Bulgaria opens doors for investment

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From the time Bulgaria was invited to commence negotiations on membership of the EU in December 1999, many proposed changes to the legal framework for doing business in Bulgaria have been brought forward in the legislative programme. Already, since 1989, Parliament has passed numerous statutes and has incorporated them into a serviceable legal basis upon which to respond to the fast developing processes of democratisation and the establishment of a market economy.

The country achieved monetary stability following the introduction of a currency board in 1997 (through enforcement of the necessary amendments to the Banks Act and other legislation), and this pegged the Bulgarian lev (BGL) to the deutschmark (DM) and chalkeed up notable achievements in its efforts to decrease the level of the shadow economy, and to improve tax collection and transparency in the investment process.

The present article will focus on the legal framework of foreign investment. One of the ways of investing in Bulgaria that has been most encouraged has been privatisation, which started in 1992 and is well under way. The transformation of state owned and municipal enterprises attracted many foreign investors and offered them a new, often-changing and sometimes contradictory legal framework, which is dealt with in the second part of this article. Also examined below are the investment opportunities created by the developing local stock exchange market and the taxation issues that are an inseparable part of the investment process.

However, the legal instruments establishing fundamental principles are the most important consideration.

Common legal basis

The Constitution of the Republic of Bulgaria (promuligated in the State Gazette No. 56, 13 July 1991) is a supreme law that, with the international treaties, is ratified and promulgated by Parliament. It proclaims in art. 19 that:

- the economy of the Republic of Bulgaria shall be based on free economic initiative;
- the state shall establish and guarantee equal legal conditions for economic activity to all citizens and corporate entities by preventing any abuse of a monopoly status and unfair competition, and by protecting consumers; and
- all investments and economic activity by Bulgarian and foreign persons and corporate entities shall enjoy the protection of the law.
Foreign Investment Act

The Foreign Investment Act (promulgated in the State Gazette No. 97, 24 October 1997), which develops the principle expressed in art. 9 of the Constitution, is of primary importance. Its main aim is to regulate terms and procedures giving security to foreign investments, as well as those implementing priority investment projects. Section 2 of the act sets out the principle of equality of rights for both foreign and local persons. It defines the term 'foreign person' by means of two general principles – citizenship and permanent residence. A foreign person will be considered to be any juristic person not registered within the Bulgarian Commercial Register or a company that is not a legal person and is registered abroad, as well as a foreign national (natural person) with a permanent residence abroad. Actually, the different legal acts dealing with this term often use different criteria for defining it, which burdens others besides the foreign community in their application.

Apart from this, the act defines ‘investment’ in art. 12 as, for example:

- investments in shares and stakes in local commercial companies;
- ownership rights over buildings, enterprises or parts thereof;
- securities, including bonds; and
- rights arising from concessions contracts, intellectual property and credit agreements with a minimum term of 12 months, and similar contracts.

The Foreign Investment Agency – a state authority created under a particular legal act – is entitled to coordinate the activities of state institutions in the investment field and to encourage investment by providing the necessary information. The act points out that a foreign person has the right to transfer/buy foreign currency in Bulgaria and have it transferred abroad after submission of a certificate for taxes paid, provided that the transferred income is generated through an investment or through the proceeds from the sale of investment assets, etc.

However, the Foreign Investment Act cannot be properly applied without reference to the legal instruments discussed below.

Commercial Act

The Commercial Act (promulgated in the State Gazette No. 48, 18 June 1991) regulates commercial relationships arising from ordinary commercial activity. It defines which person (no matter whether local or foreign) is to be regarded as a merchant and lists the types of merchants – sole proprietor, general partnership, limited partnership, limited liability company, joint stock company and partnership limited by shares.

Public limited companies are subject to the Public Offering of Securities Act, which is considered below. The main corporate entities that foreigners and local persons establish in order to conform with the Commercial Act are joint stock companies and limited liability companies, where the liability of the shareholders is, in practice, limited to the amount of their share. Through privatization measures, state owned and municipal enterprises were transformed into such companies, allowing the state to exercise ownership rights over them.

