# LEGAL FRAMEWORK OF FDI IN BULGARIA – PROBLEM AND SOLUTION

**By**

**Nataliya Mitkova Lorinkova**

**THESIS**

Submitted to
KDI School of Public Policy and Management
in partial fulfillment of the requirements
for the degree of

MASTER OF BUSINESS ADMINISTRATION

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**ABSTRACT**

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## I. Introduction

"The wind of change blows straight

Into the face of time

Like a storm wind that will ring

The freedom bell for peace of mind"

13 years ago it was Scorpions who announced to the Western part of the world that somewhere something was changing – for good or bad. One thing was certain – the so called Eastern block was done with – it was no more the closed, little known of part of the world – it was a new market, a new place to trade with and to invest in.

After the changes of 1989 Bulgaria entered a new phase in its historical and economical development – the so called transitional period. Now, 13 years later Bulgaria has not yet completed the transitional period of its economy and privatization, unemployment, low wages are still part of the everyday life. Unlike other countries in similar situation – such as Slovenia, Hungary or the Czech Republic – Bulgaria is still behind with the adjustment of its market mechanism and the overall economy.

Why? What were and still are the problems in Bulgaria?

The first problem to be defined is corruption and the next one … The next one is not that well defined, yet lots of economists and legal experts claim that the transitional economy in Bulgaria was unsuccessful due to the slow changes in the legislation system and unfavorable foreign investments laws.

So, the main purpose of this research is to examine the Bulgarian foreign investment legislation, to find out its weak points and answer the questions:

Do Bulgarian laws need to be changed? What can be changed to attract more foreign investments to Bulgaria?

## II. Objectives of the research

The objectives of the research can be defined as follows:

1. Detailed research and examination of Bulgarian foreign investments related legislation
2. Analysis of the current problems in the Bulgarian FDI related laws and suggestions for positive changes.

### i. Scope

This research is focused on Bulgaria and its legislation system.

The company discussed in the case study is the South Korean Samsung Electronics Corporation, which is in connection with the author's personal and professional experience.

### ii. Approach and methodology

Qualitative methodology is used.

The authors approach is based on descriptive analyses, utilization of her personal, educational and professional experience, as well as on case-studies based analysis.

**3. Expected results:**

1. Two main acts need to be changed in order to attract more foreign investments in Bulgaria.

## *Acknowledgements*

*Not only this research but my whole course work would not have been possible without the help of so many people – without the support of my family, friends and professors. To all of them I express my genuine gratitude: Thank you!*

*Thank you, Nick for letting your wife pursue her education, without a single word of objection or resignation. I love you.*

*Thank you, Plamy, for loving your Mom and never accusing her of leaving with you with Granny and going to study thousands of miles away from you – your "Mommy, I love you so-o-o-o much" is my biggest reward ever.*

*Thank you, Mom and Vale, for …everything.*

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*My stay at KDI was not only studying – it was a lifetime experience, worth a lot to me. Thank you, everybody who made it possible.*

*2003, February*
*Maryland, USA*

## Preface

*…No time – "gotta" run to work.*

*Wait a second - it's Friday – T.G.I.F. – the traffic jam is not that terrible on Friday. This means I still have some spare minutes to turn on the computer and read the news. Let me see what's going on home.*

*Where is "home" in fact? It's more than two years since I left my country pursuing first my education and professional goals, then my personal happiness. Having lived and experienced life in both the Eastern and the Western world, I still have this feeling of belonging to a small Eastern European country; I still feel that my home is somewhere, there, on the Black Sea coast and in the skirts of Vitosha Mountain.*

*This research is an attempt to be part of my "home", to help – if only a tiny bit – the ongoing legal and market reforms, by finding out what can be made better – be it just one or two legal acts.*

*To my Bulgaria….*

## Contents:



### I. List of Tables

## I. Introduction

Established in 681 AC by khan Asparuh Bulgaria takes pride in its long history. For more than 13 centuries the country has had its ups and downs, going through different stages in its historical and economical development. Following the changes in 1989 when the world witnessed the collapse of the socialist block, Bulgaria entered a new, the so transitional market period.

Yet, the reforms were not that easy and not that quick as anticipated. Bulgaria had a late start in the privatization of the state owned companies, the agricultural and the legislation reform also started wrongly. All these factors combined with the high unemployment rate and widely spread corruption, proved to impede the necessary reform. After wasting several years Bulgaria has been able to determine its short and long-term goals, such as joining the EU, NATO and establishing market-driven economy. At the same time Bulgaria opened its market for both national entrepreneurship and foreign investment. In 1996 the country joined the WTO, thus being one of the first Eastern European countries to be admitted to the organization.

After joining the WTO and starting EU accession negotiations Bulgaria faced more and more obligation, since it now has to develop its economy, to attract foreign investments and to comply with the regulations of the WTO and EU at the same time.

The research that follows examines the current situation with foreign investment in Bulgaria together with the legislation that governs the foreign investment. The purpose of the research is to find out what and how can be changed in the legislation in order to make Bulgaria more attractive for foreign investments ***- direct and indirect***

Basing the paper on  a detailed research, and adding to it my educational and professional experience, I decided to include in it real, personally experienced case studies, describing and analyzing two different scenarios of foreign investors on the Bulgarian market.

The purpose of the research and the expected result is to suggest a possible way of improving the Bulgarian legislation to the necessities of a market economy, open for and reasonably guaranteeing foreign investments.

# II. Body of Thesis

## III.1. Foreign direct investment – concepts and data

### 1. Overview

World foreign direct investment (FDI) has grown rapidly since the early 1980s. Indeed, FDI has become one of the most important means of integrating world economy and a major factor in the globalization of trade and economy. Global flows of FDI have grown phenomenally over the last ten years, rising by 5 times for the period 1990 – 2000. The table and the diagram below show the FDI inflows for the world and for the different regions.[1]

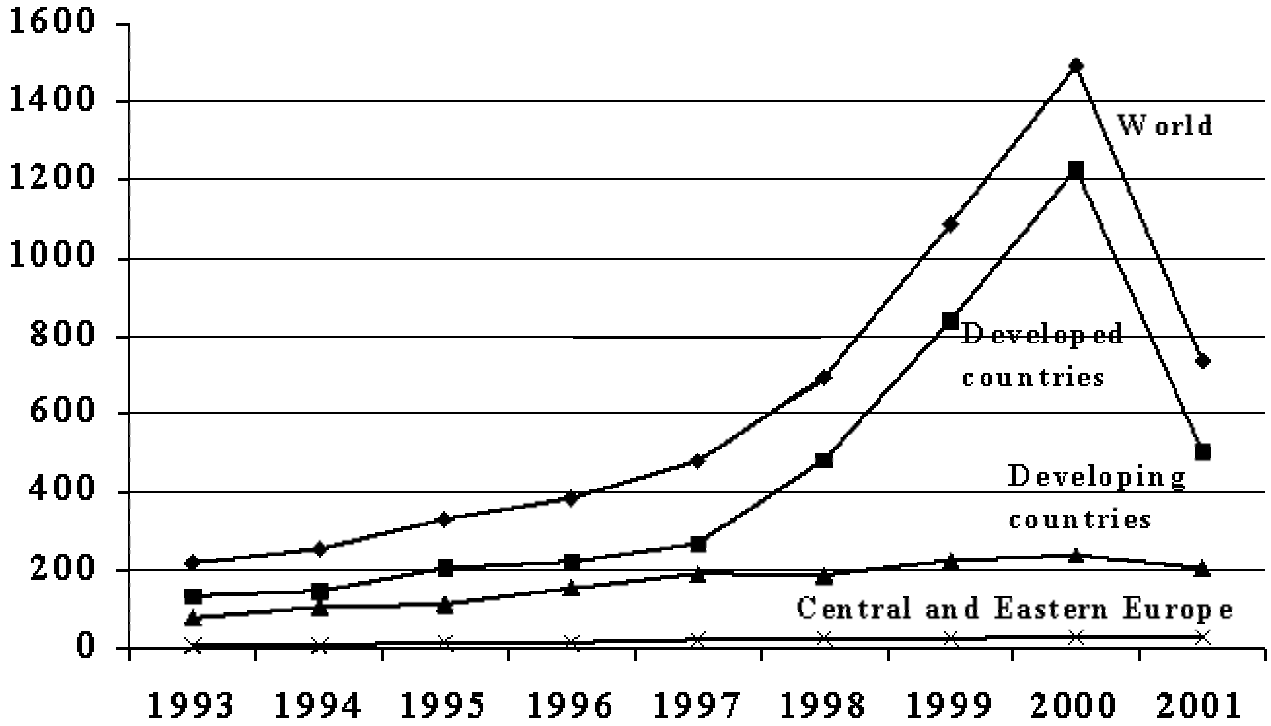
[1] Source: UNCTAD/DITE report – 2002

*Table 1*

**FDI Inflows, selected years (millions of dollars)**

| Indicator | Inflows | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Year | 1970 | 1975 | 1980 | 1985 | 1990 | 1995 | 2000 | 2001 |
| Country/Group | | | | | | | | |
| TOTAL WORLD | 12,586 | 26,580 | 54,945 | 57,596 | 202,782 | 330,516 | 1,491,934 | 735,146 |
| Developed countries | 9,477 | 16,971 | 46,530 | 42,693 | 164,575 | 203,311 | 1,227,476 | 503,144 |
| Western Europe | 5,207 | 10,160 | 21,427 | 16,762 | 96,803 | 118,265 | 832,067 | 336,210 |
| European Union | 5,127 | 9,879 | 21,317 | 15,879 | 90,213 | 114,439 | 808,519 | 322,954 |
| Other Western Europe | 80 | 281 | 111 | 883 | 6,591 | 3,827 | 23,549 | 13,256 |
| North America | 3,083 | 5,947 | 22,725 | 21,862 | 56,004 | 68,027 | 367,529 | 151,900 |
| Other developed countries | 1,187 | 864 | 2,377 | 4,069 | 11,767 | 17,019 | 27,880 | 15,034 |
| Developing countries | 3,109 | 9,609 | 8,380 | 14,873 | 37,567 | 112,537 | 237,894 | 204,801 |
| Africa | 747 | 790 | 380 | 2,407 | 2,483 | 5,743 | 8,694 | 17,165 |
| Latin America and the Caribbean | 1,438 | 4,295 | 7,485 | 7,278 | 10,282 | 30,866 | 95,405 | 85,373 |
| Asia and the Pacific | 924 | 4,525 | 516 | 5,187 | 24,803 | 75,928 | 133,795 | 102,264 |
| Asia | 787 | 4,501 | 396 | 5,110 | 24,251 | 75,217 | 133,707 | 102,066 |
| West Asia | 168 | 2,610 | -3,162 | 740 | 2,141 | 3 | 688 | 4,133 |
| Central Asia | - | - | - | - | 4 | 1,484 | 1,895 | 3,569 |
| South, East and South-East Asia | 620 | 1,891 | 3,558 | 4,371 | 22,106 | 73,729 | 131,123 | 94,365 |
| The Pacific | 136 | 23 | 119 | 77 | 552 | 711 | 88 | 198 |
| Central and Eastern Europe | - | - | 35 | 30 | 639 | 14,668 | 26,563 | 27,200 |

***Diagram 1***




A well known truth, confirmed by the diagram above is that FDI inflows and outflows "tend" to circulate among the developed countries, although it is the low and middle low income countries that need foreign investment as alternative source of capital to finance national development in addition to the bilateral and multilateral aid. With no doubt, FDI is now the largest source of foreign private capital, reaching developing countries and a significant source of development finance. Yet, for all its potential, foreign investment has much more complex nature. After all it is just the source of capital, which might or might not bring benefits to the host country – depending on the mode of entry, the conditions of the host economy and the country's ability to regulate foreign investment.

*One of the purposes of this research if to prove that country's ability to regulate foreign investment is a crucial factor for attracting and utilizing foreign investment.*

## 2. Types of FDI

### a) Classification of FDI

Direct investment undertaken by foreign firms in a host country, can take the form of either Greenfield investment or Merger and Acquisitions (M&A), depending on whether newly-created assets are coming under control of the foreign firm or existing assets are just being transferred to the foreign firm. In the case of M&A we can draw a further distinction between *cross-border mergers*, which occur when the assets and operation of firm from different countries are combined to establish a new legal entity, and cross-border *acquisitions* – in the latter case the control of assets and operations is transferred from a local to a foreign company.

As far as the host country is concerned, the Greenfield investments are deemed to be more beneficial to it, since the Greenfield investments are supposed to create new employment opportunities and bring new technologies and know-how.

Yet, there are other factors that need to be assessed in other to determine whether and to what extent FDI develops the host country's economy. Foreign companies are thought to be attracted to recipient countries for a number of different factors, e.g. political stability, market potential and accessibility, repatriation of profits, infrastructure, and ease of currency conversion. National legislation is one of the key factors that can support better investment security for local markets, fair competition and corporate

responsibility through defining and enforcing equitable, secure, non-discriminatory, transparent investment practices. (WSSD 1995, Habitat II 1996).

*This paper, in particular, examines the Bulgarian national legislation and its effect on foreign investment.*

**b) Location of FDI – factors affecting the location of FDI**

If trying to analyzing the factors affecting the location of FDI, it may be useful to divide FDI into three different groups or types, *natural resource-securing type, market-securing type, and cost-saving type.* The factors determining the location of FDI are different for these three types of FDI. For FDI of the *natural resource-type,* availability of natural resources is undoubtedly the most important determinant of FDI location. Japan is an example for actively undertaken FDI outflows of the resource-securing type in the 1960s. Some other examples are iron ore mining in Australia and oil exploration in Indonesia. This type of FDI can be traced in Eastern Europe and in Bulgaria also, though the resource –securing FDI is not the most significant investment inflow for the transitional European economies.

