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REDUCING BARRIERS IN THE BULGARIAN SECURITIES MARKET

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Introduction

One basic way of savings corresponds with the securities or equities component of capital markets. Stock markets are the most prominent example of this way of saving.¹ There is increasing recognition among policymakers of the beneficial role of equity markets in mobilising and allocating resources in support of economic growth and development.

Investors' decisions to participate in the securities markets are critical to the success of the economy. The decision to participate is predicated on the perception, and reality, of fair treatment of investors,² integrity of markets. The system will be working to raise capital and provide a wide range of investment opportunities, if allowing competitive forces to shape market structure within a fair regulatory field. However, thin markets and a lack of information make market structure segmented, heterogeneous. These barriers impede trading activities and diminish stability. Unstable³ securities markets have a large adverse impact on economic activity.

The ultimate goal of regulations of the securities market is investor protection. Effective disclosure is the means. Transparency helps to link dispersed markets and improve price discovery. Both, disclosure and transparency support the ability of customers to make informed decisions based on the maximum information available. Such markets can not efficiently allocate funds to high-return projects. The accumulation of capital is fundamental to the growth process. Countries with high growth rates devote a higher proportion of their GDP to investment and - perhaps more important- have developed domestic capital markets. The lack of information makes markets thin and unefficient, thus an obstacle to economic growth. Regulations are aimed at assuring information on securities and issuers, on markets and prices.

Given the limited availability of domestic finance in Bulgaria relative to its developmental needs, and the lack of foreign sources of funding, equity markets could play an important role in providing capital to productive sectors as well as facilitating the process of privatisation. Private sector can be financed efficiently, if equity market is vital and stable, based on modern and effective information, on prohibition by law of fraud, insider trading and manipulations. By discouraging investors for entering securities markets the lack of proper regulations, turns at a given moment to strong barrier to private sector development as an engine of stable and sustainable economic growth. On the other hand, regulatory structure is not to be directed in hampering innovation and competitiveness. Clear regulatory purposes have to be identified.

One of the difficult problems in securities regulations is understanding, and helping the public, to understand, that regulation is necessary. Since securities are a distinct type of commodity, they must be subject to specific regulations. To effectively develop an appropriate legal and regulatory framework, laws and regulations are needed, which relate directly to the unique characteristics of these financial instruments.

The paper begins with a review to identify several nonspecific laws impeding efficient functioning of the securities market.⁴ Then the paper identifies the basic issues on which the most recent initiatives to draft securities and stock exchange regulations for Bulgaria were addressed, and comments on how the emerging securities industry in Bulgaria is regulated by law. The paper focuses on three separate spheres:

- objects of regulations;
- regulatory authorities; and
- types of regulations.

The period of no specific regulations

Until recently the Bulgarian legal system offered the following laws and supplementary regulations which governed the securities market:

Laws:

-Commercial Act (covering the establishment of companies; issuance of shares, bonds; but not transactions in securities. The third part of the Commercial Act which shall regulate the securities has not yet been passed);

-Law on Obligations and Contracts (covering the contract on intermediation activities);

-Law on Banks and Banking Activities (covering banking whole-sale and retail-transactions in securities);

-Law on Assets in Foreign Exchange and on Foreign Exchange Control (covering the export of Bulgarian securities by foreign persons);

-Law on Bookkeeping (covering some disclosure requirements through the obligation of joint-stock companies to publish their annual balance sheets until the end of the fiscal year).

-Law on Foreign Investments (covering the direct and portfolio investments by foreign persons)

Regulations:

-Decree N 56/1988 and the Regulation on its implementation (in which taxation of returns on securities are regulated);

-Bulgarian National Bank Ordinance N2/1993 (on licensing financial non-banking institutions including when trading in securities⁵⁾)

-Council of Ministers Ordinance N 4/ 1994 on Export and Import of Foreign Exchange Assets (on the rules and procedures of export or import of foreign exchange assets by local and foreign persons)

-Ministry of Finance Ordinance N 3/1990 on printing requirements when issuing securities.