The Commercial Act also deals with matters concerning the ordinary running of a business, the transformation of companies, mergers and acquisitions, amalgamations and liquidation. It provides general and specific rules for conducting the different types of ordinary commercial transaction. One of the four big sections of the act deals thoroughly with bankruptcy procedures. Basically, the legal fundamentals provided by the Commercial Act are now being synchronized with European legislation (the amendments enforced in 2000 concern to a great extent limited liability and joint stock companies as well as bankruptcy procedure). Further amendments are to be enforced in order to fulfil the requirements imposed by European directives.

Concession Act

The Concession Act of 5 October 1995 is another part of the supporting legal framework for investment and represents a prolongation of the state principle of granting concessions to private persons, as established by art. 18 of the Constitution. The concession is explained in the act as:

- a grant of a specific right to the use of those items of public property over which the state exercises rights in pursuance of art. 18; or
- a grant of authorisation for activities over which the state has a legal monopoly,

and allows a kind of investment which can be made by both local and foreign persons, who are incorporated and registered as merchants under the Bulgarian legal system. The act sets out procedures for the grant of a concession. These are via biddings or auctions, in which the major role in the decision-making process is granted to a commission nominated by the prime minister. Its decision has to be approved by the Council of Ministers.

Ownership Act

The Ownership Act (promulgated in the State Gazette No. 92, 16 November 1951), is considered here with
regard to investments in the real estate market. According to art. 22, para. 1 of the Constitution no foreign natural person or foreign juridical person may acquire ownership over land except through legal inheritance (intestacy). Ownership thus acquired should be duly transferred within three years following the inheritance. Article 29 of the Ownership Act points out this prohibition and provides that these persons can acquire ownership over buildings, and other limited ownership rights. Despite this obstacle, the act was amended in 2000 so as to facilitate the purchase of real estate by foreigners. The previous ‘authorisation’ regime insisted that the permission granted by the Minister of Finance as a part of the purchase should be replaced with a new one (in compliance with the new Foreign Exchange Act) according to which foreigners can freely acquire limited ownership rights. Obviously, one of the biggest challenges that the Bulgarian legislator faces today is the eventual amendment of the Constitution to lift the prohibition.

**Foreign Exchange Act**

One more step in promoting the investment process for both locals and foreigners was the enactment of the Foreign Exchange Act in 1999/2000 which repealed the old and inefficient Transactions with Foreign Exchange and Foreign Exchange Control Act. The act deals mainly with transactions and payments between local and foreign persons, cross-border transfers, remittances and payments, export and import of Bulgarian currency and foreign exchange in cash, enforcement of an adequate currency and foreign exchange control.

This act changes the old restrictive and ‘authorisation’ system that used to be applied to these transactions and replaces it with a new ‘registration’ system, complying with the ‘freedom of concluding transactions’. In other words, the subjects of the act have to enter foreign exchange transactions in the special registers kept by the Ministry of Finance or the Bulgarian National Bank, unless otherwise provided for by the law.

In accordance with the whole process of democratisation of foreign exchange transactions, art. 10 of the Obligations and Contracts Act (1951), prohibiting the settlement of payments in currency other than the BGL, was repealed this year. This was possible owing to measures taken under the currency board regime, which lowered the inflation rate. Currently, local merchants can agree upon monetary obligations in foreign currency, but due payments have to be executed in BGL.

**Banks Act**

Other relevant legal instruments include the Banks Act (promulgated in the *State Gazette* No. 52, 1 July 1997), which regulates financial relationships involved in the investment process and provides opportunity for a foreign banking institution to operate on the Bulgarian market by establishing a branch under Bulgarian legislation.

**Further key statutes**

Freedom for foreign persons to conduct insurance business is provided for by the Insurance Act, in force from the beginning of 1998. The Consumer Protection and Trade Rules, enforced in 1999, the Law on Protection of Competition dating from 1998, the Law on Mortgage Debentures, enacted in 2000, the Law on Co-operatives, and many others, are to be taken into account in considering the legal basis of investment in Bulgaria.

