



# Country briefing Bulgaria



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This document has been produced as a part of the project “CSOs as equal partners in the monitoring of public finance“, which started beginning of 2016 and is implemented by a consortium of 10 organizations from 7 countries and will last for four years.

The aim of the project is to improve the transparency and accountability of policy and decision making in the area of public finances through strengthening the role and voice of NGOs in monitoring the institutions that operate in the area of public finances. In this way, the project will strengthen CSO knowledge of public finance and IFIs and improve CSO capacities for monitoring. Additionally, it will help advocate for transparency, accountability and effectiveness from public institutions in public finance. Moreover, this project will build know-how in advocating for sustainability, transparency and accountability of public finance and IFIs. This project will also increase networking and cooperation of CSOs on monitoring of public finance at regional and EU level. Lastly, it will increase the understanding of the media and wider public of the challenges in public finance and the impacts of IFIs.

Key project activities are research and monitoring, advocacy, capacity building and transfer of knowledge/practices and networking in the field of the 4 specific topics: public debt, public-private partnerships, tax justice and public infrastructure.

More information about the project can be found on <http://wings-of-hope.ba/balkan-monitoring-public-finance/> and on the Facebook Page Balkan Monitoring Public Finances



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## EXECUTIVE SUMMARY

According to the European Commission Bulgaria belongs to the group of countries characterised by excessive imbalances. Economic growth is unsatisfactory; its fundamental drivers are public procurement and European funds. However, the significant slow-down of the absorption of funds in between the two programming periods has affected adversely the country's development. Although government debt is well below the EU average, it is growing and is expected to reach almost 32% of Gross Domestic Product (GDP) by 2018<sup>1</sup> and then start to decline. The level of indebtedness of companies is a cause for concern: in 2014 corporate debt amounted to about 101% of GDP<sup>2</sup>, casting doubt over their stability. Loans to households are much lower at a rate of 23 percent.<sup>3</sup>

The failure of one of the largest Bulgarian banks in 2014 revealed weaknesses in banking supervision. The Deposit Guarantee Fund failed to cover protected deposits, which necessitated government intervention and new national debts. Meanwhile another large bank showed signs of instability, which, according to some experts, is intentionally caused. The government allocated 1.2 billion Bulgarian Lev (BGN)<sup>4</sup> in order to provide liquidity and prevent yet another bank failure in the course of just a few months. Although at present these funds have been restored, the recently completed banking stress test raises new questions about the stability of the financial institution and the banking system in general. Uncertainty is fuelled by government officials' statements from the end of 2015 that the new debt is incurred in order to strengthen the fiscal reserve, so as to be able to stabilize the banking system as needed.<sup>5</sup>

Public finances are chronically insufficient. This increases the pressure for more stringent limits to social benefits and pensions. Meanwhile, changes in legislation dealing with private pension funds were made that should guarantee at least the social pension (currently at BGN 118.14<sup>6</sup>, equal to around 60 euros).

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<sup>1</sup> Convergence programme of Republic of Bulgaria 2016-2019, table 4, page 81. <http://www.minfin.bg/document/17929:1>

<sup>2</sup> Country Report Bulgaria 2016, European Commission, Table 1.1: Key economic, financial and social indicators, p. 13 [http://ec.europa.eu/europe2020/pdf/csr2016/cr2016\\_bulgaria\\_en.pdf](http://ec.europa.eu/europe2020/pdf/csr2016/cr2016_bulgaria_en.pdf)

<sup>3</sup> Ibid

<sup>4</sup> The European Commission gave a deadline of 18 months for the return of the liquid support of First Investment Bank, source First Investment Bank <https://www.fibank.bg/bg/evropeyskata-komisiya-odobri-srok-ot-18-mesetsa-za-vrashtane-na-likvidnata-podkrepa-ot-parva-investitsionna-banka/page/782/item/862>

<sup>5</sup> Stoyanova, Menda, President of the Budget and finance committee of the National Parliament: "sometimes even a rumour is sufficient to put a bank under a liquidation crisis. The budget must be able to help in this moment if we don't want for the whole country to go bankrupt", an interview on the Bulgarian National Television, 11/12/2016, <http://imedia.bnt.bg/predavanyia/denyat-zapochva/otsenkata-za-byudzhnet-2016-12-11-2015?541199>

<sup>6</sup> National Social Security Institute <http://www.nssi.bg/newsbg/4129-osuvremenipensii2016> 01/07/2016.



