

## ANNEX 4: CASE STUDY – BULGARIA

### 1. Synopsis

In Bulgaria, the borderline between the legal and the illegal economies is much less clear than most of the EU MS. Organised crime, generating wealth from drugs, smuggling and prostitution, has merged with corporations and groups that have privatised state-owned assets, or has transformed its accumulated wealth into political and administrative power. This influence in the political and administrative structures allows companies to use corruption to win public tenders, avoid taxes, and systematically break the laws to gain competitive advantages. Organised crime networks have infiltrated to significant levels most public institutions: the police, customs, and prosecution. The political elite and political parties are highly influenced by organised criminals at the local level, while some criminal structures have been able to influence MPs or national level politicians.

### 2. Introduction

#### *Methodology*

The current study is based on analytical papers published by CSD, earlier interviews related to organised crime, academic research, and journalist articles. Additional interviews with key representatives of various institutions were carried out in the May-July 2009 period.

Although all interviewees were assured that their views would not be published, many of them chose to remain anonymous:

Name	Position	Institution
R1	Senior anti-corruption officer	Ministry of Interior
R2	Former Director	Special Services
R3	Senior police officer	Ministry of Interior
R4	Senior prosecutor	Prosecutor's Office
R5	Prosecutor specialized in organised crime	Prosecutor's Office
K1	Former Director	Customs Intelligence and Investigation
K2	Senior official	National Revenue Agency
K3	Former senior official	National Revenue Agency
K4	Former Deputy Minister	Ministry of Finance

### 3. Background: organised crime in Bulgaria

Over the past decade, the concept of 'organised crime' has become a universal metaphor used to explain political and business dependencies and practically any economic and corporate crime committed in Bulgaria. Similarly, the topic of corruption is perceived as closely related to anything from the underdeveloped and ineffective state institutions to the constant political conflicts in the country.

A meaningful discussion of the concepts of organised crime and corruption should begin with an overview of their recent history and a review of the current state of the institutions affected by organised crime and its corruption instruments.

### 3.1 Historical perspectives on organised crime

#### *a) Soviet period*

All sources on criminal activity in Bulgaria before 1989 indicate that organised crime was nonexistent. To address corruption, Bulgaria followed the Soviet model which created various control mechanisms utilizing both the Communist party structures and the Ministry of the Interior. Practically all major state institutions like the police, customs, prosecution, courts, and local political figures were subject to a systematic open or secret surveillance and, when necessary, investigation. As a rule, any violations at the middle and high levels were severely punished, although there have been cases of more lenient treatment due to family ties or cronyism. Certain tolerance was shown to everyday corruption at the low level (e.g. money given to traffic police officers for small violations on the road, bribes for the supply of goods in short supply, etc. ), but this type of corruption was not too widespread. At the same time, the lack of classic corruption was replaced by a model of nepotistic and informal networks. In these networks, the currency was not money but favours and loyalty to one's patrons. This model's roots can be traced to patriarchal family relationships in villages, as Bulgaria had remained predominantly rural until the mid 1950s.

#### *b) Transition period (1990-2001)*

The social and economic foundations of organised crime in Bulgaria were laid out during the transition to market economy (1990-2001). Several parallel processes were under way during this period:

- The country's economy suffered its most severe crisis since independence in 1878. Many sectors of the economy (developed within the frameworks of central planning and the Council for Economic Cooperation) abruptly collapsed. As a result, whole cities found themselves with no working enterprises. The process of privatisation redistributed 100% of the state-owned assets in the industrial, service and agricultural sectors. Often, the new owners had a criminal record and their capital had criminal origins.
- Due to the small size of the economy and its open nature, import-export volumes equalled nearly 70% of GDP. Consequently, border crossing related corruption became a major instrument for the redistribution of national wealth. The huge shortage of locally produced consumer goods was satisfied by imports, and the strategy of all importers and wholesalers was to avoid custom duties and taxes. Anyone who paid duties and taxes became uncompetitive. Thus, importing and exporting companies turned into criminal organisations, some of which employed hundreds of people. The Yugoslav embargo

of 1992-1995 had a similar effect on the Bulgarian economy as the 'prohibition period' in the USA. The smuggling of oil products into Yugoslavia became the main business for many of the largest criminal groups in the country, who applied intense violence in their trade relations.

- The social and economic crisis, together with the crisis of law-enforcement and justice institutions, created a favourable environment for the proliferation of conventional crime. Official records indicated that general crime went up four times, while for certain types of crime the increase was seven- to ten-fold. The boom of everyday street crime and the new opportunities for economic crime created the market for protection services and racketeering, and led to the emergence of 'power entrepreneurs'.
- As a result of the change of the political system, law-enforcement and justice institutions underwent overall restructuring. A wave of resignations and firings followed, drastically reducing the scope of activity of these institutions. In the following years, criminal offenders were not prosecuted, while for law-enforcement and justice institutions widespread economic crime was transformed from a target into a mere source of additional income.

*c) Recent developments and the shaping up of organised crime*

The current structure of organised crime in Bulgaria emerged in the 1997-2000 period, when the political crisis was overcome and gradual economic stabilisation was initiated. The key factor shaping organised crime was the tolerance of the authorities for all three types (see 3.2 below) of organised crime. Oligarch structures and power groups<sup>106</sup> got the opportunity to continue most of their activities undisturbed by any interference from police, tax agents or the court system.

The merging of 'organised crime' with 'white-collar crime' presents one of the main challenges in defining Bulgarian organised crime.<sup>107</sup> The transition from planned to market economy brought radical shifts in the social texture and blurred the boundaries between 'the underground' and 'the elite'. Within the last decade, criminal structures were transformed into legal business entities, and criminal bosses became legitimate business owners.

By 2004-2005 it had become clear that Bulgaria had good chances to join the EU, and the prospect of membership impacted significantly the nature of organised crime. Its current characteristics are summarized below:

- Small entities tied up in networks replaced the disintegrating large hierarchical organizations. The new networks are formed and con-

<sup>106</sup> In particular those related to the 'credit millionaires', the bankrupt banks and the liquidated state-owned enterprises.

<sup>107</sup> This is a fundamental difference between the West European and American traditions, where white-collar crime is viewed as separate from the world of organised crime, and the situation in Eastern Europe where white collar crime represents a significant proportion of organised crime.

trolled by remnants of the old leadership of the power structures (mostly oligarchs).

- Dependence on the market: the success of the criminal networks and structures is now solely dependent on their ability to compete on their respective markets of goods and services ('black' or 'grey').
- The blending of legal and illegal business has become key to survival and expansion: the new networks operate on all three layers of the internal market: namely legal (white), grey and criminal (black). In one and the same network, the structures at the lowest level are involved in 'dirty operations', managed usually by the youngest and least familiar members. The leaders of criminal groups own strictly legitimate companies with proven sources of capital and stable income. At the same time, structures operating on the grey and black markets are controlled exclusively by 'confidants' and are formally owned by socially disadvantaged people or employees of the respective company and their family members. These companies operate in large networks that could reach 200 to 300 legal entities.
- Mobility of companies: adapting to the changing environment, companies operating on the black market may significantly reduce or even discontinue their activity during periods of intensified law-enforcement operations.<sup>108</sup> Once everything returns to normal, the criminal activity in question is renewed.

