legislation governing licensing, and obtaining information from licensing authorities (Article 4);
- Provisions relating to the formation and operation of a licensing matters experts and appellate board (Article 9). The board is chaired by the Chairman of the SRS and at least half of the board must be non-government representatives. In practice the board is comprised of an equal number of representatives of licensing authorities and industry bodies. The board has responsibility for:
 - Reviewing appeals and complaints against licensing authorities; and
 - Reviewing applications from licensing authorities to carry out some types of unscheduled inspections.
- Provisions in Article 19 giving the SRS the power to carry out inspections of licensing authorities and to order authorities to take remedial action where violations are identified;
- Article 19.9 that sets out the seven grounds on which a licensing authority is permitted to carry out unscheduled inspections of licensees, and the purpose for which such inspections can take place. They are:
 1. Finding information in documents submitted by a licensee to the licensing authority which refers to non-compliance by the licensee with the requirements of licensing conditions—with the purpose of inspecting the compliance by the licensee with the requirements of the relevant license conditions.

2. Finding from governmental information sources information indicating that a licensee has violated requirements of licensing conditions or contradicts the information submitted by the licensee to the licensing authority pursuant to the requirements of the law—with the purpose of inspecting the compliance by the licensee with the requirements of the relevant license conditions or verifying the authenticity of relevant information.
 3. If a decree requiring elimination of violations of the legislation has been issued as a result of the licensing authority carrying out scheduled activities (inspections) with the purpose of inspecting the compliance with that decree.
 4. A substantiated complaint from an individual or a legal entity alleging that, as a result of violation by a licensee of the requirements of licensing conditions, the complainant has incurred financial losses or their legitimate rights or interests were infringed upon—with the purpose of inspecting the compliance by the licensee with the requirements of the relevant licensing conditions.
 5. Notices from officials of the supervisory authorities about violations by the licensee of the requirements of the licensing conditions, which violations were revealed in the course of exercising supervisory powers—with the purpose of inspecting the compliance by the licensee with the requirements of the relevant licensing conditions.
 6. A licensee's failure to submit, within the prescribed timeframe, reports that are required to be submitted by the licensing conditions without a good cause, which cause makes it impossible to submit such reports and occurs beyond the licensee's will and to notify the licensing authority thereof—with the purpose of inspecting the compliance by the licensee with the requirements of the licensing conditions in the respective part.
 7. The carrying out a threat to life or health of people, environment or public security that is directly related to the conduct by a licensee of a licensable type of business activity and documentarily proven by a body of state power authorized in the respective area—with the purpose of inspecting the compliance by the licensee with the requirements of the licensing conditions that are related to a respective occurrence.
- Article 19.10 provides that inspections on the grounds of items 2), 4) and 5) in Article 19.9 can be undertaken only with the approval of the SRS, which in turn must base its approval on a decision of the licensing matters experts and appellate board on an application from the licensing authority.

The Law on Licensing applies to the NSSMC's inspections of licensees in addition to the Law on State Supervision.

By virtue of Article 1.2, the Law on Licensing does not apply in relation to the licensing of banking activities carried out under the Law on Banks and Banking Activity.

Protections for Commission members and NSSMC staff

Dismissal of Commission members

Under Article 6 of the Law on State Regulation, the NSSMC Chairman and Commissioners are appointed to and dismissed from their positions by the President of Ukraine by issuing a decree to that effect. Article 6 further provides that the Chairman and Commissioners can be removed from office:

- By submitting a request to resign;
- If for health reasons they are unable to perform their duties;
- If they are deprived of Ukrainian citizenship;
- For gross violation of duties;
- Upon the coming into effect of a conviction for a criminal offence; and
- For other reasons stipulated by legislation.

Article 6 does not explicitly state that these are the only grounds on which the President can issue a decree dismissing the Chairman or a Commissioner, and it appears that the President may have discretion to remove the Chairman or a Commissioner for other reasons, or without cause. There are no provisions in the legislation, or that are implied by the general law, imposing procedural fairness obligations, such as the requirement to provide reasons for dismissal, or to give the affected party an opportunity to be heard before a final decision is made. A decision to dismiss can be appealed to a court.

