Kyiv National University of Trade and Economics
Banking department

FINAL QUALIFYING PAPER

on the topic:

The mechanism of functioning of private equity funds

Student of the 2nd year, group 5am,
specialty 072 «Finance, banking and insurance»
specialization «Financial intermediation»

____
(student's signature)

Golournyi Dmytro

Scientific adviser
PhD in Economics,
Associate Professor

____
(signature of a scientific adviser)

Gordiienko T.M.

Manager of the educational program
PhD in Economics
Associate Professor

____
(signature of the (Manager of the educational program)

Gordiienko T.M.

Kyiv, 2018

KNUTE КНТЕУ

CONTENTS

LIST OF ABBREVIATIONS.. 3

INTRODUCTION... 4

PART 1. FUNDAMENTALS OF PRIVATE EQUITY FUNDS FUNCTIONING AND THEIR PLACE IN BUSINESS LIFE CYCLE 7

1.1. Nature of private equity and history of its evolution 7

1.2. Role of private equity in the capital market and it's place in business life cycle 15

1.3. European and Anglo-Saxon formats of private equity 23

PART 2. DIAGNOSTICS OF PRIVATE EQUITY FUNDS PERFORMANCE AND REAL-LIFE PRACTICES OF THEIR REGULATION IN FOREIGN COUNTRIES 31

2.1. Analysis of best practices in private equity proceedings regulation 31

2.2. European and Anglo-Saxon private equity market assessment.................... 41

2.3. Analysis of private equity performance in Ukraine..................................... 44

PART 3. FORMATION OF PREREQUISITES FOR THE DESIGN AND IMPLEMENTATION OF DOMESTIC PRIVATE EQUITY MODEL IN UKRAINE 53

3.1. Justification of the necessity of development of private equity funds in Ukraine 53

3.2. Design of the private equity model applicable for Ukraine......................... 60

3.3. Roadmap for implementing proposed model of private equity in Ukraine .. 68

CONCLUSIONS AND PROPOSALS.. 73

REFERENCES 76

ATTACMENTS.. 77

LIST OF ABBREVIATIONS

AIF	Alternative investment fund
AIFM	Alternative investment fund manager
AIFMD	Alternative Investment Fund Managers Directive
AMC	Asset management company
BO	Buyout
CEE	Central and Eastern Europe
CII	Collective investment institution
ESG	Environmental, Social and Governance
ESMA	European Securities and Market Authority
EuVECA	European Venture Capital Fund Regulation
UVCA	Ukrainian Venture Capital and Private Equity Association
UAIB	Ukrainian Association of Investment Business
FCA	Financial Conduct Authority
GP	General Partner
LLP	Limited Liability Partnership
LP	Limited Partner
PE	Private equity
R&D	Research and development
SBA	Small Business Administration
SBIC	Small business investment company
SMEs	Small and medium-sized enterprise
VC	Venture Capital

INTRODUCTION

Despite of tremendous growth, particularly over the past decade, private equity as a form of financial intermediation has received little attention in the financial press or the academic literature. In recent years alternative asset classes such as private equity have become increasingly important sources of investment capital in the global financial system. Private equity activity, in particular, has noticeably accelerated: PE firms have expanded significantly in terms of the size and geographical reach of their funds. Global expansion has not only increased the number of funds expanding into different geographic areas but also the number of firms looking to complete deals outside their country of domicile. But on the way to globalization, there are some obstacles such as incompliance of legal framework of different markets organization and inability to perform on the market without accordance to general rules.

The private equity market is important for the functioning and evolution of enterprises, especially in the early phase of their development. Funding of this kind can finance risky investments in return for a higher expected rate of return on capital. Access to financial resources and the conditions under which entrepreneurs can use them can determine the introduction of new technology, new products and services, expand distribute on channels, implement changes that may lead to the growth in competitiveness and above all, innovation, thus the growth of the company.

The relevance of the chosen topic is validated by the necessity of organizing and bringing domestic approach to private equity proceedings regulation in accordance with global best practices in this sphere, due to presence of foreign private equity funds in Ukraine and willing of domestic funds to have an access to world-wide market, against a background of absence of national legislation in this sphere. Learning and adapting foreign practices can be useful for the design of our own country specific regulation.

Level of topic development. Generally, this problem reached some level of developed in the works of foreign authors such as George W. Fenn [26], Stefano

Caselli [15], Steven Neil Kaplan [37], but absolutely ignored in Ukrainian literature. This study examines the economic foundations of the private equity market, analyzes the market's development and current role in corporate finance, investigates different approaches to market governing, and, based on obtained results, offers brand-new approach to local practice in market organization.

The purpose of the work is to design and offer Ukrainian own domestic approach to PE based on analysis of world-wide best practices of market organization in this sphere.

The main tasks, which had to be resolved in the process of research accomplishment, were:

- to determine the nature of private equity and investigate the history of its evolution;
- to point the place of private equity on a capital market;
- to distinguish different formats of PE which are widely used world-wide and to assess main global markets;
- to design domestic format of private equity organization;
- to offer the roadmap for this format implementation.

The object of research is private equity investment process, and it`s specifics in Europe and USA, as a main markets for such activity.

The subject of research is Ukrainian own format of private equity governing, and the peculiar properties of its creation in concordance with countries' specifications.

Methodology, which was widely used in the process of this work execution consist of such research techniques as: observation; assessment; modeling and forecasting. Combination of mentioned methods allowed us to comprehensively consider all topics' features and create sustainable model of the investigated phenomenon.

The scientific novelty of the research consists in first-time creation of separate approach to private equity investments in Ukraine, and offering a

specified roadmap to its implementation. Also the influence of PE market development on country's economy growth was investigated.

The practical value of this research, and of suggested format of PE market organization in Ukraine as a result of it, lies in the fact that after this format implementation, Ukrainian will be open for foreign private equity investments, as well as Ukrainian private equity firms will have an access to global PE market.

Publications. Some results of the research were stated in the scientific article "Analysis of the European regulation and operational standards of private equity proceedings"//Стратегії розвитку фінансового ринку України: зб. наук. ст. студ. денної форми навчання / відп. ред. Н.П. Шульга. – К.: Київ. нац. торг. - екон. ун-т, 2018. – 366с. (С.182-186).. During the process of the research implementation, main theses were also presented during participation in all-Ukrainian student scientific and practical conference on the topic "Strategies for the development of the financial market of Ukraine" and printed "Basic approaches to private equity investments regulation"// Стратегії розвитку фінансового ринку України: Всеукр. студ. наук.-практ. конф. (Київ, 22-23 листопада 2017 р.): тези доп. / відп. ред. Н.П. Шульга – К.: Київ. нац. торг.-екон. ун-т, 2017. – 694 с. (С.384-387)..

Research structure. This paper consists of list of abbreviations, introduction, three parts, conclusions and proposals, references and attachments. Total number of pages is 93. Total number of tables is 4; figures − 5; formulas − 3; attachments − 11; references – 57.

PART 1

FUNDAMENTALS OF PRIVATE EQUITY FUNDS FUNCTIONING AND THEIR PLACE IN BUSINESS LIFE CYCLE

1.1. Nature of private equity and history of its evolution

Private Equity (PE) is a form of equity consisting of investors and funds that make investments directly into private portfolio companies not listed on a stock exchange. So, in a broad sense the private equity is any equity not traded through a public exchange. There is no uniform definition of this term and various explanation of it could be found. Definition from Cambridge Business English Dictionary says private equity is a company shares that are not available for sale on a stock market [13]. Special entity representing Europe's private equity, venture capital and infrastructure sectors, as well as their investors "Invest Europe" (ex. EVCA) defines private equity as the provision of equity capital by financial investors over the medium or long term to non-quoted companies with high growth potential [25]. Some academicians class private equity as part of the asset management industry where investments are made into securities which are usually not quoted in the public markets [48]. According to Economist [20] all types of private-equity investment share following basic features:

• The investors are typically wealthy and supposedly sophisticated – they include family trusts, university endowments and big pension funds, especially state-run ones.

• Private-equity firms take substantial stakes in a portfolio of companies, acquiring the power to sack managers and appoint new ones, with the intention of building better, more valuable businesses.

• Their route to profit is via an "exit" - a way of selling the firm, or bits of it, at a higher price than was paid for it, on some long but fixed time-scale of between three and ten years. Such a sale often takes place through a public stock market.

Private equity investments are normally made through special purpose fund structures of finite life which are established to follow specific investment strategies. According to Metrick & Yasuda [39, p.619] there are four common definitions of private equity funds:

• A private equity fund is a financial intermediary, meaning that it takes the investors' capital and invests it directly in portfolio companies.

• A private equity fund invests only in private companies. This means that once the investments are made, the companies cannot be immediately traded on a public exchange.

• A private equity fund takes an active role in monitoring and helping the companies in its portfolio.

• A private equity fund's primary goal is to maximize its financial return by exiting investments through a sale or an initial public offering.

Private equity funds provide capital to a wide array of companies, ranging from business startups to very large and mature companies. One of the reasons the private equity industry exists is that, in many cases, companies have needs for capital which, for various reasons, cannot be raised from the public markets.

Private equity investments are characterized firstly by active ownership. Active ownership entails that the private equity companies work closely with the management of the acquired portfolio companies to create value by contributing capital and complementary expertise. The private equity funds often obtain a majority stake in the portfolio company to ensure influence on the board and thus active ownership [35]. This control is to be achieved so that the strategic measures needed to assure value creation can be implemented. Active ownership means that the fund, in addition to contributing capital, actively collaborates with the company's board and management on its development. The private equity fund assists the company in strengthening management expertise, delivering operational improvements and accessing new markets.

The aspiration of PE funds is to achieve a positive economic development and cash flow growth for their portfolio companies. This is often accomplished through four value increasing roles:

1. The funds contribute to economic development through selection of the companies that will be invested in.

2. By supplying capital to the acquired companies, funds provide an opportunity for further growth and development.

3. PE funds can contribute complementary resources and expertise that the portfolio company does not already possess, through networks and advisory services.

4. The advisory process materializes through active participation in the portfolio company's board and through other contact with its management. Strategic consultation related to the company's further development might include recruitment of key employees and establishing contact with new customers and partners. Other examples of management tasks private equity funds may perform are raising additional capital and creating good internal routines and practices to ensure cooperation at all company levels.

Historically, the U.S. has been the largest PE market worldwide and is usually viewed as the founder of the modern PE. Several early establishments have incited the development of the U.S. as the PE industry leader. The War Finance Corporation was established in 1918, initially created to give financial support to industries essential for World War I, and to banking institutions that aided such industries, but later moved on to focus on financial backing of agricultural and railroad companies.

The development of the private equity industry has occurred through a series of boom and bust cycles that have been ongoing since the middle of twentieth century. The first impetus to organize investing came in the 1930s and 1940s. Members of the Rockefeller, Bessemer, and Whitney families hired professional managers to seek out investment in promising young companies [30, p.145].

The international roots of private equity investing are traced back to the establishment (by MIT president Karl Compton, Massachusetts Investors Trust chairman Merrill Griswold, Federal Reserve Bank of Boston president Ralph Flanders, and Harvard Business School professor General Georges F. Doriot) of the venture capital firm "American Research and Development Corporate" (ARDC) in 1946 as an effort to commercialize innovative technologies developed during the Second World War [50]. The founders believed that providing management skill and experience was as critical to the success of new business as was adequate funding [52, p.26]. In its 25-year history, ARD helped fund more than a hundred companies and earned annualized returns for its investors of 15.8% [26, p.65].

Also the passage of the Small Business Investment Act of 1958 and the establishment of the Small Business Administration (SBA) with the goal of supporting small businesses, and provision of financial and managerial support to small entrepreneurial businesses in the US, are considered important starting points for the modern private equity industry. Five years later, in 1958, Small Businesses Investment Companies (SBIC) were established, which may be regarded as the event where modern PE industry was born [17].

The boom in the stock market during the 1960s gave an additional strength to the growth in the venture capital (VC) industry which was primarily targeting startup firms within high-tech areas, and as a result, the term came to be almost synonymous with technology financing, but buyout experienced a slight setback as a consequence of the Employee Retirement Income Security Act (ERISA) in the following decade. The government restricted pension funds from taking excessive risk, having an effect on BO, which is considered a high-risk investment. Nevertheless, in the late 80s BO experienced a significant growth and eventually surpassed VC.

Until the late 1970s, capital provisions to the private equity markets were made in a rather unstructured and fragmented way. Investments were undertaken predominantly by wealthy families, industrial corporations or financial institutions,

which invested directly into issuing firms [27, p.10], or originated from governmental initiatives. Up to this point, private equity was primarily a US specific phenomenon.

However, towards the end of this decade and during the beginning of the next, an international private equity market emerged. At the same time, the institutional capital flows to the industry increased dramatically. The main catalysts behind this development stem from regulatory and structural shifts in both Europe and the US [10]. In the US, clarifications of the Employee Retirement Income Security Act (ERISA) in 1978, the so-called 'prudent man rule', relaxed many of the limitations of pension fund investments policies, including investments in private equity and other alternative strategies. In the UK, the move towards the Competition and Credit Control policy in the beginning of the 1970s provided banks with greater investment flexibility [10]. Similar structural and legal changes occurred throughout the rest of Europe, including changes in pension fund and insurance company regulations, which expanded the investment universe for institutional investors. In addition, a few tax reforms in Europe, e.g., more attractive gains from capital investments, positively affected financial institutions' propensity to invest in this particular asset class.

At the beginning of the 1970s, the structure of limited partnerships arose as the dominant organizational form for PE fund investing. As such, the institutional investors' liabilities were limited to the committed capital at the same time that they avoided labor-intensive direct investment activities [27, p.16]. This in turn enabled higher allocations to the asset class. Taken together, these catalyst factors promoted a rapid increase in the amount of capital used for private equity investing.

The steady growth of capital into the VC industry in the late 1970s and early 1980s caused an explosion of new VC firms in the US market. This resulted in an overcrowded market with large numbers of inexperienced venture capitalists, intense competition for promising investment opportunities, and over-investments [31, p.463]. However, these commitments came to a sudden halt in the late 1980s

due to declining returns, a collapsing stock market and the withdrawal of international capital from the US market. After a thorough shakeout and consolidation of the industry in the beginning of the 1990s, only the more successful firms survived. Eventually, the returns became attractive again, after which the industry once again expanded, constituting the basis for a new, this time worldwide, VC boom, i.e., the 'dot-com bubble' era [40]. The boom occurred in the late 1990s, when many high-tech startups benefited from massive public interest in nascent Internet technologies and when initial public offerings of technology stocks were frequent repetition incidents. However, this unsustainable way of investing in largely unproven concepts eventually gave way to reality, leading to the NASDAQ crash in March 2000 and thereby to a massive valuation drop of startup technology firms. In practical terms, this turn of events paralyzed the entire global VC industry. Over the years to come, VC firms were forced to write off large part of their investments. A significant number of venture capital firms were swept away from the market since fund investors to a large extent abandoned the industry. By mid-2003, the industry had decreased in size to less than half of its 2001 capacity [38, p.290]. A decade after the 'dot-com' collapse, little recovery has been seen in the VC industry on a general basis.

The buyout market also flourished in the 1980s. Besides the changed regulations and their positive effects on capital flows into the industry discussed above, the boom was also driven by the availability of high-yield debt, so-called 'junk bonds'. The changes in the Employee Retirement Income Security Act had enabled pension funds to invest in this type of riskier debt securities, which opened up a new financing source to buyout investments [29]. The buyout firms during this period were particularly focused on taking public companies private, and larger and larger deals were carried out as more capital flowed into the industry. As a result of the high leverage levels of most transactions, failed deals occurred regularly. However, the promise of significant returns on successful investments continued to attract more capital. During this time period, private equity was a controversial topic, commonly associated with hostile takeovers, i.e., the stripping

of assets, widespread layoffs and job losses, and wind-downs. As a response, some corporations adopted techniques to avoid unwelcome takeovers, such as so-called 'poison pills'. As a result, hostile takeovers became difficult to carry out which, together with the collapse of the junk bond market, caused the industry to face a number of bankruptcies of large buyout firms in the late 1980s. Consequently, the prevailing way of conducting buyouts by taking public firms private declined significantly [37, p.121-146]. Instead, by the early 1990s, the reemerging buyout (BO) market tended to favor midsized entities of non-publicly traded firms. In order to earn legitimacy and respectability, buyout firms now typically made attractive propositions to existing management and shareholders of identified target companies, and also accepted slightly longer investment horizons. Hence, surviving BO funds found new routes for conducting their business and eventually the returns from buyout investing turned positive again. Thus, the buyout industry once again took off and experienced steady growth in the period from 1995 to 2007, except for a dip around the millennium shift on the back of the 'dot-com' crash.

The combination of historically low interest rates and thereby widespread access to cheap debt, regulatory changes for publicly traded companies, rising profitability in most industries and the allocation of significant investments from institutional investors to this particular asset class, caused an extreme development of the BO industry during the end of this period. The deals grew larger due to the significant inflow of capital. However, this flourishing market characterized by extraordinary growth and returns came to an abrupt halt in 2008 with the collapse of the world's debt markets and a deepening economic crisis that impacted countries around the world [37, p.140].

The period immediately following the 2008 global financial meltdown was a time of anxiety about private equity's ability to deliver market-beating returns. General partners (GPs) had paid peak prices prior to the crash to acquire the assets held in their portfolios and rushed to mark them down sharply to their much lower prevailing market value. They put exit plans for their mature assets on ice and

stretched out holding periods as they waited for the crisis to pass. While market recovery has led to a general uptick in returns of funds since the 2005 and 2006 vintages that bore the brunt of the economic downturn, returns data for the 2008 and 2009 vintages now coming to fruition suggests that PE performance is again beginning to pull away from the performance of public markets. Top-quartile funds have widened their lead in returns by an even greater margin.

So, during the following decade after financial crisis, private equity industry has started the flat recovery. With the results of 2014, the characteristics of this remarkably durable private equity rebound have come into sharper focus. Worldwide, the number and value of buyout exits climbed to an industry record. Strong distributions of capital flowed back to LPs, helping to make 2014 a solid year for raising new funds. The combination of a surge in global liquidity and near-zero interest rates has inflated asset valuations, lifting acquisition multiples on PE investment targets. As the global economic expansion showed signs of strain amid continued record-low interest rates, feverish competition that had investment multiples skirting record highs and increased volatility in public equity markets, 2015 presented many challenges. PE's vital signs remained healthy in 2015, although the aggregate figures retreated somewhat from the highs in 2013 and 2014. The industry remained healthy in 2016, although some of the aggregate figures retreated from 2015. Exit activity was strong, but the totals for 2016 declined as deals that had been on hold during the global financial crisis and its immediate aftermath were finally digested. Fund-raising surged as limited partners continued to recycle distributions into new capital commitments, working hard to maintain their targeted allocations of capital to this high-performing asset class.

Time-line which represents the brief history of PE industry development is presented into Attachment A. Generally, returns in the industry continuing to outperform public markets by a sizable gap over both short-term and long-term time horizons, thus reinforcing investor confidence.

1.2. Role of private equity in the capital market and it's place in business life cycle

In September 2015, the European Commission launched the Capital Markets Union Action Plan, as a part of the Juncker Plan. The document recognizes the need and the relevance of capital market integration that can support the development of alternative channels complementary to bank credit financing, which is particularly important for small and medium-sized enterprises (SMEs).

Generally, there are two crucial questions that face all professional investors: what financial asset classes should be invested in, and what would be an optimal mix of these. A widely used practice in the financial industry, when outlining asset allocation strategies, is derived from the ideas behind modern portfolio theory, presented by Markowitz in 1952. The theory attempts to maximize expected portfolio returns from investments given a certain risk – or to minimize risk for a given level of expected return – by choosing an optimal mix of various assets. This is based on the fundamental principle of diversification, which is considered to help improve portfolio returns while reducing risk. These factors constitute the guiding stars when deciding upon investment strategies [12].

For decades, investors broadly built their portfolios using three traditional financial assets: (i) money market instruments, i.e., cash or cash equivalent securities, (ii) fixed income securities, i.e., bonds, and (iii) publicly traded stocks. These instruments have well-understood characteristics [12]. For example, money market instruments are the most liquid securities, bonds are expected to deliver relatively low returns at low risk, and stocks to deliver higher returns at a higher risk. Over time, however, institutional investors started to look for supplementary assets to add to their investment portfolios. A broad dissatisfaction with falling equity markets and generally low interest rates, together with eased restrictions and changes in regulations, all contributed to an increasing interest in new types of financial instruments [33]. Many of the new assets presented to the market were classified as so-called 'alternative assets'. The financial rationale to invest in such assets has two components. First, while alternative assets are considered more

risky than traditional instruments, their returns are expected to outweigh the additional risks. In other words, they are expected to provide a better risk-return payoff than traditional investments. Second, alternative assets are assumed to have low correlation with traditional securities, and hence are assumed to contribute positively to portfolio diversification. Consequently, the number of alternative asset classes has increased. Today this category includes real estate, infrastructure, commodities, hedge funds and private equity.