### 3.2 The social origins of organised crime

The early economic and political developments shaped three categories of actors that became involved in activities that today are referred to as 'organised crime':

- **"Power entrepreneurs"** or '*groupirovki*' (i.e. 'power groups' as they are known in Bulgaria and Russia) whose overall activity was based on protection rackets, debt collection, and business arbitrage through the use of violence (under the guise of private security companies – PSCs). These groups were made up of former sportsmen (e.g. wrestlers and boxers), employees of the Ministry of Interior and ex-prisoners. Gradually, the smaller groups united into larger organizations. After the state attempted to ban PSCs, two national companies emerged, VIS-2 and SIK, and instead of security services they started extorting companies and even citizens under the guise of insurance business. Their most successful business was auto insurance.
- **"Black merchants"** took advantage of the severe shortages of various consumer goods in the early 1990s. Later they developed smuggling channels and informal distribution networks, thus avoiding customs duties, taxes and fees. Through complex networks of state employ-

<sup>108</sup> For instance, the sale of alcohol products without license was temporarily interrupted during such a recent spate of police checks.

ees, the “black merchants” managed to circumvent the law and gain competitive advantage. It should be noted that this type of organised crime attracted very little public attention.

- **“Political investors”** were former apparatchiks-turned-businessmen, directors of state-owned enterprises, and other nouveaux riches. In the early 1990s they focused on rigging privatisation deals and smuggling, while at later stages they shifted their target to corrupting public tenders. As the resources that political investors controlled grew and as they consolidated their businesses, they created mega-business structures and spread across various industries. At that point they began to be described as oligarchs. In recent years, their ambitions were to monopolise the most profitable industries by using a set of corruption and clientelistic methods. At the local level, the aim was to control a whole region or town. In many cases, several local families control the whole local economy and naturally become political investors. Their activities would normally be described in EU-17 as white-collar crimes.

### 3.3 Market perspectives

There are two factors that have the strongest impact on illegal markets – EU accession in January 2007 and the recent economic crisis. The market for real estate was the most severely affected market structure of the criminal networks. In 2007 – the last year of the real estate’s “golden period” – expert estimates valued the market at about 11.3 billion Euro (which equalled approximately 39% of the country’s GDP), an estimated 50% of which comprised unregistered properties (Garkov 2007).

The deep crisis of the real estate market has created new opportunities for these criminal structures and entrepreneurs. Some of them continue to invest into real estate income from EU markets for prostitution, drugs, counterfeit money and documents. The market, which has been severely affected by the crisis, now offers good quality assets in many parts of central cities and resorts at significantly lower prices. Corrupt channels in banks and the local judiciary are employed to acquire such assets.

Nevertheless, those criminal entrepreneurs whose real estate investments have gone sour have been forced to look into alternative investment options. Some of them have sought new sources of income through entering directly into investments in infrastructure construction, agriculture, and clean-energy. This has been confirmed in several interviews conducted as part of the study (R1, R2)

Joining the EU has created new potential for cross-border criminal activity, continuing a trend of ‘exporting organised crime’ that started with the removal of travel visa restrictions to the EU for Bulgarian citizens in 2001. From prostitution and car-theft to cocaine and heroin smuggling, Bulgarian networks have since expanded throughout EU-17. In EU countries, criminals apply a model similar to that used in the Bulgaria by trying to corrupt law enforcement and customs authorities. Interviews

with Bulgarian criminal entrepreneurs in Italy, Spain and France reveal that occasionally they manage to achieve this by using the services of specialized attorneys, or by using local or native criminals as intermediaries.

#### 4. Background: corruption in Bulgaria

After 1990, various types of organised crime evolved and adapted to the changing institutions. As criminal entrepreneurs attempted to legalize their business, smuggling and tax fraud gradually declined and corruption techniques were adapted accordingly. Organised crime took a systematic approach to corruption, encompassing all levels of public institutions, from the lowest ranking employees to political party leaders.

In 2008, Bulgaria was perceived as the most corrupt country in the EU, with a 3.6 value of the Corruption Perceptions Index in the annual survey of Transparency International.<sup>109</sup> In fact Bulgaria's corruption perception value has fallen sharply since the previous year (when the country's CPI stood at 4.1). The indicators measuring the experience, rather than perception, of corruption show that 72% of the population in the country declare that they have not experienced corrupt behaviour, lagging behind Romania and Slovakia, which have scores of 65% and 67% respectively. (TI 2008) Corruption is defined as the number one problem by the population and despite the economic crisis in 2009 corruption continues to rank ahead of unemployment and low income (CSD 2009). In terms of linking corruption and organized crime, Eurobarometer data shows that 66% of the population believes that the two phenomena are connected. In the EU only Italy is ahead of Bulgaria in this respect, as 70% of surveyed Italians perceive a link between organized crime and corruption (Eurobarometer 2008).

#### 5. Targeted institutions

##### 5.1 Political corruption

To understand the impact of organised crime on the various state institutions in Bulgaria, it is important to review the established political model in the country.

At the beginning of the 1990s, the democratically elected political elites in Bulgaria controlled over 90% of national wealth (including state-owned enterprises and public property). They were tasked with quickly transferring this wealth into private hands. Similar to other countries in EU-10E, the institutions of political democracy (parties, political movements, trade unions, etc.) were completely undeveloped. While the major political parties retained their presence on the political scene after 1990,<sup>110</sup> they had a very limited number of professional politicians capable of managing ministries, state agencies, parliamentary commis-

<sup>109</sup> A country's CPI Score relates to perceptions of the degree of corruption as seen by business people and country analysts, and ranges between 10 (not at all corrupt) and 0 (highly corrupt).

<sup>110</sup> On the Left, the Bulgarian Socialist Party formed two governments of its own and three times was part of a ruling coalition; on the Right, the Union of Democratic Forces formed two governments on its own and was part of a ruling coalition three times. The Movement for Rights and Freedom (a party mainly representing ethnic Turks) took part in four governments as a junior partner.

sions, etc. Even the Socialist party, whose political elite came from the old Communist party, found it difficult to find capable candidates for key government posts.

The lack of legal framework for the minimal financing for political structures was another key problem for political parties throughout the 1990s. This meant that when political organizations went into opposition, they were often unable to finance their expert teams and party structure, or even to pay their office rents. Aware of this gap in financing, the emerging large entrepreneurs and business groups turned their support for individual politicians and political parties into political investments. At the same time, there were no mechanisms for effective financial and institutional control over political agents, leaving networks of politicians and ‘political investors’ untouchable.<sup>111</sup>

Political investors were not concerned which party would gain power, as they had little interest in political ideology per se. The large business groups usually diversified their investments by backing several political forces that stood a chance to get elected. Smaller political investors could only bet on a single candidate but they partnered with investors in competing political parties. The investors in the winning candidate would then help the ones who made the wrong investment.

The line between legitimate economic groups and criminal organizations quickly became blurred in that period. There were no criminal entrepreneurs who did not finance (directly or indirectly) political parties. The approaches of these ‘political investors’<sup>112</sup> evolved with the changing environment. During the first period of transition, 1990-1997, when privatisation was limited, entrepreneurs tried to get control of state enterprises.<sup>113</sup> In the 1997-2001 period, when 90% of state-owned assets were privatised, ‘political investors’ were fully involved in rigging the privatisation process by paying bribes, salaries and bonuses to politicians, or by becoming directly involved in local and national political structures.

Since 2001, a new pattern of interaction between criminal networks and local and national political entities emerged. This pattern, presently in place today, involves privileged access to public tenders, concessions, access to EU funds, public real estate fraud (including swaps of public land), corrupt licensing of business activities, protecting industry monopolies, etc.

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<sup>111</sup> In fact, investigation of politicians in power and their circles of business supporters ends up with the removal, firing or even prosecution of the investigating officers from the police, tax and customs authorities, or the prosecutors.

<sup>112</sup> The other two types of criminal entrepreneurs, the ‘force entrepreneurs’ and the ‘black merchants’, also contact key politicians and use middlemen to gain access to senior political leaders.

<sup>113</sup> At state-owned enterprises, the executive directors and Board members (appointed by the government) guarantee to the ‘political investors’ access to the ‘entrance’, i.e. raw materials and other goods needed for the operations of a given enterprise, and at the same time provide to the ‘political investors’ control at the ‘exit’, i.e. all the output of a the enterprise. Thus the political investor is able to exploit both the supply to the enterprise (selling at higher than market price at the entrance), and its output (buying at lower than market price at the exit). Similar schemes work in banks, where political investors secure credits for their own companies.

