

CORPORATE GOVERNANCE IN BULGARIA'S ACCESSION TO THE EU: CORPORATE BOARDS PERSPECTIVE²

The pressure for change and synchronization in the accession process affected, practically, all the aspects of Bulgarian corporate governance (CG), one of them outstanding – the relevance and synchronization of the Bulgarian corporate boards (CB) to the European ones. The corporate boards' issues have a specific place in the CG problems. While, having its own significance, it penetrates all the other and reveals through them. Thus, all requirements for equal treatment of the shareholders happen through the actions of the executive and independent directors and all disclosures of information are carried out under the control and in the schedule of the Managing Boards, respectively Boards of Directors. The connections with stakeholders are completely in the domain of the Investor Relations Directors. This makes the knowledge of their adjustment in the Bulgarian accession to the EU crucial for assessment of the improved CG standards and this is the primary object of the present study.

JEL: G32, G34, G38, K22

1. Introduction

The CG issues have primary significance for the functioning market economy at micro-economic level. After Enron, Parmalat, World.Com and many others, it became crystal clear, that the problem is not only of Central and Eastern Europe, but of each developed market economy.

The **corporate governance** process includes complex interrelations between wide range of economic agents and regulating organs. Shortly, it concerns the functioning of the modern corporation in a way, which insures that: 1) the managers' activity is subordinated to the supremacy of the shareholders' interests, and 2) the interests of the small, minority shareholders are respected by the majority shareholders. In this sense, the term includes legal norms, requirements, rules, as well as the behavior of

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the economic subjects, which guarantee maintaining the interests of these two groups.

This way, the modern *corporate governance* includes decisions of strategic governance (emphasis is on strategic, not the operational ones) and it includes also controlling rules of the state and self-regulating business structures of character targeted to ensure the mentioned two groups of interests.

Still important, terminology itself is not enough for determining the significance of the problem. The latter is contingent not so much on any specific development of the economy, but more on the fact that corporate governance in fact represents mechanisms and norms regulating, at large, the market behavior of the economic agents.

The term corporate governance immanently bears in itself the goal of the market economy – maximizing the economic results in favor of the principal of ownership; thus setting the requirements of competitive, transparent and economically effective behavior. This, and not the economic fashion, determines the necessity of studying, and respectively, the level of academic interest in the corporate governance.

It is also important to understand that, the corporate governance consists of various phenomena, i.e. it is not a homogeneous process to be labeled, on the basis of certain feature, as convergent or divergent, (Tchipev, P. D, 2004). Corporate governance includes normative requirements and application of different standards, for (e.g. accounting³), and economic actions (for instance the mandatory tender offers by majority shareholder when crossing 50% threshold). If we consider the term in the wide sense, i.e. including the relations with stakeholders, then corporate governance will include also aspects of corporate culture, social responsibility, etc. (Prodanova, 2006; Bakurdgieva, 2007). This makes the attempts to search for (and find!?) whatever “factors (sic!) of corporate governance” not just impossible but also pointless.

2. Problems of and new requirements for Bulgarian corporate boards in the process of accession to the EU

The process of adapting of Bulgaria to the increased requirements of the European Union, improvement of the normative base and enrichment of the economic practices for its functioning as a full member, started a few years ago. It develops steady in time, reaches its peak with the accession act and continues for a certain period of time after that with the gradual elimination of the restraining conditions, set in the initial period, further building of the needed legal framework and introducing many practices, often called *best practices*, notable of the strongest economic union of our time.

³ It is not a coincidence that the Enron affair is an accounting one.

Concerning CG, the accession process started its active development with adopting the changes in the *Law for public offering of securities (LPOS)* in 2001, went through the purgatory of many improved sub-legal acts and regulations after that, reached its highest rate with the non-precedent development of the *Bulgarian Stock Exchange – Sofia (BSE)* in the months right before and after January 2007, and ended recently with adoption of the first national corporate governance code.

The pressure for change and synchronization in the pre-accession period practically ranged all aspects of the Bulgarian corporate governance (CG), among which is especially outstanding the following one: the correspondence and synchronization of the Bulgarian corporate boards (CB) to the contemporary standards. The corporate boards issue has a specific place in the system of CG issues. It penetrates, all the other and it is being revealed through them, though it has its own significance.

For instance, all requirements for equal treatment of the shareholders are accomplished through the actions of the executive and independent directors. All disclosures of information are made under the control and through actions of the Managing Boards, respectively Boards of Directors. The connections with stakeholders are completely within the domain of the Investors Relations Directors (IRD), etc.

At the same time, *corporate boards* have many specifics, which imply special treatment. First of all, their activity is regulated at public level to a very small extent; much more they are driven by the inter-corporate regulations, as article of associations, ethic code, best-practice CG code and alike.

Generally, lot of their activities remain unregulated and depend on the good will and understanding of the boards themselves; for instance, the procedures for selection of executive directors, logic and forms of payment, etc. We study these practices only indirectly from the proceedings of their meetings. Another source is the direct interview surveys.

The challenge for corporate boards, posed by Bulgarian accession to EU, affects all their aspects – structure, formation, functions, independence and dependence of their members, commitment, scope of deals, payment regulations, etc.

The induced change is made from the positions of the mentioned best⁴ CG practices, exercised in EU (and not only there, but in this case we are interested in EU). Some of these practices are protected by different EU directives, some are suggested in the form of recommendations by OECD, World Bank, etc., and some are just practices, voluntarily adopted codes, procedures or algorithms.

The accession reveals (and influences):

- Boards' structure: size, tiers of management multitude and members' qualification;

⁴ Sometimes it is called it good, sometimes, best practice, but the underlying idea is the same.

- Creation and active involvement in the management process of different board committees;
- Functioning of the boards, like enriching the classic management and supervisory functions with new ones; rearranging their significance and time spent on them;
- Board members nominations and selection forms and level of their payment, etc.

Finally, the deepest and most profound change, inspired by the accession process, concerns the *transparency* and *efficiency* of corporate boards' functioning.

Those deep changes in creation and functions of the corporate boards, as a backbone of CG, on the way of unifying of the EU countries practices, are the central object of study here, which is done on the basis of a field survey.

And, the extent, to which those changes reaffirm the best leading practices of the European Union, should be the main criterion for development of the Bulgarian corporate control and governance, since it is the only possible way of development for the country at the moment.

3. Sample and methodology of the empirical study

The specific information, needed to survey the practices of the corporate boards' - what are their real functions, how they solve the emerged conflicts of interests, how they choose their members, etc., could be found just on the spot. This circumstance pre-determines the methodology of present study: development of a standardized questionnaire to be answered through meetings and interviews with top employees in many companies, predominantly public ones.