However, it turns out that even this minimum pension cannot be covered. This basic reform enabled citizens to choose between putting their additional insurances in a private company or transferring their accumulated payments and continuing to be insured only with the National Social Security Institute. Debates and analysis in the National Assembly show that the real profitability of the companies for the last ten years is negative, mainly as a consequence of the global economic crisis. The state pension system is not in a good condition either, however, it is a function of economic development and the demographic structure in the country. About half of Bulgarian pensioners have incomes below the poverty line (BGN 300, equal to around 153 euros).<sup>7</sup>

For the purpose of limiting government spending a plan to reduce the number of employees in state institutions by 10% was executed in 2015. While in some places the plan was not implemented, in others the target was overachieved, at the cost of additional stress for employees forced to serve several functions at once.

**The energy system** of Bulgaria is under stress. In the course of the last 6-7 years numerous unfavourable long-term contracts were signed with electricity producers at preferential purchase prices. This has led to the serious indebtedness of the National Electricity Company<sup>8</sup>, which, in turn, is unable to keep the prices for final consumers down for too long. And while the price of electricity in Bulgaria is the lowest in the EU in absolute terms, if adjusted to Purchasing Power Parity (PPP)<sup>9</sup>, it turns out to be among the highest prices, indicating that a shock rise of the price will be detrimental for both business and households.

**Corruption and the shadow economy** are key problems in Bulgaria. Sixty-one percent of private sector managers in 2015 believe that corruption is a barrier to doing business.<sup>10</sup> According to Transparency International the Corruption Perceptions Index ranks the country at 69th place, alongside Jamaica. Estimates of the scale of the informal economy vary between 33-40%<sup>11</sup>, - among the highest levels in

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<sup>7</sup> Act № 296 of the Council of Ministers from 30.10.2015 г. For defining the poverty line for the country for 2016 (approved by State Gazette, N 86, 6.11.2015)

[https://www.mlsp.government.bg/ckfinder/userfiles/files/POSTANOVLENIE\\_296\\_na\\_MS\\_ot\\_30102015.doc](https://www.mlsp.government.bg/ckfinder/userfiles/files/POSTANOVLENIE_296_na_MS_ot_30102015.doc)

<sup>8</sup> Temporary Commission for checking of the energy state in the Republic of Bulgaria as of 31<sup>st</sup> January 2015

<http://www.parliament.bg/bg/parliamentarycommittees/members/2396/documents>

<sup>9</sup> Electricity prices for domestic consumers - bi-annual data (from 2007 onwards), Eurostat

[http://ec.europa.eu/eurostat/product?code=nrg\\_pc\\_204&language=en&mode=view](http://ec.europa.eu/eurostat/product?code=nrg_pc_204&language=en&mode=view)

<sup>10</sup> Country Report Bulgaria 2016, European Commission, p. 11

[http://ec.europa.eu/europe2020/pdf/csr2016/cr2016\\_bulgaria\\_en.pdf](http://ec.europa.eu/europe2020/pdf/csr2016/cr2016_bulgaria_en.pdf)

<sup>11</sup> Shadow economy and undeclared work [http://ec.europa.eu/europe2020/pdf/themes/07\\_shadow\\_economy.pdf](http://ec.europa.eu/europe2020/pdf/themes/07_shadow_economy.pdf); The grey economy; approaches for measuring and modeling, Ministry of Finance. <http://www.minfin.bg/document/9726:2>



the EU. To deal with the problem, in 2003 the government introduced minimum insurance thresholds - the amount below which no employer may insure an employee, with levels depending on the type of economic activity and the position of the employee. This measure was adopted in order to bar employers from officially paying the minimum wage to senior management employees, for example, while the remainder of the agreed payment is received unofficially. Unfortunately, employers' organizations are constantly trying to obstruct this measure, although the levels of minimum insurable earnings (MIE) are negotiated between unions and employers. Employers published a position, calling for a boycott of the negotiations for 2017.<sup>12</sup>

One-day employment contracts were introduced last year, again as a measure against the shadow economy, despite the resistance of one nationally representative union. It is noteworthy that in recent years the fight against the informal economy is increasingly seen as "fight against informal labour". The responsibility of the powerful party on the market, namely business, is transferred to the weaker party – the employees.