As for the second type of FDI, the *market securing type,* a major determinant is the presence of sizable market, which is reflected in large population size and/or population with high income. Tariff-jumping FDI, which is induced by import protection through tariff or non-tariff measures, can be categorized under market-securing type FDI. Foreign direct investment in Asia before the 1980s was dominated by tariff-jumping FDI. Because of the prevalence of import protection in Asia, FDI was the only way to sell in the local market. Unlike Asia, Eastern Europe has not implemented very restrictive

import protection, yet this type of FDI proves a clever solution for entering the recently emerged Eastern European markets.

The last type of FDI, discussed herewith is the *cost-saving FDI*. This type of investment is undertaken by export-oriented foreign firms. To maintain international price competitiveness, export-oriented firms need to set up a production base where production can be performed at low cost.

Having in mind the considerably low wages in Bulgaria, I am tempted to draw a conclusion that the country enjoys stable inflows of cost-saving FDI – not exactly…On the contrary, countries like Hungary and Poland receive more investment than Bulgaria, regardless of the comparatively higher wages. There are other factors, such as low inflation, undervalued exchange rates, and well-developed and well-functioning infrastructure such as telecommunications and transportation systems, which are important determinants of cost-saving FDI. In addition to these, key factors such as government, local economy situation, and last, but not least, foreign investment related legislation influence not only the inflow of all types of foreign investment, but also the positive and negative aspects of FDI to a host country.

***What is the situation in Bulgaria?***

## III.2. Foreign investment & its legal frame in Bulgaria

### B. FDI in Bulgaria – overview

#### 1. Introduction

Bulgaria is a proof that not all currency boards are destined to an Argentine denouement, with inevitable collapse and devaluation lying ahead**.** Having witnessed its gross domestic product plunge by one third between 1989 and 1997, it has risen by 13 percent for the last four years, driven by net export and domestic demand and in equal measures. In addition to the stability, brought by the currency board, the last two governments took measures to improve the country's economy and overall situations. A series of well-publicized and government-sponsored raids by police and tax authorities have gone a long way towards decriminalizing the economy. Real investment, depressed wages and restructuring led to higher productivity and enhanced competitiveness. All sectors experienced growth. At the end of 2001 FDI has reached USD 694.2 million. Yet, things are not that well-going in Bulgaria as they seem when reading newspaper articles or international observers' reports. The lot of simple people has not discernibly improved. Output is 30 percent below the Communist-era peak. Unemployment is very high by European standards (between 16 and 18 percent, reaching above 30 percent in some agricultural reasons of the country). The average monthly income in southern Bulgaria (an agricultural and textile area that borders Greece) is still USD 50 or less, one of the lowest in any economy in transition. Wages are still one forth of the EU's. Cheap labor has some advantages as it attracts foreign direct investment and generates foreign exchange (seasonal workers). Cheap labor in fact is the main reason for the Greenfield Turkish and Greek investments in the textile and shoe industry – but these

unsophisticated investors are not the ones who'd help and benefit the Bulgarian economy. And though Bulgaria cannot say it lacks FDI it is still far behind countries like the Czech Republic or Hungary. One thing is certain – if Bulgaria does not attract and keep foreign capital in the form of investments it won't be able to sustain a steady growth.

## 2. Trends and statistics

According to the last survey of the European Institute[2] Bulgaria ranks 7th in terms of FDI per capita for year 2000, ahead of Romania, Slovenia and Lithuania. The data on the FDI reveals that Bulgaria has been lagging behind the other EU applicant countries until 1997. Since 1998 the improved business climate and macroeconomic stabilization have contributed to the significant increase in the inflows of FDI and the competitiveness of the Bulgarian economy. In 2000 the FDI reached a record level of over USD 1 billion, making Bulgaria rank fourth among the ten other EU[3] candidates for FDI as a share of GDP for the period 1998 – 2000. The numbers for the FDI inflows for the period 1992 - 2000 are shown in the tables below:

***Table 2***

**Bulgaria - Foreign Direct Investment inflows 1990 – 2000**

(Source – World Fact book)

| YEAR | Privatization | Capital market | Greenfield+ | Total by years |
|---|---|---|---|---|
| | **USD millions** | | | |
| 1992 | | | 34.4 | 34.4 |
| 1993 | 22.0 | | 80.4 | 102.4 |

[2] Bulgaria and the Copenhagen Economic Criteria for EU membership - summary
[3] The ten other EU candidates, mentioned here, include the 8 Easter European candidates of the first group – Slovenia, Czech, Slovakia, Poland, Hungary, Lithuania, Latvia, Estonia + Bulgaria and Romania.

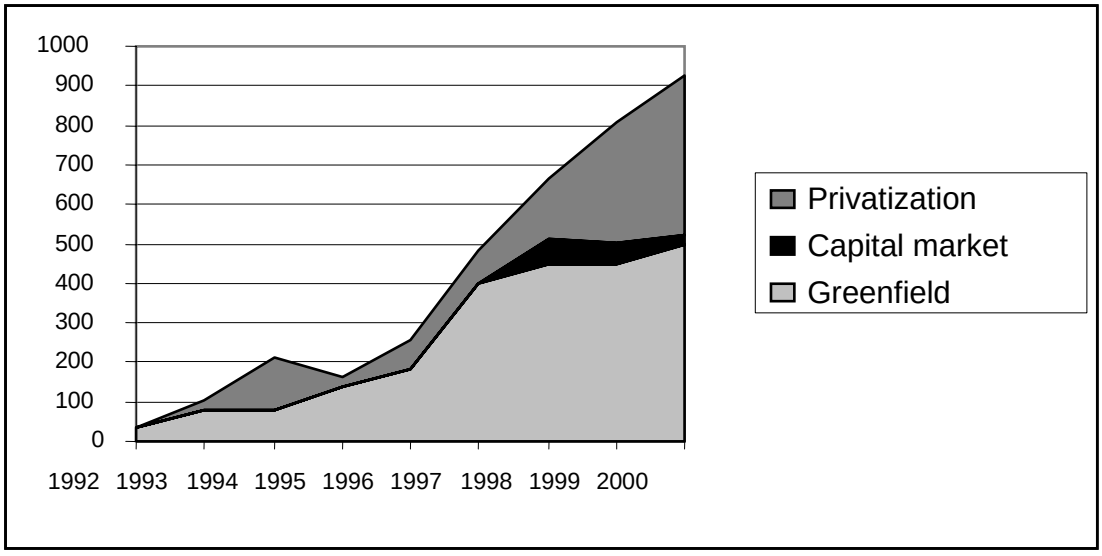
| | | | | |
|---|---|---|---|---|
| 1994 | 134.2 | | 76.7 | 210.9 |
| 1995 | 26.0 | | 136.6 | 162.6 |
| 1996 | 76.4 | | 180.0 | 256.4 |
| 1998 | 155.8 | 64.2 | 400.0 | 620.0 |
| 1999 | 305.7 | 53.1 | 447.3 | 806.1 |
| 2000 | 480.0 | 20.0 | 500.0 | 1,000.0 |
| Total 1992-2000 | 1,621.5 | 167.0 | 2,040.5 | 3.829.0 |

As seen from the table the FDI inflows increased significantly after 1997 – this was the year of introducing the currency board to Bulgaria, which guaranteed stability. The newly elected government in that year started an intensive privatization program, which attracted a number of foreign investors.

The diagram included below is an illustration of the Bulgarian FDI inflows.

***Diagram 2***

**Bulgaria – FDI 1992 – 2000 (in USD, million)**




Based on the data from the table and the diagram the following conclusions can be drawn:

i. The FDI in Bulgaria is clearly divided in two periods 1992-1997 and 1997 – until now
ii. The first period (1992 – 1997) witnessed more Greenfield investment inflows – almost double the amount of Privatization (M& A) investment inflows.
iii. The capital market investment is quite a new, not well known and not well developed type of investment.

In terms of foreign investors, Bulgaria traditionally enjoys large inflows of EU FDI inflows with Germany as number one foreign investor (totally USD 470.2 million until 2000), followed by Belgium (USD 412.5 million) and Italy (USD 372. 8 million). Divided by sectors, FDI was the largest in Industry, followed by Trade, Finance and Tourism.

In 2001 the industry profile of FDI is a bit different, as industry (manufacturing) proves to attract the largest inflows of FDI, followed by Transport, Storage and Communication.

***Table 3***

**FDI inflows in Bulgaria, by industry[4]**
**Year: 2001**
(USD million)

| **Total** | **694.2** |
|---|---|
| Manufacturing | 206.2 |
| Transport, storage and communication | 192.7 |
| Financial intermediation | 121.6 |
| Wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods | 93.2 |
| Real estate, renting and business activities | 20.1 |
| Construction | 14.6 |
| Hotels and restaurants | 12.8 |

[4] Source: BNB (Bulgarian National Bank) – 2002 report.

| | |
|---|---|
| Other community, social and personal service activities | 6.0 |
| Education | 4.3 |
| Mining and quarrying | 4.2 |
| Electricity, gas and water supply | 1.8 |
| Agriculture, hunting and forestry | 0.2 |
| Health and social work | -0.1 |
| Not-allocated | 16.9 |

The change in the investment inflows by industry sectors is by no means without reason. The FDI activity in the communication sector picked up in 2001 due to an important government decision – namely:

Foreign companies were allowed to participate on the Bulgarian telecommunication market.

Thus, licensing a Greek based Telecommunication Company for a Bulgarian mobile operator, the government provided for significant investment inflows in this sector. And this is not the only case, when a government decision affects positively or negatively the FDI activities in Bulgaria. The government determines certain priorities in the overall economic policy of the country, thus influencing to a large degree the country's investment inflows. What guarantees the investments and makes it easier or more difficult for investors to run their business is the relevant legislation.

## C. Foreign investments legal framework

### 1. Introduction

The Bulgarian legal system is part of the so called statutory system, which is based on enforced Acts, Codes and Bills. The Constitution (1991) serves as the foundation of the legal system and creates an independent judicial branch. The Acts and

Codes are passed by the Parliament and can be changed only by the Parliament. In addition to its inner laws Bulgaria has signed a number of bilateral and multilateral treaties and conventions, which regulate its international trade and politics, and frame its investment climate.

Bulgaria is said to have one of the most liberal foreign investment laws in the region. Foreign investment typically assume one of the following forms: establishing a joint venture with existing companies, state-owned or private; acquiring a company through privatization; setting up a new (Green field) venture; or making a portfolio investment.

## 2. Capital market (portfolio) investments – analysis and suggestions

**2.1. General overview -** Portfolio investment has been minimal given the relative recent development and inefficiencies of the capital market. The first record of portfolio investment dates back to 1997 – only 5 years ago and ever since then the foreign investments in the capital market has been very limited. The undervalued Bulgarian emerging market has an above average risk/return ratio. In light of the improved economic and political situation international credit rating agencies have expressed a willingness to review Bulgaria's credit rating that is currently B+ (S&P). According to the Bulgarian National Bank (BNB) statistics the portfolio investment for the period 1997 – 2002 amounts to USD 213 millions[5].

[5] Source: BNB 2002 report

## 2.2 Regulatory acts

Until 1998 Bulgaria's capital market was regulated by the Securities Act[6], adopted in late 1995 and amended in 1997 and 1998. The 1999 Public Offering of Securities Act is the currently valid law, which almost repeated the 1995 Securities Act. It currently regulates issuance of securities, security transactions, stock exchange and investment intermediaries. The regulatory body of the capital market is the Securities Commission, which controls all fields stipulated in the law. Since the very establishment of this Commission it has received ample criticism because of its bureaucratic treatment of players on the market.

## 2.3 Analyses of the portfolio investment regulatory acts & suggestions

The initial Securities Act, enforced in 1995 was severely criticized for lack of a number of regulations including:

1. Definition of a public company
2. Disclosure of information rules
3. Lack of sufficient control mechanism for the SSEC (Stock and security exchange commission) allowing it to guarantee that the stock exchange (hereinafter, the "SE") would operate according to high standards, especially as regards its Internal Rules.
4. Allowing companies to enact trading restrictions regarding their shares and making them effective against third parties by just writing them in the company's by-laws. Lack of publicity of the by-laws exposes third-party purchasers of

[6] Securities, stock exchange and investment companies Act

securities to substantial risk of bad title. While such limitations are acceptable as regards securities of "private" companies, they are totally unacceptable as regards securities admitted to public trade.

5. Under the old law, T-bills trading were not adequately provided for. In the context of a legal framework for securities provided for by an Act of Parliament (the LSSEIC), T-bills issuance and trade was governed by inferior legislation, such as a Regulation by the Bulgarian National Bank (hereinafter, the "BNB") and the Ministry of Finance. Said regulation, on the one hand, and LSSEIC and other legislation, on the other hand, are in outright conflict as regards a number of issues. That creates risks for investors relying on a formally illegitimate legal framework.