The patterns of interaction between the economic (criminal) groups and the political elites after 2001 are described in similar terms by interviewees R2, R4 and K4. The respondents use the term 'single network' – a national social network consisting of a large number of sub-networks that encompass practically all personal contacts<sup>114</sup> of the most influential entrepreneurs and key politicians. Due to the small size of the country and the clientele model of recruitment and advancement of the elites, the number of people at the core of this 'single network' is several dozens; the secondary 'hubs' add another several hundred; and the widest circle (including mayors of mid-size cities and senior administration officers) adds up to a total of 2,000 to 3,000 people. Most participants within the professional sub-networks (lawyers, bankers, etc.) and within the regional sub-networks know each other. While at the beginning of the 1990s the personal and group networks were still being built and were often isolated and in conflict with one another, at the beginning of this century they started to connect and cooperate.

It is important to note that the most influential entrepreneurs support simultaneously competing political forces. The 'political weight' of a given politician is dependent not only on the success of his or her own party, but also on their access to the largest number of entrepreneurs and networks of political investors. The leader of the Movement for Rights and Freedoms (MRF)<sup>115</sup> Ahmed Dogan provided a concise description of this ideology of network of investors just before the parliamentary elections in 2005. He used the term 'circle of firms' to describe the fact that each political party has a network of economic groups and companies that support it financially. All following political scandals have revealed that economic groups can make corruption payments only if they are accepted as part of the 'circle of firms' of a given political party. The strength of political leaders is based on their ability to form alliances and avoid and resolve conflicts with the 'circle of firms' of other influential political competitors. It is important to work not only with the companies supporting one's own party or coalition, but also with the companies supporting political opponents. For certain political parties, a clear link to criminal organizations can be traced. Others have common assets or common projects with criminal entrepreneurs.

Criminal entrepreneurs use the following models to take advantage of their influence on political authorities:

- Recruitment decisions (e.g. for ministry staff);
- Regulatory and legislative decisions (amending laws in private interest);
- Economic agreements;
- Direct influence;
- Indirect influence;
- National level policy decisions; and
- Local level policy decisions.

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<sup>114</sup> Unlike the practice in developed countries (Western Europe, USA, Canada), where the mechanism of recruitment and advancement in public administration and political government are to a great extent formalised, in Bulgaria social networks play crucial role.

<sup>115</sup> The Movement for Rights and Freedom is a political party of ethnic Turks that was part of the governing political coalitions in the period 2001-2008.

Some of these are discussed at greater length below.

### *5.1.1 Recruitment decisions*

Usually, with the change of political power all senior administrative positions, like directors of state agencies, heads of departments at ministries, regional directors, etc. get replaced. The newly elected officials come from the social networks of the most influential politicians. The appointments are made after negotiations among key politicians in the ruling party or coalition and influential businessmen. Oftentimes the veto or 'initiative' (suggested candidate) of businessmen from the personal network of key politicians is crucial.

Senior officials in the public administration, like the Chief Secretary of the Ministry of the Interior, Directors of the Customs Agency or the National Revenue Agency, who are appointed by the government, must also consider key politicians of the parties in opposition. While politicians who have lost power also lose some of their ability to exert pressure on public officials, they still retain certain influence to reach targeted officials, if not directly, with the intermediation of middlemen.

Nevertheless, the massive changes after elections at all levels of administration, typical for the 1990s, are no longer common. Interviews with former senior public officials have indicated several types of political protection:

#### *Protection of the status quo*

Interviewee K4 recalls a case from his own experience. A regional director of the National Revenue Agency complained that a very influential MP demanded that the chief of a Roma clan be spared from prosecution on VAT fraud involving millions of euro. When there was an attempt to investigate the MP, the whole party (a member of the ruling coalition) stood in his defence. In the end, the prosecution of the VAT fraud scheme was discontinued. In turn, at the local elections a Roma clan secured a significant number of votes for the political party in question.

#### *Protecting employees*

An attempt to investigate and dismiss two regional customs directors for covering up tax fraud by local firms resulted in the mobilization of the social networks of those affected. Ministers, deputy-ministers and MPs from their own party and the coalition partners got involved. The two customs directors were not punished, because that would have impacted the position of a key politician in their networks. The higher in the hierarchy a public official stands, the stronger his network, and respectively, the more effort it takes to remove him from his position.<sup>116</sup>

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<sup>116</sup> A telling case was the incident with the Director of the Roads Fund who had to be removed despite the strong political and business support he enjoyed. It was found that he had donated more than 100 million worth of contracts to firms owned by his brothers.

### 5.1.2 Regulatory and legislative decisions

*Passing legislation, changing/blocking legislation.* This is effected via influencing MPs who manage to pass, change or block certain legislation for the benefit of a criminal structure or criminal market. A typical example of this corruption practice is the change in the Penal Code related to the punishment for human traffickers. The change was introduced by certain MPs, it was passed in a very short timeframe and resulted in much lower sentences for two well-known pimps. The debates on the Law on Prostitution continued for many years and it was obvious that criminal structures exerted direct pressure. Similarly, criminal interests affected the changes in the laws on gambling, duty-free shops, antiquities, etc.

*Regulatory decision by the executive branch.* Influencing changes in policy acts, internal rules, tariffs, etc. made by ministries and agencies is much easier to accomplish because they are not subject to much less public scrutiny. For instance, small changes in the listing of goods in a customs tariff can bring significant advantages to the agent who 'sponsored' the change. These changes are made either by agreements with the party leadership or with certain lobbyists or even individual MPs who might add a word or restructure a phrase to create an opportunity for criminal or financial benefit.

### 5.1.3 Economic arrangements

*Arrangement of tax framework:* this is practiced by large business groups (including foreign corporations operating in Bulgaria). They would reach an agreement with the political party in power on the amount of taxes they would pay, the licenses they would get from state authorities, etc. These arrangements are agreed upon at a high level and the respective state employees at lower levels (who are part of the social network involved) comply with the terms of the agreements (K3, K4).

*Prevention of control:* this is an agreement at a high political level whereby the activity of certain entrepreneurs will not be subjected to state control. The respective officials from the controlling authorities are informed of the agreement, and they make sure the entrepreneur is not troubled by any audits. In some cases the controlling organ does not get direct instructions not to carry out audits. Certain business groups and companies are publicly known as untouchable and the auditors never approach them. Interviewee P2 quotes cases where a group specialised in the investigation of organised crime has abandoned the investigation just because they have observed that the suspected criminals have had lunches or dinners with influential MPs.

*Prevention of prosecution of criminal entrepreneurs.* In cases when a crime committed by members of a certain network is revealed (e.g. counterfeit alcohol licenses, noncompliance with construction regulations, tax fraud, etc.) the institutions investigating the case are forced to discontinue the investigation.

#### 5.1.4 Direct involvement of organised crime in politics

In some cases, in particular at the local level, criminal entrepreneurs may take direct part in politics. As a rule, the lower the level, the more direct the involvement of organised crime. Sometimes notorious criminal offenders get elected mayors or city councillors.

The most famous of these cases is in the town of Dupnitsa (located 65 km south of Sofia, population 45,000). Two former special services officers, known as the Galev brothers, accumulated their capital through violence in the 1990s and then, using racketeering methods against local entrepreneurs, formed a political structure that won the local elections. In this manner they gained direct control over local administrative power. Dupnitsa became the most famous case of direct involvement of organised crime in the politics of a mid-size town.<sup>117</sup> (Gounev and Bezlov 2009) Similar cases of direct participation of criminal entrepreneurs in local politics were observed in some smaller resort towns.