It is claimed that the most serious problem of the labour market is the mismatch between the skills sought and offered. The Ministry of Labour and Social Welfare has made attempts, financed by the EU, to plan the labour needs of business - an aim that is almost impossible to achieve. The lack of evidence puts into question the alleged imbalance between supply and demand - there is no supporting data and there is no uniform system to prove the claims of governments, employers and (mainly right-wing) experts. Nevertheless, an alarming number of young people neither study, nor work (so called NEETs - youngsters Not in Education, Employment or Training).

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<sup>12</sup> Position of the national representatives of the employers organisations regarding the cease of the negotiations for defining the minimum salaries for 2017 [http://bica-bg.org/wp-content/uploads/2016/08/Pismo\\_NPRO\\_prekrtiavane\\_pregovori\\_MOD\\_2017.pdf](http://bica-bg.org/wp-content/uploads/2016/08/Pismo_NPRO_prekrtiavane_pregovori_MOD_2017.pdf)



## INTRODUCTION

This paper provides a rough overview of the macroeconomic situation in Bulgaria. It examines the basic legal definitions related to public finances, as well as the most significant social problems. The information used is sourced from the Bulgarian legislation, financial reports (mainly from the Ministry of Finance and the Bulgarian National Bank), observations of union activists. Due to lack of publicly disclosed data concerning some parts of the current analysis, the author has sent inquiries to the Ministry of Finance that remain unanswered at the time of writing.

### Key economic and social indicators

Alternative indicators of economic development partly offset the shortcomings of the standard measures such as GDP. Unfortunately, the alternative index – the Genuine Progress Indicator (GPI), does not seem to be used in Bulgaria and is not subject to international studies, therefore, it cannot be used here. The following table lists the latest published figures for several basic social and economic indicators. The year to which they relate is listed in parentheses. The arrow indicates the direction of change from the previous reporting period; red colour indicates negative trends, green indicates positive trends.

rate of debt (2016) <sup>13</sup>	29.3 ↑
share of population living under threat of poverty (2015) <sup>14</sup>	22 ↑
people at risk of poverty or social exclusion (2015) <sup>15</sup>	41.3 % ↑
gini coefficient (2015) <sup>16</sup>	37 ↑
GDP (current prices) million euro (2015) <sup>17</sup>	44 162.3 ↑
real GDP growth per capita (2015) <sup>18</sup>	3.3% ↑
grey economy	33-40%
human development index (2014) <sup>19</sup>	0.782 ↔

<sup>13</sup> Government Debt Monthly Bulletin May 2016, Ministry of Finance <http://www.minfin.bg/document/18273:2>

<sup>14</sup> Severe material deprivation – early estimates for 2015 <http://ec.europa.eu/eurostat/documents/2995521/7231454/3-14042016-BP-EN.pdf/837178ca-f682-4923-8627-27767201816d>

<sup>15</sup> People at risk of poverty or social exclusion %

[http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=t2020\\_50&plugin=1](http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=t2020_50&plugin=1)

<sup>16</sup> Gini coefficient of equivalised disposable income - EU-SILC survey

<http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tessi190&plugin=1>

<sup>17</sup> Gross domestic product at market prices

<http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tec00001&plugin=1>

<sup>18</sup> Real GDP per capita, growth rate and totals

<http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tsdec100&plugin=1>

<sup>19</sup> Trends in the Human Development Index, 1990-2014 <http://hdr.undp.org/en/composite/trends>



NEETs (2015) <sup>20</sup>	19.3% ↓
economic activity rate (2015) <sup>21</sup>	54.1% ↔
employment rate (2015) <sup>22</sup>	49.1% ↑
unemployment rate (2015) <sup>23</sup>	9.1% ↓
working poor (2013) <sup>24</sup>	9.3 ↑

The human development index marks a nominal increase, while at the same time Bulgaria remains one the same level - 59<sup>th</sup> place, in the UN global ranking. The trend for the shadow economy cannot be shown, since the values used come from analyses conducted by different research centres in different years.

