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(BRITE)**



CHOOSING PROSPERITY

THE CASE FOR BUSINESS CLIMATE REFORM IN MOLDOVA

December 2012

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ACRONYMS AND TERMS

ACAP	Association of Professional Accountants and Auditors of Moldova
AMCHAM	American Chamber of Commerce in Moldova
BizCLIR	Business Climate Legal & Institutional Reform
CIT	Corporate Income Tax
CNAS	National Social Insurance Fund
CNAM	National Medical Insurance Fund
CNPM	National Confederation of Employers of the Republic of Moldova
COA	Court of Accounts (Audit)
EBA	European Business Association
FDI	Foreign Direct Investment
FIA	Foreign Investors Association
FSI	Fiscservinform
FTE	Full-time employee
IFC	International Finance Corporation
IT	Information Technology
IMF	International Monetary Fund
Government	All Ministries in the Republic of Moldova
LTD	Large Taxpayer Department
MDL	Moldovan Lei
MIEPO	Moldovan Investment and Export Promotion Organization
MOE	Ministry of Economy
MOF	Ministry of Finance
MSTI	Main State Tax Inspectorate
NSI	National Social Insurance
HIF	Health Insurance Fund
OECD	Organization for Economic Co-operation and Development
OIKOS	National Association for Rural Development
Parliament	Legislative body in the Republic of Moldova
PIT	Personal Income Tax
Private Sector	Non-government associations, businesses and individuals
Public Sector	Sector comprised of Parliament, Government and State Authorities
RM	Republic of Moldova
SIDA	Swedish International Development Agency
SME	Small and Medium Enterprises*
State Authorities	Bodies under the jurisdiction of Ministries
STI	State Tax Inspectorate
UNDP	United Nations Development Programme
UTA	Autonomous Territorial Unit (translation from Romanian)
VAT	Value Added Tax

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INTRODUCTION

CHOOSING PROSPERITY: THE CASE FOR BUSINESS CLIMATE REFORM IN MOLDOVA

Despite its potential, Moldova has remained the poorest country in Europe¹ since its independence in 1992. Over the course of the last 20 years, many individual decisions – by both the public and private sector – have slowed the development of fair, transparent, and efficient institutions and procedures. Together, these amount to a national policy choice which has done little to promote rapid economic growth and jobs creation.

A different choice is possible. Moldova, with political will, can choose prosperity for its people. This assessment report, prepared for the new Business, Regulatory, Investment and Trade Environment (BRITE)² project of the U.S. Agency for International Development (USAID), provides concrete recommendations for reforms in five key areas – Trading Across Borders, Paying Taxes, Dealing with Construction Permits, Starting a Business, and Protecting Investors – that can begin the transformation to prosperity today. The report is intended to assist USAID, BRITE, and their Moldovan public and private sector partners in identifying technical assistance priorities for the new project.

This assessment uses the USAID Business Climate Legal & Institutional Reform (BizCLIR) methodology, described more fully in Annex A, to explore in depth five key regulatory regimes that are included in the annual World Bank Doing Business survey.

The methodology provides a systematic framework for identifying the issues that affect a country’s performance on the Doing Business survey, which measures the efficiency of national regulatory regimes for ten activities in the life of a business. The survey also ranks an economy on each of its 10 indicators in comparison with the 185 economies surveyed. The individual indicator rankings are compiled into an overall “Ease of Doing Business” ranking.

Table Intro-1. Moldova’s DB 2013 Performance

Topic Rankings	2013 Rank	2012 Rank	Change in Rank
Starting a Business	92	82	↓-10
Dealing with Construction Permits	168	165	↓-3
Getting Electricity	161	159	↓-2
Registering Property	16	17	↑1
Getting Credit	40	38	↓-2
Protecting Investors	82	114	↑32
Paying Taxes	109	106	↓-3
Trading Across Borders	142	141	↓-1
Enforcing Contracts	26	24	↓-2
Resolving Insolvency	91	95	↑4
Net Rank Improvements			14
Overall Ease of Doing Business Ranking	83	86	↑3

¹ See, http://www.aneki.com/poorest_europe.html.

² BRITE is designed to help stakeholders institutionalize a process of continuous improvement in the business-enabling environment while achieving specific and measurable reforms in the areas of greatest concern to the business community. The project has three components: 1) targeted reforms in taxes and trade; 2) high-impact reforms designed in collaboration with Moldovan stakeholders; and 3) the development of a National Communication Strategy to improve information flows within ministries, between the public and private sectors, and increased outreach to the general public.

Moldova's performance on the Doing Business 2013 report is summarized in Table Intro-1, above,³ with the indicators discussed in this assessment highlighted in yellow. As appears from the table, Moldova improved on 3 of the 10 indicators, and fell on 7. It had a net improvement over all 10 indicators of 14 places, largely because the total improvement for "Protecting Investors," up 32 places, from 114 to 82, outweighed the smaller declines. The net improvement increased Moldova's overall ranking on "Ease of Doing Business" in 2013 to 83rd of 185 countries surveyed, up from 86th for 2012.⁴

A focus on improving its Doing Business rankings can help Moldova increase its regulatory efficiency and international competitiveness in two important ways:

- The 10 indicators each measure important attributes of a key regulated business transaction. Improving the indicators helps to increase regulatory efficiency, reducing transaction costs and delays. Countries that improve their rankings have discovered that streamlining and automating regulatory processes simultaneously increases both their ability to monitor and control regulated businesses, and the volume and value of regulated transactions. When government makes it easier, faster, and cheaper to engage in a regulated transaction, more businesses do it and the economy grows and creates more jobs. The chapter on "Trading Across Borders" provides an analysis of the dramatic increases in trade volumes, national GDP, and employment that Moldova can achieve by reducing the time to import and export. The chapter on "Dealing with Construction Permits" provides examples from the Republic of Georgia on how increased efficiency in regulating the construction sector produced rapid increases in the volume of construction, construction employment and wages, and construction lending.
- To attract investment in an increasingly competitive global economy, a country must not only be efficient, it must be perceived as efficient. The annual Doing Business rankings are widely publicized and taken into consideration by international investors in deciding where to invest. In Moldova's case, investors around the world know that Moldova was identified by the Doing Business 2012 as the world's Number Two reformer. Its 18-rank increase from 2011 on the overall Ease of Doing Business ranking was second only to the 21-rank increase of Number One reformer Morocco. The fact that Moldova also broke into the Top 10 on the Doing Business 2010 report, when it was Number Six, with a 14-rank increase, helps to reinforce in the global investment community that Moldova is a country to consider as an investment destination.

Unfortunately, international investors that take a closer look at Moldova will find, as stakeholders reported to the assessment team, that Moldova is not yet a good value proposition. Although each of the 10 indicators is equally weighted in determining the overall "Ease of Doing Business" ranking, they are not equal either in the eyes of investors or in their impacts on

³ The 2013 Doing Business report was released Oct. 23, 2012. Details of Moldova's performance are available online at <http://www.doingbusiness.org/data/exploreeconomies/moldova>.

⁴ With each year's new report, the World Bank recalculates the prior year's ranking, to adjust for changes in methodology, addition of new economies to the survey, and to apply new information about the prior year. This practice explains why Moldova was ranked 81st for 2012 on the 2012 Doing Business report, but is reported as having ranked 86th in 2012 on the 2013 report.

economic growth and job creation. In the chapters that follow, we examine five key indicators in order of priority for igniting rapid economic growth, beginning with “Trading Across Borders,” which has by far the greatest impact on a nation’s economy, as discussed below.

Each chapter first provides an overview of Moldova’s current ranking on the indicator, and then suggests reforms that could boost both regulatory efficiency and Moldova’s ranking. Using the BizCLIR methodology, each chapter then discusses, sometimes in considerable detail, four key aspects of the relevant regulatory environment – the legal framework, implementing institutions, supporting institutions, and social dynamics. Each chapter concludes with a set of concrete, specific recommendations. Key findings for each of the five indicators discussed in the chapters that follow include:

- *Trading Across Borders.* Those interviewed for this assessment, both from public and private sectors, were, with the exception of Customs Service officials, virtually unanimous that inefficient trade regulation is the greatest single obstacle to Moldova’s growth. As discussed in the Social Dynamics section of the Trading Across Borders chapter, simply reducing the time it takes to export and import to the average times of Eastern European and Central Asian countries would increase total annual trade turnover by \$463 million and GDP by \$538 million. The reasons for Moldova’s current excessive delays include burdensome, constantly changing, and unpublished directives from the Customs Service, as well as failure to implement legislative provisions that expedite trade. Valuation practices that violate international agreements inflate traders’ costs and complicate their interactions with the State Tax Inspectorate. The motive for these practices, which create a barrier to investment and trade, appears to be to increase revenues--both official and unofficial.
- *Paying Taxes.* Inconsistent application of revenue laws makes compliance very difficult for Moldovan taxpayers, increasing the risk that businesses will resort to bribery or operating in the shadow economy. Appeal mechanisms are costly, time-consuming, and ineffective. Accounting for tax liabilities in the area of foreign trade is further complicated by abuses of the Customs Service. Arbitrary treatment of taxpayers delays refunds. As in the case of Trading Across Borders, a primary motive for a dysfunctional tax system seems to be to increase revenues.
- *Dealing with Construction Permits.* Stakeholders say that a “revolutionary” new law governing issuance of zoning and construction permits has succeeded in reducing time and costs. However, the benefits are less than anticipated, because government agencies thwart the law to increase official and unofficial revenues. After years of delay, Moldova still lacks modern technical standards for construction, master plans for local governments, and a comprehensive, consistent legal framework. The absence of these essential elements of a modern construction regulatory regime provides increased official and unofficial revenues to some stakeholders at the expense of a thriving, growing construction sector that benefits the whole country.
- *Starting a Business.* While starting a business is less complicated than many regulated activities, it is more complicated than the law envisions, because government agencies do not coordinate — and in some cases ignore — recent reforms designed to simplify

procedures. The chapter, which explores the business life cycle, also finds similar problems in other areas, including obtaining operating licenses and closing a business, which is particularly excruciating in Moldova. Businesses are often subject to burdensome and duplicative reporting requirements, high fees, and insufficient information from government. These inefficiencies encourage rent-seeking and provide good reason for businesses to operate in the shadow economy.

- *Protecting Investors.* Formal protections for Moldovan shareholders are very strong. In practice, shareholder complaints are mostly ignored by the regulator. In some cases, however, the regulator and the judiciary contribute to abuses of some shareholders by other shareholders for political or pecuniary reasons. The improving legal framework is hindered by inconsistencies between various laws. Recent reforms, if supported during implementation, offer opportunities to deepen the financial sector and provide investors inside and outside of Moldova with secure opportunities to invest in a growing economy.

This assessment concludes with a review of Moldova's recent economic performance, its opportunities to choose prosperity, and a summary of the impact the near-term reforms identified in each chapter would have on the country's overall Ease of Doing Business Ranking.

The assessment was conducted over the course of three weeks in September 2012 using the BizCLIR diagnostic process, which is described in detail in Annex A. In keeping with this process, the assessment is intended to identify key points for USAID and policy makers to focus upon in the interest of impactful reform, rather than serve as an exhaustive study of each subject area.

Chemonics International worked with the US-based Economic Integration Forum (EIF) and the Moldova-based Business Research Company (BRC) to field the assessment team and conduct the assessment. The team included the following experts:

- E.E. Koos – Paying Taxes
- Olin McGill – Dealing with Construction Permitting, Protecting Investors
- Alan Morley – Trading Across Borders
- Charles Schwartz – Assessment Coordinator, Starting a Business

SECTION I. TRADING ACROSS BORDERS

A. INTRODUCTION

Inefficient trade regulation, more than any other factor, is responsible for Moldova's failure to reach its potential for greater competitiveness in new markets, despite its relative geographic and workforce advantages. Moldova remains one of the poorest countries in Europe despite recent progress from its small economic base. With trading access to both EU and CIS markets, a highly literate, low-cost labor force, and rich, fertile soils, Moldova should be a highly attractive investment destination. Yet, Moldova has historically lagged behind other Eastern European countries in attracting and keeping foreign direct investment, despite its key advantages. This disparity has been "caused by the low level of the country's competitiveness," and more particularly by the disconnect between the law as written and as implemented.⁵

As demonstrated in the chapter on Paying Taxes, and further supported in this chapter, customs and taxes are the two most critical sources of revenue for the Moldovan government. This reliance leads to pressure on both the State Tax Inspectorate and the Customs Service to take measures that do not always conform with the law, in order to fulfill their revenue-raising mandates. In addition, traders report, unofficial rent-seeking is pervasive. Arbitrary measures to increase revenues coupled with rent-seeking have resulted in Moldova fencing itself off from international trade. The gross inefficiency that results makes Moldova too costly as an investment destination for foreign investors despite its obvious advantages. This self-defeating pursuit of short-term gains undermines important national goals, and denies Moldova the investment that would help solve some of its more significant national problems.

The Government's primary goal of EU integration has resulted in some market-oriented progress. The granting of EU trade preferences should encourage higher growth rates, but the agreements are unlikely to serve as a panacea, given the extent to which export success depends on higher quality standards and other factors. The economy has made a modest recovery, growing by 6 percent in 2011, but remains vulnerable to political uncertainty, weak administrative capacity, vested bureaucratic interests, higher fuel prices, and the concerns of foreign investors. Moreover, much of this growth has come from remittances rather than real growth. Moldova also faces energy supply and consumption concerns, prevalence of criminal activity in illicit drugs and human trafficking, and the export implications of lacking a seaport.

The onset of the global financial crisis and poor economic conditions in Moldova's main foreign markets caused GDP to fall 6 percent in 2009. With an efficient, predictable regulatory regime, the global financial crisis might well have been an opportunity for Moldova to increase foreign direct investment (FDI), as EU manufacturers searched for opportunities to move production to lower-cost venues. The opportunity has not been lost entirely, however. With the exercise of political will, Moldova can rapidly improve its trade regulation in the short-term, and put in place the policies and strategies that can make it a world class investment destination in the medium to long term. This chapter discusses the issues that Moldova must address and concludes

⁵ V. Prohntichi, et al, "Impact of Foreign Direct Investment on Moldovan Economy, Expert-Grup Independent Analytical Center, Chisinau 2010, page 12, available online at http://undp.md/presscentre/2010/Statistics_27JULY/iis_eng_www.pdf.

with recommendations for improving trade regulation so that the country and its citizens can enjoy the prosperity they deserve.

A1. “Trading Across Borders” Indicator

Table I-1. Moldova on “Trading Across Borders”

Indicator	Moldova		Eastern Europe & Central Asia	OECD
	Score	Rank		
Documents to export (number)	7	110	7	4
Time to export (days) *	32	155	26	10
Cost to export (US\$ per container)	1,545	137	2,134	1,028
Documents to import (number)	7	66	8	5
Time to import (days) *	35	153	29	10
Cost to import (US\$ per container)	1,870	135	2,349	1,080

The Trading Across Borders indicator of the annual World Bank Doing Business survey has three elements each for import and export for a total of six that are equally weighted to determine a nation’s overall ranking. The elements include the number of documents required to import or export; the total time required for document preparation, customs clearance, and technical control; ports and terminal handling, and inland transportation; and official fees and costs. The period measured starts from the time an agreement is made between an importer in one country and an exporter in another until the goods are delivered.

Moldova ranked 142nd of 185 countries surveyed on the Doing Business 2013 report, a one-place fall from its 2012 rank of 141st. Table I-1, above, shows Moldova’s score and international ranking on each of the six elements, and compares that ranking with the average scores of Eastern European and Central Asian countries, as well as the average scores of OECD member states. Table I-2, right, shows how Moldova’s total time and cost figures break down across the four phases of the import and export process.

Moldova’ dismal performance helps explain why foreign investors choose other destinations:

- *Number of documents.* Moldova requires 7 documents each for export, tied with 27 countries for 110th place on exports and with 35 countries for 66th place on imports. The world leader, France, requires only two documents each for export and import. Georgia, a competitor for EU investment, requires only four each for export and import. Reducing the number of documents required also reduces time and costs, helping both to increase the Trading Across Borders ranking and the efficiency of trade regulation.
- *Time in days.* As shown in Table I-1, above, Moldova requires 32 days to export, ranking 155th of the 185 countries surveyed, and 35 days to import, ranking 153rd. As noted in the introduction, time to trade is perhaps the single most important variable that determines a

country's economic prospects. Every day of trade delay costs a country roughly one percent of total trade turnover.⁶ In addition, as the introduction showed, reductions in the time to trade can also produce dramatic increases in GDP. Given the gross inefficiency of trade regulation in Moldova, sharp reductions in the time it takes to export and import can be made in the near term that will lead to much more rapid economic growth and job creation in the medium- and long-terms.

- *Cost.* Moldova's official costs and fees to export – \$1,545 – and import – \$1,870 – are high, ranking 137th and 135th, respectively. The biggest cost element -- \$950 for both export and import – is inland transportation. This may be difficult to reduce because Moldova's status as a landlocked country requires accessing foreign ports. However, Moldova can do much to reduce actual costs incurred by traders, including eliminating unofficial payments and streamlining operations so that costly commercial trucks are not sitting idle awaiting processing. Improvements in customs operations and to the transport infrastructure serving the Giurgiulesti free port (discussed below) could make it a more cost-effective port of entry and export for Moldova.

Table I-2. Time and Cost Breakdown

Export Procedures	Time (days)	Cost (\$US)
Documents preparation	20	115
Customs clearance and technical control	3	50
Ports and terminal handling	5	430
Inland transportation/handling	4	950
Totals	32	1,545
Import Procedures	Duration (days)	Cost (\$US)
Documents preparation	21	200
Customs clearance and technical control	6	120
Ports and terminal handling	5	600
Inland transportation/handling	3	950
Totals	35	1,870

⁶ S. Djankov, et al., "Trading in Time," Review of Economics and Statistics, Nov. 2008, p. 1, available online at <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Methodology/Supporting-Papers/DB-Methodology-Trading-On-Time.pdf>.

B. LEGAL FRAMEWORK

B1. General Environment for Trade

International trade volume throughout the world has increased significantly over the past 30 years, along with increasing pressure on Customs Administrations to clear goods as rapidly as possible. In fact, delays or complications in the Customs declaration and release process have come to be recognized by organizations such as the WCO and the WTO as significant non-tariff barriers to international trade, and have been specifically identified in the WTO Doha Development Agenda as a focus of negotiations in the current WTO Trade Round.

The Customs Administrations of many countries have addressed this issue by developing streamlined Customs clearance procedures. These are designed to release imported goods from Customs control as soon as it can be determined that there is no undue risk of false declaration, smuggling, or contraband, and then to deal with administrative documentation and payment requirements, as well as the conduct of verification audits on a selective basis after the goods have been released. These procedures are reflected in the standards and transitional standards presented in the WCO revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures. They recognize that, once two key requirements have been satisfied, the expedited release of goods from Customs can be permitted without impacting the Customs Administration's control of importations and collection of revenue legitimately due to the government.

Moldova has joined a number of international and regional initiatives, which demonstrate its progress to-date in advancing its economic growth priorities, as well as its potential for greater alignment with, and participation in, international markets. Moldova acceded to the General Agreement on Tariffs and Trade (GATT) and became a member of the World Trade Organization (WTO) on July 26, 2001. Moldova became a member of the World Customs Organization (WCO) on October 28, 1994, and became a Contracting Party to the WCO Convention on the Harmonized Commodity Description and Coding System (the "HS Convention") on June 10, 2004. The HS Convention entered into force for Moldova on January 1, 2006. Moldova has acceded to the Madrid Agreement (December 25, 1991) and the Madrid Protocol (December 1, 1997) on the protection of intellectual property rights.

Table I-3. Moldova: Average GATT Bound and Applied Duty Rates

	Total	Ag.	Non-Ag.
Simple average final GATT bound duty rate	7.0	14.0	5.9
Simple average MFN applied duty rate – 2010	4.6	10.7	3.7
Trade weighted average MFN applied duty rate – 2009	3.7	11.6	2.4

In January 2008, the European Union approved the granting of Autonomous Trade Preferences (ATP) to the Republic of Moldova, by which Moldovan exports to the EU under a broad range of tariff headings are permitted to be imported into the EU duty free or at a reduced rate of duty, in return for which Moldova has implemented a program of voluntary export quotas for certain

Moldovan goods exported to the EU. This program of voluntary export quotas is administered by the Licensing Chamber of Moldova (see “supporting institutions” below in this section).

Moldova and the EU also signed a Partnership and Cooperation Agreement on July 1, 1998. Moldova is a member of the CIS (Commonwealth of Independent States: Azerbaijan, Armenia, Belarus, Georgia, Moldova, Kazakhstan, the Russian Federation, Ukraine, Uzbekistan, Tajikistan, and the Kyrgyz Republic) and CEFTA (Albania, Bosnia and Herzegovina, Croatia, Macedonia, Moldova, Montenegro, Serbia, and Kosovo) multilateral free trade agreements, and is currently in the process of negotiating free trade agreements with the European Union and with Turkey. Moldova is currently undertaking negotiations with the WTO that will lead, if successful, to its acceptance of the WTO Agreement on Government Procurement. A Bilateral Investment Treaty (BIT) between Moldova and the United States was signed on April 21, 1993 and entered into force on November 25, 1994. Moldova has not entered into a Trade and Investment Framework Agreement (TIFA) with the United States.

Moldova maintains barriers to trade in services in some sectors. Foreign persons cannot be employed in Moldova until a complicated process of public tender has been completed by the prospective employer to confirm that there is no Moldovan worker available with the requisite skills and capacities to fill the job. Mobile telecommunication services are open to foreign mobile telephone service providers, but landline telephone services are under a state monopoly with which a foreign provider would be unable to compete. Gas and water distribution services are state monopolies. Prices for oil and gas distribution are set by a government agency, which sets higher prices for commercial users to subsidize lower prices for domestic consumers. Prices for water distribution and connections to services are set by local government authorities. Railway services in Moldova are also a state monopoly. Moldova is a member of the SMGS Agreement on International Goods Transport by Rail of 1 November 1951, which set out common rules for railroad transportation in the former Soviet Union. Railway track lines throughout the country are on the Russian gauge, so that trains into or out of Romania must stop at the border to convert the cars to or from the European gauge. Foreign banks can set up operations in Moldova reasonably easily, and a number of foreign banks do operate in the country. The capitalization requirement for banks is set by law at 100 million MDL, but the central bank has arbitrarily increased this requirement in some cases despite the legal provision.

B2. Domestic Laws

The laws and regulations of the Republic of Moldova governing Customs administration are listed in the text box at right. The laws containing the fundamental provisions governing the Customs function are identified in bold-face type.

Officials of the Ministry of the Economy and the Customs Service acknowledged the Government of Moldova’s interest in adopting the EU Customs Code in 2014. The Ministry of Finance, however, expressed the objective not in terms of enacting the EU Customs Code, but rather, aligning the Moldovan Customs Code with it given Moldova’s current state of development. The USAID BIZTAR project assisted the Customs Service in late 2011 by developing a comparison of the current Customs Code with EU requirements and those of the Revised Kyoto Convention. Both USAID BRITE and EUBAM (see Supporting Institutions below) have expressed their interest in supporting further modernization of the Customs Code.

The Ministry of Finance did express its intention to set up a working committee before the end of this year to develop proposals for appropriate revisions to the Moldovan Customs Code, in parallel with the ongoing negotiations with the EU to conclude a Moldova-EU Free Trade Agreement.

