

## SECURITIES & BANKS

### XV.

#### XV.1.

##### XV.1.1. Overview

After the discontinuity of the public trade in securities in Bulgaria after World War II, the First Bulgarian Stock Exchange started functioning in 1991. The first law regulating the trade in securities – the Law on Securities and Stock Exchanges – was adopted by the Bulgarian Parliament in 1995. This law provided for the creation of the State Securities Commission (SSEC) – the State regulator of the stock market. At the same time most stock exchanges merged to the Bulgarian Stock Exchange. In 1997 the SSEC officially licensed the Bulgarian Stock Exchange to organize a regulated market, and in 2001 – to organize an unofficial market.

In the end of 1999 the Bulgarian Parliament adopted the Public Offering of Securities Act, which is currently in force. This law set the grounds for the development of a market working under criteria and conditions similar to those in the European Union. Further positive development was seen in 2000 with the launch of a modern trading system and of an official index – SOFIX. The latest trends in the securities market development were marked by the replacement of the SSEC with a new state regulator – the Financial Security Commission. An additional step for bringing Bulgarian securities market closer to local and international investors is the launch of the Client Order-Book Online System, a.k.a. COBOS. COBOS allows clients or stock exchange members to place real-time orders over the Internet. Now orders can be placed not just from the whole country, they can be placed from all over the world.

##### XV.1.2. Legal Framework

The most important legal rules related to securities and to their trade in Bulgaria are contained in the Public Offering of Securities Act. The law governs all material aspects related to the trade in securities, securities markets and the State control over them. The law is aimed at the investor's protection; the creation of a fair, transparent and efficient securities market and the establishment of a strong public confidence in the securities market overall. The other important laws in that area include the Commerce Act, the Privatization Funds Act, the Encouragement of the Investments Act, the Privatization and Post-Privatization Control Act, the Financial Supervision Commission Act.

The Financial Supervision Commission ("FSC") has the power to adopt ordinances related to the public trade of securities. Such ordinances are the ordinance on the licenses for the performance of activities of a stock exchange, unofficial market, investment intermediary, investment company, management company; the ordinance on the requirements for the

activities of the investment intermediaries; the ordinance on the capital adequacy and liquidity of the investment intermediaries; the ordinance on the requirements for the natural persons who directly perform the trade in securities or investment consultations and the procedure to obtain the right to perform such activity etc.

The Bulgarian Stock Exchange adopted its rules and regulations, which provide the principles governing the overall operations on the Bulgarian Stock Exchange - Sofia. It determines the listing requirements, the trading components and all related and pursuant proceedings, membership provisions, disclosure, surveillance as well as procedures pertaining to disputes and discipline subjects.

The Bulgarian National Bank is vested with the powers to adopt regulations, some of which affect the trade in securities as well. Such regulations of the Central Bank govern the Control over Transactions in Book-entry Government Securities, the Central Depository of Securities and the Government Securities Settlement.

##### XV.1.3. Legal Definitions (The Market Players)

The Stock Exchange is a joint stock company with a special status. The main business activity of a stock exchange is to organize an official securities market. The stock exchange can also organize an unofficial market. The stock exchange cannot give loans, pledge obligations of third parties, or issue bonds. Its minimum registered capital should be equal or exceed BGN 100,000. At the time of receipt of the license to organize an official securities market, the entire capital should be paid-in. At least 2/3 of the capital should be owned by investment intermediaries or institutional investors. No shareholder can own more than 5 % of the stock exchange's capital. The stock exchange can establish or join already established system for clearing, settlement and guaranty of the transactions taking place on its market.

The FSC is responsible for the issuance of stock exchange licenses. The applicant for such a license should present together with its application the Articles of Association adopted by the founders; particulars about the capital paid in and its structure; particulars about the persons involved in the management of the applicant, and information about their professional qualification and experience; the stock exchange rules and the rules of the arbitration panel; data about the premises and the technical equipment of the stock exchange; other documents. The FSC shall pronounce on the application within three months as from its receipt, and where additional information and documents have been requested – as from their receipt. Without the license, Bulgarian courts will refuse the company's incorporation. If the FSC refuses a license, the applicant can apply again after at least 6 months.

