

## ANNUAL TRANSPARENCY REPORT OF BCRA FOR THE YEAR OF 2019

This report is published in accordance with the requirements of Annex I, Section E, part III in the Regulation (EC) No. 1060/2009 of 16 September 2009 (the Regulation) and Art. 6 of the Internal Rules for the identification, management and disclosure of conflicts of interests of „BCRA – CREDIT RATING AGENCY” AD (BCRA) and includes the business activity of the Agency in 2019.

### 1. Legal status, ownership and management of BCRA in 2019

BCRA is a private company established as a joint-stock company in 2002. The registration of the Company domicile is in Sofia, 95, Hristo and Evlogi Georgievi Blvd., floor 1, apt. 1. The Company does not have any affiliates registered nor any subsidiaries. The main activity of BCRA is in the area of elaboration of creditworthiness analyses and issuing credit ratings to companies and institutions, including trade companies and enterprises, financial and credit institutions, municipalities, countries, etc.

During 2019, there were no changes in the legal status and the ownership structure. No affiliates or subsidiaries were registered. There were no changes in the shareholding structure of BCRA. The agency's equity as of 31.12.2019 was BGN 50 000 with the following shareholders:

- a) Christo Mihailovsky -57,30 %
- b) Corporate government EOOD – 37,96%
- c) Sonya Sofronova – 4,74%

#### Shareholders General Meeting (SGM)

General competences of the GSM are:

- a) Amends and supplements the by-laws;
- b) Takes a decision for increase/decrease of the capital;
- c) Appoints and discharge the members of the Board of directors;
- d) appoints and dismisses the chartered accountants;
- e) Approves the annual financial statements and takes a decision for the distribution of the profit.

SGM consists of all shareholders of the credit rating agency, notwithstanding of the fact whether the shares are paid off. The meetings of the SGM are convoked by the Chair of the Board of directors and a shareholder is participating in person or through representative who is not obligatory to be a shareholder. The members of the Board of directors may participate in a shareholders' meeting, but they have a voting right only if they possess shares from the capital.

## Board of directors (BD)

The obligation of board of directors is to guarantee:

- a) The independence of the activity of the Agency from any political and/or economic influence and restrictions;
- b) The execution of the requirements of the legal norms regulating the activity of the rating agencies, and the establishment of an adequate internal control system;
- c) The adoption of written procedures for the identification, management and disclosure of conflict of interests in the Agency, and the control over their execution.

The Board of Directors has sessions at least once every three months. The members of the Board of Directors have equal rights and obligations, irrespective of the internal allocation of the functions between them, and irrespective of the management rights granted to the Executive Director. Each member is able to call an emergency meeting of the Board of Directors. Various meetings may also be convened at the suggestion of each member of the BD. The meetings of the BD are considered for regular only in case that half of the members of the Board of Directors are present or represented by another member thereof. For all meetings of the BD, minutes shall be kept and agenda as well, the discussions held and the decisions taken on the relevant items on the agenda.

During 2019, the following changes in the members of the BD were executed.

- Mrs. Mariana Atanasova Asenova was replaced by Mrs. Tzvetanka Donkova Kroumova;
- Mrs. Jasmina Kirilova Koleva-Petrunova was replaced by Mr. Emil Rumenov Savov.

As of the end of 2019 the Board of Directors has the following composition:

1. TZVETANKA DONKOVA KROUMOVA – Chair of the Board of Directors for BCRA;
2. KATERINA DOBREVA MIHAILOVSKA – Vice Chair of the Board of Directors for BCRA;
3. CHRISTO ILARIONOV MIHAILOVSKY – CEO of the Board of Directors for BCRA;
4. EMIL RUMENOV SAVOV –Member of the Board of Directors for BCRA.

Notwithstanding of the changes in the members of the Board of Directors in 2019, the allocation of their specific assignments remains the same as before. Mrs. Jasmina Koleva-Petrunov (till October 2019)/Mr. Emil Savov (from October 2019) is in charge of the development of BCRA's credit rating policy and methodologies, as well as monitors the effectiveness of the internal quality control system of BCRA in relation to credit rating activities. Mrs. Mariana Asenova, professor of Economics at the Sofia University (till October 2019)/ Mrs. Tzvetanka Kroumova (from October 2019) performs the function of Compliance Supervisor. The members of the BD do not participate in the process of elaboration and assignment of credit ratings.

Mr. Kiril Grigorov, Ph. D. in Economics, serves as the company's Procurator.