Article 6 also stipulates that the coming to office of a newly elected President of Ukraine shall not constitute a reason for the dismissal of a Commissioner.

Legal protections for Commission members and NSSMC staff

There are no specific provisions in legislation that provide legal protection for the Chairman, Commissioners and staff of the NSSMC for the bona fide exercise of their governmental, regulatory and administrative powers and functions.

At Commission level, some protection is provided by the fact that many decisions are taken by the Commission as a collegial body, and it is therefore likely that a claim would be made against the NSSMC as a body rather than against individual Commission members. But this is not true of all decisions made by the Commission members. For example, sanction decisions are routinely taken by a single Commissioner or a panel of Commissioners to whom the Chairman has delegated decision making function. Some staff members have also been delegated the power to decide on sanctions in certain cases.

In practice, it appears most action commenced by aggrieved parties has been taken against the NSSMC as a collegiate body.

Article 15 of the Law on State Regulation provides that NSSMC officials bear responsibility for improperly performing or failing to perform their duties. It also provides that losses incurred by market participants as a result of improper actions by the NSSMC in the exercise of its regulatory and supervision powers are to be compensated in full by the State. Similar responsibility clauses are included in Article 9 of the Law on State Supervision.

APPENDIX IV. NSSMC FINANCIAL INDEPENDENCE

The following tables show the NSSMC's budget and approved staffing levels for 2011 to 2016, and the number of regulated activities and State revenue raised by its activities for 2013 to 2015:

Table 2. NSSMC Budget and Approved Staffing Levels

Year	Approved Staffing Levels			Budget (UAH million)
	Central Office	Regional Offices	Total	
2016	321	139	460	N/A
2015	272	245	517	42.2
2014	297	278	575	42.5
2013	280	295	575	48.5
2012	234	N/A	684	44.0
2011	234	N/A	684	40.3

Source: NSSMC

Table 3. NSSMC Activities

NSSMC Activity	2013		2014		2015
	Planned	Actual	Planned	Actual	Planned
Number of laws drafted	3	5	3	3	3
Number of rules prepared	92	143	75	125	43
Number of licensing actions ¹	930	860	320	436	260
Number of certificates for individuals ²	2,100	2,510	1,800	1,847	1,800
Number of scheduled inspections of professional stock market participants	192	432	385	229	190
Volume of registered securities (UAH million)	48,000	144,629	78,000	217,036	69,000

Source: NSSMC

1. Includes licenses issued, re-registered, copies issued, duplicates.

2. Certificates must be held by certain individuals to perform professional activity in the stock market.

Table 4. State Revenue Raised through NSSMC Activities

Revenue type	2013		2014		2015
	Planned	Actual	Planned	Actual	Planned
	UAH million				
Revenue to the budget from licensing actions	1.084	0.931	0.75	1.055	0.660
Revenue to the budget from issue of certificates	0.945	1.130	0.810	0.831	0.810
State duty paid for registration of securities issues	6.300	18.678	8.700	14.818	9.800
Total revenue/duty	8.329	20.739	10.260	16.704	11.270

Source: NSSMC

For the NSSMC, there are a number of limits on its ability to decide how to allocate resources within the allocated budget:

- The maximum number of staff is fixed by the President of Ukraine.

- Civil service rules determine aspects of the NSSMC structure (for example, a department must have at least four divisions and each division must have at least five staff specialists). A result of this is that a reallocation of resources within the approved budget requires a decision by the Chairman to make a formal change to the structure.
- Pay scales and remuneration levels are determined by the Law on Civil Service.

NSSMC staff resources

The NSSMC currently has approved staff levels of 460, 321 in the central office and 139 in regional offices.

