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**DISCLOSURE OF INFORMATION AND CORPORATE
GOVERNANCE OF BULGARIAN PUBLIC COMPANIES**

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Introduction

The disclosure of information is a sine qua non for good corporate practice. Irrespective of the corporate governance model (Anglo-Saxon or continental), the disclosure of information in the corporate life is established and developed via various legal and non-legal instruments and rules. In Bulgarian transition economy the disclosure of information by a public company is set up by a system of legal norms. The state initiates and adopts the legal provisions for the disclosure of information. The state – Bulgarian National Securities Commission (BNSC) monitors the compliance of the respective rules. It is not difficult to draw a conclusion, that the “top-down” approach, shaping corporate governance in Bulgaria, is a phenomenon typical for the economies in transition. It models the practice of disclosure of information by public companies. From the perspective of some companies the top down approach is regarded as an overregulation and an extra burden, imposed by the state. Disclosure is not regarded as an advantage for the public company’s image.

The objective of this paper is to present to the South Eastern European corporate governance community the achievements and the problems on the way towards the establishment of a modern pattern of disclosure of information by Bulgarian public companies. The process is seen by the authors as a mutual effort of the legislators, regulators, boards members of the public companies, SROs and the stakeholders. Relevant to this view is the paper's structure. The paper sheds light on the following issues:

- ***A systematic view of Bulgaria’s legal environment*** and the disclosure of information by public companies/ legislators’ and regulators’ approach towards the disclosure of information/;
- ***A bird’s eye view on the disclosure of information*** :the status quo and the problems, related to disclosure /public companies’ approach towards the disclosure of information/;
- ***The establishment of investor relations*** practice in Bulgarian public companies /stakeholders - NGOs approach/;
- ***Present trends in the disclosure of information-*** about the amendments in the legislation concerning the disclosure of information

Part one :***The legal environment for the disclosure of information by Bulgarian public companies or does Bulgaria's legal environment meet the OECD principle on disclosure of information?***

Disclosure and transparency are among the fundamental principles of the corporate governance concept, on one hand, and of good practice of corporate governance, on the other. In transition economies the state initiates the introduction of the above principles. The business community has to comply with them. The legislation transforms the concept into norms and requirements, which the public companies have to comply with. A few laws set provisions for the disclosure of information in Bulgaria: the Commercial Law, the Accounting Law, Law on Independent Financial Audit, Law on Public Offering of Securities- LPOS(1,2,3,4).

Bulgaria's legal system, like the legal systems in the developed countries, recognizes **two systems of disclosure-public disclosure and non-public disclosure**. *Public disclosure* usually refers to those reports (annual, quarterly, prospectuses and ad hoc information) required by the LPOS. In addition to them, a company will often proceed to *other types of voluntary disclosure* in order to promote the company and to build the confidence of its shareowners.

In Bulgaria the legislation provides **for three levels** of disclosure by public companies:

- On annual and semi- annual basis (disclosure of the annual and semi annual financial statements);
- On project basis (disclosure of information about the public offering of securities - prospectuses for corporate securities and tender offers);
- On ad hoc basis (disclosure of price sensitive information).

The LPOS has provisions for the three levels of disclosure:

- Art.94 requires that every issuer has to submit to the BNSC annual financial statements within 90 days of the closing date of the financial year. The annual report has to be certified by a chartered auditor or a licensed audit company. The issuer must submit to the BNSC a six month report within 30 days after the expiration of the first six months of the financial year. BNSC releases the reports to the public. It is the Accounting Law,

which determines *the content and the requirements for the annual financial statements; annual balance; annual report on incomes and expenditures; annual report on cash flows; annual report of the owned capital. The law foresees a management report to be prepared by companies, liable to an independent audit.* The management report has to inform on main business activities of the company; main events, occurred after the balance sheet date; forecasts for the company's business; company's R&D; trends in the company's share prices. The management report or management discussion and analysis have to present easily understandable information about the company to the public - shareholders, investors, market, who do not have a sophisticated financial knowledge. The good practice of corporate governance requires the management and the boards' members of the company in question to share their view and to express their judgements on the company's performance and future plans. This new component highlights the efforts of Bulgarian government to improve the legislation on disclosure and to establish fair and transparent rules for the performance of Bulgaria's public companies (first level of disclosure);

