Corporate Social Responsibility as Corporate Governance Tool: The practice by the business in Bulgaria

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ABSTRACT:

Purpose – The purpose of this paper is to define how Corporate Social Responsibility (CSR) is used as Corporate Governance tool. Why it is used as such and who will apply CSR as Corporate Governance tool are the additional research questions to be discussed. The practice of the business in Bulgaria will be researched. The recent joining of Bulgaria to the European Union and the fast development of both Corporate Governance and Corporate Social Responsibility makes the practice of the business in Bulgaria interesting and valuable to research. It presents example of the development process of CSR and Corporate Governance to EU level.

Methodology – The master thesis presents and discusses the summarized results of a baseline survey conducted in the period September – October 2006 on the Corporate Social Responsibility in Bulgaria, combining quantitative and qualitative methods. 121 medium-sized and large companies, both with Bulgarian, foreign or mixed ownership structure have been analyzed. The companies surveyed are both public and private, from manufacturing, services, trade, IT and other sectors from all over the country.

Findings – This research found that CSR could be viewed as a principal-agent relationship where business enterprises in general could be either agents or principals depending on the character of the relationship. From the practice of the Bulgarian business the following key groups of stakeholders have been identified: local community and society at large, employees; customers and the public and the state.

Research limitations/implications – The paper has implications in enhancing the understanding of how Corporate Social Responsibility is used as corporate governance, although it is necessarily limited by the size of the sample and the country.

Originality/value – This paper increases the understanding of the relationship between corporate governance and corporate social responsibility.

Type: Master thesis

Keywords: Corporate governance, Corporate Social Responsibility, Principal-agent relationship, Agency theory, CSR theories, Bulgaria, Corporate Governance tool/mechanism
1. INTRODUCTION

1.1 Background

Today’s corporations operate in an environment of intense media, investor, regulatory and public scrutiny which requires solid corporate governance. This creates as well need for more pro-active role by states, companies and communities in a development process aimed at balancing economic growth with environmental and social sustainability.

Most academics and business experts have noticed how since early 1990s Corporate Social Responsibility (CSR) has transformed from an irrelevant and often frowned-upon idea to an increasingly important concept globally, both in political and business agenda, and is now part of the debate about globalization, competitiveness and sustainability. CSR involves assessment of the company’s economic, social and environmental impact, taking steps to improve it in line with stakeholder requirements and reporting on relevant measurements. Corporate governance reflects the way companies address legal responsibilities and therefore provides the foundations upon which CSR practices can be built to enhance responsible business operations.

Corporate Social Responsibility has been defined in many different ways. For the purpose of this study I will use four key definitions of the World Bank, European Commission, the World Business Council for Sustainable Development and International Organization of Standardization which covers all the elements of CSR.

According to the European Commission CSR is “A concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis”. In the European Commission’s Green Paper from 2001 corporate social responsibility is expanded to “voluntary taking on commitments which go beyond common regulatory and conventional requirements” and by which companies are trying to “raise standards of social development, environmental protection and respect of fundamental rights and embrace an open governance, reconciling interests of various stakeholders”. According to the World Bank, “Corporate social responsibility is the commitment of business to contribute to sustainable economic development by working with employees, their families, the local community and society at large to improve their lives in
ways that are good for business and for development”. CSR is seen not as a one-off act but as a sustainable process which helps balance the three pillars of sustainable development – economic growth, social development and environmental protection.

The World Business Council for Sustainable Development in its publication "Making Good Business Sense" by Lord Holme and Richard Watts, used the following definition. "Corporate Social Responsibility is the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large".

The forthcoming standard on corporate social responsibility ISO 26000 defines CSR as “Responsibility of an organization for the impacts of its decisions and activities on society and the environment through transparent and ethical behaviour that:
- is consistent with sustainable development
- takes into account the expectations of stakeholders
- is in compliance with applicable law and consistent with international norms of behaviour
- is integrated throughout the organization and its relationships.”

Based on the above definitions the following elements of CSR can be defined as:

- Voluntary commitment by business
- Extends beyond the statutory obligation of what is prescribed by the law
- It is directed to society at large and large number of stakeholders (including employees, communities, customers, and the natural environment)
- Is in compliance with applicable law and international norms
- Corporate governance tool

1.2 Problem Area

“With the media dominated in recent years by such issues as the sub-prime mortgage lending crisis, unregulated greenhouse gas emissions, and the ethical failures of Enron, Worldcom, and others, the role of the firm in the society is coming under greater scrutiny. Global companies are subject to increasing demands – from activists, employees, and investors – for
responsible and social behaviours. As the first decade of the 21st century enters its finals years, we see that the trajectory of corporate governance and CSR trends are meeting head-on.1

CSR raises many corporate governance questions ranging from what it means to what it involve for companies.

- How does corporate governance link with corporate social responsibility?
- Is CSR part of corporate governance? Is CSR corporate governance tool?
- What is the business case for CSR?
- How to put CSR at the Boardroom?
- How does a company incorporate its CSR commitment into its operations?

1.3 Research Questions

The thesis aims to define how Corporate Social Responsibility is used as Corporate Governance tool. Why it is used as such and who will apply CSR as Corporate Governance tool in Bulgaria are the additional research questions to be discussed. The recent joining of Bulgaria to the European Union and the fast development of both Corporate Governance and Corporate Social Responsibility makes the practice of the business in Bulgaria interesting and valuable to research. It presents example of the development process of CSR and Corporate Governance to EU level.

For the purpose of this research the main research question which will be answered is: How Corporate Social Responsibility is used as a Corporate Governance tool? The results will be based on the practice of the business in Bulgaria.

At the discussion of the results the following questions will be answered as well:

1. Why CSR is used as a Corporate Governance tool?
2. Who will apply CSR as a corporate governance tool in Bulgaria?

1.4 Limitations

Due to the specifics of the economic development of Bulgaria the middle-sized and large companies, are the ones with more knowledge and conscience about socially responsibility as well as the financial power to implement CSR initiatives. Middle and large companies are

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1 Strandberg, Coro (2008), “The Role of the Board of Directors in Corporate Social Responsibility”
listed on the stock exchange; they have corporate governance structures and are more aware and interested in the benefits of CSR. That’s why small and micro companies will not be discussed at this research.

1.5 Structure

The Master thesis consists of six chapters. The Introduction (Chapter 1) presents the general background of the research, the definitions of CSR and Corporate Governance, the research questions and the limitations of the thesis.

Chapter 2 discusses the theoretical background of the thesis. It presents in details the agency theory basing CSR on the principal-agent relationships and the specialized theories on Corporate Social Responsibility (Utiritarian, Managerial and Relational). The chapter discusses as well the different mechanisms for managing the agency problems.

Chapter 3 presents the economic climate, evolution of business culture and business ethics in Bulgaria from centrally-planned, collectively owned enterprises towards socially and environmentally responsible and ethical private sector. This chapter makes an overview of the history, regulations and analysis of the current development of Corporate Governance in Bulgaria.

Chapter 4 presents prevailing views and definitions of Corporate Social Responsibility, overview of the CSR developments in Bulgaria, elaborates on the drivers, factors and discusses regulations of CSR in Bulgaria.

Chapter 5 introduces the methodology of the research and discusses the results. Chapter 6 presents summary of the conclusions.
2. **THEORETICAL PART**

This part is going to present the theoretical background of the master thesis. There are different theories which could be used to explain the phenomenon of Corporate Social Responsibility and its relations to corporate governance. These are agency theory based on the principal-agent relationships and the specialized theories on Corporate Social Responsibility (Utilitarian, Managerial, Relational theories). The chapter will present different mechanisms for managing the agency problems.

2.1 **Views on Agency Theory**

Agency theory analysis “situations in which one individual (the agent) acts on behalf of another (the principal) and is supposed to advance the principal’s goals.” The principal-agent relationship arises when one party (the principal) hires another party (the agent) to perform some service and then delegate decision-making authority to the agents. The management of agency relationships plays an important role in corporate governance because corporate governance is often defined as a principal-agent relation. Thus the selection of the principal and the agent is crucial for explaining the relations between the different groups and the choice of a strategy to manage the agency problems.

According to the traditional view, the primary agency relationships are those among the shareholders who own the public company (principals) and the managers (agents) which give rise to a risk that the agent does act in the interest of the principal. The complementary view broadens the principal-agents relations, introducing the “business organization of the firm as one of the most important principals”. Therefore there is agency relationships between 1) the firm as principal and the shareholders as the agent; 2) the firm as principal and the banks as the agent; 3) the firm as principal and the other stakeholders with whom the firm contracts such as employees, creditors, customers and society as a whole with a monitoring role as the agent; 4) between the firm as principal and management as the agent; 5) stakeholders as principal and managers as their agent who should take the stakeholders interests into account. “Whether somebody can be regarded as somebody else’s agent depends on who the principal is. As any stakeholder can be chosen as principal, principals can range from minority

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shareholders to the society at large and from the environment to the government.”5 The firm itself can be defined as a nexus of contracts based on the relations among different parties.

These relationships are not necessary harmonious because contracts are written in a world of information asymmetry, uncertainty and risk. The problem lies in motivating the agent to act in the principal’s best interest rather than simply in the agent’s own interest. In particular almost any contractual relationship, in which one party (the agent) promises performance to another (the principal), is potentially subject to an agency problem. The core of the difficulty is that, because the agent in general is better informed than the principal about the facts related to the company performance, the principal cannot costlessly assure himself that the agent’s actions are not pursuing some personal goals that compete with the owner's goal of maximization of shareholder wealth. For example, the owners would like managers to run the firm in ways that maximise the value of their shares, whereas the managers' priority may be, to build a business empire through rapid expansion and mergers and acquisitions, which may not increase their firm's share price.6 The rationale of the principal-agent relationship is that the agent’s effort cannot be observed by the principal.7 The main areas of conflicts can be grouped into four categories: insufficient effort, extravagant investment, entrenchment strategies and self-dealing.8 These agency conflicts have implications for corporate governance and corporate social responsibility.

When agency problem occurs, it also tends to give rise to agency costs. When agents (managers) abuse their discretion, the principal (shareholders) sustain loss (agency cost) incurred in order to sustain an effective agency relationship (e.g., offering management performance bonuses to encourage managers to act in the shareholders' interests). M.C. Jensen and W.H. Meckling (1976) defined agency costs as the sum of 1) the monitoring expenditures by the principal; 2) the bonding expenditures by the agent; and 3) the residual loss, i.e. the monetary equivalent of the reduction in welfare experienced by the principal due to the divergence between the agent’s decisions and “those decisions which would maximize the welfare of the principal”.

8 Tirole, J. (2006), The Theory of Corporate Finance, Princeton, pp 16-17
2.2 Mechanisms to Manage Agency Problems

Agency problems arise within a firm whenever managers have incentives to pursue their own interest at the shareholders expense. Several mechanisms can reduce these agency problems.

For the purpose of this research the following three categories: legal strategies, economic and social mechanisms, will be reviewed. The legal strategies are based on the Kraakman et al. “The Anatomy of Corporate Law. A Comparative and Functional Approach” set of ten strategies that taken together define the legal methods for dealing with agency problems. These legislator’s tools can be used to protect nearly any vulnerable principal-agent relationship and can in principle be applied by private parties as well.

Economic corporate governance mechanisms for reducing agency costs are 1) large blockholders, 2) market for corporate control, 3) debt policy and bank monitoring, 4) board activity, 5) executive compensation, 6) shareholder activism, 7) employee monitoring, 8) competition, 9) scarce resources and 10) transparency. Social corporate governance mechanisms are media and social control and reputation. The division of economic and social mechanisms the author has made for the purposes of the research.

2.2.1 Legal Strategies

Legal strategies described below represent a method for reducing “the vulnerability of principals to the opportunism of their agents.” They are focused primarily on standard-setting and behaviour-modification components of the management of agency problems. The strategies could be divided into two subsets. Four “regulatory strategies”, which prescribe and set terms which govern either the content, formation or finalization of the principal-agent relations (rules, standards, entry and exit) and six “governance strategies” that depend on the hierarchical elements of the principal-agent relationship (selection, removal, initiation, veto, trusteeship, reward).

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A. Regulatory Strategies:

1) Rules

The rules are mechanisms which require or prohibit specific behaviour \textit{ex-ante} constraining agents to undertake actions that will harm the principals’ interests and specifying what agents may or may not do. Rules are commonly used to protect the interests of the creditors and public investors. The corporation statutes and internal guidelines include protection rules for creditors and shareholders such as dividend restrictions, minimum capitalization requirement, rules to govern tender offers, proxy fights, and corruption.\footnote{Kraakman R., Davis P., Hansmann H., (2004), “The Anatomy of Corporate Law”, Oxford University Press, pp 22-23} In principal rules can be mechanically enforced, they require simply a decision-maker to determine compliance.

2) Standards

Standards specify the general norm against which an agent’s actions will be judged \textit{ex-post}. They are open and use discretion for adjudicator such as the duty to act in “good faith”. Standards are also used to protect creditors and public investors, but the paradigmatic examples of standards-based regulation relate to the company’s internal affairs, as when the law requires directors to act in “good faith” or mandates that self-dealing transactions must be “entirely fair.”\footnote{Kraakman R., Davis P., Hansmann H., (2004), “The Anatomy of Corporate Law”, Oxford University Press, pp 23-24}

3) Entry

The entry strategies prescribe behaviour in which “principals’ affiliate with agents”. Its purpose is to screen out the unwanted counterparties in advance. “The entry strategies are particularly important in screening out opportunistic agents in the public capital markets.”\footnote{Kraakman R., Davis P., Hansmann H., (2004), “The Anatomy of Corporate Law”, Oxford University Press, pp 24-25} For example the requirement agents to disclose regularly information about the company performance to the principals (outside investors) which otherwise cannot acquire such information is an example of entry strategy because stocks cannot be sold unless the requested information is provided by the agent.

4) Exit

The exit strategy allows principles to escape opportunistic behaviour of agents’ \textit{ex-post}. The rights to withdraw the value of one’s investment and the right of transfer i.e. the right to sell shares in the market, are the two kinds of exit rights. The entry and exit strategies are particularly important in multi-party contracts and business ventures.
B. Governance Strategies

1) Selection
The power to select and appoint directors is key strategy to address the agency problems between managers and shareholders. This appointment right gives the principals (shareholders) the right to choose the agents (managers) whom they believe will work in their best interest and screen ex-ante for loyalty.

