THE SYSTEM OF RESOLUTION/SETTLEMENT OF COMMERCIAL DISPUTES IN THE REPUBLIC OF BULGARIA AS A BUSINESS RISK FACTOR

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Abstarct: *The purpose of this paper is to establish the possible existence of business risk resulting from the legal regulation and other relevant factors to the resolution of commercial disputes in the Republic of Bulgaria. The effectiveness (the lack thereof) of the different commercial disputes resolution/settlement means are analyzed (state courts commercial litigation, arbitration, mediation and others). Historical and some comparative law references are made alongside. A conclusion that the legal regulation and the practical aspects of commercial litigation before the state courts hamper business and represent a serious risk factor. The situation in arbitration although once highly favorable has recently deteriorated. Other ADR have acquired no popularity but at a promotional level. Analysis of other factors also brings negative characteristics thus leading to the general conclusion that the state of the legal regulation and the practice in the resolution/settlement of commercial disputes in Bulgaria represents a serious risk before business.*

1. Significance of the Legal Framework of Resolution/Settlement of Commercial Disputes as a Possible Business Risk Factor

There can be no doubt that the characteristics of the existing means for resolution/settlement of commercial disputes in a given country are of great significance for the successful development of business. Each economic relationship may turn out to be in default at a certain point. In such situation it is of crucial importance whether the legal framework of the respective country and the specialized bodies authorized to resolve/settle a dispute arisen as a result of the lack of fulfillment of economic obligations (or the incorrect fulfillment thereof) are designed and function in a proper manner. An adequate legal regulation and high quality of the judicial (or: equivalent or substituting) process can certainly bring about to a solution of the dispute thus eliminating or avoiding business risks threatening all participants in the respective relationship.

2. Historical Background of the Legal Regulation of Resolution/Settlement of Commercial Disputes in Bulgaria

During the period after the occupation of Bulgaria by the Ottoman Empire was abolished and the establishment of communist rule (between 1878 and

the late 40-ies of 20th century) there were no specialized state bodies authorized to solve commercial disputes. The general courts were competent to do so. During the same period the first arbitrations as a means for settlement of commercial disputes appeared around 1896 within the system of the Bulgarian Chamber of Commerce and Industry ("BCCI")[1], [2]. However arbitration as a dispute settlement means did not acquire momentum since the Law on Civil Procedure[3] of that time would allow the conclusion of arbitration agreements concerning only already existing disputes. That type of regulation was a significant deterring factor to the use arbitration.[4]

During the communist rule (1944-1989) there were no real business relations with the exception of a limited number of such relations with foreign businesses. The entire economic activity inland and abroad was monopolized by the state. That was true both concerning relations with enterprises from other countries pertaining to the Soviet economic block (Council for Mutual Economic Aid) and relations with businesses from countries outside the Soviet bloc. Any business activity conveyed by private persons was strictly prohibited and punishable as per the then existing version of the Penal Code.

The general state courts had little to do with economic relations while there was a specialized complicated system for the resolution of economic disputes through the so called "state arbitrage"[5] Domestic voluntary arbitration was forbidden; arbitration between enterprises of the countries of the Soviet block was compulsory at the court of arbitration at the Chamber of commerce of the defendant.[6]

With regard to the present analysis only a small number of facts from that time are relevant. In 1988 a Law on International Commercial Arbitration ("LICA") was adopted by the communist National Assembly. This is one of the first laws adopted after the UNCIRAL Model-law (1986), and the first one adopted by a sovereign state.[7] The same law is in effect today (with certain changes and significantly broadened scope of application).[8] In the meantime

[1] The name of the institution at that time was Commercial-Industrial Chamber.

[2] For the historical development of Arbitration in Bulgaria see Solemn reports of the President of the Court of Arbitration at the BCCI dedicated on the 50th and 60th anniversaries of the restoration of arbitration activity after World War 2 (Sofia, BCCI, 2003, 2013). A special historical research underlying the reports was committed by the current president of BCCI Mr. Tzvetan Simeonov.

[3] Civil Procedure Act (Закон за гражданското съдопроизводство - 1892-1952).