These laws and regulations covered only partially some issues connected with securities but did not create the specific legal and regulatory framework needed for trading in securities. Within this legal framework the investor's protection was not assured both on the primary and the secondary market. Rather the final buyers and sellers of securities participated in a risky game.

Regulatory authorities

For some period of time the authorities made little effort to discover the linkage between securities markets, the legal system, taxation and property rights. Appropriate action requires more than ignoring the creation of the infrastructure of the capital market.

Primary issues or secondary trading were under the regulation of two main state institutions: the Ministry of Finance and the Bulgarian National Bank. Their authorities, responsibilities, however differ substantially from those of a Securities and Exchange Commission.

a/ Ministry of Finance

- Corporations were not required to file prospectuses with the Ministry.
- The Ministry had specific printing requirements for the securities to be issued.

- Failure of the court to require the registration of firms made it difficult for the Ministry to check the identity of the issuers.
- Additionally they might require an application from the issuer.

b/ Bulgarian National Bank

- Issuing securities was not considered as a banking transaction carried out as a business. Thus, no permit by the BNB was needed for the issuance.
- Under the Bulgarian law all securities issued should be denominated in national currency. If the issue involves foreign currency (through clauses of denomination, effective payments etc.) a special permit is needed.

The lack of specific regulations was not considered as an obstacle for issuing or trading in securities. Securities have become an important form of private property. Since the autumn of 1991 a process of creating stock exchanges occurred. In comparison to other Central and East European countries the government was not involved in this process. In 1993 the drafting of special laws covering securities issuing and trading, stock exchanges, market professionals and investment companies was acknowledged as necessary.

The drafting process

In drafting the securities markets and stock exchange regulations, Bulgaria applied a diversified approach. Preliminary investigations, studies and initiatives have been made by self-regulatory organisations⁶, the government, and by a private think-tank⁷. In April 1994, three draft laws were proposed and served as a basis on which the Securities Regulation Working Group (SRWG)⁸ at the Ministry of Justice started drafting the Securities and Investment Companies Law and the Stock Exchange Law for Bulgaria:

- Draft Stock Exchange Code (by Prof. Haupt, Drs. Dreiling and Schultze);
- Draft Securities Act (by Prof. Wymeersch)⁹; and
- Draft Securities Law (by Walter Stahr)¹⁰.

Prof. Haupt and Prof. Wymeersch addressed the basic issues in two separate laws. Walter Stahr concentrated on the major issues in one law.

For the benefit of the SRWG, several comments on these drafts have been made¹¹. At a conference, officials from the Bulgarian Government, the Bulgarian National Bank, the Privatisation Agency, and the stock exchanges discussed with the authors and other foreign experts the basic issues the SRWG needed to include in the drafts.

In mid-June 1994, the Securities Draft Law was distributed to institutions for comments. In early 1995, the Ministry of Justice merged the two drafts. In February 1995, the Council of Ministers adopted the Draft Securities, Stock Exchanges, and Investment Companies Law (SSEICL) and submitted it to the Parliament.

Additionally, another Stock Exchange Draft has been presented in the Economic Commission of the Parliament. The Commission decided to merge both drafts. Market professionals, self-regulatory organisations, and independent experts have been invited to take part in the discussions. At the end of June 1995, the (SSEICL) was passed by the Parliament and on July 18, 1995 the law was published and enforced.

In drafting the SSEICL several basic criteria have been met:

- collecting feedback from market participants and market structures through discussing all the versions before submitting the draft to the Council of Ministers;

- reviewing and adjusting basic issues with directives of the European Union such as the conditions for admission of securities to official stock exchange listing; the distribution of listing particulars; the information to be published of a regular basis by companies, the shares of which have been admitted to official stock exchange listing; on regulations on insider trading etc.¹²

Basic issues of the law

The SSEICL regulates the issuing of securities, securities transactions, the establishment of stock exchanges, investment intermediaries and investment companies, and the state control over such activities. In this paper the attention is focused on two basic issues: the treatment of the term securities and the role of the Securities and Exchange Commission.