Having more diversified sources of financing is good for investments and businesses, but it is also essential for financial stability and for investor protection. In this context, private equity, venture capital and private debt markets are mentioned as the best ways to connect financing to the real economy.

For full development of these forms of alternative financing, it is important that the legislation concerning large institutional investors, such as pension funds and insurance companies, follows the guidelines provided, not hampering the correct allocation of resources to the real economy, but allowing a continuous fundraising cycle. Recently the most important European federations of intermediaries have stimulated the specific measures needed to make the Capital Markets Union a reality. The development of the market should run in parallel with the regulatory framework of Capital Markets Union, in order to encourage long-term investments. The regulatory review could help to facilitate alternative investments, in order to promote emancipation from the banking system and boost international development.

Beyond the work and support provided by lenders who have been instrumental in industrial development in many success stories, traditionally banks look at companies in terms of default risk in lending. Differently from the bank attitude, the alternative credit market players assume logic of selection based also on qualitative variables, aimed at the development and the potential growth of the company while also valuing intangibles often overlooked by the traditional valuation analysis.

So, as an alternative source of financing, private equity's place in company's life-cycle financing must be determined. The financial growth cycle proposed for this research work is presented below in Figure 1.1.

Many sources of finance coexist in the same spaces and some start where others stop, transpiring their complementarity. Additionally, investors in the cycle overlap a curve representing firm size as time passes. The rate at which size grows, or diminishes, as characterised by this curve, combines with the stage the company is at. From Development to Early-stage, it grows at low pace. When it reaches the Rapid Growth phase, firm size increases precipitously, to stabilize in the Mature stage and afterwards start its decline.

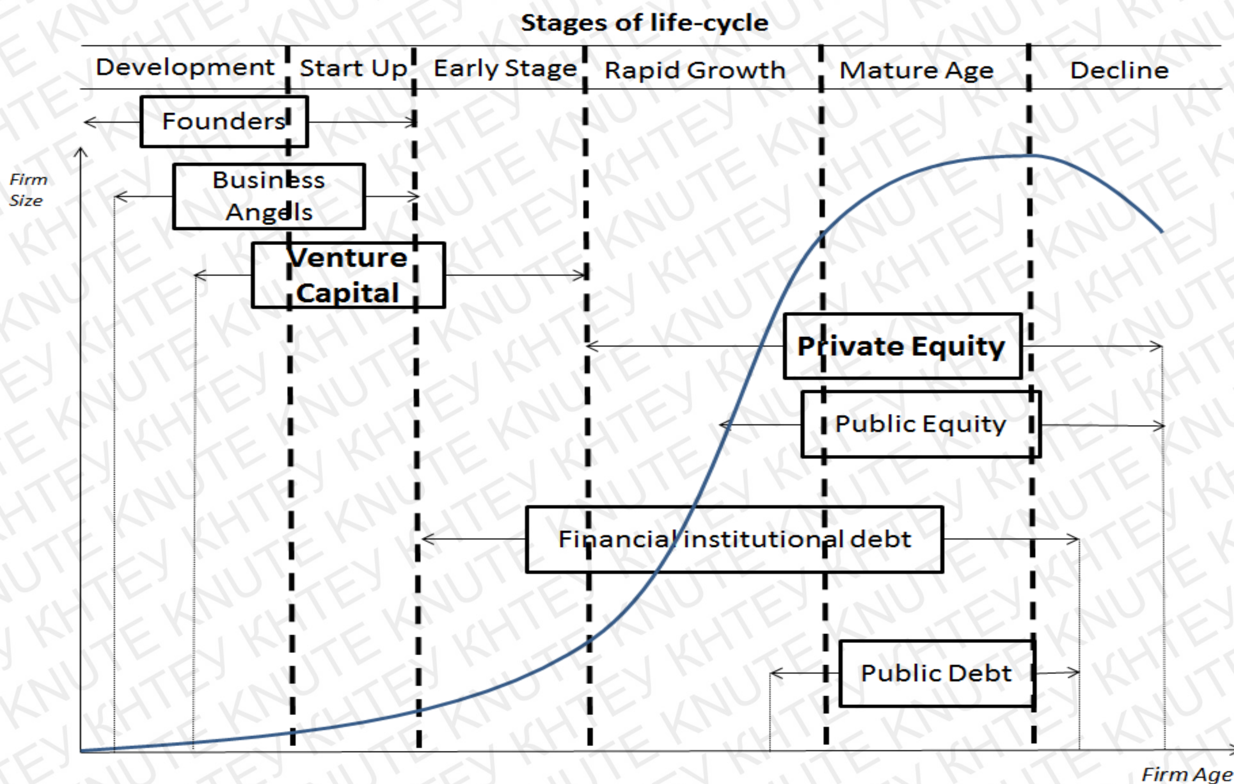


Figure 1.1 Stages of company life-cycle*
*Note: done by author by sources [11, 15]

The main source of finance in the initial stage of a firm's life is the founders' equity. The dependence on the entrepreneurs' money largely results from informational asymmetries that prevent outside, equity or debt, investors of

financing the company [11, p.613]. The high level of need for cash to invest in new projects, compared to the reduced funds provided by the founders, only makes the issue of moral hazard more acute. If the firm has great potential for growth and profitability, business angels may be present as valuable partners, given their expertise and knowledge. These investors can navigate through these companies' informational problems by closely monitoring them. As firms continue to grow they become interesting to more sophisticated investors. On the equity side, venture capital, or even private equity, apply strict screening, contracting and monitoring processes to overcome moral hazard and adverse selection [15]. While on the debt side, financial lenders also develop various types of contracts in order to manage informational problems. The flexibility demonstrated by the private debt market, allowing it to provide funds over such a wide range of ages and sizes, makes it one of the most important sources of finance in the company life-cycle. When firms achieve a large-scale size status, and have built a respectful track-record, the capital markets present important alternatives of financing and restructuring [43, p.27].

The aim of private equity and venture capital is to help companies achieve growth by providing finance, strategic advice and information at critical stages of their development [53]. Literature is far from clear regarding the definition of Private Equity or Venture Capital. Capizzi [14] commented that "the definition of venture capital in economic literature is not unequivocal" and that it is commonly used as a synonym of private equity.

A common ground in this subject seems to be the fact that private equity and venture capital operators invest in the equity of private companies, but their activity is not confined to the role of passive investor, they are also involved in management through advisory services and assistance to the firm development. Nevertheless, the ultimate goal is to make profits, therefore, they plan exit strategies from the start and limit the equity participations to a few years only.

Venture capital (VC) funds generally represent the first business entity which starts to provide small businesses with needed funds. While angels' capital

and experience, support the young firm's product test-marketing, VC investors would come later to finance full-scale marketing and production. Venture capitalists operate in Seed (Development), Start-up and Early Stage financing. As Caselli [15] describes, funds typically invest to finance activities such as Research & Development, product entry in the market and sales growth. The investors' involvement is characterised by a large ownership of shares and support in strategic decisions and financial advisory.

According to Berger and Udell [11, p.660], the positioning of Venture Capital investors in the earlier stages of the life-cycle, exposes them to agency problems associated with financing firms which are informationally opaque. Problems, which are mitigated through a barrage of screening, contracting and monitoring mechanisms that characterize venture capital investing.

As mentioned before, Private Equity investors are located in the more advanced stages of the life-cycle (see Figure 1.1). Caselli [15] established in his book that beyond Early-stage, firms leave the venture capitalists' target clusters and enter the ones where Private Equity operators are typically involved. The types of financing included are Expansion, Replacement and Vulture. Firms at the expansion phase probably have increasing sales and are about to, or have achieved, profitability. Funds are provided to finance sales growth or to improve projects in known fields, so the risk derived from uncertainty is low. The level of ownership starts to diminish as investors need to diversify portfolios, and specific technical skills are no longer required, meaning companies may be financed by a larger number of investors. Replacement capital is needed when firms reach a mature stage. In terms of involvement, the investor usually becomes a prime shareholder, and must be highly skilful structuring governance and corporate finance deals. In the final phase of a firm's life, named as the decline, the cluster of equity financing involved is Vulture financing. This cluster is dedicated to the restructuring of failing companies by improving their financial performance and exploiting new strategic opportunities.

Venture capital and private equity funds differ in many ways. It seems that the most important is diversity in terms of Mikita [41, p.1-9]: investment strategy and stage of business operations. Private equity and venture capital are two separate clusters from the firm life cycle point of view. Venture capitalists provide the funding for start-up businesses and early stage companies, whereas private equity operators are involved in deals with more mature firms. Venture capital funds invest in companies with high growth potential which have undeveloped or developing products. Sources of profitable investment activities are based on the growth prospects of companies a certain time. Private equity funds are interested in medium and large investments in mature companies with high potential for earnings and cash flow. Private equity also engages in various types of other capital transactions, including: buyouts, mergers and acquisitions, turnarounds, replacement capital, initial public offering, mezzanine and venture management [44].

Venture capital represents a specific type of governance that takes an active part in start-up processes [51, p.372]. Experienced investors can provide a wide range of business services for new or growing companies including: market research and strategy, management consulting, contacts with prospective customers or suppliers, assistance in negotiating, help in establishing management and accounting controls, help in employee recruitment, help in risk management, counseling and guidance in complying with legal regulations.

Private equity and venture capital agreements always define length and exit conditions for financial institutions. Even though funding institutions are active shareholders, engaged in company management, they are not interested in taking total control or transforming their temporary participation into long-term involvement. Venture capitalists and private equity operators, sooner or later, sell their position; this is the most important reason for defining this type of investment as “financial” and not “industrial”. The presence of a predefined time horizon for the investment makes private equity and venture capital useful for firms wanting quick development, managerial change and financial stability.

So PE and VC, even though represents same sphere of investments, have some differences in proceeding organization, which are presented in a Table 1.1.

Table 1.1

Private equity and venture capital distinctions*

	Differences	
Similarities	Venture Capital	Private Equity
1)The subjects of investment are nonquoted companies	Target share: at least 50% of company	Target share: any,which allow active management
2)Iinvest in the equity of private companies	Investment on a Seed, Start-up and Early stages	Investment in Growing and Mature companies
3) Hands-on approach	Financing and assistance in full-scale marketing and production	Financing and assistance in emerging on a market, increasing the market share, new products lounching
4)Investment in companies with high potential	Invest in companies with high growth potential	Investments in a companies with high potential for earnings and cash flow
5) Aimed to capital gains	Avarage gains relatively higher	Avarage gains relatively lower
6) Have an exit strategy	Usual exit through selling to other financial institution	Exit through the IPO or Buy-Out

* Note: Done by author by sources [48]

But also venture capital and private equity funds have a lot of similarities and common characteristics, which are also mentioned in Table 1.1: the subjects of both types of investment are nonquoted companies. The investment strategy involves a significant risk diversification through its dispersion in various financial projects. Both the private equity and venture capital funds use similar legal forms for investment. The investment process consists of the same steps and proceeds in a similar way.

Investments in equity can play a role of primary importance in modern economic systems. First of all, on the company side, the opportunity of being invested in by specialized players focused on value creation enables firms to raise "patient" capital, which can be used to plan the start-up phase, develop new

KNUTE KHTEY

strategies, acquisitions, generational transitions or other critical phases of the life cycle rather than to support development plans. Equity investments can greatly contribute therefore to the development of the industrial system and of the economy as a whole, selecting companies with a rapid growth path and providing them with the necessary capital to develop.

To clearly identify the place of PE in the capital market, investors using this asset class also should be mentioned. Talmor & Vasvari [48] interpret investors in private equity funds or LP as entities or persons that provide the equity capital to the fund. They provide a pool of capital which is governed by strict legal rules (established in the LP agreement) and task the private equity manager with executing the prescribed investment strategy of the fund and delivering attractive risk-adjusted returns.

The LPs are effectively passive investors with no influence on the investment matters of the fund once it is established. However, it is normal for funds to establish an advisory board formed by the larger and more experienced LPs in the funds. The advisory board normally meets twice per year. LPs who are not members of the advisory board rely on the annual meeting of the fund and the quarterly reporting provided by the GP as the formal means by which they are informed of the progress of their investments. There are severally types of investors in private equity funds:

- Endowments, foundations, and other not-for-profit organizations.
- Public and private pension funds.
- Family offices.
- Funds of funds (funds that invest solely in other private equity funds).
- Government funds.
- Financial institutions (banks, insurance companies, etc.).
- Corporations.
- Sovereign wealth funds.
- Wealthy individuals.

In recent years a number of institutional investors have begun to invest directly in the underlying investments made by private equity funds. These direct investments are implemented by co-investing alongside private equity partnership managed by private equity firms with whom these investors have close relations and in most cases have invested. Effectively, the co-investing LP becomes a small minority investor in the transaction led by the GP in whose fund a major commitment has been made. These co-investment opportunities are usually offered by GPs to those significant and experienced investors that have contributed a significant amount of capital to the fund and may occur when the private equity fund cannot invest the full amount due to concentration or diversification restrictions.

So, the main role of the private equity on the capital market is to be an asset class to be invested in predominately by huge institutional investors who have the patience for longer-held bets and a need for investment portfolio diversification; and at the same time to be the source of capital for small and medium enterprises, growing and mature companies.

1.3. European and Anglo-Saxon formats of private equity

The private equity industry today spans the globe, but the United States and Europe remain its two biggest markets. While there has been some convergence in the economic terms of American and European private equity funds in the past decade, there remain some significant differences.

Private equity funds on both sides of the Atlantic have comparable investment objectives and strategies, the European industry did develop largely independently of USA market, where private equity originally was born. As such it’s not surprising that there are some important differences between them, particularly at the fund partnership level and legislation peculiarities.

Generally, nowadays there are two different formats regulating private equity investments. On the one hand, there is the European Union format which is regulated by the directives of the European Union. And on the other hand, the so-

called Anglo-Saxon format, which is regulated by the laws of the U.S. and U.K. Main distinctions between those formats could be found at Attachment B.

Those two types are stated as formats, because they are not just simply applied in the European Union, and in the U.S. and U.K., but they are also used in other different countries. For example, the European Union format is also used in Brazil, in Turkey, and in Russia. On the other hand, the Anglo-Saxon format is applied in India, in Australia and Commonwealth countries.

European Union format implies that private equity is a financial service. For this reason it is regulated by the directive regulating the entire financial system. According to Anglo-Saxon format, private equity is not a financial service, but it is an entrepreneurial activity like managing whatever kind of company, but it doesn't mean that there is not an involvement of the financial system.

Also according to Jeng & Wells [36, p.241-289] and Caselli [15] there are some different meanings of the concepts of Private Equity and Venture Capital in Europe and in the United States. As both authors describe, in the American version, Venture Capital as a cluster of Private Equity is assigned to financing young ventures, while in the European sense, Venture Capital and Private Equity are two separate clusters focused on distinct stages of the company life-cycle. Specifically, Venture Capital finances young ventures in their start-up and early-stage phases, whereas Private Equity involves deals with firms in the later stages of their lives.

Mentioned formats also legally identify legal entities which are able to provide private equity activity. According to EU format, there are three different entities that can operate as a private equity investor. The three entities are: banks, closed-end funds and investment firms. Anglo-Saxon format allows five different vehicles which could run the private equity investment: venture capital funds; small business investment companies (SBICs); banks; corporate venture; business angels. All of mentioned entities acts as intermediaries between investors seeking returns in an alternative asset class and non-public companies with a need for financial resources.

In Europe banks and investment firms operate as credit intermediate so investment in equity is only one of the activities they undertake. However, it's a bit uncommon that a bank invests directly in private equity because: 1) when banks invest they must calculate regulatory capital accordingly with Basel II and Basel III regulations, and when a bank invest in private equity the amount of regulatory capital is very high which means that even if the bank generates capital gain, the most relevant part of this capital gain cancelled by the cost of regulatory capital the bank has to calculate for; 2) banks investing directly in private equity have to be compliant with a lot of limits and constraints fixed by law that make it very difficult to have a relevant portion of shares of a company directly managed by a bank.

The other legal entity in Europe is represented by investment firms. Investment firms accordingly with the banking directive are financial institutions. They cannot develop banking activity, but they can provide such services as: equity investment, lending, payment services and money transfers, and currency brokerage and dealing. And according to legislation, all of the above listed activities are carried out with no limits and no caps. For this reason, investment firms can directly invest in private equity. Also investment firms unlike closed-end fund can use debts, which mean can leverage their money.

In European private equity business, the most relevant non-banking activity is asset management, because it assumes direct or indirect investment in firms. Closed-end funds are the most common vehicle of a private equity in Europe. Typically closed-end funds are consisting of three different parts interacting all together: AMC (Asset Management Company); the funds; and the investors, investing their money into the funds. Asset Management Company, closed-end funds, and investors altogether represent the mechanism of closed-end fund investing in private equity. A fundamental rule is that a closed-end fund can invest only the amount of money received by investors. That means that by law, a closed-end fund cannot raise money through debt (the closed-end fund cannot leverage the investments).

In general in the European Union private equity investments are usually driven by close-end funds rather than banks or investment firms. The main reasons are: equity investments are not capped for close-end funds; the investment in equity does not generate a usage or regulatory capital.

As in Europe, where one of the vehicles is the most relevant for the entire system, in the US case private equity is represented by venture capital funds (VCFs), established in form of limited liability partnership (LLP). What is quite relevant in the US regulation is that if a limited partnership is going to invest only in private equity and the maturity of the vehicle is ten years, the vehicle is tax transparent. That's important because it means that the legal entity (the limited partnership) doesn't pay taxes, and taxes are paid by GPs and LPs.

So the legal entities are completely different in US and Europe, but the core of the business is exactly the same.

Another important feature which distinguishes European and Anglo-Saxon formats is the form of relationship regulation between LPs and GPs. While in Europe, there is an internal code of activity regulating the relationship between investors and managers, in the US, since there is no supervisor, LPs and GPs must write a contract. The contract is named the LPA (Limited Partnership Agreement). In the LPA all the characteristic of private equity are considered: the size of the vehicle, the class in which they want to invest, the amount of the management fee, the amount of the carried interest.

European approach to PE is based on three main documents, regulating the financial system: Alternative Investment Fund Managers Directive (AIFMD), Markets in Financial Instruments Directive (MiFID) and the European Venture Capital Regulation (EuVECA). The main concept behind those directives is that the financial system has to be organized with a right balance of efficiency and stability. The other fundamental rule is that any kind of financial institutions starting to operate in the financial system has to receive an approval by local supervisor, or by the European Central Bank, in the case of banks. Financial institutions, after the approval, can sell their service, and they are supervised,

again, by local supervisors like the Bank of Italy, the Bank of France, Bundesbank, or the European Central Bank in case of banks. PE firms must comply with rules that regulate the entire European financial system.

In the Anglo-Saxon format investments in equity are not regulated by the financial system laws because of the common law framework and the general idea that a market discipline is more powerful and important than regulating financial players. The financial market is common law driven, and great importance is placed on laws from both local as well as federal courts. Federal laws have created a general framework for a financial system based on relevant financial activities, not financial institutions. Nowadays private equity funds in the U.S. are among the least transparent financial entities. For the first 30 years following the emergence in 1979 of private equity funds as major financial players, the funds were excluded from the requirement to be registered with the Securities and Exchange Commission (SEC) and meet the SEC's reporting requirements. This changed in 2010 with passage of the Wall Street Reform and Consumer Protection Act, sponsored by Chris Dodd and Barney Frank. While all but the smallest private equity (and hedge) funds are now required to register with the SEC and report such things as total assets under management, types of services provided, clients, employees, and potential conflicts of interest, the reports – in contrast to those of other financial reporting – require far less information and are not made public. Dodd-Frank requires all private equity firms with more than $150 million in assets to register with the SEC in the category of “Investment Advisers”. Under the new legislation, private equity funds are also required to report information covering their size, services offered, investors, and employees, as well as potential conflicts of interest.

The other aspect that has to be clarified is that in the Anglo-Saxon format there is no supervision of a supervisor as there is in the European Union.

The European Union’s Alternative Investment Fund Managers Directive (AIFMD), which is being in force from July 2013, potentially has far-reaching implications for all aspects of private equity managers’ operations. Across the

Atlantic, the US Dodd-Frank Wall Street Reform Act forced managers to register with the Securities & Exchange Commission (SEC). Both regulations substantially increase managers' compliance obligations. Changing regulation, and especially Europe's AIFMD, is one of the main catalysts making private equity firms reevaluate their business architectures. The AIFMD presents a significant challenge to private equity firms – potentially preventing them from marketing to European investors unless the jurisdictions they're based in comply with the directive's key conditions.