Table 5. NSSMC Staff Establishment for 2015

Central Office	
Structural Division	Number of Approved Staff Positions
Chairman	1
Commissioners	6
Head of Staff	1
Assistants and advisers	3
Analysis, Strategy and Legislation Development Department	26
Depository, Clearing and Settlement Activities Regulation Department	22
Securities Traders and Stock Exchanges Activities Regulation Department	22
Collective Investment and Regulation of Institutional Investors Activities Department	22
Corporate Governance and Corporate Finance Department	24
Control and Legal Work Department	31
Legal Department	26
Department of Systematization and Analysis of Financial Reporting of Securities Market Participants and Issuers and Prudential Supervision	22
Financial and Economic Department	22
Informational Technologies Division	24
Law Enforcement Division	16
International Cooperation and Communications Division	14
Personnel and Prevention of Corruption Division	13
Internal Audit Division	11
Organization Provision Division	13
Major specialist on mobilization	1
Chief Inspector on Regime and Secret Work	1
Total positions attached to salary	321
Regional Offices	
Dniprovsky Eastern Regional Office	31
Eastern Regional Office	34
Pre Carpathian Regional Office	21
Southern Ukrainian Regional Office	29
Western Regional Office	30
Total positions attached to salary	145

Source: NSSMC

Staff salaries are determined in accordance with civil service rules and appear to be significantly below those available in the industry and peer regulators for similarly skilled employees. The NSSMC can pay bonuses to supplement base salary but to do this must achieve savings by employing fewer staff than the approved numbers. It has been using this method to increase staff remuneration.

In the view of senior management of the NSSMC, the civil service remuneration scales that apply to NSSMC staff make it difficult to attract staff with the knowledge and expertise the organization requires to become fully effective.

APPENDIX V. NSSMC ACCOUNTABILITY

Accountability to government

Under the legislation, the NSSMC is subordinate to the President of Ukraine, and reports to the Verkhovna Rada (Article 6 of the Law on State Regulation). The Law has no specific provisions mandating how the NSSMC's overall accountability to government is to be achieved.

In practice, the NSSMC uses a number of methods to account to government for the way it carries out its role:

- It produces an annual report which is submitted to the President, the Cabinet of Ministers of Ukraine, other ministries, authorities and state bodies for information. The annual report is also used as the basis of discussion with the special committee of the Verkhovna Rada responsible for financial policy and banking. The annual report is also published on the NSSMC's website.
- It provides non-public reports on its activities to the President, the Verkhovna Rada, and the Cabinet of Ministers. These reports typically contain information about the number of cases the NSSMC is working on and developments in the markets it regulates.

NSSMC's rulemaking is subject to the scrutiny of the SRS and MoJ and it is subject to the supervision of the SRS in the use of its inspection powers.

Transparency

The NSSMC is subject to a number of specific transparency obligations. For example:

- Article 8 of the Law on Administrative Services requires government authorities, including the NSSMC, to publish for each "administrative service" they provide details about how that service is provided. This includes information about the timing for making of decisions on that service, the list of documents an applicant must provide, whether the service is paid or free of charge, and what the fees are. The NSSMC fulfils this obligation by adopting and publishing a regulation on procedures for each of the services it provides, for example regulations on the issue of a license; the revocation of a license; the registration of securities; the issue of shares; and so on.
- NSSMC rulemaking is subject to obligations under the Law on State Regulatory Policy and the Law on State Regulation to make public and seek comment on proposed rules.
- Under the Law on State Supervision, the NSSMC is required to prepare and publish a list of its proposed scheduled inspections, including the timing of proposed inspections and the identity of entities to be inspected.

The NSSMC also has an obligation under Article 5.4 of Presidential Decree No 1063/2011 (as amended) to ensure the publication of information on its activities, to take steps to engage the

public in dialogue, and create conditions conducive to citizen participation in the process of shaping and implementing government policy.

In addition to complying with these formal obligations, the NSSMC publishes on its website an extensive range of material about the regulatory framework it administers (including all rules made by the NSSMC) and about its activities.

