

**ПРЕГЛЕД НА КОРПОРАТИВНОТО УПРАВЛЕНИЕ В
БЪЛГАРИЯ
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**OVERVIEW OF CORPORATE GOVERNANCE IN BULGARIA
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Abstract

The aim of the article is to present the good practices in corporate governance in Bulgaria. Social changes define new business models incl. in the fields of shareholding companies. On a legal basis is defined a dynamics to modern economic dimensions.

The results define ownership and its protection as a leading factor to corporate governance practices. The past dependence on the historical development and the defense of private property are the basis of the Bulgarian reality. It can be argued that there is a separate national model of corporate governance in Bulgaria.

Keywords: SMART methodology, participants and tools, corporate governance, Bulgaria

JEL Codes: G34, F63, O12

INTRODUCTION

Over the last 25 years, a number of qualitative changes have been made in the Bulgarian economic policy related to the adoption of market principles, and in the application of international good practices in corporate governance. The challenges posed by the global crisis outline corporate governance as a major factor in modernizing the national economy and improving the competitiveness of Bulgarian companies (Houbenova-Delissivkova, 2012).

The overview of corporate governance should take into account the fact that Bulgaria is not a member of the organizations developing principles and standards of good corporate governance practices - Organisation for Economic

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Co-operation and Development, and in particular the Basel Committee on Banking Supervision. Therefore, Bulgaria is not included in researches for international practices, which prevents the use of validated methodologies for analysis and comparisons.

Most overviews regarding the development of corporate governance are based on stock market data (Borisova, 2017). In some countries, however, listed companies are too few to generate representative conclusions. Similar is the situation in Bulgaria - at the end of 2016, from approximately 4,000 shareholding companies only 397 are publicly listed, out of which 56 adopted the National Code of Corporate Governance.

THE BULGARIAN PRACTICE

In order to achieve greater completeness in the overview, we will use the SMART methodology. It includes internal participants (shareholders and managers) and external participants (auditors and regulators) as well as tools of corporate governance.

Shareholders

The shareholding in Bulgaria is concentrated and is characterized by low dynamics in the transfer of ownership. After political changes in the 1990's the state ownership decreases and the family ownership does not find a wider application (Madgerova, Kyurova, Atanasova, Koyundzhiyska-Davidkova, 2016). In most cases, the controlling shareholder is a founder (introduction of market economy in 1991), a privatizer (cash privatization, 1993-1999) or a strategic investor (in the period of Bulgarian accession to the European Union, 2004).

The presence of concentrated ownership directs corporate governance practices to the "principal-principal" model (Nedelchev, 2017) instead of the traditional "principal-agent" model. The controlling shareholder reserves the right of control without transferring it effectively to the managers, resulting in a discrepancy between ownership and control. The concentrated ownership prevents the influence of checks and balances from the external environment, and therefore, in the legislation prevail hard laws. In order to reduce the agent conflict between controlling shareholder and investors, in Bulgaria are used mostly external instruments at the expense of internal ones.

In view of the concentrated ownership in Bulgaria, a special place is devoted to the protection of minority shareholders. The rule "one share, one vote" is applied, and its extended option "one share, one vote, one dividend".

The Bulgarian practice related to the protection of ownership and other shareholder rights are increasingly in convergence with international practices. This is illustrated by the increased participation of shareholders in corporate governance - a responsibility for controlling shareholders has been introduced and measures have been taken against the short-term interest of shareholders in the ownership. However, there is a divergence, especially regarding the obligations of the shareholders, due to the differences in the laws of individual countries.

In Bulgaria, the shareholders' composition is transparent, since most of the issued shares are registered, dematerialized and have the right to vote. They are deposited with the Central Depository and the change of ownership takes place in two stages: within the company itself and within 7 days within the Central Depository, the voting right being exercised after the registration by the supervisory authority.

Managers

Since 1991, Bulgarian legislation has provided a choice between a one-tier and a two-tier system of government, which ahead of the recommendations of the European Commission from the beginning of the 21st century for introduction of the dual system. In practice, both systems are applied - the one-tier system is preferred by state-owned companies and listed companies, and the two-tier system - by foreign-owned companies and by financial intermediaries.

Given the concentrated ownership and leading role of the controlling shareholder in determining the composition of the board, there is a low dynamics in the managerial staff (Filipova, 2016). In most cases the key management personnel is nominated by the controlling shareholder, which limits the decisive influence of the corporate control market. Except the statutory requirement for insurance companies and pension insurance companies, there is practically no separation between the functions of CEO and Chairman of the Board. Due to the presence of a controlling shareholder, the need for independent directors (the only exception being the statutory requirement for 1/3 of the board of directors for public companies) and committees (legally required for commercial banks and insurance companies only) are eliminated. There is no practice that the composition of the board to

include a member chosen by the minority shareholders or as a representative of the employees.

The effects of the global crisis require increasing attention to managers' risk appetite. In this respect, the "say on pay" principle has been introduced to disclose information about the composition and amount of corporate boards' remuneration. In Bulgaria, however, this principle applies only to financial intermediaries. The role of supervisors to form the remuneration of managers is entrusted to the external auditor for control and, in most cases, the procedures for its implementation are not publicly available to stakeholders. National practices for the publication of annual financial statements include only aggregated data on paid remuneration of key management personnel.