The term “securities”

Securities have no intrinsic value in themselves. They are issued but not produced in the common meaning of this activity. This is one of their main differences in comparison to other commodities. In this context, if they are not subject to special regulation, they can be issued on the basis of misleading information. They can also be traded on unfair or non-competitive prices. That is why legal regulations are needed to ultimately protect the consumer against dangerous practices. The issue is of great practical importance, because the definition of the term determines whether a transaction involves a security or not. The juridical term of securities actually controls the scope of the SSEICL.

This law applies to a part of securities subject to public distribution and to secondary trading by all securities professionals. It does not cover money market instruments and commercial paper.

The law includes a definition of securities directed to capital instruments. These securities have one common feature: investors in them expect a form of earnings. Under the law the term “securities” covers documents and rights with two specific characteristics.

The first includes the documents or rights to be transferable. In the meaning of the law there is one reason for this offering. This is for transferring the ownership of them for some kind of compensation: for payment on the basis of a buy/ sell transaction or through a barter transaction. The law does not apply to grants of securities.

The second characteristic pertains to the documents or rights to be publicly offered. Under the SSEICL, “public” securities are offered in two ways. First, documents or rights may be offered to at least 50 identified persons. According to the second, the offer shall be directed to an unidentified group of people. This means that the information about the offer shall be made available, for example, to the general public. The announcement of the offer shall cover the subject of the contract aimed to be reached by the offer.

The term “securities” covers both the markets for distribution of securities into public hands and the markets for continuous trading in outstanding securities.

The definition of securities follows two basic approaches. Under the first, the definition includes by name or description documents or rights which are publicly

offered. Some documents, such as stocks and bonds, are quite well standardised and the name alone carries a well settled meaning. The SSEICL defines securities as transferable documents and rights such as stocks and bonds. In addition, it opens the door for new instruments. Novel and uncommon instruments, however, shall be defined in case there is another document or right connected only with stocks and bonds.

In the second approach, documents of more variable character are necessarily designated by more descriptive terms. On this basis, investment contracts are considered as securities as well, when they are offered publicly. It is difficult to determine whether an investment in a money raising scheme has to be considered as a type of security.

The term "investment contract" is defined by the SSEICL as "a contract in written form, whereby an investor commits funds or other property rights to another person for investing them in an enterprise against the promise for receiving earnings." Giving the creativity of those who seek other people's money, the legislation is aimed at providing a definition which controls fraudulent practices. Examination of the parts of the definition however, illustrates that the categorisation of basic elements of the term "investment contract" are imprecise. (It is another question whether or not it is possible to reach a sufficient grade of precision at all.)

The term "investment contract" is an abstraction, over which long debates are going on. The debate has expanded to include new inquiries concerning the context of an investment contract. All of this has led to a body of law that is far from settled.¹³ Nevertheless, the experience has shown that there are some basic elements which need to be included in the definition: investment of money; a common enterprise; expectation of profits solely from the efforts of others.

According to the SSEICL the definition does not involve some of these important elements. This is the necessary specification that the investment of money is in a common enterprise and with profits to come "solely from the efforts of others (of the promoter or a third party)".¹⁴

This part of the definition of securities is a means to protect investors. It can be applied to the issuance of the "many types of instruments than in our commercial world fall within the ordinary concept of a security."¹⁵

The inclusion of the investment contract as a term in the law can have a disciplinary effects on potential issuers. This effect is very important for the present stage of Bulgarian financial market developments. One can even say that the law was passed too late in a period when pyramid promotion enterprises made small investors suffer so much.¹⁶ They offered the opportunity to investors to contribute money and to share in the profits in the form of promised dividends or fixed income. The promoters, however, did not use to manage, control or operate the enterprise as promised. They collected money from the next investors to pay interest to previous investors. At some point these respondents could not meet their promises.