Another important feature which differ EU and Anglo-Saxon formats is distribution of capital earnings between Limited Partners and General Partners: so-called "Distribution Waterfall". Carried Interest or simply "carry" is incentive compensation provided to private equity fund managers to align their interests with the fund's capital-providing investors. Basically, carry is a percentage of a fund's profits that fund managers get to keep on top of their management fees, and is a significant component of private equity compensation. Carry typically averages about 20% of the fund's profits. U.S. private equity funds have historically favored a more GP-friendly waterfall, whereby carry accrues on a deal-by-deal basis. By contrast, European funds almost always use a more LP-friendly waterfall, whereby carry is calculated on a whole-fund basis. The distinction is longstanding and ingrained enough in market practice that the deal-by-deal model is sometimes referred to as an 'American style' waterfall, while the whole-fund model is 'European style'. Under the European waterfall, the fund must first return all drawn capital back to its investors (the LPs) ahead of sharing the incremental profits between the LPs and the GP. Under the United States waterfall, the fund is instead allowed to start sharing any incremental profits between the LPs and GPs on a "per realised" investment basis, and therefore does not have to wait for all the invested capital to be returned. In practice, this has the impact of "speeding up" the time at which the GP is able to receive its share of the profits.

Although U.S. and European fund managers now compete directly for investors' capital, their traditional waterfall models have so far mostly defied the

pressure of convergence. For example, MJ Hudson's broad-based survey of PE fund terms in 2017 found that 64% of North American funds featured deal-by-deal carry, whereas 88% of European funds in the same survey offered whole-fund carry [42]. That said, GPs on both sides of the Atlantic are increasingly experimenting with the development of alternative models of carried interest, such as the hybrid waterfall, whereby a portion of returns is distributed on a deal-by-deal basis and the remainder on a whole-fund basis.

Carry clawbacks terms are also different in mentioned formats of Private Equity investments. Generally "clowback" term is used for referring any money or benefits which have been given out but are required to be returned back due to certain special circumstances which will be mentioned in the contract. In private equity industry clawback provision permits the LP's to "claw back" any carry forwarded amount which was paid during the life of the fund on prior portfolio investments in order to normalise the final carry to the originally agreed percentage. Thus, the clawback provision prevents the LP's from paying any additional amount and then suffering a subsequent loss. Both U.S. and European funds typically contain a GP clawback mechanism as protection against the overpayment of carried interest. However, by virtue of the way in which it calculates carry, a European style waterfall is less likely than an American one to result in overpayment of carry during the life of a fund. Therefore, in Europe, it is common for the clawback to kick in at liquidation only, often backed up by escrow protection. Conversely, in funds with American style waterfalls, clawback protection takes on altogether greater significance, and LPs are more likely to negotiate for interim clawbacks, from the end of the investment period through to liquidation of the fund. Escrow accounts are less common in U.S. funds than in European funds.

Another major difference in the economic terms of European and U.S. funds is the option to finance GP commitment via management fee waiver. This is seldom seen in European fundraising, but it has a history of being widely used in the U.S. The waiver mechanism involves reducing capital calls to investors for

management fees and instead drawing down the saved amounts from investors to meet the GP's obligation to contribute capital alongside investors toward the fund's investments and expenses. By recycling cash within the fund structure, rather than drawing it out in the form of fees and then ploughing it back in as capital, the GP can make its contributions on a gross basis for tax purposes. It also has the advantage of allowing first time fund managers and more junior members of the management team, who may not have enough cash on hand to meet regular drawdowns on account of GP commitment, to make more meaningful contribution to the fund.

These two different formats are quite relevant to understand the functioning of private equity system all around the world. For a local player, the availability of two formats is not so important. If the fund is an Italian private equity investor, a French private equity investor, or a German private equity investor, and it acts at a local level, it only have to apply the European Union format, just like if it is a U.S. private equity investor and it want to invest in the U.S.

On the contrary, if the fund is a global player and operates in different countries, having two different formats is quite important because in some cases it would be more advisably to use a European Union format, and in other cases it could be better to use a U.S./U.K. format. The knowledge of legal proceedings is not just simply a legal matter, but it really becomes a business matter of private equity investments.

PART 2

DIAGNOSTICS OF PRIVATE EQUITY FUNDS PERFORMANCE AND REAL-LIFE PRACTICES OF THEIR REGULATION IN FOREIGN COUNTRIES

2.1. Analysis of best practices in private equity proceedings regulation

As it was mentioned at Part 1, worldwide there are two approaches to regulate the private equity proceedings. In both cases special legislation and institutional base are to be created in order to ensure proper functioning of private equity funds among other financial institutions and financial system as a whole.

European approach to PE is based on two main documents, regulating the financial system: Alternative Investment Fund Managers Directive (AIFMD) [18] and the European Venture Capital Regulation (EuVECA) [24]. The main priorities behind those documents are that the financial system has to be organized with a right balance of efficiency and stability. PE firms must comply with rules that regulate the entire European financial system.

One of the most important features of European format of private equity regulation is that PE is identified as a financial service, but not as an entrepreneurial activity as it is in US and UK. That is the reason of such a strict regulation applied to private equity proceedings in Europe.

European Union legislation defines different vehicles for setting up an equity investment: Banks; Investment firms; Closed-end funds. All of mentioned entities acts as intermediaries between investors seeking returns in an alternative asset class and non-public companies with a need for financial resources. In general in the European Union private equity investments are usually driven by close-end funds rather than banks or investment firms. The main reasons are: equity investments are not capped for close-end funds; the investment in equity does not generate a usage or regulatory capital [47].

For private equity fund managers, the most far-reaching regulatory change has been the Alternative Investment Fund Managers Directive (AIFMD), which sets out an EU-wide standardized framework for managing and marketing alternative investment funds. It establishes a legal framework for the authorization, supervision and oversight of managers of a range of alternative investment funds (AIFM), including hedge funds and private equity. A final text of the Alternative Investment Fund Managers Directive (AIFMD) was adopted in November 2010. Officially it was introduced and implemented since 21 July 2011, and transposed into EU countries' national laws by 22 July 2013.

The Directive introduces harmonized requirements for financial intermediaries engaged in the management and administration of alternative investment funds (AIF). The Directive applies to entities established in a Member State of the EU which manage one or more alternative investment funds, irrespective of where the fund is established. The Directive also applies to managers that are established outside the EU to the extent that they manage AIF established within the EU, or market AIF to investors domiciled in the EU. AIFMs can provide their services in different EU countries on the basis of a single authorisation. Once an AIFM is authorised in one EU country and complies with the rules of the directive, the AIFM is entitled to manage or market funds to professional investors throughout the EU.

To operate in the EU, fund managers are required to obtain authorisation from the competent authority of their home EU country. To obtain authorisation, AIFMs have to hold a minimum level of capital in the form of liquid or short-term assets. No AIFM shall be allowed to manage an AIF unless it has been authorised in accordance with the Directive. This authorisation will be via the national regulator of its home Member State. The regulator must inform European Securities and Markets Authority (ESMA) on a quarterly basis of authorisations granted or withdrawn, and ESMA will keep a central public register of all authorized AIFM [22]. Once authorised, an AIFM will be permitted to provide

management services to AIFs domiciled in any Member State and to market the securities of the AIFs it manages to “professional investors” across the EU.

AIFMs are required to assure the competent authority of the robustness of their internal arrangements with respect to risk management. This includes a requirement to disclose, on a regular basis, the main markets and instruments in which they trade, their principal exposures and their concentrations of risk. AIFMs are required to take all reasonable steps to identify conflicts of interest that arise in the course of managing one or more AIFs, and then to manage and monitor those conflicts of interest in order to prevent them from adversely affecting the interests of the AIF and its investors. The Directive also requires an AIFM to implement systems designed to manage liquidity risk and to conduct regular stress tests of these systems under both normal and exceptional market conditions. These measures are designed to prevent the potential buildup of systemic risk.

AIFMs are required to ensure that the funds they manage appoint an independent depositary, for example a bank or investment firm that is responsible for overseeing the fund’s activities and ensuring that the fund’s assets are appropriately protected. A depository’s function is predominantly the safekeeping of the assets of the fund, and it is intended to protect investors against losses arising from fraud of the AIFM. AIFM come under an obligation to establish appropriate and consistent procedures for the valuation of the assets of each fund under management. AIFM also come under an obligation to put in place remuneration policies and practices for certain senior staff, designed to promote effective risk management.

One of the most significant ways in which the AIFMD attempts to manage systemic risk is via the regulation of leverage. The directive introduces specific requirements with regard to leverage, i.e. the use of debt to finance investment. Competent authorities have the right to set limits to leverage in order to ensure the stability of the financial system. AIFM are required to set leverage limits in respect of each AIF they manage. AIFM managing one or more AIF employing leverage on a substantial basis shall make available to the competent authorities information

including the overall level of leverage employed by each AIF it manages, and a break-down between leverage arising from borrowing of cash or securities and leverage embedded in financial derivatives. If it is considered necessary in order to ensure the stability and integrity of the financial system, the AIFM's regulator may impose limits on the leverage that a particular AIFM may employ or set other restrictions on the management of the AIF.

The AIFMD includes a number of measures designed to increase transparency. First, the Directive sets out the information which must be disclosed to investors before they invest in a fund, including the investment strategy and objectives of the fund, the identity of the AIFM, its pricing methodology and valuation procedure, all fees and charges, and the latest net asset value of the fund and historic performance information, where available. In order to encourage diligence amongst their investors, AIFMs are required to provide a clear description of their investment policy, including descriptions of the types of assets and the use of leverage. An annual report for each financial year has to be made available to investors on request. The Directive also requires ongoing disclosure by AIFM. Annual reports in respect of each EU fund managed by an AIFM and each fund it markets in the EU must be provided to the AIFM’s regulator. The Directive contemplates periodic disclosure to both investors and competent authorities regarding: (a) the percentage of the AIF’s assets which are subject to special arrangements arising from their illiquid nature; (b) any new arrangements for managing the liquidity of the AIF; and (c) the current risk profile of the AIF and the risk management systems employed by the AIFM to manage these risks.

There are also rules designed to prevent asset stripping. Where an AIF acquires control of a non-listed company or an issuer, the AIFM is subject to the anti-asset stripping provisions. For a period of two years, the AIFM must act against any distribution, capital reduction, share redemption or acquisition of own shares by the company. When a private equity fund acquires a controlling interest in a non-listed company the AIFM shall not, within 24 months following the acquisition, be allowed to facilitate, support, instruct, or vote in favor of any

distribution, capital reduction, share redemption or acquisition of own shares by the company and must use its best endeavors to prevent the same from occurring. The obligation is therefore placed on the AIFM rather than on the portfolio company.

EU countries may choose not to apply the directive to smaller AIFMs, i.e. funds with managed assets below €100 million if they use leverage and with assets below €500 million if they do not. Smaller funds are however subject to minimum registration and reporting requirements, presented in another important document which sets up European framework for private equity proceedings: Regulation (EU) No 345/2013 on European venture capital funds (EuVECA).

The European Venture Capital Fund Regulation (EuVECA) came into effect on 22 July 2013 to complement and coincide with the implementation of the AIFMD. As the EuVECA is a Regulation (and not a Directive) it does not need to be transposed into national law and so it has immediate effect in all Member States [21]. It sets out the criteria which managers of venture capital funds must meet in order to market their funds to investors across the EU under a new "European Venture Capital Fund" label and without needing to comply with the demands of the Alternative Investment Fund Managers (AIFM) Directive.

The Regulation, which unlike the AIFMD is purely a marketing regulation, aims to provide a voluntary EU-wide passport for qualifying venture capital funds and their managers. It is intended as an alternative regime to that set out in the AIFM Directive, which provides a compulsory regime and a marketing and management passport for private equity managers whose assets under management are above a threshold of €500 million [23].

In order to qualify for this EuVECA designation the Regulation introduces requirements relating to the investment portfolio, investment techniques and eligible undertakings that a qualifying fund needs to meet. It also sets out uniform rules on which categories of investor a qualifying fund may approach and on the internal organization of the managers that market such qualifying funds.

As the EuVECA is set out in a Regulation, it does not require separate national legislation for its implementation and is directly applicable. There is, however, in some member states, a need to change some domestic laws and regulations in order for the national competent authority to be able to oversee the EuVECA regime and to organize local registration and so venture capital managers interested in using this designation should also investigate any local requirements.

Unlike the AIFMD, which mainly regulates managers, the EuVECA Regulation's initial focus is on the fund (investment vehicle). Every fund using the EuVECA label will have to prove that a high percentage of investments (at least 70% of the aggregate capital contributions and uncalled commitment capital) is spent in supporting young and innovative companies.

Managers that intend to market a qualifying venture capital fund under the EuVECA label must first inform the competent authority in their home member state of their intention and provide to it the information including details about the owners and relevant staff of the Manager, as well as about the Fund and its marketing intentions. The manager must also give a narrative description of the arrangements which have been made with a view to fulfilling the on-going compliance requirements of the Regulation.

Described above set of different rules in EU member states have increased costs for raising venture capital funds across the EU. This has in turn contributed to reduced levels of investment in such funds. The new EuVECA regime addresses these issues and complements the AIFMD so that smaller funds can improve their access to capital. Fund managers who comply with the Regulation and achieve EuVECA status will reduce the costs they incur in raising capital across the EU. Managers will not have to comply with the full requirements of the AIFMD and will have simplified compliance procedures. Marketing venture capital funds across the EU will also be easier, as there will be no obligation to comply with the national laws of each individual member state.

The other part of global private equity market is represented by Anglo-Saxon format of PE, applied not only in USA and the UK, but also in India, Australia and Commonwealth countries.

In the Anglo-Saxon system the private equity is regulated by common law of U.S. and U.K., fiscal rules, and special laws that are provided to regulate the private equity system. Private equity funds in the Anglo-Saxon model are among the least transparent financial entities.

In the Anglo-Saxon format investments in equity are not regulated by the financial system laws because of the common law framework and the general idea that a market discipline that is more powerful and important than regulating financial players. Hence, private equity investments are recognized as an entrepreneurial activity, but not as a financial service as it is in Europe [15].

The US financial market is common law driven, that means laws from local and federal courts play a vital role in market governing. Federal laws have created a general framework for a financial system based on relevant financial activities, not financial institutions.

Nowadays private equity funds in the U.S. are among the least transparent financial entities. For the first 30 years following the emergence in 1979 of private equity funds as major financial players, the funds were excluded from the requirement that they register with the Securities and Exchange Commission (SEC) and meet the SEC's reporting requirements. This changed in 2010 with passage of the Wall Street Reform and Consumer Protection Act [19], sponsored by Chris Dodd and Barney Frank. While all but the smallest private equity (and hedge) funds are now required to register with the SEC and report such things as total assets under management, types of services provided, clients, employees, and potential conflicts of interest, the reports – in contrast to those of other financial reporting – require far less information and are not made public.

Dodd-Frank requires all private equity firms with more than $150 million in assets to register with the SEC in the category of “Investment Advisers.” The registration process began in 2012, the same year the SEC created a special unit to

oversee the industry. Under the new legislation, private equity funds are also required to report information covering their size, services offered, investors, and employees, as well as potential conflicts of interest. Certain exemptions exist for venture capital fund sponsors and sponsors of private equity funds who have less than US$150 million in assets under management. Sponsors relying on these exemptions are known as exempt reporting advisers and still have certain reduced filing obligations with the SEC.

That could change with the adoption of the Financial CHOICE Act [32], which was introduced into the U.S. Congress in an attempt to roll back regulations associated with Dodd-Frank. The act, which passed the House of Representatives in June 2017, would deregulate the U.S. private equity industry and significantly reduce oversight for all but the smallest firms. Among the most impactful changes proposed by the act would be the elimination of the requirement that private equity firms register with and submit to regulations and examinations from the SEC. Additionally, the act would limit the SEC's use of administrative proceedings, give respondents stronger tools to deploy during investigations and remove financial incentives for whistleblowers implicated in wrongdoing while also increasing penalties for violations.

From a legal point of view, equity investors in the US could be: Venture capital funds; SBICs; Corporate ventures; Banks; Business angels. Today, a venture capital fund along with SBICs constitutes approximately 60% of the US private equity market, while the other investment vehicles constitute the remaining 40%.

The other side of the Anglo-Saxon system is represented by the UK market, which together with the United States, really represent the place where private equity was born. The financial market in the UK is common law driven like the US, and great importance is given to laws from both local and federal courts. These laws have created a general framework for the UK financial system.

Following laws are considered crucial for equity investments development in the UK:

- Industrial and Financial Corporation Act (1945) – Created public funds to sustain small and medium entities (SMEs) and start-ups.
- Business Start-Up Scheme (1981) and Business Expansion scheme (1983) – Give fiscal incentive for both corporations and private individuals to invest in equity.
- Enterprise Investment Scheme (1994) and Venture Capital Trust Act (1997) − The Enterprise Investment Scheme (EIS) was designed to help small, high-risk trading companies to raise financing by offering a range of tax reliefs to investors who purchase new shares in those companies. The Venture Capital Trust Act was designed to encourage individuals to invest in a range of small, high-risk companies by investing through venture capital trusts (VCTs). Today these Acts still work for companies as well as for private individuals.

UK private equity is mostly driven by such legal entities as English limited partnerships (ELP). English limited partnerships must be registered at Companies House using an application for registration of a limited partnership to obtain the limited liability status conferred by the Limited Partnerships Act 1907 (LPA). The application for registration mandates that certain information be provided, including a description of the general nature of the business, the name of the partnership, the principal place of business of the partnership, the full name of each of the general and limited partners, the amount of the capital contributed by each limited partner as capital to the partnership and the form of contribution, the partnership's proposed term, the date of the ELP's commencement and a statement that the partnership is an ELP.

Once an ELP is registered, the Registrar will issue a certificate of registration. This certificate includes the ELP's name and registration number and represents conclusive evidence that the ELP came into existence on the date of registration. A register of ELPs is maintained by the Registrar.

Limited partners are not ones of themselves regulated entities. Instead, the focus of UK fund regulation is on the fund manager. UK-based fund managers that provide portfolio and risk management functions to alternative investment funds

(AIFs) are required to be authorised by the Financial Conduct Authority (FCA) as alternative investment fund managers (AIFMs) [28]. The AIFMD imposes substantive regulatory obligations on AIFMs, including rules relating to internal capital adequacy requirements, regulatory and investor reporting, ensuring that each AIF it manages appoints a depositary and restrictions on remuneration of employees of the AIFM, among others. As FCA authorised and regulated entities, UK AIFMs are subject to the FCA's conduct of business rules and general FCA principles of business, including the requirement to deal with the FCA in an open and cooperative manner. The FCA relies heavily on authorised firms to provide information to it but reserves the right to visit, inspect and evaluate the compliance of authorised firms, typically through thematic reviews (which focus on specific industries, for instance, asset management or retail banking), or as part of its general supervisory remit. The FCA is also able to take action at a firm-specific level where it has specific concerns about a particular regulated entity. Some larger or higher risk firms are also proactively supervised by the FCA on a 'relationship managed' basis.

Described legal frameworks represent the best practices in global private equity proceedings regulation and must be taken into account by any country, which is going to transform or create new legal prerequisites for PE regulation. Ukraine, as one of such countries must design own legal base in accordance with one of the mentioned formats to be able to get access to global private equity market and become more attractive for investors from all around the world. While Ukraine has European-integration intentions, legal format, which is used in European Union, could become the appropriate base for national legislation.

2.2. European and Anglo-Saxon private equity market assessment

The global private equity and venture capital industry has experienced significant growth during the past 10 years after financial crisis and has become an increasingly important source of finance and expertise for companies seeking to achieve their growth aspirations. Particularly in a period of economic uncertainty where there is a scarcity of capital, private equity and venture capital can be part of the solution to the current economic challenges facing companies across the globe. Private equity provides one of the sources of capital that can help to overcome the current funding crisis and thereby play its own active role in contributing to the economic recovery and continued innovation. The industry is well funded with long-term committed capital which can provide a vital, alternative form of finance to traditional banking and public equity markets. Also, private equity is about more than providing equity capital. Private equity is distinguished by its hands-on approach to working with management teams to set clear strategic priorities and develop more successful businesses. Active management, the alignment of interests between management and investor, robust corporate governance processes and a focus on value creation are all key aspects of the industry's approach to investment. This role will become particularly important as companies face up to internal reorganization and competition in a more difficult global economic environment.

To describe current situation on a global private equity market, there should be considered European and United States market performance in terms of: aggregate deal value; exit activity performance and fundraising activity performance, because mentioned indicators are representatively shows historical and current level of PE market development.

2017 was another strong year for worldwide PE performance. In Europe deal flow totaled €363.0 billion across 3,015 transactions—a 14% increase and 11% decrease, respectively, from the prior years (see Attachment C).