Investment Intermediaries are the only companies who may carry out by way of occupation transactions in securities for their own account or for the account of a third party and intermediation for entering into such

transactions; underwriting issues of securities; management of individual portfolios of securities and/or money (with the exception of portfolios of investment funds and pension funds); holding of securities and money of clients at a depository institution (custodian activity). Banks can also be licensed to carry out investment intermediaries' activities. Investment intermediaries can also trade foreign currencies, if they obtain the necessary license. The investment intermediary registered capital should be equal to or exceed BGN 250,000. A special ordinance regulates the requirements for the structure of the capital, for the company's liquidity and capital adequacy.

In order to carry out investment intermediary's activities the applicants, except banks, need a license issued by the FSC. Together with the application to issue a license the applicant should present the Articles or the Memorandum of Association; particulars for the capital; particulars for the management and the persons carrying out transactions, and about their professional qualification and experience; the general conditions applicable to contracts with clients; names or business names and particulars for the persons who hold, directly or through related persons, more than 10 per cent of the votes in the general meeting of the applicant company, or may otherwise control it; etc.

The FSC shall decide on the application within three months as from its receipt, and where additional information and documents have been requested – within one month as from their receipt.

Public Companies are those companies traded on the stock exchange. Many companies listed on the exchange are former state companies. They were listed on the exchange before or during their privatization. Therefore, many companies went public after being privatized.

To go public, a Bulgarian company should generally publish a prospectus and make an IPO. The Public Offering of Securities Act contains special requirements towards the content of a prospectus and the other requirements to be met in order the company to go public.

The Bulgarian legislation provides for a series of special rules which grant the shareholders' rights and protect their interests. For example, unlike general rules provide, whenever a public company wants to increase its capital, it has to grant the right of the minority shareholders to participate proportionately in the capital increase, thus effectively protecting the minority shareholders against dilution of their participation. The legislation also provides some rules to secure the principle of equal access to information, such as the rules on information disclosure or the insider information.

Investment Companies are joint stock companies with a capital of no less than BGN 500,000.

Investment companies carry out the activity of investing cash into publicly traded securities.

Investment companies can either be open-end or closed-end.

An open-end investment company must permanently offer its shares to the investors at their issue price based on the net asset value and, upon request of its shareholders, to redeem those shares at the price based on the net asset value. The issue price and the redemption price shall be calculated at least twice a week. A closed-end investment company redeems its shares under the general legislation. Open-end investment companies can only be managed by management companies, while closed-end investment companies can be managed by either a management company or the company's own managing bodies. Bulgarian legislation requires a license for carrying out investment company's activities. This license is granted by the FSC within 3 months of application. The application form is filed together with the Articles of Association; particulars about the capital subscribed and paid-in; information about the members of the management and supervisory bodies or about the natural persons representing legal entities authorized to manage and represent the investment company, and information about their professional qualification and experience; the contract with the management company, in accordance with Art. 168, and the contract for depository services; the names or business names of and particulars about the persons who hold, directly or through related parties, more than 10 per cent of the voting shares of the applicant or may control it otherwise; etc.

Management Companies, the companies that manage investment companies, should have no less than BGN 100,000 registered capital and should also be licensed by the FSC. The commission will issue the license within 3 months of submission of the application form, together with the documents required by law.

#### **XV.1.4. Conclusion**

Bulgaria keeps on attracting ever growing interest with its investment opportunities. Foreign investors are interested to invest in Bulgarian securities market in many forms. They can just invest in listed securities or create an investment company or investment intermediary. Foreign investors should always keep in mind that they are treated equally with local investors, thus enjoying the special investors' protection provided by the local legislation.

