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European Bank
for Reconstruction and Development

Corporate Governance in Transition Economies

Bulgaria Country Report

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This Report – along with all other country reports prepared within this initiative – is available at: http://www.ebrd.com/what-we-do/sectors/legal-reform/corporate-governance/sector-assessment.html

Foreword

As part of its Legal Transition Programme, the European Bank for Reconstruction and Development ("EBRD") has been assessing the state of legal transition in its countries of operations. These assessments provide an analysis of the progress of reform and identify gaps and future reform needs, as well as strengths and opportunities.

In 2012, the Legal Transition team within the EBRD Office of the General Counsel (LTT) developed with the Assistance of Nestor Advisors a methodology for assessing corporate governance frameworks and the governance practices in the EBRD countries of operations. This assessment was implemented in 2014-2015 (the "Assessment").

The Assessment aims at measuring the state of play (status, gaps between local laws/regulations and international standards, effectiveness of implementation) in the area of corporate governance.

The Assessment is meant to provide for (i) a comparative analysis of both the quality and effectiveness of national corporate governance legislation (including voluntary codes); (ii) a basis to assess key corporate governance practices of companies against the national legislation; (iii) an understanding whether the legal framework is coupled with proper enforcement mechanisms (e.g., sanctions) and/or with authorities able to ensure proper implementation; (iv) a support to highlight which are the major weaknesses that should be tackled by companies and legislators for improving the national corporate governance framework; and (v) a tool which will enable the EBRD to establish "reference points" enabling comparison across countries.

This country report is part of a series of 34 country reports. A general report synthesising all countries will close the Assessment.

Methodology

This Assessment is based on a methodology designed to measure the quality of legislation in relation to best practices requirements and the effectiveness of its implementation as evidenced by companies' disclosure, also taking into consideration the capacity of the institutional framework (e.g., courts, regulators) to sustain quality governance. The analytical grid developed for assessing the governance framework is based on international recognised best-practice benchmarks (e.g., OECD Corporate Governance Principles, Development Financial Institutions, EBRD, IFC and World Bank ROSC governance methodologies). The methodology is applied identically across all the countries reviewed. The process for gathering, analysing and reporting information is applied identically for each of the countries assessed, which allows comparing countries to each other across a long a set of benchmarking points.

For the purpose of the Assessment, the corporate governance framework and the practices were divided in five key areas: (i) Structure and Functioning of the Board; (ii) Transparency and Disclosure of company information; (iii) Internal Control; (iv) Rights of Shareholders; and (v) Stakeholders and Institutions. Each of these key areas is further divided in sections (for instance, the area "Structure and Functioning of the Board" is divided in five sections: Board composition; Gender diversity at the board; Independent directors; Board effectiveness; and Responsibilities of the board). Each section is further divided in subsections (for instance, the section "Independent Directors" is divided in three subsections: "Requirement to have independent directors"; "Definition of Independence"; and "Disclosed practices").

The assessment started by sending a questionnaire to law firms, audit firms, national regulator(s), ten largest (listed) companies, and stock exchange(s) in each country. Questions were different according to the respondents, which were asked to provide information on the legislation and on how they believe the legislation is implemented.

Responses were assigned to the corresponding subsection(s) and validated by the EBRD corporate governance specialists by looking at the applicable framework and at the disclosure offered by the ten largest (listed) companies in each country. In this respect, the working hypothesis was that the ten largest listed companies are those offering the best disclosure in each country. As such, we presumed that when certain practices were not disclosed by them, they were unlikely to be disclosed by smaller or unlisted companies. The ten largest companies were identified according to their market capitalisation. When a country did not have a stock exchange, there were less than ten listed issuers or there were no data on capitalisation of issuers, the ten largest companies were identified according to their revenues and size of the labour force. In case the largest companies were mostly of one sector (e.g., financial institutions), then the sample of ten companies was corrected to reflect other sectors of the economy.

The validation of responses was undertaken by the corporate governance specialists within the Legal Transition Team through desktop research. This research was conducted both on legislation and on the practices disclosed by the largest (listed) companies (e.g., companies' websites, annual reports, stock exchanges database etc.). In addition, the relevant reports by international financial institutions (e.g., IMF, World Bank, IFC, Transparency International, etc.) were analysed and taken into consideration. Answers received by respondents that were not grounded by specific references to legislation or consistent with the disclosed practices were not taken into consideration.

Following the validation process, each subsection was compiled by adding specific references to legislation and practices. Conclusions were then formulated for each subsection, each rated as per their adherence to international governance standards. The score ranges from 1 (very weak) to 5 (strong). The rating for each section was then calculated by averaging the ratings of the subsections.

Because understanding corporate governance requires a "holistic perspective", where each component needs to have a place in the overall picture – pretty much like a puzzle - in case one of the subsection was rated "weak" or "very weak", the resulting average was decreased by 0.2; in case

more than one subsection was rated “weak” or “very weak”, the resulting average was decreased by 0.5. This is because if just one component is not fitting well with the others, then all others are weakened. Similarly, the overall strength diminishes if there are more weak components.

Conversely, in order for the framework to be strong, all components need to be well fitting with each other. Hence, in case all subsections were scored “moderately strong” or “strong”, then the resulting average was increased by 0.5. However, this “positive” adjustment was used with some care as the assessment looked at the top ten largest companies in the country, hence findings tended to be often overly optimistic.

Key areas were then rated according to the same criteria.

The ratings are presented through the colours detailed in the box below and they demonstrate the adequacy or need of reform in respect to each governance area and section.

Rating:

“Strong to very strong” (DARK GREEN) - The corporate governance framework / related practices of companies are fit-for-purpose and consistent with best practice.

“Moderately strong” (LIGHT GREEN) - Most of the corporate governance framework / related practices of companies are fit-for-purpose but further reform is needed on some aspects.

“Fair” (YELLOW) - The corporate governance framework / related practices of companies present some elements of good practice, but there are a few critical issues suggesting that overall the system should be assessed with a view of reform.

“Weak” (ORANGE) - The corporate governance framework / related practices of companies may present few elements of good practice, but overall the system is in need of reform.

“Very weak” (RED) - The corporate governance framework / related practices of companies present significant risks and the system is in need of significant reform.