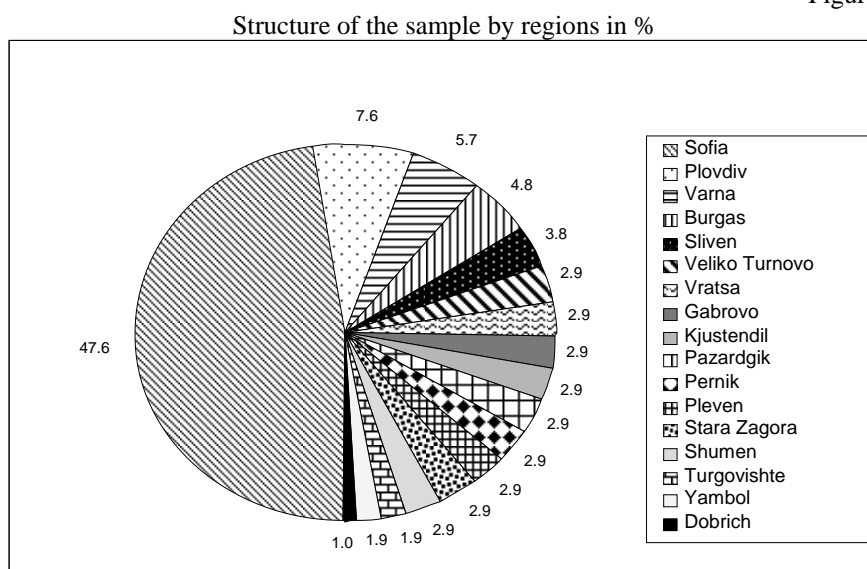
The current study has a pre-history in a pilot sociological study in 2002, which provided valuable information for constructing the questionnaire thus helping to eliminate many potential weaknesses.

The study was conducted in large joint-stock companies, the population includes practically all companies listed on Stock Exchange, plus most of the large financial companies, banks, insurance companies and pension funds, which are not yet listed, but definitely have a key role for the corporate governance. A population of about 330 enterprises was formed, which were distributed in 15 regional samples, and for which random sampling applied. Eventually interviews with representatives of 105 companies were conducted. Practically, this makes the study representative for the public Bulgarian enterprises, listed on regulated markets, plus the top financial companies.

The regional distribution of the firms is presented on figure 1. It shows well that the sample follows closely the actual model of geographic distribution of the economy,

and the Sofia firms are almost 50% of all participants. In reality, the share of Sofia enterprises exceeds half but the differentiation of *regional nests* introduced certain limit for them in the sample, so the study can better present the specifics of the corporate governance in firms outside the capital.

Figure 1



Source: own calculations based on data from the study

The distribution of the firms by size in the sample is presented in table 1. The chosen size does not correspond to the established lately in Bulgaria division to micro, small, medium-sized and large enterprises, but it is completely logical, since the study is focused on companies, which are (or will be) public, have immediate national significance and by definition are above the size of micro and small enterprises.

The chosen cluster distribution actually presents precisely the difference between those involved in the real business and the many holdings, financial institutions and other firms involved in business services, which have significant influence on the establishment of good corporate control in the sector.

Table 1

Distribution of companies by number of employed

	Frequency	Percentage	Accumulated percentage
Less than 100 people	58	55.2	55.2
From 101 to 250 people	17	16.2	71.4
From 251 to 500 people	14	13.3	84.8
From 500 to 1000 people	10	9.5	94.3
More than 1000 people	4	3.8	98.1
No answer	2	1.9	100.0
Total	105	100.0	

Source: own calculations based on data from the study

Though indirectly, the chosen distribution model offers also information for the scales of growth in the sector. The share of the large firms among the public companies is still small, about 6% both in the population and in our sample, having in mind that according to a report of the Ministry of Economy and Energy (MEE, 2004) the large enterprises in Bulgaria are more than 500. Hence, those facts show the still limited opportunities for increase of the investments in shares of public enterprises and a great potential for the recent future.

The branch distribution in the presented sample also follows the model of the population, but we should note that it is quite biased due to the very nature of the enterprises listed on Bulgarian Stock Exchange (BSE). It is additionally aggravated by the fact that from the non-listed companies we have added just financial institutions, which are promising as forthcoming listing⁵ because of their nature of operations and of their scale plus their strong positions for strict corporate governance. This distribution is based on the adopted National classification of the economic activities of NSI (2003 version, <http://www.nsi.bg/classifics/notes-kl.htm>) by economic sectors.

For two sectors – non-financial services and finance, it shows also a more detailed presentation by groups, so the studious reader can have a clear perception, which companies are referred in which sector, since for many reasons this is not always intuitively clear; to illustrate: Bulgarian practice shows the operative leasing into the second group, unlike the financial one, which is in the first group.

Table 2
Distribution of companies by sectors and groups of economic activity

Sectors	Economic groups	Frequency	Share
Processing industry	D	54	0.51
Finances	J 65.1 J 65.21 J 66.01 J 66.03 J 66.02 J 67.12 K 71	22	0.21
Non-financial services (renting, real estate, business services)	K 70 K 71 K72 K 73 K 74.15	20	0.19
Transport	I	1	0.01
Construction	F	4	0.04
Tourism	H	4	0.04
Total		105	100.00

Source: own calculations based on data from the study

The largest share of 51% of industrial companies is followed by 21% of financial institutions and 19% of the firms are in the area of financial services. This represents clearly the real sector, as well as both sectors, which are closest to development of the public enterprises in Bulgaria. The former privatization funds, which now function mainly as holding companies, are included by the statistic in the business services sector. This is the reason why this sector is so strongly represented in the sample.

⁵ This was completely confirmed by a wave of Initial Public Offerings (IPO) in the middle of 2007, when only for few weeks two average by size banks and a very active insurance company appeared among listed on BSE.

Still, the number of financial companies, listed on the exchange and offering opportunities for development of the investment process in Bulgaria, is insufficient. In the study, this is overcome by including in the population, many unlisted, but important potential candidates from this sector, like Commercial Bank Alliantz, large leasing companies, etc.

We have to note that some of the undoubtedly holding companies are referred to the financial sector due to the extreme concentration of their activity in this sector, like Alliantz Holding AD. While apparently improper, this self-identification is left unchanged in our sample, because indeed, all firms from this holding are placed in the finances – banks, pension and insurance companies.⁶ The shares of tourism and construction in the sample also represent well the actual distribution in the economy.

The only problematic area appears to be the branch of transportation, which seems under represented in this case, even though its actual share in the pool of the Bulgarian public enterprises is also small. The possible answer for this inconsistency is, that the firms with transportation business have another businesses as well, mainly commerce; thus they identified themselves in other sectors.

The cross section of the sample by type of ownership is of course most interesting. In principle, the ownership in the Bulgarian companies is strongly concentrated from the time of the mass privatization (see for example Tchipev, 2001). Then, partially as a result of unsuccessfully set model and partially because of ruthless corporate interests, the *regulative threshold*, preventing the transfer of more than 33% of assets of any mass privatized company to a single investor, was bypassed.

Table 3

Distribution of companies by form of ownership

	Frequency	Percentage	Accumulated percentage
Bulgarian shareholder with package of shares more than 50%	49	46.67	46.67
Foreign shareholder with package of shares more than 50%	13	12.38	59.05
One leading shareholder with package of shares between 33 and 50%	9	8.57	67.62
Two or more leading shareholders with packages of shares between 33 and 50%	13	12.38	80.00
Without shareholder with package of shares more than 33%	20	19.05	99.05
100% state ownership	1	0.95	100.00
Total	105	100.00	

Source: own calculations based on data from the study

⁶ This raises the principle question of how reasonable is the statistical practice to classify the structures managing large investments (i.e. the holdings) together with firms managing investments in real estates and renting activities, but this question goes beyond current paper.

In this sense, the fact that 59% of all enterprises in the sample are majority controlled is not considered surprisingly high. There is rather a slight reduction of that concentration in the last years. Just a few years ago this share was almost 62% (for the results of the pilot study here and below see Tchipev, 2002). Those almost 47% majority controlled by Bulgarian shareholder reveal the same logic of existence, but with a slight increase compared with the findings in the pilot study (42.17%).