Use of resources

As an agency funded through the government budget process, the NSSMC's use of resources is subject to supervision by the MoF. It is subject to a government audit designed to analyze and verify that it has used its resources legitimately and efficiently; that its accounting is correct; and that its financial accounts are correct and reliable. A report is prepared of the findings of the audit.

Procedural protections

There is no general obligation in legislation requiring the NSSMC to give natural and legal persons adversely affected by NSSMC decisions a statement of reasons or the right to make representations before a final decision is made. However, the NSSMC has adopted procedures for each of the administrative services it provides that set out the steps to be taken in carrying out these functions. For decisions involving the revoking of an existing license or permission, the procedures require notification to the affected person advising of the proposed decision and the reasons for it, and an invitation to make representations before the final decision is taken. For some decisions, such as a decision to refuse to register a security, only notice of the grounds of refusal is required.

In addition, procedures for decisions to refuse to issue a license are covered by Article 13 of the Law on Licensing, which requires that an applicant whose application has been refused must be given a copy of the refusal decision, which must contain a statement of the reasons for the refusal. Sanction decisions are primarily taken by a Commissioner or a panel of Commissioners appointed by the Chairman. These decisions involve a hearing at which the affected party is given the opportunity to be heard.

Review of decisions

All NSSMC decisions can be appealed to an Administrative Court. In addition, other avenues for review of decisions are available. For example, decisions on licensing can be appealed to the licensing matters experts and appellate board established under the Law on Licensing; and sanction decisions of an individual Commissioner or Commission panel can be appealed to a full Commission meeting.

APPENDIX VI. DRAFT PROPOSALS FOR STRENGTHENING INDEPENDENCE

The independence of the NSSMC is addressed in two proposals for new legislation:

- A draft law on Independent Regulators of Ukraine; and
- A draft law on Amendments to Some Legal Acts Regarding Implementation of IOSCO Principles Concerning Functioning of Stock Market Regulator.

Draft law on Independent Regulators of Ukraine

The draft law on Independent Regulators of Ukraine is a proposal for a stand-alone law that would create a new type of independent regulator (national regulator). A number of areas of commercial activity, including telecommunications, television and radio broadcasting, and the securities and stock markets, would each have a national regulator of this kind.

Some key features of this draft law are:

- National regulators are subordinate to the President of Ukraine and accountable to the Verkhovna Rada, but are not part of the system of executive bodies (Article 3.1).
- There are specific guarantees of the independence of national regulators (Article 5).
- Decisions of national regulators are not subject to approval by any bodies of state authority and can be appealed only to a court (Article 5).
- National regulators must consult with other government bodies if required to do so by law, but objections by such bodies to the regulator's proposed decisions are not binding on the regulator (Article 6).
- Decisions of national regulators are not subject to state registration and the national regulator will maintain a public register of its regulatory acts (Article 15.4).
- Decisions of national regulators are not subject the procedural rules set out in the Law on State Regulatory Policy (Article 15.5).
- The members of a national regulator are appointed by the President following a competitive tender process and the President determines the head from among the appointed members (Article 6.2).⁸
- The appointment of the head or member of a national regulator can only be terminated before the expiry of their term of office for reasons set out in Article 8.6 (for example, if convicted of a criminal offence, or ceasing to be a Ukrainian citizen).

⁸ Note that there are two Articles 6 in the version of the draft made available to the mission.

- Officials are liable for violations of legislation and for improper performance or non-performance of duties, but if an official's actions are appealed to a court, the national regulator is to be the respondent (Article 14).
- Regulators are to be funded by monies from a special fund of the state budget (Article 10.1).
- Regulator's income can be derived from administrative service charges, regulatory fees paid by regulated entities, administrative sanctions, or other sources established by law (Article 10.2).
- Each regulator has an ad hoc budget council consisting of two representatives from each of the President of Ukraine, the Verkhovna Rada, and the Cabinet of Ministers and this council approves the regulator's budget (Article 10.5).
- In preparing the state budget, allocations to national regulators must not be less than each regulator's anticipated receipts from fees (Article 10.6).
- National regulators must have annual audits, conducted by a reputable and independent company appointed by national regulators in concurrence with their budget councils (Article 10.9).
- Decisions about the number of staff and staffing structure are made by the regulator (Article 7, Article 8.3).
- The head, members and staff of the regulator have the status of civil servants but their remuneration is determined in the regulator's budget (Article 6.9).
- The head of the regulator has power to hire and dismiss employees (Article 8.3).