2) Removal
The right to remove, replace managers who act in their own interest and their actions are harmful to the company’s performance is a powerful disciplining device for addressing opportunistic behaviour by agents and punish disloyalty ex-post.

3) Initiation
These are decision rights which grant the principals the power to initiate management decisions. These rights are of less importance than the appointment rights and there is no jurisdiction which requires shareholders to initiate managerial decisions.\textsuperscript{15}

4) Ratification
Ratification by shareholders is required by corporate statues only to fundamental management decisions such as mergers and acquisitions and charter amendments. The ratification is done ex-post.

5) Trusteeship
Trusteeship strategy is type of incentive strategy which tries to eliminate the opportunistic behaviour of the agents’ ex-ante by ensuring that this behaviour won’t be rewarded. It is based on soft powered incentives of reputation and conscious. It could be applied by internal agents (in the company – outsider in the board or controlling shareholder) or by external (required by the law – court, appointed official).

6) Reward
Reward is type of incentive governance strategy which instead of expanding the power of the principals offers the agents (managers) rewards for successfully fulfilling their duties in the

best interest of the principals (firm). One way to implement this strategy is to tie the remuneration of the agents (managers) with the financial results of the company.

### 2.2.2 Economic Mechanisms

1) **Large blockholders**
Concentrated shareholdings by institutions or by blockholders could increase managerial monitoring and so improve firm performance. It is likely to be one of the most important governance mechanisms.

2) **Market for corporate control**
The threat of displacement imposed by the market for corporate control and threat of hostile takeover can create a powerful disciplining tool on managers who are performing their duties poorly. An outside owner can take over the firm to correct management failure not disciplined by existing owners, and the mere prospect of such a hostile takeover could influence management even if it never happened. The market for corporate control motivates managers to keep their reputation among theirs and other prospective employers and so improves firm performance. It is unlikely to be important when company ownership is strongly concentrated.

3) **Debt policy and bank monitoring**
The use of debt financing can improve performance by including close monitoring of the financial performance of the company by lenders and banks which serve as disciplining device eliminating opportunistic behaviour of agents. As lenders, banks will have a direct stake in the governance of corporations, requiring firm behavior that assures that their loans can be repaid. Bank monitoring is important governance mechanisms, but it depends on health of the banking system and the regulatory environment in the country.16

4) **Board activity**
Board activity is related to facilitating the interactions among board members and thus reducing agency costs. It introduces the role of independent directors, training of directors and disclosure of voting. Board activity is unlikely to be influential when controlling owner can hire and fire board members.

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16 Erik Berglöf & Stijn Claessens (2004), “Corporate Governance and Enforcement”
5) Executive compensation
Executive compensation schemes, which ties the rewards of the agents with the financial results of the company in attempt to prevent opportunistic behaviour, are more successful in companies with disperse ownership where there is no controlling owner who could hire and fire managers at his own discretion.

6) Shareholder activism
Shareholder activism is very important governance mechanism which encourages interactions among shareholders and thus fights the agency problems between managers and shareholders and between minority and controlling shareholders.

7) Employee monitoring
Employee monitoring is potentially very important governance mechanism, particularly in smaller companies with high-skilled human capital where threat of leaving is high. For this mechanism to be effective is required disclosure of information to employees; possibly board representation and mobility of employees. Employee monitoring can be an effective mechanism to enhance corporate governance as its interests are largely aligned with good firm performance and fair treatment of all stakeholders.

8) Competition
Effective competition on the local and international markets will help to improve corporate governance by putting pressure to enhance the firm’s performance. Proving a good performance increases as well the possibilities of the company to attract additional financing.

9) Scarce resources
Scares resources are incentive for companies to perform well on the market and be competitive. They are effective corporate governance tool and corporations are dependent on their customers and the value of customers’ customers. This makes stakeholders important agents to which corporations should be answerable and which monitor corporations leading to better corporate governance.

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17 Erik Berglöf & Stijn Claessens (2004), “Corporate Governance and Enforcement”
18 Erik Berglöf & Stijn Claessens (2004), “Corporate Governance and Enforcement”
10) Transparency
Transparency is an important component of the management of agency problems at firm level. Transparency is connecting with monitoring.19

2.2.3 Social Mechanisms

1) Media and social control
A system of social control of business is necessary in areas where both markets and government fail or cannot be expected to operate, and more generally is necessary to support the functioning of markets.

2) Reputation
Reputation is important mechanism to enhance the possibility of the companies to attract outside funding, growth opportunities and scope for rent seeking. For some corporations reputation comprises up to 50% of the value of the company that’s why they are putting a lot of efforts to keep good reputation.

2.3 Theories on Corporate Social Responsibility
Since the mid-1970 different scholars are making an attempt to classify theories on Corporate Social Responsibility. With the growing popularity and constant broadening and evolving of the concept for social and environment responsibility of the business there are more and more attempts of framing CSR. Here I will discuss briefly some of the theories of CSR.

In his paper Davide Secchi20 classifies the theories of CSR in three groups:

Table 1.

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<tr>
<th>Utiritarian</th>
<th>Theories on social costs</th>
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<tr>
<td></td>
<td>Functionalism</td>
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<tr>
<td>Managerial</td>
<td>Corporate Social Performance</td>
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<td></td>
<td>Social accountability, auditing and reporting</td>
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</table>

2.3.1 The utiritarian theories reflect the traditional economic approach where the firm main function in society is seen as making profits. These theories could be divided into two subcategories: the theory studying the social costs and the functionalists seeing CSR as a form of philanthropy. Economists do not think of society as an independent actor that can gain benefits or suffer costs. Rather, the social costs are the sum total of all costs to individuals in society, regardless of whether the costs are paid by the person who decides whether they will be incurred.21

In economics social cost is defined as the sum of private and external costs. Economic theorists ascribe individual decision-making to a calculation costs. Rational choice theory assumes that individuals only consider their own private costs, the costs when making decisions, not the costs that may be borne by others. In many cases, the costs borne by the individuals involved are the only costs. In some cases, there are costs imposed upon parties not involved in the economic exchange. If someone decides to light and smoke a cigarette, for example, they incur costs, namely increased health risk and the cost of one cigarette. In this case, there are costs that are incurred on agents outside the economic transaction - "external" to the economic activity.

Functionalists see the firm as a profit-making organization. Milton Friedman definition of CSR is typical for functionalist: “there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition, without deception or fraud.”22 More recently, the neo-functionalists present social responsibility issues as no more than corporate philanthropy or cause-related marketing.

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21 Wikepedia
2.3.2 The managerial theories on CSR use the approach for considering the social responsibility from inside the firm and connecting CSR directly to the management of the firm. Managerial theories could be divided into three sub-groups:

1. Corporate Social Performance

Corporate Social Performance (CSP) is connected to the need to measure the extent to which a corporation is socially responsible. CSP is a sort of measure for socially responsible behaviour. It is trying to make CSR more concrete by creating tools to measure it. Carrol creates “three-dimensional model”, where corporate performance comes from the interactions between: (1) social responsibility categories (economic, legal, ethical and discretionary); (2) social issues (environment, discrimination, product safety, occupational safety and shareholders); and (3) philosophy of social responsiveness (pro-action, accommodation, defense, reaction) This model measures social responsibility in order to contribute to corporate management. The other view is that it is very hard to find direct relation between social and financial-economic performance of the company, there is no researches showing such direct correlation, that’s why social responsibility is linked to strategy. Strategic CSR results in business-related benefits being integrated in the main business activities of the company.

2. Theories on social accountability, auditing and reporting

These theories are divided from corporate social performance as the social responsibility is measured through accounting procedures, auditing and reporting practices. The three activities are separate but they could intervene in succession. Companies, after being socially accountable, publish a social report, as part of their annual report or separate and than they might decide to have an independent evaluation from auditors. International organizations and institutions offer few models of social reporting: 1) UN Global Reporting Initiative; 2) UN Global Compact; 3) SA 8000 standards; 4) the forthcoming ISO 26 000, 5) soft encouragement (European Commission, 2001); 6) UNCTAD has just released in partnership with Ernst & Young the new publication “Guidance on Corporate Responsibility Indicators in Annual Reports”.

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3. Social issues in international business

The number of multinationals (MNC) carrying out activities in different countries is growing constantly. MNC having operations in different countries and sometimes on different continents, in countries with different development level are facing transnational competition and specific challenges in keeping same level of social and ethical responsibility. The theory is focused in defining tools and measures (codes of conduct, guidelines or principles) for management in foreign countries and is rather practice-oriented.

2.3.3 The relational theories on CSR are putting into the core of the analysis the complex firm-environment relationships, i.e. how the two interact. The category is divided into four sub-groups of theories: (1) stakeholder approach; (2) corporate citizenship; and (3) theory of social contract. The concept for (4) corporate sustainability could also be classified as a relational theory.

1) The founder of the stakeholder approach is Freeman's (1984) in his book “Strategic Management: A Stakeholder Approach”.25 As clearly expressed in the title of the book, the central purpose of stakeholder theory is to enable managers to understand stakeholders and strategically manage them. As Freeman states, "The stakeholder approach is about groups and individuals who can affect the organization, and is about managerial behavior taken in response to those groups and individuals".26 In short, the stakeholder theory identifies and models the groups which are stakeholders of a corporation (governmental bodies, political groups, trade associations, trade unions, communities, associated corporations, employees, customers, and the society at large), and both describes and recommends methods by which management can respect and take care of the interests of those groups. There have been numerous articles and books written on stakeholder theory including an entire issue of the Academy of Management Journal (v 42 n 5, 1999), and researches of Donaldson and Preston (1995) and Mitchell, Agle, and Wood (1997), Friedman and Miles (2002) and Phillips (2003).

2) Corporate citizenship is a concept very often related to the management of the multinational corporations operating in different countries, defining the corporations “next to

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the other citizens with whom the firm forms a community”.  
27 The emerging concept in this field is that of “corporate global citizenship”. Corporate citizenship is based on individual voluntary behaviour that goes beyond social, economic and legal duties.  
28 To become a “good citizen” the corporation should get involved successfully with the society. To be a global citizen the corporation should focus on basic and constant values on which the corporate behaviour everywhere, when there are operations, is based. These involves the relations the firm and the stakeholders. “Being a good global citizen in a relational context means treating well the entire range of constituencies – stakeholders – who have invested their capital in the business.”  
29 Other authors are focusing the concept for corporate global citizenship towards more traditional economic models and less philanthropic relationships: “Corporate citizenship involves actual results (what corporations do) and the process through which they are achieved (how they do it).”  
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3) The Social Contract Theory could be defined as “a new approach to business ethics, an approach that exposes the implicit understandings or “contracts” that bind industries, companies, and economic systems into moral communities.”  
31 The basic idea is that the corporate-society relations are governed by moral constraints. The social contract between the corporations and society helps in defining what is and what is not right to do in a given society.

4) The globalization of today’s world makes the concept of “corporate sustainability” to become an increasingly important issue for the business. As globalization accelerated, opportunities for business increased – but so did the worries that companies need to be more accountable. Globalization has made it both more important and yet more difficult to apply consistently high ethical standards to business in different markets.  
32 What is sustainability? The Bruntland Commission defines sustainable development as the one which “meets the needs of the present without compromising the ability of future generations to meet their own

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27 Matten et al. (2003), “Behind the mask: revealing the true face of corporate citizenship”, Journal of Business Ethics, pp 109 120  
32 “Doing good: Business and sustainability challenge”, Economist Intelligence Unit, February 2008
needs.” At its start sustainability was focusing mainly on environmental issues and later expanded to both economic and social dimensions.


There are other CSR theories and concepts but the purpose of this thesis does not aim to get into details in presenting them.

2.4 Corporate Social Responsibility and the Agency Theory

The World Bank defines Corporate Social Responsibility as “the commitment of business to contribute to sustainable economic development by working with employees, their families, the local community and society at large to improve their lives in ways that are good for business and for development”. Thus CSR could be viewed as a principal-agent relationship where business enterprises in general could be either agents or principals depending on the character of the relationship.

2.4.1 The firm as agent

In the principal-agent relationship, business enterprises could be considered as agents when having relations with different groups of principals (stakeholders) and forced by them to act in socially-responsible way, integrating social and environmental concerns in their day-to-day business. A “stakeholder is someone with the power to help or hinder your plan”  

For the purpose of this research the relations of the firm as an agent with the following groups of principals will be analyzed:

1) Local community and society at large – Laws, culture, social traditions and fundamental values influence the behaviour of everybody in society. 

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34 Stakeholder definition – “Someone with the power to help or hinder your plan” (Gerry Lewis, Think-UP Communications)
community is a powerful force, with its own priorities and it could influence the company’s business strategy by making them act in a socially-responsible manner and take into consideration the society agenda.

2) Employees – Employees are key asset of the company, that’s why they are important principals. Companies implement CSR strategies focused in keeping their employees, improving the health and safety work environment, encouraging the career development of their personnel, etc. respecting the human rights and labor standards.

3) Customers and the public – Customers could be a driver forcing companies to adopt social and environmental values in its business, because “the firm sometimes relies on its customers to force its managers to act in a certain way”.36

4) The State – As part of its policy to encourage business and improve the business environment and competitiveness, the state is responsible for developing and adopting mechanisms for encouraging CSR such as National CSR Strategies, nominating responsible for CSR governmental representatives and amendments in laws. Lately, there are debates that CSR is the “job” of the government but the “governments are only too happy to duck the issue or let business pick up the bill. In practice, however, it is often the absence of government rules that makes firms feel they have to fill the void – for example, by cutting carbon emissions or setting labor standards.”37

The relationships between the firm as agent and the different groups of stakeholders as principals is discussed in Chapter 5, section 5.2.1 How CSR is used as Corporate Governance tool in Bulgaria? and section 5.2.3 Who will use CSR as a Corporate Governance tool in Bulgaria?”