If we try to generalize, the revealed specifics of the distribution of ownership in our sample perfectly fit the logic of the current processes in the Bulgarian economy:

- a) Many increases of the capital, which (at least in the last years) lead to decrease of the concentration on account of many new portfolio and/or individual investors;
- b) Increase of the participation of Bulgarian investors, either directly through the BSE, or through collective investment schemes.

Almost 21% are the companies with leading minority controlling blocks, which is also considered a positive development in the structure of ownership, since these companies obviously strive to expand their free float on account of decreasing their controlling share, though for many reasons they still fear ownership diversification. This is valid especially for the cases (13 in the sample) of presence of two large minorities in a company, which in principle offer much better form of corporate control.

The tendency of decrease of the concentration, though not so strong yet, is felt extremely in companies with form, which does not have a clear controlling block – they are at least 19% and are a lot more than the analogous 14.46% from the pilot study.

Here, we need a little theoretical divergence. According to John Scott (1986), the level of 33% ownership of one company in same hands, is very high to speak of diversified ownership. Moreover, Scott tells that controlling block even at 17% leading block is feasible, and that is why he holds the principle that the controlling threshold should be set at the level of 20%. There are other suggestions in the literature even for 10%.

For our analysis though, we should have in mind the specifics of the Bulgarian development, the levels and the pace, of the changes of the public companies in Bulgaria. If we use the methodology of the contemporary *evolution political economy*, it is necessary to apply the “path-dependant” approach to present more adequately the Bulgarian reality. That is why this study uses 33% threshold to define the diversified ownership.

To mention the only case with 100% state ownership, it is the biggest Bulgarian provider of heating water and its ownership is actually municipal and not a state one. The population included a few more enterprises with state ownership, but they were

formed in a specific group and that is why their inclusion in the sample was not guaranteed.⁷

The picture of ownership is enriched with the answers on presence of a portfolio investor. More than 50% of the companies have a such, which is a good attestation for the development of the corporate control, since by definition it is assumed that namely this group of investors is most actively involved in it. Being generally smaller than the controlling owner, with mobile and active capital, strongly interested in the increase of the capital profits, these institutions are placed perfectly on the market for corporate control. True, in developed market economies they play a double role and sometimes (at least some of them) can remain passive, but in the Eastern European countries they are practically the only serious alternative to the controlling owners. Of course their role should not be over-estimated, since we still need another study to see which are the most active and the most passive ones in Bulgaria.

Nevertheless, the total share of these companies is increasing, compared with the pilot study, and this is more than encouraging. Table 4 shows that besides the 25% of such investors, represented by former privatization funds, which to a certain extent are inherited (though it is not a problem since this number remains stable in the time from the pilot study), there are also other, more than 12%, represented by the Bulgarian financial institutions. It is another manifestation of the encouraging trend of diversification of the ownership, which is observed among the Bulgarian public companies and reflects the creation and development of powerful investment portfolios of pension and insurance institutions.

Table 4

	Frequency	Percentage
Bulgarian shareholder from sector of finances	13	12.38
Bulgarian holding	27	25.71
Foreign shareholder	13	12.38
Another shareholder	8	7.62
There is no such	33	31.43
No answer	11	10.48
Total	105	100.00

Source: own calculations based on data from the study

The foreign companies are also more than 12%, which is considered encouraging, having in mind that they strive to avoid being bound with the Bulgarian controlling owners. And if there are some doubts about the nationally-based portfolio investors, whether they are portfolio investors, the role of the foreign investors is much more defined.

⁷ Having in mind the specific characteristic of the firms with public ownership, this additional criterion can be set in order to ensure a better representation of these firms in the sample; this is surely an important condition for improving the future studies in this direction.

It is worth mentioning shortly also the respondents who replied “other shareholder”. This category generally includes physical entities with fewer shares, which also function as portfolio investors, but the picture in Bulgaria is really very complex and that is why we preferred to refer them in separate category.

One of the strongest profiling characteristics of the corporate governance is the structure of the firms by the number of their governance tiers (one- or two-tier management schemes) and this is the reason why the presentation of the results essentially starts with it.

4. Structure of corporate boards by the tiers of management

The distribution of the corporate boards into one- or two-tier schemes is of essential significance for the world corporate practice. Traditionally, two schemes are acknowledged – Anglo-Saxon and German. In the first the management is unitary, but there is a subdivision inside the board between executive and non-executive specific management functions. Those are *Boards of Directors* and the directors can be *executive* and *non-executive*.

In the German system of corporate governance, the separation of the functions is pre-determined by the presence of two different organization structures, so it would be impossible even in theory to combine alternative functions in the hands of a single director. Respectively, those are *Supervisory Board* and *Management Board* and the participation in each is exclusive for their members. The first has supremacy over the second, which does not quite follow the principle of separation of the Anglo-Saxon system. Unfortunately this detail is completely ignored by the Bulgarian researchers, which consider the difference in the structures merely as a matter of liberty of choice.

Without going too much beyond our problem, I have to say that the number of management tiers is also *significant issue*. It concerns the presence or lack of independence among the directors. Since the independence principle is difficult to sustain, as we will see later, the formalized separation of the supervisory directors from the operative management *hinders* the attempts to mock the independence of the directors, or to exercise informal power in the Board of Directors, etc. Roughly speaking, the two-tier structure is a better guarantee for the principle of independence of the operative management from the supreme power of the shareholders.

Of course, the one-tier structure is significantly simpler and cheaper, which for Bulgaria, often, is the good reason for preference when choosing the structure.

Before we go to the results, we have to make an important addition. In some countries the mentioned difference between the two types of structures is considered so significant that a free choice and coexistence between them is not allowed (for example in Germany). Unfortunately in Bulgaria the under-estimation of this issue (or the misunderstood liberalism) has led to lack of a serious study of the advantages

or disadvantages of the mixed application of both forms. Moreover, only few people know the real picture of the corporate boards' tier-structure nationwide.

The pilot study revealed 80% companies with one-tier management structure and about 20% - with two-tier structure; the current study shows a little over 76% of the first and almost 24% of the second type. The decrease of the one-tier boards is due to the increase of the sizes of the firms, as well as the increased number of financial companies among them, and should be undoubtedly considered a positive phenomenon.

5. Size structure of corporate boards

The size structure of the Bulgarian corporate boards has substantial significance for the ways of realizing their functions. General principle is that, larger boards can carry out more differentiated and complex functions, dedicating more people to specialized tasks. This is especially valid for the Boards of Directors, which combine two functions – operational and supervisory. Second, the size of the boards determines to a great extent their transparency and predictability in decision making, and in this sense, again, corresponds well to the principle of independence of some of the directors of the corporate enterprises.

The pilot study showed that in the *one-tier* firms 54.10% of all *Boards of Directors* have 3 members, another 33% have 5 members. The current study confirmed almost completely the number of three-person boards: 55.29% of the firms with one-tier management (or 47 cases). There is a decrease for the boards with four and five members – they are under 25%, but there are another almost 12% – with 6 to 9 members, which compensate the mentioned decrease. Rest replies are invalid or not answered.

In the firms with *two-tier* management structure, there are 38.46% with three-member supervisory boards and about 40% with 4 to 7 members; their number is evenly distributed between 4, 5 and 7 members in the boards. There is also a decrease of the number of the smaller boards on account of boards with more members than that in the pilot study – over 70% have been, then, three-person boards. Unfortunately, here we have more cases of not-answered than in the case of one-tier structure.