We believe corporate governance cannot be captured and measured simply by numerical values. Hence, alongside the “quantitative” assessment obtained according to the methodology described above, a “qualitative” assessment was also undertaken, by classifying our findings for each section as “strengths” and “weaknesses”. Because understanding corporate governance requires a “holistic perspective”, when the “quantitative” assessment was finalised, the assessment team compared it with the “qualitative” assessment, and when any inconsistency (i.e. material weaknesses or strengths) was noticed, the average scores of the sections were adjusted by up to ±0.5.

A preliminary version of the Assessment was made public for consultation. The comments and corrections received during the process were analysed by the corporate governance specialists. When confirmed, the corrections were reflected in the final ratings and in this Assessment.

Overview

Legislative framework:

The primary sources of corporate governance legislation in Bulgaria are the Law on Public Offering of Securities, the Law on Accountancy,[1] the Law on Credit Institutions, the Law on the Independent Financial Audit,[2] the Law on Commerce, and specific corporate governance regulations of the for public companies issued by the Financial Supervision Commission (Ordinance № 48 of of 20.03.2013 on the requirements for remuneration and Ordinance No. 2 of 17.09.2003 on prospectuses for public offering and admission to trading on a regulated market securities and disclosure of information) and for banks, issued by the Bulgarian National Bank(Ordinance No. 7 of 24 April 2014 on Organisation and Risk Management of Banks and Ordinance No 10 of 26.11.2003 on Internal Controls in Banks). Also, regulatory requirements regarding structure and functioning of the management and supervisory bodies and internal control systems of the insurer/reinsurer are prescribed by the Insurance Code.

A Bulgarian National Code for Corporate Governance was introduced in 2007 and amended in 2012.[3] The Code – by its own wording – is to be implemented under the so-called "*comply or explain*" approach and legal requirements to this end have recently been clarified.[4] A Bulgarian National Corporate Governance Committee exists, made of academics and representatives of the market and institutions. The Committee has – among others – the function of monitoring the implementation of the Corporate Governance Code. However, no monitoring reports have been issued so far.

Structure and functioning of the board

Joint stock companies in Bulgaria can be organised under a one-tier or two-tier board system: six among the ten largest listed companies are organised under a two-tier system and four under a one-tier system. Boards are generally small and evidence has shown that smaller boards tend to perform better, provided that they have the necessary mix of skills and support (e.g., corporate secretary). Gender diversity at the board is limited and legal entities can be board members, a solution that raises some doubts. Only for banks do qualification requirements exist for board members. The Corporate Governance Code recommends that board members are qualified for their role.

Public companies are required to have at least one third of the board made up of independent directors, but disclosure on this matter is limited; most of the companies declare that they comply with this requirement, without indicating who the independent directors are. The definition of independence included in the law is not comprehensive. Public interest companies, including publicly traded companies and banks, are required to have an audit committee appointed by the general shareholders' meeting (GSM). Banks are also required to have other committees. It appears that the majority of companies have an audit committee, but this committee is not necessarily made up of board members, thus it cannot be accurately classified as "*board*" committee. The law does not clearly assign to the board of companies all its key functions. Only for banks, the law is better detailed. It appears that there is no consolidated practice of board evaluation or corporate secretary function. Disclosure on committees, board activities and meetings is extremely limited and do not allow to gauge if they are playing a strategic role in the company. Fiduciary duties, liability of board members and conflicts of interest are regulated by law. Limited case law on these issues exists.

Transparency and Disclosure

The law requires companies to prepare and disclose their annual reports, which should include financial and non-financial information. All ten largest listed companies appear to comply, but non-financial information disclosure is often vague and not comprehensive. In the majority of cases, non-financial disclosure is simply a *copy and paste* of the corporate documentation, without any reference to the practices in place. In particular, disclosure on board and committees' members' qualifications, meetings and activities, beneficial ownership

[1] Law on Public Offering of Securities was amended in 2016, while during the same year a completely new Law on Accountancy came into force. However, these amendments occurred after the cut-off date of this report.

[2] A new Law on Independent Financial Audit, which transposes the provisions of Directives 2006/43/EC and 2014/56/EU, as well as Regulation (EU) No. 537/2014, was adopted in November 2016 and entered into force in December 2016.

[3] In April 2016, a revision of the code was adopted. While acknowledging this novelty, this was after the cut-off date of this report.

[4] According to the Law on Public Offering of Securities, the declaration of corporate governance shall contain information whether the issuer complies with the National Code of Corporate Governance, or some other code. If the issuer does not comply with some parts of the code applied, the declaration must contain the reasons for this non-compliance. When the issuer has opted not to refer to any corporate governance codes - the reasons for this shall be explained by the issuer.

and transactions in company shares is limited. The websites of the ten largest listed companies include some corporate governance information, but it is often incomplete. The stock exchange offers a good repository of key corporate documents. Companies disclose *comply or explain* statements, but they are not that informative; explanations are minimal and – when available – rarely meaningful. Sometimes companies provide a corporate governance scorecard. We are not convinced this is the right method to disclose corporate governance practices, as corporate governance is not a science that cannot be measured simply by numerical values. Companies are required to disclose financial information in line with IFRS and all ten largest listed companies appear to comply. Reporting to the markets and shareholders is regulated by law and appears to be well implemented. Notwithstanding a specific recommendation in the Corporate Governance Code, disclosure in English is limited. Joint stock companies are required to have their financial statements reviewed by an independent external auditor and to disclose the auditor's report. All ten largest listed companies comply with these requirements. Provision of non-auditing services by external auditors is restricted and subject to the scrutiny of the audit committee. It is not clear how this scrutiny is undertaken as audit committees are not necessarily independent and disclosure on this matter is extremely limited. This practice should be carefully monitored as the provision of non-auditing services might compromise the auditors' independence.