B3. Tariff Regime

The Moldovan Customs Tariff is based on the WCO Harmonized Commodity Description and Coding System (HS) Nomenclature. The Customs Tariff Law, however, presents only a schedule of descriptions aligned to the HS Nomenclature and ad valorem tariff rates applicable thereto, but does not present the General Rules of Interpretation or the Legal Notes of the HS Nomenclature. The schedule of descriptions and tariff rates, together with the General Rules of Interpretation and the Legal Notes, are presented separately in a Customs Tariff regulation. It follows, therefore, that an

Key Laws:

- **Customs Code**, 1149-XIV, 20.07.2000, as amended
- Tax code, 1163-XIII, 24.04.1997 (section III VAT and IV Excise)
- **Law on Customs Service**, 1150- XIV, 20.07.2000
- **Law on Customs Tariff**, 1380-XIII, 20.11.97
- Law on State Regulation of Foreign Trade Activity, 1031-XIV, 8.06.2000
- Law on Antidumping, Countervailing and Safeguard Measures, 820-XIV, 17.02.2000
- Law on State Regulation of External Trade Activity, 1031- XVI, 08.06.2000
- Law on Free Economic Zones, 440-XV, 27.07.2001
- Law on Licensing of Some Types of Activities, 451-XV, 30.07.2001
- Law on Import and Export of Goods, 1569-XV, 20.12.2002

Key Regulations:

- Gov. Dec. Approving the Structure, Staff and Regulation of the Customs Service, 4, 02.01.2007
- Gov. Dec. Approving Normative Acts Implementing Law on Customs Service, 383, 29.05.2001
- Gov. Dec. Approving Disciplinary Statute of Customs Officers, 746, 07.08.1997
- Gov. Dec. on Flag, Banner, Signs of Customs Authorities, 554, 16.06.1997
- Gov. Dec. Approving Trade Nomenclature, 1525, 29.12.2007
- Gov. Dec. Approving the Regulation on Declaration of Customs Value of Imported Goods, 600,14.05.2002
- Gov. Dec. on Rules of Origin of Goods, 1599, 13.12.2002
- Gov. Dec. on Approving Regulation on Implementation of Customs Procedures, nr. 1140, 02.11.2005
- Gov. Dec. Approving Regulations on Customs Procedures, 1140/2005
- Gov. Dec. Approving Concept of Risk Management in Customs Service, 1144, 03.11.2005
- Gov. Dec. Approving Regulation on Import and Export of Goods by Physical Persons, 1185, 30.09.2003

uninformed observer looking at the Customs Tariff Law would not understand that the Moldovan Customs Tariff is subject to the General Rules of Interpretation and the Legal Notes to the Harmonized System, even though Moldova, having acceded to the WCO Harmonized System Convention, is committed to apply the General Rules of Interpretation and the Legal Notes to the Harmonized System in making tariff classification determinations. Moldova is technically compliant with the Convention, but in a decidedly non-transparent manner. Moldovan officials of the Customs Service and the Ministry of Economy have indicated that the Government intends to amend the Customs Tariff Law in 2013 to present the General Rules of Interpretation and the Legal Notes, as well as the schedule of descriptions and tariff rates.

The Explanatory Notes to the Harmonized System are available in Moldova in very limited numbers due to the high cost of purchasing English, French, or Russian sets from the WCO. A Romanian language translation of the Explanatory Notes has apparently been produced by or for the Romanian Customs Service, but the Moldovan Customs Service has not made any attempt to obtain copies or permission from the Romanian Customs Service to reproduce the Romanian language version for use in Moldova.

Pursuant to a bilateral agreement with the EU, Moldova administers export quotas on EU exports of wine, sugar, wheat, and corn. Moldova applies tariff rate quotas to the importation of sugar.

In addition to any applicable ad valorem rate of Customs duty that may be specified in the Customs Tariff for a particular good, the value-added tax of 20 percent is applied to most imports, as well as a Customs service fee (depending upon the Customs import regime under which the goods are declared) of 0.1 to 0.4 percent of the value of the goods imported.

B4. Specialized Trade Mechanisms

Giurgiulesti Free Port

Danube Logistics SRL, a Moldovan limited liability company, operates the Giurgiulesti Free Port, located at the south-west corner of the country, as a free economic zone pursuant to provisions of the Customs Code. The Customs Service exercises physical control of the perimeter of the zone. This is the only port facility in Moldova, occupying the very limited shoreline (480 meters) Moldova has on the Danube river. The port is capable of handling small- and medium-sized sea-going vessels of up to seven meters in draft.

Danube Logistics officials noted that the Customs Code provides inadequate mechanisms to cover the efficient operation of the port. Regulatory clarification of these provisions of the Code would help, but the Customs Service is so far unresponsive to any proposals to develop such regulations. Streamlined Customs processes are theoretically available pursuant to the Customs Code and the law on Giurgiulesti Free Port.

Danube Logistics officials noted that the Customs Service often creates delays through demands for additional documents even if, in some cases, they do not exist. One example given was a demand by the Customs Service for insurance certificates for a particular vessel, despite the fact that the vessel operator in this case had chosen not to

Too Many Rules, Too Little Control

Although Giurgiulesti Free Port is a FEZ with Customs controls around its perimeter, the Customs Service has attempted to introduce additional controls within the zone for imports processing. For example, the Customs Service required goods off-loaded at the port to be declared twice – first upon discharge of the goods from the ship to the port, and again upon exit of the goods from the port. Agreement was reached through the Ministries of Economy and Finance to discontinue this double processing, but Customs then attempted to introduce a requirement that goods in the port be stored in a temporary warehouse to await clearance. The warehouse was to be operated (and fees charged) by a state enterprise set up by the Customs Service. Danube Logistics resisted the Customs-operated warehouse, but was still required to set up an independently-controlled warehouse. Customs also attempted to create a “private entity” (again part of the state enterprise set up by the Customs Service) to check goods within the port; notwithstanding the fact that the Customs Service controls the exit points from the port into Moldova.

purchase insurance for that voyage.

Danube Logistics also noted difficulties and delays encountered over importations of new technologies not provided for in existing Moldovan standards. Even though approved for use in other countries, the lack of a Moldovan standard for the technology meant that it could not be used in Moldova until a standard had been developed. As a result, some construction in the port had to be re-designed to use older technologies as the time required to get approval to use the new technology would have unacceptably delayed the construction schedule. The problems caused by antiquated technical standards for construction are discussed in the chapter on Dealing with Construction Permits.

Danube Logistics expressed concerns over the application of the Repatriation Law, which requires that any goods purchased abroad with funds originating in Moldova must be imported into Moldova within a specified timeframe. Otherwise, significant penalties can be assessed. An example was given of a Moldovan entrepreneur purchasing manufacturing equipment for use by a foreign supplier for the production of goods to be imported into Moldova – the goods produced by the equipment are imported, but the production equipment itself remains at the foreign manufacturing facility. This would be considered a violation of the Repatriation Law.

Addressing these issues, as well as improving the road and rail links to and from the port, particularly the rail link to Romania, could significantly improve the port's competitive position relative to similar ports in Ukraine and Romania, and offer a cost-effective alternative to Moldovan traders.

Free zones

Pursuant to provisions of the Customs Code, free zones (in addition to the free port at Giurgiulesti and a free airport at Marculesti, near Balti) have been established in Chisinau; Tvardita, Taraclia, and Valcanes in the south; Otaci and Balti in the north; and Ungheni in the central-west. Private sector entities have requested establishment of additional free zones, especially in Chisinau, to reduce Customs impediments upon importation. However, the Government of Moldova has agreed with the IMF not to establish any more zones. The IMF's view is that FEZs in Moldova are no longer justified as a means of stimulating employment in remote regions of the country. These regions have more recently seen mass migration towards the cities, particularly Chisinau, and there is now less of an employment problem to address in the outlying areas. For this reason as well, many entrepreneurs are now proposing the establishment of new FEZs in and around Chisinau. The IMF believes such new FEZs in Chisinau are unnecessary to attract investment, and could create unfair competition. The Customs Code does provide for the operation of an Inward Processing program, whereby goods imported for manufacture for export could be conditionally exempted from the assessment of duties and taxes, subject to subsequent confirmation by audit that the products manufactured from the imported goods had been exported. Many exporting manufacturers, however, are apparently reluctant to enter into such a program. They express concern that Customs would impose unreasonable or arbitrarily changing requirements, or that audits conducted to confirm the export of manufactured products would be used as an opportunity to extract payments or impose penalties.

Transnistria

Complications have arisen over the passage of goods through Transnistria. Eighty percent of goods imported into Transnistria enter from Ukraine, but some importations pass through Moldova destined for Transnistria. The Moldovan Customs Service cannot officially deal with these importations as a transit movement on a temporary entry basis, as Transnistria is recognized internationally as a part of Moldova. Pursuant to an agreement between the Government of Moldova and Transnistria authorities, Moldovan Customs has implemented an administrative procedure to exempt goods destined for Transnistria from Moldovan duties and taxes. Under this procedure, effectively administered as a transit procedure but not called transit, duties and taxes are collected by Transnistrian authorities upon entry of the goods into the enclave.

Moldovan goods are generally not permitted to be exported through Transnistria into Ukraine, as the Moldovan Customs Service has no presence or control capability at the Transnistria border with Ukraine by which to confirm their export. A temporary agreement was reached in March 2012 between the Government of Moldova and Transnistria authorities to allow Moldovan goods exported by rail to Ukraine to pass through two designated railway crossing points on the border between Moldova and Transnistria (Rybiniza and Bender 2), at which joint processing facilities (separate offices in the same building) have been set up by the Moldovan Customs Service and Transnistria officials. This agreement will expire at the end of September 2012 unless extended.

As Transnistria has no international standing, producers in Transnistria must register in Moldova and seek Moldovan certificates of origin to export their goods to other countries.

C. IMPLEMENTING INSTITUTIONS

The provisions of the Constitution, laws, and regulations of the Republic of Moldova, as well as the provisions of the international treaties, conventions, and agreements to which Moldova is a party, regulate external commercial activity. Implementing institutions are currently working either for or against the efficient movement of goods in and out of Moldova. Their individual roles and responsibilities, and the extent to which they are able or willing to fulfill these duties, are described in the pages that follow.

Parliament

Article 129 of the Constitution of the Republic of Moldova (external economic activities) stipulates that: “Parliament approves the main directions of external economic activities” and “the Government ensures the protection of the national interests in external economic activities, and promotes free trade or protections, based on national interests.”

Article 7 of the Customs Law states: “If international treaties to which the Republic of Moldova is a party set forth different norms than those stipulated in this Code and other normative acts on Customs of the Republic of Moldova, the provisions of international treaties shall have priority.” Parliament, as the legislative authority, adopts laws and the most important policy documents with respect to external economic activity.

Government

The Government of Moldova defines and ensures the promotion of state policy in the field of foreign trade, adopts decisions and orders on external trade activity, and ensures their implementation.

In the domain of external trade, State policy mandates tariff-customs regulations and non-tariff regulation of foreign trade activity in accordance with the laws passed by Parliament and normative regulations approved by the Government, and also in accordance with international treaties to which Moldova is a party. State policy in the framework of external trade is directly elaborated and promoted by the Ministries of the Government, and public authorities which are subordinated to the Government, based upon their areas of responsibility, as follows:

Ministry of Economy

The Ministry of Economy determines the main directions and policies of development of foreign economic activity, as well as tariff and non-tariff regulatory principles.

Ministry of Finance

The Ministry of Finance elaborates tax policy and administration, including those related to duties and taxes collected by the Customs Service on imports and exports.

Ministry of Agriculture and Food Industry

This Ministry regulates the procedures for authorization and control of the import and export of products of animal and vegetable origin. It also administers the issuance of certificates of conformity for imports and exports of animal and plant products, currently through two agencies (the Sanitary Veterinary Animal Origin Food Safety Agency and the Phytosanitary General Inspectorate). These two agencies are planned to be amalgamated into a new Food Safety Agency in January 2013.

Certificates of conformity on imports are issued on the basis of a review of animal health in the exporting country, and through reference to reports (hard copy only, as the Moldovan government does not have on-line access) from the EU Rapid Alert System for Food and Feed (RASFF). Ministry officials noted a need for IT support to gain on-line access to international monitoring systems. Moldova has declared unilateral recognition of the EU mark of conformity.

Ministry officials noted that a serious problem in the development of export markets for animal products is the lack of resources available to Moldovan producers to upgrade their (often Soviet-era) facilities to meet international (and particularly EU) standards. The only animal product for which Moldova currently has approval for export to the EU is honey. The Ministry of Agriculture is seeking to expand EU export approval to cover eggs, poultry, and fish, and has submitted samples for review by the EU food certification authority.

Ministry of Agriculture officers were in place at the border offices until 2008, when they were removed as part of Customs implementation of an OSS approach. The Ministry of Agriculture is seeking to reinstate the presence of its officers at the border offices. Currently, exporters must obtain certificates of conformity for their goods from the Ministry of Agriculture central offices in Chisinau or regional offices (depending upon the type of certificate) before they can begin the movement of their goods to the border. The process of obtaining these and other required certifications usually takes eight hours (effectively a full day, as processing by the Customs

Service of ASYCUDA inputs closes down at 5:00 p.m. on weekdays, after which time an export declaration will not be processed by the Customs Service until the following day). These certificates are then subjected to 100 percent review by Customs officers at the border point.

Ministry of Transport and Road Infrastructure

This Ministry elaborates and promotes state policy in the field of transport, including international transport of goods and passengers.

Customs Service

The Customs Service of Moldova, along with the State Tax Inspectorate, falls under the jurisdiction of the Minister of Finance. The headquarters offices of the Customs Service are in Chisinau, and 76 border crossing offices (67 on the Ukrainian border and 9 on the Romanian border) and 21 inland processing offices report to 7 regional offices. Staff levels are 333 in headquarters and 1,395 in regional and border offices, for a total staff level in the Customs Service of 1,728.

All of the respondents, both from the private sector and all of the officials of government ministries and agencies interviewed in this assessment, with the sole exception of representatives of the Customs Service, identified Customs administration as the single most serious source of obstructions to international trade in this country. A compilation of the issues identified follows.

C1. Administrative Practices Divergent from Laws and Regulations

The principal acts administered by the Customs Service (the Customs Code and the Customs Tariff Law) are, with minor exceptions, generally consistent with international norms and agreements. Respondents in the private sector as well as government entities other than Customs noted consistently, however, a wide divergence between the provisions of the laws and the administrative practices implemented by the Customs Service.

- Respondents noted repeatedly that Customs routinely issues internal orders of instruction, which are not published. These orders are often not consistent with the provisions of laws and regulations, and change frequently. Importers, exporters, and service providers have no advance notice if a new internal order will change the requirements applied to a particular shipment, and indeed have no basis to know whether the requirements for a given shipment are the result of an internal order or the whim of the Customs officer.
- Moldova is a member of the WTO and thus has acceded to the WTO Agreement on Customs Valuation. The provisions of the Agreement, making allowances for wording modifications in translation, are reasonably well reflected in the Customs Tariff Law. In practice, however, respondents noted consistently and repeatedly that Customs officers routinely make use of reference prices and Customs-formulated tables of minimum values (which are specifically prohibited by article 7(2) of the WTO Customs Valuation Agreement) to determine Customs values, instead of the declared transaction values. This happens even when the importer is able to confirm the declared transaction values as accurate. A senior Customs official interviewed denied that the Customs Service uses reference prices or minimum values. However, the responses on this issue were inconsistent. The officer claimed that declared transaction prices were often unreliable.

Because it was difficult to identify comparable importations of identical or similar goods or to use the deductive or computed methods of valuation, recourse was generally made to the residual valuation method. Asked how a value was determined under the residual method, the officer responded that they would usually look at importations of identical or similar goods, which contradicts the earlier assertion that it is difficult to identify comparable importations of identical or similar goods.

- Tariff classification appears to be determined in many cases by reference to comparative duty rates of tariff items under consideration in order to select a classification with a higher duty rate. In contrast, tariff classification should be determined through use of the General Rules of Interpretation and the Legal Notes to the Harmonized System Nomenclature as required pursuant to the HS Convention. Private sector respondents noted that Customs officers use lists of general descriptions of goods and tariff items to be applied, rather than the Tariff itself, in making classification determinations. A Ministry of Finance official confirmed the issuance by the Customs Service of internal directives containing tariff classification lists. As described in the chapter on Paying Taxes, inflated valuations by the Customs Service creates problems in tax administration. The Customs Code makes provision for selective examination through risk management, but in practice certain categories of goods and documents are subjected to 100 percent examination with no consideration of the relative risk of such categories. For example, all parcels imported through courier companies are examined. All certificates of conformity with Sanitary and Phytosanitary standards are subjected to 100 percent verification -- not by officers with competence to evaluate the conformity of the goods, but simply to confirm that requisite stamps and signatures have been obtained on the certificate.
- After passing through the border offices, imported shipments may subsequently be subjected to roadside examinations by Customs mobile inspection teams or central anti-fraud teams. If these teams identify what they determine to be underpayments of duties or taxes, they will make additional assessments and also may launch punitive action against the Customs officer who processed the shipment at the border. This practice discourages border officers from allowing shipments to proceed without inspection, even if the shipment has been identified by the system as a low-risk, green channel shipment. It constitutes an opportunity for Customs inspection teams to extract additional unjustified official and unofficial payments from importers and transporters.
- The Customs Code allows up to eight days to complete a transit movement of goods under Customs control. The Customs Service, however, routinely limits transit movement permissions to eight hours to and from the Ukrainian border, and four hours to and from the Romanian border. This causes hardships to the transporter and may result in assessment of penalties for late arrival at the Customs transit destination point, despite the transporter's best efforts to meet the official deadline.

C2. Advance Rulings

The Customs Code provides for issuance of rulings in advance of importation on the tariff classification of goods by the Customs Service. Such rulings should be considered binding so long as the goods imported match the particulars stated in the request for the ruling. This

provision has not been used to date, but the Customs Service has indicated that it intends to implement a binding ruling program soon. Under the program envisaged by the Customs Service, rulings would also be issued on the determination of the origin of imported goods, but not on questions of valuation determination.

C3. Need for Training

Respondents noted that Customs officers often do not have a good understanding of the provisions or the procedures they are administering. In addition to issues in the determination of tariff classification and Customs value noted above, private sector respondents identified difficulties and delays encountered in the processing by Customs officials of ATA Carnets and courier shipments. Respondents suspect this situation was due not only to a lack of training offered to Customs officers, but also to the Department's policy of rotating officers frequently. Experienced officers are routinely replaced by officers transferred from other areas who have to learn the job anew.

The Customs Service has a training center, but other than a small administrative staff, there are no permanent training resources in place. The training center has no budget established to deliver training. Most of the training delivered at the training center is offered by donor agencies. This limited training is delivered on an ad hoc basis by Customs supervisory personnel seconded on a course-by-course basis. No developed training modules are on file in the training center other than compilations of acts, regulations, and procedures that might apply to certain functions.

C4. ASYCUDA Declaration Processing

The United Nations Conference on Trade and Development (UNCTAD) has developed a computer software platform designed for the processing of Customs declarations, entitled Automated System for Customs Data (ASYCUDA). Various versions of this system have been installed in and are being used by the Customs authorities in 97 countries around the world. The latest version of this software, entitled "ASYCUDA World," is available in a web-enabled, on-line platform. The Customs Service of Moldova uses ASYCUDA World for automated processing of declarations. Pursuant to the Customs Code, the only acceptable means by which a declaration can be presented to Customs is through input to the ASYCUDA system by the importer/exporter or his agent. The ASYCUDA system in Moldova is generally functioning correctly, but processing delays are routinely and frequently encountered due in part, apparently, to inadequate capacity of the server on which the software is installed. Because the Customs Service does not process declarations on the weekends except for perishable shipments, processing is routinely delayed on Mondays and Fridays due to increased volumes of declarations to be processed before and after weekends. Additional delays or service outages that occur at unpredictable times were often reported. Customs Service interviewees indicated that the Customs Service has requested funds from the Government to purchase a second server, not only to provide additional processing capacity but also to provide for the automated backup of data in case of a breakdown of the primary system. The Customs Service expects to be able to purchase a second server early in 2013.

There is currently no mechanism being used for the backup of data other than periodic download of a copy of the database to tapes. Procedures have been developed to continue processing off-

line if the system goes down, but they have not been implemented. In practice, if the system goes down, processing stops, new declarations are not accepted, and imports and exports are held up until the system comes back on-line. Furthermore, respondents indicated that the Customs Service may apply a penalty for failure to comply with deadlines, even when delays were caused by unavailability of the server.

C5. Corruption

The perception of corruption within the Customs Service stands out as the paramount issue affecting the import and export of goods. Although Customs officials did not acknowledge actual corruption, the Customs Service noted in its Strategic Plan for 2012-2014 that Customs “has an image of a highly corrupted institution.” Respondents other than Customs Service officials, both in the private sector and other government ministries and agencies, were of the view that payments to Customs officers are routinely required in order to avoid additional delays, the mis-routing of documents, or the imposition of additional requirements or stipulations that might be set out in internal orders or might simply be the invention of the officer. Customs Service officials interviewed, however, characterized the issue as more a matter of perception rather than necessarily fact.

C6. Lack of Transparency

Lack of transparency is a significant problem in the Customs Service. As noted above, internal orders and instructions are routinely issued within the Customs Service and are not published. The Customs Tariff Law is not transparent. A Customs Consultative Committee was established in 2007 at the national headquarters level to provide a mechanism for consultation with and feedback from the private sector, but the Customs Service has not convened any meetings of this Committee since spring 2010. Although three of the regional offices of the Customs Service have continued to convene regional consultation meetings on a quarterly basis, private sector respondents unanimously indicated that the headquarters level has been entirely unresponsive to any attempts they have made to seek clarification or redress of issues or to submit suggestions for the improvement or simplification of processes.

C7. Processing Delays

Delays in the processing of imports and exports are endemic. In addition to actual processing time delays, line-ups at the border of trucks awaiting processing can approach four hours or more for both imports and exports. While the official statistics published by the Customs Service reflect a standard processing time of roughly 30 minutes, this figure appears to be based on a consideration solely of the time applied directly by an officer to complete specific steps in the process (in other words, a start-stop clock), with no consideration of the actual elapsed time required for a shipment to get through the process from entry into a Customs control area to release. Private sector respondents indicated that it usually takes at least three to four days for an importation to complete the process and at least two days for an export shipment.

As noted above, the Customs Service does not process declarations input into the ASYCUDA system on weekends except for perishable shipments, so additional time is lost two days each week. Delays are also imposed overnight on weekdays, as the Customs Service will process

declarations input into the system only from 9:00 a.m. to 5:00 p.m. Mondays to Fridays. Customs officials indicated that they will process declarations for a further two hours on weekdays for a service charge, but private sector respondents noted that service after 5:00 p.m. is virtually unobtainable. Private sector respondents noted as well that Customs Service declaration processing is often shut down early on Fridays as officers prepare to leave their offices for the weekend. These extended processing delays for import and export shipments are confirmed in the statistics presented for Moldova in the World Bank Doing Business report for 2013, an abstract from which is presented in the introduction to this section of the report. These delays impose huge costs on traders, and suppress Moldova's trade.

Exporters are required, pursuant to a Customs Service internal order, to export their goods through the border point closest to the location in which the exporting entity is registered, without consideration as to whether this border point is convenient to the location of the goods or the most efficient routing to the foreign destination.

In addition to verifying certifications issued by the Ministry of Agriculture, Customs officers at the border point may impose other documentation requirements on exporters of food products. In one recent instance described by respondents, Customs officers required an exporter of goods collected from small-holding farmers in Moldova to produce individual certificates of origin issued by each farmer from whom the goods had been collected, without which permission to export through the border point was denied. Respondents indicated that this exporter has now decided to move his operations to Romania.

When pressed with accounts from traders, Customs officials made some concessions to perceived inefficiency or lack of transparency in their processing. They agreed that the official estimate of 30 minutes does not represent the actual time required to complete the import or export process. Their revised estimate was that it would normally require one to two days to obtain release of an import shipment, and longer if it had been referred for examination, and slightly less time for an export shipment.

C8. Streamlined Procedures

The Customs Service has identified 38 entities as "Trusted Economic Operators" pursuant to a definition contained in the Customs Code, but there do not seem to be any privileges or special allowances attached to that status. The Customs Service has referred to streamlined procedures that it offers to low-risk entities which may or may not be "Trusted Economic Operators." To date, only six entities have been approved by the Customs Service to use "streamlined procedures." These procedures, however, are limited to the sole privilege of having import shipments delivered directly to their premises to await clearance by a Customs officer, rather than having them delivered to a Customs control office for clearance. All of the normal declaration and payment procedures still apply.

The Customs Code already provides a legal basis for most of the mechanisms required (such as selective processes based on risk management, and the acceptance of guarantees to ensure compliance with Customs Service requirements) to support true streamlined declaration and release procedures as defined in the standards and transitional standards of the WCO "Revised Kyoto Convention on the Simplification and Harmonization of Customs Procedures" (the

“revised Kyoto Convention”). Actual implementation of such mechanisms could greatly reduce delays.