Among the *Management Boards* dominate 3 and 5-person ones – totally over 65%, distributed almost evenly between the two sizes. The cases with larger boards are just a little less than 20% totally, plus 15% not answered and they are distributed evenly in the groups of 6 to 9 members. Considering the small number of boards falling in this group, they can be seen mostly as an exception. The latter statement is confirmed by the *weighted average size* for each type of boards – 3.9 members for Board of Directors, and 4.1 for Supervisory Boards and 5.2 for Management Boards. The numbers are very close to those in the pilot study; they are even identical for Board of Directors (3.97) and for Supervisory Board and Management Board are slightly greater (respectively 3.4 and 4.4).

Though these results can be interpreted as following the principle of economic efficiency, since they keep close to the lower limits prescribed by the law, they are not so unambiguous regarding corporate governance as we will see in the next section.

6. Education and qualification characteristic of corporate boards

The pilot study could not find specific requirements concerning the background or professional qualification of the Board-members, than those required by law. That is why the questionnaire reflected the general norms for being on the board and the results were to a great extent predictable: serious pre-dominance of Master's and higher levels of education and of economics qualification, plus some share of finances and law. The "triviality" of those results caused this aspect of the study to be shortened significantly here.

7. "Connectedness" of the members of the Bulgarian corporate boards to the firms, controlled and managed by them

This section of the study concerns the presence of affiliations and features of the members of Bulgarian boards, which would encourage their behavior in a way, different from that expected by default. The questions in the interview aimed to reveal to what extent based on the cited above "complementary" affiliations and relations board members could establish a parallel network of interests, potentially not matching the interests of the independent investors, considered in the widest sense of this term.

The information for this sector is generally difficult to obtain and that is why the questionnaire included a series of questions, finding and controlling the mentioned characteristics. These questions originated from the principles and vision of OECD for "*independence*" of the directors, as well as from the concrete definitions, set in the Bulgarian legal order.

The first cross-cut of the data is the most "visible", if one can say so. It concerns the presence and number of *the members of governing boards who are executive managers or top-level officers* in the firms. The answers again are split according to the tier-structure of the boards, since the different tier-structures have different requirements. The set presumption is that a strong "connectedness" of many of the directors with the operational functioning of the firm could stimulate shortening of the time horizon for the decisions and synchronizing the maximization of the profit with the election horizons, rather with the natural production cycle.

The results for the *two-tier boards* show the following:

- There are 7 cases when the members' *supervisory boards* have management functions. For Supervisory Boards, however, this question is controlling one because, legally, they should not have members with playing executive roles and

the results should be interpreted as an error. Of course we can assume also a presence of violating behavior in some firms, but it is hardly possible such practice to be revealed in a public study such as presented.

- *Management boards* have 72 positive answers of all 114 directors, i.e. a little less than half of all cases. There are no logically invalid answers and the results are considered reliable, which leads to the interesting result (actually found also in the pilot study), that not all members of the management boards have management functions.

Most meaningful are the data for the members of one-tier **Board of Directors**. The valid answers there are 69, because 6 of the respondents have given logically contradictory answers, namely that in their boards there are no such members, and 5 other firms have not mentioned the number of these members.

- Of these 69 valid answers we find 153 members of the *boards of directors*, who have executive obligations; they are almost 50% (total number of **Boards of Directors members** in the sample is 322). The result in any case is not contradictory and fits well with the maximum share of the not-independent directors of two thirds.

The second cross-cut of the problem of “connectedness” of the board members concerns the presence among them of such members who themselves are, or represent, large shareholders in the firm. The questionnaire has a set threshold of 25% size of shareholder holdings (direct or through related parties), above which their owners are considered large shareholders. It is assumed that above this threshold there is a control according to the OECD methodology, which can be found in the Bulgaria Accounting Act as well.

It is noteworthy, that Bulgarian legislation requires disclosure of any 5% or bigger voting bloc, since there is an understanding that the underlying interest cannot be treated as independent. That is the reason, to monitor how many directors have such interest in the firms controlled and managed by them.

True, our methodic poses a less strict requirement than the legal one for detecting the substantial interests, but it is more realistic, since it reveals interests that are captured more easily and hence, that are more emphasized. This difference in the approaches leaves specific trace on the results, which show methodologically determined lower presence of influential shareholders among the board members than the real one, but this presence is more categorically outlined.

The study produced the following results:

- Among **two-tier boards**, only about 12% of the members of the supervisory boards and less than 1% of the members of the management boards are also shareholders with stake larger than 25% in the capital of the firms they control or manage.

- Among **one-tier boards**, more than 20% of the members of the boards of directors are large owners, by 25% criterion.

The results, even for board of directors, are plausible, since these are large firms and an exposure of 25% share in the ownership is not very often, and also they comply well with the data of the pilot study; we got, then, 11.76% for the supervisory boards and 1.52% for the management boards, and 35.54% for the single-board firms.

The average number of large shareholders in a board of directors is 1.83 persons in the current study against 1.79 in the pilot one. For two-tier boards, the figures are 2 persons now against 0.75 in the pilot survey (**supervisory**) and exactly 1 person in both studies (**management ones**).

The third cross-cut of the mentioned problem concerns the presence and degree of “connectedness” of the members of corporate boards of one company to positions on the boards of other firms, including related ones.⁸

The results for *two-tier firms* show (case of *supervisory ones*):

- 51% of their members are in management bodies of other firms as well
- 44% of their members are in management boards of *related* firms.

When looked firms’ distribution, 65% of all firms in the sample have Supervisory Board-members, who also sit on governing bodies elsewhere; if taken just related firms – the corresponding figure is 60%.

The results for *management boards* show, logically, lower degree of “connectedness” of their members to governing seats in other firms. Namely:

- 42% of their members are in the governing bodies elsewhere as well
- 33% of their members are in the governing bodies of related firms.
- From the other perspective, “multi-board directors” are present in almost 67% of all firms in the sample, and if taken just related firms – within little less than 48% of the firms in the sample.

For *one-tier firms* the data of the boards of directors are the following:

- 39% of all directors on the board of directors occupy positions in the boards of other firms as well
- 27% occupy such position on the boards of related firms.

⁸ When the process is bilateral, the phenomenon is known as interlocking directorship.

Distributed by firms these results are respectively 72 and 52% of the *single-board* firms in the sample, provided valid answers.

It seems quite normal that the directors' "connectedness" *only to related firms* is lower than the analogous one with firms in general for the whole sample.

From the other hand, it is logical the highest figure refers to the one-tier firms; and in cases when the firms are not related each other the figure for "connectedness" reaches even 2/3 of all members of the board. Even that this does not contradict the law, since the companies are not-related formally, the figures suggests necessity of further studying of the principles of "connectedness" adopted in Bulgaria, as well as the reasons for such "binding together" of the boards of directors.

The observation, that the management boards show generally lower values than the supervisory ones is also compliant with overall logic of the governance. This is explained by the routine of the functions of the management boards, which have more limited time and generally lower position in the firm, which prevents them from being involved in many management combinations. At the same time it is worth noticing that for the management boards these numbers are quite high.

Compared with the pilot study, when observing the "connectedness" indicators only as share of all directors, but not as distribution among the firms, the current data are definitely higher:

- For the *one-tier* firms the result is – little less than 35% of "multi-board" directors' presence (respectively, 31% – only in the boards of related firms).
- For *two-tier firms* (both for supervisory and management boards) the results are about 25% in the pilot study, with slight variations depending on whether there was or was not a formal relation between the two firms.