Internal Control

Internal audit is regulated only for banks. Companies are only recommended by the Corporate Governance Code to create an internal control system. Only two out of the ten largest listed companies - both are banks - disclose having internal audit functions in place. Banks are also required to have a compliance function, but it is not clear if it should be a standalone function. Public interest entities (which include publicly traded companies and banks) are required by law to establish an audit committee, which is appointed by and reporting to the general shareholders' meeting. It may be comprised of "*outsiders*" (i.e., non-board members), thus, it cannot be accurately classified as a "board" committee. We have reservations about this body's ability to support the functions of the board, which include the transparent and accurate presentation of information in financial reports and robustness of the internal control system. There are no independence requirements for audit committee's members. Disclosure on audit committee's meetings and activities is very limited, and reports do not unveil whether they are playing a key control role in a company. Joint stock companies must have their financial statements audited by an independent external auditor. As mentioned above, provision of non-auditing services by auditors is restricted and subject to an *independence test* carried out by the audit committee. External auditors are required to rotate after five years, but the practice does not seem to be well implemented. Only a minority of companies appear to have a code of ethics in place and it is not clear how they are implemented. Whistleblowing protection is addressed by law, but it is not comprehensive. Related party transactions and conflicts of interests are regulated.

Rights of Shareholders

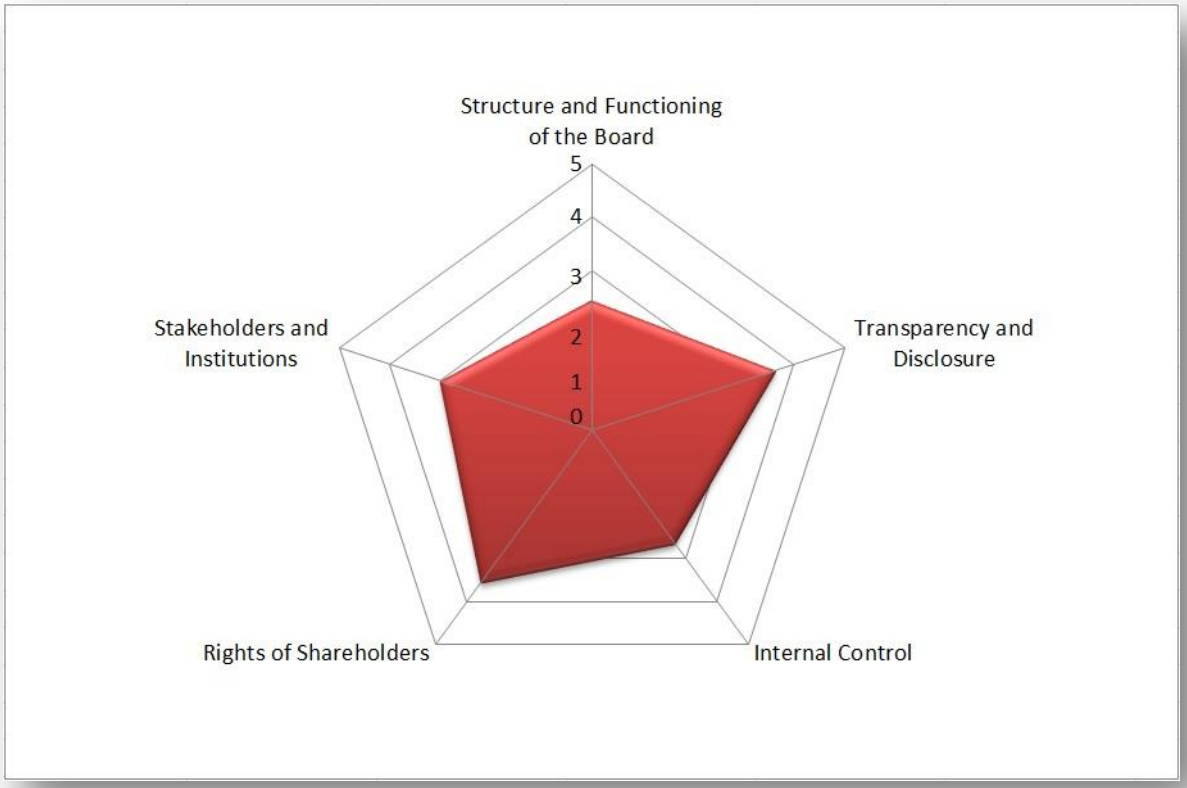
Minority shareholders are entitled to call a general shareholders' meeting (GSM), to add items to the agenda, and to nominate board members. Companies are also required to provide shareholders with timely notifications and materials for the GSM online. Furthermore, shareholders are endowed with general inspection rights and pre-emptive rights in case of capital increase. Shareholders are entitled to bring a direct or derivative claim against directors. Supermajority is required to approve major corporate changes. Cumulative voting is not regulated and it seems that it is rarely used in practice. IShareholders can count on good quality financial disclosure but the quality of non-financial disclosure is lagging behind. Self-dealing is regulated and insider trading is prohibited and appears to be enforced. Registration of shares must be maintained by an independent registry institution. The free transferability of shares cannot be limited. Shareholders' agreements and significant shareholding variations must be disclosed.

Stakeholders and Institutions

The Bulgaria Stock Exchange (BSE) is the main local stock exchange in Bulgaria. BSE's market capitalisation is around 10% of the country's GDP, but daily trading volumes are low. There are two listing tiers at the BSE: the Premium Market Segment, and the Standard Market Segment. Companies in the Premium Market Segment must "*commit to apply*" the Corporate Governance Code. The stock exchange lists on its website the companies that have made this commitment, however there is little evidence that this commitment is then translated into proper implementation. The BSE website - along with other disclosure platforms - provides thorough financial and non-financial disclosures of listed companies. There are a few inconsistencies found in laws and regulations concerning corporate governance issues. Case law is fairly accessible and regularly updated. International audit and law firms have a significant presence in the country, while international

ratings agencies are not very active and only seem to assess banking institutions. When looking at the indicators provided by international organisations, Bulgaria ranks moderately well in terms of investor protection and competitiveness, but relatively poorly in terms of corruption.

Corporate Governance Legislation and Practices in Bulgaria



Source: EBRD, Corporate Governance Assessment 2016

Note: The extremity of each axis represents an ideal score, i.e., corresponding to the standards set forth in best practices and international standards (e.g., OECD Corporate Governance Principles). The fuller the 'web', the closer the corporate governance legislation and practices of the country approximates best practices.