#### **XV.2. The Banks**

The banking sector is crucial for the proper functioning of country's economy. For many years now Bulgaria has been publishing data on its macroeconomic stability. These data, in combination with the fiscal discipline of Bulgarian governments enhance the confidence to Bulgarian economy and contribute to the high rate of economic growth over the recent years. All this was only possible after a series of measures that Bulgaria had to undertake following a wave of banks bankruptcies about a decade ago. These measures cover both the introduction of currency board arrangements and

pegging of the BGN exchange rate to EUR, and the robust regulatory framework of the banking sector. The major pillars of this framework are the Bulgarian National Bank Act and the Banks Act adopted in 1997. It also includes the Special Pledges Act (1996), the Information about Non-performing Loans Act (1997), the Bank Deposits Guaranty Act (1998), the Measures against Money Laundering Act (1998), the Foreign Exchange Act (1999), the Mortgage Bonds Act (2000), The State Debt Act (2002) and the Bank Insolvency Act (2002). Rules related to banking are also adopted by the Council of Ministers and by the Central Bank.

#### **XV.2.1. The Central Bank**

The Bulgarian National Bank (BNB) is the Central Bank of the Republic of Bulgaria. Its major tasks are – through the mechanisms of monetary and credit policies – to maintain the national currency stability, to secure the functioning of effective payment mechanisms, and to regulate and supervise the activity of banks in the country. The BNB is responsible for the stability of the banking system and the protection of depositors' interests.

The Central Bank is the only institution in the country authorized to issue banknotes and coins. It is also obliged upon request to exchange without limitation Euro for Bulgarian levs at a fixed rate. Thus the Bulgarian Lev is “pegged” to the Euro.

The BNB has the power to adopt regulations on conducting banking business in the country to the extent provided by the law.

The BNB is managed by a Governor and three Deputy Governors. The Board of the BNB comprises of the Governor, the Deputy Governors and three other members. BNB' s activities are organized in three departments, each reporting to one of the three Deputy Governors.

The Issue Department maintains full coverage of the total amount of monetary obligations of BNB and manages the international currency assets of the bank. In case of occurrence of a system risk for the banking system stability, the Banking Department performs the function of a creditor of last resort. Supervision over the banking system is exercised by the Deputy Governor in charge of Banking Supervision Department.

#### **XV.2.2. Banks and Their Scope of Business**

The law defines the bank as a joint-stock company that attracts deposits and utilizes borrowed funds to extend loans and to make investments on its own behalf and for its own account and at its own risk. The bank is entitled to conduct only the business transactions comprehensively listed in the law. In addition to the transactions in the definition above, banks can accept valuables at a safe deposit; perform transactions of non-cash payments and clearing of checking accounts of other persons; issue and manage bank cards; provide bank safe deposit boxes. The above transactions can be carried out only

a) by entities which have been granted a banking permit (license); or

b) by licensed by BNB branches of foreign banks. Banks can also perform some additional transactions indicated in the law. But banks are limited to only perform those business transactions listed in the law. They are forbidden to perform any other business activity except when required in relation to the performance of banking operations.

##### **a) Establishment and Management**

According to the Banks Act banks can only be incorporated in the form of joint-stock companies. At the time of their establishment, the paid-in capital should be equal to or exceed BGN 10,000,000. Contributions can only be made in cash.

Banks shall be managed and represented by at least two individuals jointly. The members of the Managing Board or of the Board of Directors can only be individuals with university education, master's degree or higher, in addition to many other requirements they have to meet.

##### **b) Licensing Procedures**

The BNB issues the banking permits (licenses) to the banks. Conducting banking operations without such a license is illegal.

The procedures for issuance and revocation of banking licenses are defined in Chapter III of the Banks Act and Ordinance No. 2 on Licenses and Permits Issued by BNB.

A license for banking operations in the country can only be issued by BNB to (i) a joint-stock company based in Bulgaria, or (ii) a local branch of a foreign bank. The application of a local company should be accompanied by the founding documents, the names of the members of the boards, documents providing evidence for the subscribed capital and the paid-in contributions, a business plan, certificates of the qualification and experience of the members of the Managing Board or the Board of Directors, respectively, together with information on the shareholders and the origin of capital, etc.

The application for a license for banking operations in Bulgaria through a branch of a foreign bank should be submitted together with documents for the registration of the bank in its homeland, the banking license issued by the competent local authority to the applicant bank, a business plan, annual financial statements for the last three years, a written consent of the banking supervision authority for opening of a branch, etc. In case the applicant is not by itself a firstclass bank on the world financial market, it should submit guarantees from such a bank.