The question is whether such enterprises will be within the ambit of the term security, as employed by the SSEICL; whether they involve a sale of a security and what will happen when the investors are disappointed by returns. The definition will be a polemical one as is the question of whether a pyramid arrangement falls within the definition of security.

The Securities and Exchange Commission (SEC)

Under the Securities, Stock Exchanges and Investment Companies Law (SSEICL) one governmental regulatory authority has to be created - the Securities and Exchange Commission (SEC). The Commission is designed to supervise the primary and secondary markets in securities and the professionals on them. The agency controls:

- the issuance and transactions in securities,
- the establishment and functioning of stock exchanges, of investment intermediaries and of investment companies.

The Commission is entitled to grant, deny or suspend licenses, to issue confirmations, to examine the activities of investment intermediaries and exercise control on them, to impose administrative sanctions for the violation of the provisions of the law. These activities of the Commission have to be directed to protect investors and to promote the development of securities markets.

The Commission had to be constituted a month after the enforcement of the Law. Unfortunately, two months passed after the deadline and the Commission has still not been constituted.

Under the Law the SEC is a juridical agency of the government. It is composed of a chairman, one deputy chairman and 5 members. The Commission is authorised to employ a professional staff in the form of an administrative office with its own internal rules as to the conduct of its activities under the law. The Commission has its own budget. (It has to be partially financed by the state budget and partially by fees).

The Commission is not an independent body in the sense of the US Securities and Exchange Commission. This must be considered when analysing its subordination to other state bodies and in view of the scope of its rulemaking authority.

The Commission is responsible to the Government instead of to the Parliament. The members of the Commission are appointed by the Council of Ministers with the advice and consent of the Minister of Finance for 5-year terms. They can be discharged by the Council of Ministers prior to the end of the five-year period on the proposal of the Minister of Finance

- in case of violation of the SSEICL,
- in case of committing a deliberate offence,
- in case of incapability of fulfilment of their duties.

The Commission is engaged in rulemaking. The specific procedure under the SSEICL is that the Commission is preparing the secondary laws (ordinances) connected with and prescribed by the SSEICL. The agency may not by law directly issue rules to implement specific provisions of the law. It only works out declaratory rulings as to the applicability of the SSEICL and submits them for approval. The procedure requires the drafts prepared by the Commission to be discussed and promulgated by the Council of Ministers. This procedure does not allow the agency to finalise the rulemaking process. There are other more effective ways which could have been applied to limit the rulemaking authority of the Commission. This could have been achieved, for example, through not giving it the possibility of issuing rules covered by other provisions of the Law.

The Commission is the main but not the only regulatory body of the securities market. Because of the universal character of commercial banks in Bulgaria, the Commission shares its licensing and supervisory authorities with the Supervisory Department of the Bulgarian National Bank as regards the securities trading activities of commercial banks on their own account or on the account of others.

The SEC is not obliged to report to the Parliament, in contrast to the Supervisory Department, which as part of the structure of BNB, is required to submit to the Parliament annual reports as to its activities and the development of the capital market. This means there is a different juridical approach as to the responsibilities of

similar supervisory bodies. In this context the SEC is more “independent“ than the similar authority which supervises financial institutions that conduct banking transactions as their business.

This means the Commission’s activities are not very transparent to legislators, and also means the rulemaking authority of the Commission can be modified by the executive power.

According to the SSEICL the SEC has an important regulatory role in several areas of the securities market. The Commission has supervisory functions on the institutional structure of the securities market. The Commission controls the conformity of the activities of the stock exchanges, the investment intermediaries, the issuers and the investment companies under the SSEICL and the public interest.

The Commission grants and revokes licenses, issues confirmations of prospectuses, conducts investigations, requests the waiving of bank secrets from the district judge (under the Law on Banks and Credit Activities).

The SSEICL regulates both the primary sale and distribution of securities and the trading of securities on the secondary market.