Key: Very weak: 1 / Weak: 2 / Fair: 3 / Moderately Strong: 4 / Strong to very strong: 5

Key Areas and Rating	Strengths and Weaknesses
1. Structure and Functioning of the Board *Weak*	*Companies can be organised under a one-tier or two-tier board system: six among the ten largest listed companies are organised under a two-tier system and four under a one-tier system.* *Boards are generally small and evidence has shown that smaller boards tend to perform better, provided that they have the necessary mix of skills and support (e.g., corporate secretary).* *Gender diversity at the board is limited and legal entities can be board members. This solution raises some doubts.* *Only for banks do qualification requirements exist for board members. The Corporate Governance Code recommends that board members are qualified for their role.* *Public companies are required to have at least one third of the board made up of independent directors, but disclosure on this matter is limited; most of the companies declare that they comply with this requirement, without indicating who the independent directors are. The definition of independence included in the law is not comprehensive.* *Public interest companies, including publicly traded companies and banks, are required to have an audit committee appointed by the general shareholders' meeting (GSM). Banks are also required to have other committees. It appears that the majority of companies have an "audit committee", appointed by the GSM, but the committee is not necessarily made up of board members, thus it cannot be accurately classified as "board committee".* *The law does not clearly assign to the board of companies all its key functions. Only for banks, the law is clearer.* *It appears that there is no consolidated practice of board evaluation or corporate secretary.* *Disclosures on committees, board activities and meetings are extremely limited and do not allow to gauge if they are playing a strategic role in the company.* *Fiduciary duties, liability of board members and conflicts of interest are regulated by law. Limited case law on these issues exists.*
1.1. Board Composition *Weak*	***Strengths:*** • *(Supervisory) boards of publicly traded companies are required to be composed of one third of independent directors.* • *In banks, board members are required to have certain qualifications, including a master's degree and five years of experience in the banking sector in a managerial position. The Corporate Governance Code recommends that board members should have knowledge and experience required to perform their duties and that they should be provided with continued professional training. For audit committees, the law requires that at least one member must have university education with a major in accounting or finance and at least five years of professional experience in accounting or audit.* • *Boards are generally small (average of 4.7 members).* • *In dual board systems, the law requires the roles of the CEO and board's chair to be separate. In unitary board systems, the Corporate Governance Code recommends that the chair of the board should be an independent director. Strangely, the Code does not provide any recommendations regarding the independence of the chair of the supervisory board. It appears that at least one of the ten largest listed companies combines the CEO and chair's roles.* • *Public interest entities, including publicly traded companies and banks, must set up an audit committee. The Law on the Independent Financial Audit establishes that audit committee members may not include members of the management board or executive directors.* ***Weaknesses:*** • *It is not entirely clear that companies comply with the legal requirement of having independent board members, as disclosure is limited on this matter (see below).* • *Legal entities can serve as board members and three companies in our sample have corporations represented by individuals sitting on their board. This solution raises some concerns, since it weakens board members' fiduciary duties and does not ensure that these members are fit for purpose. For banks, only natural persons can be a member of the board.* • *Only four of the ten largest listed companies disclose their board members' qualifications. Overall, these boards do not seem to have a diversified mix of skills. Amongst the four who disclosed, only one board appears to have at least one member with experience in risk, accounting or auditing.* • *The audit committee is not necessarily a board committee: the law requires that at least one member of the audit committee must be "independent from the supervisory board". This is interpreted as the committee is to be comprised of "outsiders" (i.e., non-board members). This solution raises some concerns. We believe it is important that the audit committee includes only board members if the functions delegated to the committee are typical board functions. Secondly, it is essential that those members sitting in the committee*

Key Areas and Rating	Strengths and Weaknesses
	and recommending specific actions to the board follow up on such recommendations and vote on the committee's recommendations at the board meeting, therefore reinforcing their positions and the board "objective judgement". Further, we believe that audit committee members should have a full vision of the business of the company in order to express their determinations – while outsiders might only have a partial understanding. Finally, committees that include outsiders might create problems with confidentiality and accountability issues, since such "outsiders" might not be bound by duties of loyalty and care required to board members. While it is legitimate that the audit committee might need external advice or expertise on specific issues, it should be able to request such advice, but it should not allow the advisor(s) to replace the committee in its determinations and recommendations. In practice, six companies disclose having an audit committee, but only one seems to be composed only of board members. In all other cases, they are composed of outsiders. The new Law on Auditing requires that the majority of the committee is independent from the company, but still allows "outsiders" to be committee members. • *For banks, the law requires the establishment of risk, nomination and remuneration committees, which must be composed of non-executive board members; only one bank in our sample disclosed having these committees in place.*
1.2. Gender Diversity at the Board (10.1%) *Weak*[5]	• *All ten largest listed companies disclose the names of their directors; four companies count at least one female director amongst its board members. Among these companies, and given the small size of the board, female representation averages 25.24%.* • *In total, there are 5 women out of 46 board members.* • *When counting all the ten companies in our sample, the average of female directors per board falls to 10.1%.*
1.3. Independent Directors *Weak*	***Strengths:*** • *(Supervisory) boards of publicly traded companies are required to be composed of one third of independent directors.* • *The Corporate Governance Code provides some guidance on the role expected from independent directors. Notably it refers to their role in overseeing and controlling the functions carried out by the executive management and in ensuring that the company's performance is pursued in accordance with the best interest of all shareholders and in respect of their rights.* ***Weaknesses:*** • *While the Corporate Governance Code recommends the chair of unitary boards to be independent, it is silent on the chair of the supervisory board.* • *The definition of independence provided by law is not very comprehensive, as it concentrates on negative "non-affiliation" criteria, without spelling out which positive requirements (i.e., objectivity of character and mind) are required from independent directors. It should be pointed out that the concepts of "non-affiliation" and "independence" are different. While non-affiliation can be established by negative criteria, independence necessarily needs objectivity of mind and character, which is a positive characteristic that should be demonstrated, disclosed and explained in practice. The definition also considers persons owning up to 25% of the voting rights as eligible to fulfil the independence criteria, which seems excessively high, as a person with one fourth of the voting rights can exert considerable influence over the managers.* • *Only three out of the ten largest listed companies disclose having independent directors. However, we could not find any explanation on the ground upon which the named directors – in the very few cases when they are identified - are considered independent. In most cases, it is not possible to understand who in the board is considered independent.*
1.4. Board Effectiveness *Weak*	***Strengths:*** • *The boards of banks are responsible for appointing risk committees. In turn, committees must periodically report to the board.* ***Weaknesses:*** • *Public interest entities, including publicly traded companies and banks, must set up an audit committee. However - as mentioned above - this body is not a "board" committee as members are appointed by and report to the GSM (and not to the board) and should include non-board members. The Corporate Governance Code (2012), which is more recent than the law which introduced the requirement to set up audit committees (2008), emphasises that committees in general are meant to assist the board and it states that the board should propose to the shareholders the election of an audit committee. Despite these recommendations, the audit committee appears in reality accountable only to the shareholders. We have doubts about this body's ability to adequately support the board in the fulfilment of its obligations.* • *The Corporate Governance Code only generally refers to committees, but it does not provide any guidance on them, apart from the audit committee.* • *For banks, the law requires the establishment of risk, nomination and remuneration committees, which must be composed of non-executive board members (but not necessarily independent). Only one bank in our*