BNB shall conduct all necessary investigations within 6-month period as of application filing. Having been assured in the validity of submitted documents and the financial viability of the applicant, it shall issue the banking license.

#### **XV.2.3. Banking Sector Stability**

The legal framework of the banking sector is meant to provide a high level of stability. This is an important prerequisite for the development of the economy overall. Therefore, the Banks Act, together with the BNB regulations and the Bank Deposits Guaranty Act

form a modern framework providing for the necessary strict requirements for banking in Bulgaria.

Banks have to maintain liquidity, i.e. to always be prepared to perform without any delay their daily obligations both in a normal banking environment and in a crisis situation. Banks also have to maintain obligatory minimum reserves in their current accounts in local and foreign currency with BNB against their borrowed funds in BGN and foreign currency, respectively. Capital adequacy of banks is guaranteed through requirements to the minimum amount and structure of banks' equity.

Security of cash deposited in banks is also guaranteed by the statutory requirements to the admissible risk concentration as a total for the bank or the banking group to each individual customer or related parties. Banks and banking groups should not exceed the ratios of great exposures to equity, as provided in the regulations. In the meaning of the law, an exposure to an individual customer or to related parties is considered to be great when equal or exceeding 10 per cent of the equity of the bank or banking group.

The Bank Deposits Guaranty Act provides for the creation of a Fund, insuring the bank deposits with local banks and with branches of foreign banks, licensed to operate in the country, provided the home country of the bank does not have an adequate system of deposits insurance. This Fund guarantees full repayment of client's deposits with a bank up to the amount of BGN 15,000 in case the banking license is revoked by BNB. Depositors' claims exceeding the repayments of the Fund are satisfied from the assets of the bank.

#### **XV.2.4. Bank Secret and Information**

Confidentiality of banking operations is crucial for the activities of each entity using banking services. Every legislator has to balance between the personal privacy and the public security in the combat against the money laundering and terrorism.

By virtue of the Banks Act, banks and bank employees do not have the right to disclose and to use to their personal benefit facts and circumstances concerning assets and movements in accounts and deposits of bank's customers. Pursuant to the Bulgarian National Bank Act banks are obliged to submit to BNB all requested documents and information in relation to the execution of central bank's functions. Beyond such cases, a bank may provide information on the transactions and balances of accounts of individual customers only with the consumer's consent or by decision of the court. The court may order the bank to disclose information in a limited scope of cases and by request of a limited scope of state bodies, for example in the case of data pointing to a committed crime.

The bank secret is further limited by the Measures against Money Laundering Act. As defined by law "money laundering" is the preparation, conducting and receiving the outcome of actions through which cash

or property, as well as what is acquired through these, coming into possession of an individual through or in relation to a crime, are introduced in the economic turnover".

The BNB, banks, investment companies, as well as a wide range of legal entities listed in the law are obliged to identify their customers, to collect, keep and disclose information on transactions. Banks identify their clients when establishing business relations, including opening of a bank account or securities account, and when conducting a transaction in cash in BGN or foreign currency over BGN 10,000. In addition, persons and entities are obliged to declare the origin of funds when conducting a bank transaction over BGN 30,000 or a transaction in cash over BGN 10,000, or their equivalent in foreign currency. The Financial Investigation Agency is an administrative state body under the Ministry of Finance. The law assigns to a broad range of entities, including banks, to inform the Agency of any cash payment over BGN 30,000, or its foreign equivalent made by or to a customer of theirs. This information can be used only for the needs of money laundering combat.

#### **XV.2.5. Conclusion**

A significant number of foreign banks are already present on the Bulgarian market. Most of these entered the Bulgarian market through the privatization process rather than through a licensing of a branch or subsidiary in Bulgaria. It is worth noting that the banking sector was one of the first sectors of Bulgarian economy where privatization was completed successfully.

The banking system in Bulgaria makes stable progress. The trends currently observed are credit expansion, wide spread of banking cards, Internet banking development, etc. The robust legal framework and the development of the Bulgarian economy provide good business opportunities in the banking sector at equal conditions for both local and foreign investors. The Bulgarian banking market still provides business opportunities for both new-coming and existing banks.

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