Over the past seven years in Europe value and number of closed deals tend to slightly growth, only 2015 year shows significant acceleration (20.8% increase

over 2014) in fund's activity what is explained by a flurry of buyouts with 18 transactions at or exceeding €2.5 billion in size completed. Another key factor that caused increasing of deals value is elevated level of U.S. investor involvement. With a superabundance of capital overhang to put to work, far more than Europe's largest buyout firms, U.S. counterparts contributed in no small part to last year's surge in value. Some decline in activity in 2016 is explained by the fact that European companies could no longer justify holding on to non-core assets that may have been hurting their bottom lines, and PE investors were happy to take the carveouts at a discount. Another factor of such a decline is 40% decrease in value of PE activity with US-based investor participation.

PE deal activity in the US during 2017 was roughly on par with 2016, as dealmakers put $538.2 billion to work across 4,053 deals (see Attachment D).

Over the described time period, PE activity in the USA was sustainably growing in terms of deal value and number of closed deals. But 2017 show some decline, due to 24.6% of 2017 deal volume with 999 deals completed to close out the year, so they were not taken into account into presented chart, and will be included into results of 2018 year.

Activity mirrored trends across private markets, with investors completing fewer but larger deals in 2017. The median deal size for European PE transactions increased by 67% in 2017, to €38.5 million—the highest since 2006. Given the broad-based strength in fundraising, the median fund size in US climbed from $225.0 million in 2016 to $292.5 million in 2017 (30% increase)—another record high in the database.

In 2017, European private equity firms enjoyed another strong year of exit activity. PE backed exit activity totaled €175.0 billion in value across 1,094 portfolio companies in Europe —the fourth consecutive year of at least €160 billion (see Attachment E).

Strong liquidity was aided by the buying power of other PE firms eager to deploy the sums of "dry powder" raised in recent years. Secondary buyouts (SBOs) accounted for one half of all exit activity in 2017, both in terms of number and

value of transaction. PE firms invested €88.1 billion on transactions in which another PE firm was the seller—higher than any other year on record. Meanwhile, strategic acquisitions accounted for just 44% of exit activity, the lowest in the last decade. Corporate acquirers slowed their pace of acquisition last year, as they worked to incorporate recent purchases into existing operations. Strong growth in exit activity was peaked in 2015 year, and shown some decline in 2016-2017 years because of less appetite for IPOs last years, with the decreased levels of competition from corporates, particularly for larger acquisition targets.

US private equity firms saw an 11% YoY decrease in exit volume, with exit value and volume falling below both five-year averages for the first time since at least 2010. A total of $184.8 billion in value was realized over 1,097 exits during 2017 (see Attachment F).

The downward trend in exits is largely driven by a strong pullback in strategic activity, with $95.45 billion in exit value across 505 strategic acquisitions of US-based portfolio companies in 2017. While exit value via strategic acquisition remains above pre-crisis levels, it fell below both the five- and 10-year averages in 2017, which saw the lowest amount of strategic activity since 2011. Despite several corporate mega-deals, which represented much of the industry commentary in 2017, it was secondary buyouts (SBOs) that drove the median exit size to a new all-time high of $221.5 million.

European PE firms raised €67.3 billion across 109 vehicles in 2017 (see Attachment G), a 7% decrease from the prior year in terms of value, but still the second-highest capital total since the financial crisis. Institutional investors who are starved for yield in more traditional asset classes continue to propel allocations to alternatives, including PE.

After growing every year from 2012 to 2016, the median fund size dipped slightly in 2017 to €310.0 million— below the €326.4 million recorded in 2016, but still comfortably above pre-crisis levels. The decrease in fund sizes is indicative of a growing interest in middle-market-focused funds (those with

between €100 million and €1 billion in commitments), which accounted for 77% of total closes on the year—the highest in at least a decade.

US private equity firms closed on $232.7 billion in capital commitments across 247 funds during 2017 (see Attachment H).

Capital continues to accrue to fewer yet larger funds, evident in the 8% year-over-year (YoY) increase in committed capital despite a 15% decrease in the number of funds over the same period.

So, even regardless of some decline in performance in 2008-2009, private equity nowadays is a huge market with a high potential to growth. Ukraine has to get an access to the worldwide capital market and the PE market as a part of it. While the European approach to PE legal base update was chosen, Ukraine has a chance to become a member of European private equity market.

2.3. Analysis of private equity performance in Ukraine

Negative socio-economic and political trends have affected the current state of the sphere of private equity investment in Ukraine, so activity in it stays on a low level, comparing to average figures on the world market. Investors are looking for objects for investment at relatively low prices, preferably in sectors where our country has a global competitive advantage. It is known that the investment potential of Ukraine is particularly high in two spheres that make the economy of our country unique: the first is the agricultural sector and the second - IT and Telecom. These allow us to position Ukraine as a country with achievements not only in the raw materials, but also in the intellectual sectors of the economy. So Ukraine has a great potential for developing the sphere of private equity investments, and with the growth of the economy, activity in this sphere will intensify. But to become the full member of PE market, updating of current legislation in this sphere is vital, because outdated legal frameworks is one of the main obstacles for modern financial market development.

The Civil Code, the Commercial Code, the Company Law, the Law on Protection of Foreign Investments in Ukraine (05.10.1991); Law on Investment Activity (18.09.1991); the Law on Foreign Investments (25.02.2000); and the Law on Joint Investment Institutions (05.07.2012, as amended) [8] constitute the legal framework for PE in Ukraine. Some of mentioned laws were adopted in 1991, and still regulate the activities of business entities. But they are extremely outdated and do not meet today's market needs, primarily of foreign investors and Ukrainian high-performing businesses. Those laws do not allow them to use the mechanisms that have long been included in international practice. Nowadays, in Ukraine the investor is poorly protected in corporate governance issues and associated risks. As a consequence, this factor hinders the flow of investors to Ukraine and investments are planned at the level of foreign jurisdictions with more progressive corporate legislation. Changes in the regulation of the activities of different investment funds, including private equity funds, will help to return significant investments to the Ukrainian economy.

From the point of view of the domestic legal field of functioning of private equity funds, in terms of their organizational form, they are not defined as a separate type of investment funds, but are equated to the venture capital fund as a type of CII [8].

To spot current state of Ukrainian private equity industry, its' place on the European market among other countries in terms of total value of investments and value of investments as a percent of GDP should be identified, because mentioned indicators representatively exhibit current level of PE market development.

Starting with comparison of value of investments as a percent of GDP let us identify the general position of Ukraine among all others European countries, presented in Figure 2.1

KNUTE КНТЕУ

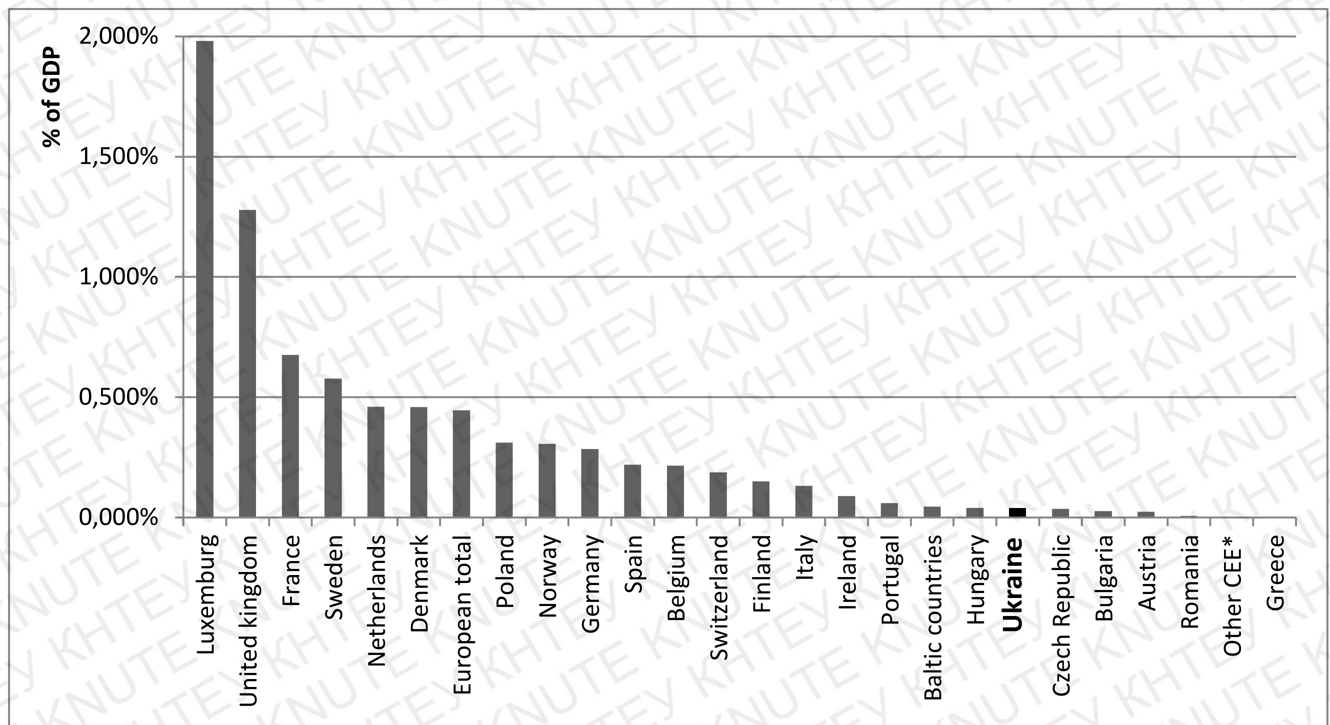


Figure 2.1 Private equity investments as a percent of GDP in Europe**

Notes: *Other CEE consists of Bosnia-Herzegovina, Croatia, Macedonia, Moldova, Montenegro, Serbia, Slovakia, Slovenia.

** Done by author by Source [34]

The indicator which represents the total value of private equity investments as a percent of GDP in Ukraine in 2017 year is equal 0.039% which is 11.44 times lower then totally in Europe (0.45%). The European leaders regarding this indicator are: Luxemburg and United Kingdom with 1.98% and 1.279% resp. By this indicator Ukraine mostly is among countries of CEE. So, total value of investments will be observed among CEE countries.

Private equity investment in the CEE region reached €3.5 billion in 2017, an increase of 113% year-on-year and a record high level for the region. This result surpasses the previous peak in 2008 by 40%. The growth in CEE investments underlines a trend across Europe as the total amount of European private equity investments in 2017 increased by 29% year-on-year to €71.7 billion, the second highest level for Europe on record and only 4% below 2007’s peak, presented in Figure 2.2.

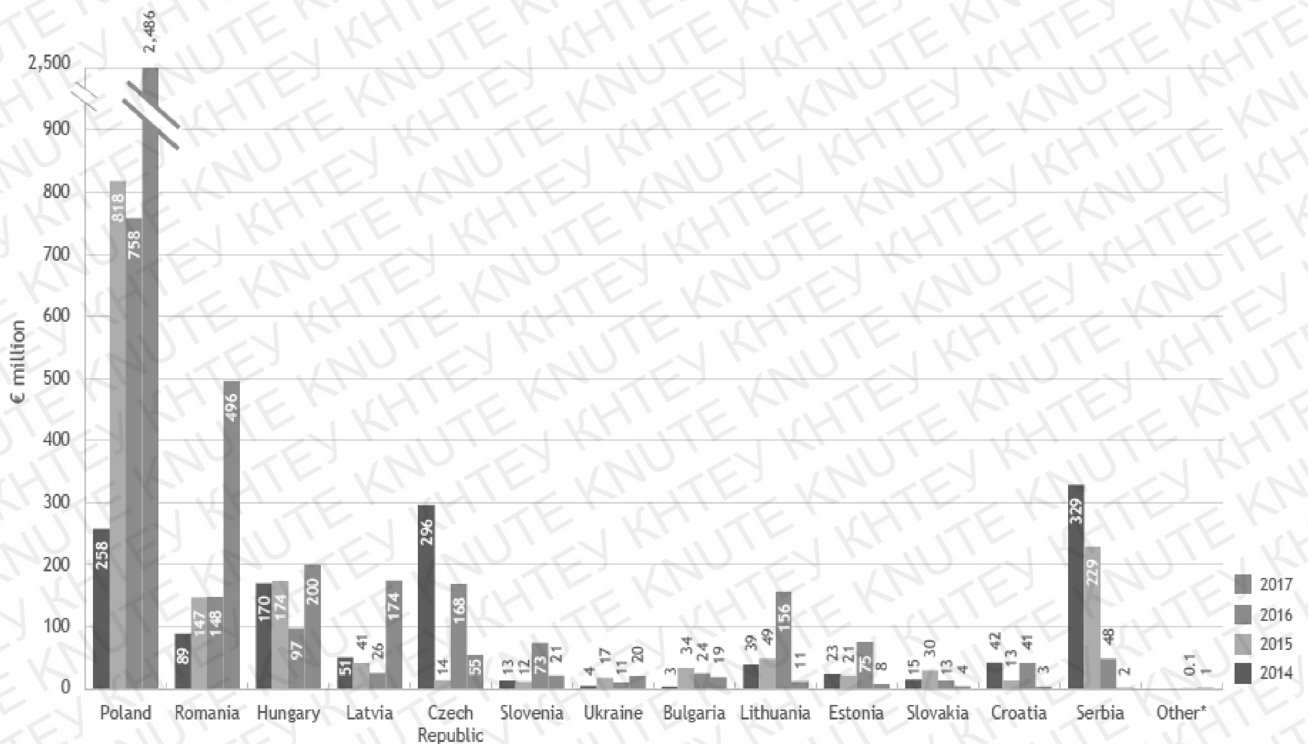


Figure 2.2 Annual investment values in CEE, 2014-2017**

Notes:
*Other consists of Bosnia & Herzegovina, Macedonia, Moldova and Montenegro
** Source [16]

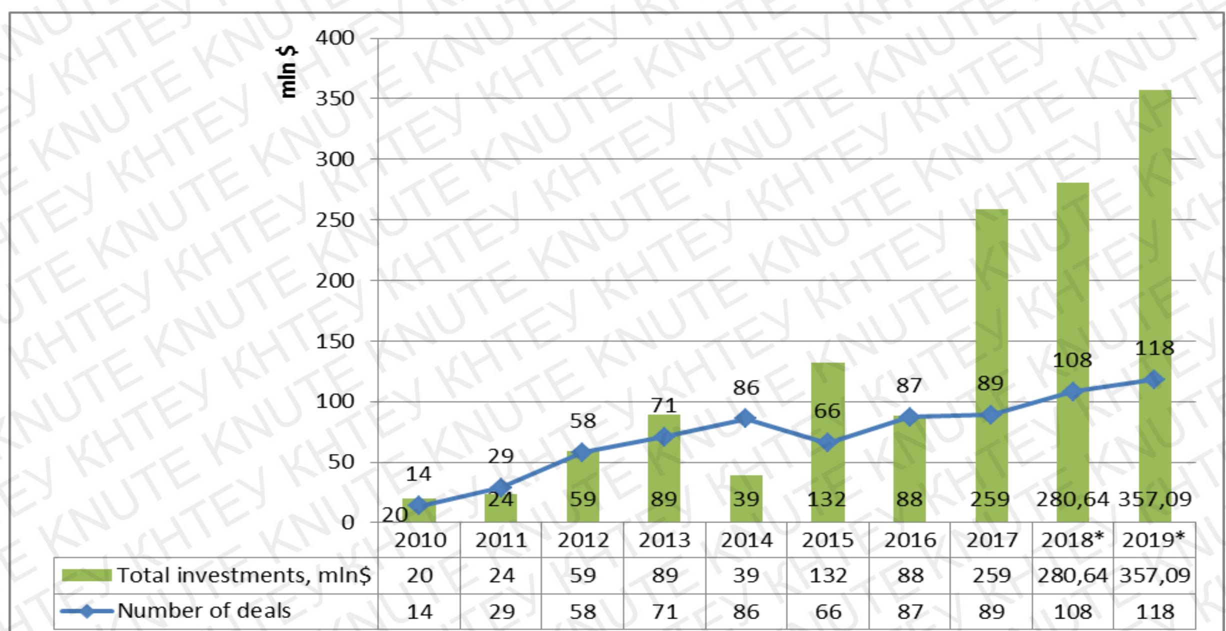
The CEE region's share of the total European investment amount rose in 2017 to around 5%, from 3% in 2016. A total of 257 CEE companies received private equity investments in 2017, a 25% decline from 2016. The drop was largely driven by a decline in the number of companies that received venture capital, a trend also seen in 2016, while the number of companies obtaining buyout & growth financing dropped only moderately.

Among CEE countries Poland remained the leading destination with 71% of the region's total investment value and home to almost a quarter of the companies receiving funding. By investment value, Poland was followed by Romania with 14% of the CEE investment value total, Hungary (6%) and Latvia (5%). Hungary saw the largest number of companies receiving private equity investment in 2017 at 104, comprising 40% of the CEE total. These four countries combined

comprised 96% of the total CEE investment by value and 70% of the companies receiving private equity investment in 2017.

Ukrainian PE market currently is significantly unexploited in comparison with other European countries, which have already arranged the common European rules and laws regulating entire financial system, and PE investments, as a vital part of it.

By the result of 2017 total capital invested by a PE funds in Ukraine was equal to $258.6m, almost 3 times exceeded 2016 and has reached it historical peak. Total number of deals in industry: 89 what is absolute high for all time of observation (see Figure 2.3). Activity mirrored trends across private markets, with investors completing fewer but larger deals, especially in 2015 and 2017 years. The median deal size for Ukrainian PE transactions increased by 3 times in 2017, to $3.3 million (from $1,1 mln. in 2016). Higher tickets in the same market point to later stage investments. The responses obtained by a joint survey by EY Ukraine and UVCA indicate that the investors' demand for later stages is going to increase further in 2016-2019.



	2010	2011	2012	2013	2014	2015	2016	2017	2018*	2019*
Total investments, mln$	20	24	59	89	39	132	88	259	280,64	357,09
Number of deals	14	29	58	71	86	66	87	89	108	118

Figure 2.3 Total numbers of deals and value of private equity investments in Ukraine, 2010-2019**

Notes:
*Calculated values
**Done by author by source [49]

Using statistical methods of forecasting we can estimate future value of deals in Ukrainian PE industry, based on a trend line built on data from previous year observations.

Total investments (in $ mln.) follows polynomial trend line of second degree (accuracy of approximation R^2=0,7452=74,52%). The equation of the trend line is

$$y = 5{,}0714x^2 - 19{,}905x + 49 \quad (2.1)$$

So calculated values for future periods, based on a formula (2.1), are: $\hat{y}_{2018}$=280,64$ mln; $\hat{y}_{2019}$=357,09$ mln.

Number of deals (in absolute figure) follows linear trend (accuracy of approximation R^2=0,7989=79,89%). The equation of the trend line is

$$y = 10{,}167x + 16{,}75 \quad (2.2)$$

So forecasted values for two nearest future periods, based on a formula (2.2), are: $\hat{y}_{2018}$=108; $\hat{y}_{2019}$=118.

The main incentives which might cause the increasing of private equity activity in Ukraine lies in the fact that in 2018 our country reached 76 position in The World Bank Doing Business rating (+4 spots up, comparing with 2017) [56]; 43 position in The Global Innovation Index (+7 spots up, comparing with 2017); 83 position in The Global Competitiveness Index (+6 spots up, comparing with 2017) [57], which mean that Ukraine become more attractive for local and foreign investors, and as a result the investing activity and private equity activity will increase.

Also through the last two years there were some legal novels, which might make the investment climate in Ukraine more favorable for the investors. The year 2016 was marked by a significant novelty in the corporate law. In particular, successful steps were taken to reforming and bringing Ukrainian legislation into compliance with the European standards. Thus, the important and long-awaited

Law on the Protection of Investors Rights dated 7 April 2015 No. 289-VIII [7] was enacted, which came into effect on 1 May 2016. The Law introduces a number of novelties into Ukrainian corporate law aimed at improving the level of protection for domestic and foreign investors in Ukraine and, as a result, to improve Ukraine's position in the Doing Business rating. The Law abolishing the mandatory state registration of foreign investment dated 31 May 2016 No.1390-VIII [4] was finally adopted. The Law introduces the application-based principle for recording investments through submission of statistical information on investments made. The introduction of such changes will ensure the approximation of Ukrainian laws to the EU standards, simplify the procedure for attracting foreign investments and will facilitate the recovery of the State economy. In turn, the end of the year was marked by the adoption of the antiraider law dated 6 October 2016 No.1666-VIII [1], which abolishes the so-called "general" extraterritoriality principle and introduces the mandatory notarial certification of signatures of a legal entity's shareholders on resolutions of its general shareholders' meetings or other management bodies, amending the records contained in the Unified State Register regarding the legal entity.