The Bulgarian practice regarding the accountability of managers to shareholders and the disclosure of information to stakeholders convergences to the international criteria. There is a divergence in board composition and requirements for education and experience of chairman.

In Bulgaria, the diversity of boards is predominant on professions, while diversity on nationality has a low dynamics given the subsidiarity of Bulgarian companies in European holdings. Diversity on gender is most often responding to social expectations and the economic effects of it are complex to measure.

Auditors

According to the Bulgarian legislation, the auditor is appointed by the General Meeting of Shareholders on a proposal by the Audit Committee. In the financial intermediaries, the appointment of auditor is confirmed by the supervisory authority (in 2016, the Financial Supervision Commission approved eight auditors to certificate the statements of insurance companies and pension insurance companies). In certain specific cases, for example in the case of the pension insurance companies, the supervisory authority, the Financial Supervision Commission, shall agree the appointment of an auditor with the Institute of Certified Public Accountants.

Due to the high share of foreign ownership and the prevailing presence of foreign subsidiaries in Bulgaria, the appointment of auditor is done by the parent company abroad - for the most part the auditors in Bulgaria are subsidiaries of leading international companies. The comparatively small scale of the shareholding companies in Bulgaria and the alignment of national requirements with those of the EU weaken the interest of newcomer audit companies for registration and re-registration. The dynamics in the auditor's composition is low - it is limited and remains constant over a prolonged period.

This, along with the requirement for rotation of the auditor every five years, creates red tapes to the appointment of an auditor in Bulgaria.

Regarding the quality of the audit activity in Bulgaria a special authority was established - the Commission for Public Oversight of Statutory Auditors. The Commission controls the admission of foreign auditors to the local market and auditing practices in Bulgaria. Indicative of the Commission's role in non-observance of the professional duties of auditors is the following case - in 2015 the Commission imposed a fine on KPMG Bulgaria for violations committed in verifying the statement of Corporate Commercial Bank that led to its bankruptcy and public funds were used to stabilize the bank. Instead of three years (as in the European Union), the Commission checks annually the Big Four auditing companies, given the large volume of their activity in Bulgaria. In some cases, the Commission receives reports of violations of audit practices directly from shareholders.

The audit practice in Bulgaria has established a minimum requirement for quality assurance for audited statements - the auditor blocks own funds amounting to 10% of the audited capital for a period of three years.

With the introduction of market principles, besides the statutory audit, some more specific measures are being used. These include cases with qualified opinion and subsequent transformation of holding groups on the recommendation of the auditor (on the example of Bulgartabac and Kremikovtzi); conducting of due diligence due to mergers (in the acquisition of Biochim Bank and Hebrosbank by Unicredit Bulbank in 2007); limited audit prior to state financial support measures (granting a state loan to stabilize First Investment Bank in 2015).

Regulators

The main feature of Bulgarian practice is that supervision is exercised by specialized authorities competent for a specific sector of the economy. For example, there are two competent supervisory authorities for financial intermediaries: the Bulgarian National Bank and the Financial Supervision Commission. There are also supervisors who are specialized according to the type of activity they carry out. These are the Commission for Protection of Competition, responsible for mergers & acquisitions cases, and the Privatization and Post-Privatization Agency, which exercises control over the privatized companies.

Although there is variety of supervisors in Bulgaria, in their practices there is a convergence in the area of securities legislation, but there are still

differences in the application of company law. The benefits of convergence are that cooperation between supervisors from home and host countries is sought to achieve prudential supervision on a consolidated basis and reduce supervisory costs.

Tools

Given the main characteristic of the joint stock companies - separation of ownership and control, information asymmetry occurs, which can be reduced by disclosure. In Bulgaria, the provision of information is legally defined by periods (every three months for financial intermediaries and every six months for public companies) and by form (standardized reports set by the competent supervisory authority). *Ex ante* requirements for *ex post* disclosure are adopted for each economic sector. Like other countries in Eastern Europe, and in Bulgaria, the role of gatekeepers (rating companies and specialized media) in generating information is diminished.

Another commonly used tool is limiting the possibilities for crisis transmission. Applying the "ring fence" approach aims at avoiding the "domino effect" - negative results being reflected in another country or economic sector. One way to isolate risk is to separate risk activities into specialized companies. Using this approach, the Bulgarian National Bank successfully neutralized the "contagion risk" from subsidiaries and overseas branches of Greek banks in Bulgaria.

CONCLUSION AND RECOMMENDATIONS

It is recommendable in case of overview of corporate governance in Bulgaria to use data from audited annual statements instead of from stock exchange. An additional factor of success is to combine surveys and interviews with leading corporate governance experts.

Essential to building up national corporate governance practices in Bulgaria is the path dependence and, to a large extent, the historical emergence of ownership. Good practice in this area is primarily the result of Bulgarian accession to the European Union and the adaptation of national legislation to international achievements, with leading role of transition from soft laws (voluntary codes on the base of "comply or explain" principle) to hard laws (mandatory directives).

Corporate governance is a major factor in the modernization of Bulgarian economy. This also determines the leading position of the normative development of good practices, which are mainly applied in the financial intermediaries (given the need to protect foreign investments and the importance of banks for the development of the national economy).

National practices in Bulgaria increasingly take into account international trends in increasing shareholders' responsibility and accountability of managers to stakeholders. As in a number of other countries, as well as in our country, the interests of stakeholders are determined as leading and the cost of making mistakes will bear by shareholders rather than being paid by taxpayers.

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