## **2. Rating process**

### a) Rating Committee (RC)

BCRA's rating committee comprises of employees of the agency who possess the necessary expertise and experience. Shareholders, employees with supporting functions and employees who are responsible for the review or business development do not take part in the RC. The RC elects a Chairman among its members. Also, in a RC meeting do not take part persons which owns shares of

the rated organization, which have relatives who have working for or dependent in some way by the rated organization. The Chairman makes an updated list of members of the RC, the secretary is responsible for producing the minutes from the meetings of the RC. The (lead) financial analyst reporting to the RC is assigned for a secretary. The decisions of the RC for assigning credit ratings are taken after a detailed discussion and unanimously by all members. Individual analysts at BCRA are not able to assign credit ratings independently. The members of the RC have equal rights and obligations, irrespective of the occupied positions/assigned functions in the Agency.

#### b) Methodologies

BCRA publicly discloses its methodologies, models and key rating assumptions used in the whole credit rating process. Before any changes in the methodologies can come into force, those are published and there is a public consultation period at least a month.

In 2019 changes were made in the Sovereign Rating Methodology<sup>1</sup>. On 11<sup>th</sup> November 2019 the updated version of the methodology came into force. The main changes in the Sovereign Rating Methodology aimed to achieve greater transparency by providing clearer and more detailed information about BCRA's analytical approach. The analysis continues conditionally to be divided into four sections, however, their names and subsections have been slightly modified. Some terminological clarifications and modifications also were made. These changes generally did not affect the underlying assumptions or key rating criteria of the previous methodology.

#### c) Code of Professional Conduct (Code of BCRA)

BCRA operates in compliance with Code of Professional Conduct (the Code), adopted in 2006 and last updated in May 2014<sup>2</sup>. BCRA respects and applies all the points that are part of the current Code of Professional Conduct. The purpose of the Code is to facilitate the transparency of the process of awarding credit ratings.

#### d) Withdrawn credit ratings

Assignment of a credit rating shows the current opinion of the agency for the creditworthiness of the rated entity, while withdrawal of a credit rating is an act of its revocation. Withdrawal of a credit rating is made by a decision of the BCRA Rating Committee and is denoted by the symbol (or) or "w" respectively in the Bulgarian and English versions of the rating. Withdrawal of a credit rating is made by a decision of the BCRA Rating Committee and is denoted by the symbol "o" or "w" respectively in the Bulgarian and English versions of the rating. BCRA announces the withdrawal of the credit rating and the rationale released includes the reasons for the decision.

During 2019, BCRA – Credit Rating Agency withdrew the assigned ratings to the following entities:

- **Piraeus Bank Bulgaria AD** - *withdrawn in June 2019<sup>3</sup>. The decision was taken because of the expiration of rating validity;*
- **ZAD OZK Insurance AD** – *withdrawn in December 2019<sup>4</sup>. The decision was taken because the maintenance of the rating does not balance the expenses of BCRA with regard to the update and monitoring processes;*

<sup>1</sup> The updated methodology is available on: [https://www.bcra-bg.com/files/Sovereign\\_Methodology\\_2019\\_en.pdf](https://www.bcra-bg.com/files/Sovereign_Methodology_2019_en.pdf)

<sup>2</sup> The updated version of the Code is available at: [https://www.bcra-bg.com/files/code\\_of\\_conduct\\_en.pdf](https://www.bcra-bg.com/files/code_of_conduct_en.pdf)

<sup>3</sup> The full rationale is available at: [https://www.bcra-bg.com/files/rating\\_piraeus\\_withdrawal\\_jun\\_2019\\_en.pdf](https://www.bcra-bg.com/files/rating_piraeus_withdrawal_jun_2019_en.pdf)

- **Municipality of Yambol** – withdrawn in December 2019<sup>5</sup>. The decision was taken because of the termination of the agreement for assigning of credit rating.

### 3. CRA Staff

Each credit rating is elaborated by a team of financial and/or economic analysts selected specifically for this engagement. The team is managed by a lead financial/economic analyst and includes one or two more financial/ economic analysts depending on the type of the rated entity. The role of the analysts is to draw a complete and clear picture of the state of the rated entity and of the risk factors which may influence its future development. During the working process, the analysts are obliged to collect the most recent and reliable information available. Their duty is to double check the collected information against various sources, which are made clear in the report.