8. Independence of the Bulgarian boards

This section in the study contains characteristics of fundamental significance, since it shows to what extent the current state of the Bulgarian boards satisfies one of the most important specifics of the contemporary corporate control and governance, namely the presence of sufficient in quality and quantity representatives of the society, of the general public, in the governing bodies of the public companies. Aphoristically, the aspect emphasized here shows how public are the Bulgarian public companies.

The actual legal norm requires at least 30% of the board-members to be independent, which is a good guarantee for ensuring an outsider view on the activity of the firm, which is supposed to be useful for small, individual and minority investors in the public company. This will make the firm attractive to the potential (including foreign) investors and in this way will be a base for its actual and active publicity.

The other moment concerning the issue of independence is its definition; the study uses complex definition, which defines as independent regarding a studied firm the people, which:

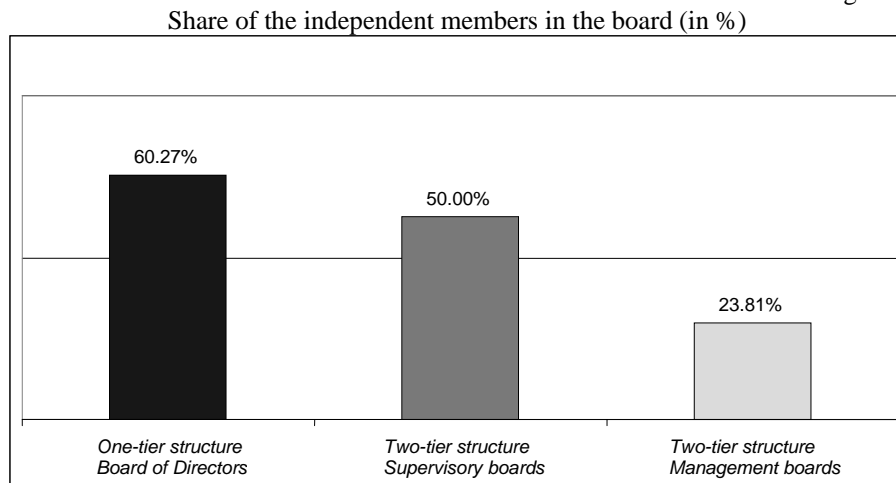
- a) Are not its employees
- b) Are not in long trade relations with it
- c) Do not own 25% (or more) of the votes in its General Shareholding Meeting
- d) Are not in the governing bodies of firms by b) and c)
- e) Are not related parties with other member of its management bodies

This definition is in accordance with the OECD requirements and gives quite clear wording without contradicting to our domestic legislation. For instance, the 25% threshold is set also in the Bulgarian norms as a bottom line for existence of control. Later, requirements c) and d) actually mean that independent is only a director in a firm, who does not exercise direct control over it or through a firm, which in turn, controls 25% of the capital of the firm in question.

At the same time, the world practice is still ahead and sets the condition for lack of control also in the cases, when a director is a director in a subsidiary firm, since both are affiliated and therefore his interest in the subsidiary firm by induction is not independent in the mother-firm as well. Besides, the world “best” practices count also the time for being member of a certain board. Though, not unanimously, it was approved that after 7 years spent in a certain firm, its directors should not be considered anymore as independent concerning the firm, since they receive different privileges, bonuses, pension options and other, which make them more or less dependent on their interests. Hence, the results from the study should not be considered conclusive. It is assumed that the actual “connections of dependence”, which can emerge between a firm and its director can be even more various, including even some undisclosed. Still, this study provides, at least by now, the only attempts to verify this “connections” in Bulgarian boards with the all qualifications, which can be made.

Our data showed 50% and less than 23% share of the independent members in the *supervisory boards* and, respectively, in the *managing boards*, and almost 60% – in the boards of *single-tier* firms.

Figure 1



Source: own calculations based on data from the study

The results, except for the management boards, are probably over-estimated, because of the reasons mentioned in the previous section, as well as because of the presence of a substantial percentage of invalid answers (20% of the answers for *supervisory boards* for example). Compared with the pilot study – 34% for boards of directors, 35% for supervisory boards, and 29% for *management boards* – these results show development in two directions:

- 1) On one hand, the pilot study was realized right in the period after adopting the requirements of independence and not all firms would succeed to implement it in practice. At that time 47% of board of directors did not state independent members at all; now this number is 39.7 of the valid and 36% of all single-board firms in the sample.
- 2) On the other hand, the increase of the share of independent members in all boards is a reflection also of the whole process of increasing transparency and disclosure of our public companies.

Such statement finds support as well from the great number of answers provided about the coincidence (actually non-coincidence) of the persons performing both functions of **Chairman** of the Board of Directors, (resp. of the Managing Board) and of the **CEO**. The study found such non-coincidence in almost 65% of all cases, which is not only evidence for good CG, but it is also an indirect proof of increased degree of independence, since the separation of the two functions means generally an opportunity of the executive directors to distance themselves from the direct shareholders representatives. And vice versa, this guarantees a certain freedom of the decisions of the Chairman of Board of Directors (resp. Managing Board) from the current situation in the firm in any given moment.

In order to evaluate how independent are the decisions made by the boards, we use two “*perception*” indices, constructed to determine the influence over them of the two potentially strongest “related parties”: that of the large shareholders and that of the managers. Figure 3 gives evaluation of the respondents on standardized scales; the values shown below the columns).

Figure 2

(In)Dependence of the decisions of Board of Directors, respectively Supervisory Board



Source: own calculations based on data from the study

The clearly outlined in both indexes domination of intermediate answers confirms the presence of sufficient number of independent directors in many of the boards. At the same time, the presence of small group of boards (17-25%) is easily detectable, where the two “most related parties”, in terms of corporate governance, (the large shareholders and the managers), are able to exercise their power over the corporate activities virtually unrestricted by the mediating role of the independent directors.

It is noteworthy another fact, in the analysis of the behavior of the managers, the cases of strong interference by them are more explicitly presented than the cases of such interference by the shareholders, i.e. the shareholders are more often inclined to restrain from interference than the managers in the work of the boards. Moreover, the total number of answers with values 4 and 5, exceeds the total number of those with – 1 and 2, in the case investigating the influence of the large shareholders, which shows, as a whole, their more moderate behavior in the corporate control.

Of course, we should not exaggerate this conclusion, since the managers themselves are appointed by the large shareholders (in some firms there are even quotas). Nevertheless, it is an evidence of “*complying*” behavior of the large shareholders, keeping in mind the world practice corporate governance mechanism: all shareholders decisions to go through the board (and not directly) and to be conformed with the independent directors.

Table 5 gives a good opportunity to “verify” the given so far answers, introducing besides “perception” replies, a piece of factually checkable information. We asked the respondents, have their companies introduced norms guaranteeing the opportunity of the board-members to sustain their independent opinions without negative consequences about their position in the firm.

Table 5
Formal protection of “independent” opinions of the Board members

	Frequency	Percentage
Yes, we have already approved such decisions in the Articles of Association	15	14.71
This opportunity is discussed but for now it is not approved	18	17.65
No, this question is not on the agenda for now	43	42.16
The problem is not actual due to insignificance of the independent directors in our firm	26	25.49
Total valid answers	102	100.00

Source: own calculations based on data from the study

Logically, the share of the answers showing presence of this “real” independence of the managers decreases. As it is shown, only less than 17% of the firms have in their articles of association norms, guaranteeing the free defense of positions by the independent directors, and another 16% will probably introduce such requirement. At the same time, quite sobering is this ¼ of the firms, which without hesitation confirm the revealed above information that for them the independence is still, far from the reality.