D. SUPPORTING INSTITUTIONS

American Chamber of Commerce in Moldova (AMCHAM Moldova). AMCHAM Moldova is a non-governmental non-profit organization, founded on September 4, 2006. AMCHAM’s Mission is to promote American trade and investment in Moldova and to work with the Moldovan Government and business leaders to foster a more favourable business climate in Moldova for foreign trade and investment. AMCHAM Moldova’s membership, currently at roughly 74 members, is composed of a diverse spectrum of businesses, from large foreign investors to small goods and service providers that operate within Moldova, as well as Moldovan companies of all sizes that are pursuing trade with the United States. AMCHAM interviewees noted that they have prepared and presented to the government a number of position papers on various issues, but that their focus and expertise is more on tax matters and less on Customs and trade issues.

European Union Border Assistance Mission to Moldova and Ukraine (EUBAM). EUBAM was launched on November 30, 2005 following a request made jointly to the European Commission by the presidents of the Republic Moldova and Ukraine. EUBAM serves as a technical advisory body established and funded by the European Commission, mandated to enhance the border-management capacities (the border guard and customs authorities and other law enforcement and State agencies) of Moldova and Ukraine. By offering comprehensive support on EU best practices from its headquarters in Odessa and six field offices on either side of the Moldova/Ukraine common border, EUBAM envisages that border and customs procedures and standards in Moldova and Ukraine will ultimately mirror those prevalent in the European Union.

European Business Association in Moldova (EBA). EBA is an independent NGO established by 10 founders in the Republic of Moldova under the auspices of the EU Delegation. EBA’s objective is the alignment of the national economy and business legislation to EU standards, and the promotion of European values and business management practices in the Moldovan entrepreneurial community. Even though it was founded only one year ago, the EBA has already been very active in soliciting input from business contacts in Moldova and presenting Customs and trade issues to the Ministry of Finance and the Customs Service.

Supporting Institutions

- The American Chamber of Commerce in Moldova (AMCHAM Moldova)
- The European Union Border Assistance Mission to Moldova and Ukraine (EUBAM)
- The European Business Association in Moldova (EBA)
- The International Association of Road Haulers in Moldova (AITA)
- The Customs Brokers Association of Moldova
- The Moldovan Chamber of Commerce and Industry – Customs Brokers Association
- The Moldovan Freight Forwarders Association – Customs Brokers Association
- The Licensing Chamber
- The Moldovan Transport and Road Union
- The Moldovan Investment and Export Promotion Organization (MIEPO)
- The National Institute for Standardization and Metrology (NISM)
- The Association of Professional Accountants and Auditors of the Republic of Moldova (ACAP RM)
- Universities and Colleges in Moldova

The International Association of Road Haulers in Moldova (AITA). AITA is a non-governmental and non-commercial organization representing transport companies in Moldova. AITA is affiliated with the International Transport Union and is the authorized issuer of TIR Carnets in Moldova. AITA was incorporated on July 1, 1998, and has been very active during the ensuing years in bringing transport and trade issues to the attention of the government.

The Customs Brokers Association of Moldova. There are three Customs Brokers Associations operating in Moldova, apparently independently of and in competition with each other. Here, we refer to this as the largest of the three associations with 24 member brokers. The three associations do not appear to coordinate their efforts to bring issues to the attention of the Customs Service or relevant Ministries. In fact, they appear to be rather ineffective or unwilling to act as an advocate of the importing/exporting community to raise issues or concerns to the Customs Service. This is a disappointment, as the Customs Broker community in a number of other countries has been an influential advocate for Customs procedural and regulatory reform. There is currently no evidence of this in Moldova, but there is potential to make the existing association more effective in serving its members.

Moldovan Chamber of Commerce and Industry – Customs Brokers Association. This is the authorized issuer of ATA Carnets in Moldova. A total of 19 Carnets were issued to date in 2012, of which only one Carnet was able to pass through the border without the need for the Chamber to instruct the Customs officer how to process it. The Association operates one of the three Customs Brokers Associations in Moldova, as well as itself offering services as a Customs Broker.

Moldovan Freight Forwarders Association – Customs Brokers Association. This is an association of freight forwarders and commercial goods transporters operating in Moldova, and operates one of the three Customs Brokers Associations, as well as acting as a Customs Broker itself.

Licensing Chamber. The Chamber is an agency of the Ministry of Economy that issues authorizations to use tariff rate quotas on import, and export licenses under the voluntary export quotas agreed to by Moldova for the export of certain commodities to the EU. The Licensing Chamber also issues licenses to applicants who wish to operate as Customs Brokers. Following recent changes to the Customs Code, there is no test or criterion applied to confirm the knowledge of an applicant of Customs laws, regulations, or procedures. The only requirement is that an applicant for a Customs Broker's license has a business office, has a connection in place to the Customs Service ASYCUDA server, and posts a bond with the Customs Service to cover the contingent liability of any duties and taxes outstanding on the declarations to be presented. There is no requirement for an applicant to post a bond to cover professional liability to clients.

The official rates quoted by Customs Brokers to importers and exporters for their services appear to be in line with the cost of such services in other countries (around 20 Euros per declaration), but the additional amounts brokers apparently pay informally to get shipments through the process result in total service charges to their clients of an average of 120 Euros for an import declaration and 80 Euros for an export declaration. The knowledge qualification requirement was removed from the Customs Code for obtaining a Customs Broker license at the behest of the

Ministry of the Economy, ostensibly to align with EU regulatory provisions. The Ministry of the Economy holds the position that the Customs Brokers should be abolished. Given the apparent apathy of the Brokers Associations in their dealings with the Customs Service on behalf of their clients, the Ministry of Economy's position is understandable. The challenge is to find or develop other mechanisms both in government and in the private sector by which to advocate for Customs reform, if competent and active Customs Brokers are not in place as an effective advocate for regulatory and procedural reform in Customs administration.

The Chamber of Commerce and Industry is attempting to establish an industry standard for a knowledge qualification requirement for anyone who wishes to offer their services in Moldova as a Customs Consultant. The standard proposed by the Chamber of Commerce and Industry would be similar to the knowledge qualification requirement previously contained in the Customs Code for licensed Customs Brokers – presentation of a certificate of completion of a customs-related course of studies at an educational institution – supplemented by a short test of five or six questions administered to applicants by the Chamber of Commerce and Industry.

Moldovan Transport and Road Union. This association represents passenger transport service providers such as bus operators operating between Moldova and other countries.

Moldovan Investment and Export Promotion Organization (MIEPO). MIEPO is an agency of the Ministry of Economy. MIEPO's mission is to support business development and partnership in Moldova through involvement, communication, and promotion. MIEPO experts provide professional assistance for the identification and exploration of investment opportunities in the Republic of Moldova. In that capacity, MIEPO advocates that Ministries and agencies of the government address trade and customs issues that discourage foreign investment to Moldova or promote Moldovan export opportunities in foreign markets.

The National Institute for Standardization and Metrology (NISM). NISM is a government agency registered as a state enterprise. NISM's mission is to deliver quality service in standardization, metrology, and conformity assessment in order to create the normative, methodological, and institutional support for quality assurance and competitiveness of domestic products, consumer protection, and free regional and international circulation of goods.

Association of Professional Accountants and Auditors of the Republic of Moldova (ACAP RM). ACAP RM is a non-profit NGO that manages the profession of accounting in the Republic of Moldova. It is more fully described in the Supporting Institutions section of the chapter on Starting a Business.

Universities and colleges in Moldova. Many of the universities and colleges in Moldova offer courses of study leading to diplomas or degrees in international trade logistics, including Customs legal and administrative processes. A certificate of completion of such a program was accepted by the Licensing Chamber as sufficient to meet the knowledge requirement to be licensed as a Customs Broker. Unfortunately, this requirement was amended and the Chamber of Commerce and Industry is attempting to reinstate this requirement.

E. SOCIAL DYNAMICS

The Customs Service appears to be focused primarily on revenue collection, with little or no consideration of the impacts of its revenue collection policies on the Moldovan economy. As noted earlier, the Customs Service is generally unreceptive to input from the private sector in the development of its policies and procedures.

The uncertainty of costs and the significant delays encountered in the processing of imports and exports through the border constitute material constraints to the development of the Moldovan economy. Delays and impediments imposed by the Customs Service in the processing of exports at the border have a direct impact on the country's capacity to develop export markets for its goods, both by increasing costs to Moldovan exporters and by reducing their capacity to compete with exporters in other countries on delivery service times. Using a methodology developed by the World Bank and the USAID/TCBoost Project, delays and impediments imposed upon the processing of imports and exports can be demonstrated to have a direct impact upon trade volumes and the generation of GDP, as demonstrated in the tables below. As in the example concerning agriculture exports presented earlier, impediments imposed by Customs officers have even caused Moldovan entrepreneurs to relocate their operations to neighboring countries.

These tables demonstrate the effect upon the Moldovan economy of delays in the processing of imports and exports. The first table demonstrates the effect upon the Moldovan economy of delays in import and export processing as compared to processing times in other countries in Eastern Europe and Central Asia. The second table demonstrates the effect upon the Moldovan economy of delays in import and export processing as compared to processing times in OECD countries. If Moldova were to reduce the time to import and export to the average times of Eastern Europe and Central Asian members, trade volumes would increase by \$463 million annually, and GDP would increase about \$538 million. Reducing times to the average of OECD member nations would bring even larger increases – almost \$2 billion in annual trade turnover and more than \$2.2 billion in increased GDP.

Table I-4. Lost Trade Volume Compared to Eastern Europe and Central Asia

Lost Trade Volumes Caused by Delay (compared to EE and CA) *		
Total exports 2011		\$ 2,829.0 Million
Export losses caused by 6-day comparative delay	X 6% =	\$ 169.7 Million
Total imports 2011		\$ 5,357.5 Million
Import losses caused by 6 day comparative delay	X 6% =	\$ 321.5 Million
TOTAL TRADE LOSSES CAUSED BY DELAY		\$ 491.2 Million
Reduced GDP Caused by Delay (compared to E. Europe and Central Asia) * **		
GDP lost from six-day comparative export delay	=	\$210 Million
GDP lost from six-day comparative import delay	=	\$409 Million
TOTAL GDP LOSSES CAUSED BY DELAY		\$619 Million

Table I-5. Lost Trade Volume Compared to OECD

Lost Trade Volumes Caused by Delay (compared to OECD countries) *		
Total exports 2011		\$ 2,829.0 Million
Export losses from 22-day comparative delay	X 22 % =	\$ 622.4 Million
Total imports 2011		\$ 5,357.5 Million
Import losses from 25-day comparative delay	X 25 % =	\$ 1,339.4 Million
TOTAL TRADE LOSSES CAUSED BY DELAY		\$ 1,961.8 Million
Reduced GDP Caused by Delay (compared to OECD countries) * **		
GDP lost from 22-day comparative export delay	=	\$770 Million
GDP lost from 25-day comparative import delay	=	\$1,706 Million
TOTAL GDP LOSSES CAUSED BY DELAY		\$2,476 Million

* From data drawn from the World Bank “Doing Business” report presented in the introduction to this section.

Trade Volume impact calculations made on the basis of the World Bank “Time to Trade” study.

** GDP impact calculations made using the Trade Facilitation Impact (TFI) Calculator developed by the USAID TCBoost project (www.tboostproject.com/resources/tools/impactcalculator.php?country_id=135#input).

With reference to the second table, it is not inappropriate to compare Moldova to OECD countries, as there are a number of nearby OECD countries that are, because of their proximity, potential trading partners/competitors to Moldova: the Czech Republic, Poland, the Slovak Republic, Slovenia, Hungary and Turkey. The point must be made, as well, that if these countries can achieve OECD levels of import and export delay reductions, there is no reason why Moldova cannot do the same. All that is required is the will to do it.

In addition to the economic benefits to Moldova from a reduction in processing delays, such a reduction would also improve Moldova’s ranking in the Doing Business Report. The following table indicates the effect that a reduction in processing delays for imports and exports could have on this ranking:

Table I-6. Effect of Delay Reduction on Doing Business Rankings

Moldova	Doing Business (Global Ranking)	Trading Across Borders Ranking
Current ranking for 2013	83	142
If delays were reduced by: Export – 6 days; Import – 6 days	83	136
If delays were reduced by: Export – 22 days; Import – 25 days	73	92

F. RECOMMENDATIONS

Based on the assessment conducted, the following recommendations are offered:

- *Eliminate or reduce the Customs Service's issuance of internal orders, and require publication of new orders prior to implementation.* Internal orders should be vetted by the Ministry of Finance, and to the extent needed based on jurisdiction, the Ministries of Economy, Agriculture, and Transportation. This greater transparency will help enforce Moldova's compliance with international treaty obligations like using minimum or reference values, for example, to determine the customs value of important goods, which is prohibited by the WTO Customs Valuation Agreement. Meanwhile, the government should take steps to eliminate unnecessary and duplicative checks and stamp/approval signature requirements. This could be done, for example, as part of a regulatory and procedural guillotine process; such as has already been undertaken successfully by the government in other areas.
- *Establish an effective mechanism of consultation and feedback between the Customs Service and the private sector.* The Customs Service has chosen not to convene since March 2010, and the administration of this mechanism should be set up in such a manner that all interested parties will have the opportunity to participate in meetings that will be scheduled on a regular basis, with provision for a formalized process of follow-up and feedback on the recommendations and action items presented in official minutes taken at the meetings. Ideally, the private sector should be encouraged to take on the role of administrator and secretariat of this mechanism of consultation and feedback, so as to gain their willing participation and support in the implementation of legal and administrative reforms. The Customs Service representative at the Roundtable discussion of this recommendation expressed support for greater private sector involvement in managing the consultative process.
- *Reconsider Customs Service policies in the application of risk assessment techniques to support the full implementation of selective examination based on risk assessment.* The conduct of supplementary roadside examinations of imported shipments by Custom mobile inspection teams and Customs anti-fraud teams should be discontinued.
- *Expand the processing of declarations to 7 days per week, and at least 16 hours per day.* Even if this expansion in the processing of declarations by the Customs Service were made subject to the assessment of special service charges, it would be of significant benefit to importers and exporters by eliminating the additional waiting time currently imposed on shipments overnight and on weekends. Expansion of processing days and hours of service would also help the Customs Service by smoothing out the system workload, thereby reducing or eliminating processing backlogs due to capacity limitations. Additionally, procedures should be implemented by the Customs Service to continue off-line processing of declarations during any service outage of the system, and to update the system database with the declarations processed off-line as soon as the system is restored to operation.

- *Train Customs officers and the private sector on Customs' legislative and regulatory provisions, especially those provisions that are in compliance with international agreements.* Not only should the delivery of training courses to students be required, but also the development and delivery to the Customs Training Center of training packages and methodologies to support and encourage their ongoing delivery of the courses on a self-sustaining basis. Even if the Training Center does not receive a budget allocation from the Customs Service for the delivery of training, such training packages and methodologies could at least support the delivery of training by the Training Center to the private sector on a cost-recovery basis.
- *Develop and implement an effective anti-corruption strategy and operational anti-corruption program.* Corruption, or at least the perception of corruption, is endemic in the Customs Service. To combat this, the Customs Service needs to develop and implement an effective strategy and operational anti-corruption program. Some successful anti-corruption programs in other countries have included a raise in salaries and operational bonuses for revenue agency officers offer a living wage, together with the establishment of severe penalties (including dismissal and prosecution) for corrupt behaviour, applied rigorously and without tolerance.
- *Eliminate or reduce the frequent rotation of officers in order to establish consistency and loyalty, as well as reduce the time it takes to continually train new officers.* Officers are either well-trained and leaving posts or untrained and unfamiliar with the requirements of their position, which in sum increases opportunities for corruption and decreases effectiveness and expediency.
- *Streamlined Customs clearance procedures.* Develop a mechanism by which an assessment can be made (based upon historical compliance patterns and other relevant factors) of the potential risk of non-compliance posed by a particular shipment, and thereby a determination can be made as to whether the shipment may be permitted to be released without examination. Incorporate a provision by the importer, or the Customs broker on his behalf, of a surety bond or other guarantee to ensure that declaration and payment requirements will be complied with after the goods have been released from Customs. Such a surety bond could be submitted with respect to an individual importation, or as an ongoing surety submitted with respect to all importations to be made over a period of time (an annual surety bond, for example). There are three procedures currently in use by the Customs Administrations of other countries that could potentially be considered in Moldova. The Customs Code of the Republic of Moldova already provides the legal basis by which streamlined Customs procedures could be implemented.
- *Establish a mechanism to consolidate import entry payments on a monthly basis to reduce administrative costs for both the importer and for the Customs Service, as there would be fewer individual payments to account for.* The concern to be addressed in setting up such a consolidated payment system is to ensure that the Government is protected from the possibility of default. This assurance can be accomplished by requiring applicants for consolidated payment privileges to post a surety bond to provide sufficient cover for the full amount of duties and taxes estimated to be owed on that

importer's importations during any monthly period. Under current procedures, importers are required to make a separate payment for each individual Customs import declaration to acquit the Customs duties and other taxes and fees assessed on that declaration. To administer a consolidated payment system, an office should be designated in the Customs Service to accept and control surety bonds provided by the importer or his agent to guarantee the payment of import duties, and track imports and issue consolidated monthly invoices to clients who have been granted this privilege. The ASYCUDA Customs computer system in use in Moldova already has the capacity to prepare periodic reports of import activity by any particular importer.

- *Institute an administrative procedure by which importers or their agents are permitted to submit Customs release documentation in advance of the actual arrival of the goods being imported, so that the Customs Service can review the documentation and determine if examination of the goods is required upon their arrival or if the goods can be released immediately upon arrival.* Subsequent to the arrival and release of the goods, the importer or his agent confirms the release documentation through the submission of a fully completed Customs import declaration, and payment is made of any duties and taxes applicable. The computer wide-area network required to ensure timely communication between Customs clearance offices and Customs Service headquarters to support the administration of this program is in place in Moldova.
- *Institute a program of release on minimum documentation, by which imported goods may be released from Customs control very quickly on provision of a legislatively defined basic minimum of information and documentation, on condition that a complete Customs import declaration is submitted and payment of duties and taxes is made by the importer or his agent within a specified period following the release of the goods.* Many Customs Administrations have instituted such programs. The documentation usually required as a release package consists of the waybill, the commercial invoice, any required import permits or certifications of conformity with product standards, and a Customs barcoded cover sheet that links to the importer's or broker's file in the computer system so that the release information can be input to the system.

Implementation of such a procedure requires a computer system that has the capacity to track and acquit release entries against subsequent fully completed Customs import declarations, and to identify and report for follow-up action any release entries not acquitted within the specified time frame. The computer system also must have the capacity to develop importer risk profiles based upon historical compliance information. The ASYCUDA Customs computer system in use in Moldova can already do this.

The compliance issue to be addressed in setting up a release on minimum documentation system is to ensure that the government is protected from the possibility that an importer will fail to present a full Customs import declaration and the payment of duties and taxes after the imported goods have been released from Customs control. This can be accomplished by requiring applicants for release on minimum documentation privileges to post a surety bond sufficient to cover the full amount of duties and taxes estimated to be owed at any one time on that importer's importations which have been released but for which a full Customs accounting has not yet been presented.

In the administration of a release on minimum documentation system in Moldova, a designated office in the Customs Service would accept and control surety bonds provided by the importer or his agent to guarantee the payment of import duties, and track release acquittals and initiate any required follow-up action with respect to released imports for which a subsequent full Customs accounting has not been presented within required time limits. The ASYCUDA Customs computer system already has the capacity to prepare periodic reports of import activity by any particular importer.

The Customs Service representative at the Roundtable discussion of this recommendation noted that the Customs Service has established as an objective to develop and implement the streamlined release mechanisms reflected in the revised Kyoto Convention.

The key benefit of implementing in Moldova streamlined Customs clearance procedures such as those noted above is not only to speed up the import process, but also to remove, as far as possible, the opportunity for a Customs officer or the Customs Service to use physical control of the imported goods to extract unjustified payments. However, streamlined Customs clearance processes cannot work well if most importations are routinely subjected to examination. Procedures must be established by which the Customs Service can identify the relatively small proportion of importations that pose a legitimate risk of non-compliance, and focus its enforcement efforts on that group of imports.

SECTION II. PAYING TAXES

A. INTRODUCTION

Taxes have been a crucial foundation for civilizations for centuries. Although generally loathed by those who must bear them, optimally applied taxes can further the advancement of a society. While debates over tax rates often garner the most publicity, taxpayers often cite the compliance costs of paying taxes as the most burdensome aspect of a tax system. In this regard Moldova is no exception, as multiple respondents, representing small to large taxpayers, cited compliance burdens as the most problematic tax area. Compliance burdens may be created by ambiguous or insufficient legislation and normative acts, or by the manner in which taxes are administered. The burdens arise not only when making payments and filing tax declarations but in other areas as well, such as when registering or liquidating a business.⁷ While tax compliance burdens alone are significant, the combination of tax and customs burdens is a lethal combination in Moldova, prompting many businesses to conduct activities but evade taxes in whole or in part,⁸ or, as was heard repeatedly, forego business opportunities altogether in Moldova. (See text box above.)

A1. Tax Revenues

Tax revenues collected in Moldova in 2011 are provided in Table II-1, at right.⁹ Challenges in designing and implementing a tax system that is conducive to business activity are exacerbated by the government's need to meet established revenue targets. In many developing countries including Moldova, the need to satisfy revenue targets may sometimes prevail over the practice of collecting only those taxes legally and currently due. This results in increased pressure being placed on compliant taxpayers who are within the "tax net" and therefore more likely candidates to produce needed tax revenues, whether or not legally owed. Such pressure forces many compliant taxpayers into the shadow economy, making it even more difficult for the government to meet future

Losing Businesses

"I know many businesses that have closed in Moldova and moved to Romania or Ukraine because of constant customs and tax problems here."

—Small business owner

Table II-1. Moldova 2011 Budget

Total Revenues and Grants	30,139.7
Revenues	28,434.6
Tax Revenues	25,303.3
Profit Tax	571.4
PIT	1,769.1
VAT	10,464.3
Excises	2,666.7
Foreign Trade Taxes	1,179.3
Other Taxes	452.4
Social Fund Contributions	6,562.6
Health Fund Contributions	1,637.5
Non-tax Revenues	1,455.7
Revenues of Special Funds	1,675.6
Grants	1,705.1
Budget Support Grants	922.8
Foreign financed project grants	662.8
Other Grants	119.5

⁷ These issues are addressed in the chapter on "Starting a Business."

⁸ While difficult to measure, according to one estimate approximately 40 percent of economic activity in Moldova is conducted in the shadow (grey) economy.

⁹ Revenue data is from the Ministry of Finance website, www.mf.gov.md.

revenue targets. The resulting paradigm is unsustainable in the long-term.

A2. “Paying Taxes” Indicator

The “Paying Taxes” indicator has three equally weighted elements – Payments, Time, and Total Tax Rate. Moldova’s performance on the Doing Business 2013 report is summarized in Table II-2, at right.¹⁰ Moldova ranks 109th of 185 countries in Paying Taxes on the 2013 report. This is a decrease of three positions compared to Moldova's rank of 106 for 2012. Moldova’s score of 48 on the Payments element ranks 165th of 185 countries surveyed. It takes Moldovan taxpayers about 220 hours to make their tax reports and payments, which ranks 94th. Moldova’s Total Tax Rate of 31.2 percent, is not high, ranking 48th.

Table II-2. “Paying Taxes”

Indicator	Score	Rank
Payments	48	165
Time	220	94
Total Tax Rate	31.2	48
Overall		109

The computation of the 48 payments that Moldovan taxpayers make each year is shown in Table II-3, left. This ranking could be significantly improved by introduction of e-filing for relevant taxes, especially for social insurance, health insurance, and value added tax, which each have 12 payments annually. When e-filing is available and used by at least 50 percent of taxpayers, the number of payments for the particular tax is counted as one, though the actual number could be higher. Thus, if e-filing were introduced and used by at least 50 percent of affected taxpayers, the number of payments for these three taxes would drop from a total of 36 to just three.

Table II-3. Computation of Number of Payments

Tax or Mandatory Contribution	Payments/Year
Social security (fund) contributions	12
Health insurance (fund) contributions	12
Land improvement tax	4
Fuel tax	1
Road tax	1
Tax on immovable property	4
Land tax	1
Corporate income tax	1
Value added tax (VAT)	12
Total Payments	48

In fact, Moldova’s 2013 Paying Taxes rank should have been higher. Five new taxes were added in 2012, all of which require quarterly payments. If just three of those five taxes apply to the hypothetical taxpayer used for the “Paying Taxes” indicator, the number of Payments would increase by 12, from 48 to 60. As shown in Table II-4, at right, this would worsen Moldova’s overall rank to 117th, without including the increase in Time and Total Tax Rate.