2.4.2 The firm as principal

The role of the firm as principal managing relations with different groups of stakeholders namely the local community and society at large, the employees, the customers and the state as agents, making them adopt CSR policies, will be presented in Chapter 5, section 5.2.2. “Why CSR is used as a Corporate Governance tool in Bulgaria?

3. ECONOMIC CLIMATE AND EVOLUTION OF BUSINESS CULTURE AND CORPORATE GOVERNANCE IN BULGARIA

This chapter presents the development of the economic climate in Bulgaria which forms the business environment in which the companies operate. The collapse of the communist regime, characterized with central planning and collective ownership, demanded new business culture oriented to social responsibility, transparency and accountability. Business ethics became a way of doing business. The chapter presents the history, regulations and analysis of the current situation of Corporate Governance in Bulgaria.

3.1 Business Environment

Bulgaria joined the European Union on January 1st 2007, after seven years of accession period and eighteen years of uneven and difficult transition towards democracy and market economy.

“As a post-communist country Bulgaria is one of the economies which experienced rapid changes without coherent strategies in the economic and social spheres. After the recovery of the dramatic crisis of 1996-1997, the 1998-2001 period is marked by a speedy privatization and liberalization of the market (the energy sector, the banks and telecommunication). A currency board was introduced in 1997 and Bulgarian lev38 was pegged to the Euro.”39 The period of 2001-2005 is marked by a reform agenda covering local government, tax system, legislation, health care, social policy, privatization, education following the start of the accession negotiations of Bulgaria to EU in 2000. The accession process demanded fundamental reforms across all sectors of the social, political and economic life in order to integrate the European standards.

The average inflation in Bulgaria for the period 2004-2006 was 6.1%, increasing to 7.6% in 2007 (with 2.3% for EU 27 for 2007) due to higher prices of natural gas, petrol, and food. The rapid growth of GDP, average of 5.7% for the period 2004-2006, went up to 6.2% in 2007 with average 2.4% for EU 27, driven mostly by increased consumption and investments. The per capita income rose 2.28 times between 1997 and 2004 but is still 25-30% of the average

38 1 EUR = 1.9658 BGN
level for EU 25 member states. Unemployment rate gradually decreased for the last seven years, falling from 16% in 2000 to 6.9% in 2007. Long-term unemployment, however, remains high 5% for 2006 with 3.7% for EU 27. As of 2004 the budget generates surplus, rising from 1.7% of GDP in 2004 to 3.2% of GDP in 2006.

Bulgaria attracted EUR 5.7 billion foreign direct investment (FDI) in 2007, accounting for 19.9% of GDP. FDIs registered strong growth from 5.9% of GDP in 2001 to an average of 8.5% of GDP in 2002-2005. Only a third of these investments were generated by privatization deals, the rest being green-field investments. The expected FDI growth for 2008 is 10%. In 2007 and 2008 only, the attracted FDIs are more than the cumulative amount of FDIs in the period 1990 to 2005. Corporate income tax in Bulgaria applies in a single rate of 10%. External investors have been attracted by rapidly developing national industry, highly skilled workforce and significant new market. The high level of attracted FDIs is evidence for the steady improvement of the business climate and competitiveness of the country.

A 67% of the companies surveyed for the research of the thesis find conditions for doing business in Bulgaria good. The results show positive correlation - the higher the number of employees, the better they evaluate the economic environment (from 58% of the companies with 11-50 employees to 75% of companies with 101-250 employees). Foreign companies are the ones expressing the highest satisfaction of the business environment 92%, followed by mixed companies with 75%, subsidiaries with 67% and last the Bulgarian-owned companies with 65.7%. Only 26% of companies evaluate the conditions for doing business in Bulgaria as bad. The results show negative correlation – 31.9% of the companies with employees from 51-100 find conditions for business as bad, 19.4% of the companies with 101 to 250 employees and 12.5% of the ones with 251 to 1000 employees. Bulgarian-owned companies register the highest level of dissatisfaction with economic conditions - 28%.

3.2 Evolution of Business Culture and Business Ethics in Bulgaria

The post-communist countries experienced periods of reforms in political, economic and social systems, in particular in the field of institutions and legislation, with one of the most important achievements the restoration of the private ownership. This required building of

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40 Statistics: Economic Intelligence Unit, 2008
41 Bulgarian National Bank
new business and ethical culture of the business and the society. “The socialists’ ethics was characterized by the primacy of collective interest, a mostly egalitarian wage system, “socialist solidarity” (subordinated to equality)” and collective activities. The business culture which was inherited characterized with “over-centralised system of management with an almost entirely state-owned property over the means of production, inefficient production structure and non-competitive productions on the foreign markets, and irrational employment structure.”

The adoption of new ethical principals and culture based on democracy, market economy, economic efficiency, “entrepreneurial spirit, personal responsibility and liberal solidarity” was long and challenging transition due to gaps in legislation, cultural and historical specifics and level of economic development of Bulgaria. The paternalistic approach, resulted in highly-concentrated ownership, where all the decisions have been taken by one person “patron” and where employees did not take part in any important decisions, still have impact on the business culture in Bulgaria. It is shown through the strong position in the decision-making of the CEO or Managing director of the company, who often is the owner. During the period 2006-2007 a lot of public offerings on entirely closed private-owned companies were held, resulting in lower ownership concentration and more traded shares on the capital market. Thus the interests of investors, minority shareholders, other stakeholders, disclosure of information, human resource policy are included in the business strategy of the companies.

Codes of ethics in general are gaining ground in Bulgaria, both in terms of individual companies, as well as collective statements of business principles. All major employers associations have their codes of business conduct to which their members commit (Bulgarian Chamber of Commerce and Industry, Confederation of Employers and Industrialists in Bulgaria, Bulgarian Business Leaders Forum). The most wide-spread are the codes of ethics which are tailored to the specificity of the sector and concern for the general public interest.

The Bulgarian Business Leaders Forum Business Ethics Standard, introduced in 2001, is currently adopted by more than 1500 Bulgarian and foreign companies. Positive sign that ethics is gaining importance for the Bulgarian business is the growing number of Codes of Ethics:

- Code of Ethics of the Bulgarian Media
• Business against Corruption – a collective initiative/appeal of business organisations against corruption
• Code of Ethics of the Bulgarian Specialists in Public Relations – Bulgarian Public Relations Society
• Code of Ethics of the Bulgarian Donor Forum
• Code of Ethics of the Bulgarian Web Association
• Code of Ethics of Pharmaceutical Companies
• Code of Ethics of the Bulgarian Oil and Gas Association
• Code of Ethics of the American Chamber of Commerce
• Code of Ethics of the Bulgarian Association of Investor Relations Directors

3.3 Corporate Governance in Bulgaria – History, Regulations and Analysis

3.3.1 History

For a number of years the Bulgarian companies have been applying the principles and norms of corporate governance as set out in the Commercial Code and the Public Offering of Securities Act. The experience accumulated by the Bulgarian companies, the entering of the Bulgarian business at the European environment as of January 1\textsuperscript{st}, 2007, the development of the capital market and the investor requirements have increased the need in 2007 for a National Code for Corporate Governance (CG). As required by European standards and the EU Action Plan for Modernization of Company Law and Enhancement of Corporate Governance, the adoption and implementation of national codes by member-states is an important condition for efficient free movement of goods, services, capital and people.\textsuperscript{43}

The number of researches conducted regarding the development level of the corporate governance in Bulgaria for the period 1992-2002 reveals the following key findings:

• There is no clear distinction between the corporate governance and the management of the companies
• High level of ownership concentration
• Existence of “transitional owners”
• Strong conflicts of interests in the companies
• Underdeveloped regulation mechanisms
• Abuse of the rights of the minority shareholders

\textsuperscript{43} Bulgarian National Corporate Governance Code, October 2007
- Lack of legal protection
- Lack of transparency
- Underdeveloped capital market in Bulgaria
- Lack of interest from investors to improve the corporate governance

This situation required the basis for a good corporate governance practice in Bulgaria to be set up on the ground of a restrictive legislation. This lead to changes in the Public Offering of Securities Act including introduction of very restrictive regulation regime for organizing General Meetings, maximum protection of the rights of the minority shareholders, introduction of the position of the Director of Investors Relations, obligatory preparation of programmes for corporate governance, etc. In the period 2003-2005, there were a lot of criticism that the companies developed programmes for corporate governance just formally without any practical value and application. Even though, the initial process of the preparation of CG programmes facilitated the introduction and acknowledgement with the CG terminology, the structure of the CG and the best practices. Despite the fact that most of the companies did not get a clear understanding of the corporate governance some managed not only to create solid corporate governance structures and documents but as well to apply the CG principles in their operations. Corporate Social Responsibility started to be considered as part of the overall concept of good corporate governance.

In 2008, one year after Bulgaria’s EU accession, the reality regarding the implementation of CG in Bulgaria is much more optimistic. Most of the managers of the Bulgarian public companies have a clear understanding of what is corporate governance and they are applying the principles of good corporate governance and the best practices in their work. The level of ownership concentration is lower and more and more shares are traded on the capital market. During the period 2006-2007 a lot of public offerings on entirely closed private-owned companies were held, after which they acquired public status and their securities were allowed to be traded at the regulated market. The newly listed companies on the stock exchange for the period 2006-2007 follow consistent policy for transparency in regard to the activities of their boards, disclosure of information to shareholders and are ready for open dialogue with the minority shareholders, the investors’ community and the economic media. The management of these companies is the one starting as well to look for other, not explicitly mentioned in the

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laws ways to improve their social and environmental policy i.e. to implement corporate social responsibility initiatives and projects.

In 2006, the Bulgarian Stock Exchange accepted the Code for Corporate Governance which was obligatory for all public companies which securities are traded on the official market. This Code has been applied until the announcement of the Bulgarian National Code for Corporate Governance on October 9th, 2007.

3.3.2 The Bulgarian National Code for Corporate Governance

The National Corporate Governance Code (CG) is a step forward towards the establishment of modern rules and norms for the good governance of public companies in the Republic of Bulgaria. The Code embodies and encourages market democracy and economic freedom of market operators. Over a period of one year a Task Force comprised of representatives from the Bulgarian business community, the Bulgarian Stock Exchange – Sofia, governmental and civil society organisations, and the academic community worked jointly to make this Code a reality. The final text of the Code includes recommendations from Bulgarian and international experts.45

The CG Code is striving to achieve a balance between the established Bulgarian practices and the international corporate governance standards. The rationale and structure of the Code follow the internationally adopted and implemented Principles of Corporate Governance of the Organisation for Economic Cooperation and Development (2004): the accountability and independence of corporate boards, the protection of shareholders’ rights, the equitable treatment of international and minority shareholders, the disclosure of information, and the integration of stakeholder interests.46

The Code addresses in detail the role of the Board of Directors in the One-tier systems, and the nature and principles of the cooperation between the Supervisory Board and the Management Board in the Two-tier systems, the internal control and auditing, rules for effective disclosure of information and protection of shareholders. Chapter 5 of the Code is dedicated to stakeholder relations and makes recommendations in line with current requirements for socially responsible businesses.

45 Bulgarian National Corporate Governance Code, October 2007, Introduction
46 Bulgarian National Corporate Governance Code, October 2007, Introduction
The Code is a corporate governance mechanism. The principles of the Code are to be applied by all Bulgarian public companies. It is recommended that the Code should also be implemented by those companies that are planning to become public and as well by Bulgarian companies with state and municipal ownership. For the other companies the acceptance of the Code is voluntary.

The Code follows the “comply or explain” principle, meaning that companies should comply with the Code, yet if they do not, the company or its corporate board must explain and disclose the reasons for non-compliance. Companies should post information about the implementation and compliance with the Code on their web sites and include it in their annual reports. Due to the development of the economy and corporate culture in Bulgaria it is envisaged the Code to be reviewed regularly and if necessary up-dated every 18 months.

3.3.3 Regulation of the Corporate Governance in Bulgaria

The Bulgarian capital market operates within the framework of the following legal provisions of Corporate and Listed Companies Laws:

  “The main objective of the Law is governance of the public offering and transactions in securities, the activities of the Financial Supervision Commission, Regulated Securities Markets, Central Depository, investment intermediaries, investment companies, management companies, terms and conditions for carrying out such activities and the State control over them. The law is aimed at providing protection of investors and creating prerequisites for development of a transparent and efficient capital market in the country.”

- **Commercial Law**
  It is effective as of 1991. The Commerce Act presents the different forms of business organization of the company and the rules and procedures of their functioning.

- **Markets and Financial Instruments Act**
- **Measures against Market Abuse With Financial Instruments Act**

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47 Bulgarian National Corporate Governance Code, October 2007, Introduction
48 All Laws are available in English at [http://www.lexadin.nl/wlg/legis/nofr/eur/lexwebul.htm](http://www.lexadin.nl/wlg/legis/nofr/eur/lexwebul.htm)
49 Bulgarian Stock Exchange – Sofia, [www.bse-sofia.bg](http://www.bse-sofia.bg)
• Special Investment Purpose Companies Act
• Law for Independent Financial Audit
• Credit Institutions Act
• Financial Supervision Commission Act
• Accounting Law

Three institutions construct the capital market infrastructure in Bulgaria – the Financial Supervision Commission (FSC), Bulgarian Stock Exchange (BSE) and Central Depository (CD).

“The Financial Supervision Commission is the State regulator of the stock market. Its foremost mission is to regulate and exercise control so as to ensure the protection of investors and to enhance the development of a transparent and efficient securities market.”50 In 2003 the Financial Supervision Commission replaced the established in 1995 State Securities Commission.

The Commission is an independent state body under the authority the Parliament and it regulates and controls the public offering of and trading in securities, regulated securities markets, investment intermediaries, Central Depository, investment companies, and management companies.

“The Commission exercises control over the public companies and issuers; issues and withdraws licenses; gives confirmations and approvals; inspects the operation of banks in connection with their activities as investment intermediaries and depositories; exchanges the information indispensable for its activities with the Bulgarian National Bank, other state institutions and bodies, bodies of local self-governance and administration, as well as with non-governmental organizations related to the securities market.”51 The work of the Commission is regulated by the Financial Supervision Commission Act and Ordinances of the FSC.