[5] Recent amendments to the Law on Public Offering of Securities have introduced a requirement for companies to publish as part of their annual corporate governance reports information on the diversity policy. This information includes a description of the policy implemented in respect of administrative, management and supervisory bodies of the issuer with regard to aspects such as age, sex or education and professional experience, objectives of such policy, the manner of its implementation and results during the reporting period. If the company has not adopted such a policy, it should publish an explanation of the reasons for this.

Key Areas and Rating	Strengths and Weaknesses
	sample affirms having these committees, which are made up of supervisory board members. • *There is no comprehensive recommendation for boards to perform board evaluations. The Corporate Governance Code only recommends supervisory boards to evaluate the performance of the management board members, without recommending the supervisory board to evaluate its own performance or referring to the case of unitary boards. None of the companies in our sample discloses having performed board evaluations.* • *There are no requirements or recommendations for companies to appoint a corporate secretary. Only one company discloses having one.* • *There are no requirements or recommendations for companies to disclose the number of board and committee meetings, or their minimum frequency. Only one company in our sample discloses such information. It appears that its supervisory board met 11 times and its audit committee met 8 times last year. Due to the lack of disclosure, it is not possible to assess whether they play a strategic role in the companies' performance. Further, the frequency of meetings seems excessive for a supervisory board. This might be an indication that the board is dealing with operational issues, which is not a good practice.*
1.5. Responsibilities of the Board *Fair*	***Strengths:*** • *By law, the board is responsible for appointing and dismissing executives. In the case of two-tier board systems, the supervisory board appoints the management board members.* • *The Law on Credit Institutions is clear in assigning to the board key strategic functions and defining the board's responsibilities.* • *Fiduciary duties, liability and conflicts of interest are addressed by the law. However, enforcement in these matters is very limited, and access to case law is subpar.* ***Weaknesses:*** • *In companies, the law does not clearly assign to the board its key strategic functions (in particular, there is no reference to strategy, risk profile or budget) and it allows shareholders to define the board's powers through the companies' Articles of Association. We are not convinced that this is the right approach. Instead, we believe that the key strategic functions of the board (e.g., strategy, budget, risk, appointment, removal and oversight of management) should be clearly set by law and should not be left to shareholders decision, as this might undermine the check and balances between corporate bodies.*

Key Areas and Rating	Strengths and Weaknesses
2. Transparency and Disclosure *Fair/Moderately Strong*	*The law requires companies to prepare and disclose their annual reports, which should include financial and non-financial information. All ten largest listed companies appear to publish their annual reports, but non-financial information disclosure is often vague and not comprehensive. In the majority of cases, non-financial disclosure is simply a copy and paste of the corporate documentation, without any reference to the practices in place. In particular, disclosure on board and committees' members' qualifications, meetings and activities, beneficial ownership and transactions in company shares is limited.* *On average, the websites of the ten largest listed companies include some corporate governance information, but it is often incomplete. The stock exchange offers a good repository of key corporate documents. "Comply or explain" statements are not that informative; explanations are minimal and – when available – rarely meaningful.* *Sometimes companies provide a corporate governance scorecard. We are not convinced this is the right method to disclose corporate governance practices, as corporate governance is not a science that can be measured simply by numerical values.* *Companies are required to disclose financial information in line with IFRS and all ten largest listed companies appear to comply.* *Reporting to the markets and shareholders is regulated by law and appears to be well implemented. However notwithstanding a specific Code's recommendation to this end - disclosure in English is often limited.* *Joint stock companies are required to have their financial statements reviewed by an independent external auditor and to disclose the auditor's report. All ten largest listed companies comply with these requirements. Provision of non-auditing services by external auditors is restricted and subject to the scrutiny of the audit committee. It is not clear how this scrutiny is undertaken in practice as disclosure on this matter is extremely limited. This practice should be carefully monitored as the provision of non-auditing services might compromise the auditors' independence.*
2.1. Non-Financial Information Disclosure *Fair*	***Strengths:*** • *Companies are required to prepare their annual reports (AR) which by law must contain a considerable amount of non-financial information, including description of main risks, overview of the company's results and developments, information on the board members' remuneration and the company's programme for application of corporate governance standards. It seems that the required information has been additionally specified in recent amendments to the Law on Public Offering of Securities and the Financial Supervision Commission's Ordinance No. 2 on prospectuses for public offering and admission to trading on a regulated market securities and disclosure of information.* • *ARs are largely disclosed and can be found on the news agency - national disclosure platforms (www.investor.bg or www.x3news.com) and on the stock exchange website (http://www.bse-sofia.bg/?page=FinancialReportsOfIssuers). Six of the ten largest listed companies also publish the ARs in English on their websites.* • *All ten largest listed companies disclose the minutes of their general shareholders' meetings on the stock exchange's platforms and in some cases, also on their own websites. All of them also provide updated information on their shares and capital.* • *All companies in our sample disclose their articles of association on their websites.* ***Weaknesses:*** • *None of the surveyed companies discloses transactions with the company's shares, or information on their board and committee meetings and activities.* • *The directors' names are generally disclosed; however, only a few companies seem to provide details on their qualifications. Only three of the surveyed companies do so, and only one discloses the composition of its audit committee.* • *Bulgarian law requires listed companies to disclose a "programme for the application of the internationally recognized good corporate governance standards" and to explain "the reasons due to which the issuer was not in compliance with the programme", without making any references to the National Code or clarifying what "programme" means.* [6] *As a result, disclosure offered by companies when reporting their corporate governance practices appears to be mostly a "copy and paste" of their corporate documentation, failing to refer to the practices in place. Explanations are rarely provided.* • *The Listing Rules of the Bulgarian Stock Exchange require companies listed on the BSE Main Market, Premium Equity Segment to "commit to apply the principles of corporate governance enshrined in the National Corporate Governance Code as approved by the Exchange". This is in conflict with the wording of the Code, which endorses the "comply or explain" approach. In practice, to comply with the Listing Rules,*

[6] It seems that this issue was addressed by recent amendments to the Law on Public Offering of Securities.