As obvious, the problems, which characterize the regulatory framework of the capital market, are common for both Bulgarian and foreign capital market investors, thus increasing the importance for better capital market regulations. The amended 1998 Securities Act provided for the following:

1. Definition of a public company: min. 10% of its capital is held by at least 50 shareholders as a result of an initial public offering of the company shares.
2. Public companies should be registered with the SSEC and should provide quarterly and annual company information;

Some other, I would say cosmetic changes, were made in the Public Offering of Securities Act, (POSA) which incorporated the old Securities Act in 1999. Yet, as far as the capital market is concerned lots of regulatory problems still remain for the foreign

investor (and for the Bulgarian one to large extent). Following the purpose of the research, the table below summarizes some of the problems, analyzes them and suggests appropriate legal changes:

**Table 4: Capital Market investments – problems and suggestions**

| Legislation problem | Explanation | Suggested action |
|---|---|---|
| 1. No protection for minority shareholders in publicly traded companies | Without proper legal protection any foreign investor would be unwilling to invest in a publicly traded company as a minority shareholder, facing the threat of dilution. | Draft appropriate legislation – providing for the possibility of waiving shareholders' right to subscribe for newly issued shares in proportion to their current shareholding must be restricted for public companies. In addition to high majority requirements (3/4 of the capital), high quorum requirements might be recommended. |
| 2. The existing T-bills registry system is not sufficiently operational. | The present registry system represents a mixture of registries and sub-registries managed by the BNB jointly with primary dealer banks. Such a system is an impediment to real market trade in T-bills. | Draft necessary legislation providing for a uniform, centralized registry system for titles and other rights in T-bills. |
| 3. T-bill trading is governed by inferior regulations. | Conflicts between inferior T-bill regulations and relevant Acts. | Place provisions governing issuance, trade and registration of T-bills in the |

| | | |
|---|---|---|
| | | POSA. (Public offerings of Securities Act). |

*Let me elaborate on problem No.3* – The Foreign Investment Law defines securities, including T-bills, with maturities over 6 months as investments. The T-bills themselves are typically short-term (3-months, 6-months and 1-year maturities). On a weekly basis the Ministry of finance holds and auction of Treasury bills. Commercial banks are the primary purchasers of these instruments. Foreign banks can participate in the treasure market only through a Bulgarian bank or the branch of a foreign bank duly licensed in Bulgaria. What are the legal problems in this scheme? What are the other problems for the foreign investors in the Bulgarian capital market?

**1. Problem:** *The regulations of the Ministry of Finance relevant to the T-bills are inferior to the legal Acts passed by the Parliament* (the Ministry of finance has no legislative power). Thus if both ministry regulation and a legal act regulate the same subject, the latter is more important and legally binding. In that way, any T-bill issuing or trading procedures, approved by the Ministry of finance might prove illegitimate in the long run.

**Suggested solution:** Provide for T-bills trading through an act of Parliament. In doing this, all conflicts between current T-Bill legislation and Public Offering of Securities Act must be resolved. The Parliament has two ways of accomplishing this task:

V. pass an addition, which regulates the issuance of T-bills placing this addition in the current POSA

VI. pass a new Act on Securities, which would include the T-bills issues

**2. Problem** – *Foreign Banks cannot participate directly on the Bulgarian treasury market*

This seems to be a far bigger and more complicated problem than the T-bills conflicting regulations. A rule like "Foreign banks cannot participate directly in the Bulgarian treasure market" automatically rules out a number of future participants. The two acts, which regulate the banking activity in Bulgaria, are the Commercial Code and the Banking Activities Act and they both specify that only a duly licensed jurist person can perform banking activities in Bulgaria. It is a very long and complicated procedure to establish a branch of a foreign bank in Bulgaria and to get all the necessary licenses. And hardly any foreign bank will ever do it for the only reason to participate in the treasury market. Yet, Bulgaria will only benefit if foreign banks participate on the treasury market – this is the only way to develop and enlarge the treasury market. What are the different options to solve the above mentioned problems?

*Unfortunately, drafting new regulations could hardly work – there are too many other rules – licensing, taxation, currency convertibility that need to be changed for allowing the foreign banks to be a direct participant in the Bulgarian treasury market. And a change won't work in the short-term. The capital market, not only the treasury one needs further development. The developing capital market will show and consequently bring the necessary legal changes – until then foreign banks have a couple of options for investing on the Bulgarian capital market:*

**Suggested solutions for foreign participants in the Bulgarian treasury market:**

a) Participate through a Bulgarian bank in the treasury market.

b) Establish a financial company, registered in Bulgaria and participate through it in the Bulgarian treasure market – establishing a financial company is much easier than establishing a branch of a foreign company – take my word on it!

**3. Problem - Tax Implications**

Tax legislature is one of the weakest points of the overall legal framework. It is inconsistent and does not allow special provisions for revenues associated with capital markets.

Foreign investors' participation in Bulgarian companies is also subject to dubious treatment. An investment is generally regulated by the Law on Foreign Investments, and is registered with the Foreign Investments Agency. In case a foreign investor has realized revenues from capital gains or dividends on the Bulgarian market, he may freely repatriate the proceeds to the home country, where they will be accordingly taxed (provided, of course, that there is an agreement for avoiding double taxation between Bulgaria and the home country). Before repatriation, revenues are subject to 15% withdrawal tax, which is subsequently refunded. The recent regulation[7] provides that the dividend and capital gains tax will be 15%. The withdrawal tax can be avoided given that there is an agreement for avoiding double taxation between Bulgaria and the country of registration of the company realizing the gains. The following three documents should be presented to the council of ministers to avoid the taxation:

- Certificate of registration of the legal entity in the country with which the double taxation agreement is signed.

[7] Corporate Income Taxation Act

- Certificate stating that the company resident in the country with which the double taxation agreement is signed is the real owner of the gains/dividends.
- Certificate that this company does not have any legal representation in Bulgaria.

As seen from above, it is not an easy job to provide all the above mentioned certificates and the Bulgarian legislator cannot be advised to simplify the procedure – an easier procedure for repatriation of capital gains might lead to avoidance of taxation. Still, there are a number of things that can be done to expedite, if not to simplify, the repatriation of capital gains:

**Suggested solution**: Draft appropriate legislation and bind the Council of Ministers to approve/disapprove of the repatriation of capital gains within 7 days of receiving the necessary certificates.

The current deadline, binding for the Council of Ministers is 45 days – it is a very long period to say “yes”, “no” or request additional documents to be presented.

Implementing any of the regulation improvements suggested above, constitutes a step towards improving the emerging Bulgarian capital market and its investment climate. True, there might be a number of other problems that need to be tackled in order to attract more investors to the Bulgarian capital market – not only regulatory problems. The capital market is too new for Bulgaria – which could be a good excuse not to criticize it and its regulations too hard. But the need for constant efforts for improvement of the relevant legislation is unquestionable. Investors need stability, predictability of the new market they are going to – relevant and good laws are the first and most important guarantee for investor’s rights.

# 3. Greenfield and M&A investments – analysis and suggestions

## 3.1 Introduction

The capital market made its "début" in Bulgaria in 1997. For the years after 1997 it accounted for approximately 4.5 % of the total investment inflows in Bulgaria, leaving the other 95.5 % to the other two types of investments – M&A and Greenfield investments. As supported by the statistics data (see Table 2), the Greenfield and M&A investments weigh almost equally on the Bulgarian foreign investments scales.

In fact, the first FDI in Bulgaria after the collapse of the socialist regime in 1989 were the Greenfield inflows from small Turkish and Greek shoe and clothes making companies, which used the cheap labor force in Bulgaria. M&A investment flows started "coming" in about 3 years, with the start of the privatization. Even now, more than 10 years later M&A investment and privatization are used as synonyms in many Bulgarian statistics data, references and other sources. This is not surprising, since privatization accounts for about 92% of the total M&A investment inflows. (The other 8% come from private companies, registered in Bulgaria and acquired by foreign investors).

With the start of the reforms the investment inflows increased, though not that much as would have been beneficial to help for a less painful and quicker transitional period. Bulgaria had a late start in the reforms – it lacked the necessary regulations and failed to start the privatization until two years after the collapse of the socialist regime[8]. The first act, regulating privatization – Act on Transformation and Privatization of State and Municipal owned Enterprises was passed by the Parliament and enforced in 1992. Not long after that followed the 1992 Foreign Investment Protection Act.

[8] The terms "socialist regime" and "communist regime" are used as synonyms in this research

*It might seem that those 2 years were not such a long period of time. Having in mind that a law cannot be drawn and passed by for a day it might have been not such an easy task for the first Bulgarian freely elected Parliament*[9] *to decide on enforcing the necessary acts. Other facts influenced the slow start of the reforms too – the unwillingness of the MPs to face and realize that the State owned companies had to be restructured, that the Bulgarian subsiding policies had to be changed and so on and so on. Common people, too, used to the old centralized economy, feared the idea that foreigners will buy and manage their companies. At the same time, other Eastern European countries like Slovenia, Hungary and the Czech Republic were quicker to adapt to the new situation and in the long-term did much better than Bulgaria did in restructuring their economies. They simply were quicker to draw and pass by the necessary regulations, to privatize quicker, attracting more strategic foreign investors, getting better prices for their ex-state owned companies. Falling behind the first two years, later fighting to catch back, Bulgaria was forced to sell state owned companies for less money, to close down production lines, which years earlier could have been successfully privatized.*

*Prof. Bernhad Seliger – University of Köln, in his doctoral dissertation "Democracy and Economics in Eastern Europe"- 1998 - focuses on the problems of the so called new democratic countries in Easter Europe, arguing that the more democratic a country is the more prosperous it proved to be as far as Eastern Europe is concerned. He points out that the first countries to change their laws and guarantee free elections, protect private property, guarantee entrepreneurs and investments rights were the first to*

[9] 1989 – 1992 Bulgarian Parliament

*complete successfully their economies' transitional period. Basing on the successful stories of Hungary, Slovenia and the Czech Republic, who were the first to re-structure their economies, on the grounds of relevant legislation and correspondent economic activities, Prof. Seliger proves his arguments. Hungary - the Eastern European leader and EU favorite is the number one recipient of FDI in Eastern Europe. Hungary, for certain was benefited by its important geographic situation, very close to Western Europe. But nobody gives money just because of geography – the truth is the Hungarians simply did better in attracting foreign investors.*

*It is impossible to change the past – neither the slow reforms, nor the late regulations. But there are always things that can be changed for better.*

*This research and the part that follows in particular analyze the current FDI regulations, identify problems and suggest solutions to them. Thus, the current acts and regulations, relevant to foreign investment could be improved.*

The first Act to regulate the foreign investment in Bulgaria was the 1992 Foreign Investment Protection Act. It was replaced in 1997 by the Foreign Investment Act, which is the currently active Act. Both in the former and in the latter Act the Bulgarian legislator makes no distinction between M&A investment and Greenfield investment – the legislator regulates the two types of investment in the same acts. Having in mind this and the almost equal amounts of M&A and Greenfield investments the next part of the research deals with the legislation problems of both M&A and Greenfield investments.

### 3.2 Analysis of M&A and Greenfield investments regulations

As long as foreign investment is part of the overall business and trade activities in Bulgaria there is a significant number of Acts and regulations closely or distantly relevant to the investment activities – starting from the Constitution as the supreme Act and adding Acts like the Commercial Code, Labor Code or Rights and Obligations Act.

There are, however, a few acts which are either specially drawn for regulating FDI or are very closely connected to the foreign investment activities in Bulgaria. Such are:

- Foreign Investment Act – 1997
- Act on Transformation and Privatization of State and Municipal-owned Enterprises[10]
- Public Procurement Act[11]

The major Act which defines and generally regulates foreign investment activities in Bulgaria is the Foreign Investment Act.

**a) Foreign Investment Act Issues**

The 1997 Foreign Investment Act (art. 2) extends national treatment to foreign investors. Thus, the foreign investor is guaranteed non-discriminatory treatment and has all the rights and obligations of a Bulgarian businessman or entrepreneur. This act also defines what a foreign investment in Bulgaria is (art.12 item (1) :

1. stock and shares of companies
2. right of ownership of buildings and limited real estate rights

[10] Replaced in March 2002 by Privatization and Post-privatization Control Act
[11] Referred to as Law on Public Procurement - LPP

3. right of ownership and limited ownership rights on chattel, classified as long term activities
4. right of ownership on affiliated parts of trade companies with more than 50 percent state or municipal capital as defined by Privatization and Post-privatization Control Act
5. Securities, including bonds and treasury bonds, as well as other derivative instruments, issued by the state, the municipalities or other Bulgarian juristic bodies with more than 6 months maturity term
6. credits, including financial leases, for a period not shorter than 12 months
7. intellectual property – subject to copy rights and its related rights, patentable inventions, useful models, trade marks, service marks and industry samples
8. concession contracts rights and management contract rights

As obvious, the above definition is quite detailed. In item 2 there is a technical mistake, which is hardly likable to cause any problems, yet the legislator should better use the term “right of ownership on real estate rights” or “right of ownership on real properties” instead of “right of ownership on buildings”. A foreign investment is not only owning a building – owning and managing a swimming pool or a tennis court by a foreign person is also an investment – or at least is usually treated like such, so this particular text should be corrected. As seen from the definition for a foreign investment owning of land is not considered to be an investment – because foreign individuals cannot own land in Bulgaria (this is a constitutional prohibition) However the Foreign Investment Act 1997 removed most restrictions on acquisition of land by locally registered companies with majority foreign participation. Local companies where foreign partners have controlling interest

must obtain prior approval (licenses) to acquire properties in certain geographical areas/zones. These zones are the zones of national interest (sea coast, preserved territories and so on) and in most cases license regime is applied not only to the foreign persons, but also to Bulgarian individuals and jurist persons.