In several larger cities, local power is practically controlled by criminal entrepreneurs and business groups through indirect participation in local politics. This trend started in 1999 and climaxed during the local election in 2007. The main incentive for organised crime was the booming real estate market. The most visible model of participation was *guaranteeing employees' votes for a certain candidate*. Criminal entrepreneurs who also owned legitimate businesses campaigned to (or rather forced) their employees to vote for a selected candidate.<sup>118</sup> Various techniques were applied, from threats to employees that they would lose their jobs to ad hoc payments, disguised as bonuses or covered travel expenses in addition to the regular salary. In other cases no cash was exchanged but voters received goods and services at lower prices or free of charge.<sup>119</sup> In the district of Sandanski there were documented cases of mobilising the black market network of dealers to influence elections. Cases of election coalitions arranged by criminal entrepreneurs and various schemes for attracting mayors and city council members were revealed in an independent study where this phenomenon was aptly called 'mayors on lease'(Tzoneva and Georgiev 2008).

## 5.2 Judicial corruption

The Constitution of 1991 established three autonomous judicial institutions: the investigation, the prosecution and the courts. As a result, the process from the registration of a crime to conviction is artificially separated into three separate stages, with different institution responsible for each of these steps. After the police completes an operation, it

<sup>117</sup> It is noteworthy that the Interior Minister Roumen Petkov was forced to resign after it was revealed that he held secret meetings with the Galev brothers.

<sup>118</sup> A recent example is Hristo Kovachki, who is investigated for a 5 million Euro tax-evasion. In the 2009 elections, the employees of all of his mines and heat generating plants were 'advised' to vote for his party "Leader" which narrowly missed getting into Parliament.

<sup>119</sup> For instance, a case was reported in Varna where prescription drugs were offered to elderly patients at lower cost, with the suggestion to vote for a certain candidate.

hands over the results to a preliminary investigator,<sup>120</sup> who delivers his or her findings to a prosecutor, who in turn decides whether to initiate a prosecution. The three professional groups – investigators, prosecutors and judges – come with exceptionally high job security. Very rarely are members of these groups fired or forced to quit, and their actions hardly ever become subject to an independent investigation.

Since 1991, two independent trends affecting the judicial system have been observed. First of all, political intervention has resulted in close interdependence between the magistrates, on one hand, and the political and business networks, on the other. Second, specific internal client networks have emerged within the judicial system. Political influence has been exercised through the Supreme Judicial Council (SJC) – the institution responsible for the management and control of the judicial system<sup>121</sup> and for guaranteeing its independence. Gaining control over the SJC has become a priority for every political party that has come to power after the Constitution of 1991 was adopted. In some cases, changes in the law have been made so that members of the SJC can be replaced at the beginning of the mandate of the new government with magistrates close to the new ruling party. In their turn, the magistrates have returned the favour when political or business disputes would arise ([izbori2009.com](http://izbori2009.com)) or even when criminal bosses are prosecuted ([sega.bg](http://sega.bg); [novinar.net](http://novinar.net)).

Similarly to politicians, magistrates found themselves in a unique position during the transition to market economy. At first the investigation, and later the prosecution became the institutions that would block or delay the prosecution of criminal cases, while crime prevention mechanisms (via the police, special services, financial control bodies) continued by inertia to feed evidence on criminal offenses. The politicians and entrepreneurs who were involved in the redistribution of national wealth had to reach an agreement with investigators and prosecutors that they would not interfere with the process. Economic disputes, including those where influential political sponsors were involved, were decided in the courts. The limited number of magistrates were ruling on these disputes made them an easy target for corruption practices.<sup>122</sup>

The small size of the judiciary, numbering 1,000 prosecutors, 1,500 investigators and 1,000 judges, makes it a closed community, with a strong sense of solidarity among its members. All penalties and promotions are the prerogative of the SJC (made up solely of magistrates). Criticism from outside the community (from journalists, police, politicians or EU administrators) rarely has any consequences even when it concerns publicly proven criminal acts by magistrates. Judicial officials are loyal not

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<sup>120</sup> According to the Constitution, the investigation is part of the judicial system and an independent institution. After year 2000 serious efforts were made to diminish the role of investigation and to remove it altogether from the judicial process since it caused most problems to those who were interested in blocking criminal cases.

<sup>121</sup> This supreme body is elected with equal quotas by Parliament and the judicial power. The Chief Prosecutor and the heads of the Administrative and the Cassation Courts have guaranteed seats.

<sup>122</sup> In Sofia and the three largest cities, where enormous resources were concentrated, there were between 100 and 200 magistrates who reviewed the most important economic and criminal cases. Accordingly, this group was identified as a prime target of organized crime.

only to the politicians who have helped them advance their careers, but also to fellow members of the magistrate community who refrain from criticism of their colleagues. Information regarding these mechanisms was revealed during the scandal surrounding the selection of the Chief Justice of the Sofia City Court (Bossev 2009).

Large law firms are another factor in judicial corruption networks (Bossev 2009). Often qualified judges, prosecutors and in particular investigators quit their state jobs due to low salaries, in order to join leading law firms as attorneys and consultants. It is this group of magistrates that are most often the middlemen between the criminal world and the magistrate community.

### **5.2.1 The Prosecution**

As stipulated in the Constitution, institution of the prosecution is independent, it enjoys extensive powers and at the same time is strictly hierarchical. A prosecutor has sole discretion whether to open a criminal case, to allow or to block certain actions in the investigation, etc. Thus the prosecutor can very effectively protect a criminal group or its members. The Chief Prosecutor is at the top of the institution, and he holds significant powers. If organised crime manages to influence the Chief Prosecutor, serious disturbances may result throughout the entire judicial system. A telling example is that of the first elected Chief Prosecutor, Ivan Tatarchev (1992-1999), under whose rule prosecutors started to delay cases, indicating clear signs of connections with criminal networks. The symbiosis of organised crime and prosecutors reached its climax under the next elected Chief Prosecutor, Nikola Filchev (1999-2006) (Hristov 2002). His brother Angel Filchev is known as one of the bosses of the antiques smuggling network. Publications in the press about his activities were followed by a series of prosecutions against newspaper publishers and politicians (*Capital* 2001; *Mediapool.bg*). Prosecutors close to Filchev were found to act in collaboration with organised crime by blocking criminal cases, participating in criminal acts and even managing criminal networks. Prosecutors at all levels were involved, from the lowest ranking district and city prosecutors to deputies of the Chief Prosecutor. Despite all evidences, including testimony of witnesses, records with special investigative means, documents, hidden currency and court rulings of foreign courts, no prosecutor has ever been convicted in Bulgaria.

Despite changes at the top level of the institution and the sharp increase in prosecutors' salaries in the past 3-4 years, old ties with organised crime, in particular at the local level, are still preserved. According to respondent R4, attempts to replace local prosecutors get blocked at the SJC level through a network of magistrate and political cronies.

According to respondents R2, R4, R6, and interviewees from other surveys, the model of interdependence between prosecutors and representatives of organised crime is changing. While before 2006 prosecutors were paid usually directly, either in cash or with other material assets, under the new model they have become part of business networks.

Prosecutors invest at local or national level and then are helped to earn maximum income from their capital.<sup>123</sup> Furthermore, prosecutors have forged stronger links with the other institutions. Publications in the press demonstrate that prosecutors get involved in regional sub-networks of large local businessmen, local MPs, judges, mayors, city council members, law enforcement officers, representatives of the Commission for repossession of unlawfully acquired property, officers from the National Revenue Agency and the Customs Agency, the Health Insurance Office and other state institutions.

Several measures could help eradicate the influence of organized crime on prosecutions. One is to put in place limitations in the powers of prosecutors and establish internal regulations, such as random the distribution of cases; another is to establish control over the terms of case schedules and procedures and ensure the systematic supervision of cases.