[4] The situation in other European countries at that time was not much different.

[5] The state arbitrages were specialized public jurisdictional bodies which were situated outside the system of the state courts. Those bodies are significantly different from voluntary arbitration.

[6] This international competence was set up by a number of international treaties the last and most important of which is the so called Moscow convention of 1972 signed by 8 countries pertaining to the Soviet Bloc.

[7] Before that laws after the UNCITRAL Model-law on arbitration were adopted by some of the US and Canada states.

[8] Initially the law concerned only international commercial arbitration while today this is the general law on arbitration in Bulgaria, regulating both international and domestic, and commercial and non-commercial arbitration, despite its somewhat misleading title.

Bulgaria had joined the so called "New York Convention", "The European Convention on Commercial Arbitration" and later ICSID.[9]

The end of the 80-ies of the previous century was marked by dramatic political and economic changes not only in Bulgaria, but in all countries from the Soviet bloc which quite unexpectedly collapsed in a spectacular way. Bulgaria took a way to democratic rule, open society and free market economy.

As a result of the above mentioned dramatic political and economic changes commercial law was reintroduced.[10] The constitutional text which confers the resolution of legal disputes only to state courts broadened the latter's jurisdiction in a similarly dramatic manner[11] and brought about the abolishment of the existing system of state arbitrages that had had jurisdiction on almost all economic disputes until that moment.

The new demand related to dispute resolution was addressed by a sequence of endeavors to improve the functioning of the state court system and the encouragement of the use of arbitration and other alternative dispute settlement means. These attempts for improvement of the means and process of resolution/settlement of commercial disputes will be the center of focus in the following presentation.

3. Legal Regulation of Commercial Disputes Resolution through the State Court System

The adjustment of the state court system to the resolution of commercial disputes can be traced in several directions:

3.1. The first line is to be found in the general changes in the structure and functioning of the system of civil litigation.[12]

In the period after 1989 one may see a major source of change resulting from the constitutional prescription that all legal disputes are to be solved by state courts. Apart from that the current Constitution nominates different levels of courts with names that pre-suppose certain procedural characteristic[13].

As it was mentioned as a result of constitutional requirements the specialized economic jurisdictions (the state arbitrages) which represented a

[9] Bulgaria joined the ICSID Convention much later.

[10] A new Commercial law was adopted in 1991 after the previous one had been abrogated as a "remnant of decadent bourgeois economic relations" in 1951.

[11] Pursuant to art. 119 of the New Constitution (adopted in 1991) only the courts are competent to solve legal disputes.

[12] Commercial litigation is a major part of civil litigation. With certain stipulation I am going to treat the existing bankruptcy procedures as relevant to commercial dispute settlement and, more importantly – as a serious factor influencing business risk.

[13] The Constitution nominates regional, district and appellate courts, as well as A Supreme Court of Cassation. It is evident that the last two names are closely related to certain important procedural characteristics, no matter how controversial that may be.

highly organized and comparatively well functioning jurisdictional system were abolished.

It took some time after the adoption of the Constitution until the first significant change in civil procedure was introduced by an amendment of the then existing CPC at the end of 1999. As a result the existing functional competence of the courts (highly effective but adopted in communist times[14]) was replaced by an out-dated three instance system. The so called reform was not adjusted to the treatment of different types of disputes and brought about an extremely burdensome and clumsy procedure that in no way facilitated the resolution of commercial disputes.

3.2. An extended debate about the necessity of special approach to the resolution of commercial disputes occurred in the course of several years. It was debated whether specialized commercial courts,[15] or specialized divisions at the existing courts should be set up. Also, the introduction of specialized procedure for resolution of commercial disputes was discussed broadly.

The discussions did not bring about but to the formation of a separate Commercial Bench of the Supreme Court of Cassation. All other ideas were abandoned.[16]

In 2007 a new Civil Procedure Code ("CPC") was adopted (effective as of March 1, 2008). The new CPC provided for a special adversarial procedure for resolution of commercial disputes (art. 365 and the following).