Moldova could reduce compliance burdens on business and improve its ranking by combining the reporting for the social and health insurance taxes. These require the same basic information, and it makes more sense to require two government agencies to share information than for tens

¹⁰ For further information on the Paying Taxes indicators refer to the Doing Business Indicator at www.doingbusiness.org.

of thousands of Moldovan taxpayers to provide the same basic information twice and make two separate payments. Combining the two would reduce the 24 payments now required to 12. Implementing e-filing for VAT would reduce 12 payments to one for Doing Business scoring purposes. The total reduction in the number of payments from these

Table II-4. Reported, Actual, Reformed

Indicator	DB 2013	Actual 2013	DB 2014 Reformed
Payments (Number) ²	48	60	37
Time (Hours) ³	220	228	228
Total Tax Rate (% of Profits)	31.2	31.2	31.2
Overall Rank	109	117	93

two measures would be 23 payments, reducing Moldova’s Payments score from the actual 60 to 37, and improving its overall ranking to 93rd on “Paying Taxes.”¹¹

A3. BizCLIR Scoring

The assessment of Moldova's tax system that follows was based on meetings held with multiple stakeholders and a review of USAID project reports (including reports drafted by BIZPRO and BIZTAR), numerous detailed IMF reports,¹² and other reports and surveys. Based on the assessment findings, the general scoring of the four pillars in the Paying Taxes chapter is shown in the textbox. Possible scores range from 1 (strongly negative) to 5 (strongly positive).

Paying Taxes Scores	
Pillar	Score
Legal Framework	2
Implementing Institutions	2
Supporting Institutions	3
Social Dynamics	2

B. LEGAL FRAMEWORK

B1. Tax Provisions Contained in the Constitution, Legislation, and Normative Acts

Articles 58 and 132 of the Constitution of the Republic of Moldova, adopted on July 29, 1994, establish the legal framework for the current tax system.

Article 58. Financial Contributions

- (1) All citizens are under obligation to contribute by way of taxes and financial impositions to public expenditure.
- (2) The system of legal taxation must ensure a just distribution of fiscal burdens over the population.
- (3) All taxation other than that established by law is forbidden.

Article 132. Fiscal System

- (1) All tax duties, and other revenue of the national budget, including the national social security budget, also the district town and village budgets shall be established under the law by the representative agencies, as required.

¹¹ Predictions about where Moldova will rank in 2014 assume that other countries do not also implement reforms that will improve their rankings.

¹² The report, *Taking Compliance Management Further*, issued by the IMF's Fiscal Affairs department in April 2012, as well as other reports issued by the IMF, provided relevant information for this assessment.

(2) Any other types of taxation are forbidden.

The primary law¹³ governing taxes in Moldova is the Tax Code of the Republic of Moldova ("Tax Code"), and its amendments. The Tax Code was drafted with donor assistance, and is based in part on the WB's model Basic World Tax Code. The first titles of the Tax Code became effective in 1998.¹⁴ Additional titles to the Tax Code were added through legislation passed from 2000 through 2006. The Tax Code has been amended frequently since 2006. The most recent amendments became effective in January 2012. The Tax Code appears to be gender neutral.¹⁵ In general, the tax rates are competitive with those imposed by other countries, including countries in the region. Some of the more significant taxes imposed on legal entities and individuals are listed in the following table.¹⁶

Table II-5. Taxes Imposed in Moldova

Tax	Rate
CIT (legal entities)	12% of taxable income*
CIT (SME legal entities)	3% of revenues**
CIT (farming enterprises)	7% of taxable income
Capital gains	50% of gain is subject to tax
VAT	20% (standard rate, lower rates applied to certain types of supplies)
PIT (residents)	7% on annual income up to MDL 25,200, 18% on income exceeding MDL 25,200
Social fund contribution (employee)	6%, subject to cap
Social fund contribution (employer)	23%, subject to cap
Health fund contributions (employee and employer)	3.5%

* From 2008 through 2011, the CIT rate was 0 percent. For legal entities whose income is estimated through indirect methods, a CIT rate of 15 percent is applied on the excess of taxable income over accounting gross income.

** The 3 percent tax on revenues is mandatory for entities with operating revenues of less than 100,000 MDL during the previous year, and is optional (i.e. they may use this method or the standard income tax method) for entities with revenues of 100,000 to 600,000 MDL during the previous year.

¹³ Other laws affect taxation, including: The Customs Code of the Republic of Moldova (RM) (nr. 1149-XIV, 20.07.2000), the Law of the RM on Free Economic Zones (nr.440-XV, 27.07.2001), and laws and decrees intended to establish a more favorable business and investment climate, including Law No. 424-XV dated 16.12.2004, Law No. 235-XVI dated 20.07.2006, Government Decision No. 317 dated 18.07.2003, and Government Decision No. 1429 dated 16.12.2008). For a list of relevant tax laws, normative acts, and reports prepared by international organizations see *Annex 2 of The Development Plan of the Moldovan State Tax Service for 2011-2015* issued by the STI.

¹⁴ The initial Tax Code became effective through Law No.1164-XIII of the Republic of Moldova of April 24, 1997 on application of Titles I and II of Tax Code and through Law No. 1417-XIII of December 17, 1997 of the Republic of Moldova on application of Title III of Tax Code.

¹⁵ A current English version of the Tax Code is not available from the public or private sectors. No normative acts are available in English on the STI's website.

¹⁶ For a list of taxes and fees see Articles 6 and 289 of the Tax Code. The information in Table II-5 is from *Investing Guide Moldova 2012* published by MIEPO and PricewaterhouseCoopers.

Excise duties are imposed on a number of goods in Moldova, including but not limited to:

- alcohol products
- tobacco products
- fuels
- jewelry
- precious metals
- motor cars and other motor vehicles

For a complete list of goods subject to excise duties and applicable rates refer to Title IV of the Tax Code. Revenues collected from excise duties continue to be low compared to EU countries. Excise rates are expected to be harmonized with EU minimums in the medium term, which may lead to increased tax evasion if tax and customs administration remain at current levels.

Moldova has entered into conventions for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital ("conventions"¹⁷) with more than 40 countries. Most of the conventions are based on the OECD Model Tax Convention on Income and Capital, and Moldova applies OECD commentaries when interpreting the conventions. Legislation¹⁸ states the common practice that, in the event of a conflict, convention provisions control over domestic legislation. However, paragraph 2 of the same article provides an exception to this rule, which is not clear to many tax practitioners. Existing Moldovan legislation and normative acts do not adequately address certain complex tax issues, such as transfer pricing (governing transactions between related parties in different tax jurisdictions).¹⁹

Moldova allows preferential tax (and customs) regimes for enterprises that engage in certain types of activities in any of the seven Free Economic Zones (FEZs)²⁰ that have been established in Moldova.²¹ According to a report prepared by the MOE, as of July 1, 2012 there were more than 160 "residents" of the seven FEZs (including 60 in the Expo-Business-Chisinau FEZ and 37 in the Ungheni-Business FEZ) that employ more than 6,000 individuals. FEZ residents are protected "from worsening of tax and other regimes," and may, within a specified period, elect to be subject to "old" laws. FEZ residents are granted the following corporate income tax (CIT) and VAT incentives:

¹⁷ Tax conventions are also referred to as "tax treaties."

¹⁸ See Article 4(a) of the Tax Code.

¹⁹ Issues pertaining to permanent establishments (PEs) are not a high priority, as few businesses operate in this form in Moldova.

²⁰ FEZs are also addressed in the Trading Across Borders chapter of this assessment.

²¹ Industrial Parks (IPs) are also used in Moldova to create a favorable tax and customs regime for those enterprises that have been designated as an IP. In 2010-2011 three enterprises obtained the title of an IP. IP incentives include but are not limited to: entitlement to privatize public property land associated with construction; free-of-charge transfer of public property assets; and changes in the category of certain land.

- Application of 50 percent of the applicable CIT rate on gains earned on goods exported from the FEZ to outside the customs territory of the RM, and application of 75 percent of the CIT rate on other gains;
- Income from the export of goods or services originating in the FEZ is exempt from CIT for a period of three years if the resident invested a capital equivalent of at least USD 1 million in the fixed assets of its enterprise and/or in the development of the infrastructure of the FEZ (five year exemption for an investment of at least USD 5 million); and
- Goods and services supplied in the FEZ from abroad, outside the customs territory of the RM, and from other areas of Moldova; and goods and services supplied to other FEZ residents are subject to 0 percent VAT.²²

FEZs or their equivalent are utilized in other countries, often with limited success. Rather than authorize FEZs that serve to reduce tax revenues while benefiting only selected enterprises, a country the size of Moldova may be better served by creating a tax climate that is conducive to all current and future economic activity, regardless of location, industry sector, or type or size of investment.²³ A cost/benefit analysis of FEZs should be undertaken to determine if such preferential tax regimes are justified.

Normative acts²⁴ comprise regulations (sometimes referred to as instructions), Government decrees, and other pronouncements issued by the Government or State Authorities. Normative acts cannot conflict with

underlying legislation, but many respondents stated that this rule is often violated. Beginning in 2003, three "Guillotine" projects were implemented by State Authorities (with donor assistance) to eliminate unnecessary regulations and permissive acts and to amend legislation in order to improve the regulatory environment.²⁵ Even with these regulatory improvements, a Member of

IMF Statement on Tax Preferences Granted in Moldova

All major tax initiatives in Moldova since 1998 have resulted in reduced taxation – both lowering the tax rates and narrowing the tax base. The decline in rates should have been accompanied by an enlargement of the tax base, particularly by abolishing tax preferences and exemptions.[Footnote omitted] While reducing the initially high rates may have been beneficial for growth in the beginning, the process went overboard by 2008, with detrimental effect to structural revenues [Table omitted]. Narrowing the tax bases was the opposite of what is usually recommended - broaden the tax base by gradually eliminating all existing exemptions and incentives. There are many arguments against tax incentives (Box omitted) and much of the complexity of tax system typically comes from exemptions and incentives. Enlarging the tax base according to the most widely used international practices would make the system more transparent, stable and understandable, including for foreign investors.

IMF Working Paper, *Fiscal Policy Response to External Crises: The Case of Moldova 1998-2010*, issued in March 2012, p. 7.

²²Information obtained from *Investing Guide Moldova 2012* published by PricewaterhouseCoopers and MIEPO.

²³ Additional tax incentives, including incentives for IT companies, investments in fixed assets, and the creation of new jobs in particular industries, are also granted through the Tax Code.

²⁴ Very few normative acts concerning taxation are available in English.

²⁵Under Guillotine 1 over 1,000 regulations were reviewed and hundreds were abolished. Guillotine 2 resulted in changes to legislation to improve regulations, while Guillotine 2+ eliminated unnecessary acts and those without legal justification.

Parliament recognized that normative acts are still used to circumvent tax legislation passed by Parliament. More distressing is the general recognition by all respondents that this practice cannot be readily abated.

The most common complaint raised by all respondents is the lack of consistency in the application of laws and normative acts. Many believe amendments to legislation alone will eliminate such inconsistency. However, international experience suggests that a number of additional reforms (e.g., expanded public outreach by the STI and by associations, increased training of STI staff, stiffer sanctions imposed on STI staff who intentionally disregard laws and normative acts, and improved dispute resolution mechanisms) must be undertaken to create an environment where tax laws and normative acts are applied on a consistent basis and in a transparent manner.

B2. Substantive and Procedural Tax Issues

Associations, accounting and audit firms, companies, as well as Moldovan tax experts, have compiled lists of problematic tax issues that they would like to see reviewed and remedied through legislative amendments or normative acts.²⁶ Possible issues for review include:

- Simplification of procedures concerning branches of legal entities
- Clarification of deductible expenses (especially with respect to entrepreneurs)
- Review of multiple VAT issues (including advance payments and refunds)
- Review of mandatory imposition of three percent tax on revenues for small businesses
- Possible combination of income tax, social fund,²⁷ and health fund filing and payments
- Possible reduction in payment and filing requirements for local taxes²⁸
- Improvement of the tax appeals system (described below)
- Imposition of fines and penalties for tax violations (described below)
- Additional guidance for taxation of partnerships
- Clarification of changes in the calculation of depreciation

The purpose of this assessment is not to review and comment on each of the possible tax issues that have been raised by both the public and private sectors. Rather, it is to assess the overall

²⁶ For example, see *AvizAmCham_PoliticaFiscala_21.05.2012_final*. At the time of this assessment the report had not been translated into English.

²⁷ As part of a review of social fund contributions, the potential labor and tax impact of the 23 percent social fund contribution rate (subject to a cap) imposed on employers should be addressed.

²⁸ There are 17 reports required for local taxes. Combining these reports to the extent possible (preferably into a single report) will significantly reduce taxpayer compliance burdens.

need for amendments to tax legislation in order to reduce problematic tax policies and procedures. Almost all respondents, from both the public and private sectors, cited the need for amendments to the Tax Code (through specific amendments or complete redrafting of some titles) as a high priority for reform. As described below, any proposed changes to tax legislation must consider input from the private sector. Prioritizing problematic tax issues and initiating a process that provides the private sector with greater input during the design and drafting of tax legislation and normative acts are two related reforms that are included in recommendations provided at the end of this chapter.

B3. Legislative and Normative Act Process

The process of formulating, drafting, and enacting legislation and normative acts (including regulations and Government decrees) is an area in need of substantial reform. According to most respondents, although one or more procedures exist that provide for a working group or committee to participate in the discussion of possible amendments to tax legislation, these procedures are neither very effective nor applied on a consistent basis. According to respondents, the legislative and regulatory processes are often not transparent, and the private sector rarely is provided adequate input. Furthermore, the process is often not well-coordinated among public sector stakeholders (Parliament, MOF, STI, and other stakeholders). According to respondents, RIAs are rarely performed for proposed tax legislation, although such assessments, possibly conducted in cooperation with the private sector, would likely improve the quality of the legislation. Further discussion of this process is provided in the Social Dynamics section of this chapter.

B4. Tax Dispute Resolution Mechanism

Taxpayers electing to dispute a tax assessment issued by the STI may appeal their assessment through the following appeals process, starting at the administrative appeals level and proceeding to the judicial level,²⁹ as shown in Table II-6, at right.

Table II-6. Tax Appeals Process

Level	Review Body
Judicial	Supreme Court
	Court of Appeals
	Territorial (District) Court
Administrative	MSTI
	STI Municipal, UTA or Territorial (District) Office

The administrative appeal is filed at the same tax body that issued the decision or whose official issued the tax decision. Thus, the likelihood that a taxpayer will be successful at this appeal level is remote. The likelihood that the Main State Tax Inspectorate (MSTI) will find in favor of the taxpayer is also remote, as approximately 99 percent of cases appealed at this level are rejected. The current administrative appeals process is ineffective and time-consuming for both taxpayers and the MSTI. The first level review serves little purpose, and the review conducted by the MSTI lacks

²⁹ The tax appeals process is set forth in Chapter 17 of the Tax Code (Articles 267-274).

the independence required to produce an impartial administrative decision. The recommendations at the end of this chapter propose that a more independent review body be established at the administrative level and that the administrative appeals process be streamlined. Delegating the appeals function to an outside (non-government) review body, as some respondents have proposed, would create a number of significant problematic issues, and should be considered (if at all) with caution. Creating a mediation system for tax cases, as well as establishing a Tax Ombudsman, have been proposed in the past and may be considered again when designing a more effective tax appeals system.

Compared to the administrative appeals process, the judicial system offers a more independent review process, although it also suffers serious deficiencies. Most significantly, many judges do not possess adequate knowledge of tax legislation to decide the cases brought before them, and they receive infrequent and insufficient training in tax legislation. Respondents stated that it is not possible to establish a specialized court in Moldova with jurisdiction limited to tax issues. Providing increased tax training to judges (possibly jointly with STI staff), preferably to a limited number of judges who will be designated to hear tax cases, would greatly improve the judicial dispute mechanism.

In 2011, 1,396 tax cases were filed in the court system: 640 were filed against the STI and 756 were filed against the taxpayer. (No statistics were available on the number of cases appealed at the administrative level.) The vast majority of cases were filed in Chisinau, but a significant number were also filed in Hîncești, Cimișlia, Călărași and other districts.³⁰ According to one respondent, it takes at least one year, and often three or more years, for a case to be heard and a court decision to be entered due to the complexities of tax cases, the backlog of cases, and the limited number of STI staff who are available to represent STI in court. Judicial decisions are accessible through judicial websites, but the format of the decisions makes it difficult to quickly identify and retrieve cases addressing specific tax issues. Making changes to search parameters or to the format of court decisions could make the database of judicial decisions a more useful tool for taxpayers as well as for the STI.

One mechanism that could be utilized to reduce the number of cases subject to appeal is expanded issuance of advance rulings by the STI. According to respondents, legislation does not permit the STI to issue binding rulings. However, if requested, in some instances the STI will issue non-binding rulings ("comfort letters"). While the STI may ultimately not follow its ruling, sanctions (fines and penalties) cannot be assessed against a taxpayer who follows a ruling received from the STI. Expanded use and publication of rulings would provide greater certainty to taxpayers, allowing them to undertake, restructure, or forego transactions based on the ruling.

In sum, the lack of a fair and effective means to resolve tax disputes is a significant deficiency in Moldova's tax system, creating uncertainty for taxpayers as well as for the STI. Recommendations concerning the dispute resolution process at the administrative and judicial levels are provided at the end of this chapter.

³⁰Information obtained from dare RM anuala 2011 nat001_EN (1) compiled by the MSTI Appeals Department.

B5. Fines and Penalties Imposed for Tax Violations

Fines and/or penalties provided in Articles 253-263 of the Tax Code are imposed for violations of the Tax Code and accompanying normative acts. While respondents generally focused on two other issues (lack of consistency in the application of tax legislation and the absence of an effective appeals mechanism), many did raise complaints concerning the imposition of fines and penalties for tax violations.³¹ Specifically, they believe that fines and penalties are used by the STI primarily to raise revenues and not as punishment for violations. As a result, fines and penalties are thought to be routinely imposed, often for actions considered to be minor violations.

As with other issues raised in this assessment, many of the issues in this area stem from ambiguities in legislation and/or improper or inconsistent treatment in applying the legislation. Excessive and/or inconsistent fines and penalties provide companies and individuals with an incentive to resort to bribes or conduct their activities in the shadow economy. A review of the appropriateness of fines and penalties and their application should be the subject of continued evaluation, and when warranted, modification. However, reforms in this area are unlikely until fines and penalties are considered a punishment for tax violations rather than as an additional source of government revenues.

C. IMPLEMENTING INSTITUTIONS

Four institutions play a primary role in forming or implementing the tax system in Moldova (see box at right). A description of the role these implementing institutions play in Moldova's tax system is described below. The current level of interaction among implementing institutions, supporting institutions, and the private sector is described in the Social Dynamics section.

Key Implementing Institutions

- Parliament, and its Economy, Budget, and Finance Committee
- Ministry of Finance
- State Tax Inspectorate
- Judicial Courts (Territorial, Appeals, and Supreme)

Parliament. As the legislative body in Moldova, Parliament has the sole authority to enact legislation in Moldova. Tax legislation is drafted and introduced in Parliament by the Economy, Budget, and Finance (EBF) Committee. The EBF Committee admits that it lacks technical expertise in some areas, including formulating and drafting complex tax legislation. Donor organizations should consider providing technical assistance to the EBF Committee, as needed, in these and other areas. Interaction between the EBF Committee and the MOF and other agencies appears to be very limited, as the Chairman of the EBF Committee stated that the Committee must redraft significant portions of proposed tax amendments it receives from the MOF.

Ministry of Finance. The MOF is primarily responsible for tax and fiscal policy in Moldova, which it addresses through its Fiscal Policy and Tax Legislation Division. The STI (described below) and the Customs Service are under the MOF. As with the EBF Committee, the MOF could also benefit from technical assistance from donor organizations when analyzing specific tax issues, drafting proposed legislation, and translating documents into English for its website

³¹ Respondents cited multiple types of fines and penalties that they consider excessive or inappropriately applied.

and other purposes. The MOF maintains a website that provides the public with selected tax information.

State Tax Inspectorate. The STI is the primary State Authority responsible for administering tax laws and normative acts, including assessing and collecting taxes and transferring revenues to the budget.³² It is comprised of the MSTI, which governs the two municipal STIs in Chisinau and Balti, the Autonomous Territorial Unit (UTA) in Gajauzia, and 32 district STIs. For organizational charts of the STI and MSTI please see *Annex 1 of The Development Plan of the Moldovan State Tax Service for 2011-2015* issued by the STI. The STI has implemented a number of meaningful reforms (many with assistance from donor organizations) during the past decade. For example, the STI's FISC.MD website³³ provides useful information to the public (including a monthly newsletter), while e-declaration and rapid declaration filing programs help ease taxpayer compliance burdens. While these and other accomplishments are significant, much more can be done to improve STI communications with the public and in the area of e-filing. (Recommendations in these areas are provided at the end of this chapter.) With assistance from USAID and the IMF, the STI drafted and published *The Development Plan of the Moldovan State Tax Service for 2011-2015*. This plan summarizes initiatives the STI plans to undertake during this period. In general, these initiatives are consistent with the recommendations provided in the report. The current status of the STI initiatives is not known.

As mentioned, a number of respondents stated that Tax Inspectors at the STI fail to apply tax legislation on a correct and consistent basis. A number of respondents believe Tax Inspectors, as well as other STI staff, are not accountable for their actions, which often adversely impact taxpayers. Many respondents called for sanctions to be imposed on STI staff whom are found to have acted illegally or inappropriately.³⁴ The MSTI maintains that it has an Internal Audit Department that investigates possible cases of abuse and sanctions STI staff when warranted. No further information on the number of cases investigated, or the outcome of the investigations, was made available.

Fiscservinform (FSI) is a state enterprise established in 2008 to manage the IT system at the STI. According to an FSI representative, the current STI IT system is both fragmented (consisting of 4 separate platforms and 17 different programs) and outdated. SIDA and the World Bank may provide funding to update the STI's IT system. While the STI is responsible for

Arbitrary STI Practices

During the course of this assessment a tax practitioner in Moldova stated that a representative from the STI informed him that he must resubmit his tax declaration for the 2011 tax year, even if the declaration that he submitted previously is accurate. Based on his declaration the taxpayer is due a refund. However, the taxpayer was not to submit his declaration until January of 2013. By requiring the declaration to be resubmitted the Government avoids having to pay interest (which begins to accrue 45 days after the declaration is filed) on the amount of the refund. There appears to be is no legal basis for this action.

³² For additional information see *Objectives and Basic Function of the Tax Bodies* prepared by the STI and Articles 132-134 and 136 of the Tax Code.

³³ See <http://www.fisc.md>.

³⁴ Article 10 (2) of the Tax Code provides that, "The tax authorities and their authorized officials who fail to perform properly their obligations shall be held accountable under the current legislation."

its IT system, in certain areas the STI and FSI need to coordinate their activities with activities conducted by the E-Governance Center (described below).

Judicial Courts (Territorial, Appeals, Supreme). Taxpayers may appeal tax decisions entered by the MSTI to Territorial Courts and, if desired, to the Court of Appeals and the Supreme Court of Moldova. A description of the role the courts serve in the tax system is provided in B4. Tax Dispute Resolution Mechanism in the previous section.

D. SUPPORTING INSTITUTIONS

Supporting institutions in the public and private sectors play a key role in the functioning of any tax system, and Moldova is no exception. A non-exhaustive list of such institutions is provided in the box at right. A description of the role these supporting institutions play in Moldova's tax system is described below. The current level of interaction among supporting institutions and implementing institutions is described in the Social Dynamics section that follows.

D1. Ministries, State Authorities, and the Court of Accounts

Although the MOF enjoys primary responsibility for matters governing tax policy, the MOE also plays an important role in the tax system. The MOE is responsible for economic and investment policy in Moldova, and has primary responsibility for legislation affecting the business environment and regulatory reforms. The NSI and HIF collect declarations for social fund contributions and health fund contributions, respectively, while the STI collects these two payments.