In addition to defining foreign investment, Foreign Investments Act also guarantees compensation in the event of expropriation and allows for the repatriation of profits. The law does not limit the extent or amount of foreign participation in companies – with one exception – arms manufacturing: only firms with over 50 % Bulgarian participation can be licensed for international trade in arms.

Bulgaria's military complex employs more than 10 000 people and with the lost of the Russian markets after '89 is in gloomy situation. In 1998, the government developed a strategy for privatizing the military-industrial complex.

*The 1998 plan for the privatization of the military complex allows for the privatization of non-military operations and some defense firms, while ensuring that the government retains a blocking share (34 %) in strategic arms producing enterprises to guarantee the country's defense priorities. Regardless of the existence of the privatization plan the arm manufacturing complex is still state owned. Few workshops are working, while a significant number of the workshops are closed. Years ago the arm manufacturing complex was the second income generating company for Bulgaria (8 % of GDP after an oil refinery, which accounted for 11 % of GDP). At present, the complex works with about 30% of its capacity, struggling to restructure part of its product lines and convert to non-military products, while waiting for its privatization. Needless to say*

*the privatization of the military complex is an important and very difficult issue for Bulgaria and its government – the right strategic investor is still "wanted".*

As a whole, having in mind all said above, the Foreign Investment Act provides for very liberal and considerably well defined investment activities. In addition to the national treatment of foreign investors and repatriation of profits the law provides for expropriation compensations of foreign investors.[12] (There have been no cases of expropriation up to now since enactment of the Foreign Investment Act).

In addition, the current Foreign Investment Act – part 2 - also incorporates the basic regulations for the Bulgarian Foreign Investment Agency.

**BULGARIAN FOREIGN INVESTMENTS AGENCY**

The Bulgarian Foreign Investments Agency was established in April 1995 as a one-stop shop institution for foreign investors. It is a governmental body with the Council of Ministers for coordinating the activities of the state institutions in the field of foreign investments and for promoting of foreign investments in the country.

A key function of the Agency is to assist the companies in the investment process. It supplies the prospective investors with up-to-date information about the investment process in the country, legal advice, identification of suitable Bulgarian partners, co-ordination of the investment policy with other institutions, etc. The Agency has a staff of 27 experienced experts, and is headed by a Director. In addition to the Foreign Investment Act regulations, the Agency has its own Rules for its structure and its

[12] According to Article 26 of the Foreign Investment Act, property can be expropriated on the grounds of a law "for exceptionally important state purposes." Owners must be compensated with nearby property of equal value at current prices. Monetary compensation is also permitted with the consent of the property's owner.

activities. As specified by law the Agency provides the following services to foreign investors:

**Core services**

- Pre- and after-investment care
- One-stop shop
- Up-to-date information on all existing FDI in Bulgaria
- Detailed information on infrastructure investment projects
- Assistance when choosing the most appropriate form of investment
- Legal advice
- Investment projects databank
- Support for priority investment projects

The Foreign Investments Agency has been around for about 7 years now, providing guidance to foreign investors. The Agency maintains its own database about existing FDI in Bulgaria and investment projects. The official web site of the Agency, maintained in Bulgarian and English in many cases proves to be the first "stop" of a future foreign investor in Bulgaria.

**Problem:** The official site of the Foreign Investments Agency – www.bfia.org **–** is maintained only in English.

According to the statistics[13] number one investor in Bulgaria is Germany, followed by Belgium, Italy and Greece, which means that the native English speaking investors in Bulgaria are greatly outnumbered by other investors. It takes very small effort to add other translations – German, Russian, French or Greek to the official site of the Foreign

[13] Source: Bulgarian National Bank statistics

Investment Agency, which can be useful and very convenient to investors from different, non-English speaking countries.

**Suggestion:** Add links to other languages (German, Italian, French and other) to the official web site of the Foreign Investment Agency and its database.

Thus investors from different countries will be able to use the resources of the Agency's web page. It is a common believe that English is the language of business, and hardly a businessman knows no English. But both English and German are equally popular in Bulgaria as foreign languages, and many foreign companies come from non-English speaking countries. So, providing investors-to-be with an option for a language they would like to browse in is a question of convenience for the investors.

Discussing further the activities and the legal status of the Investments Agency it can be noticed that the Agency offers no services connected to privatization. Yes, it does exist to help investors and advice them on the most appropriate to their needs investment project, yet there is another agency – the Privatization agency – which is in charge of the privatization projects. Both the Investments Agency and the Privatization Agency are government bodies with the Council of Ministers supported by the State budget. While the Foreign Investments Agency has more consultant functions, the Privatization Agency has more regulative functions. The Privatization Agency monitors the whole process of privatization of any state owned company, and makes the final decision on who, in fact, is going to be given the right to acquire the company subject to privatization. The decision is supposed to be made after careful screening of all the potential investors, their financial status and the investment plan they have come up with. In many cases the Privatization Agency has been criticized for corruption based decisions, and in the last 2-

3 years there has been a very strong public and government demand for transparency of the privatization process. In addition to playing a major role in the whole privatization process, the Privatization Agency is the one, which registers and keeps track of all the currently announced for selling state owned companies. The, Foreign Investments Agency on the other side, has a database of potential investor projects. Thus, some one interested in investing in Bulgaria has to contact both Agencies in order to scan through and find the best investment opportunity (be it Greenfield investment or M&A investment, the latter being mostly privatization). It is absolutely true, that most future investors have a project or a company in mind, before "heading" for Bulgaria, yet, when presented with other opportunities for investment and properly guided by the correspondent Agency they might be interested in investing in another project, not the initial one. But communicating with two different government bodies is often time-consuming and not that effective.

**Problem:** Different government bodies being in charge of investment projects, on the one hand, and privatization projects on the other hand.

Thus, investors lack the opportunity to compare the pros and cons of all the existing projects at once, let alone the burden to the budget for the cost of the two agencies**.** Furthermore, there are less and less state-owned companies to be privatized (at present 85% of all ex-state owned companies are already private), which means less and less work for the Privatization Agency.

**Suggestion:** Merge the Investment and Privatization Agency, creating one Agency in charge of the Foreign Investments in Bulgaria.

The newly created agency might still have two Departments – Privatization and Investment, but it will use and maintain one database, thus serving better the needs of present and future investors.

Fully aware of all the legal problems a merge like the proposed one might cause, it might not be such an easy task – the Privatization Agency and the Foreign Investments Agency are regulated by different Acts, they have their own Rules and Regulations. Still, merging the two agencies should be based on the correspondent legal adjustments. My suggestion is to provide for the existence of a single Investment Agency in a future edition of the Foreign Investment Act, specifying the rights and obligations of the future Investments Agency.

Speaking of an Investments Agency and of the Foreign Investment Agency in particular, the legislator provides it with the right to declare an investment "a priority investment project". The FIA[14] reads like this:

"Art. 21. At the request of the investor the foreign investments agency may suggest to the Council of Ministers to establish inter-administrative group with representatives of the interested ministries and administrative bodies for providing institutional support to the investment projects, which the Council of Ministers may recognize as priority investment projects."

*Excuse me, but there are too many "may" in this article for it to sound as a rule – it is far more an advisory, than a regulative article. The Foreign investments agency "may suggest" …What if the foreign investments agency does not want to, or thinks it is*

[14] Foreign Investment Act

*not necessary to bother the Council of Ministers with a certain project. The legislator fails to say what happens if the Agency turns down the requestor. The Council of Ministers also "may" recognize a project as a priority investment project – but it might decide not to do so. Then what? There are no further regulations in this, or any other act. Knowing the situation in Bulgaria, I can state that all these "may-s" and the overall vague regulation of this issue provides for nothing else, but corruption – a very big problem in Bulgaria. If there is no clear definition of which investment projects are considered to be priority projects, benefiting by institutional support and other benefits quite a few government employees will be tempted to "claim" something "under the table" to declare a project a priority one. This can be easily stopped by passing appropriate regulations, defining priority investment projects on their own merits, thus denouncing the vague, highly subjective and easy to abuse rules of the current legislation.*

**Problem:** Lack of clear legal definition of priority investment projects.

**Suggestion:** Specify by law (in Foreign Investment Act) conditions to be met by a priority investment project.

Such pre-conditions, for granting a priority status to an investment project might be:

- Hiring and guarantying employment to more than 500 persons (unemployment rate in Bulgarian is between 17-18%, the highest for the region)
- Employing more than 200 or 300 persons in certain areas of the country, where the unemployment rate is considerably higher than the average.
- Investing a certain amount of money (specified by law amount of money)

- Investment in specified by law priority industries – agriculture, high-tech and so on
- Reinvesting more than 30% of their gains in the Bulgaria-based business

Thus, when there are clear and legally defined conditions to be met by a priority-to-be project the corruption among government employees in charge may be minimal and the investors can rely in advance on the benefits applicable to a priority project.

What, in fact are the priority project benefits and why is it beneficial for a project to be a priority one?

Under the current law a priority project enjoys the institutional support of a commission "inter-administrative group with representatives of the interested ministries and administrative bodies for providing institutional support to the investment projects recognized by the Council of Ministers as priority ones." (Art.21 FIA).
Furthermore Article 22 of the same act grants another right to the priority projects: "Art. 22. (1): At the request of the investor the foreign investments agency shall propose to the competent bodies to grant limited real rights on a real estate – state or municipal property, with the purpose of realization of a priority investment project." This means that a certain priority investor can be given the right to use a building with or without paying for the use. This benefit to a priority project might seem a minor, unimportant right, but it might and it has proved beneficial to a number of investors, especially those dealing with agricultural business (according to the Foreign Investment Agency for 2001 2 big foreign investors were given the right to use ex-municipally owned agriculture-related buildings for the needs of their investment projects).

Still, except for the above mentioned privilege no other priority investment benefits are defined by law.

**Problem:** Lack of legally defined benefits for priority investment projects.

**Suggestion:** Incorporate regulations, guarantying benefits to priority investment projects in the relevant laws

Giving a number of privileges to CLEARLY defined by law priority investment projects is one of the opportunities for Bulgaria to attract big, strategic investors – otherwise they can go to a neighbor country (Macedonia, Romania ) and enjoy similar high-quality, low-paid labor force. At present, priority investment projects enjoy institutional support. Until 1997 foreign businesses, investing more than USD 1 million in Bulgaria were allowed to use 3 years tax free period. This provision was revoked in the last edition of the Taxation Act, due to concerns expressed by Bulgarian companies, that investors were better treated than local businessmen. Unfortunately, the abolishment of the preferential treatment for priority investors neither helped the Bulgarian businessmen, nor provided for better tax revenue – it was only a drop in the ocean of tax problems of Bulgaria.

b) Taxation issues

The current Taxation Act treats equally investors and local legal persons, allowing only for priority application of international (bi-lateral and multi-lateral) tax treaties. No special provisions are made for foreign investors. The public opinion about foreign

investors' treatment varies, yet a great number of people think that some special taxation treatment of big investors has more advantages, than disadvantages.

The suggestion made below is based on an interview research, with a sample of 32 participants (17 Bulgarians, residing in Bulgaria and 15 Bulgarians, residing abroad) who were asked to answer the question "What, in your opinion, could be the best privilege for a foreign investor?" The results could be summarized as follows:

| Number of participants | Suggestion |
|---|---|
| 3 | Foreign investors should not be given any privileges |
| 15 | Let strategic foreign investors have a grace period for paying corporate taxes |
| 8 | Allow for low-interest credits for foreign investors |
| 6 | Allow for tax free period for foreign investors |

Joining the majority of the interview participants, I am suggesting the following to the Bulgarian legislator:

**"Provide for a tax grace period of 3 to 5 years for priority investment projects with no interest on unpaid taxes for the grace period."**

Such a regulation would give some time to investors before paying corporate taxes (15 percent profit tax and 10 percent municipal tax) and is by no means discriminatory against Bulgarian companies – investors are not exempted from taxes, they are given some time to start their business and to adjust to the Bulgarian market.

For obvious reasons this tax-related suggestion has no place in the Foreign Investments Act, no matter that it governs investment activities – rules, giving a tax-delay period for

priority investment projects shall be incorporated in a future edition of the Corporate Taxation Act.

In addition to the lack of tax incentives for investors, foreign entrepreneurs have asserted that widespread tax evasion combined with the failure of authorities to enforce tax collection from small and large privately owned Bulgarian companies, places foreign investors at a disadvantage.

**Problem: Wide spread tax evasion**

**Suggestion: Enforce strict rules and effective mechanism for tax collection**

As a rule, large ex-state owned, currently privatized companies – major investment objects – are more strictly monitored by government institutions and tax authorities. By paying all the taxes such companies and their owners find it very difficult to compete against grey economy companies, which do not pay taxes and produce cheaper goods.

*When asked to comment on obstacles for FDI in Bulgaria, a high-ranked official from the Ministry of Economy – chief of a Department,( a close friend of mine, who asked to remain anonymous) expressed his concerns that the high tax rates in Bulgaria are killing not only any foreign investment incentives, but the local business too. An incorporated business in Bulgaria has to pay more than 40 % from its income in taxes – corporate tax, patent tax, VAT, and has to contribute to the Social Security and Health Insurance Funds too. Thus a lot of companies choose to risk a fine and not pay taxes – as long and as much as they can, there is not enough tax revenue and no money in the budget and therefore more taxes are necessary for the state to be able to function. The only "exit" from this vicious circle is improved tax collection.*

Improved tax collection will not only guarantee higher revenue for the state budget, but will allow for a tax cut in the long run. The current government and the government officials have indicated their long-term intention to lower marginal rates as tax collection improves.