50 Bulgarian Stock Exchange – Sofia, www.bse-sofia.bg
51 Bulgarian Stock Exchange – Sofia, www.bse-sofia.bg
Central Depository AD is the only organization in Bulgaria providing settlement of corporate securities in book-entry form, established in 1996. “The central depository is a joint stock company with a one-tier management system and with the following activities:
1. opening and keeping of accounts for securities;
2. registration of transactions in securities;
3. keeping of cash accounts and effecting of payments in relation to transactions in securities;
4. administration of securities, including keeping of the books for dematerialized shares and bonds.”52 Financial Supervision Commission, Bulgarian National Bank and Ministry of Finance directly control Central Depository operations.

The Bulgarian Stock Exchange is a “joint stock company that organizes an official securities market and ensures to its members and their clients equal access to the market information and equal conditions for participation in trading”.53 The Bulgarian Stock Exchange is licensed on October 9, 1997. On October 21, 2000 the BSE-Sofia launched its official index – SOFIX. The Rules and Regulations of the BSE-Sofia specify the principles governing the overall operations on the Bulgarian Stock Exchange-Sofia.

3.3.4 Analysis of the Corporate Governance in Bulgaria

In six months, after the adoption of the National Code on Corporate Governance 40 Bulgarian public companies54 have accepted to follow its principles. The analysis on the corporate governance practice in Bulgaria will be based on the review of the experience of the companies that have accepted the National Code on Corporate Governance. The market capitalization of these companies up to April 2008 amounts to BGN 7 mln (approx. Euro 3,6 mln.), with total market capitalization of the Bulgarian Stock Exchange amounting BGN 22 mln (approx. Euro 11,2 mln).

Twenty one of the 40 companies have been obliged to accept the Code by the Rules and Regulations of the Bulgarian Stock Exchange while the other 19 have joined voluntarily. Even though, that for the companies which have accepted the National Code the requirement for preparation of separate corporate governance programmes was withdrawn, 22 of these companies still continue to prepare CG programmes or up-date their existing ones.

52 Art. 127. (2), Law on Public Offering of Securities
53 Art. 20. (1), Law on Public Offering of Securities
54 Names of the companies enclosed in Annex 1
I. Corporate Management

Twenty of the public companies have two-tier systems (Management Board and Supervisory Board) while the other 20 apply one-tier systems. Neither of the companies conveys in its Annual Report the number of the independent directors at the board. Twenty two of the companies have not reported on the division of functions among the members of the corporate management or the disclosed information is partial and insufficient. The other 18 companies have presented information regarding the responsibilities, obligations and activities of the members of the corporate management.\(^{55}\)

Twenty five of the companies report data and provide information regarding the participation in the managing and supervisory bodies of the members of their corporate management. The other 15 have not revealed such information.

Companies which report on the remuneration of their members of corporate management are 60 %. Some of them provide only the total amount of the remuneration for the participation in the board. Not one company has reported for conflict of interests.

II. Protection of the Shareholders Rights

All the companies, that have joined the Corporate Governance Code, have organized General Meetings of the shareholders within the set by the law deadlines and provided detailed and sufficient information to all groups of investors. Every one of the companies has announced the decisions of the General Meeting through published Minutes of the Meeting. Only 6 of the companies have prepared and approved rules for the organization of regular and extraordinary General Meetings of the shareholders. These rules grant equal treatment of all groups of shareholders and rights to every shareholder to express its opinion on the issues at the agenda of the meeting, as recommended by the Corporate Governance Code.

II. Audit and Internal Control

It is still not a practice in Bulgaria companies to form audit committees, even though in the internal regulations such recommendation exists. Proposals for the selection of external auditor are included in the materials provided for the General Meeting of the shareholders.

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Companies tend to keep one and the same external auditor for years. It is common practice one auditor to examine and certify the company reports for 4-5 years.

In their periodical reports the companies identify the risks which they are facing and the ways to manage these risks. This leads to the conclusion that the process for establishment and implementation of systems for internal control has started.

III. Disclosure of Information

All reviewed companies disclose information periodically or ad-hoc according to the legal requirements of the Public Offering of Securities Act. The analysis is based on the annual and intermediate reports of the companies for 2007, as well as the ad-hoc disclosure of information.56

Twenty five of the companies disclose information limited within the set by the law minimum. Only 15 of the companies disclose additional information over the required minimum and target it to wide range of stakeholders (investors, economic media, financial analysts and other stakeholders).

Thirty three out of the forty public companies which have accepted the Code have corporate web sites. The corporate web sites of 15 of the companies comply with the requirements of Chapter IV “Disclosure of Information” of the National Corporate Governance Code. Eighteen of the companies have corporate web sites but the web sites do not have “Investor Relations” section. The published information is difficult to access, fragmented and out-of-date. Seven of the companies which have accepted the National Code do not have at all corporate web sites. In conclusion, twenty five of the companies do not comply entirely with the principles for the disclosure of information at the National Code. Information for this non-compliance has not been presented at their Annual Reports as the “comply or explain” principle of the National Code requires. Some of the reasons for unwillingness of the companies to disclose information are grounded in the business culture in Bulgaria, which is still in process of changing from inward-oriented, closed and high-concentrated ownership system to transparent and external-oriented structure with diverse ownership.

IV. Stakeholders

Chapter V of the National Corporate Governance Code sets recommendations for the relations with stakeholders. Thirty of the companies accepted the Code neither identify their stakeholders nor have clearly defined policy towards them. The other ten companies identify as stakeholders mainly their clients, creditors, suppliers, employees and business partners, and express readiness to cooperate with them.57

The National Code recommends companies to disclose regularly the non-financial information for their activities. The companies should inform their shareholders, the public and other stakeholders about their policy, projects and activities regarding the social and environmental responsibility of the company. Such issues are anti-corruption, human resource policy, relations with suppliers and clients, social-responsibility of the company, protection of environment, etc.

Despite these recommendations, only 10 of the companies have reported about their Corporate Social Responsibility policy in the Annual Reports, separate report or via the corporate website. The corporate web sites of these 10 companies provide detailed and complete information about their CSR policy. Some of the companies though disclose information only about their environment responsibility, concluding that this covers all the issues. Thirty of the companies do not disclose any non-financial information neither in their Annual Reports nor on their corporate web sites.

It is still early to evaluate the level of compliance of companies with the principles of the National Code for Corporate Governance. In May 2008, for a second consecutive year, the Bulgarian Daily Newspaper “Dnevnik” made a classification of the best companies traded on the Bulgarian Stock Exchange. A classification of the first 10 public companies with the best corporate governance has been made based on the principles of the Bulgarian National Corporate Governance Code. The list with the companies is enclosed at Annex 1, 1.2.

4. OVERVIEW OF THE CORPORATE SOCIAL RESPONSIBILITY IN BULGARIA

While CSR literature emphases its cultural universality and benefits, in practice the particularities of cultural, economic and social development in a certain country lead to differences in CSR perceptions and practices across countries. For this reason this chapter presents prevailing views and definitions of CSR, overview of the CSR developments in Bulgaria, elaborates on the drivers, factors and discusses regulations of CSR in Bulgaria.

4.1 Prevailing Views and Definitions of Corporate Social Responsibility

Corporate Social Responsibility is seen as a newer concept which, although it was discussed by the classics of liberal thought like Milton Friedman and Friedrich Hayek, did not become a part of corporate practice until the second half of the 20th century. Professor Friedman measured social responsibility in earnings per share.

CSR is not a static issue, and is constantly changing and at the moment CSR is seen as incorporating much wider issues based on social, environmental and economic matters of the company and the company itself is responsible to wide range of stakeholders not only its shareholders. CSR should not be seen as a new phenomenon, but rather as an ongoing process of defining and operationalising the relationship between business and society and its responsibilities towards it. Adrian Cadbury in his book “Corporate Governance and Chairmanship A Personal View” defines social responsibility as a contract between business and society. According to him “There is no conflict between social responsibility and the obligation on companies to use scarce resources efficiently and to be profitable – an unprofitable business is a drain on society. The essence of the contract between society and business is that companies shall not pursue their immediate profit objectives at the expense of the longer-term interests of the community.” The term “corporate responsibility” and related terms were not used in the literature until Carroll (1999), a leading scholar in the field published an overview of the historical perspective of CSR in the Journal of Business and Society. The different definitions of CSR, used for the purposes of this research, are discussed at Chapter 1, section 1.1.
4.2 Changing Context for Corporate Social Responsibility in Bulgaria

Socialism (1944 – 1989)
In socialist times there was a common perception that businesses existed to purely serve society. If this meant hiring more workers than was necessary, so be it; if this meant reducing service or product prices to fit within affordability profiles, it was done. Regardless of impacts on profits, state-owned companies in Bulgaria implemented large-scale and costly social programs. Employees were provided with health services, nurseries, kindergartens, summer camps, sport centres, cultural institutions etc.

In some regions where a large state-owned company provided jobs for most of the local residents, the company became a sort of patron. This patron-company not only provided occupation but also shaped the way of living of entire communities. Employees were encouraged to do the so-called social work. This would involve anything from working in the fields, through cleaning in parks to spending time with kids from orphanages. However, the social involvement of employees was very often ill planned, and sometimes unnecessary and redundant, thus distorting the tradition of voluntarism.

First Phase of the Transition (1989 – 1997)
With the move towards a free market system, social activities were quickly abandoned in the belief that they were part of the old system. In addition to this ideological barrier to the advancement of CSR, there was an economic one. The first phase of the transition to market economy was marked by unpredictable inflation rates and a strong depreciation of the local currency. The buyers of the Bulgarian products – the other former socialist countries – turned to new suppliers, thus the market for local production dwindled. Unemployment was rising dramatically, enhancing employers’ bargaining power. This, coupled with the decreased respect for ethical values and the instable legal and institutional framework, allowed employers to make employees put up with low wages, bad working conditions, and lower social payments.

In this second phase of its transition Bulgaria achieved steady progress in the process of establishing a democracy and a market driven economy. As a result of a good policy mix

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58 World Bank, 2005
comprising a currency board arrangement, a tight fiscal stance and deep structural reforms, the Bulgarian economy achieved a high degree of stability.

Following negative real GDP growth in 1996 and 1997, the country was recording sustained economic growth. Between 1998 and 2004, real GDP growth averaged 4.4 a year. Inflation decreased significantly from more than 1,000 per cent in 1997 to 2.3 per cent in 2003. From 18.1 per cent in 2000 unemployment has been reduced substantially to 12.7 percent by 2004. The improved business climate was reflected in a rising inflow of foreign direct investment with a record high in 2003.

The second phase of the Bulgarian transition coincided with a growing world-wide demand for companies to be accountable for the social and environmental dimensions of running their business. In the early days of transition when survival was the main item on most companies’ agendas, the vivid debate about CSR that was taking place in more advanced countries did not mean much for businesses in Bulgaria. However, the social and economic progress as well as the accelerated preparation for the EU membership (after 2000), made the changes in business thinking and practices unavoidable.


Bulgaria is among the youngest members of the European Union, accepted on January 1st, 2007. The EU membership has a positive impact on the development of modern corporate culture and adoption of social standards and implementation of socially responsible projects and initiatives in Bulgaria. Not only the foreign companies or subsidies of big multinationals but purely Bulgarian-owned companies and corporations are putting CSR in their business strategies, especially the ones which already are or planning to export. The local companies which are established after the fall of the communism in 1990 are gathering financial power and starting to expand to the neighboring countries (Macedonia, Croatia, Serbia, Bosnia and Herzegovina, Turkey) taking advantage of the EU membership. In the new economic reality, transparency, social policy towards employees and environmental and social concerns to society are not luxury but necessity for companies required by stakeholders and needed for their good image and competitiveness for the scarce resources on the market.
4.3 Drivers for CSR in Bulgaria

With the opening of its economy, Bulgaria saw an influx of foreign direct investments. While entering the Bulgarian market the large multinationals brought with them a tradition of community engagement, environment-friendly technologies, a new management culture, and a practiced eye for how business might help solve social and environmental challenges.\footnote{Simpson, Susan (2002); “From Transition to Accession: The Experience of Corporate Social Responsibility in Central and Eastern Europe”; International Business Leaders Forum, London.} The initial motivation for their CSR engagement was part of their market entry strategy. They used CSR as a tool for obtaining the licence to operate through demonstrating that the company can be trusted and that it can bring benefits for the wider community while gaining competitive advantage. The foreign subsidies are the pioneers bringing knowledge and awareness of socially-responsible practices which gradually become a model for gaining economic power Bulgarian companies to start developing CSR activities first oriented mostly inside the company towards employees and than developing to activities towards communities and other stakeholders.

The county’s positive economic development allowed a growing number of local companies after 1997 to start making contributions to the welfare of the communities where they operated. “The companies which consider the general conditions and their own development to be positive spend between 1.5 and 2.5 times more than other on donations and community activities.”\footnote{UNDP and BCAF (2006), “Corporate Social Responsibility within the Bulgarian Context”, p. 9} The reasons for that are that companies with better performance have more resources to spend on PR, marketing, HR and activities to improve the needs of the community in which they operate. These companies are conscious about their social and environmental policies as they might have impact on their public image and relations with their shareholders and other stakeholders. The subsidies of the foreign companies are encouraged by the mother companies to implement global policies towards CSR, for example Planet me of TNT.