**Law on privatisation and stock exchange trading**

The Transformation and Privatisation of State-Owned and Municipal-Owned Enterprises Act (published in the *State Gazette* No. 38, 8 May 1992, and regularly amended) sets out basic principles for the transformation of the old state owned and municipal undertakings into companies under the Commercial Act, and for the process of privatisation of these transformed enterprises.

All Bulgarian and foreign natural persons and legal entities are entitled to equal rights in participating in the purchase of entities being privatised, unless otherwise provided for by the act for social or economic reasons. The act lists the entities for privatisation, e.g.:

- the above-mentioned transformed companies;
- those that are not transformed but are registered under the abrogated Decree 56 for economic activity and that are to be sold as undertakings (Commercial Act, art. 15); and
- autonomous parts of enterprises that are independent with regard to their functions and locations.

The act also prescribes the privatisation institutions:

- the Privatisation Agency;
- ministers and institutions exercising, by the Council of Ministers’ decision, the state’s rights of ownership over the relevant enterprises; and
- the municipal councils and the Council of Ministers, which are responsible for the enterprises included in so-called mass privatisation.

These bodies have freedom within the yearly privatisation programme approved by the National Assembly to take decisions on privatising sites at their own discretion, although guided by social and state interest. The act lists several forms of privatisation transactions:
sale;
- leasing with a buy-out clause;
- management with a buy-out clause; and
- sale under suspending and cutting-off conditions
  (investment plan, keeping jobs, ecological
  management, etc.).

Consequently, the procedures for concluding a
privatisation deal may produce various types of
negotiations with a potential investor: open auction,
open tender, public offer of stocks and shares offered
(sale through a stock exchange or investment
mediator). The particular requirements for foreign
investors are not many and are mostly connected with
the regime for land acquisition by foreign persons.
The Public Offering of Securities Act, adopted in
December 1999, has the aim of regulating:
- the public offering of and trade in securities;
- the activities of regulated securities markets;
- the Central Depository;
- investment intermediaries;
- investment companies;
- management companies;
- the conditions for carrying out such activities; and
- state control over them executed by the State
  Securities Commission.

It provides investors with necessary protection, and
sets out the prerequisites for development of a
transparent and efficient capital market. As a
consequence, the Bulgarian Stock Exchange in Sofia
has adopted the Rules and Regulations of BSE-Sofia,
which establish the principles governing overall
operations on the Stock Exchange. The relevant
legislation in this field is found mainly in the
Commercial Act, Privatisation Funds Act, Foreign
Investment Act and the Transformation and
Privatisation of State-Owned and Municipal-Owned
Enterprises Act.

**Taxation, customs, excise duties and social
securities**

Tax legislation regarding investment is found mainly
in the double-taxation treaties concluded between
Bulgaria and over 30 other countries, plus several
legal acts.

**Corporate Income Tax Act**

The Corporate Income Tax Act (promulgated in the
State Gazette No. 115, 5 December 1997) regulates
the taxation of income and profits earned by local and
foreign legal entities, including budget organisations,
as well as local and foreign companies, which are not
legal entities. The local companies and entities are
liable for corporate income tax on their world-wide
profits, and the foreign legal persons (regardless of
whether they are legal entities or not) are subject to

taxation with profit tax and municipal tax on the
incomes originating from their business activity in
Bulgaria, including that conducted through a
permanent establishment.

The act deals with the taxable base, the prevention of
tax evasion, etc. The corporate income tax that is
collected for the state budget amounts to 25 per cent
over the taxable base and the one that is in favour of
the municipalities' budget is ten per cent. Companies
whose annual taxation base is less than a certain level
(50m levs, i.e. the equivalent of DM 50m) are liable
for 20 per cent corporate tax only. Various categories
of income are exempted. The foreign source income
may obtain relief for tax paid on that income by
means of credit against Bulgarian tax due, provided
that Bulgaria has signed a double tax treaty with the
country in question. Dividends paid by a company are
subject to a 15 per cent withholding tax.