The Law requires that issuers register their securities with the SEC before the securities may be offered to the general public. Issuers shall file with the Commission information describing the offering. The Commission is the only body under the Law which issues confirmations of prospectus for public offerings. The Commission does not evaluate the merits of the prospective offering; rather, it reviews the adequacy of the disclosures. The SSEICL requires that the Commission determines whether the applicant has supplied enough information to enable potential investors to take a sound, reasoned decision about the impending offering. The Commission is not liable for the correctness of the information included in the prospectus. In case of false information or if material information has not been included in the prospectus, the investor may ask the sale contract to which he is a party to be voided (except if the investor had not acted in good faith).

The Commission has broad powers governing the disclosure of information. Companies registered with the Commission must file reports with the Commission in order to keep both the agency and the investing public informed of their activities. These are annual reports, including certified balance sheets, information on the company, its activities, on members of its managing and controlling bodies, and on persons owning more than 10% of the votes. The Commission defines the additional information that registered companies must file together with their unaudited semi-annual reports. Quarterly reports have to be filed by companies in cases of issuance of debt securities. The Commission is to be immediately informed about changes in the statutes and managing bodies of the companies, and changes in their activities which can affect directly or indirectly the price of company’s securities etc. The Commission makes data of current reports publicly to ensure that information on issuers and issues is widely disclosed. In some instances, these obligations will require more vigorous oversight of issuers.

The main objectives of the Commission with respect to the secondary market are to enhance market participants to act within a fair regulatory framework. The agency’s supervisory activities on the secondary market cover the following institutions:

Investment intermediaries

Under the Law transactions in securities may be carried out as a business activity only by investment intermediaries (brokers/dealers). The Commission issues

and revokes licenses of investment intermediaries and registers them. The Commission has to be kept informed by the investment intermediaries about separating the securities they owe from the securities of their clients.

Investment companies

The Commission issues and suspends licenses of investment companies. The agency defines the minimum amount and structure of the capital and the minimum amount of liquid funds of investment companies.

Stock exchanges

It is reasonable to expect, that the broad definition of “exchange” in the Law gives the Commission the power to provide enhanced oversight not only of traditional stock exchanges but of automated or other types of entities that perform the function of an exchange. Stock exchanges act under the licensing regime of the Law.

- The Commission issues licenses for creating and for suspending the activities of stock exchanges. The Commission has to be informed when a stock exchange suspends trading on a temporary basis or permanently. An approval of the Commission is needed when a stock exchange stops trading within a period of more than 3 days.

- The stock exchanges inform the Commission about all amendments or supplementary provisions made to the stock exchange rules.

- The Commission defines the general listing requirements of stock exchanges.

Civil enforcement

The Commission provides civil enforcement of the SSEICL and of the rules (ordinances) issued by the Council of Ministers under this Law. The Commission is entitled to require documents and explanations in writing and to carry out enquiries to any persons when there is an information that they are violating the SSEICL. In carrying out its investigations

- the Commission has free access to the office premises of all physical and juridical persons subject to its supervisory power.

- The Commission is allowed to attend meetings of managing bodies of juridical persons supervised.

The Law gives the Commission wide enforcement powers for violations of any provision of the Law or of ordinances in connection with the Law. The agency has the power to apply administrative sanctions like penalties unless the action committed does not constitute a crime. For example, if a person commits or allows violation of requirements for a granted license to a stock exchange, to a broker /dealer, to stock exchange or to an investment company, the Commission has the power to revoke the licence or/and to penalise the person by fine in the amount of BGL 200 000 to BGL 1 000 000 unless the action is not considered as a crime. In case a person is dealing in securities as a business without obtaining a license under the terms and procedures of the SSEICL, the Commission will challenge those transactions violation and such persons will be penalised by the amount of BGL 500 000 to BGL 2 000 000 unless the action is not considered as a crime.

Outlook

The specific regulations towards securities issuance, trading, on market professionals and marketplaces concentrated in one legal act - the Securities, Stock

Exchanges and Investment Companies Law, provide a appropriate legal framework for the development of sound securities markets in the country.