### 5.2.2 The Courts

In contrast to the prosecution, the structure of the courts is anti-hierarchical. Nevertheless, the courts are also targeted by organised crime, although to a lesser degree than investigators and prosecutors are. Some respondents suggest that the more authority a given court has, the more often criminal entrepreneurs attempt to influence it (R2-R6 and K1). The most widespread cases of such influence involve refusals by judges to authorise the use of electronic surveillance, refusals to issue arrest warrants, dismissals of cases for lack of evidence, and most commonly, delays of trials. Without formally breaking the law, a judge can indefinitely postpone any trial for technical reasons (choice of new attorney, illness of a witness or defendant, etc.).

The courts have been under most pressure from criminal entrepreneurs with regards to the settlement of trade disputes in court. As capital accumulated through criminal affairs is being transformed into legitimate assets, organised crime has undertaken aggressive legal attacks against competitors. In some notorious cases, it has managed to take away companies from their lawful owners.

Various schemes have been recorded in which judges *directly participated* in actions benefiting organised crime. Most often these have been cases of fraud relating to real estate. By law, a judge can assign ownership over a certain piece of land if there are two witnesses. Taking advantage of this provision, organised crime has acquired hundreds of attractive plots of state- or municipality-owned land in resorts on the Black Sea coast or in mountain resorts, and in the largest cities. Fictitious 'owners' would go to court with two witnesses claiming to own the land and although the fraud may be obvious to everyone judges would claim that they have no reason to rule against these 'landowners'.

<sup>123</sup> A prosecutor cannot openly demonstrate the capital he/she has accumulated, but they can take advantage of it through their relatives. For instance, Hristo Manchev, former deputy Chief Prosecutor, and Nikolay Ganchev, a prosecutor in the Sofia Appellate Court, in actuality have acquired luxury hotels officially owned by their daughter and spouse, respectively (Lex.bg 2007; Sega 2008).

Another form of direct collusion of judges in organised criminal activities involves providing lenient sentences. One of the most famous cases, among hundreds of similar ones, is the ‘Opitsvet’ affair (Opitsvet is a village in western Bulgaria, where workshops for illegal production of drugs were located). After first and second instance courts had found the defendants guilty, a Supreme Judge ruled in favour of the defendants claiming that 600 kg of amphetamine had been used for the purpose of chemical experiments instead of drug distribution. After this ruling the judge retired, and there have been speculations in judicial circles regarding the amount of the payment received since. Similar rulings of the Supreme Court have been passed in cases involving bankers, smugglers of cigarettes, and some famous singers acting as organisers of a pimp network.

The Supreme Administrative Court is also suspected of corrupt practices. The most discussed cases include the overturning of the privatisation decision on the Bulgarian tobacco monopoly Bulgartabak and the concessions for the Varna and Bourgas airports. Interview respondents pointed out that direct bribes are paid only in Sofia and in several other large cities. In smaller towns judges are part of local sub-networks and convictions of local criminal entrepreneurs are hardly possible. Examples of this practice are the cases of the Galev brothers in Dupnitsa or Koce-Mace<sup>124</sup> in Petrich, where, in the words of respondent R4, „if a magistrate (either a prosecutor or a judge), ruled against a well-known local criminal entrepreneur, he and his family would have to leave the town“. In this context, at the regional level a ruling may be a voluntary or a forced favour. At the same time, there are small towns where cash payments to judges are wide-spread. Most often these are towns close to the national borders where a lot of trans-border criminal activity takes place.

Another approach of organised crime is to find a small town court that would pass a favourable decision on a certain matter. Unlike large cities where cases are now randomly assigned, in smaller towns there is usually just one judge who deals with all the cases. An example of this practice is the small town of Peshtera (with a population of 21,000) where a judge used to change the names of convicted criminals, thus in effect clearing their criminal records (Nezavisim.net 2005).

### 5.2.3 Attorneys

Attorneys and law firms play a significant role in corruption practices in the judicial system. Most often, they act as middlemen between magistrates and criminal entrepreneurs. In some instances, attorneys directly pay bribes to magistrates who are known to be receptive to such practices. In large cities, young magistrates are initially ‘tested’ by attorneys from other towns who have not established a regular practice in the respective city. If the magistrate refuses the bribe, the attorney is under no risk as such offers are rarely prosecuted. The most common model would typically involve a family working together, where one of

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<sup>124</sup> A local city-councilor and football club owner who was convicted in 2008 by a German court for cigarette smuggling.

the spouses is an attorney and the other one is a prosecutor or a judge. The attorney would get clients and easily win cases even when the other spouse may not be directly involved in those cases – yet would still be familiar to the local judges' community, so that the attorney's clients would get favourable treatment in court.

Another type of network is made up of former colleagues. In Sofia, for instance, the so called 'black attorneys' (CSD 2003, Bezlov et al. 2007) work for the major mid-to high-level drug dealers. Customers are referred to the respective attorney who has connections in the district where the dealer has been arrested. There are also 'star' attorneys, who usually defend big criminal bosses and typically win their cases. Unlike their western counterparts, who usually try to find weak points in the prosecution, Bulgarian 'star' attorneys look for channels to directly influence the court.<sup>125</sup> Similar models are used by a few famous law firms specialising in commercial and administrative law. They rarely lose cases as they employ former magistrates with large personal networks. Several interviewees have claimed that 'star' attorneys and the law firms that never lose cases can influence the appointment of magistrates and even change the law in favour of their clients (R2, R4).

### 5.3 Police corruption

The Ministry of Interior (MVR) is the institution that has the broadest responsibilities and power in regards to organised crime. It is larger than any other public or private organization in Bulgaria, totalling about 55,000 employees.<sup>126</sup> In 2008, a specialised body called the State Agency for National Security (DANS) was created, whose responsibilities include countering organised crime and corruption at the highest levels of power.<sup>127</sup>

As is the case in other countries, Bulgaria's institutions charged with internal security are isolated from other professional and social groups. This isolation and stigmatization is not new to Bulgaria and was widespread during communism, when the police was called the People's Militia. Police officers provided security for the communist political elites and were guaranteed higher income despite their lower education compared to other professional groups. The tolerated use of force against criminals and citizens alike (whenever incidents occurred) was another reason for negative public attitudes toward the police. This isolation has led to recruitment of new police officers mainly from families of active or retired police officers, which guarantees additional, 'family-based' loyalty.

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<sup>125</sup> *The professional experience of such attorneys is impressive: consultant in the parliamentary Judicial Commission, former judge in the Sofia City Court, former Interior Minister.*

<sup>126</sup> *Under the umbrella of the Interior Ministry there are various independent services like police, gendarmerie, border control, fire departments, police academy, and technical services.*

<sup>127</sup> *The agency was created from the National Security Service (counter-intelligence), which was previously part of the Interior Ministry, and from the Military counter-intelligence (previously part of the Defence Ministry). The new agency is under the direct supervision of the Prime Minister.*

This model has naturally created family and crony networks, where personal contacts and favours were a major resource. The exchange of favours and the size of one's personal network was the main factor for advancement in the system, while rational criteria for effectiveness had limited impact. Only in the special services whose mission was to defend the most sensitive systems of the state were meritocracy principles applied. The police subculture is characterised by the existence of specific destructive networks, which corrupt police officers use to counteract or disrupt their (also corrupt) colleagues' networks by means of spreading rumours, producing secret investigations, and feeding information (or misinformation) interfering with their work. In contrast to other systems, 'anti-networks' play a significant role in police officers' career advancement.

The transition to market economy preserved and even reinforced the subculture of exchange of favours and nepotistic networks. At the same time, due to frequent political changes, the former loyalty to the ruling (Socialist) party withered away and was replaced by links to the sub-networks of the new political elites. While in the communist period the police network was deliberately isolated from the political elite (the *nomenklatura*), in the new social framework the police built up contacts with all political forces as a means of enhancing job security and career advancement. At the same time, the transition placed the Ministry of Interior structures in a state of constant financial constraints and shortages, such as low salaries, lack of payment for overtime served, delay of salary payments during crisis periods, etc.