Customs service. The Customs Service plays a significant role in Moldova's tax system, including collecting import and export duties, as well as collecting VAT on imports.³⁵ An extensive assessment of Customs is provided in the “Trading Across Borders” chapter. An inefficient, non-transparent customs system has an adverse effect on Moldova's tax system. For example, Customs practice of determining the value of imported goods on the basis of inflated reference prices also inflates VAT collections on imports. At the next trade level the inflated Customs value may be more than the eventual market value, meaning the importer has overpaid for VAT with no recourse to STI. Two anecdotal cases provided by respondents are summarized in the text box to the right.

Supporting Institutions
Ministries and State Authorities
MOE
NSI
HIF
Customs
E-Governance Center
Court of Accounts (Audit)
Donor Organizations
USAID
IMF
World Bank
UNDP
SIDA
OECD
Associations
AMCHAM
ACAP
FIA
EBA
CNPM
Accounting and Auditing Firms
PricewaterhouseCoopers
KPMG
Ernst & Young
Grant Thornton
ECOFIN

³⁵ See www.customs.gov.md for a description of Customs' mission and functions.

E-Governance Center. The E-Governance Center was established to provide uniform solutions to IT issues facing the public sector, including the MOF and STI. Recently, the E-Governance Center designed an e-payment system³⁶ that the STI can utilize when it offers an e-payment system to complement its e-declaration system.

Court of Accounts. The Court of Accounts (also designated as the Court of Audit or CA) was established under Article 133 of the Constitution of the Republic of Moldova. The CA assesses whether Ministries and their subordinate State Authorities have utilized budget revenues effectively. It, therefore, reviews expenditures incurred by the MOF and STI. The CA submits annually to Parliament a report on the administration and utilization of public financial resources.

Moldova's SME Sector

More than 95 percent of all enterprises operating in Moldova are classified as SMEs, which number more than 45,000 and employ approximately 60 percent of the workforce. The majority of SMEs operate in the wholesale and retail trade, agriculture, forestry, and processing sectors. More than half of all large enterprises and SMEs are registered in Chisinau.

Donor organizations. Multiple donor organizations (including USAID, the World Bank, IMF, SIDA, UNDP and OECD) provide funding as well as technical assistance to both implementing institutions described in the previous section (Parliament, MOF, STI and judicial courts), as well as to many of the supporting institutions listed in this section. Opportunities for increased coordination of activities conducted by donor organizations are described more fully in the following section on Social Dynamics.

Associations, accounting and auditing firms, and companies in Moldova.

Multiple business associations, accounting and auditing firms, and companies in Moldova, including but not limited to those listed in the Supporting Institutions box on the preceding page, are dedicated to improving Moldova's tax system for the benefit of their clients and, it appears, for the benefit of the country as well.³⁷ They offer experts in the tax field who should be utilized by Parliament, the MOF and the STI to design tax policies and procedures that serve to reduce taxpayer compliance burdens (thereby increasing business activity and investment), increase tax administration efficiency, and increase tax revenues by increasing tax compliance among taxpayers. AmCham, with input from its

Examples of the Effect Customs Actions may have on Tax Collections

Case 1. An importer imports 27 tons of logs by truck, but only 20 tons are declared by the importer and recorded by Customs. The importer sells the extra 7 tons in Moldova without incurring any tax liability, producing no tax revenues for Moldova.

Case 2. An importer of consumer goods imports items with a declared valuation of 300,000 MDL, and has supporting documentation for this amount. Customs does not accept the declared valuation, and increases the valuation to 350,000 MDL. STI requires that VAT collected on the subsequent sale cannot be less than that on the final declared value. If the subsequent resale of the goods is less than the declared value the difference in VAT paid and collected cannot be recouped.

³⁶ The e-payment system is to be tested on a pilot basis in late 2012.

³⁷ While the reviewers for this chapter did not hold meetings with any law firms, those that provide tax services should also be included in the list of supporting institutions. According to respondents, educational institutions currently do not play a significant role in advancing taxation, as few (if any) tax courses are offered at universities and tax textbooks are not readily available.

member accounting firms, auditing firms and companies, is one of the strongest proponents of tax reform in Moldova.

E. SOCIAL DYNAMICS

The current tax environment in Moldova, including positions maintained by the public and private sectors, is not conducive to creating or sustaining a transparent, equitable tax system. Companies and individuals are concerned, with some justification, that the STI will misapply tax laws and procedures to meet revenue targets, creating unwarranted compliance burdens and/or the imposition of fines and penalties the private sector deems excessive. In order to reduce their tax liabilities, taxpayers may resort to attempting to bribe tax officials, conducting activities in the shadow economy, or when possible, conducting activities in another country. The likelihood that illegal actions will be uncovered is low, and even if this occurs they face little fear of being prosecuted under the current system.

The STI is under enormous pressure to meet tax revenue targets. As this is its primary short-term goal, there may be little incentive to create a tax environment that is conducive to long-term business development in Moldova. Moreover, Tax Inspectors may be of the belief, again with some justification, that many taxpayers evade taxes in whole or in part, and therefore believe the imposition of multiple fines and penalties, as well as other punitive measures, are justified.

The result is a state of distrust with respect to taxes (and likely to Customs and other areas) among representatives from the public sector and private sector that results in low taxpayer compliance. While this exists to varying levels in most if not all countries, the situation in Moldova is acute and has a significant impact on short- and long-term economic growth prospects. It also creates a significant "tax gap" (the difference between taxes owed and taxes paid).³⁸

In order to create a more effective tax system, including but not limited to increasing voluntary taxpayer compliance, all stakeholders need to be engaged in the process that governs them. The remainder of this section addresses the level of interaction, or dialogue, between and among implementing and supporting institutions described in the previous two sections of the Paying Taxes chapter. A review and assessment of current social dynamics is provided, followed by recommendations on how to strengthen social dynamics to create a more efficient, effective and business-friendly tax system while generating sufficient tax revenues. The assessment of social dynamics is divided into the following four parts:

- Social dynamics between Parliament, government, state authorities and the private sector concerning proposed tax legislation
- Social dynamics between the STI and taxpayers
- Social dynamics within the public sector

³⁸ The IMF has outlined a development strategy for the STI to reduce the tax gap that focuses on increasing compliance in specific industry sectors. For additional information on this strategy see *Taking Compliance Management Further*, issued by the IMF's Fiscal Affairs department in April 2012, p. 12.

- Social dynamics among donor organizations

*Social dynamics between the public sector and private sector concerning proposed tax legislation.*³⁹ Currently, there is no effective, transparent mechanism for the private sector to interact with Parliament, Government, and State Authorities (referred to as the "public sector" in this chapter of the report) on the design and drafting of proposed tax legislation. According to some respondents, one or more procedures exist that provide for a working group or committee, consisting of public sector representatives and a limited number of private sector representatives, to participate in the discussion of tax issues and formulation of tax legislation. However, according to respondents, these procedures are neither very effective nor applied on a consistent basis. Rather, with respect to proposed tax legislation, interaction between the public and private sectors occurs primarily on an *ad hoc* or informal basis. Some of the more active associations and major accounting firms reported that on some occasions they are able to provide input to the public sector (primarily to the Parliament EBF Committee or to the MOF), although the extent that such input is considered is not always known. One association reported that, despite its best efforts, it currently has little or no significant interaction with the public sector concerning proposed tax legislation. Individual companies, primarily larger companies in Moldova, also report to having some degree of interaction with the public sector with respect to proposed tax legislation. However, smaller companies and individuals appear to have little or no ability to engage in meaningful dialogue with the public sector to discuss proposed tax legislation. Draft tax laws are placed on various public sector websites, but only after the first reading of the laws. At this stage of the legislative process the ability to change the proposed laws is more problematic than it is during the preceding design and drafting stages.

This general absence of meaningful interaction between the public and private sectors in the legislative process may result in inappropriate, or at least sub-optimal, tax policies and procedures. Furthermore, if the private sector believes their comments on the formulation of tax policies and procedures are ignored this likely will have adverse impact on taxpayer compliance and resulting tax revenues. According to some respondents, the process used to design and approve normative acts (e.g., regulations) is even less transparent and closed than the legislative process.

Compared to associations and businesses, donor organizations enjoy much greater access to the public sector with respect to the formulation of tax policies and procedures. Past USAID projects (BIZPRO followed by BIZTAR) interacted with Government representatives on a number of reform initiatives during the period covering 2001-2011. The recently-initiated USAID BRITE Project also has had access to some representatives from the public sector to discuss possible activities to be included in BRITE's work plan to improve the business environment in Moldova with respect to taxes and other areas. The IMF, World Bank and SIDA, as well as other international organizations, also are provided opportunities to interact with the public sector in the design of strategic plans and in the formulation of tax policies and administrative procedures. (An assessment of the interaction among these organizations is provided below.)

³⁹ For a review of interaction between Parliament and other agencies refer to Independent and Regulatory Agencies in Moldova and their Interaction with Parliament, published in 2011 with the support of DANIDA, SIDA and UNDP.

Social dynamics within the public sector. While consistent meaningful interaction between the public and private sectors is lacking, so, too, is effective interaction within the public sector. There appears to be insufficient interaction between the EBF Committee and the MOF, as the Committee often must redraft significant portions of proposed amendments it receives from the MOF. According to respondents, there is limited interaction between the MOF and MOE, which may be attributable, in part, to the fact that the Ministers of the MOF and MOE represent different political parties. Some respondents from the private sector commented that interaction between the EBF Committee and the STI, as well as communication between the MOF and STI, is also lacking, which may result in the passage of tax legislation that presents challenges for the STI to administer effectively. Finally, some respondents also mentioned the lack of sufficient interaction between the MSTI and STI District Offices.

Social dynamics between the STI and taxpayers. Mass communication from the STI to taxpayers has improved considerably through the expanded use of the FISC.MD website and the publication of a monthly newsletter and other informational materials. In the OIKOS⁴⁰ survey, 39.7 percent of respondents indicated that the MSTI website is an important source of tax information. The website provides information in Romanian and Russian, with limited information available in English. Many respondents stated that they are able to contact staff at the MSTI and District Offices, but this appears to be mainly through personal connections they have established. In the same OIKOS survey, only 6.7 percent of respondents indicated that the MSTI Call Center is an important source of information. Many respondents also expressed negative views of the Call Center. Taxpayers can submit written requests to the STI, but respondents claim that they often do not receive replies, and even when they do the replies often do not address the questions asked.

Is Anyone Listening?

"Businesses need to know that their views are considered by Parliament and Government."

—Moldovan business owner

Social Dynamics among donor organizations. Although not routinely considered, an assessment of the interaction among the various bilateral and multilateral donor organizations is also an important factor. In Moldova, it appears that the multiple donor organizations interact on an "as needed" basis, either through bilateral meetings or conferences. During this BizCLIR assessment representatives from donor organizations were willing to meet to discuss their projects and also provided copies of their reports. It does not appear that all organizations have formally established the reform areas they intend to address and the time period for doing so. Increased coordination in this area may yield efficiencies in reforming Moldova's tax system while reducing the possibility of duplicate or inconsistent reform initiatives. Moreover, when possible, incorporation of selected conditionalities into agreements between donor organizations and the public sector may provide the leverage needed to prompt reforms sought by all donor organizations.

Ready to Work Together

"We [taxpayers] want to be treated as partners [by the STI]."

—Moldovan SME owner

⁴⁰*Study of Level of Satisfaction of Taxpayers with the Activities of Line Authorities in the Tax Administration Process, Final Results of Quantitative Study (survey)*, conducted by the National Association for Rural Development (OIKOS), published 8 September 2011.

F. RECOMMENDATIONS

Based on the assessment conducted, the following recommendations are offered.⁴¹

- *Create a formalized process that allows the private sector to interact with Parliament, MOF, and the STI in the design of tax policies and procedures and ultimate implementation.* Increased interaction between the public and private sectors is a critical component to achieving meaningful reforms to Moldova's tax system. A formal process will improve the frequency of open interaction among various stakeholders in Moldova's tax environment. One mechanism is a permanent committee comprised of representatives from Parliament, the MOF, STI, other public sector stakeholders (as appropriate), donor organizations, and the private sector (either through associations or companies). Subcommittees may be formed to address specific tax areas (e.g., tax administration or VAT).⁴² The process should include discussion, design, performance of RIAs, drafting, implementation, and subsequent evaluation of the reforms implemented. All proposed legislation and normative acts should be subject to a sufficient review and comment period, while the effective date of adopted legislation and acts should provide sufficient time for the STI and taxpayers to take actions required to implement and comply with the changes imposed. Internal orders, while not subject to the same review and comment procedure applied to proposed legislation and normative acts, should also be issued in a transparent manner and be consistent with existing legislation and normative acts.
- *Using the process described in the previous recommendation, identify and prioritize problematic tax issues and, through the committee established, make appropriate amendments to the Tax Code or to normative acts.* Respondents from both the public and private sectors identified a number of issues (examples provided previously) that need to be clarified to determine if the legislation or act clearly conveys the intent of the provision or, in other cases, needs to be reviewed in order to determine if the policies and procedures are appropriate. The committee should prioritize issues based on the need for reform, scope of taxpayers affected, extent of reforms required, effect on taxpayer compliance, tax administration efficiency and revenues, and likelihood that the issues can be resolved in the short-term. Initially, the issues addressed should focus on clarifying existing policies and practices rather than on proposing new policies. The objective is to amend legislation or normative acts that will yield a more predictable, consistent and correct application of legislation and normative acts. While some respondents proposed sweeping changes to tax legislation, incremental changes are preferred at the outset in order to provide a relatively stable tax system for the benefit of the public and private sectors.

⁴¹A number of possible areas of assistance to be provided to the STI or other stakeholders were considered during this assessment. Some possible areas (e.g., audit, including indirect audit methods, STI IT, and collections) were excluded from the recommendations in full or in part because other donor organizations (e.g., IMF or SIDA) are or plan to provide technical assistance in these areas. Other possible areas of assistance were excluded due to the level of time and resources that would be required to achieve reforms or because they were deemed to be of lower priority.

⁴² The IMF has proposed that a tax compliance council be created, which would be composed of representatives of the STI at senior level, industrial groups, chambers of commerce and tax professionals.

- *Create a more efficient, fairer and effective tax dispute resolution mechanism.* The STI and taxpayers both are highly critical of the current tax appeals process. A number of reforms should be implemented to create a more efficient and effective tax appeals process, including:
 - Create a more independent review procedure at the administrative appeals level;
 - Allow greater public access to tax decisions issued at the administrative and judicial levels;
 - Providing expedited dispute resolution procedures for tax disputes below a defined threshold;
 - Expand the use of advance tax rulings;⁴³
 - Train STI staff attorneys and judges (possibly through joint training sessions) in tax issues; and
 - Consider and, if appropriate, implement one or more alternative dispute resolution methods.
- *Adopt and expand e-governance initiatives at the STI.* The STI has adopted some e-governance initiatives, including e-filing of declarations. However, despite the advantages to taxpayers and the STI, e-filing is not widely used. An e-payment system has been designed by the E-Governance Center, which can be implemented at the STI. E-filing of invoices can also be initiated in the near future. The STI, possibly with donor assistance, should undertake to expand its current e-governance initiatives and, when possible, adopt new initiatives that will benefit taxpayers as well as the STI.
- *Identify tax processes that increase taxpayer compliance burdens and/or reduce tax administration efficiency, and take remedial actions.* In conjunction with the previous recommendation, the STI, with input from other public sector stakeholders and the private sector, should examine means to reduce compliance burdens on taxpayers, including but not limited to burdens associated with making payments and filing declarations. One possibility mentioned in this report is to combine monthly payments (and possibly accompanying filings) for social and health fund contributions. When possible, many of the filings and/or payments can be submitted electronically, further reducing taxpayer compliance burdens and increasing tax administration efficiency.
- *Review existing fines and penalties to determine which are duplicative, ineffective or excessive and, based on the results of the review, take appropriate actions, which may include eliminating or modifying selected fines and penalties.* The imposition of excessive and/or inconsistently applied fines and penalties creates a significant compliance burden for taxpayers and has an adverse effect on the business environment, on tax administration efficiency and, in the long-term, on tax revenues. Rather than

⁴³ If possible, the issuance of binding, rather than current non-binding, advance tax rulings should be implemented.

impose fines and penalties to generate revenues, the STI should provide assistance to taxpayers in the form of educational materials, seminars, and other mediums to inform taxpayers of their obligations under the Tax Code to reduce the number of violations committed and to raise tax compliance.

- *Provide targeted training coupled with practical application of knowledge to STI staff.* STI staff could benefit from training in general areas (e.g., collections practices) and specialized areas (e.g., transfer pricing). Joint training with (or conducted by) tax practitioners would provide an excellent medium to increase dialogue between the public and private sectors. Donor organizations could coordinate and provide funding for the training and, when appropriate, bring in experts to provide training. As part of the training, participants should be required to demonstrate that they can apply the knowledge they acquired to active tax cases.
- *Expand communication and public outreach efforts at the STI.* All of the recommendations included in this chapter contain a communications or public outreach component that is critical to the success of the proposed reform. Improving and expanding the STI's website (including the English version), publicizing and soliciting input on proposed laws and acts (using the MOF, STI and possibly other websites), and creating an improved, publicly-accessible, tax appeals database are among the communication and outreach initiatives that can be undertaken. Donor organizations should assist the STI and other stakeholders in notifying the public of the reform efforts, soliciting input, and promoting the benefits realized when a reform is accomplished. If the STI plans to maintain a Call Center it should, based on the negative rating provided by the respondents, provide greater resources and training to improve the effectiveness of the Call Center.
- *Evaluate the revenue impact of current tax preferences (including FEZs) and, based on the results, propose legislation to maintain or phase-out the preferences.* Tax legislation includes a number of incentives (or preferences) for certain activities or industry sectors, or for activities conducted in certain areas (e.g., FEZs). Analyses should be performed to determine the revenue impact of such incentives. Incentives that fail a cost-benefit analysis should be restructured, phased-out, or eliminated. Economists provided by donor organizations could assist the public sector in performing the analyses.
- *Establish a donor working group to coordinate all tax-related activities conducted by donor organizations and leverage resources to achieve meaningful reforms.* Increased coordination among donor organizations may yield efficiencies in reforming Moldova's tax system (including monitoring and evaluating reform efforts), while reducing duplicate or inconsistent reform initiatives. Moreover, when possible, incorporation of selected conditionalities into agreements between donor organizations and the public sector may provide the leverage needed to achieve reforms sought by all donor organizations.

SECTION III. DEALING WITH CONSTRUCTION PERMITS

A. INTRODUCTION

Appropriate regulation of the construction sector is critical for rapid economic growth, particularly in developing countries that seek to attract investment. A well-regulated sector is essential for modernizing infrastructure, renewing housing stocks, and creating new business workplaces. Regulators must achieve a precarious balance between enforcing standards that protect the public from the hazards of shoddy construction, while administering regulations efficiently. Inefficient regulation that makes compliance costly and burdensome produces a variety of negative results. Illegal construction proliferates. Projects that would otherwise make business sense don't get built because compliance costs make them unprofitable. Finally, sector participants find informal mechanisms to reduce compliance costs, including giving and receiving bribes. The net effect is that overregulation can become the functional equivalent of no regulation.

A well-regulated construction sector can become a powerful engine of growth that contributes to economic transformation. Georgia's experience, discussed below, is that as its regulation of construction became more efficient, the volume of construction and sector employment and wages all grew dramatically. Moreover, growth of the construction sector also helped deepen and strengthen the financial sector. As lenders gained trust in an improving regulatory regime that reduced the risks and delays associated with inefficient regulation, builders had increased access to capital. Mortgage lending to consumers for purchases of new homes and apartment units suddenly blossomed, providing a spur to even more growth of the construction sector.

Although Moldova has a long way to go to achieve an efficient regulatory regime, it has made a promising start. Building on the existing foundation, Moldova can make important strides forward that do not need to take a long time, to begin receiving now the many important benefits that a well-regulated society can provide in spurring economic growth and jobs creation.

A1. "Dealing with Construction Permits" Indicator

Table III-1. Moldova's Performance on Dealing with Construction Permits

Indicator	DB 2013		Law 163 As Now Enforced		Law 163 If Fully Enforced	
	Score	Rank	Score	Rank	Score	Rank
Procedures (number)	26	170	24	106	21	152
Time (days)	291	161	282	158	205	130
Cost (% of income per capita)	69.3	76	38.3	49	23.6	33
Overall Rank	168		144		118	
Ease of Doing Business	83		80		74	

The Doing Business "Dealing with Construction Permits" indicator evaluates the regulatory process required, from beginning to end, to build and occupy a standard warehouse. The indicator measures three elements – the number of procedures required, the total time in days to complete them, and the cost of associated official fees as a percentage of Moldova's per capita

income. The World Bank scores each element, ranks Moldova as compared with other countries, and then averages its ranking on the three elements to produce Moldova's overall "Dealing with Construction Permits" ranking. The table above shows how Moldova compares to the 185 different economies surveyed under three scenarios:

- As reported on the Doing Business 2013 report;
- As stakeholders report Moldova actually performs as the result of partial enforcement of Moldova's new Law 163 on Authorizations of Construction Works; and,
- Moldova's estimated performance if all state agencies respected the terms of the law and did not actively thwart its full implementation.

Moldova ranked 168th overall on "Dealing with Construction Permits" in the DB 2013 report. On the individual elements, it ranked 170th for 26 procedures, 161st for the 291 days it takes to complete them, and a relatively good ranking of 76th of 185 countries in the cost of official fees – 69.3 percent of per capita income. Stakeholders report that the new Law 163 is having a measurable positive impact in reducing compliance burdens involved in the zoning and construction permit process, despite the fact that the law's provisions are being undermined by agencies anxious not to lose their revenue streams, as discussed hereafter.

Despite these problems, the law has reduced the number of procedures involved in the zoning and construction permitting stage, bringing the total down from 26 to 24. Stakeholders also report that the time involved in the pre-construction phase has also been reduced, though this seems to vary considerably depending upon location and type of construction. Based on stakeholder feedback, the assessment team estimates that the number of days required for permits associated with the standard warehouse assumed in the methodology's indicator has been reduced from 291 days to 282. The biggest improvement, however, is to the cost element. Law 163 reduces official fees in several ways. Value-based construction permit fees that ranged from 1,000 MDL to 20,000 MDL have been replaced by a simple, inexpensive 100 MDL charge. Eliminating the state monopoly on verification has reduced the time and delay associated with this procedure. Charges associated with other procedures disappeared when they were eliminated. These changes, stakeholders say, reduce costs from 69.3 percent of annual income per capita to 38.3 percent. The net effect of the current partial enforcement of Law 163 would improve Moldova's "Dealing with Construction Permits" ranking from 168th to 144th.⁴⁴ This improvement would lift Moldova's overall "Ease of Doing Business" ranking from 83rd to 80th.

Full enforcement of Law 163 would improve Moldova's ranking even more significantly: the number of procedures would drop to 21, time would be reduced to 205 days, and costs would fall to just 23.6 percent of per capita income. The net effect of full enforcement would be to improve Moldova's ranking to 118th, and its overall "Ease of Doing Business" ranking from 83rd to 74th.

⁴⁴ Estimates of the impact of reforms on Moldova's rankings are based on the *Doing Business* 2013 Reform Simulator, which assumes no countries ahead of Moldova simultaneously also reform. The simulator is available online at <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Simulators/DoingBusiness/DB13-Simulator.xls>.

Because Law 163 is focused only on streamlining the pre-construction phase, Moldova can achieve even more significant improvements by reforming the permitting phases that deal with construction and reception of the building, as discussed hereafter.