Key Areas and Rating	Strengths and Weaknesses
	companies generally declare that they comply with the Code and the Bulgarian Stock Exchange lists on its website (http://www.bse-sofia.bg/?page=CorporateGovernance) all companies that "have declared to comply". We wonder whether such a declaration of compliance really means full adherence to the Code.
2.2. Financial Information Disclosure *Strong*	***Strengths:*** • *Companies are required to publish their ARs and financial statements along with the auditor's opinion.* • *Publicly traded companies must prepare separate financial statements in line with IFRS.* • *All ten largest listed companies disclose their financial statements on the national disclosure platforms www.investor.bg or www.x3news.com and/or on the stock exchange website (http://www.bse-sofia.bg/?page=FinancialReportsOfIssuers). Their financial reports are prepared in line with IFRS.*
2.3. Reporting to the Market and to Shareholders *Fair*	***Strengths:*** • *The quality of financial information appears generally robust and all ten largest listed companies submit their ARs on the national disclosure platforms and stock exchange website.* • *Companies are expressly required to disclose the minutes of their general shareholders' meetings and all ten top listed companies comply with this requirement.* • *Listed companies are required to make timely disclosure of price sensitive events. The Corporate Governance Code recommends that companies disclose such information on their websites.* • *Failing to comply with disclosure rules can be punished with fines.* ***Weaknesses:*** • *The websites of the ten largest listed companies are not always complete and up-dated, especially as regards corporate governance issues.* • *The quality of corporate governance disclosure should be improved.*
2.4. Disclosure on the External Audit *Moderately strong*	***Strengths:*** • *Public companies are required to disclose their ARs, which must contain their auditor's report. All ten largest listed companies disclose their auditor's opinions on their financial statements. The auditors of nine of them declare to be independent (auditors are international audit firms).* ***Weaknesses:*** • *Provision of non-auditing services is allowed, but subject to an "independence test" by the audit committee. It is not clear how this independent test is undertaken in practice, as disclosure on this matter is very limited. Also to be noted that in most cases the audit committee is not a board committee. Only three of the surveyed companies declared having received non-auditing services from their external auditors. The other companies do not disclose this information. The new Law on Independent Financial Audit restricts the provision of non-auditing services to tax consultancy and services which are not prohibited by Regulation (EU) № 537/2014, provided they do not impact the audited financial statements and the auditor's independence.*

Key Areas and Rating	Strengths and Weaknesses
3. Internal Control *Weak/Fair*	*Internal audit is regulated only for banks. Companies are only recommended by the Corporate Governance Code to create an internal control system. Only two out the ten largest listed companies (both banks) disclose having internal audit functions in place. Banks are also required to have a compliance function, but it is not clear if it is required to be a standalone function.* *Public interest entities (which include publicly traded companies and banks) are required by law to establish an audit committee, which is appointed by and reporting to the general shareholders' meeting. It may be comprised of "outsiders" (i.e., non-board members). Thus, this body cannot be accurately classified as an audit committee. We have reservations about this body's ability to support the functions of the board, which include the transparent and accurate presentation of information in financial reports and robustness of the internal control system. There are no independence requirements for audit committee's members (apart from the fact that at least one member should be independent from the supervisory board). Disclosures on audit committee's meetings and activities are very limited, and reports do not unveil whether they are playing a key control role in the company.* *Joint stock companies must have their financial statements audited by an independent external auditor. Provision of non-auditing services by auditors, while simultaneously providing auditing services to a company, is restricted and subject to an "independence test" carried out by the audit committee.* *External auditors are required to rotate after five years, but the practice – as evidenced by companies' disclosure - does not seem to be well implemented.* *Only a minority of companies appear to have a code of ethics in place and there is no indication on how the code is implemented in practice.* *Whistleblowing protection is addressed by law, but it is not comprehensive. Related party transactions and conflicts of interests are regulated.*
3.1. Quality of the Internal Control Framework *Weak*	***Strengths:*** • *Banks are required to have a compliance function, but it is not clear if it is required to be a standalone function. One bank in our sample disclosed having such a function, which has been recently created.* ***Weaknesses:*** • *Banks are required to establish an internal audit department, but its head is appointed by the general shareholders meeting (GSM). This solution raises some doubts: according to best practices, the internal auditors' accountability line is to the board (via the audit committee) and not the shareholders. Only two of the surveyed companies (both banks) disclosed having internal audit functions in place.* • *Public interest entities must create an audit committee, but this committee cannot be accurately classified as a "board" committee. Further, independence and qualification requirements for audit committee members are limited (see below).* • *Companies are recommended to have a code of ethics, but only two out of the ten largest listed companies disclose having one. Further, when the code exists, it is not clear who the officer in charge of monitoring compliance is. This is a key issue as the value of the code is in its implementation.* • *The law provides for whistleblowing protection, but legislation is not comprehensive.*
3.2. Quality of Internal and External Audit *Fair*	***Strengths:*** • *Joint stock companies and limited liability companies meeting certain criteria are required to have their financial statements reviewed by an independent external auditor appointed by the general shareholders' meeting.* • *The auditors of nine of the ten largest listed companies declare to be independent. They are all international audit firms.* • *The audit committee is in charge of assuring the independence of the external auditor. We would point out, however, that there are no requirements that the majority of audit committee members be independent, hence we have some doubts about the effectiveness of the "independence test".* • *The external auditor and the audit committee are in charge of the review of the internal control system.* ***Weaknesses:*** • *Banks are required to establish an internal audit department, members of which shall be appointed by the GSM. As mentioned above, this solution raises some doubts. Only two of the surveyed companies (both banks) disclosed having internal audit functions in place.* • *The key auditor of the audit firm and the auditor who works directly through individual practice with a certain public interest company are required to rotate after five years, but the practice – as evidenced by companies' disclosure - does not seem to be well implemented.* • *Provision of non-auditing services by auditors is allowed, provided that it does not undermine the auditor's*