The work of analysts is focused on the assessment of the ability of the rated entity to service its obligations in a timely manner, therefore, after the analysis of every risk factor, its significance for the overall risk evaluation should be clarified. The analysts' assessment of the separate risk factors and the overall condition of the rated entity shall be unbiased and independent. The analysts shouldn't allow their assessment to be swayed by their own or others' interests. In July 2019 one financial analyst was hired in the agency – Silvia Gergovska. In October 2019 Tzvetanka Kroumova was discharged as Advisor – Methodology development and appointed as a member of the BD. In 2019, the position Senior Compliance Officer was taken by Hristo Kiproviski till August 2019 and by Radoslav Marinov from August 2019. CRA's employees are hired on labour contracts, and their remuneration and performance evaluations do not depend on the fees contacted on with the clients of rating services.

#### Statistics on the allocation of BCRA's staff

Staff allocation	End of 2019	End of 2018	End of 2017	End of 2016
Rating Process*	7	7	7	7
Corporate ratings	7	7	7	7
Sovereign ratings	7	7	7	7
Methodologies**	2	3	2	2
Senior Management***	3	3	3	3
<b>Total***</b>	<b>10</b>	<b>11</b>	<b>10</b>	<b>10</b>

\* This number includes all staff members involved in the analysis, evaluation, approval and review of credit ratings. There is no staff segregation between ratings of various asset classes. The Corporate class includes ratings of banks, insurers, and non-financial companies. The Sovereign class includes ratings of states or the local or regional authorities of states. There is no staff segregation between work on new credit ratings and credit rating reviews. BCRA has not issued credit ratings of structured finance instruments or covered bonds in the past.

\*\* This is the number of staff involved with methodology or model appraisal.

\*\*\* The number does not contain the members of the Board of Directors (see page 2)

\*\*\*\* This total doesn't include support staff such as office coordinators, accountants, hygienists, couriers etc. The counts of staff members in the categories do not add up mechanically to this total, as a single person can be involved in more than one of the activities categorized.

### 4. Description of the system for achieving and storing information

<sup>4</sup> The full rationale is available at: [https://www.bcra-bg.com/files/rating\\_ozk\\_dec\\_2019\\_withdraw\\_en.pdf](https://www.bcra-bg.com/files/rating_ozk_dec_2019_withdraw_en.pdf)

<sup>5</sup> The full rationale is available at: [https://www.bcra-bg.com/files/rating\\_yambol\\_dec\\_2019\\_withdrawn\\_en.pdf](https://www.bcra-bg.com/files/rating_yambol_dec_2019_withdrawn_en.pdf)

BCRA keeps the following information related to the process of elaboration and assignment of credit ratings:

- The names of the analysts participating in the elaboration of the credit rating, the minutes from the meetings of the Rating Committee, information whether the credit rating is solicited or not, declaration confirming the presence/lack of any conflict of interests;
- Bookkeeping documents for the payments received in connection to the issue and the use of credit rating;
- The methodology used and the procedure for elaboration and assignment, the credit report and internal working documents during the elaboration of the credit rating;
- The internal and external correspondence, all e-mails related to the elaboration of the credit rating.

BCRA keeps the information for a minimum of five years following the assignment of the credit rating. Considering the confidentiality of some of the information needed for assessing the level of creditworthiness, the following documents are stored in a restricted-access network information system created for BCRA's needs, with a private physical server secured in a single room: data collected by the analysts from public sources and from meetings with the management of the client, financial statements provided by the client, the preliminary analyses of separate sections of credit report, the draft and final report of creditworthiness. The information provided in hard copy is kept in a secured archive in BCRA's office protected by a private security company. The information received electronically is archived once per month on external data carriers kept in a separate location from the Agency's office in accordance with the security requirements.

During 2019, there were no material modifications made to BCRA's IT.

## **5. Internal control**

In addition to the adopted internal regulations, methodologies and models the quality of the credit rating activities is assured through the implemented internal control mechanisms.

Within BCRA are established and maintained effective compliance and internal audit functions that operate independently.

The compliance function monitors and reports on compliance of BCRA and its employees with the credit rating agency's obligations under the Regulation 1060.

The internal audit function is responsible for providing reasonable assurance to executive management and the Board about the adequacy and effectiveness of the risk management control framework in operation and also to make proposals for strengthening and improvement of the risk management and control framework through the promulgation of best practices.

During the 2019, the compliance officer made current checks in the following directions:

- Assessment of the adequacy and effectiveness of the internal rules and procedures;
- Review of the areas for potential conflicts of interests.

The conducted in 2019 internal audits were in following directions:

- Checkup of the data in the insurance companies' credit rating reports and regarding the conformity of their content to the requirements of the Methodology for rating of the ability of the insurance companies to pay claims;
- Checkup of the filled in the process of preparation and assignment of credit ratings declarations.