3.2.1. The specialized procedure is applicable before district courts as first instance[17] only when the value of the claim is over 25 000 levs[18]. If the value of the claim is lower than that sum the same commercial disputes are to be treated by a regional court as first instance. The regional courts however apply the general civil litigation procedure instead of the special procedure for treatment of commercial disputes (Argument from art. 365 with relation to art. 104, para 4 of the CPC). This approach clearly demonstrates that the treatment of commercial disputes under the current regulation is dependent only on quantitative measurements, i.e. the same dispute is liable to treatment with different procedures dependent only on the value of the claim.[19]

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[14] Being a vocal critic of communist and any other totalitarian rule I cannot hold back my criticism against senseless changes of positive phenomena only because they were introduced in communist times.

[15] The Constitution allows the formation of specialized courts (art. 119, para 2). Under different programs serous financial and organizational means were consumed. The experience of a number of European countries (such as Belgium, Spain and others was studied.

[16] In countries with similar historical background the so called state arbitrages were turned into specialized economic and administrative courts (Russian Federation, Ukraine and others) and the results of their functioning has been reported as relatively satisfactory.

[17] These represent the second level in the vertical structure of the existing judicial system.

[18] Which is the equivalent of approximately 12 500 Euro (or 13 960 USD).

[19] The CPC uses a simple trick to undervalue a claim. Whenever there is joinder of claims the total value of all claims is not taken into account for the purposes of venue and application of the special commercial litigation procedure. This absurd solution also strongly affects the availability of cassation procedure to a certain case (see art. 69 and 72, para 1 of CPC). The abrogated CPC provided that in case of joinder of

3.2.2. As a matter of fact the specialized procedure for treatment of commercial disputes only slightly differs from the general procedure which in itself is highly formal and burdensome (as shown below).

- A characteristic feature of the commercial disputes procedure is related to the double exchange of statements and referral to evidence between the parties before the court sets up an open hearing. This is a positive feature in itself. A number of existing serious problems concerning delivery of notices and notifications and other organizational aspects of the procedure override the advantages of the double exchange almost in full. In reality the exchange of statements and presentation of evidence takes months on end.

- The procedure provides for treatment of a case without open hearings. This however is only an option, dependent on the parties' wish, and to my knowledge, it is hardly ever used.

- The procedure provides a requirement that the claimant present a provisional account of the amount of the claim. This was introduced as facilitation aimed at the avoidance of unnecessary use of experts' opinions.

- Finally, the deadline provided for a reply to the statement of claims is set to 2 weeks from the date of the delivery.

It is totally unnecessary to explain that 2 weeks' time is highly insufficient for the preparation of a reply to the statement of claim, especially in high profile cases.[20]

3.3. As a matter of fact nothing in the special procedure is really specific and outlined as to accommodate the specificities of commercial disputes. At the same time as default rules the rules of the general procedure are applicable and namely these characteristics determine the final outlook of commercial disputes solving by the state courts.

3.3.1. On its turn the general procedure introduced by the new CPC is highly oriented towards preclusion of both procedural and substantial rights for the sake of speedy completion of the separate proceedings.

If the parties to any dispute fail to introduce relevant facts that might have been known to them at a very early stage of the procedure they lose the right to do that later. After the short deadlines for introduction of facts and relevant evidence the parties may refer only to newly arisen facts and the respective evidence. In realty this means that if a party fails to comply with the short deadlines it will lose the case on the merits even though its position has merits. There is a similar situation if a party introduces a forged document or a document containing untrue information. If the opposing party fails to challenge the document immediately upon its presentation it loses the right to

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claims the value of the claim is equal to the sum of the values of all separate claims. There is no such provision in the present CPC.

[20] In many cases of disputes related to procurement disputes only choosing an appropriate legal counsel takes much longer time

do that and the document shall be used by the court upon deciding on the merits of the case.

3.3.2. A major inadequacy of the new CPC is related to the fact that although it was adopted in 2007 it barely contains any regulation of the use of electronic means of communication.[21]

3.3.3. Commercial disputes, no matter if they are treated following the general procedure (when the value of the claim exceeds 20 000 leva| or following the specialized procedure (if the value of the claim is over 25 000 leva) are liable to 3 instance procedure.[22]

These are only some examples of how formalistic and unfriendly towards the parties the procedure is.