Key Areas and Rating	Strengths and Weaknesses
	independence (i.e. subject to the "independence test"). Three companies in our sample disclose having received non-auditing services; other companies do not provide any information on this matter and it is not clear whether this is due to the absence of non-auditing services being provided or because no test has been undertaken. The new Law on Independent Financial Audit restricts the provision of non-auditing services to tax consultancy and services which are not prohibited by Regulation (EU) № 537/2014, provided they do not impact the audited financial statements and the auditor's independence.
3.3. Functioning and Independence of the Audit Committee *Weak*	***Strengths:*** • *Public interest entities, which include publicly traded companies and banks, must set up an audit committee.* • *The law requires that at least one member of the audit committee should have university education with a major in accounting or finance and at least 5 years of professional experience in accounting or audit.* • *The audit committee is in charge of monitoring the independence of the external auditors.* ***Weaknesses:*** • *There are many inadequacies in the composition and functioning of the audit committee required by law. As mentioned before, it should be composed by at least "one member who is independent from the supervisory board". We believe this is not a good practice (further details in the section on board composition). There are no further independence requirements for audit committee members. The new Law on Auditing requires that the majority of the committee is independent from the company, but still allows "outsiders" to be committee members.* • *Qualification requirements for audit committee's members are limited to the "member who is independent from the supervisory board".* • *Audit committee's members are appointed by and report to the GSM, which is also in charge of regulating the committees' functions and activities. Therefore, despite the Corporate Governance Code's recommendation that the audit committee should support the board, audit committees seem in reality only accountable to the shareholders, rather than to the board. We have doubts about this body's ability to ensure fit-for-purpose internal control systems and external auditing services.* • *Only one company discloses having an audit committee at the board level in place. This company has one independent board member on its audit committee. Five other companies disclose having it all made up of outsiders. Only one of them discloses the number of meetings held per year (8 times) and its activities.*
3.4. Control over Related Party Transactions and Conflict of Interest *Moderately strong*	***Strengths:*** • *Conflicts of interest and Related Party Transactions (RPT) are regulated by law. Board members, senior managers and shareholders should abstain from voting on decisions regarding a transaction or issues that they have any personal interests. Board members are required to inform the chairman of their interest and they are generally required to avoid any conflicts of interests that might affect their judgement.* • *RPTs must be approved by non-conflicted directors if such transaction's value is less than 2% of company's assets. In all other cases, RPTs should be approved by the GSM.* • *All ten largest listed companies disclose RPTs as sections within their financial statements.* • *It seems that significant penalties have been imposed by courts or regulators in cases of misuse of corporate assets or of unauthorised/undisclosed related party transactions over the last 10 years.* ***Weaknesses:*** • *No material sanctions have been imposed by the regulator for breaching rules on disclosure of conflicts of interest. This can be either a sign of perfect compliance with the rule or lack of monitoring.*

Key Areas and Rating	Strengths and Weaknesses
4. Rights of Shareholders *Moderately strong*	*Minority shareholders are entitled to call a general shareholders' meeting (GSM), to add items to the agenda, and to nominate board members. Companies are also required to provide shareholders with timely notifications and materials for the GSM online. Furthermore, shareholders are endowed with general inspection rights and pre-emptive rights in case of capital increase. Shareholders are entitled to bring a direct or derivative claim against directors. Supermajority is required to approve major corporate changes. Cumulative voting is not regulated and it seems that it is rarely used in practice.* *While financial disclosure has reached a good standard and is generally considered reliable, non-financial disclosure is lagging behind, especially on corporate governance issues.* *Self-dealing is regulated and insider trading is prohibited, and some few insider trading cases have been investigated in the past five years.* *None of the ten top listed companies appears to provide information on transactions with the company's shares by its directors.* *Registration of shares must be maintained by an independent registry institution. The free transferability of shares cannot be limited.* *Shareholder agreements and significant shareholding variations must be disclosed.*
4.1. General Shareholders' Meeting (GSM) *Moderately Strong*	***Strengths:*** • *Shareholders representing 5% of the capital can call a GSM, propose new items to the GSM agenda, nominate directors and the company's auditor.* • *The GSM announcement and agenda are required to be sent to shareholders at least 30 days before the meeting. All ten largest listed companies publish the GSM notifications and materials on their websites.* • *The law allows shareholders to vote electronically, by proxy, or by post.* • *Five of the ten largest listed companies provide information about voting rights, and their exercise, on their website.* •
4.2. Protection against Insider Trading and Self-dealing *Moderately Strong*	***Strengths:*** • *Insider trading is prohibited by law and can be punished with fines. A few insider trading cases have been investigated in the past five years.* • *Transactions between the shareholders, directors, officers and other related parties must be based on fair terms; otherwise, they can be invalidated in court and action can be taken against the relevant parties. Judicial practice on this matter is very limited though.* • *Board members, senior managers and controlling shareholders are required to disclose transactions with the company's shares.* ***Weaknesses:*** • *None of the ten largest listed companies appear to disclose transactions involving the company's shares.*
4.3. Minority Shareholders Protection and Shareholders' Access to Information *Moderately strong*	***Strengths:*** • *All ten largest listed companies disclose their annual reports (ARs) on the stock exchange's and on their websites. Six of them also publish their ARs in English.* • *Shareholders have general inspection rights. Additionally, minority shareholders have the right to call a GSM, add items to the agenda, and nominate board members.* • *Pre-emptive rights are assigned to shareholders in all cases of capital increases in cash, and can only be waived by a three-quarters majority vote at the GSM.* • *Shareholders representing 5% of the share capital can bring a derivative claim against the company's directors and shareholders representing 10% of the share capital can bring an action in the name of the company. There have been several cases brought to court over the past five years.* • *A supermajority is required for major corporate decisions and to amend the articles of associations. Minority shareholders may block major corporate changes with a 33%%+1-vote.* • *Shares carry proportional voting rights.* ***Weaknesses:*** • *Cumulative voting is not provided by law and does not seem to be widely used in practice.*
4.4. Registration of Shareholdings *Moderately strong*	***Strengths:*** • *A share register of all companies shall be maintained by an independent registry institution.* • *In public companies, if a person's shareholding exceeds 5% of the share capital, he must inform the regulator and the company. Failing to comply with this obligation can be punished with fines.* • *The free transferability of shares cannot be restricted.* • *Shareholder agreements are enforceable and must be disclosed in the AR.*