□ The economic analyses of this legal environment could be evaluated by several criteria. From the investors' point of view, the market can be expected to offer a greater extent of protection than was previously available for several reasons:

- there are strong requirements of disclosure to be followed by issuers;
- there are tight rules on insider trading;
- there is an execution of the transaction at the best terms available;
- there are administrative and criminal penalties included in the Law.

Several expenses are connected with the registration of issuers and issues. From this point of view higher transactions costs are to be expected by issuers. This might become very important for the small business. Revisions of the rules can be expected intending to reduce compliance burdens for small businesses. The Commission will be engaged in rulemaking initiatives to assist greater amount of capital raising by small firms. Perhaps they will be subject just to antifraud prohibitions.

□ Some issues are not covered by the SSEICL. This can have consequences for the effectiveness of the remaining regulations. One of them are the linkages between the Commission and the self-regulatory organisations. Except on stock exchanges there are no provisions in the Law regulating the relationship of the Commission with other self-regulatory organisations such broker-dealers associations, clearing agencies, or an arbitration court.

In Bulgaria there are two registered market professionals' associations and an association of the stock exchanges. The SSEICL does not require such organisations to register with the Commission.

Under the SSEICL the stock exchanges are obliged to create a clearing system. It is however not necessarily for these systems to directly be registered with the SEC.

In the Law there is only one provision regarding the links between the SEC and the arbitration courts. The chairman of the Stock Exchange Arbitration Court has to be approved by the SEC. The self-regulatory organisations of any type will initiate contacts with the Commission, in case of arbitration for example, to clarify procedures for selecting and training arbitrators, to setting up more detailed rules on the authority of arbitrators, to work out interim orders during an arbitration proceeding etc.

It is therefore reasonable to expect, that self-regulatory organisations will maintain close contacts with the Commission. Simultaneously the Commission will issue regulations on the basis of recommendations by self-regulatory organisations.

□ The Privatisation Funds to be established under the Mass Privatisation scheme to start at the beginning of 1996 are bodies to be regulated by the Commission. These are not included as objects for regulation in the SSEICL. The establishment and the functions of privatisation funds are subject to specific regulations prescribed by a Privatisation Funds Law.

Basic principles covered by the Draft Privatisation Funds Law are:

- The privatisation funds shall be created as joint stock companies. For the creation of a privatisation fund a minimum capital of 70 mln BGL is required. The structure of the capital shall be 10 mln. BGL and 60 mln. investment bonds. From the moment of being licensed the privatisation fund must keep the proportion of 10 per cent capital in local currency and 70 per cent in investment bonds.

- Privatisation funds shall be licensed by the Securities and Exchange Commission¹⁷ which has not been constituted yet.
- To participate in the centralised auctions privatisation funds have to publish a prospectus on public offering of shares in exchange of investment bonds. The privatisation funds shall issue registered shares and their capital shall consist only of shares which carry equal rights. The Commission is responsible for issuing confirmations of the prospectus in case it meet the requirements of the PFL. There is a provision specifying the elements of the prospectus on initial and subsequent offerings.
- Privatisation funds will be allowed to redeem their shares after a 5-year period.
- The PFL envisages the existence of an independent custodian with which the privatisation fund signs a contract.
- The privatisation fund may choose a management company with which a management contract has to be signed. A maximum rate of annual remuneration for the management company is set up by the PFL.
- The portfolio of a privatisation fund may consist of shares of enterprises for privatisation, of shares traded on a stock exchange, and of government securities.
- The maximum investment in the securities of one issuer may not exceed 10 per cent.
- The privatisation fund may not acquire more than 34 per cent of the registered shares of a company.

In accordance with the Draft Privatisation Funds Law the SEC would have to take specific responsibilities in licensing and supervising the privatisation funds. A very important duty of the Commission would be the confirmation of the prospectus of privatisation funds on public issuance of shares against investment bonds (the Bulgarian term for vouchers). Despite of the special regulatory regime, established for privatisation funds, after a certain period the privatisation funds will have to comply with the investment companies provisions of the SSEICL.