Another tax-related problem, underscored by investors, is the **frequent revision of tax laws,** sometimes without sufficient notice. In an attempt to solve this problem the Parliament is currently launching all draft acts on its web site and the public has free access to all the draft laws. A suggestion to the Foreign Investments Agency is to provide an e-mail based service, as all interested investors may subscribe to receive notices for oncoming legislation changes.

### c) Privatization Acts issues

Going deeper into the FDI related legal frame of Bulgaria, the next stop is the Privatization law. The 1992 Act on Transformation and Privatization of State and Municipal-owned Enterprises[15] was passed by in 1992 and amended more than 15 times until it was annulated on 19th March 2002 by the new Privatization and Post-privatization Control Act. The old Act ruled the privatization in Bulgaria from the very beginning of the privatization process and thus accounts for the majority of M&A investments in Bulgaria. According to this Act the Council of Ministers had a yearly privatization program, which included all the state-owned enterprises that were to be sold to investors in the coming year. Before being subject to privatization state and municipally owned enterprises were transformed in legal persons (in most of the cases in sole limited liability

[15] referred to as "the old Act" below

companies) by the Council of Ministers and as such they were sold to the future investors. The transformation, though rather costly, was necessary in order to determine and justify the activities and the liabilities of the enterprises. Once a state or municipal-owned enterprise has been announced for privatization the law allowed the privatization to be executed in several ways:

1. Public offer
2. Public auction of company stocks
3. Publicly announced competition
4. *Negotiations with potential buyers*
5. Centralized public auction

According to this law, every investor (physical person or legal entity) that complies with a number of rules[16] (not insolvent, not under arrest and so on) is allowed to purchase state-owned firms, utilizing one of the procedures mentioned above. All previous governments have emphasized their openness to foreign capital. However, privatization transactions are often protracted, in part because the Privatization Agency often tries to secure a price, which the market will not bear. Furthermore, the frequent use of direct negotiations in the privatization process has fostered allegations of corruption and political influence in the sale of state enterprises. For more than ten years the Privatization Agency and all the government officials connected to privatization have been constantly criticized and alleged for corruption.

Corruption, as reported by all local and international reports and researches for Bulgaria is by far one of the biggest problems of the country and not only for foreign investors. Thus, any regulations, which can allow even for a small chance of corruption,

[16] The rules applied to bidders in the privatization process are discussed in details in Part V of this research

shall be abolished. The privatization alternative – direct negotiations with potential buyers is the absolute legally established pre-requisite for corruption – no public control, no need to announce all potential investors (buyers) and their problems. Only direct negotiations with whomever the Privatization Agency chooses. Thus, the generally low paid top employees of the Agency can negotiate with the potential buyer who is ready to "pay the commission" – i.e. pay the bribe - and sell him the company in question.

This issue has been widely discussed in public and in the media since there are evidences of but one ex-state owned enterprises being privatized by means of corruption. A number of cases with evidences have been submitted to the prosecution, a number of charges have been levied on the Privatization Agency. But all these measures cannot compensate the employees laid off by an investor, who had taken a company "under the table" not to develop it but to close it and sell the machinery and the equipment. These measures cannot make up for the corruption alleged investment climate of Bulgaria in the international circles. Regardless of the efforts of the current government and the overall public demand for transparency in all the privatization and investment deals there is still a lot to be done.

In conclusion the biggest problem of the old Privatization Act was:

**Problem: Direct negotiations with potential buyers in the privatization process allowed for extensive spread of corruption.**

In its efforts to improve the Bulgarian investment climate and to attract more FDI the National Assembly abolished the 1992 Privatization Act and enforced a new one –

Privatization and Post-privatization Control Act[17]. Art. 2 of the new Privatization Act reads like this: “The goal of this Act is to provide for transparent, fact and economically efficient privatization guaranteeing equality to all investors”. The law makes no difference between Bulgarian and foreign investors – they all have equal rights and obligation. Article 31 of the Act determines the privatization methods:

- Public Offer
- Public Auction
- Publicly announced competition
- Centralized Public Auction

Obviously, the new Act abolishes the direct negotiations which (at least legally) puts a stop to the opportunities for bribery in the privatization process. The National Assembly and all the officials who have worked on the new Privatization Act should be given credit for listening to the demands of the public and the foreign observers. Thus the solution to the old Act problem has been found in the brand New Privatization Act (2002).

**Solution: 2002 Privatization and Post-privatization Control Act does not allow direct negotiations with potential investors.**

All the privatization methods are public and the Privatization Agency is legally obliged to announce any future privatization deal in the State Gazette and in two central daily newspapers at least two months in advance. Thus the privatization process is given publicity and all potential investors would know in advance for a coming public offer or public auction.

[17] Referred to as the new Privatization Act

A novelty in the New Act is the creation of the Agency for Post-privatization Control. Just like the Privatization Agency the Agency for Post-privatization Control is a government body with the Council of Ministers and is financed by the state budget. The main purpose of the newly created Agency is to execute post-privatization control over the privatized companies which had more than 50 % government participation in the capital before the privatization. (Article 18 item 1 Privatization and Post-privatization control Act).In details the activities of the new Agency are summarized by its governing Act as follows:

“Art. 19 item (1) The Agency for Post-privatization Control executes post-privatization control over privatization contracts, signed by the authorized government bodies.

(2)When executing its functions under item 1 the Agency:

1. Executes all the necessary activities for filing claims and collecting penalties, determined by the contract in case of breach of privatization contract.
2. Controls payments under privatization contracts, allowing for long-term payment of the price
3. Requires information in case of signals for breach of privatization contracts.
4. Checks the fulfillment of the obligations, assigned by the privatization contracts in the privatized enterprises.
5. Gives consent and approval on behalf of the buyer if provided for in the privatization contract.”

All these functions and obligations of the newly created Agency for Post-privatization contract are in answer to the widely spread demand for strong post-privatization control and creating an effective mechanism for monitoring the fulfillment of the privatization contracts.

*…A joint venture (usually between a Bulgarian and foreign company, both of them recently established and notoriously unknown to the general public and to the business circles) buys under circumstances, far from fair trade practice a working ex state owned company. The company is slightly profitable (not in perfect condition) but is by no means bankrupt. The new owners manage their investment for a while, draw huge credits, guaranteed by the equipment and the machinery, then sell most of the equipment to unaware other investors, cut down the production or simply closes the company …and disappear.*

This was not uncommon scenario for the first years of the privatization process in Bulgaria. Companies, sold to fake investors were being closed down, which accumulated number of problems (among which unemployment was the biggest one). The lack of strict and effective mechanism for monitoring the privatized companies not only created a negative feeling against the privatization process in the society, but also put real strategic investors – such as Deutsche Telecom, Lukoil, Daewoo and others at a disadvantage. Playing by the rules, paying income taxes and VAT, caring for employees the investors, who had come to Bulgaria to really work there and develop something had to compete against those, who were avoiding any taxes, social security and thus managed to produce very cheaply and to sell what they can from the investments … and to declare bankruptcy … and disappear.

The establishment of the new Agency for Post-privatization Control, with detailed functions and purpose is a nice try to enforce mechanism for monitoring privatized companies. The Agency also sees for fulfillment of the obligations assigned by the privatization contracts. In this way, on the one side, the public is sure that the ex-state companies are not simply "given" to suspicious investors "under the table" and that investors are bound to their investment projects, and on the other side all the investors can rest assured that their competitors on the local market are at a similar position and every investor, violating his privatization contract shall be subject to administrative and legal procedures.

One might argue that such strict rules might limit the freedom and the business initiative of investors. Yet, if the new owners of a company follow their investment plans and fulfill their contracts there is nothing they can be afraid of or charged with – an agency official is likely to go and check a privatized company if there is a signal for wrong-doing, not just checking on a daily bases. The purpose of the Post-privatization Agency is to control the execution of the privatization obligations of investors, not to control their overall business activities.

Speaking of the fact, that the Agency for Post-privatization control initiates a check up having received a signal, the Act[18] has hardly any regulations, determining who, how and when can submit a signal for breach of privatization contract.

**Problem: Lack of a rule, defining the form, the subject and the time frame of the signals, eventually submit to the Post-Privatization Control Agency, alerting it for breach of privatization contract.**

[18] Privatization and Post-privatization Control Act

A vague rule, like article 19 (2) item 3 raises a number of questions. Can simply anyone pick up the receiver and tell to a Post-privatization agency official that company XYZ is violating its privatization contract's obligations and is the agency obliged to proceed with such a signal?

**Suggestion: Let the legislator determine and add to the current law who and how can submit a signal for breach of a privatization contract.**

Thus there will be effective post-privatization control, executed by the relevant Agency on behalf of the government. Yet, the investors won't be bothered with time and human-capital consuming inspections, initiated by fake signals (for example by fierce competitors, angry employees and so on).

Presuming that the signal, submitted to the agency is a real one, supported by evidence the agency, according to the current Act, can require information or go on an inspection. The Agency determines that the investor in question has really violated a term or two from his privatization contract. What next? The law gives no answer.

**Problem: The Agency for Post-privatization Control is not authorized to proceed with any actions against wrongful investors.**

**Suggestion: Authorize the Agency for Post-privatization control to charge an investor with a fee in minor cases and to summon the Privatization Agency[19] or the court in more serious breach-of contract cases.**

[19] Under the current Bulgarian legal system the Privatization Agency is authorized to summon the court and plead for termination of the privatization contract in serious cases of breach of contracts and damages.

In addition to the establishment of the above mentioned Agency, the New Act has another novelty – the Act assigns as an obligation to the Privatization Agency to supply any potential investor with an official statement about the legal status of the privatized (and upon request of investors any other, subject to investments) company. What happened before was, that after a successful purchase of ex-state or municipal enterprise the new owners not seldom found themselves "bombed" by a number of pending law suits they had been completely unaware of. At present, with the statement issued by the Privatization Agency, investors shall know well in advance about the oncoming legal "struggles". Because, not knowing the legal system and the language foreign investors are at a disadvantage, unaware how and when to check about pending law cases with the company they intend to invest in.

Having fully discussed the theoretical aspects of the New Act it is time to see its practical side. The truth is that both the Bulgarian officials and the foreign investors are still suspicious about the Act – it was only recently enforced and there are lots of ongoing debates for this Act. Only time and practice will show how good the New Privatization and Post-privatization Control Act is. The issues, discussed in this paper are part of the loopholes that remain to be filled-in or changed in order to produce a better Act, laying grounds for more and better FDI in Bulgaria.

Keeping in mind that most foreign investors are attracted to Bulgaria by its high-qualified, cheap labor force, they staff their companies or branches with mostly Bulgarian workers. Thus foreign investors have to comply with the Bulgarian Labor Law and labor issues prove to be of particular importance to them.

**D. Labor Issues**

Bulgaria's working-age population consists of around 4.8 million highly educated and skilled men. The literacy rate in Bulgaria is 93 percent. A high percentage of the work force has completed some form of secondary, technical or vocational education. Many Bulgarians have strong backgrounds in engineering, medicine, economics and the sciences. The aptitude of workers and the relative low cost of labor are considered incentives to foreign companies, especially to those that are labor intensive, to invest in Bulgaria**.** The country has long-term traditions in the IT education and highly qualified specialists in this field. (According to a recently published editorial in Business Week[20] – "Bulgaria and Romania are growing as IT workshops for German multinationals").

Under the 1993 Labor Code, relations between an employer and an employee are regulated by employment contracts. The code extends some benefits to workers such as maternity, post-natal child care or sick leave, and some investors complain that these are excessive benefits. Employers, in fact, are not burdened with additional payments out of their pocket (which is the case for sick leave in the US for example) because all the money for maternity, post natal child care or sick leaves comes from the social security fund. But, for instance, post-natal child care is a requirement dictating that employers not void a position for nearly two years, while the employee continues to receive payment from the social security fund. The old version of the Code determined 3 years paid leave and the change was made as an attempt to compromise between employers and the general public. The Code also addresses worker occupation safety and health issues, establishes a minimum wage (determined by the Council of Ministers) and prevents

[20] See Business Week – issue February 3rd, 2003 – "Is your job next?"

exploitation of workers, including child labor. The Code clearly defines employees' rights, strengthening management's hands in disciplining the workforce. Unresolved disputes between a worker and the management (employer) can be referred to courts, but resolutions are often subject to delays.

**Problem: Lengthy, protracted labor-related court procedures.**
**Suggestion: Expedite the so called labor law cases by imposing resolution deadlines on the courts.**

After all the labor suits are neither very difficult, nor very complicated (with few exceptions) and it is unfair to both sides – employee and employer (be it a Bulgarian entrepreneur or foreign investor) to delay resolutions and to engage them in costly, time consuming court procedures.
Parliament is currently considering draft amendments to the Labor Code, from which neither foreign companies nor Bulgarian companies having majority foreign control are exempt.

Most foreign investors find it difficult to grasp the Labor Code and it usually takes them some time to master it and operate under the Bulgarian labor law. The labor and the social security issues, which foreign investors face in Bulgaria, are addressed with more details and genuine examples in the case study part of this paper.