The EU membership is another factor that influenced positively the advancement of CSR in Bulgaria. There are two reasons why the preparation and the EU accession turned into a major driver for CSR practices: firstly, CSR practices help enhance companies’ competitiveness, needed in the European markets, and, secondly, for Bulgaria CSR is an accession requirement. Important parts of the acquis cover CSR issues such as consumer and environmental
protection (chapters 22 and 23), the promotion of fair competition (chapter 6), and anti-corruption. The programmes under EU funding are giving opportunities for socially-responsible projects to be financed under “Competitiveness” programme at the Ministry of Economy and Energy, “Human Resource” under Ministry of Administration and Administrative Reform and European Social Fund at the Ministry of Labor and Social Policy. The first project in Bulgaria funded under EU programme starting in February 2008. The project “Supporting the capacity of the civil society structures to improve the corporate governance and development of corporate social responsibility” is funded under operational programme “Administrative capacity” and will be implemented by the Association of the Industrial Capital in Bulgaria in partnerships with the Association of the Investors’ Relations Directors. The project duration is 18 months amounting 270 000 euro. A project funded directly by the European Commission aiming at accelerating CSR practices started at the end of 2006. This is the first regional project aiming to accelerate the implementation of Corporate Social Responsibility practices in 8 new EU Member States and in candidate countries: Bulgaria, Croatia, Hungary, Lithuania, Macedonia, Poland, Slovak Republic and Turkey. The project duration is 18 months. Total budget of the Project is 1.36 million USD (775 636 Euro). The contribution from the European Commission stands at 620 199 Euro, while the partnering organization United Nations Developing Programme is contributing 155 437 Euro to the Project. The main objective of the Project “Accelerating CSR practices in the new EU member states and candidate countries as a vehicle for harmonization, competitiveness, and social cohesion in the EU” is to promote the importance and advantages of doing socially responsible business and developing national CSR agendas in the project countries.

The data from the research for the thesis shows that in Bulgaria 28% of the companies with employees from 50 to 100 people consider CSR as an issue which is developing at the moment but which is potentially of great interest, 42% of the companies with 101 to 250 people and 44% with 251 to 1000 workers thinks the same. Companies from the service and manufacturing sectors are expressing higher interest in CSR issues as well as foreign companies evaluate social responsibility of the business better developed than Bulgarian.

**CSR as a tool for improved competitiveness.** The European Union’s 450 million potential consumers represent an important customer base for Bulgarian companies. Many indications suggest that Bulgarian companies are not in a position yet to successfully compete in this market. According to the Global Competitiveness Report for 2007-2008 of the World
Economic Forum Bulgaria ranks 75th out of 131 countries. This is far below all EU member countries even below Romania which is 74th. At the Business Competitiveness Index Bulgaria ranks 83rd, 10 places below Romania and more than 20 places below any of the older EU member states. A European Commission Green Paper entitled “Promoting a European Framework for CSR” (2001) stresses that CSR is important in increasing competitiveness: “the experience with investment in environmentally responsible technologies and business practice suggests that going beyond legal compliance can contribute to a company’s competitiveness.” Companies in Bulgaria are increasing becoming aware of CSR’s ability to help achieve the level of competitiveness required by the common market.

4.4 Key factors affecting CSR in Bulgaria

CSR is not performed uniformly across companies in Bulgaria. From the research it was determined that there are three factors determining the differences in scope of the CSR engagement.

- **Ownership structure.** CSR at private companies tends to take more innovative and sophisticated forms. Ownership by multinational investors also has a positive impact on the scope of a company’s CSR engagement. However, the presence of a foreign investor alone is not a guarantee for socially responsible behaviour. Strong ownership structures mean as well less monitoring from shareholders and very often the owner and CEO are one and the same person. The big multinationals are very often following their common CSR policy all around the world. Some of the companies in Bulgaria like Coca Cola for example, are making as of this year their own CSR reports especially for the local activities.

- **Top management commitment.** The interviews established that in Bulgaria the scope of the CSR engagement of a company is a function of the top management interest in and commitment to CSR. The top-down approach is common in the administration of many issues in the Bulgarian companies, and CSR is not an exception. Hence, the positive correlation between personal engagement and a company’s CSR commitment. Throughout the interviews the names of several individual leaders were repeatedly mentioned in the context of key promoters and leaders of CSR in the country (Mr. Ivan Vassilev from TNT and Mr. Sasho Donchev from Overgas).

- **Company size.** In Bulgaria, larger companies tend to have the most visible CSR engagement. In SMEs, CSR is local in scope and occasional in nature. Because of the
strong role of the owner, these firms often manage their societal impact in a more intuitive and informal way than large corporations.

4.5 Regulation of CSR in Bulgaria

At present Corporate Social Responsibility in Bulgaria is not regulated by any specific strategic document (national agenda, guidelines or strategy). Different elements of CSR such as human rights, labor standards, environment and social protection, anti-corruption, are covered by the respective laws and regulations. International standards and Codes of Conduct and Ethics are gaining popularity among the business associations and the business itself. Even though there are no special financial instruments in place to encourage social responsibility of the business in Bulgaria, the legislation provides some tax relieves.

The recent joining of Bulgaria to the EU brought CSR higher in the national agenda. Up to this moment CSR development and promotion was left in the hands of the non-governmental organizations, business associations, international organizations and the business itself. The government institution which took the lead is the Bulgarian Ministry of Labor and Social Policy (MLSP). The Compendium on national public policies on CSR in the European Union (2007) for Bulgaria confirms that “CSR is a highly important issue and a permanent priority in the government policy of the Republic of Bulgaria. In accordance with the European CSR policies, government policy is oriented towards promoting CSR at national level. The targets set are focused on promoting sustainable development, including the aspects of socio-economic development and preserving the environment, as well as creating economic and financial tools for CSR promotion.”

The Director of Euro-integration Directorate at the MLSP is the National Rapporteur at the High Level Panel on CSR within the European Commission. In May 2008 will be the first meeting of the specially established working group on CSR within the Ministry, comprising representatives of all stakeholders, which main objective is to develop National CSR agenda or strategy for Bulgaria. It is expected this strategic document to set the basis of regulated, long-term and strategic development and implementation of CSR issues among the Bulgarian business and society.

During the last years more and more Bulgarian companies have been certified under the international standards for quality of the management systems, health and safety practices,

environmental management, production, etc. Over 3121 companies are certified under ISO 9001 and 117 under the ISO 14001 (environment management system). Two companies have been certified to Social Accountability SA 8000 standard, popular as the CSR standard, ensuring ethical sourcing of goods and services. The international standard for health and safety management systems, have been awarded to 107 companies in Bulgaria. The European Foundation for Quality Management Excellence Model (EFQM) is possessed by 5 companies. Eco-labels of goods and services and so called bio-products are becoming increasingly popular in Bulgaria. Over 107 companies are registered as producers and importers of products and foods based on bio-technologies in the Organic Farming Register of the Ministry of Agriculture and Forestry. “The Federation of Consumers in Bulgaria possesses a Mark, that is granted under licence for marking goods with guaranteed safety and high and stable quality, in accordance with the acting regulations and the Bulgarian State Norms – BDS, branch and company standards, technical specifications, sanitary norms, safety norms and other approved state regulations.”

Fair trade is still new concept for the Bulgarian business. Only one NGO – Association Integra BDS implements projects for promotion of fair trade in Bulgaria. Ten Senses is the only Bulgarian company certified by the International Fair Trade Association.

Codes of conduct in general are gaining ground in Bulgaria, both in terms of individual companies, as well as collective statements of business principles. Codes of ethics are covered in chapter 3.2 Evolution of Business Culture and Business Ethics in Bulgaria.

Local networks of companies committed to apply CSR principles could be considered as a form of regulation and platform for sharing knowledge and experience why and how to do socially responsible business. The UN Global Compact is a voluntary initiative encouraging private sector, civil society structures, trade unions, UN agencies, and other stakeholders to apply ten universal principles for social and environmental responsibility in their daily practices. The Bulgarian Global Compact Network is an informal assembly of more than 130 companies, non governmental organizations and academia engaged in Corporate Social Responsibility who strives to learn from each other, to share experience, to promote CSR and

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64 http://www.consumers-bg.com/engl/sign_e.htm
65 www.unglobalcompact.bg
initiate dialogue or partnerships with other actors such as the government, local authorities, labour organisations, civil society organizations and academia. The Network is administered by the United Nations Development Programme office in Bulgaria.

The business association which has played the most very active role in promoting the idea of the ethical and responsible business, since its launch in 1998, is the Bulgarian Business Leaders Forum (BBLF). BBLF has over 220 members - both Bulgarian and international companies. Its Business Ethics Standard has been accepted by over 1500 companies, and the Anti-Corruption and Education statements influenced the national policy. The Code of Business Ethics and CSR of the major employer’s and public organization - the Confederation of Employers and Industrialists in Bulgaria, is accepted by its 400 individual members and over 6000 members through collective membership of branch associations, regional structures and holdings.

Relations between employees and employers and protection of the employees’ rights in Bulgaria are regulated by the Labour Code, as well as by a number of statutory instruments of secondary legislation. The Constitution of the Republic of Bulgaria and the Labour Code expressly forbid the imposition by employers on employees of any restrictions whatsoever on the basis of race, gender or any other discriminatory grounds. The Labour Code provides the special protection of the employee: duration of the working day and entitlement to rest, labour remuneration, entitlement to leave, health and safety at work, social, welfare and cultural services. Along with the Labour Code, a special law: the Health and Safety at Work Act, also regulates the employer's obligations to ensure health and safety at work. Bulgarian National Labour Inspectorate supervises for violations on the labor standards.

“Although environmental awareness (in Bulgaria) improved in the post-communist era, the state’s lack of administrative strength and fears of unemployment prevented the curtailment of many dangerous practices. Therefore, in the mid-2000s Bulgaria still faces severe environmental problems, such as air pollution from industrial emissions, the inability to filter effluents into rivers, diminishing natural forest cover and damage from air pollution and resulting acid rain, or soil contamination by heavy metals resulting from improper industrial waste disposal.”

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66 UNIDO (2005), “Issue Paper On The State Of Corporate Social Responsibility (CSR) In Central And Eastern Europe (CEE) Special Focus: Bosnia And Herzegovina, Bulgaria, Romania And Serbia”
environment protection. Specific issues like waste management and protection of waters are covered by separate laws.\textsuperscript{67} Special regulation sets the structure and actions of the company in relation to the management of the environment protection activities.\textsuperscript{68} The National Eco-Labeling Scheme is an instrument that allows companies to label and distinguish their product on the market in terms of its environment-friendliness. The National Environmental Management and Audit Scheme is a scheme for organizations accepting to independently assess, improve and report on their progress in the implementation of environmental requirements.\textsuperscript{69}

Many of the companies consider and report their Human Resource or Environment Protection policy which is in compliance of the regulations set by the law as CSR. The reason for that misconception of CSR is the fact that up to 30% of the companies in Bulgaria still operates in “grey” economy, i.e. not complying with the legislation (hiding tax, not covering health and pension of their employees, etc.). The established norms and requirements are widely perceived as an obstacle to business for making profits and the actions of control bodies are regarded as an unnecessary state intervention. To overcome this misconception the Bulgarian Ministry of Labor and Social Policy established in 2006 an award for a socially responsible enterprise. “The purpose is to identify socially responsible attitudes and practices within Bulgarian enterprises that go beyond the requirements of Bulgarian labour legislation, and are introduced voluntarily.”\textsuperscript{70} Another initiative to promote the responsible behavior of the business in Bulgaria is the Bulgarian Business Leaders Forum Annual Awards for Responsible Business\textsuperscript{71}, established in 2003 and awarded in 5 categories. The main objective of the Awards is to give credit to companies with remarkable record in the field of corporate social responsibility and encourage other business leaders to start or further develop socially beneficial activities.

**Financial instruments**

There are no special financial instruments in place in Bulgaria to encourage social responsibility of the business. Few tax relieves are available in the legislation.

\textsuperscript{67} Law on Waters (1999), Law on Waste Management (2003)
\textsuperscript{68} Regulation on the Structure and Actions of the Company in Relation to the Management of the Environment Protection Activities (2003)
\textsuperscript{69} Decree No 61 of the Council of Ministers 12.03.2003, in force since 22.09.2003 am. No 31 of 4.04.2003
\textsuperscript{71} http://www.bblf.bg/projects.php?sub=reward
• Tax exemption for companies hiring people with disabilities
The corporate tax due by companies who employ people with disabilities is written off under art. 178 (1) of the Corporate Income Tax Act.

• Tax relief for companies hiring unemployed persons
Companies hiring unemployed persons under employment contract for minimum of 12 months, are entitled for deduction with an amount equivalent to the remuneration paid for 12 months and the employer’s contributions to social and health security for the first 12 months of the employment. The tax relief is regulated in Art. 177, para 1-4 of the Corporate Income Tax Act.

• Tax exemption on donations
At the moment individual donors have the right to deduct up to 5% of their annual income for donations given to certain categories of organizations, listed in the Personal Income Tax Act (art. 22, para 1) such as legal entities, which are not commercial enterprises, having charity, social, environmental, healthcare, scientific-research goals. If donations are for culture development the reduction is 15% and it could go down up to 50% for donations to the Fund for the Treatment for Children.

Corporate donors enjoy a similar benefit; companies could register their donations as expenses under the Corporate Income Tax Act. “If the sum of all donations is up to 10% of the positive financial result, it is not taxable and could be excluded from the financial result.”72 The institutions to which the donations could be made are listed in the Law. 73

If any of the above-mentioned conditions is not fulfilled (e.g. the recipient is not among the specified categories of organisations, the donor does not have a positive financial result or capital reserves, etc.) or the donation exceeds 10%, then the donation is accounted as an expense. The total expenses for deductible donations may not exceed 65% of the profit.

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73 Art. 31, para 1 (1-17), Corporate Income Tax Act
5. EMPIRICAL STUDY

The data analyzed in the master thesis are collected for the baseline survey on the understanding, experience, attitudes, gaps and challenges in implementing the CSR practices by the Bulgarian business: “CSR within the Bulgarian context”, conducted in the period September-October 2006 and published in February 2007. The author was responsible for the development of the methodology for the research, drafting the questionnaire, training the research company on the content, substance and basic principles of CSR, and conducting some of the detailed interviews with companies CEOs and responsible for CSR managers. The research is ordered by the UN programme for private sector Global Compact and the author as Coordinator of the Bulgarian Global Compact Network (www.unglobalcompact.bg) is allowed to use for its research the full set of data which are not published. The author used as well its own experience collected during its daily work with the private sector in Bulgaria on the issues of CSR.

5.1 Methodology

This report presents and discusses the summarised results of a baseline survey conducted in the period September – October 2006 on the Corporate Social Responsibility in Bulgaria, combining quantitative and qualitative methods. 121 medium-sized and large companies, both with Bulgarian, foreign or mixed ownership structure have been analyzed. The companies surveyed are both public and private, from manufacturing, services, trade, IT and other sectors from all over the country.