Some issues in connection with the existing market characteristics and the law enforcement that warrant additional investigation have to be risen.

First, the establishing of a regulatory structure is not sufficient for having a good functioning equity market. It is important to know whether the regulatory policy itself can be designed on a way to encourage effective capital allocation. Something, that is crucial here is that at the time of drafting the Securities, Stock Exchanges and Investment Companies Law Bulgaria had a functioning equity market to be regulated. Nowadays, there is the market of government securities only. The equity market is relatively underdeveloped. The role of the market diminished. The depth and liquidity of the market are low. The market capitalisation in 1995 was approximately 235 million US\$. The daily turnover amounted 7100 US\$, which is a decrease compared to 1994 by more than 50%. The number of private companies with tradable shares is small.. The total turnover on all stock exchanges compared with the GDP shows a deepening of the equity market in 1993 of 0,01 per cent, an increase in 1994 to 0,1 per cent, and a slowdown of this ratio in 1995 to 0,5 per cent. This means, that the regulator has to create conditions for re-establishing of equity trading. Sufficient flexibility has to be delegated to the regulator to react appropriate to the dynamic of the market.

Second, for securities markets supervision to be effective, the unique role of the Commission must be clearly defined and understood by policy makers. Simultaneously with the activities of the Commission there are currently several government bodies in Bulgaria, which to some extent assume (or are expected by market participants to assume) responsibilities on taking decisions about the structure of the capital market. This is the case with the Ministry of Economic

Development, which is trying to duplicate functions and tasks of the Commission. For this reason, the issue as to whether to set up or not a national stock exchange, whether to have a state participation in it, is a question, which has not received an answer for over an year. The vagueness of policy makers' views puts additional uncertainty to the market and contributes for its getting thinner and thinner. The supervision must enjoy the support of government officials, and political interference must be held to a minimum.

Third, in considering the existing deepness of the equity market measured by daily number of shares traded on the existing stock exchanges, one can say that these market disappeared. The weekly information, which the public receives, concerns the stocks which are offered for trade on the over-the-counter market. Professionals on the se market are not trading on a computerised system to enable them contacting on a regular and transparent basis. This leads to the situation, that markets are fragment to the point where several prices for the same "good" occur and where price discovery is unpaired and maintenance of fair and orderly markets is difficult. The over-the- counter market is not transparent because no real-time information on prices, volumes and trades is disseminated. If existing, equity markets are unlinked in an economic sense.

Fourth, very important issue is the creation of the equity market in the context of applying the mass privatization scheme. The scheme envisages the transferring of state ownership in exchange of vouchers, which in Bulgaria are cold investment bonds. The prospect for an increase in activity along with the mass privatisation program is a source of positive expectations. The sell of large volumes of shares generated by the privatisation program is expected to beneficially effect the equity market providing an impetus for reforms to enhance its efficiency. Privatization through vouchers has been introduced later than announced. Several people suffered by ponzi schemes recently, associate the privatization funds with ponzi schemes. In addition, if the mass privatization program will be rescheduled several times, the shacked confidence of investors in the market as a whole will be lost for decades.

Conclusion

1. The adoption of the Securities Stock Exchanges and Investment Companies Law can be considered as a positive action towards clear regulations on the Bulgarian securities market. The SSEICL covers basic regulations required. Several of the provisions are in compliance with the respectively EU Directives.

2. The delay in constituting the Securities and Exchange Commission is made a very negative impact on the market: existing structures can not be registered with the Commission; the privatisation funds could not be licensed to act in the mass privatisation scheme; primary market is hampered; liquidity on the secondary market is going down.

3. Various users still find existing equities market to be inadequate for their particular needs. It is important to recognise that this is not a healthy trend. Among several other reasons, this is because of the uncertainty, that laws and regulations will be adequately enforced and that several government bodies have the same subject of their responsibilities.