The general procedure itself is three-instance for the major part of cases[23]. The procedures before all instances, though claiming to be aimed at expedient solution of the cases are complicated, lead to considerable delays that result from characteristics of the legal regulation.[24]

The present paper does not (and due to volume restrictions - cannot) contain thorough and complete analysis of the general and the specific rules concerning the resolution of commercial disputes. Rather it is aimed at establishing whether the current civil litigation procedure before the state courts in Bulgaria provide adequate and timely protection of the rights of businesses and whether it represents a shield against business risks related to the existence of disputes between enterprises.

Apart from a few courts in larger cities the ordinary first instance courts do not dispose of organizational potential to have specialized panels for treating of commercial disputes. That is partly true when smaller district courts treat such cases as a second instance following the general procedure. This further deprives commercial disputes of proper treatment.

Even only the brief look at the procedures that was made so far gives a negative answer: neither the general nor the specific procedure under the current CPC of Bulgaria are adapted to ensure expedient and at the same time just and rightful resolution of commercial disputes.

The situation is quite different in some business friendly developed countries like Germany[25], France[26], Belgium[27], etc.

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[21] A joke says that one may study the history of communication means through the texts of the new CPC which provides for the use of telex, telegrams and other such means long forgotten.

[22] As a matter of fact the procedure provides for 5 instances – the Cassation instance court may revert a case for a second treatment by the court of appeal; afterwards a second treatment by the Court of cassation is possible.

[23] Commercial cases with value of the claim lower than 20 000 leva (around 10 000 Euro, 8 500 USD) are not eligible for cassation review.

[24] Delays and other defects that are due to organizational reasons or bad practices will be shown later in the presentation.

[25] In Germany the general courts resolve commercial cases. According to a study the major part of commercial cases end up in 8.2 months, and less than 20% take more than a year to be resolved – see Global Legal Insights, Litigation and Dispute Resolution, 2016.

3.4. The institute of class actions was introduced with the CPC of 2008[28]. So far there have been no reports that decisions on serious cases have been reached.

3.5. The new CPC introduced a procedure for issuing of a court order that may directly serve as a title for forced execution. This procedure has been sharply criticized, very low results have been reported. It is widely shared that this procedure is of no special use for business relations.[29]

3.6. Apart from the state of the legal regulation other characteristics of the legal framework have serious influence over the effectiveness of the state courts delivery of justice in commercial cases.

The public opinion of the independence state courts in Bulgaria is very low. In a survey commissioned by the European Commission in 2017 only 28% of the respondents give a positive assessment of the judicial system while the average figure for all 28 European Union countries is 56%.[30] In another recent poll conveyed by the Institute of Modern Politics (November, 2016) 78% of the respondents qualify the work of the state courts system as ineffective, 2% are of the opinion that it is effective and 20% qualify it as neither effective nor ineffective.[31]

A major problem is related to the fact that the prevailing part of Supreme Court justices never got serious training in commercial law.[32] Without sufficient training the judges and justices got oriented towards highly formalistic application of the laws observing the literal text, failing to grasp the real meaning and the depth of the disputes often not fully realizing the economic aspects thereof. This unfortunately has been transmitted to the younger generations of judges. The reality offers a lot of unacceptable decisions including so called "interpretative decisions" [33] One has to stress on the fact that many of the interpretative decisions are made against numerous dissenting opinions.

Suspicion of corruption is widely spread[34],[35].

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[26] Special Commercial Courts exist in France (Tribunaux de Commerce), Delcade SAS Interbureau. Most cases are solved in 1-2 years, and – if appealed – in another 1-2 years.

[27] There are specialized Commercial Courts before which most cases end up within a year (information personally obtained during a professional visit to Belgium).

[28] See – Чернев, С. Прозиводство по колективни искове, списание „Труд и право", бр. бр. 9 и 10, 2008 г.

[29] Корнезов, Л., Гражданско съдопроизводство: Съдебни и несъдебни производства, София 2010, стр. 182 и сл.; Чернев, С. Заповедно производство, изд. Сиби, 2012 г.