- Art.81 defines the scope and the contents of the prospectuses. LPOS requires the disclosure of information about the issuer and the securities in order for the investors to make an accurate assessment of the economic and financial status of the issuer and the rights attached to the securities (second level of disclosure);
- Art. 98 requires the issuer to notify the BNSC about any changes in the business. Art. 145 requires the disclosure of participation. BNSC must release the above information. At present the legal requirements do not explicitly target price sensitive information. It is the proposed amendment on the acting LPOS, which sets a provision on explicit ad hoc disclosure (third level of disclosure).

The disclosure of information on the second level is regulated by the Ordinance on Prospectuses and the Disclosure of information (5). It sets the requirements for the scope of the prospectus and on the annual reports of the issuers of securities. The above regulations oblige the issuer to present a lot of information, pertaining to. the directors' remuneration, their interest in corporate shares and the risks, which are typical for the respective issuer's activities or its environment.

It is note worthy to point out that the Bulgarian legislation on disclosure follows the EU practice with respect to the disclosure regime required for public companies or issuers of publicly traded

securities. To a certain degree it mirrors the OECD principles on disclosure and transparency. *The fourth OECD principle states that the corporate governance framework should ensure that timely and accurate disclosure on all material matters regarding the corporation including the financial situation, performance, ownership and governance of the company.* (6) Special attention is paid to the disclosure structure. Disclosure should include, but should not be limited to, material information on: the financial and operating results of the company; company objectives; major share ownership and voting rights; members of the board and key executives, and their remuneration; material foreseeable risk factors; material issues regarding the employees and other stakeholders, governance structure and policy. When referring to the fact that it goes about good practice and worldwide accepted principles it is note worthy to state that transition economies including Bulgaria follow the above concept and principles. The comparison between the disclosure structure, advanced by the OECD and the disclosure structure, set by Bulgarian legislation reveals similarities and deviations. According to the present Bulgarian legislation (management report, required by the new Accounting Law) the companies do not disclose information in their annual financial statements about material issues regarding employees and other stakeholders, governance structure and policy. It is only the Ordinance on Prospectuses and the Disclosure of Information, which follows the standards of good corporate governance practice.

The existence of differences is not surprising. The economies in transition are at the very beginning of the establishment of the disclosure of information standards. The existing gap is an objective one, which can be explained with the nature of the transition from one system to another system. Bulgarian legislation and even the harmonization of the National Accounting Standards with the International Accounting Standards reflect the transition processes and nature, on one hand, and the continental concept of accounting and reporting. The legislation facilitates the change from pure reporting and accounting to disclosure. The regulator has to promote this process.

Irrespective of the existing differences, it is noteworthy to point out that the Bulgarian legislation encourages fair and transparent business practice. This is a step ahead in the struggle with corruption and the gray economy. For the public companies and the capital market per se the Bulgarian legislation on disclosure sets effective barriers against assets stripping, manipulation with securities prices and insider trading. From the perspective of the foreign investors the

legislation on disclosure could be labeled friendly: the established norms and rules follow the good practice in the developed market economies on one hand, and on the other - they encourage fair and transparent business. Stating it in another way: Bulgaria's legislation on disclosure of information encourages the development of modern pattern of corporate governance and minimizes the gap between local and the world wide accepted norms and rules.

The review of the basic legal requirements on the disclosure of information encourages the drawing of some conclusions:

- Bulgarian legislation sets up a broad framework for the norms and principles of corporate governance;
- The legal requirements on the disclosure of information (Commercial Law, Accounting Law, Law on the Independent Financial Audit, LPOS and the Ordinance on Prospectuses and the Disclosure of Information) provide conditions for disclosure ,similar to the conditions of disclosure in developed market economies;
- Bulgarian legislation sets up disclosure standards, which support the development of the local capital market.

