

07_Requirements to Contracting Bonded Loans in Bulgaria_VI[english]

The general legal framework of bonds is set out in the Commercial Code (Chapter 14, Articles 204-218), whereas the special provisions are laid down in the Public Offering of Securities Act (the Securities Act), the Mortgage Bonds Act, the Special Pledges Act, the Credit Institutions Act and others.

It is only the shareholding company (AD in Bulgarian) among all legal forms of companies that is entitled to issue bonds. Neither the Bulgarian legislation nor the EU law gives a legal definition of the term “bond”. Due to this lack of a definition, the legal science views bonds from two main perspectives: as a bonded loan contract and as a security.

The bonded loan is a way for the shareholding company to raise financial resources from external sources. The bond does not come as a substitute for the loan contract given in writing, it only certifies the fact that the contract has been concluded. It is a contract between the shareholding company as the bond issuer and borrower, of the one hand, and all persons who have subscribed to bonds and lent money to the shareholding company to use it on a temporary basis for consideration, of the other part. These persons are referred to as “bondholders”. Any person may conclude a bonded loan with the shareholding company, i.e. any person may subscribe to bonds and become a creditor to the company. The difference between a bondholder and a shareholder is that the bondholder is a creditor who does not take part in the business operations of the company and is not responsible of their effects, while the bondholder’s interests are satisfied before those of the shareholder. However, the shareholding company has to fulfill a number of statutory requirements for the purpose of raising money on the basis of a bonded loan contract.

The prerequisites for the issuance of bonds by a shareholding company through public offering are as follows: at least two years should have elapsed after the entry of the company in the commercial register and two annual financial reports should have been approved by its General Meeting. A bonded loan may be contracted through subscription or other forms of public offering under terms and conditions as prescribed by the law. It should be noted that the Commercial Code regulates the non-public bond issues.

The following procedure applies to the issuance of bonds: the General Shareholders’ Meeting

makes a decision to issue bonds, a power that the law allows to be delegated to the Board of Directors or the Managing Board respectively in accordance with Article 196 of the Commercial Code. The decision on the issuance of bonds specifies the details, such as the type and quantity of bonds to be issued, their face value and issue value, the place, procedure, starting and end date for the subscription of bonds, the term of the bonded loan, and the interest to be paid to bondholders and the ways and time limits for its payment. The company prepares a proposal for the subscription of bonds on the basis of the decision to issue bonds. Any person may subscribe to bonds and the procedure may vary, depending on the choice whether the bonded loan will be issued with or without subscription. The proposal is deemed accepted upon the subscription of a certain number of bonds. The loan is considered to have been contracted where the issue value of all subscribed bonds is fully paid in. The financial resources are raised and bonds are delivered through a bank or an investment intermediary. In accordance with the Commercial Code, the managing body of the shareholding company has to notify the Commercial Register of the bonded loan it has contracted within a month of the deadline for the subscription of bonds. If the deadline expires and the terms and conditions for the loan have not been fulfilled, the money raised is returned to the subscribers together with the interest accrued at the bank in which it has been paid.

In terms of the rights they confer, bonds are either common or preferred. A common bond gives two rights to its holder: the right to receive an amount equal to the face value of the bond at maturity and the right to receive interest, if this is agreed in the contract. A preferred bond gives some additional rights to its holder among the following options: indexed bonds – bonds in which the interest is not fixed but it depends on inflation rates; bonds which entitle their holders to the face value and also to a dividend equal to the one paid out to the shareholders; bonds which provide for the face value, interest and a dividend smaller than the one paid out to the shareholders; bonds with an early payment option.

As stated above, the special requirements to the initial public offering and to the admission of bonds to trading on a regulated market are set out in the Securities Act.

There is a case of public offering of securities where information on the offer of securities is communicated to 100 or more persons or to an indefinite number of persons, regardless of

the form or means of communication, with sufficient details of the terms and conditions of the offer and the securities offered so that investors can make a decision to subscribe or purchase these securities. The offer of securities through an investment intermediary is also deemed to be public offering, as is the case of involvement of a person who is neither an investment intermediary nor a holder in the offering of the securities.

Initial public offering is the offering, under the terms and conditions described above, of securities to be subscribed as offered by their issuer or an investment intermediary authorized by the issuer (subscription) or of securities for initial sale by an investment intermediary on the basis of an underwriting agreement concluded with the issuer.

Initial public offering of secured bonds is allowed if the issuer has concluded an agreement with a trustee of the bondholders. Any issuer of secured bonds which are not subject to public offering and which are to be admitted to trading on a regulated securities market in accordance with the terms and conditions of the issue has to conclude an agreement with the bondholders' trustee within seven days of the first general bondholders' meeting. Trustees are nominated by the issuer. The general bondholders' meeting approves the trustee among at least two nominations made by the issuer. The requirement for an agreement to be concluded with a bondholders' trustee applies also to unsecured bonds provided that this is laid down in the decision to issue a bonded loan and it does not apply to bonds issued in accordance with the Mortgage Bonds Act.

Where he has not concluded an agreement with a trustee of the bondholders, the issuer has to submit to the regulated market on which the bonds are traded and to the Financial Supervision Commission a quarterly report on the observance of the terms and conditions of the bonded loan within 30 days of the end of each quarter or 60 days of the end of each quarter if the issuer is under the obligation to prepare consolidated reports.

It is worth noting that any waiver or restriction of the trustee's liability to bondholders for reasons of negligence is deemed invalid.

The trustee is not liable to the bondholders for any damage they have sustained provided that the trustee's actions or inaction followed a decision of the general shareholders' meeting taken by a majority of more than a half of the votes of the bondholders who have subscribed

to the loan. Only a commercial bank whose seat is within the country or a bank operating in the country through a branch licensed by the Bulgarian National Bank may serve as a trustee of the bondholders. There exist additional restrictions to the trustee and its relationships with the bonded loan issuer.

The debt to the bondholders may be secured with a pledge, a mortgage or another way and the bondholders' trustee is specified as the secured creditor. Businesses may not be pledged to secure the debt to bondholders. Only first pledges and mortgages may be used to secure this debt. Initial public offering of secured bond issues are allowed only after the security has been duly given and registered.

At the time when the security is given or, if the security is given prior to the conclusion of the agreement, immediately after its conclusion and then within the time limits set out in the agreement but at least once a year and upon the occurrence of circumstances which may lead to the conclusion that the value of the security has been reduced by at least five per cent, the trustee bank assigns independent valuers, at the expense of the issuer, to evaluate the pledged or mortgaged assets at market prices.

Against the backdrop of the current economic situation and the lending conditions, one could draw the conclusion that bonded loans are among the most popular financial instruments on developed markets and they tend to become a major way for shareholding companies to raise capital in Bulgaria.