Twenty of the companies are members of the Bulgarian Global Compact Network and due to their better knowledge and experience with CSR is used as a control group. The rest of the companies are randomly selected in order to have a nationally representative survey.

<table>
<thead>
<tr>
<th>Criteria for defining SMEs according to the data from the Ministry of Economy and Energy from 2004</th>
<th>Middle enterprises</th>
<th>Large enterprises</th>
</tr>
</thead>
<tbody>
<tr>
<td>Requirement for turnover</td>
<td>from 5 to 15 mln. BGL</td>
<td>above 15 mln. BGL</td>
</tr>
<tr>
<td>Requirement for the number of personnel</td>
<td>from 50 to 250</td>
<td>more than 250</td>
</tr>
<tr>
<td>Number of enterprises</td>
<td>3321</td>
<td>532</td>
</tr>
<tr>
<td>Part of all companies in Bulgaria</td>
<td>1.5%</td>
<td>0.2%</td>
</tr>
</tbody>
</table>

74 UNDP and BCAF (2006), “Corporate Social Responsibility within the Bulgarian Context”
75 www.unglobalcompact.bg
• Research with qualitative methods – this first stage involved one focus group with 8 participants and 20 in-depth interviews with representatives managing corporate social responsibility (CSR) actions in medium-sized and large companies. The aim was to establish the understanding of CSR, the motivations behind it and the ways in which it is practiced, and the constraints and barriers before its development in Bulgaria. The companies interviewed are ones which already have made or showed interest in developing CSR projects and initiatives.

• Quantitative research – conducted by means of direct standardised interviews with Corporate Social Responsibility managers in 121 medium-sized and big companies. Target group: Managers, CEO and people responsible for CSR in the middle and large companies.

The aim of the research is to contribute to the evolution and understanding of Corporate Social Responsibility among the Bulgarian business, government and the society at large.

5.2 Discussion of the Results

This chapter presents the results of the research and is answering the research questions. The author discusses how CSR is used as a Corporate Governance tool by the business in Bulgaria, why it is used as such and who will use CSR as a corporate governance tool in Bulgaria.

5.2.1 How Corporate Social Responsibility is used as a Corporate Governance tool in Bulgaria?

I. Perception of CSR by the business in Bulgaria

The conceptions of CSR differ according to national, social and economic priorities - which are themselves influenced by historical and cultural factors - and according to the different types of social actors that are demanding action on these priorities. Traditionally in the United States for example, CSR has been defined much more in terms of philanthropy and giving. Companies make profits, they pay their tax and then they donate a certain share of the profits to charitable causes or they make a foundation which sponsor different charitable causes and projects all over the world.
The European model is focused on operating the core business in a socially responsible way, complemented by investment in communities for solid business case reasons. CSR is a voluntary commitment and is integrated in the long-term strategy of the company. Several studies prove that there is positive correlation between the level of economic development of the country and the perception and implementation of CSR. The countries which are in transition or new members of European Union are in the early stage of CSR development due to the transitory state of the institutional culture of the business. In Bulgaria a transition is under way from a predominately inward oriented, paternalistic corporate culture towards more outward oriented, socially sensitive and ecologically responsible way of doing business. Unlike countries, old members of EU (countries from Western Europe) where customers and stakeholders are key drivers for CSR in Bulgaria these structures are still weak and the owners and the state or municipality are the major drivers of socially responsible initiatives. “Many companies do not make a clear distinction between giving, sponsorship and socially responsible activities. When a distinction is made it is for the purposes of accounting and not for identifying different levels and focus of company policy.” 76 Even though the number of companies which engage in public-benefit activities has been growing in recent years, the amounts for support are relatively small.

The process for professionalization of the CSR policy and practice in Bulgaria is at an early stage. That’s why CSR is perceived by different companies as part of their corporate Marketing, Communications and Public Relations, or Human Resource policy rather than as a long-term strategy and involvement with the stakeholders.

Positive tendency is that many large and middle-sized companies consider Corporate Social Responsibility as part of the good corporate governance policy, even though up-to-the-moment the promotion and development of CSR and Corporate Governance in Bulgaria has been done separately and by different organizations. The subsidiaries of big multinational companies in Bulgaria like Coca Cola or Bulgarian companies bought by strategic foreign investors like pharmaceutical plant Actavis and open-copper mine Assarel Medet JSCo are the first ones which are starting to incorporate CSR in their long-term strategy and corporate governance model based on the imported models from mother companies.

76 UNDP and BCAF (2006), “Corporate Social Responsibility within the Bulgarian Context”, p. 25
Most of the business leaders rely on their own common sense judgment, which is typically ill informed and often impulsive, driven by the urge of the moment, and thereafter ad hoc rather than strategic. 42% of the surveyed companies decide separately for each proposal, for 30.7% decisions are taken by the general manager/owner upon every concrete case, and only 10.2% of the companies have common CSR corporate policy and budget. This is the reason why 60.2% share the opinion that the social responsibility of the business in Bulgaria is underdeveloped, ad-hoc and not many companies are interested. Positive trend is that 40% of the companies think that even though it is developing area there is a great interest about it.

II. Corporate Social Responsibility as a Corporate Governance Tool – The practice of the business in Bulgaria

Today’s corporations operate in an environment of intense media, investor, regulatory and public scrutiny. The accession to the European Union and the improved business environment in Bulgaria during the recent years has created a significantly more constrained regulatory environment. At the same time, increasing public and stakeholder concern about the social and environmental impacts of business practices is forcing Bulgarian companies to come to terms with a much broader set of interests and expectations.

Generally, companies don’t want to be answerable to stakeholders, especially the ones with strong ownership structures, however the stakeholders (employees, customers, suppliers, communities and society) in practice monitor companies and can force them to adopt certain set of social and environmental values. That’s why they could be in the role of principals in the principal-agent relationship.

The ways how Corporate Social Responsibility is used a Corporate Governance tool will be presented through the relationship between the business enterprises, as agents having relations with different groups of stakeholders being the principals. From the practice of the Bulgarian business the following key groups of principals have been identified:

- Local community and society at large;
- Employees;
- Customers and the public;
- The state.
III. Relations with Local Community and Society at Large

As part of the new business culture the companies in Bulgaria are taking into account the social and environmental impacts of their operations towards the society. 18.2% of the surveyed companies’ associate corporate social responsibility with engagement with social activities supporting the society at large (Annex 2, Graph. 1). “In most cases this means improving the urban environment, PR with a social focus, help for orphans, children and elderly people i.e. where the government lacks the money business comes into support of the community. As a rule there are no long-term strategies and the approach is on a case-by-case basis.”77

Companies share two main views what should be the relationship between the business and the society (See Graph 2 below). The first one, shared by 26.1% of the surveyed firms indicates that companies must participate in all projects in their sector contributing to the society. According to the second view, if the company is profitable it contributes to the development of the society by providing jobs and social contributions and there is no need to do anything extra. The predominant percentage of companies 36.4% shares this view.

Graph 2.

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At the same time 55.7% of the companies participated in the research share the opinion that the successful people should support the other members of the society (Annex 2, Graph 3). And 39.8% believe that the successful people should develop and leave something socially responsible behind them. This attitude comes from the paternalistic corporate culture in Bulgaria, where the owner is considering himself as the “father” of the company responsible for its personnel and his wish to create something to be remembered by.

The relations between the firm and the local community and the society at large could be expressed through programmes for waste management, supporting the social integration, improving the healthcare, urban environment and cultural heritage, educational and internship programmes targeted to the people living in the community where the company operates or to the broader members of the society. The level of the involvement in different CSR programmes is illustrated at Graph 4, Annex 2.

43.8% of the reviewed companies have **programmes for improving the ecological impact from the company’s operations**. Encouraging is that nearly 45% of these companies are Bulgarian, and 47% are middle-sized, with 51 to 100 employees. **Programmes for supporting the social integration** are implemented by 33.9% of the business. Companies with highest level of involvement in social integration initiatives are firms with employees above 250 employees (56.3%) and foreign companies (61.5%). **Programmes for improving the healthcare of targeted groups of stakeholders** are realized by 30.6% of the companies. Highly involved are as well foreign companies and companies with employees above 250 people. At the last few years **programmes for improving the urban infrastructure and environment** are gaining popularity among the business, due to the high public and media impact of such projects. 28.1% of the companies are involved in projects for refurbishing public gardens, renewing streets lightening, planting trees, etc. Subsidiaries of the foreign companies in Bulgaria are implementing the largest number (66.7%) of socially responsible initiatives for renovating the cities. **Programmes for protecting the cultural heritage** are priority for 18.2% of the surveyed companies, with subsidiaries of foreign companies and large companies holding the first places in implementing projects for preserving the local culture.

Due to the need of qualified working force in Bulgaria during the last couple of years, especially in highly specialized sectors, the companies started to invest in **programmes for**...
cooperation and support of the education in their area of business (34.7%) and internship and scholarship programmes (22.3%). The first group is preferred for support by the foreign companies, while internship programmes are implemented mostly by Bulgarian companies.

For 2005, the surveyed companies have invested 46.6% of their funds in socially responsible activities (See Annex 2, Graph 5). The Graph 6, below illustrates clearly the priorities in allocating resources among different social groups:

**Graph 6.**

<table>
<thead>
<tr>
<th>Social Group</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Children in institutions for orphans</td>
<td>52.1%</td>
</tr>
<tr>
<td>Staff</td>
<td>44.6%</td>
</tr>
<tr>
<td>People suffering from diseases and disable people</td>
<td>32.2%</td>
</tr>
<tr>
<td>Children and young people</td>
<td>19.0%</td>
</tr>
<tr>
<td>Elderly people</td>
<td>17.4%</td>
</tr>
<tr>
<td>People in the community in which the company operates</td>
<td>14.9%</td>
</tr>
<tr>
<td>Students studying in the targeted business area</td>
<td>12.4%</td>
</tr>
<tr>
<td>People affected by natural disasters</td>
<td>11.6%</td>
</tr>
<tr>
<td>Clients</td>
<td>10.7%</td>
</tr>
<tr>
<td>The broader members of the society</td>
<td>7.4%</td>
</tr>
<tr>
<td>People living in the region of the company</td>
<td>7.4%</td>
</tr>
<tr>
<td>Others</td>
<td>5.0%</td>
</tr>
<tr>
<td>People affected by corruption</td>
<td>0.8%</td>
</tr>
</tbody>
</table>

7.4% of the socially responsible activities companies target on the broader members of the society. Twice more, 14.9% they focus towards the people in the community (city) in which the company operates and 7.4% towards the people living in the near-by region. Interesting trend is that the small companies with employees between 11 and 50 people and the large firms with over 1000 workers register the highest level of socially responsible activities both towards the local community and the society at large.

**IV. Developing Relations with Employees**

The surveyed representatives of the business in Bulgaria shared that the first and most spread perception of socially responsible business is caring about company staff (20.7%) and their families (See Annex 1, Graph 1). Even though large companies pay attention to their relations
with employees, the exclusive focus upon it is typical of medium-sized companies. Companies in manufacturing and service sector are the ones focusing most on developing their human resources. Foreign companies slightly prevail, with 2%, over the Bulgarian ones.

The relations between the firm and its employees could be expressed by programmes for improving the labor conditions, training and qualification of the personnel, regulations for prohibiting child labor and against discrimination, hiring people with disabilities.

**Plans and programmes for training and qualification of the personnel.** 65.3% of the 121 researched companies have staff support policy by means of qualification and training courses. All large companies with employees between 251 to 1000 people implement programmes for training and qualification of their staff. 69.4% of the companies with employees from 101 to 250 people offer training to their personnel. Companies operating in the sectors of technologies and services organize the highest number of training courses for their staff – respectively 100% and 81%. Foreign companies are leading in providing learning opportunities with 84.6%, followed by Bulgarian firms with 62.6%.

84.3% of the surveyed companies report that they have in place programmes for improving the working conditions. The percentage of large companies having such programmes is higher than the middle-sized ones. Improving the working conditions is priority for the sectors of technologies and services.

**Special regulations prohibiting child labor and discrimination** are available in 56.2% of the companies. It is interesting to note that higher number of middle-sized companies 61.7% implement strict regulations of child labor and discrimination, compared to 56.3% of the large companies. Big firms are the ones which predominantly hire and create conditions for development of people with disabilities – 56.3%, while only 12.8% of the middle-sized companies hire employees with disabilities. The reason for that is that creating working environment for disabled people is associated with higher costs and new corporate culture. Foreign companies have the practice and are more willing to provide employment opportunities for disabled people (61.5%), only 21.2% of the Bulgarian companies have programmes for disadvantaged people. A total of 28.1% of the researched companies have social policy and activities towards people with disabilities.
Employees are the second favorite beneficiary on whom companies target socially responsible activities. 66.1% of the total funds invested during 2005 by the surveyed companies are targeted for social activities towards the employees; only the budget for advertising is higher (See Annex 2, Graph 5). Large companies and firms with foreign or mixed ownership had allocated in 2005 higher budget for social policy and development of their employees than the middle-sized and companies with Bulgarian ownership. The reasons for that are the stronger focus on human capital, availability of funds and well structured Human Resource policy imported from the mother company. For these companies as well the human asset is important part of their good corporate governance, that’s why they are investing in attracting, keeping and training their employees.

Even though the first and most wide-spread perception of socially responsible business is caring about company staff most of the surveyed companies 35.5% invest annually up to BGN 5 000 (about Euro 2.500), only 19% invest up to BGN 50 000 (about Euro 25000) and just 2.5% up to BGN 150 000 (about Euro 75000) per year. The results show that the volume of support is directly correlated with the size of the company. The larger the company the more resources it invests in its HR policy. Companies with mixed ownership or subsidiaries of foreign companies plan higher costs for qualification and social needs of its personnel. Positive tendency is that 50% of the companies which invest up to BGN 5000 and 10% which plan up to BGN 50000 costs for programmes for their employees are middle-sized companies. This is evidence for introducing and improving the social responsibility and corporate governance among growing number of companies, especially middle-sized which are predominant in the Bulgarian economy. 19.3% of the surveyed companies share a common view that good working conditions are in favor of both the business and the employees.