4. The licensing and supervision of the investment intermediaries is under the authority of two bodies: the Bank Supervision Department of the Bulgarian National Bank and the Securities and Exchange Commission. This dualism could provide misunderstandings and erode confidence in the institutions.

5. The lack of specific provisions on the relationship between the SEC and the self-regulatory organisations will require additional efforts to regulate these links

and will decrease the effectiveness of their co-operation. These organisations are in the market every day and they could contribute to the simplification of procedures and could take responsibility for market surveillance on a broader basis.

6. A very important issue is that regulation can be influenced by political pressure. It reflects the interest of special groups, which include the entities subject to regulation. The government still indifferent behaviour towards the merging initiatives of the Bulgarian Stock Exchange creates uncertainty as to the future structure of market places and their management. In case the state participates in this or another stock exchange or set up a new one, it is reasonable to suppose, that the securities commission will hardly be able to exercise its oversight responsibilities.

7. Although there are no provisions in the SSEICL on the links of the Commission with international organisations, these contacts will be of substantial importance in keeping the market regulations in accordance with international standards.

8. Critical point of enhancing regulations is the mass privatisation program. The core stone are the licensing and supervisory activities of the Commission towards the privatization funds. Now they still have been associated with ponzi schemes of 1995. If the mass privatization program will be rescheduled several times, the shacked confidence of investors in the market as a whole will be lost for decades.

¹ Capital Markets and Development, (edited by Steve H. Hanke and Alan A. Walters), Institute for Contemporary Studies, San Francisco. p. 2

² Market 2000 - an Exemination of Current Equity Market Developments, US SEC, 1994, p. III-7

³ Long and Vittas suggest three criteria for evaluating financial regulation and structure:- stability, efficiency, and fairness (Financial Regulations. Changing the rules of the game, edited by Dimitri Vittas, EDI, Development Studies, p.4.

⁴ Actually the review does not include laws and regulations governing taxes, investment, accounting and auditing.

⁵These are regulations, concerning licensing of a domestic or foreign bank or non-bank financial institutions (exchange bureaus, brokers, financial houses) conducting transactions in the country. For brokerage and financial houses the Regulations provide additional requirement for submitting to the Bulgarian National Bank a bank quarantine.

⁶ Since the beginning of the 1990's the Bulgarian Chamber of Industry organized a series of seminars and round-table discussions with foreign experts.

⁷ Based on the project on Emerging Securities Markets the Institute for Market Economics organized a round table discussion in early June 1993, on which an assessment of the existing practice has been presented by Susan Woodward, Chief Economist at the US Securities and Exchange Commission.

⁸The SRWG included representatives of the Legal Commission at the Bulgarian Parliament, the Ministry of Justice, the Ministry of Finance, The Bulgarian National Bank, the Privatization Agency, the stock exchanges, the Institute of Market Economics (Sofia), the University of Domestic and World Economy (Sofia).

⁹Both drafts have been prepared under the World Bank Technical Assistance Loan within the World Bank's Harvard Law School Project.

¹⁰The author, an Assistant General Counsel of the US Securities and Exchange Commission, has been requested and invited by the Institute for Market Economics to draft the law on Principles proposed by the Institute.

¹¹The conference was organized by the Ministry of Justice and the Institute for Market Economics and was held in March 1994.

¹²More detailed information see in: IME Newsletter, N 4/1994

¹³Cox, Hillman and Langevoort , Securities Regulation, p. 124.

¹⁴Jennings, R. W. and Harold Marsh, Jr., Securities Regulation. Cases and Materials, fourth ed., Mineola, New York, The Foundation Press, 1977, p. 225.

¹⁵Ibid.

¹⁶There are several cases of pyramid promotion enterprises being under juridical procedures before the enforcement of the SSEICL on the basis of applications by investors deceived by such enterprises ("Pari daily news", 27.07.1995)

¹⁷The Commission is a governmental body under the Securities, Stock Exchanges and Investment Companies Law which has been passed by the Parliament in July 1995.