Bulgaria, in the shape of the government, is planning entry into the Eurozone and therefore trying to comply with all accession criteria. However, the public is divided on this issue and scepticism apparently prevails. Disappointment from the EU, and fears that prices of goods and services for consumers will increase, dampen popular enthusiasm for more serious EU integration. Globalization in general is increasingly losing public support. It has not brought perceptible progress to Bulgarian citizens: in the past 25 years over 2 million people have left Bulgaria. Those living in the country feel the European social model moving further away from Bulgaria's borders, instead of Bulgarians gradually fitting into it. In addition, there is strong discontent with the international financial institutions under whose guidance the country carried out numerous reforms in various social sectors. Although their negative role was exaggerated, the behaviour of current emissaries in Bulgaria does not help to improve their image. For example, as part of the consultations for IMF's annual monitoring report (Article IV), IMF experts meet with civil society organizations, but only with very specific, right-wing, neo-liberal think-tanks. From the consultations with trade unions, almost none of the views and comments expressed are reflected in the final report. This fact gives rise to the feeling that the pro-market enthusiasm of 1990 still hangs over Bulgaria, although IMF's global conclusions and analyses are gradually changing direction, IMF experts are beginning to abandon neoliberal measures and are increasingly turning to support workers' rights, citizens' social interests and the fight against inequalities.

<sup>20</sup> Young people neither in employment nor in education and training by sex, age and labour status (NEET rates) age 15-24 [http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=edat\\_lfse\\_20&lang=en](http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=edat_lfse_20&lang=en)

<sup>21</sup> Работна сила и коефициенти на икономическа активност на населението на 15 и повече навършени години през 2015 година [http://www.nsi.bg/sites/default/files/files/data/timeseries/Labour\\_3.2.1.xls](http://www.nsi.bg/sites/default/files/files/data/timeseries/Labour_3.2.1.xls)

<sup>22</sup> Employed persons and coefficients of employment of the population of 15+ during 2015 [http://www.nsi.bg/sites/default/files/files/data/timeseries/Labour\\_3.2.2.xls](http://www.nsi.bg/sites/default/files/files/data/timeseries/Labour_3.2.2.xls)

<sup>23</sup> Unemployed persons and coefficients of unemployment of the population of 15+ years during 2015 [http://www.nsi.bg/sites/default/files/files/data/timeseries/Labour\\_3.2.3.xls](http://www.nsi.bg/sites/default/files/files/data/timeseries/Labour_3.2.3.xls)

<sup>24</sup> Indicators for poverty and social inclusion for Bulgaria [http://www.nsi.bg/sites/default/files/files/data/timeseries/SILC\\_1.xls](http://www.nsi.bg/sites/default/files/files/data/timeseries/SILC_1.xls)





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**The findings in brief:** GDP and employment are growing, as are poverty, inequality and the government debt. The percentage of young people who neither study nor work has decreased since 2014, but it should be noted that emigration has continued during the past year, so without further analysis it cannot be concluded whether more young people have become active or whether they have simply left the country. There is an obvious need to intensify the state's redistributive function and reinforce the social, health and educational systems.





## LEGAL DEFINITIONS

### Government debt

Bulgaria adopted a Law on Public Debt in 2002.<sup>25</sup> Article 2 states that: "*All financial commitments made by, and on behalf of, the State, in compliance with the Constitution, constitute government debt and represent a liability of the State.*"

Art. 5. (1) Government debt can be taken in the following cases:

- to finance the budget deficit;
- to finance of investment projects and specific programs as approved by the National Assembly;
- to refinance government debt in currency at maturity date or before;
- to provide payments required for government guarantees;
- to support the country's balance of payments.

### Public-Private Partnership

The Law on Public Private Partnership (PPP) was adopted in 2012.<sup>26</sup> The essence of PPP is described in Article 3 of that enactment. **Brief official definition:** "Public-private partnership is a long-term contractual cooperation between one or more public partners of the one part, and one or more private partners of the other part, to carry out activities of public interest, while achieving better value for the public money invested and distributing the risks between the partners, which is carried out under the terms and provisions of this Act." **The objectives are:** to ensure the development of high-quality and affordable public interest services by achieving better value for public money invested; to encourage private investment in construction, maintenance and management of facilities of the technical and social infrastructure and in the performance of activities of public interest; to create safeguards to protect public assets and to effectively manage public funds in the implementation of PPPs.