Section VI of the draft law contains a detailed list of the administrative fees and annual regulatory contributions that would apply to administrative services provided by and entities regulated by the NSSMC.

Mechanisms to guarantee independence are set out in Article 5 of the draft law, which provides:

1. The independence of national regulators shall be guaranteed by:
 - a. The fact that the regulators' interactions with bodies of state authority, other bodies of state, and local government bodies are to be governed solely by the law;
 - b. An exhaustive list of grounds for suspending the powers of the head or members of a national regulator, as specified herein;
 - c. Competitive selection of national regulators' employees, their special legal and social protection, and adequate compensation packages defined by the heads of the national regulators;
 - d. A legally established procedure for funding and material/technical support of national regulators; and
 - e. Other means identified herein.

Section VI of the draft law also proposes a number of consequential changes to other legislation. In particular, it provides that the Law on State Regulatory Policy, the Law on State Supervision and the Law on Licensing do not apply to the activities of independent national regulators covered by the law.

Draft NSSMC Independence Law

The draft NSSMC Independence Law seeks to achieve the same objectives as the proposed law on Independent Regulators but in a way that is specific to the NSSMC. It does so by proposing amendments to the Law on State Regulation, and a variety of other laws. It draws heavily on the draft Law on Independent Regulators and inserts provisions of that draft law into the Law on State Regulation and in other laws. Examples of changes proposed to the Law on State Regulation include:

- The guarantees of independence quoted above are inserted as new Article 5-1 of the Law on State Regulation.
- Decisions of the NSSMC are not subject to approval by any bodies of state authority (new Article 5-1).
- Decisions of the NSSMC are not subject to state registration and the NSSMC is to maintain a public register of regulatory acts and arrange official publication (new Article 6-1).
- Article 18 of the existing Law on State Regulation is amended to reflect the funding arrangements in the draft Law on Independent Regulators, including a list of the administrative fees and annual regulatory contributions that would apply to administrative services provided by and entities regulated by the NSSMC.
- A new Article 19 is added providing for an NSSMC budget council responsible for approving the NSSMC's budget.
- A new Article 20 is added requiring independent audit of the NSSMC each year and providing the audit reports to the NSSMC's budget council and the Verkhovna Rada each year together with a copy of the NSSMC's annual report.
- A new Article 21 provides that the remuneration of the NSSMC's Chairman, Commissioners and employees is to be set by the Chairman within the limits of the outlays designated in the NSSMC's budget estimate.
- A new Article 22 makes officials liable for violations of legislation and for improper performance or non-performance of duties, but if an NSSMC official's actions are appealed to a court, the NSSMC is to be the respondent.

Like the draft Law on Independent Regulators, the draft NSSMC Independence Law excludes the operation of the Law on State Regulatory Policy, the Law on State Supervision and the Law on

Licensing in matters relating to the decisions and activities of the NSSMC. It also amends the Law on Civil Service to permit the NSSMC to establish procedures for appointing and dismissing civil servants, and for their compensation to be determined under the Law on State Regulation, rather than under civil service rules.

The draft NSSMC Independence Law differs from the draft Law on Independent Regulators in two main areas:

- It retains the present process for the appointment of the Chairman and Commissioners in the Law on State Regulation, and does not contain a requirement for a competitive tender process after which the President determines the head from among the appointed members.
- The provisions on the method of setting Commission member and staff remuneration in proposed new Article 21 of the NSSMC Independence Law differ from the provisions in the draft Law on Independent Regulators (which requires that remuneration levels are to be set as part of the budget process and therefore require the approval of the ad hoc budget council).