With achievements of 2017 the reform of corporate legislation presents a comprehensive upgrade of the business sphere, stock market, investments and the economy of Ukraine in general, particularly: the system of corporate governance in joint stock companies was improved. Such mechanisms as squeeze-out/sell-out, escrow agreements the Law No.1983-VIII [3] were introduced simplified way of doing business and investments involvement by securities issuers: a substantially distinct approach to differentiation of public and private joint stock companies was introduced; creation of the transparent information field for the participants of a stock market; improved corporate governance in joint stock companies and the procedure of issuance of securities (the Law No. 2210-VIII) [5]. But in fact, the effects of these Laws are quite controversial as for today, due to specific Ukrainian market environment and problems of implementation. Corporate agreements were introduced as an efficient legal instrument for structuring of corporate relations of

shareholders, distribution of authority between shareholders, protection of minority shareholders, establishing restrictions on transferring shares, resolution of any future disputes between shareholders (the Law No. 1984-VIII [2].

A long-awaited legal base for formation, corporate governance and conduct of activities of limited liability companies was introduced. More comfortable and viable rules for companies and increased level of discretion of its participants related to issues of corporate governance comprised a huge step ahead for Ukraine to become an attractive field for business development the Law No. 2275-VIII [9].

Procedure of hiring of foreign professionals was simplified. The list of documents to be submitted for obtaining the residence permit is shortened, while the period of its validity for special categories of professionals is extended (the Law No. 2058-VIII [6]).

Also, on March 23, the Verkhovna Rada adopted in the second reading Law 5105 On Investment Activities, which improves the mechanisms of selection and financing of state investment projects. Adopted law:

•Simplify the procedure for obtaining state support for the implementation of investment projects by changing the role of the State Register of Investment Projects allowing for informative.

•Will give the right to local authorities to take decisions on granting consent for investment activities, simplify access to budgetary financing in the regions.

•Allow to make projects that have received state support, and state investment projects in the State Register of Investment Projects to monitor their implementation.

On May 23, was approved a law on the abolition of registration of foreign investments and the simplification of the employment of high-quality foreign specialists in Ukraine. This law will allow companies to quickly attract personnel to a specific job, in which there is a deficit in Ukraine. Thus, the development of one or another company can accelerate, which will enable it to create more quality products.

Mentioned laws have a chance to become the base for PE activity volume increasing over years to come, but to become a full member of European PE market, Ukraine has to bring domestic legislation in full accordance with legal frameworks, regulating entire European financial system.

But, at the same time, some constraints, which might block Ukrainian aspirations to develop PE industry, must be taken into account: first of all it is political instability; second, low level of financial services market development and inability of financial intermediators execute their functions properly; third, low level of investors rights protection; and, finally, discrepancy of domestic and world-wide legal base, regulating PE industry.

PART 3

FORMATION OF PREREQUISITES FOR THE DESIGN AND IMPLEMENTATION OF DOMESTIC PRIVATE EQUITY MODEL IN UKRAINE

3.1. Justification of the necessity of development of private equity funds in Ukraine

Private equity investments are experiencing growing interest, especially from the young, small and fast growing enterprises which face a financing problem when borrowing money from the banks due to strict bank requirements. Over past few years, Ukraine's private equity industry has seen some recovery, with several Ukrainian private equity funds announcing new investments from international financial institutions like EBRD. But at the same time, while some private equity funds with a focus on Ukraine have been actively fundraising in order to explore distress opportunities, and to acquire new stakes or build up their stakes in existing portfolio companies, other private equity funds with a focus on other markets have been seeking to exit Ukraine at any cost just because they have stayed in the country for too long and their Ukrainian investments have exceeded their normal investment lifecycle. That means that PE market in Ukraine is sufficiently undeveloped, comparing to others worlds' markets: nowadays domestic realities are characterized by low possibility for fundraising, investment and exit activity. So consequences of PE format implementation in Ukraine must be determined as for capital market, as for a country economy as a whole.

Private equity is an effective model for sustainable development and an important source of risk capital in countries with shallow capital markets and underserved SMEs. It is increasingly being used as an instrument for sustainable growth of the private sector in developing countries. Private equity, through a long-term horizon, a focus on value creation, a flexible investment approach and a strong position of influence to improve Environmental, Social and Governance (ESG) standards can provide a sustainable solution.

PE investing has been utilized for well over five decades by development finance institutions and by commercial PE firms as a method to invest in developing countries. Most of these firms envisage realizing economic and social change as a critical a part of their success. The International Finance Corporation (IFC) has also pointed out that the vast majority of private equity capital flows to emerging markets is in the form of growth capital using relatively little leverage. The most recent development is the adoption of the model by ‘impact investors’, who specifically aim to realize a beneficial social or environmental impact alongside a financial return. There could be identified four main characteristics of the PE model which could explain why it can be appropriate for developing and enhancing the private sector of emerging economies.

1. Long-term investment horizon: PE fund managers have a long-term investment horizon, with the regular lifespan of a closed-end PE fund being ten years and the average holding period of an investee company being five years. The long-term commitment and involvement of a private equity investor ensures that there is sufficient time and a stable environment to put an expansion or professionalization plan to work. This is a prerequisite for successfully growing a business in developing market, like Ukrainian. Nowadays undeveloped financial services market have no players, which are able to provide needed amount of capital for such a long time period, or the interest rate are too high. PE’s patient capital could be appropriate option for SMEs in Ukraine in the period of political instability.

2. Value creation: a strong focus on improving a company through active management such as through board seats is key to the PE model. Fund manager team members often have previous boardroom experience, a good business network and specific sector or technological expertise. Companies can tap this expertise and use the network of its investor. This focus on growth and knowledge transfer is unique to the PE model and is in great demand in developing countries. Lack of professionals on the labor market make it impossible for young new-established companies to attract high level labor force, which leads to lower

growth rate of the company. Attraction of high-skilled managers with wide network within the sphere could boost the company's growth and expand Ukrainian start-ups industry.

3. Flexible investment approach to fill the financing gap: PE can be flexible, allowing the provision of tailor-made financing solutions appropriate for the individual company's cash flows. It can target companies in all stages and sectors, including SMEs. The World Economic Forum has coined SMEs in emerging markets the 'missing middle' – enterprises that are too large to receive finance from microfinance institutions and too small for bank finance. Yet at the same time SMEs are the engine of social and economic development, being the primary source of new job creation and a key contributor to GDP growth. However, SMEs in emerging markets are often constrained due to inadequate access to capital. In fact, according to IFC data up to 68% of formal SMEs in developing countries are unserved or underserved financially. The fundamental problem is that banks are wary to give out loans to SMEs, as they often lack fixed assets and have low cash reserves, or charge excessively high interest rates. PE offers an alternative: it can provide capital without these high interest rates, by participating in a share of the profits and sharing in capital gains instead. In addition, PE has the ability to target and boost all sectors of a developing economy, creating a diversified portfolio, unlike stock market investments in these countries.

4. Opportunity to improve ESG: PE investors are well-positioned to improve the environmental, social and governance (ESG) management of a business, mainly for two reasons. Firstly, due to a general lack of knowledge of the business case for sustainability in developing markets, PE fund managers can play a crucial role in introducing or improving ESG management. Secondly, PE's long-term horizon provides the prerequisite for ESG improvements to really materialize. Awareness among fund managers that ESG can mitigate risks and offer opportunities to add value only notably appeared over the last few years, but is gaining recognition rapidly. According to research by PwC [55], 71% of private equity firms currently include ESG aspects in their due diligence processes. Apart

from managing risks, ESG management also provides opportunities for fund managers to generate more value. There is often potential for substantial cost savings through energy efficiencies, reduced use of resources or improved waste management. Therefore ESG management can mitigate risks, improve the value of a business and benefit society.

A shortage of capital is still considered as one of the major constraints to private sector development in developing countries. As it was mentioned before, PE can be a highly effective model for providing capital and growing businesses sustainably in developing economies. It can particularly be suitable for realizing inclusive growth of SMEs, as it can create several characteristics of an enabling environment for SMEs.

Also, literature overview concludes that development of the capital market has a positive effect on GDP growth. One of the indicators, which can show the level and tendency of development of capital market in one country, is volume of investments (i.e. PE investments) and the growth rate of these investments. Positive sign of this indicator mean that country attract more investments on the year-to-year basis. Also this indicator could be analyzed with relation to GDP growth rate to determine how changes in factor parameter (growth rate of investments) will affect changes in dependent value (growth rate of GDP).

While the European format of private equity proceedings was chosen as a base for domestic approach, the correlation between growth rate of PE investments in Europe and growth rate of European GDP must be investigated in order to enable Ukrainian GDP growth rate forecasting for future periods.

The data for growth rate of PE investments in Europe and growth rate of European GDP is presented in Table 3.1.

Table 3.1

Dynamic of European PE investments growth rate and European GDP growth rate in 2010-2017*

Year	European PE investments, growth rate,%.	European GDP growth rate, %.
2010	64,29	2,08
2011	8,70	1,63
2012	-16,00	-0,85
2013	2,38	-0,24
2014	9,30	1,42
2015	19,15	2,05
2016	1,79	1,89
2017	28,07	2,39

Note: *Done by author by sources [34, 49]

Analysis of the data shows that values, presented in a table are correlated. Correlation coefficient is Cc=0,6638=66,38%, which mean that the strengths of correlation is moderate; positive changes in factor value “x” (European PE investments growth rate) will cause positive changes in dependent value “y” (European GDP growth rate). The following scatterplot, presented in a Figure 3.1 illustrates the correlation between capital market development (measured by PE investments growth rate) and GDP growth rate.

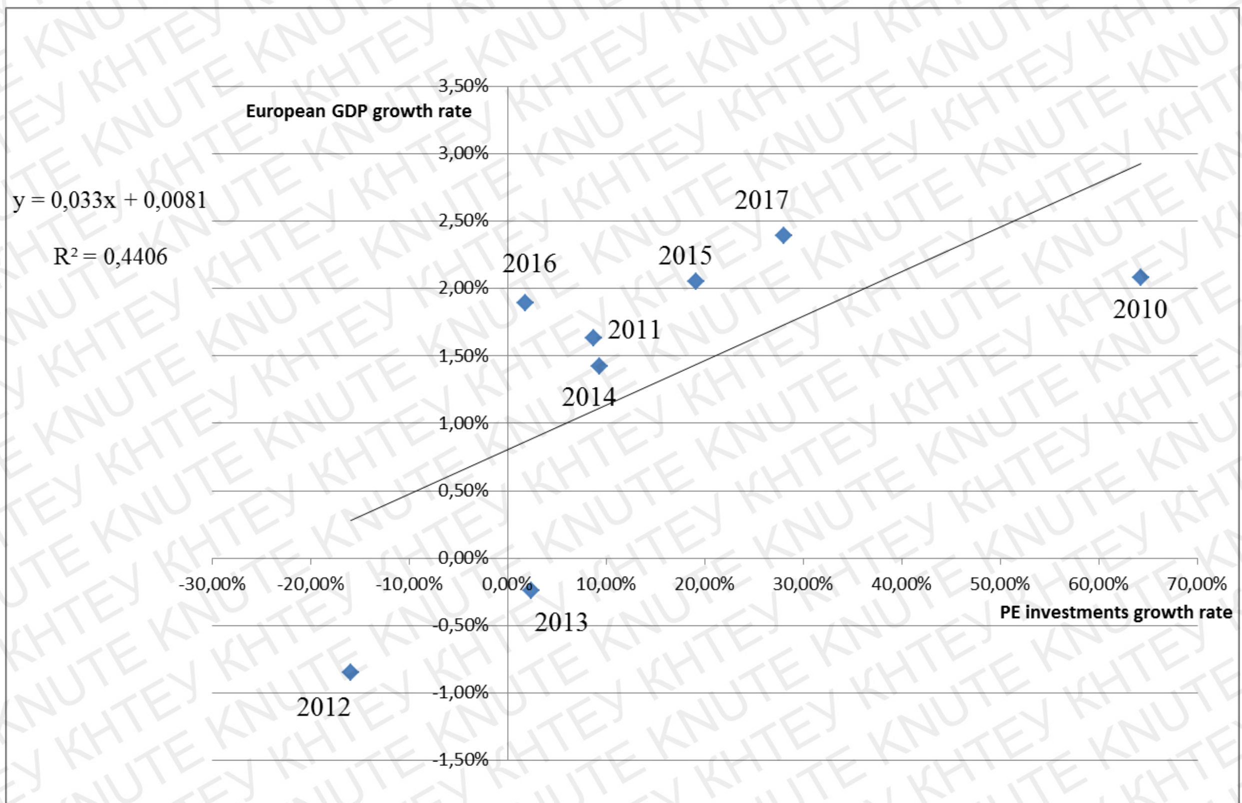


Figure 3.1 European GDP growth rate distribution 2010-2017*

Note: *Done by author by source [34, 46]

The distribution of dependencies follows the linear trend, described by formula (3.1), which in this case represents the average dependency of GDP growth rate from PE investments growth rate.

$$y = 0{,}033x + 0{,}0081 \quad (3.1)$$

The coefficient of determination is quite low (R^2=0,4406=44,06%) that means that forecasts, based on this equation will have some level of error.

"b" coefficient has a positive sign, which means that increasing of factor, will cause the increasing in dependent value.

Assuming that Ukraine will have the same legal prerequisites of PE activity as Europe has, we can use the equation of a trend line, described by formula (3.1), to predict future value of Ukrainian GDP growth rate, based on PE investments growth rate in Ukraine.

Using the data, obtained as a result of statistical modeling in chapter 2.3, Table 3.2 is developed, and further GDP growth rate in Ukraine can be forecasted.

Table 3.2

Dynamic of private equity investments growth rate in Ukraine 2010-2019**

Year	PE investments in Ukraine, $mln.	Growth rate, %
2010	20	
2011	24	20,00
2012	59	145,83
2013	89	50,85
2014	39	-56,18
2015	132	238,46
2016	88	-33,33
2017	259	194,32
2018*	280,6384	8,35
2019*	357,09	27,24

Notes:
* Forecasted values
**Done by author by source [49]

Using the formula (3.1), GDP growth rates in Ukraine for 2018 and 2019 years can be calculated. Forecasted values for future periods are: $\hat{y}_{2018}$=1,09 %; $\hat{y}_{2019}$=1,71%.

Obtained values are quite low, but while the error in such model is significant, further elaborations of this model can become directions of topic development.

Anyway, achieved results in correlation between PE investments growth rate and country's GDP growth rate investigation shows that increasing in PE activity (increasing the volumes of investments) has a positive influence on country GDP growth in general. So while PE has a lot of positive effects on country's capital market development and buildout of a country as a whole, we can state that domestic approach, based on European practice must be developed in Ukraine.

3.2. Design of the private equity model applicable for Ukraine

To bring the Ukrainian corporate law into compliance with the European standards, it is primarily necessary to adopt the laws, regulating the entire financial system and, particularly, sphere of PE investments. Adoption of the new laws will allow considerably improve prerequisites for PE firms proceeding and will create an attractive alternative for many foreign investors, as well as Ukrainian companies.

As it was mentioned, European approach to PE is based on two main documents, regulating the financial system: Alternative Investment Fund Managers Directive (AIFMD) and the European Venture Capital Regulation (EuVECA). In European governing practices, Directives, issued by over-countries' authorities must be transported into national laws to ensure proper functioning of legal frameworks, but the Regulations, does not need to be transposed into national law, but just must be taken into account by parties included into activity, regulating by this document. So the Directive must be transposed into Ukraine's national laws, while the EuVECA just must be adapted for usage for Ukrainian companies with some minor legislative changes.

One of the most important features of European approach to private equity regulation is that PE activity is identified as a financial service. So the private equity proceedings in Ukraine must also be recognized as a financial service and must become the legal part of financial services market of Ukraine. For this reason it will be in sphere of regulation of authorities and laws, regulating the financial services environment in Ukraine.

As we know, European Union legislation defines different vehicles for setting up an equity investment: Banks; Investment firms and Closed-end funds. All of mentioned entities acts as intermediaries between investors seeking returns in an alternative asset class and non-public companies with a need for financial resources. So, European format is eligible for domestic economy, because legal entities, used for PE investments already exist.

Alternative Investment Fund Managers Directive (AIFMD), which sets out an EU-wide standardized framework for managing and marketing alternative investment funds, must become the base for domestic legal frameworks for PE activity governance. It establishes a legal framework for the authorization, supervision and oversight of managers of a range of alternative investment funds (AIFM), including private equity funds.

Directive maintain following rules, which will be transported into Ukrainian national legal documents to ensure compliance with EU-wide frameworks:

1) To operate in the EU, fund managers are required to obtain authorisation from the competent authority of their home country. In Ukraine the authority, which will provide such authorization must become NSSMC (The National Securities and Stock Market Commission) as current supervisor for asset management companies under the Ukrainian legislation. Also such authority might be National Bank of Ukraine (as in other European countries) or National Securities and Stock Market Commission. There is no need for creation new specialized governing body. To obtain authorization, AIFMs will have to hold a minimum level of capital in the form of liquid or short-term assets. No AIFM shall be allowed to manage an AIF unless it has been authorised in accordance with the Directive. The regulator must inform European Securities and Markets Authority (ESMA) on a quarterly basis of authorisations granted or withdrawn, and ESMA will keep a central public register of all authorised AIFM. Once authorised, an AIFM will be permitted to provide management services to AIFs domiciled in any Member State and to market the securities of the AIFs it manages to “professional investors” across the EU. This is a vital part of format implementation because it will open European market for the Ukrainian PE firms, and, on the other hand, will allow foreign PE funds to invest in Ukraine without any undesired circumstances.

2) AIFMs will be required to assure the competent authority of the robustness of their internal arrangements with respect to risk management. This includes a requirement to disclose, the main markets and instruments in which they trade, their principal exposures and their concentrations of risk. The Directive

mandates that an AIFM implement risk management systems designed to measure and monitor all risks to which the AIFs it manages may be exposed by virtue of their investment strategies. It further requires the separation of portfolio and risk management functions within the operational environment of an AIFM. AIFMs are required to take all reasonable steps to identify conflicts of interest that arise in the course of managing one or more AIFs, and then to manage and monitor those conflicts of interest in order to prevent them from adversely affecting the interests of the AIF and its investors. The Directive also requires an AIFM to implement systems designed to manage liquidity risk and to conduct regular stress tests of these systems under both normal and exceptional market conditions. These measures are designed to prevent the potential buildup of systemic risk.

3) AIFMs will be required to ensure that the funds they manage appoint an independent depositary, for example a bank or investment firm, which is responsible for overseeing the fund’s activities and ensuring that the fund’s assets are appropriately protected. A depository’s function is predominantly the safekeeping of the assets of the fund, and it is intended to protect investors against losses arising from fraud of the AIFM. AIFM come under an obligation to establish appropriate and consistent procedures for the valuation of the assets of each fund under management. AIFM also come under an obligation to put in place remuneration policies and practices for certain senior staff, designed to promote effective risk management. In Ukraine`s case such a depositary must become legal entity, allowed to provide such type of activity and licensed by NSSMC (The National Securities and Stock Market Commission) which currently is the case for the ‘depositary institutions’ under the domestic legislation.

4) Another step, which should be taken to bring domestic governing framework in accordance to AIFMD is regulation of leverage. The directive introduces specific requirements with regard to leverage, i.e. the use of debt to finance investment. Competent authorities have the right to set limits to leverage in order to ensure the stability of the financial system. AIFM are required to set leverage limits in respect of each AIF they manage. AIFM must be able to

demonstrate that the leverage limits it has set are reasonable and are complied with at all times. AIFM are required to disclose to AIF investors, the circumstances in which the AIF may use leverage, any restrictions on the use of leverage, and the types, sources and maximum level of leverage permitted. AIFM managing one or more AIF employing leverage on a substantial basis shall make available to the competent authorities information including the overall level of leverage employed by each AIF it manages, and a break-down between leverage arising from borrowing of cash or securities and leverage embedded in financial derivatives. If it is considered necessary in order to ensure the stability and integrity of the financial system, the AIFM's regulator may impose limits on the leverage that a particular AIFM may employ or set other restrictions on the management of the AIF. ESMA will have the power to determine that the leverage employed by an AIFM, or by a group of AIFM, poses a substantial risk to the stability and integrity of the financial system. If ESMA makes such a determination then it can issue advice to the AIFM's home Member State regulator specifying remedial measures (which may include leverage limits).

5) The AIFMD includes a number of measures designed to increase transparency, which also must be adopted into our legal base. First, the Directive sets out the information which must be disclosed to investors before they invest in a fund, including the investment strategy and objectives of the fund, the identity of the AIFM, its pricing methodology and valuation procedure, all fees and charges, and the latest net asset value of the fund and historic performance information, where available. In order to encourage diligence amongst their investors, AIFMs are required to provide a clear description of their investment policy, including descriptions of the types of assets and the use of leverage. An annual report for each financial year has to be made available to investors on request. The Directive also requires ongoing disclosure by AIFM. Annual reports in respect of each EU or Ukrainian fund managed by an AIFM and each fund it markets in the EU must be provided to the AIFM’s regulator. The Directive contemplates periodic disclosure to both investors and competent authorities regarding: (a) the percentage of the

AIF's assets which are subject to special arrangements arising from their illiquid nature; (b) any new arrangements for managing the liquidity of the AIF; and (c) the current risk profile of the AIF and the risk management systems employed by the AIFM to manage these risks. An AIFM will also be required to provide information to the competent authorities regarding the main instruments in which it is trading, markets of which it is a member or where it actively trades, and on the principal exposures and most important concentrations of each of the AIF it manages.