[30] See Flasheurobarometer 447, January 2017.

[31] The results were presented in TV 3 and concern the whole judicial system not only civil litigation.

[32] A serous part of them was trained under communism, when the economic relations differed from commercial relations immensely.

[33] Decisions with compulsory effect to lower courts issued by the commercial or the civil benches of the Supreme Court of Cassation. A number of such decisions can be pointed out see – Interpretative decision No 3/2013, No 5/2012 and others.

[34] An enormous scandal with direct accusation of corruption broke out when in 2014 the French ambassador in Bulgaria – his excellence Xavier de Laper Kaban openly accused Sofia City Court of Corruption practices in a bankruptcy case using the phrase "there are rotten apples in the Bulgarian Court

4. The Use of Arbitration in Commercial Disputes Settlement

As it was said earlier under communist rule the use of arbitration in the traditional sense (as a voluntarily jurisdiction used by parties to a dispute to derogate state jurisdiction over civil cases) was significantly restricted[36]. At the same time (although in its shape as compulsory tool both in domestic and international arbitration between enterprises within the bloc) the characteristics and the essence of this jurisdictional tool were widely popular. The popularity of arbitration in economic relations between state-owned enterprises made the transition to the use of arbitration in free business relations comparatively easy.[37]

On the eve of the transition Bulgaria had a highly modern law on arbitration (LICA) whose application had to be extended to domestic arbitration and this was achieved through a series of amendments. In general the legal regulation reform must be considered as completed by 1993[38]. Later there were major improvements in 2001[39] as a result of which domestic arbitration was finally made available to state entities (ministries, agencies and municipal bodies as well as other entities subsidized by state and local budgets) and in 2002[40] when control over arbitral awards was set up as a one instance procedure before the Supreme Court of Cassation and nullity of arbitral awards was abandoned – only setting aside was provided.

At that time the legal regulation of arbitration can be assessed as highly successful and favorable for arbitration. That was a time when arbitration in Bulgaria thrived – the leading arbitration institution – the Court of Arbitration at the BCCI was treating between 600 and 800[41] cases per year (which attributed it a leading position among arbitrations of Central and Eastern Europe). Other arbitration institutions appeared and started treating cases.[42] One of the reasons for the extended use of arbitration (apart an economic crisis which developed after 2008) was the inadequate state of the state court

System" – see newspaper Capital of 05.12.2014. A case of investment arbitration pending against the Bulgarian state at the ICSID court in Washington DC – VR 2000 v/s Bulgaria contains similar accusations. Earlier (during the 90-ies) such accusations were related to the Commercial registry activity of the courts.

[35] Publications of electronic edition Club Z (2016) show index of corruption of the judicial system in Bulgaria 41 (out of 100). Data concerning former Soviet republics and other socialist countries are similar. See the Annual Corruption Assessment Report: State Capture Unplugged: Countering Administrative and Political Corruption in Bulgaria – Center for the Study of Democracy, 2016 (at http://www.csd.bg)

[36] Arbitration was not applicable in domestic cases, while the use of arbitration in disputes between enterprises from countries pertaining to the communist bloc was made compulsory by the Moscow convention.

[37] In some cases even mechanical – existing clauses of contracts from communist times were mechanically reproduced in contracts of former state-owned enterprises transformed into commercial entities.

[38] Official Gazette No 93/1993

[39] Official Gazette No 38/2001

[40] Official Gazette No 102/2002

[41] Both domestic and international

[42] See electronic site http/wwwlex.bg

system and in particular the low quality of the highly controversial new CPC. While the normal treatment of a case before the state courts usually takes a number of years (4 to 8 at least) the number of arbitrations concluded with a final award within a year, year and a half exceeds 75%[43].

There was one feature of the legal regulation which had always provoked fears of abuse: the LICA does not provide and special requirements for the establishment of an arbitral institution. In practice anybody and any formation could nominate itself as an arbitral institution and start delivering justice. In the last 4-5 years a serious number of complaints of abuse of arbitration appeared. Numerous persons complain that arbitral awards were issued against them as a result of arbitrations that probably never happened and forced execution based on such awards was started and carried out. They only learned about the respective arbitration cases at the phase when their property was arrested and they were invited to pay.

