THE FUNDAMENTAL CONTRADICTION OF AN EMERGING SYSTEM OF CORPORATE GOVERNANCE IN UKRAINE

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Abstract: *In the article, the key features of development of national corporate case frame in Ukraine are considered. It is retained that the legislation of Ukraine from point of presence of the formal generally accepted measures on defiance of rights for a shareholder can be appraised as highly developed enough. Thus, the personal touch of redistribution of equity in the Ukrainian corporate sector is prevailing of property of insiders. The folded situation allows talking about steady and fundamental contradiction of the formed national system of corporate management.*

Keywords: corporate government legislation; financial system of Ukraine; insider's ownership; ownership's structure; shareholders' rights.
JEL Classification: G34; G28.

INTRODUCTION

Among the key features of the national model of the corporate governance development in Ukraine it should be identified: a permanent process of property redistribution in corporations, insiders specific motivations associated with the control of financial flows and the "output" of corporate assets, the weak role of the traditional "external" corporate governance mechanisms, inefficient or politicized State enforcement.

In Ukraine, as in continental Europe, is used the generally accepted division of the rights into public (the organization of the state and its relations with individuals) and private (the regulation and protection of the interests of individuals). Private law, in its turn, is divided into two main parts: civil (general rules governing the relations of individuals) and trade (the ratio of individuals with regard to the recovery of profits). "Trade Association" is regarded as a branch of commercial law, and the "joint stock companies", in its turn, as part of the "trade associations" ("economic partnerships and companies").

Another formal difference is the specification (or lack thereof) of company law norms in special laws. The special laws related to the joint-stock companies (JSC) (other than codes) are currently available in most countries, such as France (the law of trade associations in 1966), Germany (the law

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on joint stock companies in 1965). Almost in all countries with transitive economy JSC are already the subject of a particular type of legal regulation.

Hungary was the first that went along with the French way (Company Law 1988, amended 1991). Similar legislation (where JSC is regulated on a par with other companies or partnerships) has been adopted in Albania, Bulgaria, Kazakhstan, Mongolia, Russia and Ukraine.

The paper (Кубліков, 2008) shows that none of the existing models of corporate governance is perfect. Similarly, no other country has reached a 100 percent level of most conciliatory implementation of Principles of Corporate Governance in terms of international practice the OECD (OECD, 1999). The most developed countries walked closer to it then other, primarily belonging to the Anglo-American legal system. This is followed by the country's civil law.

The analysis of the Ukrainian legislation in terms of availability of formal common measures for the protection of shareholder rights shows that it can be rated as sufficiently highly developed. Of course, in the domestic legislation on joint stock companies there is a significant adoption of the Anglo-American protection mechanisms of shareholder rights. However, the general traditions of European civil law remain dominant, which determines the proximity of Ukrainian corporate law to the standards of EU legislation on formal criteria set forth in the Regulations and Directives of the European Council (Database of EU legislation on http://www.europa.eu/) (Table 1).

Table 1 - The basic norms of company law presence in Ukraine and the EU

Norms	**Ukraine**	**EU**
Tight and detailed procedure for creating a joint-stock company	Yes	Yes
Tough and detailed procedure for maintaining the size of the authorized capital stock	Yes	Yes
Regulation of creation of branches, representative offices and other separate units	Yes	Yes (in reporting)
The main issues of reorganization	Yes	Yes
The possibility of company with one participant	Yes	Yes (for closed / private companies)
Pre-emptive right to purchase the shares by shareholders	Yes	Yes
Stringent requirements for reporting and auditing	Yes	Yes
Absorption and protection of minority rights	Yes (details required)	The general principles under discussion
Bankruptcy	Yes (a modification of legislation needed)	Yes (minimum)
Insider transactions	Yes (minimum)	Yes (outright ban)
Liquidation	Yes	No

On the other hand, the analysis of the mechanism of the property structure formation and its redistribution in Ukrainian specifics suggests that this mechanism is primarily performs the functions

associated with the struggle for control of the company. Typical feature of the share capital redistribution in Ukrainian corporate sector is the dominance of insider ownership (Table 2).