Employees monitor in order to make sure that their labor and human rights are protected, which is a corporate governance tool which complements CSR policy, ensuring that employees’ interests are safeguarded.

V. Relations with Customers and the Public

Customers are important asset of the firm. Companies develop their long-term strategies aiming to attract new and keep loyal their customers and clients as they guarantee the growth potential of the company, its competitiveness and access to resources. Thus customers could
be a driver forcing companies to adopt social and environmental values in its business. As well, the firm sometimes relies on its customers to force its managers to act in a certain way. Customers require transparent and socially responsible behavior from companies and monitor their behaviour, which forces companies to put efforts in developing socially responsible activities and good corporate governance.

In the countries old members of the European Union customers and stakeholders are the key drivers of CSR. In Bulgaria, these structures are still weak. Only 10.7% of the surveyed companies have targeted their socially responsible activities towards their clients. 46.2% of them are foreign companies; only 6% of the Bulgarian companies develop strategies to their customers. The explanation of this big difference is that foreign companies in Bulgaria are introducing general corporate policy and as they are mostly from EU countries, the customer relations are part of their CSR policy and corporate governance. More than 25% has above 250 employees (large companies) while only 8% of the middle-sized companies focus socially responsible activities to their customers. 3.4% of the researched companies define CSR as a responsibility of the company to be fair and loyal to its clients.

At the same time, very high percentage of the companies 62% report that they implement programmes for customers/shareholders/partners. In my opinion, this percent cannot provide true picture of the relations between the firm and its customers as it merges it with shareholders and partners, for which companies generally focus more initiatives. With the EU membership and the modern business culture relations with customers are gaining importance and more companies are focusing programmes and initiatives towards them. At the same time, the customers in Bulgaria are realizing their power as agents who could force companies to behave in a certain way and are becoming more active and sensitive in their consumption. This makes companies to think how to get better to satisfy their customers.

VI. Relations with the State

Traditionally, in Bulgaria the relations with the state (local and central authorities) have important role in the economic development of the country. The results of the survey clearly shows that the business is supporting socially responsible initiatives and projects in areas which the state had failed to support (children in homes, elderly people, urban infrastructure, students, kindergartens, fight with corruption, etc.).
The following paradox exists in Bulgaria – the state consider CSR to be obligation solely of the business while the companies think that the state should provide benefits for CSR as they are supporting socially responsible activities which should have been in first place funded by the government. The business associations and international organizations are trying to create a platform for dialogue between the business and the state so they jointly develop National CSR strategy/agenda. At the end of May 2008, a working group with representatives of the social partners within the Bulgarian Ministry of Labor and Social Policy is starting to draft the first strategy for Corporate Social Responsibility of Bulgaria.

The relations with the state in the survey could be followed by the attitude towards the compliance of the business with the legislation in its area of activity. 69.4% of the reviewed companies implement targeted efforts and measures for complying with the legislation. The relationship with the state is the second most important one for the business, right after the relations with the employees. Positive trend is that companies with employees between 50 and 100 people introduce mechanisms for legislation compliance (78.7%) at nearly the same level as the large companies with employees above 250 people (81.3%).

At the question how would you define CSR, 9.9% of the surveyed companies answer that for them social responsibility is compliance with legislation. This perception is widely spread among the small companies with employees between 11 and 50 people which can’t allocate extra funds to invest in socially responsible activities. In Bulgaria, the local and central authorities are viewed by the business more as partners in CSR activities under Public Private Partnerships and will be analyzed further in Chapter 5.2.3

5.2.2 Why CSR is used as a Corporate Governance tool?

In order to present why Corporate Social Responsibility is used as a corporate governance tool, the results from the survey will be linked to the discussed in the Theoretical part three types of corporate governance mechanisms – legal strategies (standards, rules, entry strategies), economic corporate governance tools (employee monitoring, scarce resources, competition, transparency) and social mechanisms (media and social control, reputation and image). This section presents CSR from the perspective of the firm as principal and uses CSR as a corporate governance tool itself. For example, the firm could use generally accepted ideas about CSR as standards and rules to guide its managers and employees to act in a certain way such as to protect the environment thus reducing the risk of environmental liability.
Social mechanisms

1) Image of the company

Asked to evaluate which effects have been achieved by the socially responsible activities of the company, the respondents ranked first the establishment of **positive image and branding of the company**. 56.8% of the surveyed companies consider it as the most widely spread and desirable effect from their CSR policy (Annex 2, Graph 7). The large companies and firms with mixed ownership report the highest increase in the positive perception of their image as a result of their involvement in socially responsible activities.

Image is the way others (clients, employees, the community, competitors, etc.) perceive your company and its products. Image is important in dealing with the community in which the company works, governmental agencies, lenders and so on.

2) Reputation

36.4% of the reviewed companies indicate **enhancing the reputation of the company’s production** as the second highest effect achieved as a result of the socially responsible policy of the company (Annex 2, Graph 7). It is interesting to note that the number of the Bulgarian companies and middle-sized firms which use CSR as a tool to enhance their reputation is increasing. Company’s reputation is an asset and wealth that gives companies competitive advantages because companies with good reputation will be regarded as reliable, credible, trustworthy and responsible for employees, customers, shareholders and financial markets. Good reputation enhances profitability. As the reputation shows the social evaluation of the public towards the business, it is highly efficient mechanism for social control.

The firm has the difficult task to manage properly the relationships between stakeholder groups and it must consider the interests of each stakeholder group carefully. CSR and public relations integrate into corporate governance to manage the relationships between the firm and its stakeholders to enhance the company reputation. This is the reason why 37.5% of the researched companies consider the media, providing public exposure of their socially responsible activities, as the key partner for the success of a CSR initiative (Annex 2, Graph 8).
Legal strategies

3) Standards
50.4% of the surveyed companies are satisfied by the impact their socially responsible activities had on the stakeholders and the society at large. The percentage is evenly distributed, showing no difference based on the size or ownership structure of the company. In relation to the internal CSR activities, 40.5% of the companies report satisfaction by the effect of the socially responsible policy towards the company staff (See, Graph 9 below). Companies with higher number of employees, which are in position to invest more in their human resources, show as well higher satisfaction of their social policy.

Graph 9.

The largest percentage of the surveyed managers (20.7%) indicate as the main reason for their satisfaction from doing a responsible business the moral contentment that they have fulfilled their fiduciary duty towards the targeted groups of stakeholders.

Compliance to standards (Codes of Conducts, Corporate Governance Codes, ISO 9001, ISO 14001, OHSAS 18001, EFQM, EMAS, SA8000, etc.) is enhancing the CSR policy of the company. Chapter 4.5 “Regulation of CSR in Bulgaria” is presenting the state of play in Bulgaria concerning the introduction of international standards and indicators of CSR implementation.
4) Rules
The rules are mechanisms which require or prohibit specific behaviour ex-ante constraining agents to undertake actions that will harm the principals’ interests and specifying what agents may or may not do. The only result from the questionnaire which could be related to this issue is that 44.6% of the surveyed companies answer that as part of their socially responsible activities have in practice Ethical Codes and/or Anti-corruption rules (Annex 2, Graph 4). These rules are more popular among the middle-sized companies (up to 46.8%) and the companies operating in the trade sector (74%). Companies in the trade business strive to attract and keep loyal clients, get access to new funds, markets and partners, and have a good reputation among their supply-chain so for them doing ethical and responsible business is a competitive advantage. Middle-sized companies are more vulnerable to corruption because they are less powerful, profitable and popular than the large companies. That’s why to prohibit attempts for corruption they are developing and implementing anti-corruption rules and procedures to manage the relations with their partners.

5) Entry strategies
The requirement agents to disclose regularly information about the company performance to the shareholders and other stakeholders which otherwise cannot acquire such information is a typical entry strategy. The companies cannot sell their stocks unless the requested information is provided by the agent. Unfortunately, the research does not provide information about the disclosure policy of the surveyed companies. Analysis of the disclosure of information of the public companies in Bulgaria that have adopted the National Corporate Governance Code is made at Chapter 3.1.4 “Analysis of the Corporate Governance in Bulgaria”.

Economic mechanisms

6) Employee monitoring
The first and most wide-spread perception of CSR among the surveyed companies – caring about staff – is reaffirmed by the evaluation what effects have been achieved due to the socially responsible activities of the company. 54.5% of the respondents access that CSR initiatives has lead to establishing better team spirit and sharing common goals of the company. The importance of this criteria rose by more than 15% for one year (from 38.7% to 54.5%). There is no difference between middle and large companies, as well team building is equally important for Bulgarian and foreign companies.
According to 52.3% of the companies CSR has helped them to become more attractive employer. This criterion registered two-fold increase for one year. Due to the deficit of highly qualified personnel in Bulgaria the companies are using every opportunity to gain competitive advantage in attracting and keeping their employees.

7) Competition
Competition is very important corporate governance mechanism. In order to be competitive companies have to adopt social and environmental values and do business in ethical and reputable way. For 21.6% of the companies, being responsible, lead to expansion of their possibilities for access to local markets, especially for middle-sized companies.
Positive trend is the fact that companies which improves financial results in effect of their CSR initiatives has increased to 28.4% in 2006, compared to 12.3% in 2005.

8) Scarce resources
Scarce resources are effective corporate governance tool as corporations have to compete for them and thus oblige to doing reputable business in order to attract new customers and partners and get access to resources, funds and markets.

26.1% of the surveyed companies find that as a result of the firm CSR activities new clients have been attracted. The results show that for companies, with personnel between 11 and 50 employees, socially responsible behaviour is highly efficient strategy for bringing new customers.

Another strategy for companies to compete for the scarce resources on the market is through attracting new partners in their business. 18.2% of the managers of the middle-sized and large companies’ access that new partners had join as a result of the Corporate Social Responsibility policy of the company. For companies with employees between 11 and 50 people and large firms (above 250 employees) CSR seems to have the highest effect in establishing new partnerships. Both effects from CSR activities though register slight downsize since 2005.

9) Transparency
Transparency is important corporate governance tool which is related to monitoring of the development of the company and disclosure of information. Result of good relationships with the stakeholders and business done in reputable and responsible way is the customer
satisfaction and loyalty to the company and its products. 23.9% of the surveyed companies indicate that CSR activities increased the loyalty of their clients.

5.2.3 Who will use CSR as a Corporate Governance tool in Bulgaria?

1) The State
Traditionally, the state plays very important role both in the development of Corporate Governance and Corporate Social Responsibility in the countries of Central and Eastern Europe.

As shown on Graph 10, 30.7% of the surveyed middle and large companies in Bulgaria have implemented their socially responsible projects in partnerships with the local authorities and municipalities, while only 12.5% partner with the central authorities. Big companies, with more than 250 employees are in better position to initiate and implement public private partnership projects on central and local level due to their financial power and enhanced understanding and focus on CSR.

Graph 10.

Respectively, as it could be concluded from the higher number of socially responsible projects executed in partnerships with the municipality, the level of satisfaction from the cooperation
between the business and the local authorities is higher (27.3%), than the one with the central government only 9.1% (See below, Graph 11). The municipalities are more flexible and willing to implement joint projects in which the business supports areas for which there are not enough funds such as (renewing public gardens, lightening, hospital equipment, school modernization, etc.). As CSR in Bulgaria is “still fragmented, with piecemeal implementation, decisions made mostly by manager for every specific case and not as the outcome of a long-term company policy and analysis of social tendencies”\(^7\), municipal authorities respond more easily and fast on individual projects basis.

Graph 11.

![Graph showing the relationship between partners and satisfaction](image)

Even though the media is the first and most preferred partner that companies would invite to support their CSR initiatives, as they ensure publicity, eight of the other partners that business pointed out are government institutions (ministries, local and municipal authorities, central government). (Annex 2, Table 2) “In the process of disseminating CSR the government institutions can play an important role by creating a favourable environment for the promotion of socially responsible business practices and also for a more active business stance of citizens

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\(^7\) UNDP and BCAF (2006), “Corporate Social Responsibility within the Bulgarian Context”, p. 18
In Bulgaria, the Ministry of Labor and Social Policy took the leading role in formulating the CSR policy. Under its auspices a working group comprising representatives of different social partners (Ministry of Economy and Energy, Ministry of Education and Science, Ministry of Environment and Waters, Ministry of Agriculture and Food, Ministry of Public Administration, business associations, international organizations and NGOs) is starting to develop a national CSR strategy for Bulgaria.

The views of the stakeholders on the role of the state in encouraging CSR practices differ. In one view, the government must play a leading role in CSR promotion and enhancement, by introducing legal requirements, tax incentives, and public-private partnerships. The opposite view, favours the voluntary application of CSR by business, without interference by the state. The intermediate view is that government instead of regulating should focus on creating favourable environment for CSR implementation.

On the question, what will encourage the business in Bulgaria to perform more CSR projects, 72.7% of the surveyed companies answered – amendments in the legislation for establishing tax incentives, and 38% - higher support from the national and local authorities. This leads to the conclusion that middle-sized and large companies in Bulgaria would like the government to be involved in creating favourable environment in order to encourage CSR practices.

2) The Management of the Firm

“In a more globalized, interconnected and competitive world, the way that environmental, social and corporate governance issues are managed is part of companies’ overall management quality needed to compete successfully. Companies that perform better with regard to these issues can increase shareholder value by, for example, properly managing risks, anticipating regulatory action or accessing new markets while at the same time contributing to the sustainable development of the societies in which they operate. Moreover these issues can have a strong impact on reputation and brands, an increasingly important part of company value.”

As discussed previously, the effects which Bulgarian companies achieved as a result of their socially responsible activities are enhancing the company’s reputation, establishing positive

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image of the company’s brands, attracting new clients and partners, increasing customers’ loyalty, broadening the possibilities for access to local markets, enhancing the company’s image as a good employer and the team spirit among the employees, and achieving better financial results.

The firm faces a broader portfolio of risks today, which the traditional corporate governance tools fail to capture such as labor issues, human rights, environmental stewardship and other issues society cares about and which have material impact. The positive management of stakeholder relations results in lower operational risks, fewer law suits, reduced brand risks, increased market opportunities. In other words, CSR is increasingly becoming a factor in risk management and ethical considerations need to be included in the good corporate governance, therefore in the business strategy of the company.