If a more serious analysis be made the pointed peculiarity of the legal regulation of arbitration would be qualified only as a minor factor leading to the abuses cited. First of all numerous uncontrolled credit companies exist offering credits at extremely burdensome conditions. Such credit companies usually form their own debt collection companies and the latter start up arbitral institutions. Arbitration clauses are included in General conditions (usually undisputed and in very small letters). The situation is similar with other types of companies offering services to numerous customers. At the same time under the CPC a forced execution may be started against a person without the latter being informed beforehand.

The abuse is not attributable only to the regulation of arbitration but to the absolute lack of control by competent bodies and their insufficient functioning (Finance and Bank control agencies, Consumer Protection Commission, Prosecutor's Office and others).

In the beginning of 2017[44] a reform in the regulation of arbitration was carried out as a result of which arbitration in consumer cases was practically excluded. The reformers however lacked sufficient knowledge about arbitration and although their intention was good and acceptable, the reality of the texts puts a serious threat before arbitration and seriously deteriorates the quality of the regulation thus posing a serious threat to the use of arbitration in general[45], [46].

[43] Own information obtained as a result of my work as President of the CA at the BCCI (2000-2014).
[44] Official Gazette No 8/2017. Certain texts from the CPC (art. 19), from the LICA and from the Consumer protection act were amended or added.
[45] The current legal regulation puts threats concerning the participation of international arbitrators in arbitration in Bulgaria, may lead to the exclusion of the use of arbitration ad hoc, etc. The volume of the paper does not allow for analysis of the particular technicalities.
[46] Similar processes of abuse are reported in other Eastern and Central European counties – see Jukova, G., Arbitration Institutions: Establishment, Attributes, Regulation, Supervision in International Arbitration Law Review, 2016, vol. 19, issue 4.

5. Use of Other ADR in Commercial Disputes Settlement

There was serious promotional activity for the use of conciliation, mediation and so on. Serious organizational and financial resources were engaged. As a result a Mediation act was adopted in 2004 (amended in 2007 in relation to Bulgaria's entry into the EU, and, finally amended in coordination with a European Directive in 2011).

At the moment ADR are taught in 3-4 universities and some institutions offer teaching courses.

The reality (similarly to the situation in other European countries)[47], [48] is that few mediations take place in reality. There are no serious statistical data but it is broadly accepted that mediation has not acquired momentum as a dispute settlement tool in Bulgaria. The law itself concerns only one ADR - mediation – other ADR remain practically unrecognized at a legal level.

6. Conclusion

6.1. The analysis contained in the present paper leads to a conclusion that the state courts in Bulgaria do not offer adequate protection of commercial interest due to shortcomings of the legal regulation, the existence of certain organizational deficiencies, a lack of adequate performance on behalf of the judges and justices involved in the process. The negative characteristics are enhanced by serious suspicions and open accusations of corruption in the judicial system.

6.2. Despite strong positive tradition in arbitration dating far back in time from the end of 19th century recent cases of abuse and a dubious attempt to overcome such abuse at legislative level pose a serious challenge before the use of arbitration as a tool for the settlement of commercial disputes.

6.3. The use of mediation and other ADR is at rudimentary level, despite the fact that awareness of this tool has considerably increased as a result of promotional efforts and some legislative attempts (although with uncertain practical effect).

6.4. The general conclusion is that the legal framework and the legal environment related to the resolution/settlement of commercial disputes is far from satisfactory which represents a serious deterring factor before foreign investment and put business at a serious risk.

The subsequent surveillance reports issued as a result of the monitoring mechanism of the European Commission and the results public opinion polls

[47] In a highly controversial move Italy has introduced compulsory mediation.

[48] This happens if certain mediation centers get financial support and only while there is such support. Apart from that a number of centers are situated with some of the courts. It is natural if court directs the parties to a dispute to mediation that the parties would oblige and go through mediation – see Chernev, S. - Annual reports before European group on arbitration – 2013, 2014, etc.

reflect the above conclusions about the state of the judicial system in Bulgaria[49].

[49] See note 30 above.