B. LEGAL FRAMEWORK

The legal framework governing construction in Moldova is a complex set of laws and regulations dating back almost two decades, with a very modern overlay. The texts of applicable laws and regulations, listed below, are freely available in Romanian and Russian, but many haven't been

List of Key Laws

- Law 163 on Authorizations of Construction Works, July 9, 2010
- Law 835 on Principles of Urbanistics and Territorial Development, May 17, 1996
- Law 1350 on Architectural Activity, November 2, 2000
- Law 721 on Quality in Constructions, Feb. 2, 1996
- Law 451 on Regulating Entrepreneurial Activity through Licensing, July 30, 2001
- Law 235 on Basic Principles Regulating Entrepreneurial Activity, July 20, 2006
- Law 1543-XIII on Cadastre of Real Estate, Feb. 25, 1998
- Law 393 on Approving the Methodology for Calculating the Tariffs and Services provided by State Cadastre and its Branches, Dec 8, 2006
- Law 1247-XII on State Land Structure, State Land Cadastre, and Land Monitoring, Dec. 22, 1992
- Law 778-XV on Geodesy, Cartography and Geoinformatics, Dec.27, 2001

List of Key Regulations

- Gov't. Decision 499 Approving the Framework Regulation on Local Authorities in Architecture and Urbanism, May 30, 2000
- Gov't. Decision 329 Approving the Regulation on Technical Competency Assessment of Specialists in Construction Field, April 23, 2009
- Gov't. Decision 5 Approving the General Urbanism Regulation, Jan. 5, 1998
- Gov't. Decision 951 on Approving the Regulation on Public Consultations Regarding the Draft and Approval of Land Arrangements and Urbanistic Documents, Oct. 14, 1997
- Gov't. Decision 361 on Ensuring the Quality in Constructions, June 25, 1996
- Gov't. Decision 285 Approving the Regulation on the Reception of Buildings and Related Facilities, May 23, 1996
- Gov't. Decision 360 on State Control of Construction Quality (Regulation of the State Inspection in Constructions), June 25, 1996
- Gov't. Decision 936 Approving the Regulation on Technical Expertise in Constructions, Aug. 16, 2006
- Gov't. Decision 306 Approving the Regulation on Authorization of Running and Changing the Use of Buildings and Lands, March 30, 2000
- Gov't. Decision 461 on Approving the Regulation on Technical Approval of Construction Products, Procedures and New Equipment, July 6, 1995
- Gov't. Decision 382, Observation on Buildings Behavior in Service, Intervention During and in Post-Usage Period, April 24, 1997
- Gov't. Decision 900 on Competency Assessment of Real Estate Appraisers, July 24, 2003
- Gov't Decision 524, Cadastral Engineers' Certification, May 16, 2006
- Gov't. Decision 770 Approving Tariffs for Services Provided by State-Owned Company "Cadaster" and its Branches, July 2, 2007

translated into English, the international language of business and investment.⁴⁵

An especially serious problem is the lack of modern technical standards. While a handful of Moldovan standards have been adopted, most are Soviet-era “SNIPS,”⁴⁶ which stakeholders say were often more suitable for Moscow than Moldova, even when new. Intervening decades have rendered many obsolete. Because they do not take into account technological advances in building materials and construction processes that improve quality, the SNIPS sometimes require expensive overkill that raises costs and distorts land use and building construction. Stakeholders report that in some cases, such constraints can be overcome with due consideration paid for consultations with appropriate agencies to produce waivers. The standards are not now available online, but paper copies can be purchased individually.

Several important initiatives are underway to address these problems. The Ministry of Regional Development and Construction (MRDC) is working with stakeholders to consolidate and rationalize all construction-related law into a single, comprehensive Construction Code. The current draft is available online for review and comment.⁴⁷ MRDC and Moldova’s E-Governance Center are collaborating to collect and publish all current technical standards, including both the Soviet-era SNIPS and the more recent Moldova standards online. One stakeholder estimated there are approximately 3,000 different construction-related technical standards. MRDC is also working on a long-range plan to adapt the EU-based Eurocodes technical standards for use in Moldova. Unfortunately, the process contemplates years for adapting the Eurocodes, training up specialists, Private-sector stakeholders would prefer a much more accelerated process, pointing to the example of Belarus, which reportedly made the transition in a year.

The modern overlay to Moldova’s legal framework is Law 163 on Authorizations of Construction Works. Adopted in July 2010, stakeholders call Law 163 “revolutionary” because of the streamlined procedures and re-engineered conceptual framework it introduces for zoning and construction permit approval. Unfortunately, Law 163 leaves off when construction begins. Approval powers retained by various state agencies at the end of the process, when a new building is accepted for use, allows them to thwart the reforms introduced at the beginning of the process, during zoning and construction permit approval. The discussion that follows will examine issues identified by stakeholders in all three stages – zoning and construction permit approval, the construction itself, and the post-construction “reception” process, when the builder gets the approvals necessary to put the project into use.

Zoning and construction permit approval. The procedural innovations introduced by Law 163 to reduce the time and expense required for zoning and construction permit approval are discussed in the pages that follow.

⁴⁵ An online database of Moldovan laws and regulations in Romanian and Russian is available at <http://lex.justice.md>. Some English translations are available at <http://www.lexadin.nl/wlg/legis/nofr/oeur/lxwemol.htm>.

⁴⁶“SNIP” is the acronym for *Stroitelinye Normy I Pravila*, which in Russian means “constructions norms and rules.” Most of the SNIPs are in Russian only.

⁴⁷The draft is available online at http://www.mrdc.gov.md/public/files/oldsite/files/7814_Codul_Urbanismului_si_Constructiilor.pdf.

A state monopoly was broken on review and approval – “verification” – of architectural drawings prior to submission for a construction permit. Before Law 163, builders were required to obtain, for a fee, approval from the State Service for Verification and Expertise of Projects and Construction, a state-owned enterprise subject to the MRDC. Law 163 has opened the way for independent, certified verifiers to compete with the prior state monopoly. Stakeholders say that competition has served to reduce the prices and time for verifications.

Law 163 gives local authorities sole responsibility for approving zoning and construction permits when appropriate development master plans are in place. Unfortunately, almost 15 years have elapsed since Moldova’s Parliament mandated that all municipalities adopt master plans, and very few have. Some stakeholders complained that while Chisinau Municipality does have detailed master plans for some areas, the municipality has yet to approve them. In addition, although the plans were once available online, they are not currently, which complicates matters for those planning new projects. Implementation of master plans across Moldova would reduce the time and expense now required for consultation with state enterprises owned by MRDC -- "UrbanProject," "IndustrialProject," and "RuralProject." One stakeholder who contributed to the preliminary findings in this chapter suggested that the time and cost of producing master plans could be reduced dramatically if utilities were required to disseminate maps of their nationwide infrastructure, including water, sewer, heating, gas, electric, telephone, and so forth.

Municipal OSSs are created for permit processing with the strict deadlines of 20 days for zoning permits and 10 days for construction permits. While stakeholders report that the law has helped reduce time overall, they note a number of problems that keep it from fully delivering the efficiency improvements envisioned by drafters and Parliament:

- The law’s “silence is consent” provision deems a permit granted if the municipality fails to act within the required time frame. This provision does not work in practice, for two reasons. First, when deadlines near, municipal officials ask for more documents, which restarts the clock. Second, builders face retaliatory measures at the “reception” phase, when approval is needed by various government agencies for the building to become operational. As discussed hereafter, the provisions of Law 163 that eliminate approval rights of these agencies during the initial permit process should be expanded to eliminate them from interfering in the construction and reception phases.
- Municipalities adopt various approaches to engaging neighbors in the zoning permit approval process. Applicable law now requires the consent of apartment owners to install “mansards” – new rooftop living quarters – in an existing building. However, builders say municipalities sometimes force them to get the consent of neighboring landowners for stand-alone projects, which is not a legal requirement. The State Construction Inspectorate reports that complaints by neighbors have increased since Law 163 went into force, and that greater accountability is needed for municipal authorities who issue permits when they should not. Measures to help mitigate these concerns include:
 - In the current depressed environment, mansards are a bright spot. In addition to providing new housing, jobs, and sector profits, they also can result in upgrades in the building and grounds that benefit all residents. If Moldova determines that mansard construction is a socially beneficial sector that ought to be encouraged, then special

regulatory provisions should be adopted that provide clear rules for those concerned. A provision could be adopted for determining what percent of building residents must approve mansard construction, and a pricing scheme that gives those owners most affected – for example, those on the floor beneath the construction – a larger payout. The ability of the last hold-outs to extract extra payments depresses construction activity and the benefits it brings to all.

- In the case of stand-alone projects, clear regulations and procedures for neighbors to be informed and express their concerns should be established. Builders who propose lawful projects that conform to applicable zoning requirements should not be blocked by neighbors. Neighbors, however, should have an opportunity to understand what is proposed and object to zoning violations. Moldova could require a simple hearing at which the builder presents its plans, and the municipal authorities invite objections based on zoning law. In the absence of legally valid objections, the permit should be granted.
- For a variety of reasons, including the intervention of neighbors, builders say they are often pressed to present their detailed architectural drawings at the zoning phase. This is an unnecessarily burdensome requirement. Preliminary drawings of how the building will look from the outside, and projected burdens like occupancy, etc., should be all that is required. Only if zoning approval for the project is granted should builders have to bear the considerable expense of developing detailed architectural drawings.

Law 163 eliminates from the permit issuance phase the approval authority of several agencies, including fire, sanitation, and ecological services. Their participation was to confirm that the drawings comply with applicable technical standards, which already happens in the verification stage. There is even less need to have these agencies present at the “reception” phase, when their role is only to confirm that the building was constructed in accordance with the drawings. However, municipal authorities, the agencies themselves, and builders all confirm that in practice, builders generally schedule visits with these agencies to get their approval to the drawings as part of the construction permitting process. Stakeholders all agree this helps avoid retaliation by the agencies at the reception stage for having been ignored at the permitting stage. Retaliation can take several forms, including refusing to approve, imposing additional features not required by the applicable standards, and so forth. Barring these agencies from contact with architects, engineers, and builders would empower the verifiers and the Inspectorate to carry out their proper roles.

The Ministry of Culture has inserted two new procedural obstacles that will, when recognized by the World Bank, worsen Moldova’s ranking on “Dealing with Construction Permits.” The problems they create are especially difficult in Chisinau Municipality, officials there say, because special permitting is required. Getting a permit from the Ministry can take years, stakeholders say, because the special commissions formed to rule on applications are reluctant to meet without getting paid. Builders are also required to have an archaeological expert on the scene when breaking ground. The one remaining wall of what was once Chisinau’s oldest building stands next to a new, modern hotel as a monument to the need for cultural preservation. However, requiring builders to wait on the Government for prolonged periods undermines the

industry and Moldova's economy. The logic of Law 163 could be expanded to cover the Ministry of Culture. If the Ministry cannot act within the 20-day deadline for construction permits, it should be deemed to have granted approval. If the Ministry's archaeological experts wish to attend ground-breaking, they may attend on the date builders are legally required to publicly announce for commencement of construction.

The role of the State Construction Inspectorate is also curtailed during the construction permit stage by Law 163. As was the case with other agencies, the Inspectorate's role in approving project drawings as part of the construction permit stage has been eliminated. Law 163 did not eliminate the requirement that the Inspectorate register the permit before it is issued to the builder. The Inspectorate is supposed to complete the registration process within three days. Builders and municipal authorities say the inspectorate is rarely timely, and they cited examples of prolonged delays of many months to complete the registration. The inspectorate concedes some past delays, but says that it changed its procedures in July 2012 and now consistently meets its three-day deadline. However, changing its procedures to comply with Law 163 creates several issues for the Inspectorate:

- Earlier laws and regulations make the Inspectorate responsible for assuring that zoning and construction permits are validly issued. Inspectorate officials note that their potential liability for failing to prevent unauthorized issuance of permits is considerably heavier than the minimal fines facing municipal officials who act unlawfully. As complaints by neighbors have grown in response to the accelerated zoning permit issuance procedures, the only point at which the Inspectorate can investigate before construction begins is during its construction permit registration process. Meeting the three-day deadline makes it more difficult for the Inspectorate to meet its separate statutory obligations to ensure zoning permits are issued appropriately. Stiffer penalties for unlawful acts by municipal authorities and more and earlier opportunities for neighbors to understand and be heard, as suggested above, would address this issue.
- Registration with the Inspectorate as a prior condition for permit issuance is unnecessary, and causes builders to wait for the Inspectorate to perform a simple administrative act. A simple notice from the municipality to the Inspectorate is all that should be required.
- The Inspectorate maintains an online database of registered construction projects. Municipalities are developing their own separate systems. All stakeholders involved should work with MRDC and the E-Governance Center to develop a single online registry that all share collaboratively. Creation of such a unified registry would reap multiple benefits. For example, when the municipality logged the issuance of a construction permit, the entry would automatically be registered for the benefit of the Inspectorate. Moreover, an open, transparent log would make it clear who was responsible for any delays, and ensure greater ownership over the process and meeting the deadline by eliminating confusion over bottlenecks. Finally, such a log would provide builders with clear evidence of when deadlines have passed and their permits have been deemed issued.

Regulatory oversight of the construction phase. Moldova's procedures for regulating the construction process are stunningly inefficient. Once a construction permit is issued, the builder

must formally announce and notify the Inspectorate of the date upon which construction will begin. Before construction can begin, the builder must have an official book approved by the State Inspectorate that describes the technical sequencing of the construction. The most important role for the book appears to be to collect the extraordinarily high number of signatures and approvals required during construction, including:

- Laboratory tests of each batch of concrete delivered to the site, after it has been poured and has hardened. For large projects, this could require hundreds of tests.
- The responsible structural engineer is required to inspect and approve four times for every floor – for outer walls, interior walls, ceiling, and final floor sign-off. One project with five buildings of ten floors each would require 200 signatures just from a structural engineer.
- The owner’s mandatory clerk of the works and the builder’s site manager and licensed tradesmen responsible for various aspects of construction – electrical, plumbing, windows, and so forth – are all required to sign at frequent intervals.
- Approvals are required by the Inspectorate for every floor.
- To avoid retaliation at the reception phase, builders must also get the approvals of the same agencies that Law 163 attempted to eliminate from the permit issuance process.

Requiring such an extraordinarily high number of signatures helps to enforce a curious system of criminal accountability for mistakes in construction that puts the signatories at great risk, but provides little benefit for those who may suffer the consequences of such mistakes. The system also provides numerous opportunities for lowly paid civil servants to seek unofficial payments. These issues are discussed more fully in the Social Dynamics section of this chapter.

Reception phase. The unreformed reception phase makes the builder critically vulnerable to the demands of government agencies that Law 163 eliminated from the construction permit issuance phase. The current regulatory framework requires their approval at the reception phase. Stakeholders and the agencies themselves agree that reception works much better for builders who have engaged fire, sanitation, and ecology agencies in their project from its inception, including paying fees for services rendered, whether necessary or not, and whether official or not.

Another source of expense and delay for builders comes after reception when the building is registered with “Cadastre,” the state-owned property registration company under the Agency for Land Relations and Cadastre. However, Cadastre will not register the property after reception until it again confirms that the architectural drawings for a building accurately reflect the actual as-built dimensions. Builders report that this requirement can introduce months of delay before a project is finally registered.

Municipal authorities also complain about the large number of illegal construction projects that they say result from a legal framework that doesn’t give any enforcement body a clear mandate to ensure compliance with construction norms. A complicating factor, they say, is that the

regulatory regime fails to adopt a risk-based approach that has simpler procedures for simpler projects that present less risk than others. Illegal construction is of concern to local officials because they can't tax the property until it is properly registered. One mechanism to discourage illegal construction is to empower municipal authorities to tax such projects at punitive rates until they are properly registered.

The logic and efficiency of Moldova's "revolutionary" Law 163 should be extended from construction permitting to cover the whole construction regulatory regime. The need is urgent, because Moldova's construction sector is struggling. The effort to enact a comprehensive Construction Code is worthy, but that effort should not delay reforms to eliminate the bureaucracy that depresses the sector now.

C. IMPLEMENTING INSTITUTIONS

As described above, the legal framework sometimes hampers the institutions responsible for implementing Moldova's construction regulation regime. In other cases, however, different choices could reduce compliance costs and delays, and help improve the health of the construction sector. This section provides a brief overview of key implementing agencies.

Moldova's Ministry of Regional Development and Construction. This Ministry is responsible for developing, promoting, and implementing government policy in a variety of areas affecting the construction sector, including the regulatory regime, urban planning, technical standards, construction procedures and materials, and housing and regional development. Also under its jurisdiction are the State Construction Inspectorate and several state-owned enterprises that provide specialized fee-based services related to construction.

Ministry officials interviewed are technically well-versed and passionate about the role that a well-regulated sector can play in Moldova's economic development. The Ministry, which was responsible for Law 163, is promoting a number of initiatives that can dramatically improve the construction sector, including:

- A draft Construction Code will rationalize the regulatory regime and replace the many separate pieces of legislation that now govern the sector. Stakeholders worry that this effort will distract and delay the specific reforms necessary to rapidly extend the Law 163 framework to the whole construction process.
- All technical standards are in the process of being published online, which will provide practitioners easy access to the estimated 3,000 Soviet-era SNIPS and a handful of specific Moldovan standards that are sometimes difficult and expensive to acquire.
- The Ministry is preparing for the adaptation and implementation of the EU-based Eurocodes technical standards. As envisioned, this will take years at best, leaving the sector subject to obsolete standards that drive up costs and reduce quality. Support is required for a more aggressive approach.
- One area in which more aggressive leadership by the Ministry would be productive is in working with local authorities to generate master plans for their communities. This would

require the Ministry to work adversely to its own interests because its state enterprises (UrbanProject, RuralProject, and IndustrialProject) provide fee-based services in connection with issuance of zoning permits in areas where master plans are not in place. Some stakeholders observe that the Ministry was not entirely supportive of Law 163, which served to break the monopoly on verification of project designs previously held by another of its enterprises, the State Service for Verification and Expertise of Projects and Construction.

- Stakeholders also complain that the Ministry has not aggressively pursued revision of secondary regulations to eliminate conflicts between older legislation and Law 163.

State Construction Inspectorate. Under MRDC, the State Construction Inspectorate is responsible for assuring compliance by other stakeholders, including local authorities, builders, and the construction professionals who serve them, at all stages of the construction process, including after projects are put into use. The primary complaint against the Inspectorate, by builders and local authorities, is that it routinely takes considerably longer than the three days allotted it to register construction permits. The Inspectorate's response, as discussed earlier, is that the registration window provides its best opportunity to carry out its obligations to ensure that local authorities comply with zoning requirements and to follow-up on citizens' complaints that they haven't. Builders report that engagement with employees of the Inspectorate during construction is the least of their worries, and that they are generally reasonable in helping to avoid undue delay. Some stakeholders suggest that more effort should be made to help improve the technical skills of Inspectorate personnel.

As part of the overhaul of the Construction Code and expansion of Law 163 to the entire construction process, consideration should be given to offering more authority to the Inspectorate in several areas:

- Clarifying the Inspectorate's role in assuring compliance by other government authorities and increasing the consequences for such non-compliance;
- Giving the Inspectorate sole responsibility for assuring compliance by the builder with the construction permit and project design in all areas, during both construction and reception. Involvement by other agencies, including fire, sanitation, and ecology, serves no useful purpose. Law 163 already recognizes that they can be involved in permit issuance, not directly with the applicant, but only with the issuer (the municipality). Inspection thereafter is merely to ensure that the builder has built as designed.
- Perhaps making the Inspectorate responsible for enforcing the law against illegal construction.
- Supporting the Inspectorate in making its current database of construction permits a web-based log of all activity by all agencies involved, including especially logging in the date builders file zoning and construction permit applications, and the date municipal authorities issue the permits.

- Authorizing the Inspectorate to enforce the “silence is consent” provisions of Law 163 by issuing “deemed granted” permits, and to investigate and report to the Ministry on the reasons the relevant deadlines were missed, so that appropriate remedial measures can be taken.

Municipal authorities. Although Law 163 gave municipal authorities increased authority and responsibility for issuing zoning and construction permits, they appear not to have been provided much support in actually implementing the one-stop shops that are supposed to shift the burden of chasing signatures from the private sector to the public sector. Assessment team members talked to permitting authorities in two municipalities, both of which have master plans. The officials themselves were knowledgeable about legal and technical requirements, but admitted that they are unable to routinely meet Law 163’s deadlines of 20 days to issue zoning permits and 10 days to issue construction permits. Stakeholders raised a variety of concerns over the operation of the one-stop shops and the reason for delays:

- The State Construction Inspectorate says zoning permits are sometimes issued improperly, and for unofficial payments, and that the penalties for such behavior are too low to discourage it.
- Builders say some municipal authorities require the consent of neighbors before issuing zoning permits when there is no legal justification to do so. A better approach would be to provide community members with a structured opportunity to present legally valid objections before a zoning permit is issued. Unless they can show that a project violates applicable zoning requirements, however, the permit should be issued.
- Municipal authorities in some case also want detailed architectural drawings submitted with the zoning permit application. Builders are reluctant to make a costly investment in developing detailed drawings until after zoning is approved.
- Some municipal authorities continue to require that builders obtain approvals from the agencies Law 163 locks out of the process. Indeed, officials at one municipality admitted to reviewing construction permit applications while sitting around the table with representatives from these agencies and collectively deciding which applications should be shunted to the agencies for their approval.
- Builders and municipal authorities blame the Inspectorate for long delays in registering construction permits, a precondition to delivery of the permit to builders. In some cases the Inspectorate insists on receiving a complete set of architectural drawings, duplicating the package submitted to the municipality. This violates Lejava’s First Law, a fundamental reform principle described in the chapter on “Protecting Investors.” The Inspectorate concedes having attempted until July 2012 to use the registration period to confirm that the underlying zoning permit was properly issued and to investigate related complaints from neighbors. However, the Inspectorate says that since it changed its procedures in July 2012, it habitually turns registrations around within the three days allocated for the process.

Measures that could improve municipal authorities' implementation of the OSSs for zoning and construction permits include:

- Standard operating procedures, checklists, etc., could help make OSS permit processing more consistent among municipal authorities across the country.
- More impact in supporting municipal authorities nation-wide could be achieved by working through the Congress of Local Authorities of Moldova (CALM) to gather input and disseminate solutions to the problems they are experiencing.
- Developing a web-based log of construction projects, from the beginning of the permitting process through reception, to be shared by relevant stakeholders, would help to introduce accountability and transparency and reduce costs and delays.
- Measures to reduce delays caused by the Inspectorate registration process and interventions by agencies with no legitimate role to play are discussed elsewhere.

Cadastru. The state enterprise responsible for land registration, *Cadastru*, operates a land registration system that the Doing Business 2013 report ranks as 16th best in the world on the “Registering Property” indicator. Major changes are in the works that will propel *Cadastru*'s rank even higher. A data exchange system with the population registry is already in effect so that entering a citizen's unique identification number in *Cadastru*'s registry pulls identifying information like name and address from the population database. *Cadastru* is working to implement a data exchange system with the company registry. Such information exchange reduces the possibilities of error and relieves both public and private sectors from the burden of having to assure accurate information in multiple registries.

Persons seeking *Cadastru* information about specific parcels of land can now request that information online, but have to physically go to a *Cadastru* office to get a legally valid paper registry extract. *Cadastru* is working on legal and infrastructure changes that will enable it to deliver legally valid extracts electronically.

Cadastru's role in construction regulation comes after the reception phase, when the approved property is entered into the property registry. As noted above, *Cadastru* again verifies that the buildings constructed match up exactly with the drawings submitted before registering the property. Builders report that this process can take months and considerable expense in the case of large projects like apartment buildings, delaying their ability to begin selling the units. This procedure is redundant in many respects. The numerous approvals that builders undergo now are often to ascertain that the actual construction does in fact match the project drawings. Another approach to ensuring that *Cadastru* information is scrupulously accurate might include tasking the State Construction Inspectorate with verifying that projects are built as designed during the course of their other, ongoing inspections. Alternatively, *Cadastru* could simply register the project subject based on the drawings with a notation that actual dimensions have not been verified. If and when a subsequent verification is made, the notation could be revised.

D. SUPPORTING INSTITUTIONS

This section contains a brief overview of some of the key supporting institutions related to the construction sector.

Moldova judicial system. Construction sector participants have the same concerns about Moldova's judiciary that were identified by stakeholders in the "Protecting Investors" chapter of this report. These concerns center around corruption, results that seem inexplicable, and costly delays.

Technical University of Moldova. The Technical University has faculties in architecture and structural engineering that offer both undergraduate and graduate programs. The university has been converting its academic structure from its Soviet-era framework to the Bologna Process envisioned by the June 1991 Joint Declaration of European Ministers of Education.⁴⁸ The goal is to make the University's offerings comparable in quality and content to those of EU-member states.

Poor preparation of incoming students was cited as a significant problem. While the faculties limit admission to only students with high scores on the standardized tests administered after high school, those scores are increasingly unreliable. As a result, more focus is put on remedial work in areas such as basic mathematics, and not all graduates are able to perform at the level required for professional architects and structural engineers.