Although, the neutral answers are more than those in the previous analysis (more than 40%), they are still the same as importance and support the statement, that in the majority of cases there is “*independent presence*” of directors, but its position is not explicitly confirmed.

9. Identification and resolving of conflict of interests

One of the most interesting and most actual issues of the contemporary corporate governance is whether and how is revealed the presence of conflicts of interests in them. The actual best practices in the European Union require disclosure of information for the cases when the board-members of a firm have vested interests in a business partner firm; or their family-members are in similar position. Or they are involved in decisions for acquisition and takeover of firms, in which they have holdings or by some other way are related to both parties of a deal or possess an insider information, which make their position favorable of a certain decision.

All these and similar cases of conflicts of interests are more or less elaborated in the relevant legal norms of the European countries and require appropriate disclosure. Common rule is that after announcing the event, usually to the relevant corporate board and/or GSM, there are applied some procedures for their resolving. Most often the person subject of the conflict restrains from voting in the specified deal or the deal is rejected (Directive, 2003/125).

The adopted in Bulgaria text requires avoiding conflicts between the interests of the board-members and the interest of the company, and if they occur – disclosure to the relevant organ and non-participation (plus non-interfering) on the other members of the board in making decisions in these cases (LPOS, 1999). Nevertheless, the practical procedures identifying and treating the conflicts of interests are left to the firm articles of incorporation.

That is why the study set this problem as one of the most actual questions of our accession to EU concerning corporate governance. The received answers are summarized below:

- We have detailed assigned procedure – 23.08%.
- The procedure is not assigned but there is a practice – 14.42%.
- There is no practice in such area – 4.81%.
- This problem is not in the agenda – 57.69%.

There is a presence of quite large number of firms, which have such procedure and/or prepare it; the accumulated result of the first two options is 37.5%. In comparison, the pilot study showed 35%, and just 7.5% were working procedures and the other – would-be. Now we can see, that many of them are already adopted, though there is still something to desire. Analogically, the share of the firms, which reject or have no such a practice, has dropped from almost 70% to 61% in the last few years.

10. Functions of the corporate boards

The functions of Corporate Boards are various and depend on the firm's discretion. Although, all large public companies face the same problems, the ways they solve them are far not from being standardized. Moreover, these functions practically cannot be regulated. At the same time they are strong marks about the development of the process. Thus, besides the wide-spread like strategic planning, monitoring of management performance, there are some, which develop under the influence of the contemporary best practices for good corporate governance. And, namely the latter are most likely to be subject of influence in the EU-accession process; that is why our study tries to define the degree of their development.

Nevertheless, the attempt to catch the latest development about the most sophisticated functions, the present study reports all performed functions. Thus, it creates a picture showing the dynamics of the process rather than a *fact complete*.

The observant reader has perhaps, already guessed, what a huge difficulty is the analysis of this section of the activity of the modern corporate boards. Besides the variety, which has to be restrained in an inevitably frame, the issue of quantifying and comparing of these functions is a serious challenge.

With the important exception of the already mentioned pilot survey (Tchipev, 2002), which differentiated to some extent, the study presented here is the only known to us study for Bulgaria in the field; thus offering solutions, which are necessarily initiating, but inevitably bearing all the possible shortcomings.

The methodology was developed in a dialogue within *the OECD South-East European CG Roundtable* and it is based on a few elements. Most important, the clusters of functions are summarized following the approach applied in OECD principles of corporate governance.⁹ There, the functions are recommended, but not mandatory and cover a wide range of important activities, more or less embedded in the *corporate boards*. Their character is quite substantial and their observance them does not seem to create a problem for a standard company.

After grouping, the functions are ranked by significance as a result of the answers of the respondents, the function with highest frequency of appearance in the responses has highest rank, and the rest are ranked accordingly with the decrease of the answers mentioning them.

The answers of the respondents refer to the functions performed of the relevant board (or boards) twofold: a) whether the function in question is formalized, i.e. whether it is included among the board responsibilities by a written document (Statutes or else), and b) if not, whether it is still considered significant by the Board, i.e. whether it is supposed to be performed, though without formal sanction.

This, rather complex, methodology aims to identify whether the Bulgarian public firms are ready to expose, to make transparent and respectively to allow for debate their activities, thus, ultimately, **subordinating** them to their shareholders.

The results from the direct answers are presented in *table 6*. They show, first, that the function referring to the *corporate strategy development* is ranked 1st, i.e. the largest number of formalized cases. It is followed by the *overseeing of the relations with shareholders, regulatory bodies and the society*. Third is the classic function of *monitoring of the overall governance*, aiming ensuring the most basic essence of the firm, *its effectiveness*.

The functions so far, can undoubtedly be determined as more or less standard and traditionally performed, referring to the main activities of the firm: optimizing

⁹Section V of the OECD (1999).

against the most important factors of its existence, including the shareholders. They also strive for achievement of that needed market effectiveness and corporate strategy. This is most clearly seen for function ranked 1, which is *par excellence* embodiment of the supreme governance of the most important corporate events.

Table 6

Ranging by significance of the functions of the Bulgarian corporate boards

Written, i.e. formalized functions	Rank	Frequency
M onitoring* and guiding corporate strategy , major plans of action, risk policy, annual budgets and business plans; setting performance objectives; monitoring implementation and corporate performance; and overseeing major capital expenditures, acquisitions and divestitures.	1	76
G Overseeing the process of disclosure and communications	2	67
F Monitoring the effectiveness of the governance practices under which it operates and making changes as needed.	3	64
E Ensuring the integrity of the corporation's accounting and financial reporting systems , including the independent audit, and that appropriate systems of control are in place, in particular, systems for monitoring risk, financial control, and compliance with the law.	4	61
C Reviewing key executive and board remuneration , and ensuring a formal and transparent board nomination process.	5	61
B Selecting, compensating, monitoring and, when necessary, replacing key executives and overseeing succession planning.	6	58
D Monitoring and managing potential conflicts of interest of management, board members and shareholders, including misuse of corporate assets and abuse in related party transactions.	7	36

Source: own calculations based on data from the study

Not until Function #4, one can speak about a relation to the good corporate governance in its own specific sense; the *disclosure of information* is a primary mechanism for ensuring transparency and predictability of the company's activity for the sake of interests of all its shareholders.