Part two:***A bird's eye view on the status quo of the disclosure of information in Bulgarian public companies***

The legal framework for disclosure of information encourages the good practice of corporate governance in Bulgaria. It is interesting to trace out what the attitude of local public companies towards the legal requirements is or if there are any problems in terms of compliance. It is a well known fact that the transition from legislation towards implementation and compliance is a difficult process. In Bulgaria some of the public companies consider disclosure a burden and an instrument of state overregulation. There are a lot of discussions on the roots of the problem and on the work out of adequate measures to sort it out. Some explain the lack of disclosure with old socialist habits and traditions. The problem is seen as a purely subjective one. A lot of efforts are put into education of management and boards members in terms of transparency and disclosure. Politicians, regulators and academics try to find adequate measures, stimuli and enforcement measures in order to make the public companies more active in disclosure, neglecting the real problem.

Disclosure is typical for the developed market. The undeveloped market does not encourage the disclosure of information. This could be considered one of the main reasons and it sheds light on the attitude of some local public companies towards disclosure. Disclosure as a principle and as a requirement is a product of the developed capital markets economies. The problem with disclosure, seen by the regulators, professionals and foreign investors, is typical for the transition from a planned towards a market economy. The efforts to sort out this problem have to take into consideration some objective trends. The improvement of the disclosure practice will have an impact on the capital market development in the transition economy, on one side, and on the other- will strengthen the investors' confidence.

The theoretical speculations could be supported *by the results of the projects and surveys, implemented by the Center for Economic Development - Sofia/Bulgaria/ and other Bulgarian NGOs (7); foreign experts(8) and Bulgarian consultants(9) in the period:2000 -2002. They shed light on various aspects of the status quo of the disclosure of public information by local companies.* One of the projects had to reveal the level and quality of disclosure of information

by Bulgarian public companies. The self assessment approach was used in order to diagnose the level of disclosure practice. The answers of the boards members and managers of 167 public companies revealed interesting trends in terms of quality of disclosure and the attitude towards the disclosure. Disclosure of information was ranked very high by the Bulgarian directors.

A project, funded by the World Bank and executed by foreign experts cooled the enthusiasm of the Bulgarian directors. The assessment, based on the international expertise did not mark excellent the disclosure of information by Bulgarian public companies. The controversial estimations reflect the status quo of the disclosure of information /see Table below/. The conclusions drawn by the results of both projects present an important information about the practice of disclosure of public information in Bulgaria, on one hand, and about the gap between the legal environment and the practice of disclosure, on the other.

Level of disclosure in Bulgarian public companies

Criteria	Self -assessment of the directors of 167 Bulgarian public companies	Assessment by independent foreign experts
1. Compliance of Bulgarian public companies with legal requirements of disclosure	1.1 More than 2/3 of Bulgarian public companies comply with the legal requirements 1.2. 1/2 of Bulgarian public companies face difficulties to comply with legal requirements on disclosure	1.1. The scope and the quality of the disclosed information do not meet the legal requirements
2. Motivation of the corporate board members of Bulgarian public companies to disclose information	2.1. The corporate board members are not motivated to disclose information. 2.2. Only 1/5 approved the requirements for the disclosure of financial information.	2.1. There is no motivation for the corporate board members level for disclosure 2.2. The disclosure of information is considered a leak of information, from which the competition may only benefit.

Source: Corporate Governance Assessment Report-2000- Corporate

Governance Initiative/Vitosha Research 2000
Assessment Report of Corporate Governance, World Bank, 2000

The latest research on the disclosure of information by Bulgaria public companies reveals interesting trends, supporting some of the previous estimations and presenting new data:

- Less than a half of all public companies comply with the legal requirements of disclosure according to the statistics, released by BNSC. This group includes: companies, whose securities are traded on the official and unofficial markets of Bulgarian Stock Exchange; among them are some blue chips companies; local and internationally owned companies.
- More than a half of all Bulgarian public companies do not meet all legal requirements for disclosure according to the statistics released by the Bulgarian National Securities Commission. The group includes: companies, whose securities are traded on the official and unofficial market of Bulgarian Stock Exchange; some of the biggest state owned companies; some of the biggest ex privatization funds and some of the blue chip companies.
- The most frequent omissions in the annual financial statements are as follows: lack of management report on the results and future activities; lack of information on the share prices.
- The lack of relation between economic performance of the public companies and their disclosure practice.