### Tax Justice

Justice, including tax justice, is rather an ethical category. In Bulgaria there is no legal definition of 'tax justice'. The only statutory text that refers to justice is contained in **the Constitution** of the Republic of Bulgaria Article 60, paragraph 1: Citizens shall pay taxes and duties established by law, proportionately to their income and property.<sup>27</sup>

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<sup>25</sup> Law on the State debt <http://www.lex.bg/laws/ldoc/2135458339>

<sup>26</sup> Law on public private partnership <http://www.lex.bg/laws/ldoc/2135798101>. It is foreseen that the law is annulled.

<sup>27</sup> Constitution of Republic of Bulgaria <http://www.parliament.bg/bg/const>



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## **Public infrastructure**

There is no legal definition of the term 'public infrastructure'. The Law on Spatial Planning contains definitions of subtypes of infrastructure, such as 'technical infrastructure, and 'municipal projects of paramount importance', 'project of regional importance, 'social infrastructure'.





## RESEARCH RESULTS

### Gross Domestic Product

The Gross Domestic Product (GDP) at current prices has gradually increased in recent years, but is far from the levels of growth before the global crisis of 2008. This positive trend becomes even more negligible, when one takes into account that PPP-adjusted GDP per capita decreased in 2015 compared to the previous year.<sup>28</sup>

### Currency Board

A currency board is in operation in Bulgaria since 1997. The central bank may not lend to the government and there is no possibility for conducting monetary policy. The rate of the Bulgarian Lev to the euro was fixed at 1.95583 BGN per euro. The cover for the monetary supply with reserve foreign currency should be at least 100%; currently it is over 170%. On the one hand this gives security, but on the other, it blocks resources that could be used to strengthen the social systems and economic development of the country.

Although the debate about the need for a currency board is gaining momentum, distrust in government gives rise to a prevailing public opinion that if the currency board would be repealed, that would allow for yet another robbery. On the other hand, beyond the purely economic motives, there is resentment against the loss of sovereignty over Bulgaria's monetary policy. Observations from debates between the social partners - employers' organizations, trade unions and government representatives, indicate that the board will be cancelled only in the eventual accession to the Eurozone. And this is yet another version of externally imposed rules on national monetary policy. Therefore, scepticism towards the Eurozone is relatively high.

### Public Finance

Revenues in the 2015 budget amount to 16 463.8 million euro or 37.3% of GDP.<sup>29</sup> Over the past five years this share has been increasing. The lowest point since 1998 until now is 31.7%, recorded in 2011. Not only is the level of redistribution relatively low, **Bulgaria's GDP is at the bottom of the comparative table in the European Union:** for 2015 the per capita indicator is at 46, while the EU28 index is 100. The next Member State is Romania with 57. Since the global crisis and until the present moment Bulgaria's annual budget has been closing with a deficit every year. For the last fiscal year this was 2.9% - a decrease of 0.8%, compared to the previous year.

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<sup>28</sup> GDP per capita in PPS, Eurostat

<http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tec00114&plugin=1>

<sup>29</sup> Data on the Consolidated Fiscal Program (annual), Ministry of Finance <http://www.minfin.bg/document/3044:17>



The Bulgarian national budget relies heavily on revenue from VAT and excise duties, as they constitute 38% of the revenue to the Treasury. The most significant item of expenditure is 'Social security and welfare' (40% of total costs). However, it includes not only social benefits and programs, but also the cost of pensions for Bulgarian citizens.

The minimum amount of the fiscal reserve is determined annually by the Law on State Budget of the Republic of Bulgaria. Since 2010 it amounts to BGN 4.5 billion. For the last six months the reserve has almost doubled to BGN 14.13 billion.<sup>30</sup> Nevertheless, far from being the result of better functioning of the economy or increased tax collection rates, this is due to new loans taken by the state.

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<sup>30</sup> Fiscal Reserve Account (FRA) by months as of 30.06.2016, Ministry of Finance  
<http://www.minfin.bg/document/18431:2>



## PUBLIC DEBT

The indebtedness of the country is far below average European levels. Currently, it is 29.3% of GDP.<sup>31</sup> However, the rate at which debt is growing is disturbing. The first significant increase dates from 2014, when total state debt increased by more than 56%.<sup>32</sup> In 2015 the National Assembly approved an additional debt of BGN 16 billion over the next three years. It should be noted that the accompanying reasoning contains legally inadmissible goals, such as increased fiscal reserve.<sup>33</sup> When taking the last tranche, the government acknowledged that the aim was to ensure the sustainability of the banking system in anticipation of the audit of Bulgarian banks in 2016. This was due to the bankruptcy of the Corporate Commercial Bank (CCB) - one of the largest banks in Bulgaria in 2014, as well as to another financial institution's need for additional liquidity – that of First Investment Bank.