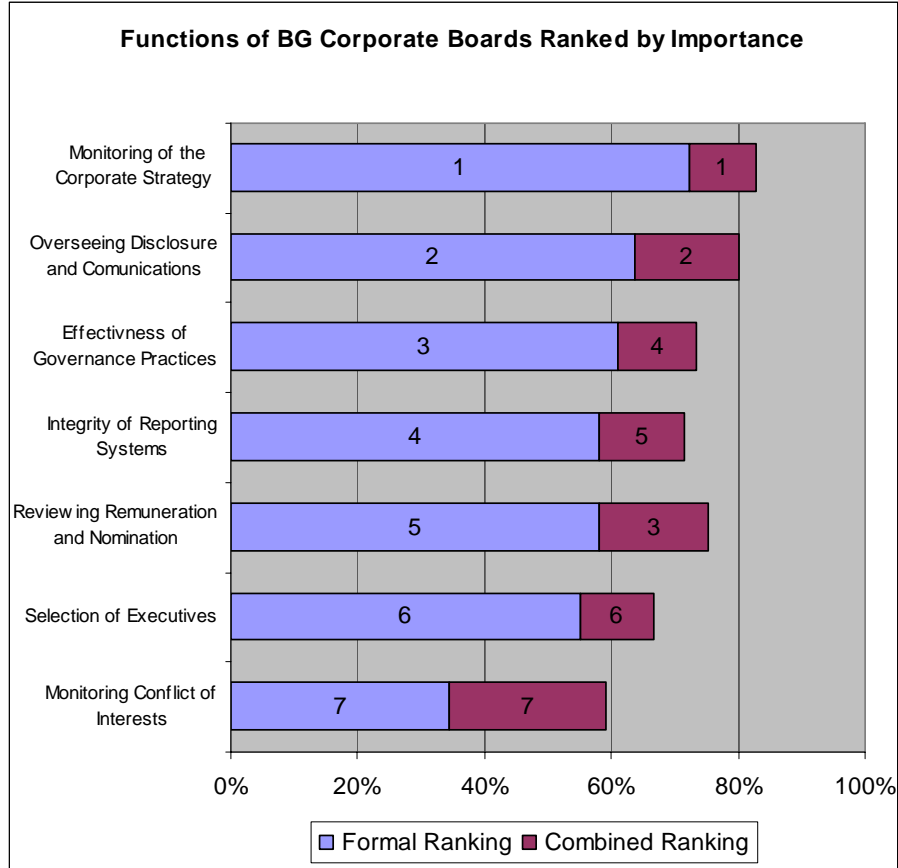
At the same time we have to mention that this function is "*imposed*" from outside and hence, it is unavoidable for the firm. The whole procedure of who, in what case, to whom, how soon and by what channels discloses corporate information is written in most details in laws, ordinances and corporate codes for good corporate governance. So the presence and relatively high place of this function is a good, but not decisive attestation of progress in the analyzed field.

The function of *control of the remuneration of the executive directors* and other members of the boards, *their selection* and when necessary – their *replacement* is far more important and substantial for the corporate governance. And of course, the function of *solving the conflicts of interests*.

As figure 4 shows, these functions are not only far behind the others, as frequency of formalization, but even as informal preference; as a result of which, their combined ranks are also low (In combined ranking the supposed, though not-formalized functions are added to the formalized functions, in order to get a more complete picture.).

* The text in bold form short name of the function, used in figure 4.

Figure 4



Source: own calculations based on data from the study

The only case of switching the places as a result of added combined ranks is the function of *control of the remuneration of the executive directors* going up to the third place on the scale, thus pushing down two of the more conventional functions. Especially unfavorable is the position of the *Function of management the conflicts of interests*, which not only is on last place as formalization (little less than 1/3 of the cases), but it is at the same place even after combined ranking.

This shows that the most sophisticated functions concerning terms of working governance and transparency of the CB actions remain considerably underestimated. It also shows the lack of explicit understanding of the danger and seriousness of emerging conflicts between the interests of the firm and those of its managers.

Still, we can say, that the accession of Bulgaria to the EU plays a positive role, since, with the exception of the latter, all other functions have meaningful values (and formal acknowledgement) in more than 50% of all cases in the sample.

When compared, they almost completely repeat the ranging in the pilot study, except only for the functions of *controlling of the remuneration of the executive directors* and of *selection*, which have switched places there.

The level of significance in the pilot study, was a little higher; Function #1 had value of over 90%, and the last one (rank 7) – over 40%. The drop, however, is due to the changed methodology in the current study, where for the first time we used the technique of combined evaluation, and that is why we referred the positive answers to the whole sample and not only to the valid cases, as it was in the pilot study.

11. Diversification of the activity of the corporate boards through establishing of board-committees

One of the important ways for development of the corporate governance in our accession to the EU is enrichment and specialization of their activity through establishment of special committees. These committees have a task to perform certain activities, which are normally in the area of the boards. The difference is that there is:

- Specialization of certain number of members in certain activities;
- Increase of the transparency, since they plan and report their activity usually to the boards, but often to the General Shareholders Meetings as well;
- Institutionalization and in this way decrease of the subjectivity of the made decisions.

In this way, the committees become an important instrument for introducing the best CG practices of the European Union in Bulgaria. Their introduction is new neither for the EU nor for the Bulgarian practice. The new is that applying the OECD recommendations the process becomes organized and hopefully more decisive.

Our study showed that some of the firms apply more or less systematically this European (and world) practice. Table 7 shows the results.

Table 7

Bulgarian Corporate Board Committees

Committees	Number	Share in the sample	Average number of members	Evaluation of their effectiveness
For strategic planning	2	1.90	3,50	4,00
For audit	15	14.29	3,53	3,76
For payments	1	0.95	3.00	3,67
Other	11	10.48	3,67	2,09
Total	29			
Without committees	75	71.43		
Total valid	104			

Source: own calculations based on data from the study

Almost 28% of the boards report application of those practices, which is evidence of a good start. Unfortunately, almost half of them concern again a routine and required legally operation, namely the choice of auditor, who will certify the annual report to the General Shareholders Meeting (GSM). This shrinks a lot the field of this modern CG practice and gives it a supporting role.

On second place with about 7% of all practicing companies are the ones establishing planning committees for supporting the management in setting and reporting its goals concerning the effective governing of the firm.

Committees for determining the remuneration of the executives, which are considered the most contemporary and best practice in this relation, exist only in 3-4% of the firms. Committees for selection and nomination of the members of the boards and executive directors do not exist at all. The latter is the best guarantee anywhere in the world for objectification of the process of a choice of business leaders and the most powerful restraint against the corruption in this field.

Unfortunately, the results are worse (even by little) than the pilot study, where about 33% of the firms showed such practices, but again there is certain incomparability of the results, since then we were interested in the number of committees, and now we are interested in the number of committees applying the practice. However, the practice at that time was also mainly about the auditing and planning committees.

The only positive moment for now is in the presence of considerably large number of so-called other committees, which deal with:

- specialized branch problems (particularly useful for the holdings), including the sectors of company's investments;
- the changes of the legislation;
- technical issues;
- management of the investments;
- risk appraisal.

As a whole, those new forms of committees count over 10% of the sample and over 1/3 of all committees. This diversifies and enlarges the practice, and it is definitely a positive moment of the accession process.

The evaluation of their effectiveness logically counts for an average mark, with slight prevalence of higher marks for the widest distributed and most routine form of committee, that for planning. The low marks of the committees dealing with new functions are a little strange, but it is probably determined by the lack of experience. The average size of the committees ranging between 3 and 4, is also plausible, having in mind the small number of all members of our corporate boards.

12. Evaluation and compensation of the activity of the corporate boards

One of the most important characteristics of the corporate boards in the context of the improved European CG practices concerns the ways, in which they evaluate the activity of the boards as a whole and of their members in particular.

The applied methodology here deals with some important points:

- First, the beginning of that analysis concerns the presence and form, in which they perform the evaluation of the activity of the management organs.
- Second, the next section aims to determine only the place and work of the executive directors.
- Third, the goal is to reveal the presence of a connection between the remuneration of the executive directors and the firm performance.
- Fourth, the goal is to determine the presence of a system of complementary to the main payment privileges and bonuses, which will allow to judge whether the activity of the executive directors can be stimulated more complexly, which is a world trend in the good CG practice.
- Last, an important characteristic of the evaluation of corporate boards concerns the relation executive – non-executive directors, and that is why the study tries to answer the question “Is there sufficiently strong interest in the independent directors to act effectively and really independently?”

These main points of next analysis are added by an attempt to see what is the practice concerning the level of compensation and whether there is an attempt to improve the qualification of the directors.