6) Regulation is also imposed at the level of the portfolio company. The Directive imposes disclosure obligations on the acquisition of major holdings (starting at 10 per cent of voting rights) in non-listed EU or Ukrainian companies. It imposes more onerous obligations on AIFM whose AIF acquire "control" of EU companies (whether or not listed). The AIFM will need to make certain disclosures to the regulator, and to the relevant non-listed company and its shareholders and employees (or their representatives). This information includes: the identity of the AIFM that have control; the policy for preventing and managing conflicts of interest, in particular between the AIFM, the AIF and the non-listed company/issuer and the policy for external and internal communication relating to the non-listed company/issuer, in particular as regards employees.

7) There are also rules designed to prevent asset stripping. Where an AIF acquires control of a non-listed company or an issuer, the AIFM is subject to the anti-asset stripping provisions. For a period of two years, the AIFM must act against any distribution, capital reduction, share redemption or acquisition of own shares by the company. When a private equity fund acquires a controlling interest in a non-listed company the AIFM shall not, within 24 months following the acquisition, be allowed to facilitate, support, instruct or vote in favor of any distribution, capital reduction, share redemption or acquisition of own shares by the company and must use its best endeavors to prevent the same from occurring. The obligation is therefore placed on the AIFM rather than on the portfolio company.

Ukraine, as others EU countries may choose not to apply the directive to smaller AIFMs, i.e. funds with managed assets below €100 million if they use leverage and with assets below €500 million if they do not. But those funds still will be the subject to minimum registration and reporting requirements, presented in Regulation (EU) No 345/2013 on European venture capital funds (EuVECA). Usage of this Regulation is not mandatory, and it does not have to be introduced into national laws, but adoption of EuVECA will let smaller PE funds provide their activity into Ukraine, and what is even more important, will organize the conditions in which smaller new-established Ukrainian PE funds will have an access to EU-wide PE market. This regulation sets out the criteria which managers of private equity funds must meet in order to market their funds to investors across the EU under a "European Venture Capital Fund" label and without needing to comply with the demands of the Alternative Investment Fund Managers (AIFM) Directive. In order to qualify for this EuVECA designation the Regulation introduces requirements relating to the investment portfolio, investment techniques and eligible undertakings that a qualifying fund needs to meet. It also sets out uniform rules on which categories of investor a qualifying fund may approach and on the internal organization of the managers that market such qualifying funds.

Managers that intend to market a qualifying venture capital fund under the EuVECA label must first inform the competent authority in their home member state (in Ukraine it will be NSSMC) of their intention and provide to it the information including details about the owners and relevant staff of the manager, as well as about the fund and its marketing intentions. The manager must also give a narrative description of the arrangements which have been made with a view to fulfilling the on-going compliance requirements of the Regulation.

Another key issue on joining the EU market is taxation. Taxation is quite tricky because it's different in every country. There is no single approach which can regulate taxation within the EU format of equity investments. Generally all EU Member States are party to two European Directives which remove withholding tax on dividends, interest and royalties in most cases – the Directive

on parent companies and subsidiaries in different Member States (commonly known as the EU Parent-Subsidiary Directive) and the Interest and Royalties Directive. But still there are some differences in taxation mechanism. Detailed approaches to taxation are reviewed in Attachment J. For Ukraine own approach to taxation mechanism based on world best practices is offered in Table 3.3.

Table 3.3

Taxation mechanism for private equity participants in Ukraine*

		Entities involved in taxation mechanism		
		Vehicle	Investor	PE-backed company
Areas of impact	Taxation on capital gains	**Tax transparency.** Is a special case where the flat tax is equal to 0%. That means that the vehicle doesn't pay taxes and cost and revenues pass through the investor.	**Flat tax mechanism.** Which mean that an investor has to pay a lower amount of taxes compared to income taxes in the country.	Non relevant
	Taxation on dividends	Non relevant	Non relevant	Non relevant
	Incentive to start up	Non relevant	Non relevant	**Mark-down mechanism.** If the company manages a startup, it benefits of a markdown, that means decreasing of the tax rate.
	Incentive to R&D	Non relevant	Non relevant	**Mark-down mechanism.** If the company invests in R&D, it benefits of a markdown, that means decreasing of the tax rate, in proportion to such investments.
	Taxation of the debt to equity ratio	Non relevant	Non relevant	**Dual income taxation.** Which means to give tax incentives if the company collects money only through equity.

* Note: Done by author by sources [15]

Offered mechanism makes PE more attractive for investors, because of lower tax pressure; and stimulate R&D activity as well as new companies launching, which may have a good consequences for domestic economy.

On the level of fund, there are also some features that must be taken into account and be implemented in domestic format of private equity to ensure full compliance with EU private equity proceeding frameworks.

First of all, in Europe, there is an internal code of activity regulating the relationship between investors and managers which consider: the size of the vehicle, the assets in which they want to invest, the amount of the management fee, the amount of the carried interest etc. Therefore, in Ukraine such relations will also be under the regulation of internal code of activity and current Law On CII, which already introduced requirements on some of these matters [8].

Another important obstacle which is typical for EU formats is distribution of capital earnings between Limited Partners and General Partners: so-called “Distribution Waterfall”. European funds almost always use a more LP-friendly waterfall, whereby carry is calculated on a whole-fund basis. Under the European waterfall, the fund must first return all drawn capital back to its investors (the LPs) ahead of sharing the incremental profits between the LPs and the GP.

To become the full part of European financial market, first Ukraine has to transpose the European fund law under the EU-UA Association Agreement and get the positive assessment by the European Commission which should allow for the EU market access. Offered format of domestic PE proceeding regulation will bring our legislation in compliance with European practice of PE governing and increase the chance of Ukraine’s integration into European capital market.

That means Ukraine will have a possibility to ease the access to long-term patient financing for the economy, and on the other hand, local funds will be able to invest in foreign companies in order to obtain capital gains. But this aspect also depends on the NBU currency and capital controls lifting, which is currently underway, as well as on the development of the post-trading capital markets infrastructure and international correspondence relations of the National Depository of Ukraine, which is also being done by the NDU, in coordination with NBU, but both will take time.

3.3. Roadmap for implementing proposed model of private equity in Ukraine

European Union format of private equity proceedings, which was chosen as a base for Ukrainian domestic format, is suitable for Ukraine's economy, but its implementation require a lot of structural changes and legal improvements to be taken to bring our financial services market governing in accordance to Europe-wide framework of financial market organization. This developed domestic private equity model and roadmap is intended to support Ukraine's efforts to build economic growth, create jobs and raise the material standard of living for all of its residents. This is a set of suggested decisions to be taken by the Government under that framework.

This catalyst function of financial market – matching investors with entities seeking capital – helps ease 'financial friction' for the economy. Without an organized, centralized way to raise funds, companies and governments would be required to seek investors "door to door", approaching each on an individual basis and repeating their proposition endlessly. The capital market offers "one stop shopping" for both investors and issuers. Each investor can come to the market to see all available choices. Each issuer can come to the market to address all interested investors. All of deficiencies which now characterize the current state of local PE market can be remedied. The required actions, stated in positive terms, can be organized along 4 sets of Strategic Goals, also presented in Attachment K:

I. Increasing investor interest and protection of investors' rights
II. Making the PE investments more attractive to SMEs
III. Ease of doing business
IV. Development of investment sector

Broadly speaking, this strategy represents a change of approach and vision for the PE market.

So, to make our legal base compliant with European, further strategic goals and needed actions must be undertaken:

I. Increasing investor interest and protection of investors' rights

1. Increasing investor interest

a) Solving legal obstacles by adopting AIFMD to enable authorization process for funds. According to European legislation only funds which are fully compliant with AIFMD are allowed to operate on the single EU market, and also EU-based funds are able to provide their services only on markets, legal framework of which is fully compliant with mentioned Directive. So adoption of AIFMD must become the first step on Ukraine's way to the European PE market: it will allow foreign funds to invest in Ukrainian companies as well as Ukraine-based funds to interact with EU-based companies.

b) Improving Ukraine's position in international ratings (i.e. Morgan Stanley Capital International rating, Doing Business rating, The Venture Capital & Private Equity Country Attractiveness Index etc.). It will increase attractiveness of Ukrainian companies for foreign investors and, as a result will open the huge source of needed capital for Ukrainian SMEs.

c) Providing important Information in English. This step will ease the process of due diligence for foreign funds, and will cause the increasing of investors' interest to Ukrainian companies.

d) Revising the tax treatment and withholding for foreign investors. The vital task is to create clear approach to tax treatments both for foreign and local investors and avoid double-taxation.

2. Legal framework arrangement for investors' rights protection.

a) Protection of minority shareholders rights. Is needed in order to ensure protection of investors, aimed to obtain minor share within the company.

b) Adoption Shareholders Agreement clauses according to European legislation. All the internal relations between shareholders of a company must be predetermined in Agreement and be compliant to rules, which are in forth in European Union. It will let to clarify rights and responsibilities of all, even minority shareholders and will protect rights of all parties.

c) Implementation laws on protection of the Intellectual Property. This step will stimulate Research&Development activity within the country and will enforce investing in high-intelligence spheres of economy.

d) Implementation of risk management system for funds under AIFMD frameworks. This step aimed to solve conflict of interest clauses and will stimulate local funds to provide full and transparent information to the investors.

II. Provision of capital for Small and Medium Size Issuers

1. Inserting private equity and venture capital funds to the list of investment institutions as separate legal entities. While legal entities, allowed to run PE investments are not identified, they could not provide their activity properly. Set of such entities must be presented in laws with their power and responsibilities. Only after this step execution PE funds will be able to operate on a financial services market among other financial institutions.

2. Ease of access for PE capital to SMEs by marketing through conferences, business forums and meetings with investors. This step will increase interest from the companies' side, and also will show to PE investors that in Ukraine there are a lot of target companies for their investments.

III. Ease of doing business

1. Simplifying the process of setting up business and liquidation of the business. Will increase Ukraine's position on Doing Business rating; also will stimulate organizing of private equity firms.

2. Decreasing number of regulation authorities including by merge and/or delegation of their functions to self-regularity institution. There is no need to create new separate legal entity to organize oversight in the sphere of private equity. Responsibilities of supervision could be divided between UVCA, UAIB and NBU.

3. Introduction clear rules for controlling bodies, including possibility of sanctions application. All full powers of regulation authorities must be clearly stated to avoid overlapping of oversight spheres.

4. Clear and transparent licensing procedures and bases. Single base of all PE market players must be introduced to provide transparent information for all members.

5. Ensuring free and easy cross-border movement of capital. The vital step to ensure foreign investments into Ukrainian economy.

IV. Development of investment sector

1. Filling the gaps in the market.

a) Tax incentives to certified business angels investing in early-stage companies. Those incentives are offered into developed approach to taxation within domestic PE format; it will result increasing of R&D activity of young companies and stimulate start-ups to faster development on a market.

b) Supporting and initiating creation of co-investment vehicles and matching funds; supporting and initiating attracting the fund-of-funds and other investment vehicles to Ukraine. Diversity pf investment vehicles on a market will increase the competitiveness on the investors' side, and will provide a wide array of options for companies, looking for the capital.

2. Privatization of non-strategic government companies.

The main idea behind proposed actions is to organize capital market as a whole, and the sphere of PE as a part of it. While the European private equity format was chosen as base for domestic approach, in order to achieve high-developed PE industry main European regulation documents must be transported into national legislation. First of all AIFMD must be implemented to domestic regulation on a governance and institutional level.

To be compliant with the Directive, following steps must be taken:

1) Appoint competent authority to provide authorization for PE funds.

2) Oblige PE funds to implement wide-spread risk management system to avoid potential buildup of systemic risk.

3) Oblige AIFMs to ensure that the funds they manage appoint an independent depositary, for example a bank or investment firm, which is

responsible for overseeing the fund's activities and ensuring that the fund's assets are appropriately protected.

4) Oblige AIFMs to regulate the leverage.

5) Increase transparency by disclosure investment strategy and objectives of the fund, the identity of the AIFM, its pricing methodology and valuation procedure, all fees and charges, and the latest net asset value of the fund.

All mentioned steps are vital for domestic private equity industry development, because they will bring Ukrainian national legislation in accordance with European approach to private equity regulation and allow foreign investors to invest in Ukrainian companies, as well as Ukrainian investors to search for investment options on the European market. The sequence of needed actions is presented into Attachment L, with the parties, which are responsible for its implementation. While most of further actions require legislation changes, Cabinet of Ministers and Verkhovna Rada of Ukraine are in charge of majority of further steps. Other parties which are involved into legislation adoption process are National Commission in Financial Services (NCFS), because it regulates most activities into Ukrainian financial market, and State Fiscal Service of Ukraine, because a lot of amendments require changes in the taxation policy of Ukraine. UVCA, as a self-regulatory organization on a PE market of Ukraine also must be an active player in the process of private equity industry development in Ukraine.

So, novelties, which must be implemented, will significantly change not only our domestic approach to private equity investments, but also increase efficiency of entire financial services market, and, as a result, welfare of the country, and allow to become a full-member of European private equity market.

CONCLUSIONS AND PROPOSALS

In the final qualification work the mechanism of functioning of private equity funds and principal approaches to private equity proceedings regulation on main global markets were considered. By the result of execution of this research following conclusions and recommendations were identified.

By the economical nature, private equity is a form of equity consisting of investors and funds that make investments directly into private portfolio companies not listed on a stock exchange. Private equity funds provide capital to a wide array of companies, ranging from business startups to very large and mature companies. One of the reasons the private equity industry exists is that, in many cases, companies have needs for capital which, for various reasons, cannot be raised from the public markets. Private equity investments are characterized firstly by active ownership, which entails that the private equity companies work closely with the management of the acquired portfolio companies to create value by contributing capital and complementary expertise. There must be mentioned that PE is related to alternative types of asset, and it's main role of the on the capital market is to be an asset class to be invested in predominately by huge institutional investors who have the patience for longer-held bets and a need for investment portfolio diversification; and at the same time to be the source of capital for small and medium enterprises, growing and mature companies.

The development of the private equity industry has occurred through a series of boom and bust cycles that have been ongoing since the middle of twentieth century. Historically, the USA has been the largest PE market worldwide and is usually viewed as the founder of the modern PE. The first PE-style company "The War Finance Corporation" was established in 1918, but only when Small Businesses Investment Companies were established in 1958, modern PE industry was born. Whole timeline of PE industry development is represented by growth and decline cycles, caused by different events, but nowadays PE industry

overpasses the decade of stable growth after the epic drop during the 2008 financial crisis.

World-wide, nowadays there are two different formats of private equity investments. On the one hand, there is the European Union format which is regulated by the directives of the European Union. And on the other hand, the so-called Anglo-Saxon format, which is regulated by the laws of the U.S. and U.K. The main differences between those to formats are: 1) European Union format implies that private equity is a financial service, but according to Anglo-Saxon format, private equity is not a financial service, but it is an entrepreneurial activity like managing whatever kind of company. 2) Legal entities which could run such a specific type of activity are also differs in those formats, as well as legal documents, regulating this type of investments. 3) Internal rules, which arrange specifications of PE firms organization and internal rules of proceeding are also differs in mentioned approaches.

It was investigated that global private equity and venture capital industry has experienced significant growth during the past 10 years after financial crisis (+ 94%) [54] and has become an increasingly important source of finance and expertise for companies seeking to achieve their growth aspirations. Assessment of the market capacity shows that even regardless of some decline in performance in 2008-2009, private equity nowadays is a huge market (ab. 600$ bln.) [54] with a high potential to growth.

PE industry in Ukraine is also exist but it currently is significantly undeveloped in comparison with other European countries, which have already implement the common European rules and laws regulating entire financial system, and PE investments, as a vital part of it. The indicator which represents the total value of private equity investments as a percent of GDP in Ukraine in 2017 year is equal 0.039% which is 11.44 times lower then average in Europe (0.45%). Ukrainian PE industry now also faced a lot of problems such as undeveloped legal base of funds functioning, low possibility to attract foreign investments, lack of target companies and lack of local investors, willing to invest in such type of fund.

European Union is a strategical partner of Ukraine on its way to economic development, and signed Association Agreement between EU and Ukraine implies strengthening of relationship between them. So European format of private equity proceedings regulation was chosen as an appropriate base for Ukrainian domestic format of PE governing development. But, according to European rules, legislation of Ukraine in this particular sphere must comply with EU-wide legal frameworks, to become the full member of the market and get the possibility to attract foreign investments and provide PE services on the common market. Model offered in this research also shows that bringing in accordance our legal base and increasing level of private equity investments activity, will also have a positive influence of Ukrainian GDP growth rate.

So, separate, country-specific approach to private equity in Ukraine has become the result of this work. It is based on main regulative documents of European Union and implies adoption of some Directives and Regulations into Ukrainian domestic legislation. This step will allow Ukraine become full compliant with European standards and join the entire market as a full member. To implement offered format also have been set four strategic goals, such as:

1) Increasing investor interest and protection of investors' rights;

2) Making the PE investments more attractive to SMEs;

3) Ease of doing business

4) Development of investment sector.

The Roadmap, which represent the set of needed actions, its rationale and entities which are responsible for its execution is also offered by the result of research accomplishing.

REFERENCES

1. Про внесення змін до деяких законодавчих актів України щодо вдосконалення державної реєстрації прав на нерухоме майно та захисту прав власності: Закон України від 6 жовтня 2016 No.1666-VIII [Електронний ресурс]. – Режим доступу: http://zakon.rada.gov.ua/laws/show/1666-19
2. Про внесення змін до деяких законодавчих актів України щодо корпоративних договорів: Закон України від 23 березня 2017 No. 1984-VIII [Електронний ресурс].– Режим доступу:http://zakon.rada.gov.ua/laws/show/1984-19
3. Про внесення змін до деяких законодавчих актів України щодо підвищення рівня корпоративного управління в акціонерних товариствах: Закон України від 6 січня 2018 No.1983-VIII [Електронний ресурс]. – Режим доступу: http://zakon.rada.gov.ua/laws/show/1983-19
4. Про внесення змін до деяких законодавчих актів України щодо скасування обов'язковості державної реєстрації іноземних інвестицій: Закон України від 31 травня 2016 No.1390-VIII: [Електронний ресурс]. – Режим доступу: http://zakon.rada.gov.ua/laws/show/1390-19
5. Про внесення змін до деяких законодавчих актів України щодо спрощення ведення бізнесу та залучення інвестицій емітентами цінних паперів: Закон України від 7 березня 2018 No. 2210-VIII [Електронний ресурс]. – Режим доступу: http://zakon.rada.gov.ua/laws/show/2210-19
6. Про внесення змін до деяких законодавчих актів України щодо усунення бар'єрів для залучення іноземних інвестицій: Закон України від 23 травня 2017 No.2058-VIII [Електронний ресурс]. – Режим доступу: http://zakon.rada.gov.ua/laws/show/2058-19
7. Про Закон України від 07.04.2015 № 289-VIII "Про внесення змін до деяких законодавчих актів України щодо захисту прав інвесторів".: Інформаційний листю [Електронний ресурс]. – Режим доступу: http://zakon.rada.gov.ua/laws/show/v0474600-16

8. Про інститути спільного інвестування: Закон України від 06 січня 2018 5 липня 2012 року No.5080-VI (зі змінами) [Електронний ресурс]. – Режим доступу : http://zakon.rada.gov.ua/laws/show/5080-17

9. Про товариства з обмеженою та додатковою відповідальністю: Закон України від 6 лютого 2018 No.2275-VIII [Електронний ресурс]. – Режим доступу: http://zakon.rada.gov.ua/laws/show/2275-19

10. Bance, A. (2004). Why and how to invest in private equity. EVCA Investor Relations Committee Paper.

11. Berger, A. N., & Udell, G. F. (1998). The economics of small business finance: The roles of private equity and debt markets in the financial growth cycle. Journal of Banking & Finance, 22(6), 613-673.