Key Areas and Rating	Strengths and Weaknesses
5. Stakeholders and Institutions *Weak/Fair*	*The Bulgaria Stock Exchange (BSE) is the main local stock exchange in Bulgaria. BSE's market capitalisation is around 10% of the country's GDP, and the market seems to be fairly illiquid.* *There are two listing tiers at the BSE: the Premium Market Segment, and the Standard Market Segment. Companies in the Premium Market Segment must "commit to apply" the Corporate Governance Code. The stock exchange lists on its website the companies that have made this commitment, but it hard to say whether this correspond to full adherence to the Code.* *The National Corporate Governance Code was first issued in 2007 and reviewed in 2012. It seems that a new revision is currently undergoing. All ten largest listed companies in Bulgaria disclose a "comply or explain" statement, however disclosure is often vague, explanations are rare and not much meaningful. Sometimes companies provide a corporate governance scorecard. We are not convinced this is the right method to disclose corporate governance practices, as corporate governance is not a science that can be measured simply by numerical values.* *A Bulgarian National Corporate Governance Committee exists, made of academics and representatives of the market and institutions. The Committee has – among others – the function of monitoring the implementation of the Corporate Governance Code. However, no monitoring reports have been issued so far.* *The BSE website along with other disclosure platforms provide thorough financial and non-financial disclosures of listed companies.* *Case law is fairly accessible and regularly updated. There are a few inconsistencies found in laws and regulations concerning corporate governance issues.* *International audit and law firms have a significant presence in the country. International ratings agencies are not very active within the country, and only seem to assess banking institutions.* *When looking at the indicators provided by international organisations, Bulgaria ranks moderately well in terms of investor protection and competitiveness, but relatively poorly in terms of corruption.*
5.1. Corporate Governance Structure and Institutions *Fair*	***Strengths:*** • *There are two listing tiers at the Bulgarian Stock Exchange's Main Market: the Premium Segment and the Standard Segment. The Premium Segment requires higher corporate governance standards. Additionally, equities can be listed in the Alternative Market if they do not meet the capital and performance requirements of the first two listed segments.* • *International audit and law firms have a significant presence in the country.* • *The rulings of regulatory agencies are documented, publicly available, and easily accessible.* ***Weaknesses:*** • *The BSE is the main local stock exchange in Bulgaria. BSE's market capitalisation is around 10% of the country's GDP but liquidity and daily trading volumes are relatively low.* • *International ratings agencies are not active within the country; only one of the top ten listed companies has been assessed.* • *Availability of training courses for company directors appears limited.* • *A Bulgarian National Corporate Governance Committee exists, made of academics and representatives of the market and institutions. The Committee has – among others – the function of monitoring the implementation of the Corporate Governance Code. However, no monitoring reports have been issued so far. More efforts on this issue would be needed.*
5.2. Corporate Governance Code *Weak*	***Strengths:*** • *The Bulgarian Code for Corporate Governance was issued in 2007 and reviewed in 2012 and 2016.* • *The Bulgarian National Corporate Governance Committee appears to be the authority in charge of monitoring companies' compliance with the Corporate Governance Code in Bulgaria.* ***Weaknesses:*** • *As per EU legislation, Member States should adopt a Corporate Governance Code applicable on a "comply or explain" basis and require listed companies to explain departures from the Code's provisions. Bulgaria has not yet fully transposed such legislation and its framework lacks clarity in relation to the disclosure obligations of companies concerning their compliance with the Bulgarian Code for Corporate Governance. The Bulgarian Public Offering of Securities Act requires listed companies to disclose a "programme for the application of the internationally recognized standards of good corporate governance" and to explain "the reasons due to which the issuer was not in compliance with the programme", without making any references to the National Code or clarifying what "programme" means. As a result, disclosure offered by*

Key Areas and Rating	Strengths and Weaknesses
	companies when reporting their corporate governance practices appears to be mostly a "copy and paste" of the corporate documentation, failing to refer to the practices in place. Explanations are rare and – when available – rarely meaningful. Further, the Listing Rules of the Bulgarian Stock Exchange require companies listed on the BSE Main Market, Premium Equity Segment to "commit to apply the principles of corporate governance enshrined in the National Corporate Governance Code as approved by the Exchange" without giving companies the option to deviate from the Code's recommendations. The Code, in turn, provides that "the Code is to be adopted and implemented according to the "comply or explain" principle. It means that companies should comply with the Code, yet if they do not, their corporate boards must explain and disclose the reasons for non-compliance." In practice, to comply with the Listing Rules, companies just vaguely declare that they comply with the Code, while the Bulgarian Stock Exchange lists on its website (http://www.bse-sofia.bg/?page=CorporateGovernance) all companies that have declared to comply. We wonder whether such a declaration of compliance really means full adherence to the Code. We believe that all pieces of legislation should be consistent and refer to the "comply or explain" principle. This should be combined with appropriate monitoring activities. • *Despite the National Corporate Governance Committee's commitment to conduct annual monitoring reports, its website has only disclosed one 2012 study, which does not report how companies comply with the Code.* • *There is no case law referring to the Corporate Governance Code.*
5.3. Institutional Environment *Weak*	***Strengths:*** • *International indicators rank Bulgaria moderately well in terms of investor protection (Doing Business Index 2014) and competitiveness (World Economic Forum's Global Competitiveness 2013-2014).* ***Weaknesses:*** • *According to the 2015 EBRD Assessment on Accessibility of Court Decisions, It seems that case law is fairly inaccessible to the general public.* • *There are a few inconsistencies found in laws, regulations and the Corporate Governance Code concerning governance issues.* • *There are limited active players for the promotion of corporate governance in the country.* • *International indicators rank Bulgaria relatively poorly in terms of corruption perception (CPI).*