Having witnessed the developments in neighbouring Greece and the arm-twisting applied by financial institutions on the Greek government in 2015, citizens were strongly against the taking on of new debt. In addition, the memory is still alive of the rescue of banks after the global financial crisis and the austerity measures imposed in Western countries. There was a stormy debate about the new debt in social networks and some media, where new credits were also referred to as “odious debt”. NGOs sent their positions to all the ruling parties demanding that the decision be reviewed. However, as there was little protest reaction, the government seized the opportunity to adopt the planned new levels of state debt.

So far, no direct impacts from the growing debt are noticeable on people's lives. This is probably due to the fact that the government's social commitment to citizens has already been extremely low. New measures are being taken to reduce government spending on health, education, social benefits and pension payments. In general, this policy is not new for Bulgaria, as the redistributive function of the state budget is traditionally weak.

No plan to cover the debt has been made public as of yet. It is concerning that **there is no plan to use these fresh funds to improve economic and social activities**, the proceeds from which could cover debt repayment instalments, as well as increase the funds available in the state budget. On the contrary – the course taken is clearly to deepen the opening up and withdrawal of the state from the economy. Despite the overall disappointing results of privatization and concessions, there is a new law which stipulates increasing the term of concessions to over 35 years; there are plans to outsource administrative tasks as well. Not quite manifestly, the expert functions of the state in developing strategic national documents are already being carried out by external consultants and financial institutions - primarily the World Bank.

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<sup>31</sup> Government Debt Monthly Bulletin May 2016, Ministry of Finance <http://www.minfin.bg/document/18273:2>

<sup>32</sup> Government Debt Review 2014, Ministry of Finance p. 27 <http://www.minfin.bg/document/16941:2>

<sup>33</sup> Law on the ratification of the contract for dealings between the Republic of Bulgaria and dealers for issuing of bonds for the amount of 8 million euros <http://parliament.bg/bills/43/502-02-3.pdf>



## Tax Justice

Since 2007 a 10% tax is applied on **corporate profits** in Bulgaria. A higher income tax of 15% is levied on sole traders. These are the smallest companies, in terms both of turnover and number of employees. A proportional 10% tax is also levied on personal income. In addition to the fact that the same burden is applied to all income groups, there is no income tax-exempt threshold for taxes on salaries. Although there is no legal definition of 'tax justice', it is obvious that a 20-euro tax on a 200 euro monthly salary is a considerably more serious burden than a 200 euro tax on a 2 000 euro monthly salary. Progressive taxation was revoked in 2008, in the absence of any resistance. The reasons for this are the following: On the one hand, the 'reform' was executed instantly, without any debate even among MPs. On the other hand, low-income groups do not have a powerful voice to stand for their interests; besides the minimum wage was raised, so as the decrease in income would not be felt immediately.

**Value Added Tax** is 20% - the same for all products and services, with the exception of tourist services, where VAT is 9 percent. Bulgaria still refrains from using the practice of differentiation of VAT on essential goods - food, medicine, water, electricity, books, textbooks and so on. Debates were initiated last year, proposing various options for differentiated rates, but so far without success.

Bulgaria is active on the issue of **double taxation**: about 70 international agreements were concluded with different countries in order to prevent repeated taxation.

**Tax relief for individuals** comes in several types: for disabled persons, donations, young families, voluntary additional insurance. Two years ago, an experiment was conducted: instead of having a tax-exempt minimum salary, the tax levied was to be returned annually in the shape of tax relief. This experiment lasted only one year, since the new government was against the income-tax-exempt threshold. On the other hand, the procedure was tainted by the conditions that had to be fulfilled by employees in order to redeem the taxes they had paid.