12. Bodie, Z., A. Kane and A. J. Marcus (2005). Investments. Sixth edition. McGraw-Hill, New York.

13. Cambridge Business English Dictionary. Cambridge University Press, 2011

14. Capizzi, V. (2004). The constitution of a venture capital company: The case of Italian closed-end funds. Venture Capital. A Euro-System Approach. Springer-Verlag: Berlin

15. Caselli, S. (2009). Private equity and venture capital in Europe: markets, techniques, and deals: Academic Press.

16. Central and Eastern Europe Statistics 2017; Economic outlook by Invest Europe.

17. Demaria, C. (2010). Introduction to Private Equity. John Wiley & Sons.

18. Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 Text with EEA relevance [Electronic resource]. – available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32011L0061

19. Dodd-Frank Wall Street Reform and Consumer Protection Act [Public Law 111–203] [As Amended Through P.L. 115–174, Enacted May 24, 2018]. [Electronic resource]. –available at: https://legcounsel.house.gov/Comps/Dodd-

Frank%20Wall%20Street%20Reform%20and%20Consumer%20Protection%20Act.pdf

20. Economist (2003): "The charms of the discreet deal." The Economist July 5th.

21. European Comission: Applying EU law. [Electronic resource]. – available at: https://ec.europa.eu/info/law/law-making-process/applying-eu-law_en

22. European Securities and Stock market Authority: GUIDELINES AND TECHNICAL STANDARDS [Electronic resource]. – available at: https://www.esma.europa.eu/regulation/trading/market-abuse

23. EuVECA essentials. European private equity and venture capital association.

24. EuVECA: Regulation (EU) No 345/2013 of the European Parliament and of the Council of 17 April 2013 on European venture capital funds Text with EEA relevance [Electronic resource]. – available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32013R0345

25. EVCA (2007): "Guide on Private Equity and Venture Capital for Entrepreneurs."

26. Fenn, G. W., L. W. . S. P. (1995): "The economics of the private equity market." Federal Reserve Bulletin (168): pp. 1–69.

27. Fenn, G. W., N. Liang and S. Prowse (1997). The private equity market: An overview. Financial Markets, Institutions & Instruments, 6(4), 1-16

28. Financial Conduct Authority; International standards and regulations [Electronic resource]. – available at: https://www.fca.org.uk/about/international-standards-regulations

29. Friedman, M. J. (2009). Outline of the U.S. economy. Bureau of International Information Programs. United States Department of State.

30. Gompers, P. A. & J. Lerner (2011): "The venture capital revolution." The Journal of Economic Perspectives 15(2): pp. 145–168.

31. Gompers, P. and J. Lerner (1996). The use of covenants: An empirical analysis of venture partnership agreements. Journal of Law and Economics, 39(2), 463-498.

32. H.R.10 - Financial CHOICE Act of 2017. [Electronic resource]. – available at: https://www.congress.gov/bill/115th-congress/house-bill/10/text

33. IMF (2005). Aspects of global asset allocation. In: Global Financial Stability Report, Chapter III, International Monetary Fund.

34. IMF, World Economic Outlook Database (GDP) / Invest Europe / EDC

35. Isaksen, J. B. and Bjørnstad, K. (2006). Avkastning i Private Equity fond (Master Thesis, Norwegian School of Economics)

36. Jeng, L. A., & Wells, P. C. (2000). The determinants of venture capital funding: evidence across countries. Journal of corporate Finance, 6(3), 241-289.

37. Kaplan, S. N. and P. Strömberg (2009). Leveraged buyouts and private equity. Journal of Economic Perspectives, 23(1), 121-146.

38. Kedrosky, P. (2009). Right-sizing the US venture capital industry. Venture Capital, 11(4), 287- 293.

39. Metrick, A. & A. Yasuda (2011): "Capital and other private equity: a survey." European Financial Management 17(4): pp. 619–654.

40. Metrick, A. (2007). Venture capital and the finance of innovation. John Wiley & Sons.

41. Mikita, M. (2009). Fundusze Private Equity w dobie kryzysu finansowego. Financial Internet Quarterly e Finanse, No. 4, 1-9.

42. MJ Hudson: Private Equity Fund Terms Research (2017), P 7. London EC2R 8DN, United Kingdom

43. Pagano, M., Panetta, F., & Zingales, L. (1998). Why do companies go public? An empirical analysis. The Journal of Finance, 53(1), 27-64.

44. Piotrowski, S. (2011). Venture Capital jako forma fi nansowania MSP w polityce wspierania innowacji UE, Poznań.

45. PITCHBOOK: 2017 ANNUAL US PE BREAKDOWN.

46. PITCHBOOK: ANNUAL EUROPEAN PE BREAKDOWN 2017

47. Stefano Caselli, Emilia Garcia-Appendini, Filippo Ippolito : Explaining Returns in Private Equity Investments; Universitá'Commercial L. Bocconi

48. Talmor, E. & F. Vasvari (2011): International private equity. Chichester: John Wiley and Sons Ltd.

49. Ukrainian Venture Capital and Private Equity Overview 2017; UVCA 2017

50. Venture capital at the crossroads / William D. Bygrave, Jeffry A. Timmons. Bygrave, William D., 1937- Timmons, Jeffry A., 1941-2008. Boston (Mass.): Harvard business school press, 1992.

51. Walicka, M. (2014). Evaluati on of Technology Based Business Proposals by Venture Capital Investors – Example of Healthcare Sector. Annales UMCS, Vol. 48, No. 3, 371-382.

52. Winegerd, D. A. (1997): "The private equity market: History and prospects." Investment Policy 1(26): pp. 26–41.

53. Wright, M., Lockett , A., Pruthi, S., Manigart, S., Sapienza, H., Desbrieres, P., Hommel, U. (2004). Venture Capital Investors, Capital Markets, Valuati on and Information: US, Europe and Asia. Journal of International Entrepreneurship, 2, No. 4, 305–26.

54. World global private equity report 2017. Bain&Company 2017.

55. Worlds Private Equity Trend Report 2018 The Coming of Age. 12th annual survey on current developments in German and European private equity investment. //PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft. By Steve Roberts and Elena Naydenova. February 2018.

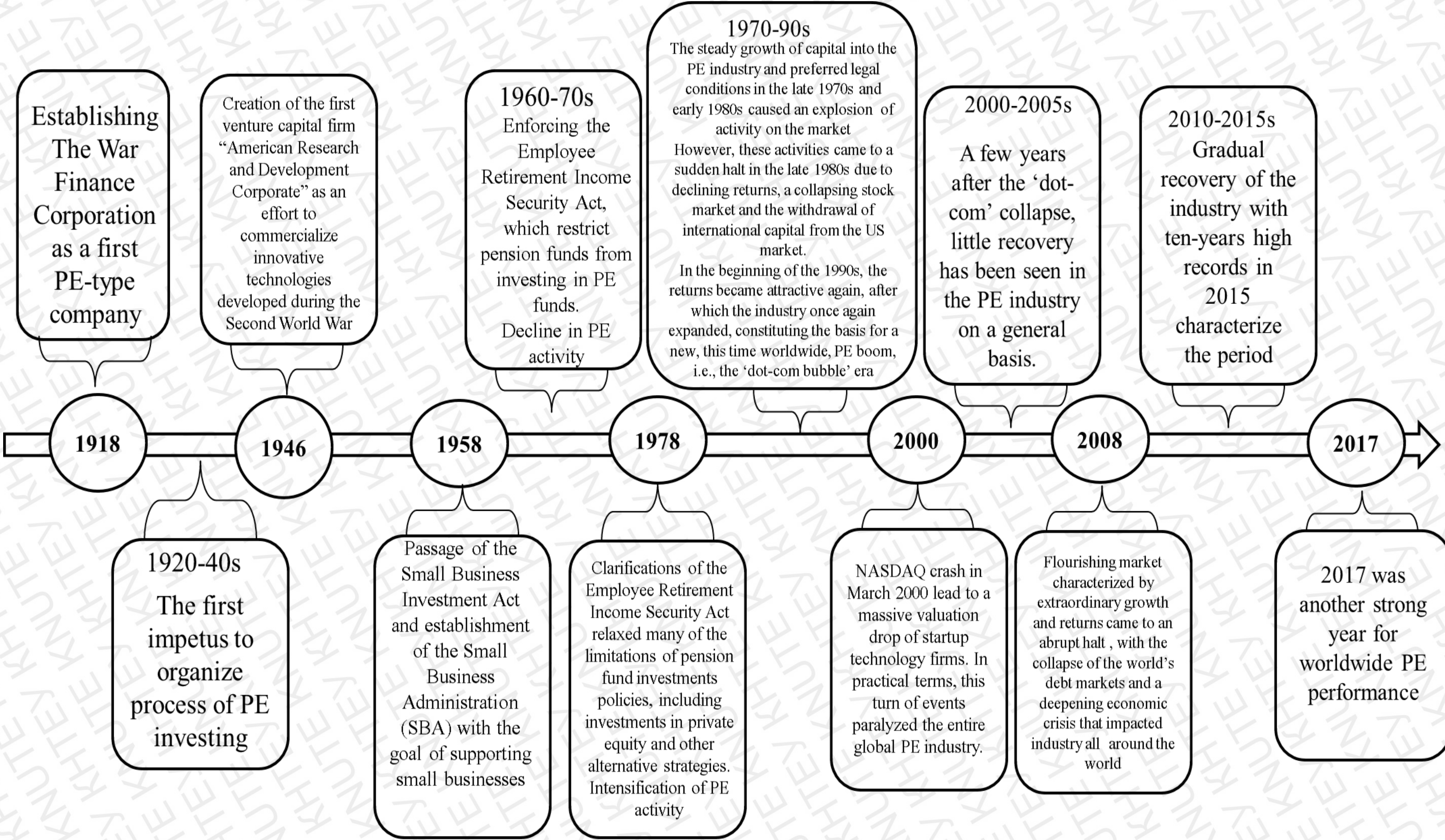
56. World Bank Group Flagship Report 2018: Doing Business 2018. [Electronic resource]. – available at: http://www.doingbusiness.org/content/dam/doingBusiness/media/Annual-Reports/English/DB2018-Full-Report.pdf

57. World Global Competitiveness Report 2018, Klaus Schwab, World Economic Forum. [Electronic resource]. – available at: http://www3.weforum.org/docs/GCR2018/05FullReport/TheGlobalCompetitivenessReport2018.pdf

ATTACMENTS

Attachment A

Phases of private equity industry evolution*



*Done by author, based on sources [17, 26, 30, 50]

Attachment B

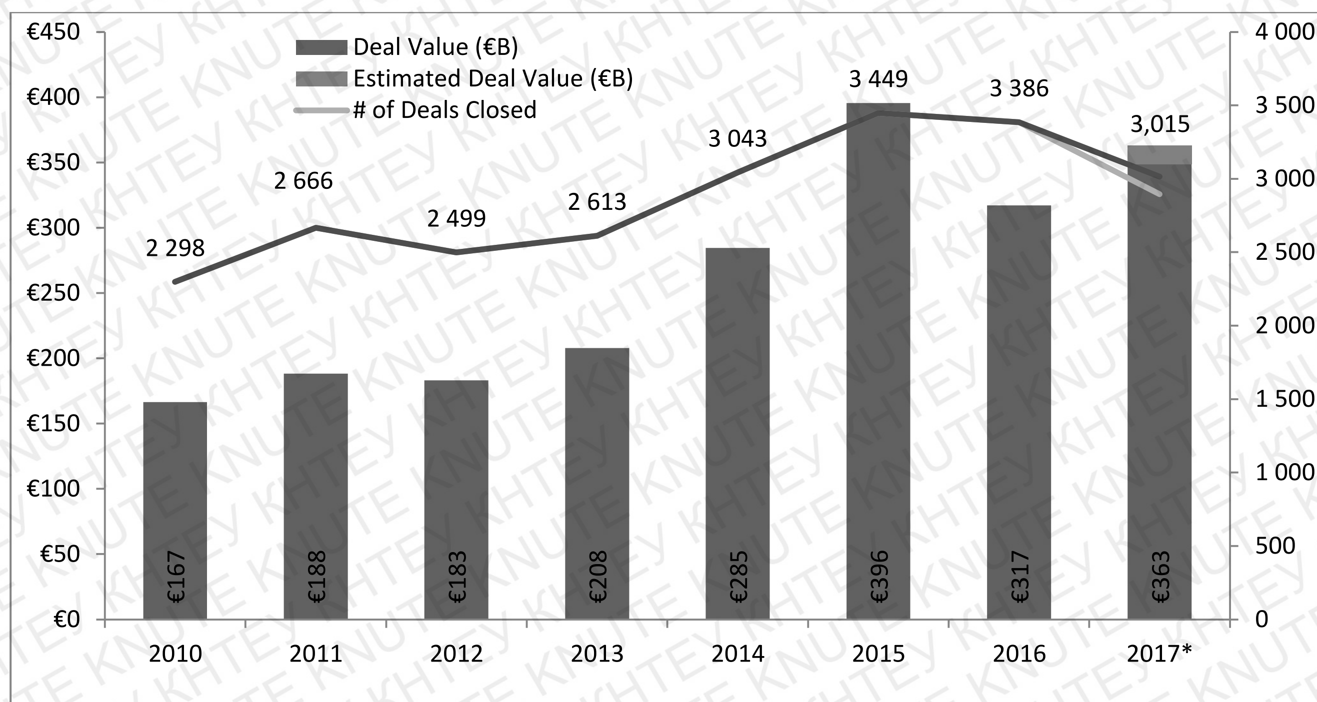
Main differences between European and Anglo-Saxon formats of private equity proceeding regulation*

Characteristic	European approach	Anglo-Saxon approach
Source of legal prerequisites	Directives of the European Union	Internal laws of the U.S. and U.K.
Georaphy of extension	European Union countries,Brazil, Turkey Russia	USA, United Kingdom, India, Australia and Commonwealth countries
Legal positioning of PE	PE implied as a financial service	PE implied as a entrepreneurial activity
Legal entities to run investments	Bank;, closed-end funds; investment firms	Venture capital funds; small business investment companies; banks; corporate venture; business angels
Regulation the relationship between LPs and GPs	Internal code of activity	Limited Partnership Agreement
Main documents, arrenging the legal framework	Alternative Investment Fund Managers Directive; Markets in Financial Instruments Directive; European Venture Capital Regulation	Consumer Protection Act
Need of supervisor	Activity is supervised by supervisor	No supervision

*Done by author by sources [15, 17, 29]

KNUTE KHTEY

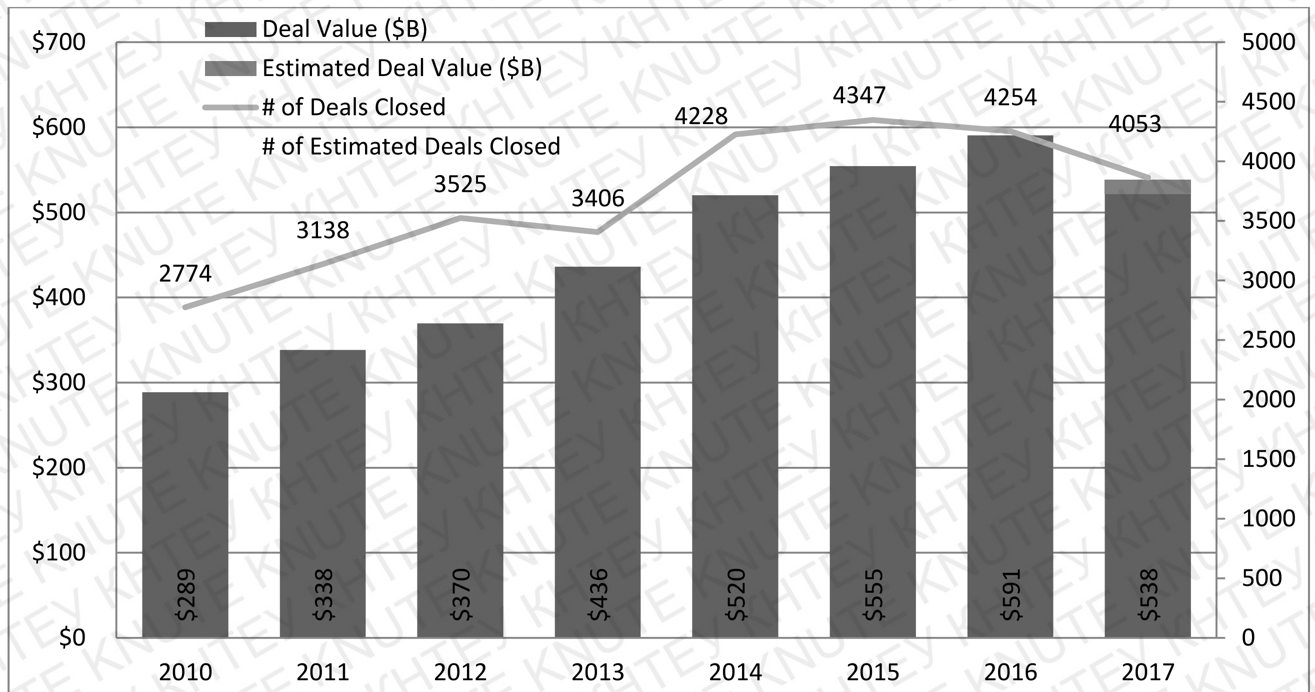
European private equity investment activity by years 2010-2017*



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Deal Value (€B)	€ 272,07	€ 309,55	€ 206,64	€ 89,35	€ 166,56	€ 188,30	€ 183,03	€ 207,88	€ 284,58	€ 395,58	€ 317,13	€ 348,83
# of Deals Closed	2 048	2 801	2 436	1 650	2 298	2 666	2 499	2 613	3 043	3 449	3 386	2 896
Estimated Deal Value (€B)												€14,19
Estimated # of Deals Closed												119

* Source [44]

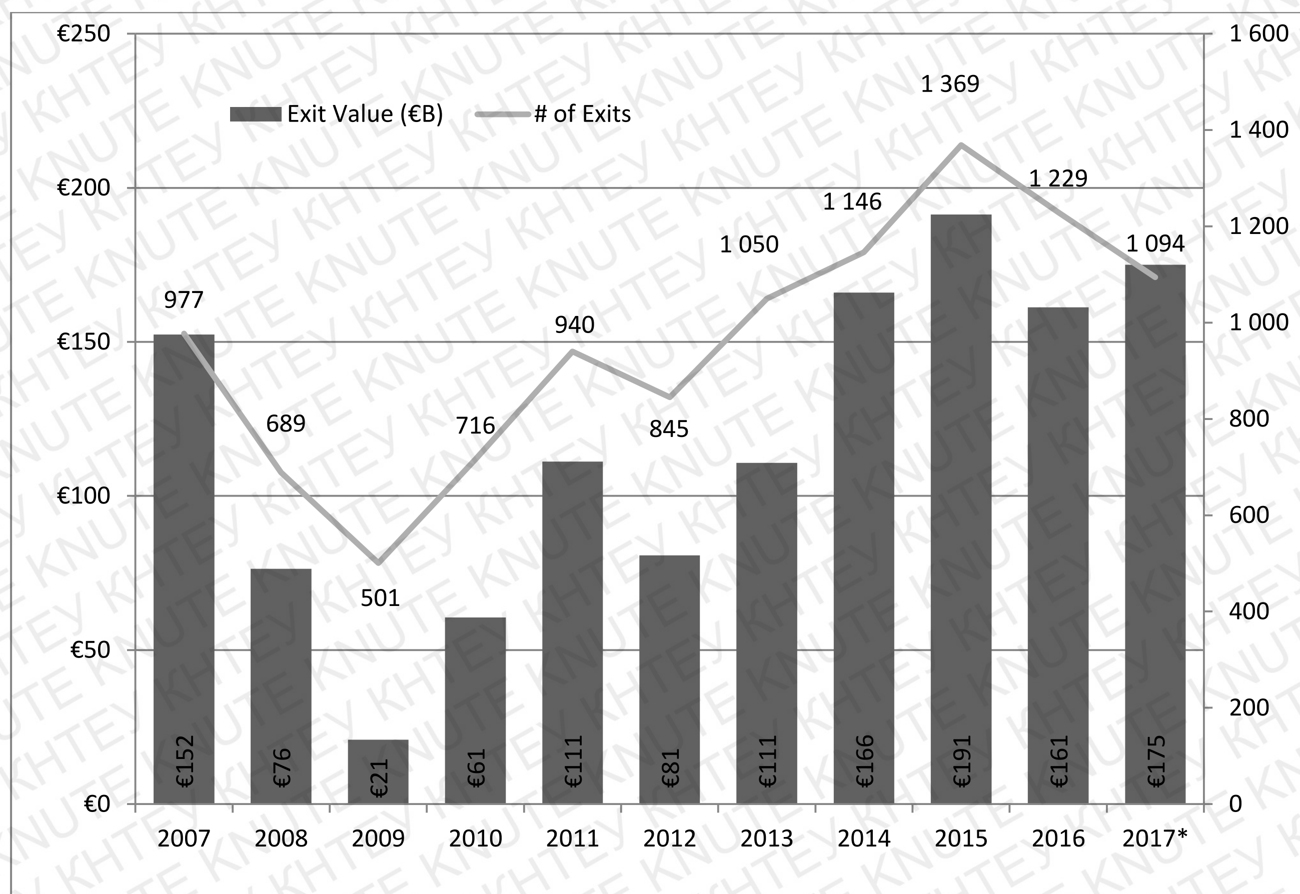
United States private equity investment activity by years 2010-2017*