The analysis of Table 2 suggests that from 2003 to 2009 there was a decrease in the company's capital share for shareholders who own less than 15% and an increase the share of owners who own more than 80% of the share capital. Thus, the structure of share ownership, which has developed in the Ukrainian economy, can be characterized as highly concentrated.

Table 2 - Changes in the proportion of owners in joint stock companies in Ukraine (as for January 1)

Year	Shareholders portion in the company who own more than 5% of share capital (%)								
	<15	15-20	>20-30	>30-40	>40-50	>50-60	>60-70	>70-80	>80-100
2003	27,6	5,2	6,0	8,3	8,7	12,1	10,8	9,7	11,6
2004	21,2	4,9	5,7	7,8	9,5	11,4	11,0	12,2	16,3
2005	21,0	3,9	5,4	6,7	8,0	10,1	12,1	14,5	18,3
2006	10,8	3,2	4,8	6,2	7,4	9,9	14,5	17,5	23,9
2007	4,8	3,8	11,0	6,1	9,5	10,0	11,1	12,1	31,6
2008	4,5	3,7	10,4	6,4	9,2	9,4	11,5	12,6	32,3
2009	4,5	3,7	9,9	6,0	8,7	9,6	12,5	11,6	33,6

Based on the above, as well as taking into account a number of empirical data we can talk about sustainable and fundamental contradiction emerging national system of corporate governance. Its essence lies in the fact that in the current system two fundamentally different approaches coexisting:

1. Concentration of share capital, which implies a minimum of legal protection of shareholders;
2. Anglo-Saxon legal tradition, which is characterized by maximization of minority shareholders legal protection.

This combination of approaches has led to the unique situation of reciprocal neutralization:

- On the one hand, the concentration of the share capital and the gradual reduction in the proportion of minority shareholders in principle reduces the importance of a broad legal instruments of minority shareholders protection in terms of the corporate sector in general, and the tools themselves to protect small shareholders are transformed into instruments of corporate blackmailing;
- On the other hand, the establishment of a comprehensive system of legal protection of shareholders, in turn, hampers the further process of concentration of share capital (as a factor of the inverse effect of the right of economic processes).

In this case, it should be noted that the protection of their interests through further concentration – it is the prerogative of large shareholders, primarily for ordered enforcement.

In this regard, an important issue is the existence of economic and institutional prerequisites for attraction to a particular classical model of corporate governance.

The model with the domination of minority shareholders' interests is not impossible in Ukraine, as it quite complicated in practice. The implementation of such a model would require a serious economic breaking of the existing relationship. Sharp focus in favor of the interests of minority shareholders violates the balance of interests of all the other subjects of corporate relations. The role of minority shareholders, however, is crucial to ensure the corporate transparency.

However, the lack of legal protection of minority shareholders and the relatively low level of stock market development related in both direct and inverse feedbacks. The lack of liquidity of the majority of the shares of domestic corporations on the weak development of the stock market makes their owners substantially even less protected. The presence of such a situation, in its turn, promotes the concentration of corporate ownership and reduction of stock market mobility.

In fact, disparate components of all the traditional models are now formally presented in Ukraine:

- relatively dispersed ownership with illiquid stock market and weak institutional investors;
- steady trend towards concentration of ownership and control;
- elements of cross-holdings and the formation of complex corporate structures of different types.

Such a blurring of the Ukrainian model creates evident difficulties for decision-making in the field of economic policy and the law.

A type of financial system that dominates in the country provides a particular importance on the formation of a national corporate governance model. The main feature, constituting a particular type of financial system is the role of commercial banks in providing activity and financing of industrial corporations. Depending on the value of banks in long-term financing of economic growth can be spoken about either a banking-oriented, or a market-oriented financial system.