As a result, the behaviour of police officers became subject to a new, parallel system of norms and values, as they were forced to find additional sources of income (some unlicensed and some outright illegal). Police officers started working second jobs as private guards of buildings or as bodyguards. In addition, abusing their official status, law enforcement officials developed a whole new system of obtaining additional income while performing their regular duties. The most massive sources of income were bribes for the traffic police, for customs officers, and for street patrols, i.e. police officers who dealt with petty crimes and misdemeanours and had extensive powers to apply penalties. These small bribes may add anywhere from 50% to 300% to the salary of a regular street policeman. The practice has become extremely widespread due to severe peer pressure – any officer who does not play by the new rules is isolated from his peers and if he still refuses to adapt to the system, „everyone will make sure the rebel is destroyed“.<sup>128</sup>

There are various description of the relationship between police and organised crime. Henk Van De Bunt identifies four categories: 1) 'donkeys', or individual officers who take bribes randomly and without systematic coordination with the rest of their workmates); 2) 'hawks', or high ranking officers who observe and 'take bribes' only when there is a large booty; ) 3) 'vultures', or officers operating in their 'home territory',

<sup>128</sup> This phrase is repeated very frequently at various levels of the Interior Ministry. In our case, we quote respondents R1, R2 and R3.

with defined 'hunting partners' and 'enemies', with whom vultures compete; and 4) 'packs', which are a more advanced form of the 'vultures' model, including representatives of other public institutions in addition to police officers.

In Bulgaria the 'vultures' model is the most widespread one and is observed both in the regional structures (local police departments, district and regional headquarters), and in the special departments of the Ministry of Interior (those dealing with organised crime, economic crimes, wire tapping, inspectorate, etc.).

If the managing officers are highly 'infected', there is a system of redistribution of income to higher levels: the lowest ranking officers (usually a group of five to twenty people) share part of their bribes with their supervisor; in turn, the supervisor shares with his superior officer, and so on. Such schemes can thus encompass as many as one hundred to three hundred officers in regional police districts. Very large 'targets', generating respectively large incomes,<sup>129</sup> are considered 'big bosses' territory.

Nevertheless, the above system and its full absorption of a police department is becoming an exception rather than the rule in recent years. One of the reasons for its disappearance is the economic stabilisation of the country in recent years. Another reason is that highly infected structures pose problems for the very officers who participate in them, because such structures trigger numerous complaints from citizens and employees of other agencies, leading to the involvement of politicians. As a consequence, supervising officers are being replaced and outside agents enter the system, forcing insiders to impose self-limitations on their incomes. The 'vultures ecosystem' of paying upward has remained in existence only in some of the most infected district offices in Sofia, in some of the largest cities and in the resort towns of the country. A more typical case nowadays is that of supervisors allowing subordinates to acquire additional income (for instance from prostitutes) without taking any payments from them. Supervisors don't need these payments because they have their own sources of income (e.g. from local criminal bosses/white-collar criminals).

The genesis of the relationship between organized crime and law enforcement has been the subject of intense debates. Contrary to hypotheses that remnants of the Communist senior elite at the Ministry of Interior created and indirectly managed 'organised crime' at the beginning of the 1990s, the authors of this study consider the forming of the symbiosis between organized crime and law enforcement to have been more random. (CSD 2004) The political changes at the beginning of the 1990s caused restructurings in the Ministry of Interior followed by a wave of firings and resignations. Some of these former employees then found jobs with companies involved in semi-legal or outright criminal activities. Familiar with the inner workings of the Mol, these individuals knew how to avoid prosecution. They used their skills and knowledge

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<sup>129</sup> For instance, the bosses of the drugs regions, owners of prostitution networks or of chains of stores selling excisable goods.

and their networks of colleagues and friends who retained their old jobs to pursue illicit activities. The new criminal entrepreneurs offered favours (such as job positions for a relative, colleague or friend) and payments to law enforcement officials aiming to integrate them in criminal networks. Another form of collaboration involved offers of information leading to the successful investigation of a certain criminal incident.

The most widespread form of corruption within law enforcement is the direct or indirect payment for certain favours. These payments affect all levels, from the very bottom of the system reaching even to Ministers themselves. These are the well-known corruption practices in ascending order:

Organised crime is less interested in the *lowest levels* because they cannot offer many of the services it needs, but still various forms of cooperation have emerged. For instance, payments are made to street officers in order for them not to 'disturb' prostitutes and their clients, to 'look the other way' when excisable goods like alcohol and cigarettes are illegally sold in small shops, or to avoid areas where street drug dealers practice their trade. A more active form of cooperation is the deployment of street police officers for security or delivery services. This form is used when drugs or illegal excise goods are transported, when cars are stolen or when prostitution homes require protection. Due to inefficient controls, low level police officers often reach agreements with the respective level of organised crime.

Under the dominating 'vultures model', monetary income is possible only in the largest cities of the country. In smaller towns, the prevailing method is either a favour or some payment in-kind. If a police officer is loyal to the local criminal bosses, he may get daily 'extras' like cheaper food in a restaurant, help in finding a job for his relatives, or an opportunity to become part of a local business.

Middle levels of organised crime deal with the respective middle levels in the Ministry of Interior. For instance, district drug bosses in large cities have agreements with the deputy directors of the respective district police department, the heads of criminal investigation groups, etc. In Sofia, the borders of drug distribution districts coincide with the borders of district police departments (CSD 2003, Bezlov et al. 2007). Similar agreements are observed in other markets like prostitution and trade with illegal excise goods. After the 2003-2005 period real estate frauds become common. The function of the middle level in law enforcement is to cover up these frauds, to warn if a counteraction campaign is planned and if an incident is revealed, or to appoint a preliminary investigator who would block the investigation. As a rule, middle level officers get regular payments for protecting the activities of brothels, or a certain number of prostitutes, drug dealers, or pawn houses and entertainment or commercial establishments operating in the grey area, which are left undisturbed by police control.

In smaller towns, high ranking police officials often have direct or indirect connections to influential criminal bosses who are in charge of

criminal or legal markets, or participate in a national criminal network. A widespread practice for police officers, prosecutors, judges and tax officials is to own significant shares in companies, hotels, restaurants, etc.

Officials at the highest levels, like directors and deputy-directors at the special services or directors of regional police headquarters are usually part of the networks of famous and influential entrepreneurs. One amongst many examples is the case of the deputy director of the Special Service for Combating Organised Crime, Ivan Ivanov. As a result of internal conflicts among senior officials at the Ministry of Interior, electronic surveillance transcripts were leaked to the press, demonstrating that Ivanov, together with other senior police officers, had held meetings with key organised crime figures. Ivanov had arranged for lower payments of excise tax for the largest producer of alcohol in the country.

At the highest level of organised crime, where black entrepreneurs and oligarchs are involved, the relationships are usually with key politicians. A case illustrating such ties are the secret meetings held between the Galev brothers (based in Dupnitsa – see above) and the former Minister of Interior Roumen Petkov, who was forced to resign when the meetings became public knowledge in 2008 (see Gounev and Bezlov 2009).

The total ‘infection’ of the Ministry of Interior creates great difficulties for the internal control departments of the ministry. In the transition period the internal control departments were under constant pressure from influential political and police sub-networks. ‘Anti-networks’ were used to remove inconvenient officers. When serious connections with organised crime were revealed, usually department heads were fired. There were cases when even the special services that wiretap and track suspects were infiltrated with corrupt agents who would deliver secret information to criminal networks.