**e) Other issues –** the last, but not the least important foreign-investment related issue addressed in this research is Dispute settlement.

e.1) Bulgarian Court System

Bulgaria's constitution creates an independent judicial branch. The judicial system consists of three levels of courts.

On the first level, 124 regional courts exercise jurisdiction over administrative, civil and criminal cases. Cases are brought before one judge and two jurors. The 29 district courts are the next higher level, and have jurisdiction in civil cases where the claim exceeds 10 000 BG levs, in serious criminal cases[21] and in other cases as determined by a special law. The district courts are also vested with the authority of appellate review for regional court decisions. District courts are presided over by one judge in most cases, although three judges preside in some others defined by the amended Civil Procedure Code. There are five appellate courts (in major big cities) which review appeals of first instance decisions of the district courts. On the highest level are the Supreme Court of Cassation and the Supreme Administrative course. The former has jurisdiction over all civil and criminal cases and hears appeals on issues of law. The Supreme Administrative Court rules on the legality of acts by the Council of Ministers and the ministries. Decisions by the Supreme Court are final and binding.

The Constitution also establishes the Constitutional Court which stands apart from the Supreme Court. The Constitutional Court issues binding interpretations of the constitution; rules on challenged regarding the constitutionality of laws and acts; rules on international agreements prior to Parliamentary ratification; and reviews domestic laws to determine consistency with international legal norms. Any law or act found unconstitutional ceases to apply as of the date ruling comes into force.

e.2) Investment Disputes

[21] Determined by the Penalty Code

An example of an investment dispute is one recent case, involving a US investor. In this case a Bulgarian minority shareholder attempted to seize control of a privatized manufacturing company by replacing the board of directors at an illegally convened shareholders' meeting. The US Company, which with the support of other minority shareholders has the controlling interest in the firm, successfully overturned that decision in the Bulgarian Court system.

Given the frequent use of direct negotiations in the privatization process until recently, there have been numerous allegations of corruption and political influence in the sale of state-owned enterprises. However, relatively few unsuccessful bidders have pursued their complaints in domestic court or have sought international arbitration. In a minority of these cases, complaints have stopped the disputed sale. **Theoretically**, the law gives the right to every bidder in a privatization deal or public tender offer to appeal the decision of the authorized for the bid institutions**. In practice**, few investors have used this opportunity.

E.3. Execution of Judgments

To execute judgments, a final judgment must be obtained so that the court can order payment; make a judicial request to perform an act or abstain from acting; or order the surrender of possession of property/goods. To obtain payment, complicated foreclosure procedures must be initiated. The court of first instance must be petitioned for a writ of execution (based on the judgment). The issuance of a writ enables the seizure of assets. If the party is seeking a judicial request to act or abstain from acting, the final judgment must be brought before an executive judge. The executive judge is authorized to issue fines up to 400 levs. The judge possesses the authority to resort to the police in

instances such as the vacating of property and, possibly, for the surrendering of possessions.

Foreign judgments can be executed in Bulgaria. Execution depends on reciprocity as well on the basis of bilateral or multilateral agreements, as determined by an official list maintained by the Ministry of Justice. All foreign judgments are handled by the Sofia City Court, which must determine that the judgment does not violate public decrees, standards or moral before the foreign judgment can be executed.

In practice, execution of judgments is subject to delays, sometimes resulting from corruption and inefficiency in the judicial system – this is a problem discussed at lengths by judicial officials and government, but the problem remains open. The execution system exists, but it is a very long, tedious, protracted procedure to get a judgment executed**. Something must be done to expedite the execution** and guarantee everybody - foreign investors, Bulgarian businessmen and ordinary people that they will get, quickly and efficiently, what the court decision entitles them to get. This something **shall start with firm, legally binding terms and deadlines for the execution judges and their administration.** Only firm, firmly enforced deadlines can expedite and make more efficient the Bulgarian execution system.

## C. Conclusion

At the end of 1989 Bulgaria abolished its old communist regime and started the march towards a fully functioning market economy. Many, many mistakes were made in the transitional economy period. Bulgaria fell behind countries like the Czech Republic,

Slovenia, Hungary and even Poland – all these countries managed to restructure their economies quicker and more efficiently than Bulgaria. Part of their success was due to the fact that these countries attracted more foreign investments, which helped them out on the way to a new economy. In the last years Bulgaria is struggling to "catch up" and putting efforts on developing a better investment climate – both through legislation reforms and market conditions. The last two governments, in response to broad public demand abolished or changed not-working investment related laws, introduces rigid financial discipline, cut down inflation and to some extent did change Bulgaria's international image.

Yet, as this research shows, as far as the investment legislation is concerned, there are things to be done. All the problems analyzed and their possible solutions are summarized in Table 5.

**Table 5: Conclusion to part III.2.**

| Legal Issue | Problem | Idea | Benefits |
|---|---|---|---|
| **Capital market legal framework** | Regulation of T-bills with inferior to a Law rules, insufficient regulation of trade, issuance, and registry of T-bills | Improve regulation of T-bills' issuance, trade and registry. | More efficient system of T-bill issuance and trading, which eventually will lead to a more active capital market |

| | | | |
|---|---|---|---|
| | Capital gains repatriation | Introduce a legally-binding deadline for the decision of the authorities in charge of allowing the capital gains' repatriation. | Expedite the procedure for the repatriation of capital gains by |
| **Foreign Investments Act Issues** | Bureaucratic problems | Merge the Privatization Agency and the Agency for Foreign Investments | This merge will:<br>- decrease budget expenditures for maintaining the Agencies<br>- Allow for a more compact and efficient guidance of investors through possible both privatization and investment projects. |
| | Lack of clear criteria for defining priority investment projects | Define priority investment projects by clear criteria included in the Foreign Investments Act. | This will provide for less corruption and priority investment projects will enjoy benefits, guaranteed by law. |

| | | | |
|---|---|---|---|
| **Taxation issues** | No tax benefits for priority investment projects | Allow for postponed payment of corporate taxes for priority investment projects. | This will give some tax break to big investment projects, thus making Bulgaria more attractive for strategic investors. |
| | Tax collection problems | Improve tax collection by introducing higher penalty-rates and giving more rights to tax authorities | The improve tax collection will allow for reduced tax-rates in the long run, which will be beneficial for both local and foreign investors. |
| **Privatization Act issues** | Privatization and Post-privatization Agency rights – incomplete definition | Give more controlling rights to the Privatization and Post-privatization Agency | This will enable the agency not only to monitor privatized companies, but to take enforce fines and other penalties in cases of breach-of-contract |
| **Dispute settlement issues** | Long and protracted execution procedures | Define and enforce short-term, efficient rules binding for the execution authorities | Investors will be able to rely on quick and efficient execution procedures in cases of problems with debtors. |
| **Labor issues** | Protracted by courts labor law suits | Shorten the time frame of the labor law suits' court decisions. | Investors will be able to use resources to concentrate on business, not on law |

| | | | |
|---|---|---|---|
| | | | cases. |

Some of the problems identified – such as the inefficiency of the execution system – are obstacles not only for the foreign investors, but for the Bulgarian businessmen too. Others – such as the labor issues or priority investment projects determination are of exclusive interest to foreign investors. But, step by step, all these problems, and others which the author of this research might have missed, should be addressed by the legislators in order to improve Bulgaria's investment jurisdiction and eventually, attract more foreign investors.

Apart from the theoretical issues, elaborated on in the research, foreign investors coming to Bulgaria experience a number of pure practical problems – problems arising from the difficulties they have to grasp and understand the Bulgarian laws and work in compliance with them.

The case study that follows presents two cases, illustrating what (legal) problems foreign investors encounter in Bulgaria and how they manage with them.

## III.3. Case study

The two case studies, discussed herewith, present real, recent cases of foreign investors doing or trying to do business with Bulgaria[22].

[22] *I won't say the cases and the investors were picked up at random or for the only purpose to please the KDI School of Public Policy and Management thesis committee – the two cases reflect the authors' professional and personal experience in two very different situations – as an employee of a company, acquired by a Korean giant and as a legal advisor to another Korean giant, in its attempt to play on the Bulgarian market.*

**A. Case study I**

## Daewoo Corporation in Bulgaria

In June 1997 the cabinet approved "Daewoo Corporation" as the buyer of 70 % of the World Trade Center "Interpred"-Sofia. The Korean company had to pay 20 million U.S. dollars in cash within 30 days after signing the contract and to invest additional 5 million U.S. dollars within the next 5 years. The corporation was also obliged to keep the personnel during the first year after the ownership transfer. During the second and the third year the number of employees could be reduced by 20% annually.

In 1997 the World Trade Center “Interpred” – Sofia was by far the only business center in Bulgaria. With 2 10-storeys blocks it was a modern, fully functioning business center and the competition among the candidate-investors was fierce. Daewoo did not bid the highest price, but it offered the best investment plan, committing to invest 5 million dollars for renovation.

The acquisition of the WTC by Daewoo was one of the biggest privatization deals for 1997 in Bulgaria. At that time the Korean giant Daewoo pursued a policy of extensive international expansion. In Bulgaria Daewoo had already established a successful auto dealership network, which was one of the first Daewoo dealership networks in Central and Eastern Europe. So, as an investor Daewoo corporation was already a well-known name on the Bulgarian market. Soon after acquiring Interpred, Daewoo purchased hotel “Balkan-Sheraton” in another successful privatization bid.

Upon acquiring Interpred – WTC, Sofia, Daewoo was registered as the new, major shareholder in the JSC, owning 70 % of the company’s shares. The other owners

were the Bulgarian government, represented by the Ministry of Economy – owning 26 % of the company's shares and a small number of private shareholders.

Interpred was and remained profitable after its privatization. The new Korean owners followed strictly their investment plan, doing the necessary renovations and not trying to cut down on the USD 5 million projected investment regardless of the 96-97 Korean crisis. This, however, does not mean that managing Interpred went smoothly and easily for the new owners. On the contrary – the new management, trying to adapt to the Bulgarian conditions faced a number of problems – cultural differences, labor issues and social security issues.

**a) Cultural differences –** It's never easy for a company, which expands abroad to adapt quickly to the new culture of the host country. Even harder it is when going to a country with completely different culture from the investor's own country. A few employees, sent from their Far-East based company, to manage a new Eastern European acquisition face enormous cultural challenges. Suspicious employees and language barriers are only the top of the iceberg. An investor may buy a company and start running it, but changing the company's culture and traditions is neither an easy, nor a quick process. Both the new management of Interpred and Interpred's employees had a long way to go for adapting to each other. Used to long office hours, the Korean management demanded the same from the Bulgarian employees – it did not work, Bulgarians are going home at 5.30 PM and are not willing to stay in the office for the sake of being there. Bulgarian employees, on the other hand, had to get used to submitting detailed reports for the weekly activities to the new management. These are only few examples of the cultural differences that had to be overcome in a company

privatized by a foreign investor. Very closely related to the cultural differences were the labor issues which the new management bumped into. It is true the labor issues stemmed from not knowing the laws governing employee – employer relations, but the reason for the non-understanding of the laws was the enormous differences that lay between employers and employees under this particular scenario.

**b)Labor issues –** the privatization plan allowed the new management to cut down the working force with 20% annually, starting in June 1998.

What did the management do? On L-day (lay-off day) the executive director calls in the employees to-be-laid-off and hands each of them a letter saying something like "Thank you for your hard work and your contribution to the company. We are sorry to inform you that from today you are not WTC Sofia's employee."

What happens next? In a week or so all laid-off employees file a law suit for wrongful dismissal against "Interpred WTC Sofia" and in a month the company finds itself defendant in a dozen labor law suits.

At that time all Interpred employees, as required by law, work with permanent labor contracts. Bulgarian labor code which regulates the relationship employer-employee determines in the details the grounds on which a worker shall be discharged – for example "Lack of qualifications/education to perform his/her duties" or "Consistent bad performance, after minimum three disciplinary reports" or "Severe stagnation for the company, causing a minimum of 3 months unpaid-leave for the employees due to lack of work". Any worker's discharge on grounds different from those, specified in the Labor Code or on no grounds is considered wrongful and the worker can sue the wrong-doing company free of charge (no fees are to be paid by the worker to the Court). A wrongful

dismissal, identified as such by the court, binds the employer to restore the worker and to pay him/her compensation for the time of unemployment due to the wrongful dismissal (up to 6 months).

In mid 1998 Interpred had full-time legal staff – 2 in-house legal advisors and a part-time chief legal advisor who in a number of memos tried to explain to the new management the principles and the rules of the Bulgarian Labor Law. Yet, due to lack of experience under similar circumstances and total unawareness of the consequences the new management was unwilling to change their methods of cutting down the work force and to reason with the workers, persuading them to leave voluntarily. The new management could not realize "How come it you cannot just hand the "pink-slip" to an employee you don't need any more! How come it you cannot cut down the expenses of the company you just bought by getting rid of the unnecessary employees?" But the rules of the Bulgarian Labor Code determine how an employee working with a permanent labor contract shall be dismissed. These rules shall be followed by every employer – no matter whether a Bulgarian or a foreign national who operates a company in Bulgaria.

What was the problem that the new Korean management had to face and deal with - lack of understanding of the Bulgarian Labor Law? The answer is a resounding "Yes!". And the Daewoo case is just an example. Most foreign companies find it difficult to understand and comply with the Labor Code. My **suggestion** to the foreign investors operating a company in Bulgaria is:

Take some time to study the Labor Code or hire a legal specialist to explain to you the most important parts of the Labor Law – this will definitely prove cheaper and less time and efforts consuming than a couple of law suits.