3) The Customers, Local Community and Society at Large
The social and environmental impacts have tangible financial results for companies. Developing strong relationships with key stakeholders can be a source of competitive advantage for the firm. The customers, local community and the society at large are stakeholders that can force companies to consider certain set of social and environmental values, such as what kind of products and services and how it produces them, as their behaviour could impact the image, reputation and share price of the company.

“CSR connects to governance at the values level, determining the boundaries and accountabilities of the company in relation to a broad universe of stakeholders and its social and environmental responsibilities and opportunities.”

4) The Employees
“As a stakeholder group, employees were identified as a key driver of CSR. There is a growing recognition that to produce long term quality and sustained market leadership, and thereby generate shareholder returns, companies must unlock employee motivation. Companies that live a values-based approach can generate employee pride, motivation, and dedication with positive benefits on employee productivity and ultimately financial performance.”

6. CONCLUSIONS

Corporate Social Responsibility is increasingly moving into the board room. Social responsibility connects to governance at values level, making companies accountable to broad range of stakeholders (employees, suppliers, local community, and society at large) and incorporating social and environmental values in their operations in order to manage their relations with these stakeholders that can have impact on the company development. Doing business in ethical and responsible way is slowly but surely becoming part of the new business culture in Bulgaria, according to the results of this research.

The surveyed 121 representatives of middle-sized and large Bulgarian companies acknowledge that in today’s economy they are facing a broader portfolio of risks and they are realizing that CSR, social and environmental risks can have financial impact on the company. That’s why companies should manage their relations with the employees, customers, local community, society at large, the state and its managers. CSR is viewed as leverage for bringing competitive advantages to business enterprises such as enhancing the company’s reputation, reducing brand risks, attracting new clients and partners, increasing customers’ loyalty, widening the access to new markets, enhancing the company’s image as a good employer and the team spirit among the employees, and achieving better financial results.

The purpose of the master thesis was to define how Corporate Social Responsibility is used as Corporate Governance tool in Bulgaria. The additional research questions answered at the paper were: why CSR is used as a Corporate Governance tool in Bulgaria and who will apply CSR as Corporate Governance tool. The recent joining of Bulgaria to the European Union, giving a “push” to the development of both Corporate Governance and Corporate Social Responsibility, makes the practice of the business in Bulgaria interesting and valuable to research, both from local and from regional perspective.

This research found that CSR could be viewed as a principal-agent relationship where business enterprises in general could be either agents, having relations with different groups of principals (stakeholders) and forced by them to act in socially-responsible way, or firms as principals managing relations with different groups of stakeholders (agents). The role depends on the character of the relationship. From the practice of the Bulgarian business the following
key groups of stakeholders have been identified: local community and society at large, employees; customers and the public and the state.

The ways how Corporate Social Responsibility is used a Corporate Governance tool in Bulgaria have been presented through the perspective of stakeholders being the principals and the business enterprises - the agents.

As part of the new business culture the companies in Bulgaria are taking into account the social and environmental impacts of their operations towards the society. 18.2% of the surveyed companies’ associate Corporate Social Responsibility with engagement with social activities supporting the society at large. The relations between the firm and the local community and the society at large in Bulgaria are expressed through programmes for waste management, supporting the social integration, improving the healthcare, urban environment and cultural heritage, educational and internship programmes targeted to the people living in the community where the company operates or to the broader members of the society. Prevailing number of companies participated in the research share the view that the role of the business is to be profitable and thus ensuring jobs and social contributions. At the same time 55.7% of the companies share the opinion that the successful people should support the other members of the society. This reflects the paternalistic corporate culture in Bulgaria.

The other reflection of this paternalistic model, which is characteristic to all countries in the Central and Eastern Europe, is the attitude towards the employees. The surveyed representatives of the business in Bulgaria shared that the first and most spread perception of socially responsible business is caring about company staff (20.7%) and their families. The relations between the firm and its employees are expressed by programmes for improving the labor conditions, training and qualification of the personnel, regulations for prohibiting child labor and against discrimination, hiring people with disabilities.

Proving once again the impact of the business culture on CSR and Corporate Governance, the customers in Bulgaria are weak driving force for socially responsible initiatives. In the countries old members of the European Union customers and stakeholders are the key drivers of CSR. In Bulgaria, only 10.7% of the surveyed companies have targeted their socially responsible activities towards their clients. This is true for the other CEE countries as well.
Traditionally, in Bulgaria and the CEE region the relations with the state (local and central authorities) have important role in the economic development of the country. The results of the survey clearly shows that the business is supporting socially responsible initiatives and projects in areas which the state had failed to support (children in homes, elderly people, urban infrastructure, students, kindergartens, fight with corruption, etc.). The relationship with the state is the second most important one for the business, right after the relations with the employees.

Answering the second research question: Why Corporate Social Responsibility is used as a corporate governance tool, the firm has been viewed as a principal using CSR as a corporate governance tool itself. CSR activities are perceived by Bulgarian business as ways to establish positive image and branding of the company and enhancing the reputation of the firm. The economic corporate governance mechanisms which are considered by the business in Bulgaria are employee monitoring, scarce resources, competition, and transparency. The relevant legal corporate governance tools are the standards, rules and entry strategies all related to compliance of different international labor and environmental standards, introduction of ethical codes and anti-corruption rules and disclosure of information based on the National Corporate Governance Code.

Answering the third research question: Who will use Corporate Social Responsibility as a corporate governance tool the business enterprises again have been viewed as agents which are influenced by different groups of stakeholders – the state, the customers, local community and society at large, the management of the firm and the employees.

“Vanguard companies anticipating these trends will be engaging stakeholders in the identification of their new accountability boundaries and establishing governance systems, structures, processes and policies to provide oversight on these 21st century business issues.”

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ANNEXES

ANNEX 1

1.1 Public companies adherent to the principles of the Corporate Governance Code, approved by BSE-Sofia. (in Alphabetical order)

Advance Invest AD-Sofia
Agria Group Holding AD-Varna
Albena Invest Holding AD-Albena
Alfa Property 1 REIT-Sofia
Balkan AD-Lovech
Billboard AD-Sofia
Bulgarian River Shipping AD-Ruse
Bulgarska Roza-Sevtopolis AD-Kazanlak
Bulvesta Holding AD-Sofia
CB Central Cooperative Bank AD-Sofia
CBA Asset management AD-Veliko Tarnovo
Chimimport AD-Sofia
Doverie United Holding PLC-Sofia
Euroterra Bulgaria AD-Sofia
FIA Bulgaria AD-Sofia
Holding Nov Vek AD-Sofia
Holding Varna A Co-Varna
Industrial Holding Bulgaria PLC-Sofia
Investor.BG AD-Sofia
Katex AD-Kazanlak
Kristera AD-Popovo
Lead & Zinc Complex PLC-Kardzhali
Monbat AD-Sofia
Nash Dom Bulgaria Holding AD-Sofia
Nikrom trabna mebel AD-Lovetch
Odessos Shiprepair Yard AD-Varna
Oil & Gas Exploration & Production AD-Sofia
Orgachim AD-Ruse
Petrol AD-Sofia
Pirinhart AD-Razlog
Serdika Properties REIT-Sofia
Sofia Mel AD-Sofia
Sopharma AD-Sofia
Sopharma Logistics AD-Sofia
Sparky AD-Ruse
Sparky Eltos AD-Lovech
Stara Planina Hold AD-Sofia
Svilosa AD-Svishtov
Synergon Holding AD-Sofia

Source: Bulgarian Stock Exchange
1.2 Bulgarian Public Companies with the Best Corporate Governance

<table>
<thead>
<tr>
<th>Place</th>
<th>Company</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Monbat AD - Sofia</td>
</tr>
<tr>
<td>2.</td>
<td>Bulgarian American Credit Bank</td>
</tr>
<tr>
<td>3.</td>
<td>Euroholding Bulgaria</td>
</tr>
<tr>
<td>4.</td>
<td>Kaolin</td>
</tr>
<tr>
<td>5.</td>
<td>Sopharma AD - Sofia</td>
</tr>
<tr>
<td>6.</td>
<td>Orgachim AD - Ruse</td>
</tr>
<tr>
<td>7.</td>
<td>Industrial Holding Bulgaria PLC - Sofia</td>
</tr>
<tr>
<td>8.</td>
<td>Enemona</td>
</tr>
<tr>
<td>9.</td>
<td>Stara Planina Hold AD - Sofia</td>
</tr>
<tr>
<td>10.</td>
<td>Fair Play Properties</td>
</tr>
</tbody>
</table>

Source: Dnevnik 100, May 2008

ANNEX 2 – Graphics

Graph1.

How would you define a socially-responsible business?

- Cares about staff: 20.5%
- Is committed to social activities that benefit the community: 10.2%
- Has a successful business: 9.1%
- Complies with legislation: 8.0%
- Is fair and loyal to partners and competitors: 6.8%
- Promotes the development of civil society: 4.5%
- Is fair in dealings with clients: 3.4%
- Is active in environmental protection programmes: 3.4%
- Supports projects with a long-term social effect: 3.4%
- Helps improve the social and health situation of the population: 1.1%
- The business is not insulated in economic relations alone: 1.1%
- Supports the education of disadvantaged children: 1.1%
Graph 3.

Which of the following opinions about the successful people, you are sharing?

- The successful people should support the other members of the society 95.7%
- The successful people should leave behind something socially responsible 39.8%
- The successful people owe everything to themselves 3.4%
- No answer 1.1%

Graph 4.

In which activities your company is involved?

- Programmes for improving the labor conditions 84.3%, 14.0%, 1.7%
- Targeted efforts for following the legislation in your business area 69.4%, 28.1%, 2.5%
- Plans and programmes for training and learning of the personnel 68.9%, 31.4%, 2.5%
- Programmes for customer/investor/partner relations 62.0%, 35.5%, 2.5%
- Special regulations for prohibiting child labor and against discrimination 56.2%, 40.5%, 3.3%
- Humanitarian programmes - support by money, clothes, other materials 52.1%, 45.5%, 2.5%
- Ethical Codes and/or Anti-corruption Rules 44.6%, 51.2%, 4.1%
- Rules for improving the ecological impact of the work of the company 43.8%, 53.7%, 2.5%
- Educational programmes in the area of activity 34.7%, 62.8%, 2.5%
- Programmes for supporting the social integration 33.9%, 62.0%, 4.1%
- Programmes for improving the healthcare of targeted groups 30.6%, 64.5%, 5.0%
- Hiring and creating conditions for development of disable people 28.1%, 66.9%, 5.0%
- Programmes for improving the city environment 28.1%, 67.8%, 4.1%
- Participation in working groups for amending the legislation 24.0%, 68.6%, 7.4%
- Internship programmes 22.3%, 75.2%, 2.5%
- Programmes for supporting the cultural heritage 18.2%, 77.7%, 4.1%
- Yes
- No
- No answer
Graph 5. For which areas you have provided funds during the last year?

- Advertising: 77.7%
- Human resource: 66.1%
- Consulting: 47.9%
- Marketing research: 47.1%
- Socially-responsible activities: 46.3%
- PR: 31.4%

Graph 7. What effects were achieved in result of your CSR activities?

- Positive image in 2006: 56.8% Yes, 13.0% No, 29.6% I don't know
- Improved reputation for 2006: 34.1% Yes, 22.7% No, 43.2% I don't know
- Increased clients' loyalty: 23.9% Yes, 29.5% No, 46.6% I don't know
- Attraction of new clients: 26.1% Yes, 29.5% No, 44.4% I don't know
- Attraction of new partners: 18.2% Yes, 37.5% No, 44.3% I don't know
- Possibilities for access to local markets: 21.6% Yes, 38.6% No, 39.7% I don't know
- The company becomes more attractive employer: 52.3% Yes, 10.2% No, 37.5% I don't know
- Better team spirit: 54.5% Yes, 9.1% No, 36.4% I don't know
- Achievement of better financial results: 28.4% Yes, 21.6% No, 50.0% I don't know
Graph 8.  

Who should support a CSR initiative in order to be successful?

- Media: 37.5%
- MNC: 31.8%
- Famous musicians, sportsmen, stars: 28.4%
- Not special support is needed if the company has its own policy: 25.0%
- Famous politicians: 20.5%
- NGOs: 14.8%
- Others: 6.8%

Graph 12.  

What will encourage the business to implement more CSR projects?

- Changes in legislations for tax relieves: 72.7%
- Greater support from the national and local authorities: 38.0%
- Better awareness of the benefits of such activities: 34.7%
- Greater support from the media: 28.9%
- More active NGO sector: 25.6%
- More active business associations: 19.8%
- Looking for support from the society and different organizations: 7.4%
- Customers requiring such responsibility: 3.3%
Table 2. Which organizations, public figures, and institutions, your company would invite as partners in its CSR projects?

<table>
<thead>
<tr>
<th>Organization</th>
<th>Percentage</th>
</tr>
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<tbody>
<tr>
<td>Media</td>
<td>4.5%</td>
</tr>
<tr>
<td>Ministry of Labor</td>
<td>2.3%</td>
</tr>
<tr>
<td>Ministry of Healthcare</td>
<td>2.3%</td>
</tr>
<tr>
<td>Ministry of Ecology</td>
<td>2.3%</td>
</tr>
<tr>
<td>Other partners</td>
<td>2.3%</td>
</tr>
<tr>
<td>Famous musicians and singers</td>
<td>1.1%</td>
</tr>
<tr>
<td>Bulgarian Red Cross</td>
<td>1.1%</td>
</tr>
<tr>
<td>Companies from the same sector</td>
<td>1.1%</td>
</tr>
<tr>
<td>Local authorities</td>
<td>1.1%</td>
</tr>
<tr>
<td>Central authorities</td>
<td>1.1%</td>
</tr>
<tr>
<td>Government</td>
<td>1.1%</td>
</tr>
<tr>
<td>Ministry of Education</td>
<td>1.1%</td>
</tr>
<tr>
<td>Ministry of Culture</td>
<td>1.1%</td>
</tr>
<tr>
<td>No one</td>
<td>2.3%</td>
</tr>
</tbody>
</table>
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