The advancing economic development of the country and the ongoing normalisation of all institutions are gradually diminishing the influence of organised crime. As the black and grey markets shrink, the economic base aiming to corrupting the Interior Ministry slowly begins to disappear. Thus the new controlling structures in the ministry are able to exert broader and more systematic pressure on officers connected to organised crime. However, as pointed out by respondent R1, there is still not enough capacity to deal with corruption at the highest levels.

#### **5.4 Customs and tax corruption**

The links of the Customs Agency (CA) and the National Revenue Agency (NRA) to organised crime may be best understood, as with other public institutions, in the context of the social and political transformations of the 1990s. Until the end of the 1990s, relatively little attention was paid to the work of tax authorities, as the general attitude in Bulgaria was

that tax evasion was something quite natural.<sup>130</sup> At the same time, the Customs Agency became one of the most significant institutions of the transition period.

#### 5.4.1 Customs corruption

The Customs Agency has been identified in public opinion polls as by far the most corrupt state institution. Similar to magistrates, customs officers are a very small professional community (numbering about 3,000 employees in the 1990s) and hence they developed a strong social network. In contrast to magistrates, there are no requirements for specialised education and the profession is open to almost anyone. Customs officers cannot make arrests and do not have access to agents or wire-tapping facilities, but at the same time they have access to cash – since the beginning of the transition period through 2006 between 1,000 and 2,000 customs officers<sup>131</sup> controlled as imports and exports crossing the state borders evaluated at over 70% of GDP.

Access to customs officers in key positions (fee collection, control and personnel management), on the one hand, and to businessmen who conduct cross border transactions on the other, was (and continues to be) a crucial asset to any criminal network. Unlike police officers, who need to ‘hunt’ for their victims to earn additional income, customs officers operate on a purely ‘market’ principle: they provide a ‘service’ in high demand. The officers of the Customs Agency are involved in a complex, multi-layer corruption infrastructure that serves thousands of people, from households engaged in ‘suitcase/shuttle trade’ to the enormous networks of organised crime. Surveys of customs corruption have identifies numerous factors contributing to this phenomenon (CSD 2000; CSD 2002; CSD 2002a; CSD 2004): low salaries at the Customs Agency, the exceptionally high share of the grey economy (reaching over 50% during the crisis of 1996-1997), lack of control mechanisms in combating corruption, frequent politically motivated personnel changes, etc.

The emergence of so-called *brokers*, or officers who are not high in the agency’s hierarchy but can act as middlemen, is new phenomenon in the customs community. Entrepreneurs look for their services when they have a problem, and brokers can solve it by relying on the size and effectiveness of their networks. They are able to provide these services only because their networks overlap with other networks: those of ‘power entrepreneurs’, police officers, magistrates, and, most importantly, of ‘clients in possession of goods’. According to respondents K1 and R2, at the time when Bulgaria joined the EU there were probably 20 to 30 ‘brokers’, usually rank-and-file current or former employees of the Customs Agency, who exercised stronger influence than the directors of regional headquarters. They are actually the basic channel through which all major criminal networks operate.

<sup>130</sup> Tax revenues were collected mostly from state-owned enterprises (until 1997 privatisation had practically not begun), and the pressure for collection came mainly from the respective ministries.

<sup>131</sup> The headcount of the Customs Agency in the period 1990-2005 is not more than 3,000 employees.

With every change of government, big criminal entrepreneurs try to promote their own candidates for Director of the Customs Agency, for deputy-directors, and for heads of key departments. Even if they cannot secure the appointment of their candidates, the practice of newly appointed directors is to look for compromises with the oligarchs and to avoid audits of the companies that make up their network of friendly businesses.

Regional customs directors are forced to perform a more difficult balancing act. On the one hand, they have to comply with the average national requirements for collected revenue. On the other, they have to meet the demands of local criminal bosses. As pressure from the top intensifies, regional customs directors start to exercise pressure on their criminal clients.

The significant corruption pressure on the customs<sup>132</sup> is driven by the small size of the national market and the open nature of the Bulgarian economy, which make imports and exports a decisive factor for the success or failure of all types of businesses in Bulgaria. In the 1990s, over 300,000 people made their living by crossing the border with suitcases of goods such as clothes and cheap accessories and selling them at a higher price in a neighbouring country (the so-called "suitcase trade"). Organised crime took advantage of the same weaknesses in the operation of customs that allowed suitcase merchants to make a living by daily crossing of the border. Instead of mere suitcases, however, large companies were importing train-loads and ship-loads, avoiding any customs fees and taxes.

The most common imports for organised crime were the commodities in short supply on the internal market (cooking oil, sugar, etc.) and excise goods (alcohol and cigarettes). The smuggling of excise and consumer goods from food to luxury cars became the main engine of the market economy. Criminal entrepreneurs earned their highest profits from the smuggling of natural oil products into former Yugoslavia during the embargo.

The changed economic and political environment in Bulgaria diminished the opportunities for organised crime to illicitly import consumer and excise goods in mass quantities. The shrinking of the black and grey markets and the entrance of multinational companies had a significant effect to that end, as did Bulgaria's EU entry in 2007 since over 60% of the exports/imports of goods to and from EU countries are no longer subject to customs control.

Despite all this, some very important sources of income for organised crime still remain under the control of customs: namely the Chinese and Turkish imports as well as excise goods. The equalization of excise tax<sup>133</sup> on alcohol, cigarettes and oil products resulted in steep

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<sup>132</sup> The institution invariably ranks as the most corrupt in opinion polls.

<sup>133</sup> In the middle of 2006, the Customs Agency takes control of excisable goods, to soften the sever job cuts in customs officers after the country joins the EU.

increases in prices, making smuggling and black market sales very attractive.

A typical example of 'looking the other way' is the case of alcohol producing companies. In 2004, they paid for 112,9 million excise tax bands,<sup>134</sup> while in 2006 this number declined to 25,9 million. At the same time, marketing surveys indicate that the consumption of hard liquor had actually gone up. The only explanation for the decline is that following the increase of excise tax (from 5 to 11 cents per alcohol degree), companies turned to smuggling alcohol, using fake bands, or selling alcohol illegally. At the same time, no one in the Customs Agency raised the question of uncollected revenue from excise tax. Furthermore, the President and the Prime Minister attended the opening ceremonies for the new facilities of the two largest producers of alcohol, Peshtera and S&S Industries, responsible for almost 60% of hard alcohol sales in the country.<sup>135</sup> Similar is the treatment of the monopolist in oil products, Lukoil. According to respondents K1 and K4, the Bulgarian state does not monitor the quantities of raw oil that Lukoil imports or the quantities of processed oil it exports. The reason is that no one dares to force the company to install metering machines at the entrance or at the exit of loading pipelines. No one can verify the losses that Lukoil reports from its operations.

The influence of organized crime has been somewhat diminished by a series of reforms at the Customs Agency. The introduction of an electronic system for real time processing of imports and exports, the setting up of mobile groups for control inside the country, the adoption of special anti-corruption measures targeted at customs officers (i.e. declarations of income and personal property and limitations on business activities) have had a positive effect. The more active role of the inspectorate and the hiring of foreign consulting companies to enhance the analysis and control of revenues have also contributed to more transparent customs operations.

#### **5.4.1 Corruption at the National Revenue Agency (NRA)**

When the period of mass extortion and racketeering ended<sup>136</sup> in 1998 and the cross-border smuggling traffic was sharply reduced at the beginning of the century, criminal entrepreneurs turned their attention to legalising their accumulated wealth and income. As a result, the tax administration gained significant importance and power. With the centralization of the tax administration and consolidation of information resources in the 2001-2008 period, whole sectors of the economy and regions of the country that until then evaded payment of taxes, now felt under pressure to comply with the law.

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<sup>134</sup> Specially printed bands by the Ministry of Finance with holograms, stuck on liquor bottles to indicate that excise tax is paid.

<sup>135</sup> According to Jan-Feb 2008 alcohol market retail sales data from ACNielsen (not published), at the beginning of 2008 S&S Industries had 25.1% of the sales volume of rakiya, and Vinprom Peshtera had 34.5%.