The reports with the incomes of these inspections together with the proposals made in them were adopted at a session of the Board of Directors in 2019.

The BCRA organizational structure ensures the independence of the internal audit and compliance functions.

## **6. Management system and rotation policy of the financial analysts of BCRA and its implementation**

### Management

BCRA operates through a single office located in Sofia, Bulgaria. This BCRA office is managed by Christo Mihailovsky – CEO, Ventseslav Petrov – Deputy Executive Director, and Dr. Kiril Grigorov – Procurator, to whom report the analytical and the support staff either directly or indirectly, whereas the compliance, internal control and internal review functions report directly to the Board of Directors.

### Rotation Policy

According to art.7, p.4 of Regulation 1060 a credit rating agency shall establish an appropriate gradual rotation mechanism with regard to the rating analysts and persons approving credit ratings as defined in Section C of Annex I.

Requirements of p.8, Section C, Annex I of regulation 1060:

Quote

*8. For the purposes of Article 7(4):*

*(a) credit rating agencies shall ensure that the lead rating analysts shall not be involved in credit rating activities related to the same rated entity or a related third party for a period exceeding four years;*

*(b) credit rating agencies other than those appointed by an issuer or a related third party and all credit rating agencies issuing sovereign ratings shall ensure that:*

*(i) the rating analysts shall not be involved in credit rating activities related to the same rated entity or a related third party for a period exceeding five years;*

*(ii) the persons approving credit ratings shall not be involved in credit rating activities related to the same rated entity or a related third party for a period exceeding seven years.*

*The persons referred to in points (a) and (b) of the first subparagraph shall not be involved in credit rating activities related to the rated entity or a related third party referred to in those points within two years of end of the periods set out in those points.*

Unquote

With a decision of ESMA of 15.09.2015, BCRA is officially exempted from the rotation requirements.

## **7. Financial information about BCRA's revenues in the period 2018-2019.**

The relative shares of revenues from credit ratings by asset classes and from ancillary services in the last two years are given in the table below:



	2019 (Unaudited)		2018 (Audited)	
	(BGN )	(%)	(BGN)	(%)
<b>Net revenues from operating activity</b>	558 841	100,00%	569 604	100,00%
1. Credit ratings	547 098	97,90%	531 628	93,33%
<i>a. Corporate ratings*</i>	530 319	94,90%	513 349	90,12%
<i>b. Sovereign ratings**</i>	16 779	3,00%	18 279	3,21%
2. Ancillary services	11 743	2,10%	37 976	6,67%
From ancillary services to clients of credit rating services	11 143	1,99%	27 526	4,83%
*The Corporate class includes ratings of banks, insurers, and non-financial companies.				
**The Sovereign class includes ratings of states or the local or regional authorities of states.				

Geographical distribution in revenues				
Year	2019 (Unaudited)		2018 (Audited)	
	Amount/ %	(BGN)	(%)	(BGN)
Worldwide	558 841	100,00%	569 604	100,00%
1. EU	553 952	99,13%	564 714	99,14%
2. Out of EU	4 890	0,87%	4 890	0,86%

Below are the rated entities or related third parties from which BCRA received more than 5% of its total revenues from main activity, listed in alphabetical order:

- D COMMERCE BANK AD
- DSK BANK EAD
- EUROBANK BULGARIA AD
- MAB HUNGARIAN GENERAL INVETSMENTS PLC
- STARCOM HOLDING AD
- VARENGOLD BANK AG

## 8. Ancillary services provided by BCRA in 2019

Below is a list of ancillary services provided by BCRA during 2019. The asterisk (\*) marks the ancillary services provided to clients of credit rating reports;

- Credit reports;
- Bank rating information;
- Evaluation of financial state and preparation of financial analyses and reports for companies\*;
- Information product with aggregate data for the result from the main activity of the companies\*.

BCRA also offers the following ancillary services:

- Market analyses (of sectors and subsectors of economy, companies and projects) and preliminary assessment of economic trends and forecasts;
- Risk analyses and assessment;
- Elaboration of scoring models and scoring cards for creditworthiness assessment of individuals;
- Elaboration of scoring models and scoring cards for creditworthiness assessment of corporate small and medium-sized companies (SME's);
- Preparation and database processing and analyses;
- Analysis (based on its own database of companies in Bulgaria) and estimation of probability of default using an internal rating method for credit risk assessment;
- Information product with aggregate data for the result from the main activity of the companies.

**March 2020**