



## LEGISLATION MONITORING: MANDATORY DIVIDENDS

December 8, 2010

### Summary

**On November 30, 2010**, the Constitutional Court of Ukraine ruled once again that it was unconstitutional to use amendments to the Budget Law to nullify, cancel, or amend other laws. The issue in this case was a provision mandating minimum dividend payments by joint-stock companies to shareholders. However, the Rada passed a separate law mandating these provisions, so a minimum dividend payment is in effect at least through 2010.

### Overview

On **November 30, 2010**, the Constitutional Court of Ukraine adopted the Decision #22-rp/2010 in response to constitutional petition of 54 People's Deputies of Ukraine concerning, in particular, compliance with the Constitution of Ukraine (constitutionality) of provisions of items 10-11 of Section VII "Final Provisions" of the Law of Ukraine "On the State Budget of Ukraine for 2010" of 27 April 2010 (hereinafter referred to as **Budget Law**). The mentioned provisions **mandated that joint stock companies subject to either law were required to pay dividends in an amount not less than 30% of their net profit in a reporting year and/or retained earnings within six months of the end of the reporting year**. According to the Court's decision, these provisions were recognized as non-compliant with the Constitution (unconstitutional) due to procedural violations under which they had been adopted.

In its Decision the Constitutional Court concluded, similarly with its previous Decisions (#6-rp/2007 of July 9, 2007 and #10-rp/2008 of May 22, 2008), that the Budget Law has a special subject matter – only establishment of the state's incomes and expenditures on general social needs. Thus, the Budget Law cannot amend other laws, terminate their implementation or cancel them since these actions lead to inconsistencies in legislation. Separate laws would have to be adopted to accomplish these objectives. Thus, since November 30, 2010 these amendments would become ineffective.

However, on December 3, 2010 the Verkhovna Rada of Ukraine passed the Law "On Certain Issues of Budget Process Arrangement in 2010" which mandated the same provisions of the Joint Stock Company Law and Business Partnership Law that were previously included as amendments to the Budget Law. This Law is to be applied effective November 30, 2010 and is valid till January 1, 2011.

Thus, although Constitutional Court ruled that provisions of Budget Law mandating dividends were unconstitutional due to certain procedural violations, Verkhovna Rada of Ukraine re-enacted these provisions by adopting a separate law. Provisions requiring a joint-stock company to pay 30% dividends are still valid. The only positive feature is that it has been clearly established that mandatory dividends provisions shall remain effective only until January 1, 2011. However, one should keep in mind that the Verkhovna Rada may adopt similar changes for another year after January 1, 2011.

### History and Process

**April 27, 2010.** The Law of Ukraine "On State Budget of Ukraine for 2010" was approved by the Rada. It amended both the Joint Stock Company Law and Business Partnership Law, mandating that joint stock companies subject to either law are required to pay dividends in an amount not less than 30% of their net profit in a reporting year and/or retained earnings within six months of the end of the reporting year. The amendments became effective as of April 30, 2010, the date of publication of the Budget Law.

In addition, on October 1, 2009 the Verkhovna Rada registered Draft Law #5183 submitted by A. Pavlovskiy which proposed substantially the same amendments to the Joint Stock Company Law. This Draft Law was

included into the Verkhovna Rada agenda to be additionally worked out for consideration on its current seventh session of the sixth convocation. The amendments limited the powers of the General Meeting of Shareholders by providing that decisions of this body can only increase the amount of dividends more than the mandatory minimum amount.

Inappropriate government interference in the operations of legal business entities violates core principles of a free market economy and the basic rights of shareholders of a joint stock company. Arguments that the amendments protect “minority” shareholder rights are not supportable. The argument that the amendments curb “asset stripping” by affiliates of legal entities does not justify eliminating basic rights of shareholders. Improved enforcement and an honest and transparent judicial process with effective sanctions is the international standard for addressing such abuses.

**May 14, 2010.** People’s Deputy Yuriy Voropaiev submitted to the Verkhovna Rada Draft Law #6396 amending the Budget Law to cancel the amendments on dividends in both the Joint Stock Company Law and the Business Partnership Law. The accompanying explanatory note stated that the amendments violate Article 22 of the Constitution of Ukraine, which provides, in part, that adoption of new laws and/or the amending of existing laws cannot restrict existing rights and freedoms. The explanatory note further stated that the Constitutional Court of Ukraine, in a decision dated July 9, 2007 (#6-rp/2007), said that the Verkhovna Rada, when adopting the Budget Law, is not allowed to provide, in its text, for amendments to other laws, terminate other laws or somehow modify provisions of other laws in the sphere of social relations. The Draft Law #6396 was included into the Verkhovna Rada agenda to be additionally worked out for consideration on its current seventh session of the sixth convocation.