The survey on the legislation and the disclosure practice or in other words the survey on the level of compliance encourage the formulation of the following conclusions:

- The Bulgarian legislation and disclosure practice mirror the norms and standards of good disclosure practice;
- The legislation and regulation encourage the transition from the reporting and pure accounting system to disclosure standards;
- Both objective and subjective barriers block the introduction of the modern disclosure standards;
- One of the weaker links in the legislation and the disclosure practice is the lack of real management *report or management discussion and analysis (MD&A)*. It is well

known that the management view on the company's activities and future plans are very important for the investors. The future efforts have to sort out the issue;

- ***The case study survey , implemented by the Center for Economic Development in 2001, revealed a lack of good communication between the public companies and the shareholders and investors.*** The progress, registered in terms of disclosure of public information is not supported by an adequate system for investor relations. Only a few Bulgarian public companies formalize their investor relations or stating it in another way only a few Bulgarian public companies have integrated investor relations units in their structure. Hence the training programme, run by the Centre for Economic Development for investor relations, could be considered very important. The programme targeted the management and the directors of Bulgarian public companies. It was driven by the role of investor relations in the modern disclosure practice. The well developed investor relations strategy facilitates and supports the establishment of good corporate governance practice.

Part three:***Investor relations - a new trend in Bulgarian public companies disclosure activities (Center for Economic Development experience – www.ced.bg)***

An effective system of corporate governance is a critical component in the development of a capital market and of Bulgaria's transition to a market economy. Sound corporate governance practices promote investor confidence in the integrity of the capital market and in those companies who follow good corporate practices. The company following good corporate governance practices will have a better opportunity to grow its business by attracting capital (domestic and foreign) and achieve a greater valuation of its overall business in a sound capital market. Investors, management, and employees all benefit from this approach by their investment in a business which is stronger, coupled with an ability to realize the return on their investment through a capital marketplace, that is, the stock exchange.

Despite of a series of positive developments in Bulgaria in the last several years, the Center for Economic Development (CED) recognizes that good corporate governance practices cannot simply be legislated and that the private and public sector must jointly work to improve corporate governance and encourage enforcement of and compliance with legislation. Bulgaria is still developing its legislative and regulatory structures and, perhaps more importantly, must still develop the human resources and corporate culture, essential to uphold good corporate governance systems.

Building on its achievements in previous years, in 2001 CED has implemented a corporate governance program to improve companies' corporate practices beginning with investor relations training seminars including accounting presentations. The accounting presentations are seen as tool to enhance management' skills and a component of an investor relations program. The project is being implemented based on a subcontract between the Bulgarian Capital Markets Project and the Center for Economic Development.

The objective of the investor relations/corporate governance program is to prepare issuers, underwriters and the BSE/S (with the involvement of the Securities Commission) to successfully attract capital, supply long-term fixed income securities/equity securities and increase

confidence, integrity and liquidity in the market/Exchange. In addition, an increase in the number of listed securities will improve the efficiency of the capital market with a resulting compounding of the positive effect.

In Bulgaria, as in many transition economies, managers, board members and shareholders of newly formed, joint stock companies are unaware, not only of their rights but of their responsibilities. Moreover, managers of these companies lack the skills and know-how to systematically produce, process and provide sophisticated information. This information deficit adds another element of risk to investor and lowers the (potential) market value of companies and their ability to raise capital on more attractive terms. In addition, the information deficit inhibits the movement of capital into the most productive long-term uses. An efficient capital market that is based on good governance will select the businesses that can most efficiently produce valuable goods and services for the economy.