Nowadays, there is a situation where none of the above types of financial systems do not only prevaile, but, more importantly, functioning in isolation from industrial corporations in Ukraine. The banking model of economic growth proved to be ineffective in the late 90s of the last century, and in 2008 - 2009. The stock market as a potential mechanism for financial resources mobilization throughout the time of its development was unable to cope with the tasks.

As a result, the only reliable option for which you can try to determine the attraction to a particular type of financial system is the structure and level of concentration of the share capital, which determines the form of the right of control.

Assuming that the result of many stages of redistribution of property in Ukraine will be a highly concentrated ownership, legal disclosure requirements in existing and even more tightening form does not have a real foundation. Moreover, they are also extremely poorly executed now.

The problem of selective law enforcement by order of interested private organizations – a key drawback of modern domestic model, that is systemic and cannot be rectified by editing regulations and codes of corporate governance.

The Ukrainian model of corporate governance is formed in two parallel trends:

- Managers are gradually becoming the controlling shareholders of the corporation, i.e. key feature is the "capitalism of Governors", which became the owners or "insider capitalism";
- external shareholders, as the consolidate control themselves, begin to function as managers or transfer those functions to an authorized representative of a group of shareholders associated with them not by a formal contract, but by a whole set of economic and non-economic interests.

Obviously, this is a forced situation, which is connected with a number of circumstances.

Firstly, the continued merging of functions due to the fact that under the current external environment ("gray" schemes of corporate finance "tax optimization", control of financial flows, asset stripping, etc.), and the continued trend of struggle for control, the formal owner must remove the risk of loss at the same time both the property title and control of financial flows.

Second, the system is organized on the principle of two, three, four partners that share both property (control), and business. There are at least two problems in such public corporations.

The first problem is concerns the short-term investments. It is necessary to take into account that many domestic corporations are guided by the foreign profit centers, and their ongoing activities make the most of the internal sources, including the pseudo-foreign loans, etc. It should be noted that in the period 2003-2007 reinvestment process is enhanced, by Ukrainian owners, and namely in the practice of various forms of pseudo-foreign investment. Consequently, the requirement of transparency insurance of ownership structure and finance, i.e. every tightening of enforcement, could indicate the break of the re-investment process from abroad.

The second problem is the accomplishment of a long-term investment strategy in such corporations. The system of partnership involves focus on current short-term profits, and thus there are problems regarding the negotiation and implementation of a long-term investment strategy. It is obvious that such an organization involves a strict system to minimize the losses associated with the opportunistic behavior of managers.

The ability to use the Ukrainian banking system as a driver of corporate governance and financing has been adopted by the beginning of this century and brought negative results. At present, banks are still not able to carry out long-term external financing of the real sector of the economy due to the insufficient domestic capital and short-term liabilities.

Some countries, with a transitive economy, were able to use foreign direct investment to stimulate corporate investment and restructuring.

It should be noted that the corporate governance model, based on a broad presence of foreign strategic investors in key sectors of the economy, requires a stable and carefully cultivated political climate (in this case, the stability is crucial, as the example of China). Although Ukraine's foreign direct investment should be a priority in some industries, a significant influx in the medium term is unlikely to happen.

CONCLUSIONS

As a result one can identify the following fundamental processes: for the prospects of forming a national model of corporate governance

- latency of the separation of ownership and control process will remain in the medium term;
- the financial system of Ukraine in its present precarious state does not evaluate the attraction of national systems of corporate governance in any classical models;
- concentration of share capital is an obvious process by which takes place not only the consolidation of control, but also the realization of economic methods of "self-sufficient" model of corporate governance;
- legal innovations in the field of corporate law itself (shareholder rights) are largely reached its peak in terms of current economic conditions;
- methods of protection of shareholders' rights cannot be further developed without adequate general measures in the area of enforcement.

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