There are two basic kinds of **tax breaks for companies**: for regional development and for carrying out production activities in municipalities where the unemployment rate is 25% higher than the national average. However, according to data produced by a currently ongoing project for tax justice (funded by the European Commission under the program DEAR - Development Education and Awareness Raising), big companies are avoiding tax by incurring pseudo-costs, where funds are transferred to related parties, e.g. fees for consultancy services, loans, trademark payments to the parent company. Thus, although they have billions in BGN of turnover, it appears that those companies are running at a loss and therefore they do not pay taxes. Even in the case of registering a minimum profit for one year, under Bulgarian law these companies are entitled to deduct the losses of the previous five years from their final financial result. For example, an oil refining company has a revenue of over BGN 5 billion for 2015, but at end of the year it turns out that it closes with a loss of BGN 122 million.



The proposals for **a global tax system and disclosure of tax and other information by large multinationals** are hardly discussed in Bulgaria. There is not even so much as an official governmental position on those issues, neither from the Ministerial Council, nor from the Ministry of Finance. No public debates are held, except for a few publications in specialized media in the past two years. However, since the outbreak of the scandal about the Panama papers and the letterbox companies in Luxembourg, the problem of tax avoidance is gaining publicity. The only statement from the Ministry of Finance on a related topic was published in a pro-corporate newspaper: in response to a question from journalists, the Ministry replied that the Government did not support the introduction of a minimum income tax rate in the European Union, as this would reduce economic growth and opportunities for development.<sup>34</sup> An important detail illustrating the heavy protection of low taxation exercised by Bulgarian authorities is the fact that in the autumn of 2015 Bulgaria filed a complaint to the European Commission against Greece.<sup>35</sup> The cause for the complaint was the inclusion of Bulgaria in the list of countries applying a preferential tax regime. One of the arguments against the measures taken by Greece was that there is no practice for EU Member States to label other Member States as having preferential taxes.

Traditionally, the government of Bulgaria is non-transparent. Bulgarian ministries do not publish their opinions and plans, even on issues of key significance, like the Transatlantic Trade and Investment Partnership (TTIP) and (CETA), against which there are campaigns, protests, and questions, not only by individuals, but also by trade unions. Despite the silence, it is almost certain that if the European Commission insists, the Bulgarian government will adopt measures against tax evasion. It is quite another matter whether the government would truly cooperate for their proper implementation.

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<sup>34</sup> States against corporations: the fight over taxation, Capital newspaper, [http://www.capital.bg/politika\\_i\\_ikonomika/bulgaria/2015/10/06/2622742\\_durjavite\\_sreshtu\\_korporaciite\\_bitkata\\_za\\_dan\\_ucite/](http://www.capital.bg/politika_i_ikonomika/bulgaria/2015/10/06/2622742_durjavite_sreshtu_korporaciite_bitkata_za_dan_ucite/)

<sup>35</sup> Presentation of the complaint of the Republic of Bulgaria against the Republic of Greece at the oral hearing before the European Commission. Ministry of Finance <http://www.minfin.bg/document/16463:2>





## PUBLIC INFRASTRUCTURE

Every seven years the Bulgarian government focuses on building road infrastructure, particularly **motorways**. Keeping down the minimum wage, and hence - all income; refraining from investments in health, education and culture, were all explained by the need for construction of motorways - a prerequisite for attracting foreign investment. At the same time, the government continues to neglect the railway, which is the most environmentally friendly and energy-efficient mode of transport. The state-owned railway company, **BDZ**, has accumulated losses which, although they declined last year, are still critically high. Passenger train services to remote locations that are not profitable are being discontinued without much ado. According to the current Minister of Transport, the Government, in the shape of the Minister of Finance and the Prime Minister, refuses financial support to the company. The goal is the privatization of Rail Freight, but it is hampered by the company's outstanding debt.

The 2016 State Budget Act stipulates the concession of **Sofia Airport**<sup>36</sup>, the initial amount of which is to be used to pay BDZ's debts. Once the railway company's obligations have been paid, its privatization would become possible.

Meanwhile, the national strategies envisage increased traffic along rail freight routes in Bulgaria. One obstacle to the stabilization of the sector is the high relative price of freight. The vignettes used for charging motor cars are significantly cheaper than the fees charged by the NRIC - the National Railway Infrastructure Company.