Bulgaria's capital market is in its infancy and thus, is still viewed with suspicion. An IR program will partially reduce this suspicion and diminish investment risks. By working with the handful of underwriters and issuers already assisted by the Resource Center, we aimed at preparing a pilot group of transaction that will serve as an example for future issuers, investors and underwriters. This group illustrates the value of good corporate governance and the importance of underwriters and investors to expect better disclosure, transparency and accountability.

More specifically, CED has organized a series of four training seminars for Bulgarian joint stock companies' representatives in the period from June to October 2001 with approx 55 participants (board members, CEO, financial managers, and heads of investor relations departments, representatives of holding companies and private pension funds). Their goal was to assist Bulgarian joint stock companies to establish and developing efficient relations with current and potential investors by providing an opportunity for their representatives to participate in the two-day practical training seminars aimed at shaping specific practical skills.

The lecturers in the seminars were distinguished Bulgarian experts in corporate governance with extensive practice and teaching experience, as well as representatives of institutions directly related to the issues in question, namely – the Bulgarian National Securities Commission,

Bulgarian Stock Exchange - Sofia and the Institute of Certified Public Accountants. The project is being implemented in institutional partnership with the multinational company PriceWaterhouseCoopers. The company experts presented the accounting aspects of the topic.

The agenda for the seminars has been agreed on as a result of a series of consultations with the Capital Markets Project Team and the CED Resource Team Members as follows:

- prof. Bistra Boeva, University of World and National Economy, former SEC Commissioner
- Valentin Nedev, Member of the National Securities Commission
- Dr. Vessela Stancheva, Attorney-at-Law
- Manu Moravenov, Director, Bulgarian Stock Exchange – Sofia
- Blenika Djelepova, PR Expert, Center for Economic Development
- Petko Dimitrov/Gueorgui Nikolov, PricewaterhouseCoopers
- Boyko Kostov, Institute of Certified Public Accountants
- Dr. Stefan Petranov, Member of the Board, Golden Lev Investment Company
- Dr. Christo Pamukchiev, Bulgarian Consulting Group
- Nikolay Stoikov, Executive Director, ING Pension Insurance Company
- Kamen Kolchev, Manager, Elana JSC

The agenda covered broad range of topics that relate to investor relations' strategy.

Follow-up activities within the project envisage offering on-the-job training to interested seminar participants. Additional TA to develop an investor relations program and model slide show presentations will be provided to Bulgarian companies ready to issue corporate securities.

Part four:***Present trends in disclosure***

Irrespective of the problems the Bulgarian public companies ***are progressing on the way of establishing a good practice of disclosure***. New amendments of the LPOS are on the way. Some of these amendments target the improvement of disclosure of public and non-public information:

- The amendments foresee the disclosure of conflict of interests by the boards' members. The adoption of the provision will increase the level of fairness and transparency in Bulgarian public companies and will limit the assets stripping of the respective company;
- A special legal provision for investor relations director is opening a new page in Bulgarian corporate governance. According to the proposed amendments Bulgarian public companies have to integrate a new director in their governance structures. The practical dimension of the legal provision is clear- an improvement of the general communication and disclosure climate of Bulgarian public companies;
- A new norm of disclosure is envisaged –a ***management report and a report on the completion of the annual corporate governance programme***.

These provisions will improve the legal framework for the disclosure of information in Bulgarian public companies. From the perspective of the OECD principles it is a step ahead and a promise for modern norms and standards. The positive effect has to be estimated with the respect of the harmonization of the National Accounting Standards and the introduction of the IAS for Bulgarian public companies in the foreseeable future /2003-2005/. The results of the envisaged improvements of the legislation will strengthen the whole system of corporate governance checks and balances in Bulgaria. The missing parts of the puzzle are good practice and the sine qua non position of the disclosure of information. The mutual efforts of the State, business and the stakeholders could work out a way to find the missing pieces. Lets start!!!

Sofia, May 2002

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