**c) Social security issues**

Closely related with the labor issues that foreign employers face in Bulgaria are the Social Security issues. Under the Social Security Act all employees, employers and self-employed persons are mandatory contributing to the Social Security fund. There is no exception to this rule and everybody working in Bulgaria – regardless of nationality – is covered by and has to contribute to the Social Security fund. The contribution rate is 34.7%. The employer's contribution is 75% of the total contribution – that is 26.2 % of employee's gross monthly income, and the employee's contribution is 25 % or 8.5 % of the gross monthly income. (The self-employed and free-lance professionals pay the whole contribution by themselves).

While the Interpred WTC Sofia management strictly followed the procedures of the Social Security Law applicable to those employed by the WTC Sofia, the management was a bit confused as to their status within Bulgaria. In the one hand they were employed by the Korea-based Daewoo Corporation, but on the other hand they were head of and therefore employed by the Bulgaria-based and registered in Bulgaria "Interpred WTC". Thus, according to the Bulgarian Social Security regulations the management was also obliged to contribute to the Bulgarian Social Security Fund, since they were earning income in Bulgaria.(the source of their income was a Bulgaria-registered company).

*…When I started in Interpred WTC in 1999 my first task as a legal department specialist was to examine closely both the Bulgarian and the Korean Law and to find a loop that would allow the Korean management to avoid paying the social security contribution in Bulgaria. Regardless of my efforts it did not work – the Bulgarian legislator made it clear*

*that everybody working in Bulgaria, and receiving payment there for services rendered IN BULGARIA has to pay social security contribution.*

*It might seem unfair to the foreigners and to the investors hiring expatriate staff, who will work only a couple of years in Bulgaria and never will be eligible for Bulgarian pension, but the legal presumption is very simple – with the aging population in Bulgaria the Social Security Fund needs money. Everybody who does not pay, regardless of his nationality, violates the law.*

**Thus, foreigners working in Bulgaria or rendering services in Bulgaria as investors should be aware of the fact that their total Bulgarian income is levied with the Social Security contributions**.

The case study, discussed above implies that successful M&A investment is only the beginning of a long and not an easy path of operating a company (investment) in Bulgaria. In this process of operating a company in Bulgaria the understanding and the applying of the correspondent rules and regulations is of major importance – no matter whether the applicable law is a good or not that good one. Because neither local, nor foreign businessmen can change a law – they might like it or not like it, may even try to lobby for the change of a particular regulation. But while a certain rule is in force all the player on the Bulgarian market are required to comply with it – on their own merits or by searching legal help when necessary.

## B. Case study II

### Samsung's attempt for participation on the Bulgarian market

### a. Overview

While the first case is a clear and definite M&A investment, the case that follows is not a specific investment case. It can be best described as an attempt to work with and for a company, in order for a potential investor to get the feeling and the situation on a market he is interested in. The case is a very good example of what sort of problems a company, coming to Bulgaria for the first time, might bump into. The story goes like this…

### b. Interested parties:

1. **Bulgarian Telecommunication Company - BTC**
2. **Samsung Electronics Corporation – SEC**

**BULGARIAN TELECOMMUNICATIONS COMPANY (BTC) Plc** is a state-owned public limited liability company set on 1st of January 1993, with its rights and obligations defined by a Decree of the Council of Ministers and a License issued by the Committee of Posts and Telecommunications.

The managing body of **BTC Plc** is the Board of Directors.

The major policy and purchase decisions are made by the Board of Directors.

**BTC Plc** has exclusive rights for establishment, operation and maintenance of the National Public Telecommunications Networks on the territory of Republic of Bulgaria and provisioning of International and Domestic telecommunications services. In addition to having exclusive rights for the Public Telecommunications Network, BTC is a shareholder in a number of joint ventures and partnerships – such as Radio-telecommunication Company Ltd; Bulfon Co and others.

One of the few remaining monopolists on the Bulgarian market, BTC was put in the privatization program 4 years ago and the Privatization Agency was assigned the task to execute and complete the privatization deal for BTC – the Privatization agency being the government body responsible for the privatization. The BTC privatization process is still on-going and still one of the hottest topics for the Bulgarian mass-media and one of the biggest problems for the Bulgarian government. The privatization deal has been suspended a number of times and though at present a possible buyer has been chosen the privatization contract is not signed yet. The Bulgarian Privatization Agency recently announced that the sale of BTC is likely to be finalized this year.

Meanwhile, the telecommunication company continues to operate, to expand and as required by law to use procurement practices for its auctions.

That's where Samsung comes in.

*It's hardly necessary to elaborate on the subject about Samsung and its activities – this is a too well-known company in Korea.*

…The South European division of SEC[23], through its divisional manager Mr. Park, became aware of the ongoing public tenders in Bulgaria and submitted an offer to its headquarters for participation in the bid. The offer was accepted very positively by the people in charge and viewed as an opportunity not only to bid, but to test the Bulgarian market and the Bulgarian system for possible future expansion (at that time Samsung was in the process of building a brand-new production plan – Greenfield investment – in Hungary and the newly built plant promised to be a success). So, SEC decided to bid in the BTC auction and its South European Department started gathering the required

[23] Samsung Electronics Corporation

documentation. The papers necessary for participation in a Bulgarian public offer had to be issued according to the applicable Bulgarian law.

### c. Procurement practices and requirements in Bulgaria

The Bulgarian Law, which regulates the procedures for assigning public procurements (PAPP) and the requirements for candidates in PAPP, is the Law on Public Procurement[24]. Under this law any person (Bulgarian or foreign national) meeting the requirements announced for the specific public procurement is entitled to participate in the PAPP. The LLP contains an exhaustive list of "negative prerequisites" i.e. conditions, the presence of which disqualifies a person as a candidate in a PAPP. The presence of any of the following constitutes such a condition[25]:

1. pending insolvency procedure or an effective court decision announcing the candidate insolvent
2. a pending litigation procedure
3. a ban for exercising business activities by the candidate
4. outstanding obligations to social security funds
5. outstanding obligations to the state budget evidenced by an effective deed of the competent authorities
6. a criminal conviction for crimes against property and/or against economy, unless such convictions have been later cancelled.

The lack of the above circumstances is to be evidenced by certificates issued by the competent state authorities for items No. 1,2, 4 and 5 and with a declaration for items 3

[24] LLP
[25] Art. 24 of LLP

and 6. In case of a candidate, who is a legal person item the lack of the pre-requisites 3 and 6 shall be evidenced for the managers or for the Board of Directors.

All these certificates and the declarations are to be submitted with the tender offer, which shall include the offered price, the timeframe for the performance of the public procurement and other details.

*So, to make things clearer – all the above certificates and declarations are necessary for a candidate to be eligible to participate in a PAPP.*

The LLP also requires a number of other documents to be enclosed to the offer[26]:

a. certificate of the candidate's registration
b. documents evidencing that the candidate is a reputable business partner
c. a document for the deposited guarantee
d. a copy of the annual financial statement of the company and of the profit and loss report for the previous year (unless the company is a newly incorporated entity)

All this certificates, together with the certificates and the declarations evidencing the lack of the negative pre-conditions banning a person (legal or physical) to participate in public procurement procedure shall be submitted with the tender offer within the announced deadline.

Failure of the candidate to present any of the above documents constitutes legal ground for dismissing the candidate's offer before it has been considered on its merits.

The time constrain for submitting offers varies, but the legally defined term is at least forty days as of the date, on which the invitation to the candidates is published in the

[26] Art. 26 or LLP

State Gazette. Most companies stick to the 40-days term and very seldom the time frame for a tender will be 50 or 60 days.

The term for the tender in which Samsung Electronics Corporation tried to bid was 40 days.

However, Samsung made a decision to submit an offer for the BTC tender three weeks before the deadline. So, in three weeks time all the required certifications, declarations and the tender offer had to be ready, shipped to Bulgaria and submitted to the BTC.

*An impossible task! When I was contacted by Samsung via the Bulgarian Embassy in Seoul to help them with the public tender project there were 20 days left for submitting the offer. Giving my credit to the Samsung team for their efficient and expedite work, there were obstacles that were beyond our limits. In less than a week we had most of the documents such as:*

- *declaration for the lack of a ban for exercising business activities*
- *a declaration for the lack of criminal conviction for crimes against property and/or against the economy signed by Mr. Lee – Chairman and CEO*
- *letters of references from business partners, evidencing that the candidate – namely Samsung Electronics Corporation is a reputable business partner*
- *a certified copy of the annual financial statement of the company*

All the above mentioned documents were duly translated from Korean into English or issued directly in English. The real **problems** came with the requirements for presenting a **number of documents which are not compatible with the standard business**

**practice** in Korea and with the **procedural requirements** for the issuance and the certification of such documents.

**d) Problems**

Before discussing the problems, which Samsung faced under the Bulgarian procurement practices let me explain how these problems and the whole case are relevant to the investment practices in Bulgaria. Simply, when announcing the opening of a procedure for privatization of a state or municipally owned enterprise (or part of an enterprise) under any of the methods allowed by law (see page 34) the Privatization Agency refers the potential investors to Article 24 and Article 26 of LLP. The two articles determine the eligibility criteria for the potential investors – that is – a potential buyer in a privatization deal and a candidate for PAPP shall meet identical criteria and present all the documents, determined by LLP, in order to be eligible to participate in the privatization procedure or in the procurement procedure. As the criteria of eligibility for candidates in public procurements, included in the LPP are the only one available and legally defined, these criteria are widely used not only by government bodies and state-owned companies, but also by private companies in their procurement practices.
Thus, the difficulties that Samsung faced in its attempt to participate in the BTC tender could be an example of all the problems that potential investors face in Bulgaria.

To start with, an official certificate for the initial registration of Samsung was nowhere to be found – Samsung Electronics Corporation is registered on KOSDAQ and Nikkei, but an initial company registry was not found.
Furthermore all the documents that shall evidence lack of pending insolvency, lack of bankruptcy sentence (for each of the company's managers) are to be issued by the

correspondent court authorities. While in Bulgaria every person – physical or legal entity can go to court and submit a request for the issuance of such certificates, the procedure in Korea[27] proved to be completely different. In Korea all documents issued by the courts or police authorities (such as police clearance; non-bankruptcy or non-litigation-pending certificates) shall be claimed not by the subject of the documents, but by the organization, institution or legal entity, which require such a document. In the case of a Korean company, participating in a Bulgarian PAPP, the certificates shall be claimed from the Korean court directly by the Bulgarian public procurement assignor. However, the Bulgarian assignor (BTC in our case) is neither obliged by law to claim such documents, nor aware of the different countries' procedures – the assignor is a Bulgarian legal entity sticking to the Bulgarian law. Although the Bulgarian law, rules that certificates under Articles 24 and 26 of LPP shall be issued by the competent state authorities of the country in which the candidate is registered, a Bulgarian PAPP assignor is highly unlikely to claim any documents in accordance with any other country's regulations. Thus, the requirement of LPP, though involuntary, puts foreign entities - new to the Bulgarian market and willing to participate directly in bidding for privatization or procurement procedure – at a disadvantage to the Bulgarian-registered legal entities. This is a typical problem not only for Bulgaria but for a great deal of other EU and Eastern European countries – not theoretical, but almost practical impossibility to participate in and win a tender without a local subsidiary. In Germany and France, for example, procurement practices and regulations are "cut" to fit German and French companies correspondently and Bulgaria is not far behind.

[27] The term "Korea" used in this paper refers to Republic of Korea or South Korea

In the case of Samsung's attempt to participate in the BTC tender, the Korean corporation not only had to issue quite a number of documents from different authorities – hardly known in the Korean business circles documents – but also had to issue the documents very quickly. According to the Bulgarian LLP in the event of a foreign entity and/or a manager, who is a national/resident of foreign country, the certificates shall be foreign public documents, and in order to be recognized and used in the Republic of Bulgaria they would need to undergo certain translation, certification and legalization procedures. Such procedures involve certifications both in the country where the documents were issued and in the Republic of Bulgaria. The time usually necessary for accomplishing these steps vary between two weeks to two months. In the case of a Korean company engaged, the process of issuance, certification and legalization of documents to be valid in Bulgaria takes approximately 2 months:

1. One month for legalization with the Korean Foreign Ministry
2. 1-3 days certification with the Bulgarian Embassy in Korea + shipping
3. Two weeks legalization with the Bulgarian Foreign Ministry

And neither the Korean nor the Bulgarian Foreign Ministry really cares that a company has a deadline to meet or a term expires – there are too many deadlines and too many companies out there to care for a single company.

Thus the 40-day advance announcement of a PAPP in the State Gazette is hardly sufficient for foreign entities willing to participate in procurement or privatization procedure (unless they are not new players on the Bulgarian market and keep the necessary documents handy for participation in different procedures). And having available all the necessary documents , which, as specified by law, are standard for all the

privatization and procurement auctions, is a standard practice for the Bulgarian companies and for the foreign companies, with steady positions on the Bulgarian market – companies that know the rules and play well by them.

Most foreign entities, however, establish a subsidiary in Bulgaria (with a Bulgarian-national manager) and bid on the Bulgarian procurement and privatization auctions via the subsidiary. This improves significantly the time and the cost-effectiveness of the application procedures – documents are issued by Bulgarian authorities in Bulgarian, there is no need for lengthy certifications and legalizations.

Establishing a subsidiary in Bulgaria is exactly what Samsung did, after all.