Concerning the evaluation of the activity of the governance bodies as a whole, the results are as follows – 88.57% of the whole sample state that the evaluation is done only at the Annual Meeting of Shareholders. Only 2% state that the evaluation is done only when mandate of the relevant boards expires, but 9.5% state that there is no practice of direct evaluation of the boards, which means that the only evaluation is indirect through firing or ending the term of somebody.

To complete the picture, we set a second section in the study, where we elaborated the question only for the executive directors and we were interested whether they report regularly their activity for the period to the Board of Directors, respectively the Supervisory Board. The idea was to see, whether there is some stricter form of control besides the mandatory report to GSM. Of all companies in the sample 75% stated that there is such a form, which is very encouraging practice. Another 7% stated that the control organ monitors few indicators of the activity of the firm (like volume of sales) and based on them evaluates the activity of the executive directors.

Only in 18% of the cases there is no such practice or they state that the only control is through GSM. The number is not so high but we should have in mind that the control performed through GSM is quite formal; at these meetings, the majority dominates, which usually choose the executive directors and know their activity through information channels, different from the official report.

That is precisely, why the European-recommended-practice includes alternative forms. Even when they are indirect, like monitoring some benchmark numbers, they are still more effective than the total formal report, since they make some obligatory criteria explicit. And, the evaluation of the activity of the directors can be done even without a special report from the simple comparison of the result with the benchmark.

The picture of our study is enriched by a self-evaluation, which our respondents give for the activity of their board. It is a positive one – the excellent evaluations are almost 50% and another 44% give a good mark, which is not surprising and those answers could be dubbed as prejudiced, or even moderate (having in mind that they are not 100% excellent), but it cannot be base of a learned conclusion.

For the third point of analysis, we got the following results – over 34% of the respondents confirmed presence of a relation between the effectiveness of the firm and the size of both elements of the compensation for the top managers (the main one and the additional bonuses). Another 23% state that the main one is fixed and that the bonuses depend on the results. Here come the sobering ones – 42.4% state that their firm follows a policy of fixed payment. The last result is really quite scandalous one, since it speaks of a system, where the considerably strict control over the executive directors, stated above, does not lead to any sanctions for them.

Concerning the bonuses, the results are confirmed to great extent. Besides the 27% of the boards without any bonuses, another 44% – have only monetary bonuses, which after all is nothing else but paying part of the salary in another form (most often tax deduct), but it is far from the world best practices in the area of the corporate control and governance.

Only 1% of the board-members receive corporate securities for their good work in the firm; 5% practice other benefits and privileges, like payment of the housing rentals, education, etc. A little surprising, and perhaps, encouraging, 23% state that they practice giving a mix of bonuses, different in different situations. However, it is difficult, to see a break in the traditional model of rewarding in this statistics.

The last essential result of this aspect of our study concerns the relation executive – non-executive director regarding the level of payment. The goal of this recourse is to know whether and how the firm differentiates its attitude regarding its independent directors. The world practice strives to eliminate the existing differences and to impose an equal treatment of both groups of directors. In our cases only 30% of the firms perform a policy of eliminating the differences, and another 25% think that this difference should not exceed by more than 30% the average payment of the non-

executive directors. Again, the discouraging 46% state an unequal treating of groups of directors.

The last issue, which is rather an additional brush stroke, concerns some idea of the real level of remuneration of the board-members in our sample. It is interesting that we got plausible answers, though not statistically significant. Except the normal 54%, who “have no right” to give such answers, 28% pointed out an average firm salary multiplied three times, 13% – between 1 and 3 times, and only 5% – 5 and more than 5 times; in one case it is explicitly stated that it concerns only executive directors and that the difference between them and the others is more than five times. Actually, the column “Other”, quite surprisingly, contains the detailed answers from the above, which show an important information for different levels of remuneration, but in their majority they are not very high compared with the other specialists and qualified personnel of the firm.

13. Conclusions

As a whole, the changes occurring in the Bulgarian corporate boards in the process of accession to the EU give opportunity to summarize their degree of enhancement and of adjustment to their European partners.

1. Concerning the tier-structure of governance: Bulgarian boards use both known world systems in a unique mix, with domination of the American one, but with a lot of involvement of the German one. At the same time, there is no clear distinguishing principle when and why each of them is being applied. This leads to compromises in the system as a whole. The preferences to one-tier system in Bulgaria because of its lower costs bring risks for the independence of the non-executive directors.
2. Concerning the size, Bulgarian boards, probably because of striving the lower costs, are close to the bottom prescribed limit, which also distance them from their European partners, since it lowers the level of transparency in their work. Additionally, it is an obstacle to the development of specialization among the members of the boards and to establishing permanent committees at them.
3. The educational and qualification requirements follow strictly the legal base, i.e. they are again at minimum standard level, i.e. there are no specific obstacles to occupying positions except criminal past or previous membership in bankrupted firm, and only for certain term. Probably it is the reason why we can still see cases portrayed by media of board-members at teenaged age, with vision rather for show business than for corporate governance. However, as stated above, the world practice rarely impose mandatory norms on this issue and all depends rather on the maturity of the firm.
4. Although many of the members of the Bulgarian CB are “complementary connected” [“related”] either with the firm they govern, or with other related firms, we can say that they not differ much from the European norms; Bulgarian CB

follow the legally imposed norms and we cannot say this “connectedness” restrains their objective governance. At the same time, we should not forget that each “complementary relation” has risks and often create conflicts of interests.

5. The number of independent members of the Bulgarian boards is very similar to the European norms. There is an improvement also concerning our previous study and this is quite encouraging result. At the same time, the issue of the quality of this independency is open – there are not enough guarantees whether the members can pass independent decisions and whether they are sufficiently protected in this case.
6. The emerging conflicts of interests in Bulgaria, though already placed in the agenda, are yet not enough dealt with and rarely the corporate boards have strict rules and procedures for solving them.
7. Quite substantial problem of the Bulgarian corporate boards is their functioning. Although their functions have diversified significantly in the process of accession to EU, the classic functions of strategic supervision and control, audit, planning, etc. are still overwhelming. Only few of them consider sufficiently significant the fight for avoiding the conflicts of interests between their members and the firm as a whole. Also, only few have control over the nomination, selection and remuneration of their members, which is considered a very important contemporary characteristics. There is a lot to expect in their functionality from the Bulgarian boards.
8. The accession process has confirmed and developed the practice of the Bulgarian boards to establish their specialized sub-structures for solving certain questions. At the same time, these committees are often standard and mandatory structures dealing with the audit, planning and to a small extent work for increasing the public access and transparency in the processes of paying the top managers, its forms and level.
9. Practically the same conclusions are obtained, when we went into the details of the processes of compensation itself: predominance of traditional forms, lack of sufficient control, lack of stable binding of the firm performance with the remuneration, predomination of traditional pecuniary bonuses and almost complete rejection of the use of shares, bonds and other diversified forms of compensation, typical for the public enterprises. Also, a discriminating attitude to the independent members regarding the compensation, which can stimulate their activity, is revealed. In the same direction acts also the considerably low total level of compensation of the members of those boards, imposing this way, the idea that the main component of their incomes comes from their functioning in other quality. The latter bears moral hazard for unbiased governance of the firm in favor of all its shareholders.

To summary, the conducted detailed study of the practice and state of the Bulgarian corporate boards revealed an active and adapting behavior of Bulgarian public and close to them companies towards establishing a practice, which is better and more

responsible both for its shareholders and for the public. At the same time, we have to admit that this process is not complete yet and there are many things to desire in this direction. The adoption, in the end of 2007, of the first in Bulgarian National Corporate Governance code added a further positive influence.

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