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Deal Value ($B)	$456,57	$820,53	$316,40	$141,67	$288,68	$338,31	$369,59	$436,34	$520,23	$554,54	$590,71	$521,61
# of Deals Closed	2839	3569	2770	1894	2774	3138	3525	3406	4228	4347	4254	3864
Estimated Deal Value ($B)												$16,61
# of Estimated Deals Closed												189

*Source [45]

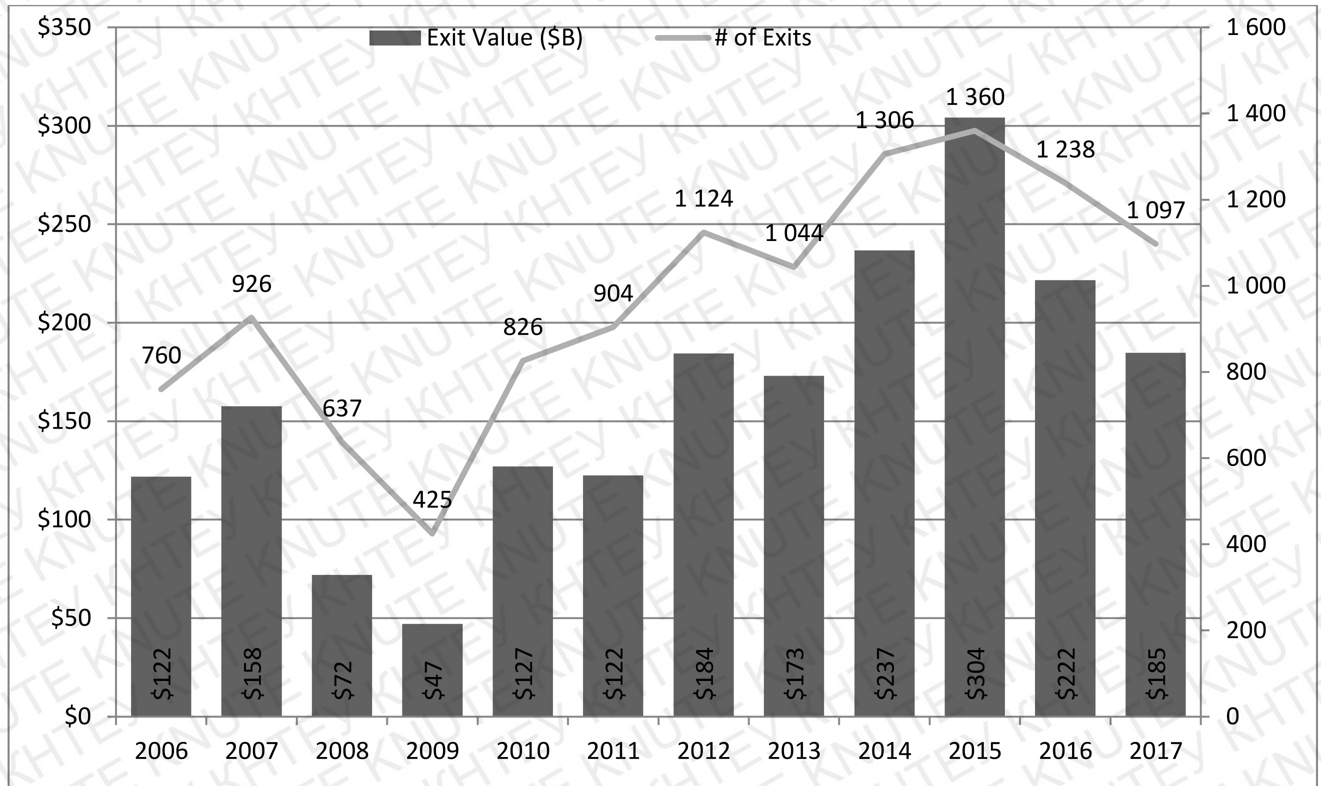
European private equity exit activity by years 2007-2017*



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Exit Value (€B)	€ 126,64	€ 152,40	€ 76,40	€ 20,87	€ 60,62	€ 111,12	€ 80,69	€ 110,76	€ 166,02	€ 191,37	€ 161,24	€ 175,02
# of Exits	755	977	689	501	716	940	845	1 050	1 146	1 369	1 229	1 094

* Source [44]

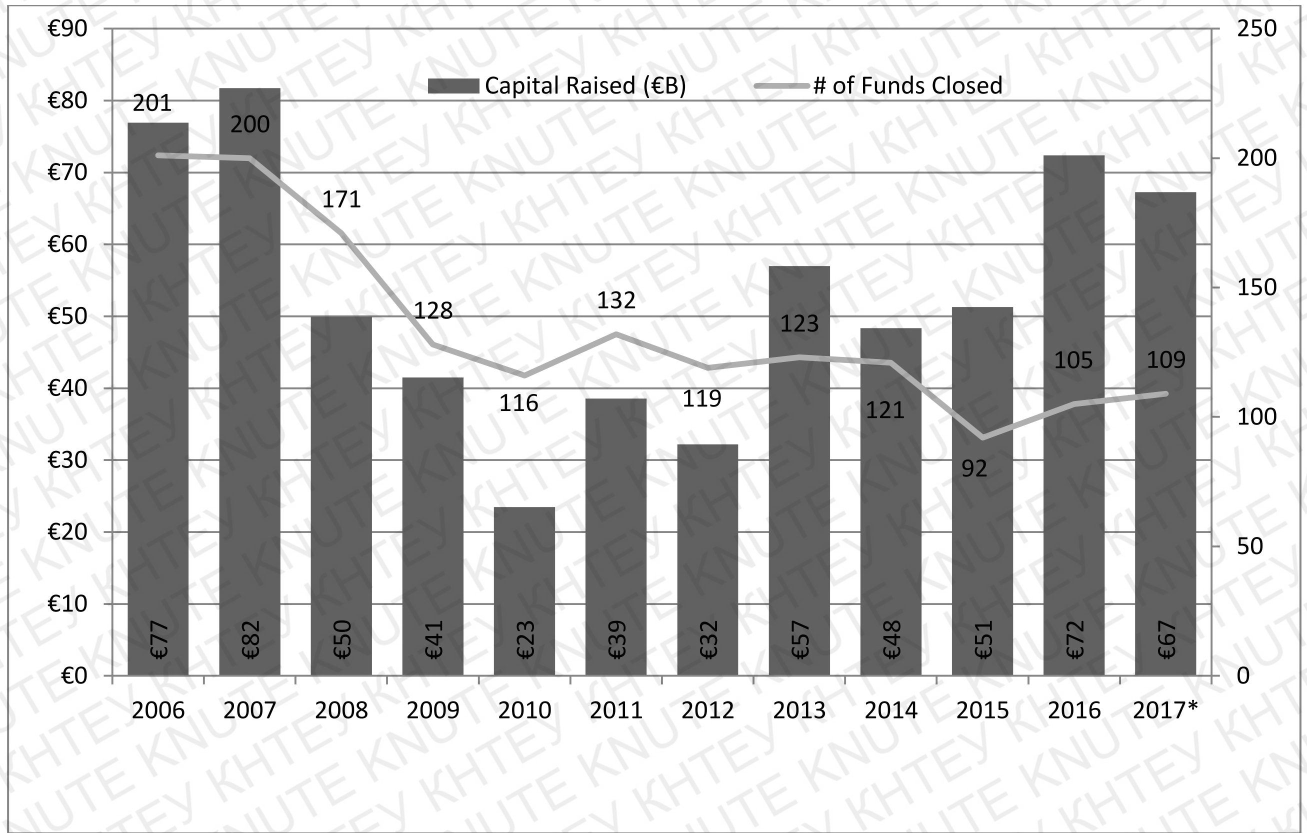
United States private equity exit activity by years 2006-2017*



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Exit Value ($B)	$121,91	$157,58	$72,01	$47,05	$126,97	$122,41	$184,38	$172,97	$236,69	$304,14	$221,65	$184,78
# of Exits	760	926	637	425	826	904	1124	1044	1306	1360	1238	1097

*Source [45]

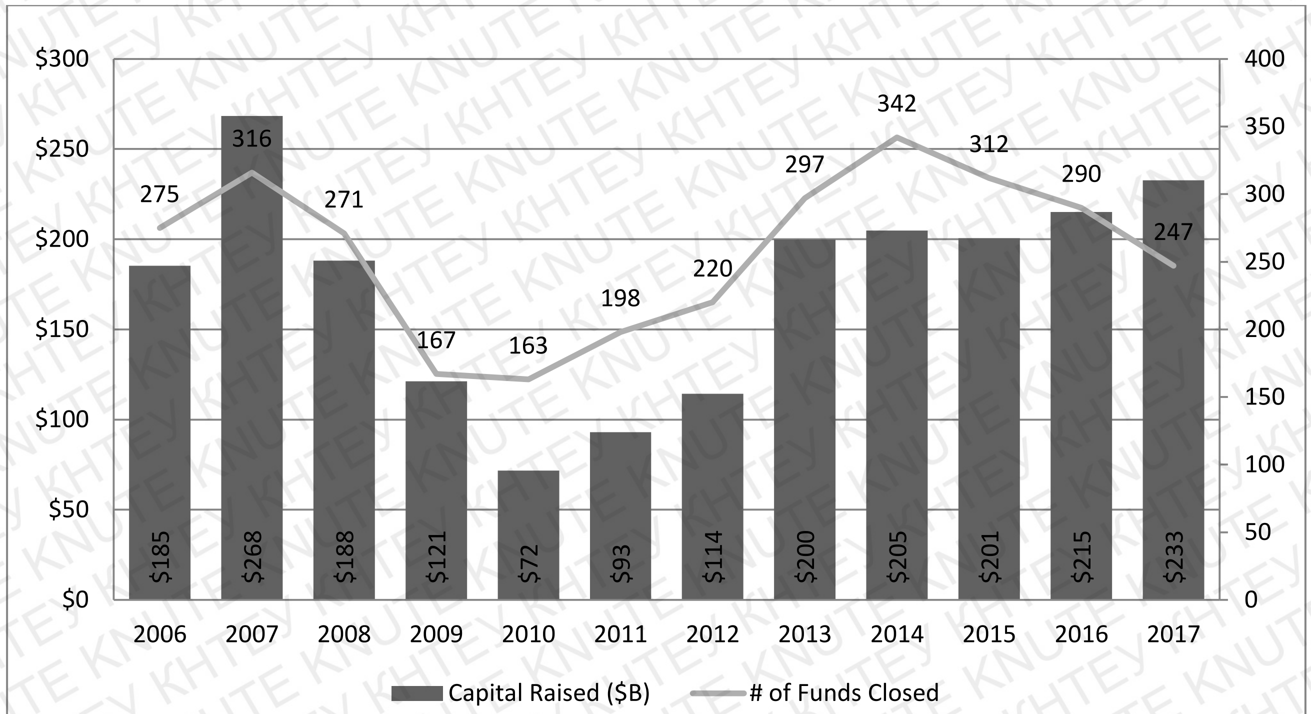
European private equity fundraising activity by years 2006-2017*



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Capital Raised (€B)	€ 76,90	€ 81,74	€ 49,96	€ 41,49	€ 23,49	€ 38,54	€ 32,18	€ 56,97	€ 48,33	€ 51,28	€ 72,40	€ 67,28
# of Funds Closed	201	200	171	128	116	132	119	123	121	92	105	109

* Source [44]

United States private equity fundraising activity by years 2006-2017*



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Capital Raised ($B)	$185,26	$268,35	$188,22	$121,22	$71,62	$93,04	$114,31	$199,87	$204,88	$200,59	$215,05	$232,74
# of Funds Closed	275	316	271	167	163	198	220	297	342	312	290	247

*Source [45]

Attachment J

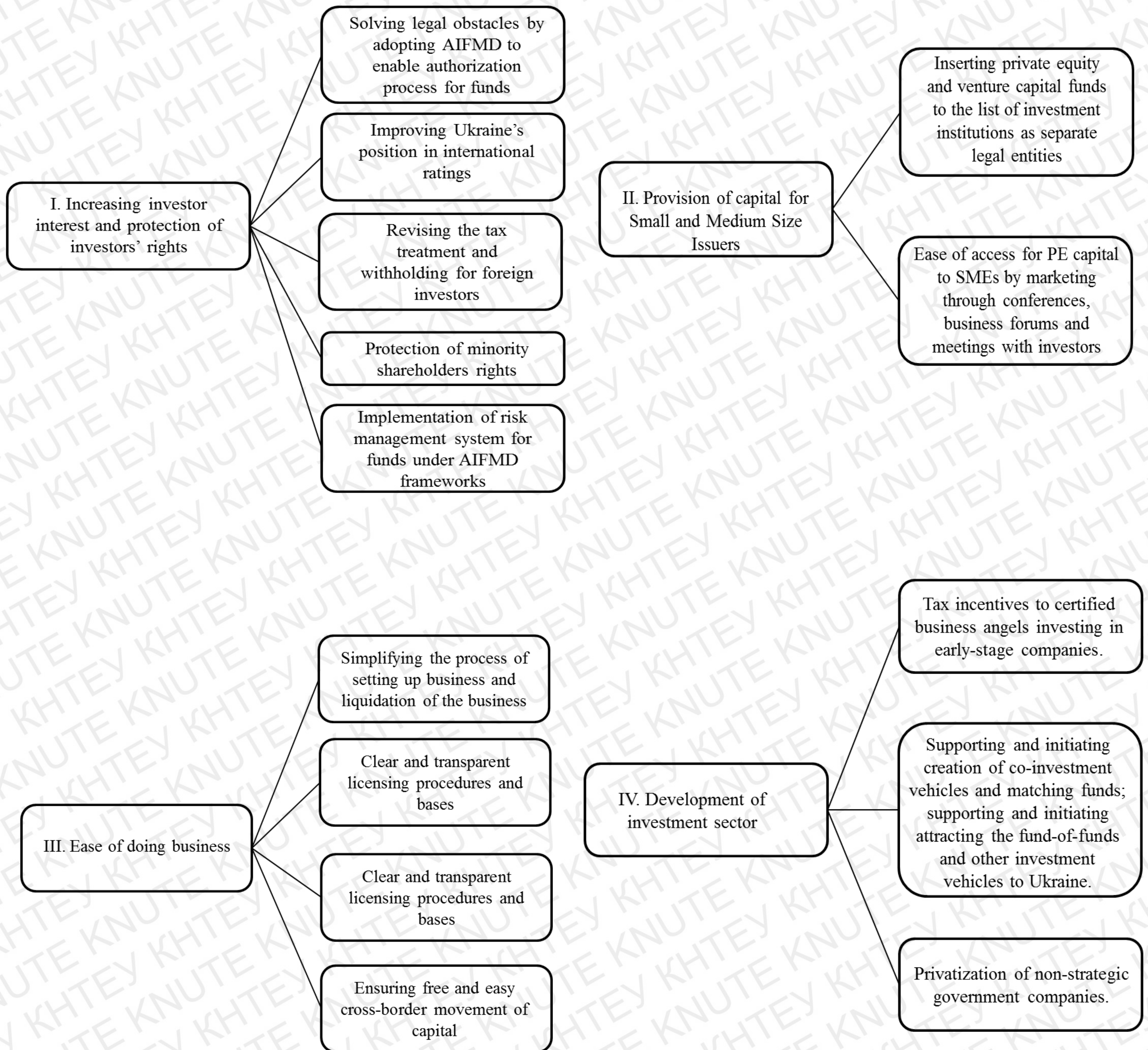
Taxation mechanism organization techniques in different formats of private equity*

<table>
<tr><td colspan="2" rowspan="2"></td><td colspan="3">Entities involved in taxation mechanism</td></tr>
<tr><td>Vehicle</td><td>Investor</td><td>PE-backed company</td></tr>
<tr><td rowspan="5">Areas of impact</td><td>Taxation on capital gains</td><td>1) Flat tax mechanism
2) Tax transparency
3) Participation exemption</td><td>Depending on country`s internal tax laws, taxation mechanism differs if the investor is a corporation, a legal entity or a private individual, andif investor is domestic, or is a foreign investor.</td><td>Non relevant</td></tr>
<tr><td>Taxation on dividends</td><td>Non relevant</td><td>Non relevant</td><td>Non relevant</td></tr>
<tr><td>Incentive to start up</td><td>Non relevant</td><td>Non relevant</td><td>1) Mark-down mechanism
2) Shadow cost
3) Tax credit</td></tr>
<tr><td>Incentive to R&D</td><td>Non relevant</td><td>Non relevant</td><td>1) Mark-down mechanism
2) Shadow cost
3) Tax credit</td></tr>
<tr><td>Taxation of the debt to equity ratio</td><td>Non relevant</td><td>Non relevant</td><td>1) Thin capitalization
2) Dual income taxation</td></tr>
</table>

Note: *Done by author by source [15]

KNUTE KHTEY

Strategic steps and tasks in process of domestic PE model implementation*



Note: *Done by author by sources [39]

KNUTE KHTEY

Attachment L

Roadmap for domestic private equity format implementation*

	Action	Rationale	Responsible entity
1	Adoption AIFMD and EuVECA into national legislation; implementing legislative, procedural and other relevant reforms as outlined there.	Adoption of EU-wide regulation documents will bring domestic legislation in accordance to European governance of PE activity, and allow Ukraine become a full-right player on a European PE market.	Cabinet of Ministers; Verkhovna Rada; NSSMC;
2	Inserting private equity and venture capital funds to the list of investment institutions as separate legal entities	To create another source of financing for SMEs	NCFS; Cabinet of Ministers; Verkhovna Rada;
3	Allow to banks; investment firms and closed-end funds such type of activity as private equity investments		NCFS; Cabinet of Ministers; Verkhovna Rada;
4	Enable Venture Capital and Private Equity Funding for SMEs	Private equity and venture capital funds must be inserted into the list of investment institutions as separate legal entities; Banks, investment firms and closed-end funds must be allowed to provide such type of activity as private equity investments.	NCFS; Cabinet of Ministers; Verkhovna Rada;
5	Determine and implement domestic approach to private equity entities taxation	Determine the appropriate approach to taxation of entities, involving into PE activity, based on world`s best practices.	State Fiscal Service of Ukraine

	Action	Rationale	Responsible entity
6	Eliminate Tax Withholding for Tax Exempt Foreign Investors	The tax withholding rules should be revised to exempt any foreign investor which can establish its tax exempt status in its home jurisdiction, according to rules established by the tax service.	State Fiscal Service of Ukraine
7	Simplifying the taxation and reporting requirements	To ensure clear and transparent rules for all entities, involved into PE proceedings.	State Fiscal Service of Ukraine
8	Tax incentives to certified business angels investing in early-stage companies	Will allow to promote venture investments activity on a local market and ensure start-ups development	NCFS; Cabinet of Ministers; Verkhovna Rada;
9	Ensure GDPR compliance	Compliance with GDPR is an obligatory precondition for local companies, willing to provide their activity on a European market	NCFS; Cabinet of Ministers; Verkhovna Rada; UVCA.
10	Framework to support of accelerators and incubators	Will allow to promote venture investments activity and ensure R&D by local companies.	NCFS; Cabinet of Ministers; Verkhovna Rada;
11	Protection of minority shareholders rights	Adoption of European approach to minority shareholders rights protection will ensure increasing of foreign investments into Ukrainian market.	AMC; Cabinet of Ministers; Verkhovna Rada;

	Action	Rationale	Responsible entity
12	Adoption of the LLC Law.	Adoption of the LLC Law will stimulate investing with enforceable protection of investors rights.	Cabinet of Ministers; Verkhovna Rada;
13	Law on protection of the Intellectual Property	Updating Law on protection of the Intellectual Property will increase level of R&D of domestic companies.	Cabinet of Ministers; Verkhovna Rada;
14	Cancelling registration for foreign investments	Only supervision by local authority (NBU)	NBU; Cabinet of Ministers; Verkhovna Rada; NSSMC;
15	Free and easy cross-border movement of capital		NBU; Cabinet of Ministers; Verkhovna Rada;
16	Simplifying the process of setting up business and liquidation of the business	These steps are aimed to make Ukraine more attractive for foreign investors.	Cabinet of Ministers; Verkhovna Rada;
17	Simplifying/shortening the termination/ reorganization of the business;		Cabinet of Ministers; Verkhovna Rada;
18	Reorganization of the licensing/regulatory authorities, optimization of their work.	Delegation some full powers to self-regulatory organisations	NCFS; Cabinet of Ministers; Verkhovna Rada; UVCA.
19	Improving Ukraine's position in international ratings	The market infrastructure institutions, led by the NCFS, should organize a review of the needed steps to improve Ukraine's place in international rankings, and then to execute these steps.	NCFS; Cabinet of Ministers; Verkhovna Rada;

Note: *Done by author by sources [1-9]