*But let's see how the whole story went…*

*Despite all the bureaucratic difficulties Samsung did not give up and submitted a direct tender offer for the Bulgarian Telecommunication Company Procurement. However (not unexpectedly) the offer was dismissed without being considered on its own merits on the grounds of lacking essential documents. Luckily, this BTC procurement bidding was later cancelled on the grounds of procedural mistakes and a new PAPP was to be announced. Meanwhile, the South European department of Samsung contacted a Bulgarian law firm – the law office of Djingov, Godjinski, Kyutchukov and Velichkov with the request for a legal advice on the subject matter.*

*After careful reviewing of the Bulgarian laws and practices the law firm advised Samsung what seemed most reasonable and practical – to establish a subsidiary in Bulgaria.*

With its Bulgarian subsidiary, Samsung had no problems preparing and submitting the necessary documents (now for a Bulgaria-registered company) for the second BTC public

tender. The subsidiary bid successfully and Samsung's offer was closely beaten by a Turkish company.

Samsung's subsidiary is still functioning in Bulgaria – keeping handy all the necessary certificates for a bidding procedure – procurement or privatization in which Samsung might be interested.

Convenient it might be to operate in Bulgaria through a subsidiary it does not mean that Bulgarian law cannot be changed to save time and efforts and to allow for easier direct participation of foreign entities in privatization and procurement procedures.

In that aspect, the table below (based on Case study 2) summarizes this research analysis and suggestions.

**Table 6 – Problems and ideas regarding Bulgarian procurement/privatization practices**

| **Problem** | **Idea** | **Benefits** |
|---|---|---|
| Certificates issued for a foreign entity or manager shall be foreign public documents, certified and legalized appropriately. | Foreign entities to be allowed to participate with only official translations of their certificates and documents. Foreign entities shall be required to present certified and legalized certificates if winning the bid. Failure of presenting the original legalized documents upon winning the bid might constitute a ground for the candidate's dismissal. | This will safe both time and efforts of foreign entities and they will be able to meet the officially announced deadlines. Thus, time consuming and cost involving legalization procedures will be undergone only in case the candidate is a winner. |

| | | |
|---|---|---|
| All documents and certificates submitted with a tender/privatization offer shall be in original accompanied by an official, legalized translation. | Allow both foreign entities and Bulgarian companies (for reference letters for example) to participate in the procurement/privatization bidding with documents issued originally in English[28] and claim the legalized translations upon winning the bid - this is a standard practice in a number of European countries. | Bulgarian Privatization Agency and other entities have enough English speaking personnel who can verify the contents of a document. With initially presenting documents issued in English foreign entities can avoid costly and lengthy translation processes and execute them later if necessary – upon assigning the public procurement or signing privatization contract. |
| Short-term public notice for oncoming privatization and tender auctions. | Oblige the Privatization Agency and the Bulgarian companies using procurement practice to announce the oncoming auctions at least 60 days in advance in the State Gazette. | The suggested term gives more time to foreign entities (and to Bulgarian companies also) to prepare a tender offer and issue the accompanying documents. |

A lot of time and costly procedures for different companies can be avoided if they are allowed to participate in auctions with official, but not legalized documents. Originals – certified and legalized can be easily claimed in a later period only from the auction/bid winners and disqualify those who fail to present them. Yet, the other companies – the non-winners are spared from the certification/legalization process.

[28] Most foreign companies can issue a document directly in English

If nothing else, there is one thing that can be acquired by implementing these proposals – less unnecessary bureaucracy. And bureaucracy is the problem most often cited by foreign companies and experts as one of the biggest impediments to doing business in Bulgaria.

In addition to the bureaucratic, capital market and labor problems, to the taxation and practical issues discussed above, there is a legal problem, closely related to foreign investments, which was only mentioned in this research – land ownership. Foreign individuals cannot own land – this is a constitutional prohibition. This constitutional prohibition, however, must eventually be changed in compliance with the EU legal requirements. As a European Union candidate country and as a member country of the WTO Bulgaria has obligations it has to fulfill and, if necessary, to adjust its current laws to the requirements of the WTO and the EU.

## III.4. Bulgarian foreign investments legislation through the prism of Bulgaria's WTO and EU obligations

### A. Bulgaria and WTO

Bulgaria joined the WTO in December 1996, being in the second group of Eastern and Central European countries to join the Organization. In accordance with its WTO obligations Bulgaria adopted a policy for reduction and elimination of trade barriers. The Bulgarian economy is strongly dependent on foreign trade, which accounts for a high relative share of its GDP.

As to date, Bulgaria has successfully complied with all its WTO obligations – it has reduced it tariffs in accordance with its WTO accession program and continues to do so with annual tariff adjustments.

For the period 1996-2003 Bulgaria has not been involved in GATT or GATS disputes, which once again prove Bulgaria's compliance with its WTO obligations. Foreign investors in Bulgaria, especially those involved in industry are benefited by Bulgaria's WTO membership since they can export Bulgaria-made products to foreign member countries under the Organization determined tariffs.

Yet, as a country with a transitional economy Bulgaria experiences a lot of difficulties resulting from imports of subsidized products from more developed countries, or form its inability to sell its products due to effective antidumping or sanitary and phytosanitary measures imposed by other countries. In its support for a new WTO round, Bulgaria expresses its concern that within the WTO a number of countries use rights and privileges as "developing countries", although they often have much better economic indicators than Bulgaria. There is no officially adopted definition of "a developing country" in the WTO and some member countries are of the opinion that belonging to that category is a matter of self-defining. Any further division of the WTO members into unclearly or subjectively defined categories would undermine the nature of the WTO as a rule-based organization. For this reason Bulgaria defends the position, which was reiterated many times within the WTO, namely that specific norms for separate categories of countries should be established and new special rights and privileges should be provided on the basis of objective criteria and economic indicators. Such an indicator is the GDP per capita, for example, and the categorization of the World Bank could be

applied (whereby the countries are classified as "low", "lower middle", "upper middle" and "high" income countries). Bulgaria's view is that all WTO members fulfilling the objective criteria of categorization should be able to apply the existing rights and privileges granted to the separate categories of countries.

Establishing of objective-based criteria for country's economic situation and their correspondent treatment within the WTO will be beneficial for both Bulgarian and foreign companies operating on the Bulgarian market. A new criterion for countries' categorization and correspondingly adjust trade tariffs could help increase the export of Bulgarian made products, preventing the Bulgarian market and its companies (no matter with local or foreign control) from the strong competition of more-developed countries.

### B. Bulgaria and the EU

Unlike its non-problematic and effective WTO membership, the EU accession of Bulgaria seems far from non-problematic. And problem number one is – economy. Bulgaria still has very low economical results, falling far behind the EU standards. Attracting more FDI and making its stagnated economy into a working one is a priority Bulgaria has to work on in order to be accepted in the EU.

In July 1993 Bulgaria signed on to the European Free Trade Agreement (EFTA). The provisions of the EFTA Agreement mirror those of Bulgaria's Europe Agreement. The Europe Agreement is now the legal basis for relations between Bulgaria and the European Union. Its aim is to provide a legal framework for political dialogue, promote the expansion of trade and economic relations between the parties, provide a basis for EU

technical and financial assistance, and an appropriate framework to support Bulgaria's gradual integration into the Union.

In December 1995 Bulgaria presented its application for membership of the EU and the Commission submitted a positive Opinion on Bulgaria's application on 15 July 1997. Accession talks between Bulgaria and the EU commenced in March 2000.

According to the last report of the European Commission Bulgaria has closed a total of twenty two of the thirty one chapters that make up the acquis communautaire, the EU's body of laws. (By way of comparison, Malta and the Czech Republic, which tail the ten expected entrants in 2004, have closed 25 each).The nine remaining subjects that need to be tackled are: competition and state aid, transport, energy, regional policy, the environment, justice and home affairs and financial and budgetary provisions. The agricultural chapter also remains open, as it does for all other candidates, even those that are expected to join in 2004. While there is going to have a lot of work to be done to close these chapters, with five years in which to meet the goals, they should pose few major problems. A key point here, closely related to the foreign investment activities in the country, is the energy subject of Bulgarian EU accession.

Until last year the Bulgarian National Electrical Company (NEC) was a monopolistic, state-owned enterprise. Now the government is in the process of privatizing NEC and bringing the country's electricity market inline with EU directives. The current situation is that generation and distribution activities have been separated from NEC and are now run by separate state owned entities. The 2002 program for privatization of state-owned enterprises, adopted by the Parliament on 14 December 2001 included a total of 6

power plants[29] and 7 electric power distribution companies[30], announced for privatization, following approval by the Council of Ministers.

One of the NEC sub-companies (separately state-owned companies) included in the 2002 privatization program – Maritsa East represents the biggest foreign investment in the country to date and all Eastern Europe. The deal between NEC and the US Entergy, which together acquired Maritsa East Power Plant, includes a $ 470 million investment in a joint venture to upgrade and operate an 840-megawatt coal-fired plant at Maritsa East- Another project between NEC and the US AES Corp. involves a 900 million USD investment to build a new, 670-megawatt coal-fired plant at Maritsa East 1 that will replace an old output.

A major electricity exporter to Turkey, Greece, Serbia, Macedonia and Kosovo, Bulgaria views its energy sector as a priority and realizes that without foreign investments and partnership with foreign companies it cannot update and modernize the sector.

The regulatory framework of the energy sector consists of the Law on Energetic. A recent change in the law, aiming to improve Bulgarian legal system in accordance with the EU

[29] The six power plants included in the 2002 privatization program are:

1. Maritsa East - 3 Power Plant, a self-standing unit of Natsionalna Elektricheska Kompania EAD - Sofia
2. Varna Power Plant EAD - Varna
3. Maritsa East 2 Power Plant EAD
4. Bobov Dol Power Plant EAD - Bobov Dol
5. Maritsa East 3 Power Plant EAD - Dimitrovgrad

[30] Electric power distribution companies included in 2002 privatization program:

1. Sofia City Electric Power Distribution Company
2. Sofia District Electric Power Distribution Company
3. Pleven Electric Power Distribution Company
4. Stara Zagora Electric Power Distribution Company
5. Gorna Orjahovitza Electric Power Distribution Company
6. Varna Electric Power Distribution Company
7. Plovdiv Electric Power Distribution Company

requirements, allows for the building of new electrical power plants by local and foreign persons, after getting a license from the Ministry of Energetic. Thus, the law lays the foundations for not only M&A investments in the energy sector, but also for Greenfield investments. Bulgaria has no choice but to adjust its energy sector regulations to the EU requirements, and one of the requirements is de-monopolization of the sector. The energy sector regulations, together with the liberalization of land-ownership are part of the legal issues Bulgaria faces before joining the EU and as pre-requisites for its successful EU accession. In addition to all the issues, analyzed in this research, energy sector issues and land ownership are also important for Bulgaria's investment climate and overall FDI attractiveness.

Economy, for certain is the biggest obstacle which Bulgaria faces on its way to EU. There is, however, no successful economy without a good legal system, good laws, which guarantee economic activities, private property, taxes and investments.

Because Law matters…

# III. Conclusion

As stated at the beginning, the purpose of this research was to examine and analyze the FDI relevant legislation and basing on this analysis to make suggestions for necessary law-corrections.

As expected this research found out a number of FDI related laws that need to be changed in order to improve the Bulgarian investment climate and attract more foreign investments, to which stability and predictability to be guaranteed. All the suggestions, in details, can be found in Tables 5 and 6. Without repeating them and summarizing the

issues, examined in the research, it is clear that 5 Acts need to be changed, i.e. 5 major Act shall implement the suggestions made above in order to improve Bulgarian FDI legislation. These Acts are:

1. Foreign Investments Act
2. Corporate Income Taxation Act
3. Privatization and Post-privatization Control Act
4. Law on Public Procurements
5. Securities, Stock Exchange and Investments Act

Contrary to the initial expected results, which predicted that 2 Acts need some corrections, the number of Acts "to-be-made-better" proved to be bigger. Yet, all the suggestions aim at solving problems most of which are known to the Bulgarians and to the foreign investors in Bulgaria:

1. Limiting bureaucracy
2. Providing more flexible system for foreign entities participation on the Bulgarian market (in privatization process, in public procurements or on the stock market)
3. Long-term tax cut
4. Efficient institutions (government agencies and courts)
5. Transparency in business activities

In a recent address to the National Assembly the latest Bulgarian Prime Minister stressed on the key transition challenges and Government priorities for Bulgaria. Number one among them was (and still is):

- "Improve the country's investment climate and tackle corruption by providing a transparent and predictable operational environment for private business in order to attract further Foreign Direct Investment (FDI)."

This quotation comes to show that the Bulgarian government fully realizes the importance of foreign investments for Bulgaria - Bulgaria has no way to continue to grow by 5 percent a year if investment rate does not. The investment rate needs to increase by about 20 %[31] and this is the only way to achieve economic growth and drop in the unemployment rate.

The government and the National Assembly still have a lot work to do to achieve this goal, by improving both legislation and economy.

This research is an attempt to point out some problems ant to suggest solutions - according to international observers and investment consultants[32] what Bulgaria needs most for attracting more FDI is to complete its structural reform – de-monopolize the last remaining monopolists (energy sector); to limit bureaucracy and to wipe out corruption. And all these starts with the relevant legislation reforms and changes – and that's what this research is about.

[31] Source: National Statistics Institute
[32] Source: "Directional economics 2002" – Sam Vaknin

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