Another issue that handicaps University graduates is that to practice in Moldova they have to learn the prevailing technical standards in construction. Most of these standards are obsolete Soviet-era SNIPS, although in a few areas Moldova has adopted its own technical standards. Students in architecture and engineering programs in EU countries learn a shared body of knowledge based on the much more modern Eurocodes technical standards. The Technical University does offer graduate programs in the Eurocodes, and is eager to play an active role in helping Moldova adapt and adopt those technical standards.

Congress of Local Authorities of Moldova (CALM). Municipal officials describe CALM as an important resource in sharing information and advocating for the interests of local authorities. Working with CALM might be an effective way to support improvements in operation of the

Supporting Institutions

Moldova judicial system

Technical University of Moldova –scientific research, training specialists in the fields of architecture and structural engineering

Employers Federation of Building Companies, Road Workers, and Producers of Building Materials

"Condrumat" - protecting and promoting the interests of construction companies, road builders, and producers of building materials

Congress of Local Authorities of Moldova - protecting and promoting the interests of local communities

E-Government Center – developing common IT infrastructure and platform for data exchange among government agencies

Working Group for regulating entrepreneurial activity (WG) – reviews and approves regulatory impact assessments and draft laws and regulations regarding state regulation of entrepreneurial activity

⁴⁸ The Joint Declaration is available online at https://docs.google.com/viewer?url=http%3A%2F%2Fwww.bologna-bergen2005.no%2FDocs%2F00-Main_doc%2F990719BOLOGNA_DECLARATION.PDF.

one-stop shops for construction permitting operating throughout Moldova, and accelerating progress on development of local master plans.

E-Government Center. Moldova’s E-Government Center is working to develop a shared platform for government agencies that provides essential functionality for registries, administration of regulatory processes, and sharing of information among agencies and with citizens and businesses. The level of expertise and commitment to increasing the efficiency of government regulation and operations is impressive. Leadership expressed eagerness to collaborate with all stakeholders to create an efficient construction regulation platform that will increase transparency and accountability, and reduce transaction costs and delays.

Employers Federation of Building Companies, Road Workers, and Producers of Building Materials "Condrumat." Officials at Condrumat, an association of construction-related contractors, paint a picture of an industry that is well off peak levels reached in 2007. Condrumat estimates that employment in the sector was 20,000 to 30,000 in 2005, rose to more than 60,000 in 2007, and is now back to about 30,000. Average monthly salaries for construction workers ranged from 2,900 to 3,900 Lei in 2007, but are now about 30 percent less. The nature of the projects being constructed has also changed. In 2007, construction companies were working on apartment and office buildings, hospitals and shops. Now, there are few major projects, and much of the construction is for social purposes – construction and rehabilitation of government buildings, for example. A major cause of the decline in the sector, Condrumat says, is reduced flows of remittances. Many of the projects undertaken at the sector’s peak were financed by investment from Moldovans working abroad. The global financial crisis reduced those investments. Although remittances are picking up again, higher construction costs and less faith in Moldova’s economy makes those working in other countries more reluctant to invest in new projects.

Table III-2. Georgia Construction Growth – 2005-2008

Indicator	2005	2006	2007	2008	Growth
Number of square meters under issued building permits in Tbilisi (million sq. meters)	1.0	1.1	1.5	2.4	240%
Total Sales (million GEL)	779	1,125	1,605	-	206%
Value added (million GEL)	245.9	401.4	630.6	-	256%
Construction jobs	38,560	46,681	52,572	-	136%
Average monthly salary	292.3	391.0	495.1	723.0	247%

Condrumat was engaged in drafting of Law 163, and echoes the complaints about implementation previously discussed, while pointing to very real savings in time and money produced by the new law. Its officials would like to see a more effective collaboration between MRDC and the private sector to eliminate the implementation issues and extend Law 163’s conceptual framework to the construction and reception phases.

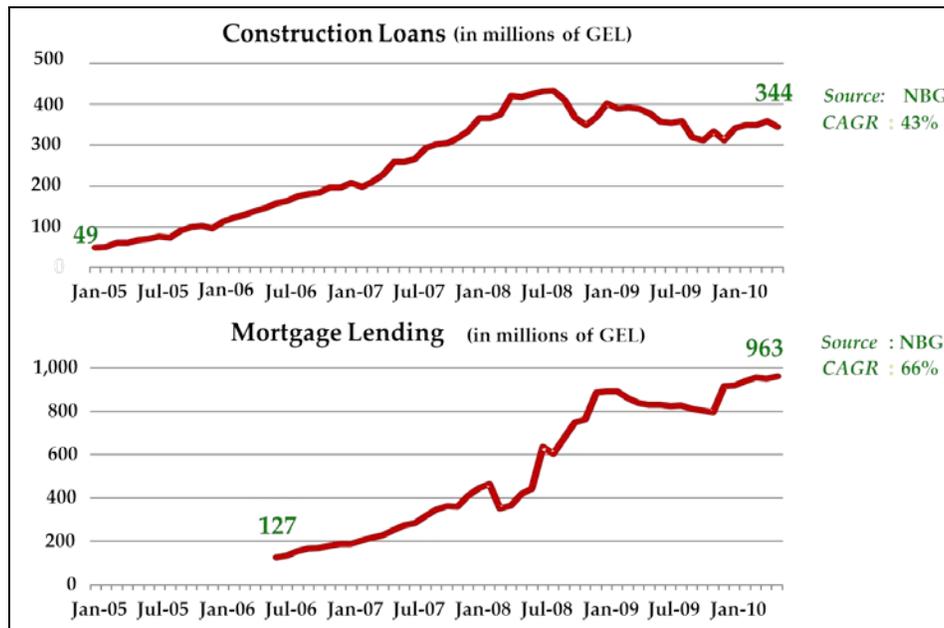
Working Group for Regulating Entrepreneurial Activity (WG). Stakeholders expressed appreciation for the role of the WG, comprised of equal representation from public and private sectors, in helping to enact Law 163. The WG’s activities in reviewing regulatory impact assessments of draft laws that affect business, gaps in its coverage, and recommendations for closing them, are described in the Chapter on “Protecting Investors.”

E. SOCIAL DYNAMICS

Moldova has one of the world’s most burdensome construction regulatory regimes, ranking 168th out of 185 economies surveyed, as noted in the section of this chapter on the “Dealing with Construction Permits” Indicator. International experience demonstrates that when increased government efficiency makes regulatory oversight simpler, faster, and less expensive, the volume and value of regulated transactions increases, often dramatically. Georgia’s experience with construction sector regulatory reform demonstrates this. An aggressive series of reforms increased Georgia’s rank on “Dealing with Construction Permits” from 152nd in 2005 to seventh by 2008. Table III-1, above, illustrates the dramatic increases in construction, jobs, and average salaries that accompanied Georgia’s rise in rankings.

The reforms of the construction sector also had an unanticipated impact on the financial sector. As illustrated by Table III-3, below, construction lending grew from \$49 million to \$344 million,

Table III-3. Growth in Georgia’s Construction Lending



which is a cumulative annual growth rate of 43 percent per year, from January 2005 to January 2010. Similarly, mortgage lending exploded from nowhere, and grew to almost \$1 billion, during a period that included the conflict with Russia and the onset of the global financial crisis. Regulatory reform increases access to finance because by reducing costs, delays, and uncertainty, it makes market participants more profitable and better credit risks.

Two mutually exacerbating factors appear primarily responsible for Moldova’s highly inefficient regulatory regime. First, requiring such an extraordinarily high number of signatures helps to enforce a curious system of accountability for mistakes in construction. By their signatures, technical experts assume criminal liability for construction flaws and they can be jailed or fined for mistakes. While this puts them at great risk, it provides little benefit for those who may suffer the consequences of such mistakes. Countries with more advanced construction regulation do not

provide criminal liability for mistakes. Requiring responsible experts to obtain insurance bonds and similar products provides a source of real relief for the victims of construction mistakes. Moreover, insurers' interest in reducing their own losses leads them to take measures to enforce quality. At this time in Moldova's development, such a requirement can also help develop a weak insurance sector. The pools of premiums would develop additional sources of capital for investment in the economy. In any event, requiring multiple signatures by the same person isn't necessary to create liability. The law can simply make the technical expert responsible without regard to whether or how many times he signs.

The second factor encouraging inefficiency is the very low pay scale for civil servants. The government officials encountered in the course of this assessment were among the most technically proficient we have encountered in development work. They deserve to be treated like the professionals they are, instead of having to resort to a range of efforts, sometimes inventive and sometimes mundane, to increase their own and their agencies' incomes. The current inefficiencies of the construction sector regulatory regime offer various opportunities for lowly-paid sector participants to increase their incomes, and, perhaps, help explain why some things never get fixed. The distortions to efficient regulation include:

- Sector representatives say that bribes are frequently required to get those whose approvals are necessary at various stages to sign off or simply to show up when they should, etc. Obviously, when bribes work to get people to do their jobs they are more likely to be effective in getting the same people to overlook compliance obligations, which makes the regulation worthless.
- As described above, agencies cut out of the permit issuance process use their power over the reception phase to re-engage and protect both their personal and agency incomes.
- Sometimes, the fact that Moldova still uses obsolete technical standards provides agencies with additional sources of income. Builders can "voluntarily" avail themselves of the agencies' consulting services to develop Eurocodes-based exceptions to the Soviet-era SNIPS.
- Similarly, regulator-owned companies that are free from civil service pay scales and require fees for services that may or may not be necessary creates opportunities for income generation. MRDC, which stakeholders say was resistant to Law 163, has several fee generating state enterprises. Law 163 broke the monopoly formerly enjoyed by its official verification company that was required to sign off on all project designs. Since the monopoly was broken by the introduction of competition among the verification company and certified verifiers, both costs and the time required have fallen sharply. The absence of master plans in most municipalities is a burden on many stakeholders, but MRDC's UrbanProject and RuralProject benefit from consulting fees charged on mandatory "coordination" in the absence of master plans.
- Finally, low compensation requires obviously talented people to scramble for as many sources of income as possible, creating egregious conflicts of interest. Architects and engineers, for example, may simultaneously work for municipalities, design projects, work for state enterprises, and/or serve as verifiers.

As noted in the chapter on “Protecting Investors,” it is probably neither fair nor useful to call such practices corrupt when they are so necessary and so widespread. When civil servants don’t earn enough to provide decent, normal lives for themselves and their families it may be more accurate to characterize the natural result as social policy rather than as corruption. The sector is likely to stay depressed, however, until reforms reduce the current inefficiency and high transaction costs. Given political will, aggressive reforms like those in Georgia are well within reach. Coupled with Moldova’s closer proximity to the EU, such reforms would likely produce even greater construction sector growth than in Georgia, and the opportunity to provide a decent wage to construction sector professionals, public and private.

F. RECOMMENDATIONS

The recommendations that follow are a combination of measures suggested by stakeholders and by assessment team members. They were vetted with financial markets representatives who attended a briefing on the preliminary findings of this chapter. This discussion highlights critical issues, the details of which have been discussed in more depth, earlier in this chapter:

Holding Government Accountable

Citizen Report Cards are participatory surveys that provide quantitative feedback on user perceptions on the quality, adequacy and efficiency of public services. They go beyond just being a data collection exercise to being an instrument to exact public accountability through the extensive media coverage and civil society advocacy that accompanies the process.

- *Enforce Law 163:* The failure of Law 163 to provide the full measure of relief to the industry from regulatory oversight is a failure of Moldovan governance. Ministers in charge of agencies that circumvent Law 163 don’t have to wait for new legislation. They can act now. To encourage more accountability from government and from the political parties responsible for its various subdivisions, Moldova may want to consider implementing a “Citizens Report Card” system to measure the perceived effectiveness of governance.⁴⁹ See text box above.
- *Extend Law 163’s conceptual framework:* The “revolutionary” conceptual framework of Law 163 should be extended to cover the entire regulatory process, from issuance of zoning and construction permits, through construction, reception and registration. This is an urgent task that should not await adoption of a new comprehensive Construction Code. Details that need to be addressed are discussed in the preceding text. The new regulatory regime should:
 - Eliminate involvement by any agency whose participation is not absolutely necessary.
 - Implement the principle that government should never ask any citizen or business for information that another agency already has.

⁴⁹ Tools and materials for implementing a Citizens Report Card program can be found online at <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTSOCIALDEVELOPMENT/EXTPCENG/0,,contentMDK:20507680~pagePK:148956~piPK:216618~theSitePK:410306,00.html>

- Minimize the number of inspections and approvals required – requiring laboratory tests of every batch of concrete and four inspections per floor by structural engineers is excessive.
 - Consolidate all inspections in the State Construction Inspectorate, including verification that a project is built as designed for purposes of registration with Cadastre.
 - Provide clear responsibility for acting against illegal construction, and allow municipal authorities to apply punitive tax rates until such projects are legalized.
 - Introduced risk-based regulation that matches the level of oversight with the degree of risk.
- *Understand and re-engineer incentives and activities of state enterprises:* The various construction-related state enterprises employ construction professionals whose skills should be usefully deployed in reforming and implementing a world-class construction regime. Too often, their livelihoods depend upon fees for services that are only necessary because of the numerous insufficiencies and inefficiencies plaguing regulation in Moldova. UrbanProject and RuralProject, for example, should profit from leading implementation of master plans all across Moldova, not just from their absence.
 - *Accelerate transition to Eurocode-based technical standards:* Moldova's adherence to the obsolete Soviet-era SNIPS is wasteful, costly, and inhibits growth in the sector. A more rapid transition to Eurocode based standards is essential.
 - *Accelerate adoption of master plans in all Moldovan municipalities:* Municipal authorities are tasked with responsibility for developing master plans, but claim they lack the financial resources. National initiatives can lay foundations that simplify and reduce the cost for municipalities. Examples include use of aerial photography and requiring utilities to release accurate maps of their infrastructure in a format suitable for master planning. Appropriate resources also need to be deployed to assist municipalities in this task, including perhaps the expert assistance of professionals from UrbanProject and RuralProject, and designating punitive taxes on illegal construction for master plan development.
 - *Implement a single, web-based log of all construction regulation:* It makes no sense for each municipality to develop its own database of construction activities and other agencies like the Inspectorate to maintain their own. The E-Governance Center is willing and able to work with stakeholders to develop a single system for shared use. This will reduce costs and delays, including, for example, need for the current requirement for registering permits with the Inspectorate, a source of many and bitter complaints from other stakeholders.
 - *Accelerate adoption of comprehensive Construction Code:* The many and conflicting laws now affecting regulation need to be not just collected, but comprehensively overhauled. Among the issues that need to be sorted out are the future roles of current state enterprises. Until this is done, there may be resistance to efforts to rationalize regulation. The current system of criminal accountability for mistakes in construction should also be re-thought, and civil liability introduced with requirements for insurance

products to provide relief for victims. More accountability for improper behavior by civil servants also needs to be introduced, with clear allocation of responsibility for enforcement and the powers necessary to do so.

SECTION IV. STARTING A BUSINESS

A. INTRODUCTION

The World Bank's *Doing Business* ranking for Starting a Business focuses on the time and cost of business registration. However, there is more to starting a successful business than getting it registered. If an entrepreneur can register a business successfully but cannot obtain necessary licenses or authorizations, registration alone will be meaningless. What the assessment team learned in the course of its work is that, in Moldova, it is the processes beyond the legal registration of a company, including closing a business, that present the biggest problems and costs to local businesses. Therefore, this chapter looks beyond the World Bank indicator to the broader framework of business creation, from incorporation to startup, and includes a brief discussion of business liquidation as well.

Overall, starting a business in Moldova does not appear to be a major problem area. Certainly there are problems and issues, as will be discussed below. However, few respondents said that the processes were so burdensome as to actively deter business startup and investment, whether domestic

or foreign. Rather, Moldova appears to fall in an intermediate category where the costs of business startup, though not exorbitant, are high enough to add significantly to the overall cost of doing business. These can act to discourage investment, especially in the case of small businesses and individual entrepreneurs.

A1. "Starting a Business" Indicator

The World Bank's *Doing Business* rankings for 2013 place Moldova in the upper half of the 185 economies in the survey with respect to Ease of Starting a Business, with a ranking of 92. This assessment found consensus that starting a business was neither difficult nor burdensomely expensive. This is consistent with the statistics on business formation (which show an increase over time) and FDI (which has been flowing steadily over the last three years). However, laws and practices involving operating a business and liquidating a business do present significant barriers for private businesses and entrepreneurs, which can discourage potential investment.

Starting a Business BizCLIR Scores	
Framework Areas	Score
Legal Framework	3
Implementing Institutions	3
Supporting Institutions	4
Social Dynamics	3

Starting a Business (Doing Business Rankings)	
Doing Business Ranking 2013	92
Doing Business Ranking 2012	82
Procedures (number)	7
Time (days)	9
Cost (% of income per capita)	5.7
Paid-in Minimum Capital (% of income per capita)	8.7

B. LEGAL FRAMEWORK

There are a number of forms in which business can be carried out in Moldova. The most common forms are the Joint Stock Company (JSC) and Limited Liability Company (LLC). In addition, Moldovan law also allows the formation of a General Partnership, a Limited Liability Partnership and a Cooperative; however, these three forms are rarely used.

The formation of these businesses is governed by the Moldovan Civil Code.⁵⁰ In addition, the Law on Entrepreneurs and Entrepreneurial Activity provides for three other forms of conducting business: the State Enterprise, the Municipal Enterprise, and the Individual Entrepreneur. As a practical matter, the private sector is dominated by three forms: LLCs, JSCs and individual entrepreneurs.⁵¹

Investors tend to prefer the LLC and JSC forms of ownership since both of these give investors protection: shareholders do not have liability for the obligations of the company, and their sole risk is the extent of their share capital. An LLC may have 1 to 50 shareholders, while a JSC may have an unlimited number of shareholders. Both corporate forms have minimum capital requirements: the minimum paid in capital for an LLC is 5,400 Moldovan Lei (MDL

Key Laws and Regulations

- Law on Entrepreneurs and Entrepreneurial Activity no. 845 dated 03.01.1992
- Law on Normative Price and Mechanism of Buying and Selling of land no.1308 dated 25.07.1997
- Law on Joint Stock Companies no. 1134 dated 02.04.1997
- Law on Chamber of Commerce and Industry no.393-XIV din 13.05.99
- Civil Code no. 1107-XV dated 06.06.2002
- Law on Licensing of Business Activity no. 451 dated 30.07.2001
- Law on Investments in Entrepreneurial activity no.81 dated 18.03.2004
- Law on State Registration of Legal Entities and Individual Entrepreneurs no. 220 dated 19.10.2007
- Law on Basic Principles of Regulation Entrepreneurial Activity no. 235 dated 20.07.2006
- Law on Limited Liability Companies no. 135 dated 14.06.2007
- Law on Labor Migration no. 180-XVI dated 10.07.2008; in force - since 01 January 2009
- Law on the Status of Foreigners no. 200 dated 16.07.2010
- Law on Internal Trade no.231 dated 23.09.2010
- Law on Implementation of the One-Stop-Shop in Business Activity no.161 dated 22.07.2011
- Law on Authorization of Business Activity nr.160 dated 22.07.2011
- Law on State Control of Business Activity no. 131 dated 08.06.2012;
- Government Decision on implementation of the One Stop Shop within Licensing Chamber no. 1068 dated 19.09.2008
- Order on licensing conditions and lists of documents to be annexed to the application form on the issuance of the licenses for certain business activities No. 12-q, approved

⁵⁰ Specifically Law No. 1107-XV dated 06.06.2002. This law will need review and updating in the next few years for consistency with Chapter VI (“Companies”) of the EU’s Acquis Communautaire. However, this is not likely to be a priority until Moldova achieves EU candidate status, which is not expected in the near (<5 years) future.

⁵¹ As of September 2012, the SRC had approximately 162,600 businesses registered. These broke down as follows: 79,742 limited liability companies (the most common form, about 48%); 66,063 individual entrepreneurs; 4810 joint stock companies; 4012 cooperatives ; 1497 state and municipal enterprises; 3342 Non-Profit Organizations and 3133 “Other”. The first two forms accounted for more than 90% of all registered entities, although this figure is somewhat complicated by the existence of “zombie” registrations – see below.

(approximately US \$477 as of the date of this report), while the minimum amount of capital of the JSC is 20,000 MDL (approximately US \$1,770.)⁵² As with most countries in the region, the process of incorporation is included in the overall process of business registration.⁵³

Registration. Moldovan LLCs and JSCs are established through registration with the State Register of Legal Entities. This Register is at the State Registration Chamber (SRC), which is under the Ministry of Justice. Prices for registration are not high: it costs approximately \$62 USD to register an LLC within 5 days, and approximately \$160 USD to register it on an expedited basis of just 4 hours. Similarly, it costs approximately \$74 USD to register a JSC within 5 days, and approximately \$220 USD to register it on an expedited basis of 4 hours.⁵⁴ There is general consensus that registration with the SRC is fairly easy: the costs are not onerous, the staff are competent, and expedited registration is transparent and affordable.

In 2010, a One Stop Shop (OSS) mechanism was established through which the SRC provides information on newly-registered companies to a number of other authorities, such as the STI, the National Bureau of Statistics⁵⁵, the National Social Insurance Fund (“National Social Insurance,” often known by its Romanian acronym, CNAS), and the National Health Insurance Company (“National Health Insurance,” or CNAM)⁵⁶. However, a number of interviewees noted that both CNAS and CNAM continue to require additional registration with them of these newly-created businesses. In the case of the STI, their legislation still contains a provision requiring information to be submitted to it independently. In the case of CNAS and CNAM, the requirement to register with them separately is mandated through internal directives.

These duplicative filing requirements pervade the legal and regulatory environment, generating additional time and administrative burdens for entrepreneurs and creating uncertainty. More generally, several interviewees noted that:

- Laws intended to simplify procedures are often ignored by the implementing agencies;
- Regulations may not track the laws, either because the laws have changed, or because the regulations were not drafted in accord with the laws; and,
- Agencies may issue technical directives which are contrary to existing laws. Additionally, while laws and regulations are published in the official gazette, technical directives are not. This means that it can be difficult to find exactly what the rules actually are for a particular act of registration.

⁵² Minimum capital requirements (MCRs) were once common around the world, but modern best practice is to sharply reduce or eliminate them for standard corporate forms. (There are exceptions, such as banks and insurance companies, where best practice is to keep a high MCR.) Moldova is somewhat unusual in keeping a relatively small, token MCR for all LLCs and JSCs. Note that simply having a MCR – even a small one – results in a significant reduction in a country’s World Bank Starting a Business rank.

⁵³ This is different from the American and Anglo-Saxon traditions, where it is possible to create a corporation but not license it as a business – i.e., a “shelf” corporation that is created and kept against future needs.

⁵⁴ <http://cis.gov.md/en/content/666>

⁵⁵ <http://www.statistica.md/>

⁵⁶ This mechanism was created with the support of the USAID BIZTAR project (2006-2011).

As noted above, Moldova ranks only 92nd among 185 countries worldwide in the 2013 Doing Business rankings for Starting a Business. This is lower than other countries in the region. By way of comparison, Belarus is ranked 9th, Ukraine is 50th, and Romania ranks 63rd.

The Doing Business Report has summarized the steps for registration in a chart, which is reproduced in relevant part below:

Table IV-1. Procedures to Eliminate for ‘Starting a Business’ in Moldova

No.	Procedure	Time to complete	Cost to complete
* 2	Open a temporary bank account and deposit at least 40% of the registered capital of the company; pay the registration fee	1 day, included in the previous procedure	no charge
4	Register with the Territorial State Fiscal Inspectorate	1-3 days	no charge
5	Convert the company’s temporary bank account to a permanent one	1 day	no charge
6	Register the company with the Social Security Fund	1 day	no charge
7	Register the company with the National Medical Insurance Company	2 days	no charge

It appears likely that some of these steps could be eliminated without any negative consequences for the registration process. The registration with CNAS (Social Security), and with CNAM (Medical Insurance) have already been formally, legally eliminated. As noted above, parallel registration does still occur sometimes. However, eliminating this should be fairly straightforward, and would provide a swift and significant “bump” to Moldova’s ranking.

The requirement to deposit 40% of the registered capital, on the other hand, is required by law, but is no longer carried out in practice. The requirement is still on the books, but the SRC does not require companies to deposit the paid in minimum capital.⁵⁷

If a policymaker or donor wishes to improve Moldova’s Starting a Business rank, it would be quite easy to do so. Assume that Moldova undertakes the following simple reforms: eliminate the minimum capital requirement altogether, and affirm that registration at SRC includes registration with CNAM and CNAS. Using the simulator, we can see that this jumps Moldova’s ranking from 92nd to 38th – well above average in both the world and the region, and comfortably in the middle of the pack for Europe as a whole.