Passage through the road network in Bulgaria is significantly cheaper in comparison with road tolls charged in neighbouring countries and the EU as a whole. For that reason, the government had a plan to introduce tolls for the use of motorways and primary roads. For the time being this cannot happen because the motorways are built using European funds, on the one hand, and on the other, often there are no alternative roads – which is one of the prerequisites for introducing additional fees for motorways. **Many stadiums and cultural centres were built in rural areas** using EU funds. The plan was to have them inaugurated before the last local elections. This would not be a problem if there was a need for these facilities. In many cases, however, they were constructed for their own sake - because of the depopulation of small settlements often the total number of residents is far smaller than the spectator seats available at the new stadium. Nobody is practising ballet or taking lessons in the cultural centres, as there simply aren't any children around.

**Social infrastructure** is neglected. Probably the reason is the need for additional funds for its operation. The depopulation of peripheral areas and small towns, as well as the failure of health-care facilities, have led to the closure of many schools and hospitals. By contrast, there are many private hospitals that have contracts with the National Health Insurance Fund. The problem is that the purpose of medical

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<sup>36</sup> Law for the state budget 2016 <http://dv.parliament.bg/DVWeb/showMaterialDV.jsp?idMat=99252>



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professionals is no longer to treat patients, but to draw in money from the National Fund, including by performing unnecessary operations. Private hospitals often specialize in areas that are more highly paid and, unlike the state, have no obligation to carry out loss-making activities, such as emergency medical care, for example.

**Challenges in the sphere of energy.** In relation to pollution reduction measures, many of the thermal power plants are to be closed in the next 10 years. On the one hand this will lead to increased unemployment, on the other – to a shortage of electricity. That does not mean that we should extend the life of coal mines, but it is imperative to adopt consensual national decisions about alternative ways to meet energy demand.





## **PUBLIC-PRIVATE PARTNERSHIPS**

The debate on PPPs in Bulgaria dates back several years before the country's accession to the European Union, although PPP as a legal form was regulated only in 2012. Nevertheless, the mechanism has not yet been developed. According to the Law on Public-Private Partnership, the Ministry of Finance shall keep and maintain a public register of PPP, which should include the National Public-Private Partnership Program and the Operational Plan for each programming period. As none of these documents can be found on the website of the Ministry, this impedes an objective review of PPP in the country.<sup>37</sup>

Many municipalities have established joint ventures with private investors - municipalities contribute land and the investor provides funding. In this way were built many hotels, spas, golf courses, office buildings and more. Although all these projects are presented as "public-private partnerships", it is questionable to what extent this is the case. Based on published methodological guidance by the Ministry of Finance, it is easier to determine what PPP is not, rather than what it is.

PPP is not:

- outsourcing of functions via public procurement;
- privatization;
- "commercialization" of a public function by creating a state enterprise;
- loan to the state from the private sector;
- commercial activities via forming joint ventures for the realization of spas, golf courses, hotels, renewable energy projects, etc.

The PPP Law adds that PPP are not:

- Concession contracts awarded under the terms and provisions of the Law on Concessions and the Law on Mineral Resources;
- contracts to be awarded under the terms and provisions of the Public Procurement Act.

Although in the third point above the Ministry of Finance excludes the commercialization of public functions from the scope of PPP, the methodological documents give as an example the construction of a kindergarten, where one of the factors for approving this theoretical option is the increased income from higher fees payable by the parents. Precisely these higher fees, that are to guarantee a specific return of investment for the private investor, reveal commercialization – only the profits are taken into account, but not the social aspect of the project. It seems that even the government is not quite aware of what should be the essence of public-private partnership. Browsing through the websites of some larger municipalities shows that they see concession as PPP - obviously the wrong approach. Notably, however, the PPPs planned by municipalities pre-date the adoption of the law, so they could not have known that the concession falls outside the sphere of public-private partnership.

The current review shows that, despite the existence of a law, legal uncertainty does not allow projects to be assigned to public-private partnership. This does not prevent the government to periodically

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<sup>37</sup> Public private partnership, website of the Ministry of Finance <http://www.minfin.bg/bg/page/523>



present one or another project to the public as a PPP, even when legally it is not constituted as one. Most frequently this happens with contracts for management, construction, operation, concessions and so on. The business certainly supports the PPP idea because it sees a chance to expand and increase profits.

**Is there an alternative to PPP?** The alternative is for the state and municipalities to assume their inherent functions and deliver public services, without trying to transfer their obligations to private bodies. Because, as they relieve themselves from their intrinsic governing functions, this increases the costs and thus restricts citizens' access to basic services.