<sup>136</sup> Power insurance' companies, like VIS-2, SIK, Apollo-Balkan, Levski-Spartak, Zora etc., lost their licenses to operate.

At the beginning of 2006, the functions of the Tax Administration (TA) and the National Insurance Institute (responsible for the collection of payments for health insurance, pensions and additional pension insurance, etc.) were integrated into one entity. All these changes prompted criminal entrepreneurs to pay special attention to the tax authorities.

As in the case of customs and law enforcement institutions, organised crime uses two main channels of influence the tax administration. At the first or political level, it promotes its own candidates or defends those ones who have already infiltrated the tax administration. The second channel is through tax brokers (similar to customs brokers) who arrange the covering up of tax offences, set up false tax audits of certain firms, or provide insider information to organised crime. In addition, tax authorities are used as a tool to attack competitors – criminal entrepreneurs may trigger tax audits to disturb competing firms.

The National Revenue Agency is decentralised into territorial directorates (TD) that hire their tax agents and initiate tax audits of local companies. Respondents K2, K3 and K4 believe that the TDs are probably the institution that suffers the highest degree of interference from the political elites. The appointments and resignations of TD directors are always surrounded by waves of lobbying efforts from members of parliament elected in the respective regions or from high-ranking local politicians. Personnel decisions affecting the TD directors are practically always taken not only by the Director of NRA but also by the finance minister and the respective deputy minister.

Similar to the Customs Agency, the NRA has a 'political contract' with the largest tax payers. The agency has a special department, 'Large Taxpayers', designed to work with the largest companies in the country. It is currently in charge of 700 companies that generate about 70% of the national tax revenue. According to respondents K2 and K4, all large companies in the country strive to get included in this group because allegedly each company under this section 'pays as much as it negotiates with the politicians'. The tax officers responsible for big business are all located in Sofia and their number is only 70 (with the argument to save expenses). The audits performed by these agents are mostly related to reimbursement of VAT, and due to their high workload, audits are a mere formality ([www.legalworld.bg](http://www.legalworld.bg)). Moreover, according to respondent K4, in the past 10 years the same teams perform all audits.

The gaps in the operation of NRA and its Large Taxpayers department are best illustrated by the decline in VAT collection. After Bulgaria joined the EU in 2007, NRA has to collect VAT on the imports of large companies, based on data from the Customs Agency. Despite the economic growth and the explosion in consumption, the VAT collected turned out to be 15% less. Periodically, incidents with the Large Taxpayers department result in personnel changes, such as the firing of its head Dima Zaharinoва followed by the dismissal of the Director of NRA, Maria Murgina.

At the regional and local levels, similar negotiations are practiced. The regional directors, just like their counterpart at the Customs Agency, have to balance the pressure from the state to generate higher tax revenue, and the demands of local businessmen for lower taxes and lighter tax audits. Systematic under-achievement of tax collection goals, or incidents revealing the milking of VAT, may result in the firing of the regional director. At the same time, the director and the deputy directors are part of the local social network and they try to promote the interests of large economic structures on their territory.

The election campaign in 2009 revealed various corruption schemes of the regional directorates of NRA. The former Director of NRA was accused of not reacting to a conflict between the director of the revenue agency in Silistra and a high-ranking local leader of the Movement for Rights and Freedom in regards to tax evasion. Similar accusations have been raised in other regional centres, such as Vratsa, Plovdiv, Bourgas and Sliven<sup>137</sup> (Lazarova 2009). One of the big problems of local tax authorities is that in small and mid-size towns all residents know each other. Any planned audit becomes public knowledge before it starts, and any punitive measure is met with social disapproval and isolation of the agents who apply it. Rotation of auditors is not practiced, with the argument that local agents know best who is who in the local business community and are best equipped to discover offenses.

With smaller criminal entrepreneurs, brokers are used to exert pressure on the NRA. A certain amount is paid to the broker who then distributes it among the tax officers involved. Bribes vary depending on the complexity of the 'service': for severe abuses, audited by officers from a different town, prices are much higher, while for simple 'consulting' in the grey economy they are low. There are tariffs for the provision of information on upcoming audits, for conducting a 'lighter' audit or speeding up the reimbursement of VAT. Respectively, payments can be used against competitors, when agents are asked to delay VAT reimbursement, initiate an audit or 'find' abuses in the operation of a competing company.

'Closed circles' in the network exist to deal with high-risk activities such as VAT milking. Usually these operations involve high-ranking officials of NRA who assume that a given company is compliant with the law and that any consequent audit is covered (CSD 2005).

## 6. Private sector corruption

Despite the normalization of the political and economic environment in Bulgaria, the line between criminal and legitimate business remains very fuzzy. There are different patterns of influence of criminal structures on business. Firstly, many companies and economic groups have their origins in criminal activity or criminal capital. Part of them have been set up with the purpose of legitimising people and business structures. Hence, even after these companies are sold to large international corpo-

<sup>137</sup> Sliven is a regional centre in South Bulgaria with a population of about 100,000.

rations, they are still influenced by the connections of the management or even mid level employees to the criminal world.

The influence of criminal groups remains also with normal companies that, at the beginning of transition, had had relationships with different leaders and criminal gangs (for instance by paying of protection racket). They continue to comply with criminal leaders by refraining from competing in public tenders, or refusing to supply to certain clients.

Even major Bulgarian and foreign companies that have never had contact with criminal structures use opportunities for exerting influence and mediating in procurement, or for achieving market dominance at the local, and in some cases the national level. Influence is also exerted for the adoption of laws, regulations and amendments, through the involvement of lobbying groups in the legislature or the executive. In recent years, several court cases have revealed that powerful criminal networks have been used for commercial gain, even by large and reputable foreign companies.

## 7. Conclusion

The isolation caused by the wars in former Yugoslavia, together with the long and rough transition to market economy, weakened the state and led to a sharp decline in households' incomes. As a result, for the first time in history, classic structures of organised crime emerged in Bulgaria. They got involved in trafficking heroin to Western Europe, in the trafficking of people, trading in stolen cars, etc. However, much harsher were the consequences of the criminal redistribution of national wealth (which was almost entirely state-owned until 1989), and the legalisation of all capital accumulated through criminal activities. Thus organised crime, political and economic elites formed a unique symbiosis.

As the country returned to political and economic stability (1997) and the process of joining the EU was launched (2000), structures of organised crime started to disintegrate and certain criminal markets began to shrink (i.e. the smuggling of consumer and excise goods, stolen cars, racketeering, etc.). When large multinational corporations entered the Bulgarian market, and the national economy got more integrated into the European market, Bulgarian economic groups that had benefited from criminal privatisation and were linked to criminal activities began to steadily lose importance, in particular in key sectors like banking, insurance, and retail. Despite the positive changes in the socio-economic and institutional environment, organised crime groups managed to adapt by concealing their criminal activities under the cover of legal companies. Mass violence got replaced by mass and systemic corruption. Taking advantage of the culture of family and clientelistic networks in public institutions, organised crime retained its privileged access to national wealth via rigged public tenders and concessions, the cartelisation of gambling, tourism, real estate, etc.

Organised crime exercises its influence at all levels: at the political level, votes get bought at national and local elections and the passing of laws favouring certain business interests is negotiated through lobbying

groups; at the magistrates' level, selections, appointments and rulings are being influenced and paid for by middlemen; at the level of the revenue administration, employees of all ranks are being recruited and corrupted to ensure custom duties, income tax and other taxes are avoided; and at the law enforcement level organised crime invests both in horizontal and vertical structures to cover up crimes or to destroy competition.

A new trend in the activity of Bulgarian criminal networks, after the country joined the EU, has been the attempt to corrupt officers of foreign administrations to make criminal activities abroad less vulnerable.