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**Value Added Tax Act**

The Value Added Tax Act, which came into force as
of 1 January 1999, provides that all persons
conducting business in Bulgaria and having a turnover
exceeding BGL 70,000 for the last 12 months are
subject to VAT registration. Imported goods are
subject to a 20 per cent tax levied on the amount of
the goods and services provided (including the customs and the excise duties paid); exported goods are levied with zero rate. There are of course several goods and services that are exempt from VAT. A decrease in the tax rate is being considered at this stage. Other relevant provisions are covered by the Customs Act, the Excises Act, the Mandatory Social Insurance Code, the Labour Code and the Law on Mandatory Health Insurance.

Conclusion
The legal fundamentals are already established in a way to permit the promotion of foreign investment in the Bulgarian market. The present legal system is being further improved and developed in pursuance of the two general trends which characterise present legislation: the establishment of new, modern legal principles following the democratisation of the economic and social life of the country, and the harmonisation process in preparation for membership of the EU.

POLAND
New Code brings commercial law up to modern market speed
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The Commercial Code of 1934 (as amended) ('the CC'), the respected hallmark of Poland's pre-war legislation, was not abrogated during the Communist period. It is now to be replaced by the Commercial Companies Code ('the Code') on 1 January 2001. The legislation was passed by the Sejm, the lower house of Parliament, on 15 September and awaits signature by the President.

The CC has long been due for an overhaul in order to meet modern commercial conditions, but for practical reasons it was decided to draw up a new code. It has almost twice as many articles and sub-paragraphs as the CC. The legislation introduces significant changes to the present provisions on limited liability and joint stock companies (the two company types allowed for foreign investors under the CC).

New types of companies
The greatest number of changes and new requirements have been made in the case of joint stock companies. The Code provides for two new types of companies which are allowed only to Polish citizens:
(1) partnership companies for persons authorised to practise certain professions; and
(2) limited joint stock companies to facilitate the expansion of small and medium-sized businesses.

In addition to expanding the legal provisions necessary for modern market conditions, the Code also adjusts Polish company law to EU standards, as required by the Europe Agreement. Together with the new Law on Economic Activity (Official Journal of Laws of 1999, No. 101, Item 1178) and an amended Civil Code, the new year will see equal legal treatment of both businesses and companies.

Initial capital requirements increased
To increase the security of commercial transactions it will no longer be possible to establish a limited liability company with a minimum initial share capital of PLN 4,000 (about US$880), with each share at a minimum of PLN 50, as is presently allowed by the CC. The minimum initial capital under the new Code is much higher at PLN 50,000 (about US$11,111) with a minimum of PLN 500 per share. Once the Code comes into force limited liability companies registered under the CC will have a two-phase period for meeting the new capital requirements:
(1) in three years to a minimum of PLN 25,000 with the value of each share to PLN 500; and
(2) within five years to a minimum of PLN 50,000.

The minimum initial joint stock company capital of PLN 100,000 will be increased to PLN 500,000 under the Code, with a similar two-phase schedule for meeting the new capital requirements:
(1) in three years to a minimum of PLN 250,000; and
(2) in five years to a minimum of PLN 500,000.

Two new methods of increasing capital
Under the Code it will be possible to increase initial capital by two new methods:

(1) In the case of a joint stock company, the articles of association may give the management board power to increase initial capital (the final capital amount) for a maximum period of three years. This would avoid any blockage by a general meeting resolution against such an increase. However, the final amount thus increased cannot exceed three quarters of the initial capital on the day the authorisation was granted to the management board by the articles of association. This increase cannot cover authorisation for an increase of capital from the company's own sources.

(2) The general meeting may pass a resolution allowing an increase in initial capital on condition that the shares are issued to:
(a) owners of convertible bonds or bonds with priority rights;
(b) employees; and
(c) members of the management or supervisory boards.

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