Permissions. Registration of a business is just the start of its life-cycle, and in many ways the easiest. More issues surface when businesses must contend with securing the various “permissions” required. The Moldovan term “permission” includes the various authorizations set forth in the relevant law:

⁵⁷ It is noteworthy that the Bank is counting two procedures (registering with CNAS and CNAM) that are no longer legally required but are still carried out, but also is counting a third procedure (depositing the 40%) that is no longer carried out but is still formally, legally required. For consistency, they should pick one or the other.

- (1) A business may be started up and/or run based on an authorization.
- (2) The authorization is a document, issued by the competent public administrative authority, which authorizes the applicant to start up and/or run a business. The notion of authorization includes licenses, permits, certificates, notices, approvals, coordination, and other similar administrative operations, prior to or following the issuance of the authorization.⁵⁸

Article 10(2) is not an exhaustive list; it provides that the “notion of authorization” includes six different names of documents (licenses, permits, certificates, notices, approvals, coordination) and then adds the catch-all “other similar administrative operations,” which are obtained “prior to or following the issuance of the authorization.” This very broad language has given administrative agencies a powerful mandate to demand a wide range of “permissions” from businesses.

In common parlance in Moldova, “license” is used most often to refer to a permission to carry out a certain activity set by the Law on Regulation of Entrepreneurial Activity through Licensing, e.g. tourism. In effect, the national government checks a person’s ability and qualifications to conduct the activity. There are 44 types of licenses, 32 of which are issued by the Licensing Chamber and 12 by State regulatory bodies such as the National Agency on Energy Regulation. The recently-approved “Nomenclature” of permitted documents lists those documents which may be requested by the licensing authorities for each particular license. Notwithstanding adoption of the Nomenclature, agencies continue to seek documentation not included therein. The Licensing Chamber contends that it follows the requirements imposed by each agency for which it issues licenses, suggesting that clear lines of authority are not established among the agencies.

The Licensing Chamber is established in Chisinau, and is generally considered successful and fair in its application of licensing. If an applicant collects all necessary documentation, the process moves smoothly and a second appointment is arranged to conclude the process. The Licensing Chamber recently introduced E-Licensing, whereby applicants can submit an application and all the relevant documents on-line, and receive confirmation and approval via e-mail. This enhancement should benefit applicants outside of Chisinau.

In any event, the Licensing Chamber is far from the only body issuing “permissions”. An “authorization”, for instance, is a type of permission granted by a local authority for a construction permit or to conduct an activity at a particular location. As the issuing of authorizations is done at the local level, there is considerable local variation in the nature of the application, the time required, and the scope of the authorization once granted.

Moldova has made several attempts to cut back the jungle of “permissions”. The most recent was the Regulatory Guillotine Law of 2011, which (in theory) reduced a great many regulations while requiring many more to be clarified and consolidated. However, while much work has been accomplished, it is clear that much remains to be done.

⁵⁸ Law on Basic Principles Regulating Entrepreneurial Activity, No. 235-XVI as of 20/07/2006, Official Monitor No. 126-130/627 as of 11/08/2006, Article 10

Workforce permitting issues. Workforce issues are not, strictly speaking, issues of business creation. However, the complex permitting system for foreign workers presents special problems for foreign businesses seeking to start a business in Moldova, and thus deserves at least a brief mention here.

When a foreign company invests in Moldova, it will often seek to bring in foreign individuals to work for it. This can be the owner/founder of the company or others to work in managerial and high level positions. To be employed in Moldova, a foreigner must obtain two permits: a work permit (obtained from the National Employment Agency) and a residence permit (obtained from the Bureau of Migration and Asylum)⁵⁹. Normally the work permit must be obtained before the residence permit can be applied for. The residence permit itself will be issued by the Ministry of Information Technologies and Communication.

The need for two permits, obtained by working with three different ministries, can raise significant administrative burdens. Problems with residential and work permits are regularly cited by foreign investors as minor but chronic and annoying issues.

Another workforce issue is with the Law on Internal Trade (Law No. 231). Article 13 (2) of the Law requires that those conducting “trade activities” must either have training at a specialized institution, or be certified to have the necessary skills as a result of work experience. However, this provision does not state what kind of training will be required, or which institutions might provide and certify this training. Nor does it provide any standards for certifying work experience. Section 13 (2) was originally supposed to enter into force on January 1, 2012, but according to the Ministry of Economy’s Internal Trade Division, Article 13 (2) is not currently being applied as there are no mechanisms for doing so. Nonetheless, the provision remains on the books. If ever applied, it is likely to be a significant source of confusion and delay.

*Liquidating a business.*⁶⁰ The procedures for liquidating a business in Moldova are complicated and time-consuming. There are several reasons for this, but the most important seems to be the protracted process of proving that no debts are owed to creditors or to the State.

A party wishing to liquidate a business must publish a notice twice in the Official Gazette of the Republic of Moldova during two successive weeks. Publication in the Gazette gives formal notice to creditors that they have six months to make a claim against the company. There is near-unanimous agreement among businesspeople that six months is an unnecessarily long duration for creditors to make a claim against the liquidating company, and that a shorter period of two months would be adequate. In addition to the six months of vulnerability to claims, the company cannot distribute assets to its shareholders for twelve months after the second publication of the Notice in the Official Gazette. Presumably this is intended to prevent the shareholders from

⁵⁹ Without a residence permit, a foreigner can stay in Moldova for no more than 90 days during a six-month period. Special rules enable some investors to benefit from less burdensome administrative requirements and allow for the granting of longer work permits. Currently, the head of an enterprise can stay in Moldova for 1 to 5 years, depending on the amount invested

⁶⁰ This deals with liquidation in a general sense, not with the “Closing a Business” rankings of the World Bank’s “Doing Business” survey. This is because “Closing a Business” uses a very complex and specific case for their methodology – one which is not always applicable in a broader analysis.

claiming a company's assets via dividends. Its effect, however, is to encourage investors to avoid the lengthy liquidation process, instead keeping the business in existence as a "zombie" company.

Another major difficulty is the need to get clearances from the state that no amounts are owed them. The most onerous of these clearances is secured through the STI and involves two tax audits. Immediately after the second publication in the Official Gazette, the company may approach the STI to request an audit. Because the STI has no legal requirement to audit within a specified timeframe, the company may wait for months to be audited. The audit process itself is stressful – a company may be fined for even innocent or inconsequential errors – and unpredictable.

While the company waits to liquidate, it must continue to retain and pay a managing director and a chief accountant. A further problem is the fact that the Labor Code stipulates that an individual is not permitted to be a managing director of more than one company at the same time. This can prevent entrepreneurs from trying to create a new business for a long period of time after the decision has been made to liquidate the old business.

Finally, because assets cannot be distributed until all approvals and clearances are obtained, a shareholder's money is tied up in a company throughout the lengthy process of liquidation described above. Many businesspeople asserted that inasmuch as the STI already has voluminous information on the taxpayer and company, and inasmuch as creditors have the opportunity to make claims in the first six months after notice publication, the prolonged procedures with the STI are unnecessary, burdensome, and an impediment to business investment.

It is understandable that Moldova wants to ensure that creditors and the State fiscal resources are protected when a company wants to liquidate. Reasonable rules should exist to protect those to whom money is owed while allowing businessmen to close a business. At present, though, the scales are tipped in favor of the State and creditors. Most businessmen respond by undergoing informal liquidation – shutting down the business, selling off assets, and resigning as managers and directors – without ever formally terminating the business, leaving an inactive company on the books of the SRC.⁶¹

The practice of abandoning companies is by and large negative; it creates considerable administrative problems for the Licensing Chamber and also for STI. It can also lead to unpleasant surprises for the entrepreneur if either of these bodies decides to chase down the owners of an abandoned enterprise – which does occasionally happen. That said, the practice is so common that, while formally illegal, it must be considered the default method of liquidation.

⁶¹ The exact number of such companies is unknown, but it is possible to make reasonable estimates. One method is simply to check the difference between the number of registered enterprises and those submitting regular reports to the Statistics Bureau or STI. In the official SRC database there were 103,412 enterprises as of October 1, 2012. However, according to the Statistics Bureau only 48,541 were submitting regular reports as of the end of 2011. This means that about 55% of all companies registered with SRC are inactive. The bulk of these are probably companies that have been de facto liquidated, as described above.

Regulation and small businesses. Laws and regulations in Moldova tend to be rigid and to be written with regard to a particular model business – usually a large business. For example, Law 1100/2000, Art. 13, requires wine producers to have a 500 sq. m. warehouse. This is an excessive size for a small producer. Yet Moldova has many small wine producers. If this requirement is imposed before registration, or as a condition for licensing, they will not be able to register or license their businesses. Even if they do, they will still be in formal violation of the law. This type of problem is common across a wide range of businesses. The imposition of the Regulatory Guillotine last year gave some relief, but many of these laws and regulations are still on the books.

C. IMPLEMENTING INSTITUTIONS

State Registration Chamber (SRC). This Chamber serves as the gateway into forming a company. While the process is generally rapid and not cost prohibitive, there are issues to address. For example, SRC insists that businesses use its Charter template rather than a Charter drafted specifically for the company with provisions tailored to its particular situation. This is a nuisance for businesses and restricts the power and flexibility of the corporate form.

Key Implementing Institutions

- State Registration Chamber
- State Licensing Chamber
- Regional and Municipal Authorities
- State Tax Service

As discussed in the Legal Framework section of this chapter, another lingering constraint is SRC's ineffective use of the OSS to streamline reporting of business registrants. A lack of coordination and communication between governmental ministries and agencies further thwarts the process. Hence, although the law governing registration is “modern” in that it provides for an OSS, the process remains limited by conflicting legislation (e.g. Art. 163 of the Tax Code) or by agency directives. One lawyer interviewed noted that his distrust in the OSS filing process causes him to file reports separately to secure proof that the documentation was received by all parties.

Licensing Chamber. The Chamber rests under the Ministry of Economy of Moldova, and manages the issuance of licenses to perform an activity. It acts as an OSS by collecting the various documents needed for the license, transmitting them to the agency participating in the licensing process, and then issuing the license after review by the participating agency. It was observed that the Licensing Chamber requests documents from applicants that are not required by the Nomenclature. If a document is not listed in the Nomenclature, it is unlawful to require it for registration. The Chamber contends that its agencies request the documents and it follows these orders. This process has negative effects on public trust of the process and on the enforcement of the Nomenclature. Despite this concern, the Chamber is largely considered an efficient organization that is a fairly user-friendly OSS to secure licenses. And, as noted earlier, has recently streamlined the process further by introducing on-line E-Licensing.

Regional and municipal authorities. A different set of One Stop Shops – not to be confused with the One Stop Shop represented by the Licensing Chamber – are the “One Stop Shops” in the

municipalities.⁶² These OSSs deal with construction permits and trade authorizations. As described in the Legal Framework section of this chapter, trade authorizations are specialized business permits issued by local officials such as the mayor – i.e., to open and operate, e.g., a food store at a particular location.

The legal framework was needed because these local One Stop Shops operated on an ad-hoc basis. Through the USAID/BIZPRO project (2003-2006), OSSs were established in 15 locations throughout the country. These OSSs were managed by third parties, generally through local branches of the Chamber of Commerce and Industry. They served two key functions: receiving and processing construction permits and trade authorizations. Management by a third party eliminated direct interaction between the applicants and the local public authority, which had proven a fertile source of petty corruption and delay. The difficulty in maintaining these OSSs lay in political transitions, which brought new mayors and authorities. Over several years, the new authorities reverted roughly half of the OSS back from transparent operations, or simply shut them down. “In effect, they backslid, once again permitting unofficial payments.”⁶³

The USAID/BIZTAR project (2006-2011) supported new legislation giving the OSSs formal legal recognition. This law, enacted in the summer of 2011, clarifies the authority of the OSSs and prevents mayors or other local authorities from summarily closing them. Furthermore, the new legislation will enable new OSSs to open in Moldova. Fee schedules are still very modest, and OSS can operate under the umbrella of a non-governmental organization (NGO) or a Chamber of Commerce.

That said, there are still issues with the municipal OSSs. There are currently less than ten across the entire country.⁶⁴ A municipal OSS can assist with trade authorizations and construction permits, but the entrepreneur is nonetheless required to personally ensure that various inspections are performed (e.g. fire department and sanitary inspections of the proposed premises) before operations can begin. Most OSSs charge modest fees that do not necessarily cover their costs, and certainly do not allow for new equipment or expansions.⁶⁵

There are also some legal issues with the OSSs. The granting of trade authorizations is governed by Law No 231, the “Law on Internal Trade”. Article 15 of the Law requires the local government to examine a request for a trade authorization, along with its supporting documents, within 20 calendar days. During this period, the government is supposed to check with the “public authorities” (e.g. fire department, health official, police) for “compliance with legal provisions on the principle of single window.” However, Law No. 231 does not clearly define the “principle of ‘single window’”. This has led to occasional confusion, and in some cases

⁶² These were established by the “Government Decision on Implementation of the One Stop Shop within Licensing Chamber,” no. 1068 dated 19.09.2008, and the “Law on Implementation of the One-Stop-Shop in Business Activity” no.161 passed in July 2011. The latter is often called the “One Stop Shop Law”; it was designed to give a detailed legal framework for the municipal OSSs, which the earlier Government Decision had authorized.

⁶³ Draft Quarterly Report January – June 2011, USAID / Moldova Business Regulatory & Tax Administration Reform (BIZTAR) Project, p, 18

⁶⁴ The exact number is between five and eight, because several OSSs are only working partially or intermittently. In 2006 there were fifteen.

⁶⁵ Several OSSs receive support either from the municipality or from the local chamber. All the OSSs have asked for donor assistance.

applicants have been forced to walk their applications around to the other authorities – thus negating the whole point of a One-Stop Shop.⁶⁶

State Tax Inspectorate. The State Tax Inspectorate is extensively examined in the Chapter on “Paying Taxes.” It is mentioned here because registration with the STI is required for a company’s initial registration. Most businesses say that this is not a significant obstacle to starting a business. The process of registering with STI and acquiring a Taxpayer ID Number is reasonably straightforward and predictable, and not excessively expensive. However, when terminating a business, the STI is seen as perhaps the greatest barrier to liquidation. The reasons for this are discussed under “Legal Framework”, above. It should be noted here that the STI is not seen as sympathetic or helpful to businesses attempting to liquidate.

D. SUPPORTING INSTITUTIONS

Supporting institutions are those which provide services that complement the legal framework and implementing institutions, and enable the system to function as intended. To the foundation and beams established by the legal framework, which are put into place by the implementing institutions, are added critical functions like electricity, which allow the structure to serve its purpose. In this same way, supporting institutions, such as the professions of law or accounting, enable modern business systems to operate.

In addition to professions such as law and accountancy, many of the institutions supporting entrepreneurs throughout the life-cycle of a business (i.e. starting, operating, or liquidating a business), are engaged in important advocacy work on behalf of these businesses. Much of this work will be described in the Social Dynamics section of this chapter, but these institutions should be described through the lens of their important role as supporting institutions.

E-Governance Center. The E-Governance Center is the government’s initiative to provide a “Cloud” portal to host the electronic services provided by various public institutions. For example, e-Licensing is under development and may become available by the end of 2012. This initiative will enable the Licensing Chamber to gather information directly from governmental agencies, the process for which currently requires the applicants to submit this information themselves.

The E-Governance Center faces some problems. Its grant of authority is shallow but broad: in theory, it has an interest in almost every electronic interaction between government and citizens. In practice, it faces considerable opposition from other government agencies, many of which have their own plans and priorities for e-development. The Center received a large grant of funds from the World Bank in 2011; however, in proportion to the very broad scope of its responsibilities, and the amount of work to be done, the Center’s resources are limited. At this time, the Center does not play a direct role in supporting business registration and liquidation. However, if the Center’s plans for expansion are successful, it could become a significant implementing as well as a supporting institution.

⁶⁶ The BIZTAR project recommended amending this provision when passing the 2011 “Law on One Stop Shops” (see above), but this recommendation was not followed.

Chambers of Commerce linking Moldova to international markets and to the U.S. The Moldova Chamber of Commerce and Industry (“CCI”) provides an extensive array of services for Moldovan businesses. The CCI is defined in Law 393-XIV as a “non-governmental, autonomous and independent organization, which represents common concerns of the Republic of Moldova entrepreneurs.” Although supported by the State, it has been independent since 1991. The CCI has one main branch in Chisinau, nine regional branches, and approximately 1,500 members.

The objective of the CCI is to represent its members in connection with domestic and international business and economic matters, before Moldovan governmental authorities, and with foreign business organizations. Among its goals is to be involved in reviewing and commenting on legislation and normative acts affecting business, to assist in contacts between the business community and state authorities, to organize professional training and improve the professional skills of its members, to provide businesspeople with necessary information, and to promote the development of foreign trade and export of goods and services. The CCI also houses a Court of Arbitration, and it sees the need for arbitration and mediation as an alternative to commercial dispute resolution in the courts. The CCI hopes that alternative dispute resolution (ADR) may be a strong solution for reducing corruption and delays in the courts, and the number of disputes brought before the CCI’s arbitration court has been growing each year.

The CCI assists businesses in registration in two major ways. First, it runs or supports several of the municipal One Stop Shops, discussed above. Second, it provides advice and guidance on the registration and licensing processes to members and potential members. It appears to be doing a reasonably competent job with both of these functions.

American Chamber of Commerce in Moldova (AmCham). AmCham Moldova was founded in 2006. It has 70 members, large and small, including both foreign and Moldovan companies.

AmCham performs a wide range of advocacy services. One example is a draft law that it has proposed to amend current legislation in order to facilitate the procedure for issuing work and residence permits. These permits are important for businesses, as described in greater detail in the section on “Obtaining and Retaining a Qualified Workforce.” AmCham also lobbied in support of Law 160, which listed permissive acts for licensing and which entered into force in April 2012.

Organizations representing foreign investors in Moldova. There are a number of other organizations representing foreign companies. One key organization is the Foreign Investors

- | Key Supporting Institutions |
|--|
| <ul style="list-style-type: none">• E-Governance Center• Moldova Chamber of Commerce and Industry• Moldova-American Chamber of Commerce• European Business Association• Foreign Investors Association• National Confederation of Employers’ Associations of Moldova (CNPM)• Association of Accountants and Auditors• Moldova Bar Association• Large auditing firms• E-Government Center• Prime Minister’s Office for Attracting Investments• Notaries |

Association (FIA). Founded in 2003, the FIA currently has 15 members. These are all large foreign investors – the 15 members together employ about 15,000 Moldovans and represent over US\$900 million of investment. The FIA engages in advocacy in matters such as taxation, corporate governance, and labor law. The FIA also enjoys access to proposed legislation through its membership in commissions and consultative councils. The FIA is perceived as a powerful and influential voice, but one whose interests are limited to those of its membership, i.e. large foreign companies.

Another such organization is the recently-formed European Business Association (EBA). The EBA currently has 25 members, which includes European companies working in Moldova as well as Moldovan companies, law firms, and the Moldovan-based operations of non-Moldovan companies. Its goals include advocating for improving the legal and regulatory environment, through proposing and discussing legislative amendments with the Government and relevant parliamentary committees, espousing European standards and good governance, as well as serving as a platform between the public and private sectors. At this time, the EBA is not as prominent as AmCham or the FIA. However, the experience of other countries in the region suggests that the EBA will become better known and more influential as Moldova moves forward into the EU candidacy process.

CNPM. The National Confederation of Employers' Associations of Moldova (CNPM in Romanian) is an umbrella group comprising employer associations in different industries, ranging from roads and transport to sugar production. While membership is open to all employers, the majority of its members are SMEs, and CNPM is one of the few organizations that undertakes advocacy on SME-specific issues. CNPM does not have a strong record of influencing legislation or the business environment in Moldova. CNPM representatives say that this is because the government lends a more attentive ear to larger businesses.

Professionals and professional associations in the business environment. Professional associations play a relatively limited role in Moldova compared to other countries in the region. In Romania, for example, the Bar Association is relatively prominent and may advocate for changes to laws, including commercial laws and procedures involving business creation and liquidation. This is not the case in Moldova. The potential for this does exist – the lawyers' and accountants' associations both have a formal mandate to consider such issues – but it has not happened yet. The Bar Association, in particular, clearly has the capacity for advocacy on these issues but has shown no interest to date.

Lawyers. Access to legal services does not appear to be a limiting factor for starting or closing a business. There are 2,400 lawyers in Moldova, of which 1,400 are in Chisinau. Several respondents claimed that the quality of individuals going into the legal profession has deteriorated in recent years. Reasons cited included the “brain drain” of talented young people out of the country and the relatively low salaries in the legal profession. But while quality may be an issue, it appears that cost and availability are not; as one respondent noted, “one can always find some sort of lawyer”.

Accountants. Accountants occupy a critically important place in the life-cycle of a Moldovan business. Government agencies require numerous tax and financial reports, and tax audits play a

crucial role in the closing of a business. (Tax reporting is dealt with more fully in the section entitled “Paying Taxes”.)

Accountants are organized into the Association of Professional Accountants and Auditors of the Republic of Moldova (ACAP RM). ACAP RM has approximately 1,000 individual and firm members, including students. It is a member of various international bodies such as IFAC

(International Federation of Accountants), SEEPAD (South-Eastern European Partnership on Accountancy Development) and ECCAA (Eurasian Council of Certified Accountants and Auditors). Among ACAP RM’s primary goals is to increase Moldovan compliance with IFAC and EU standards.⁶⁷ It provides a wide range of educational programs, trainings, and certification programs to this end, including instruction on electronic submission of tax declarations and on the new International Financial Reporting Standards, which will come into force on January 1, 2013. These standards will require a shift from Moldovan national standards to the international standards at that time.

Key Legal Resources in Moldova

- ACI Partners Law Firm
- Grant Thornton
- PWC (PriceWaterhouseCoopers)
- Vernon David Law Firm
- Turcan Cazac Law Firm

Certifications like Certified Account Practitioner (CAP) and Certified International Professional Accountant (CIPA) are intended to engage Moldovan professionals in international standards and processes, elevate the skills of Moldovan firms, and ultimately encourage trained Moldovans to pursue employment in Moldova. However, the experience of other transition countries suggests that, in the short term, they may have the opposite effect: by giving Moldovans access to international certification, they may make “brain drain” even easier.

Access to accountants is occasionally a problem for Moldovan businesses, especially smaller ones. The number of accountants is limited, especially outside of Chisinau. The brain drain is a serious problem in this profession; unlike (for instance) a law degree, an accounting certificate travels well and can be used to hunt for jobs abroad. The limited number of accountants, combined with the very high demand for accounting services, means that smaller businesses sometimes must “stand in line”. One response to this has been the rise of large numbers of uncertified bookkeepers. Often these are people with little or no professional training who have learned how to prepare books and do simple accounting for small businesses. In many cases, bookkeepers will prepare documents for a quick review and signoff by the accountant.

Auditing firms and their role in advocacy. The major auditing firms, including the “Big Three” accounting firms, have taken an active role in advocacy, both through organizations such as AmCham and directly. PWC, for example, has made comments and recommendations directly to the government on tax laws and on accounting requirements. It should be noted that these firms tend to have a large-business perspective, since most of their clients are large. Nonetheless, they could be useful potential partners in a reform effort, as the relevant Ministries tend to take them seriously.

The Government’s role in investment. The Prime Minister has established an office, the Prime Minister’s Office for Attracting Investments, which aims to serve the following purposes:

⁶⁷ Compliance with EU accounting standards is a requirement for membership.

improving Moldova's image for investment generation, providing investment aftercare, and advocacy. In theory, the Office's mandate covers all investment. In practice, it is very focused on FDI. It is a small office, with four FTEs. The Office claims that associations and investors in Moldova are already liaising with them to advocate on behalf of the business community. In theory, the Office could advocate with the Prime Minister and government agencies for positive change. However, it should be noted that the Moldovan Investment and Export Promotion Agency (MIEPO) is supposed to serve this same advocacy function

Notaries. Moldova's notaries provide official translations and also notarize corporate documents such as charters, articles of association, and amendments to corporate documents. They are also required by law to notarize many sorts of contracts, including contracts for the sale of land. In many countries, notaries are gatekeepers and/or rent seekers, adding significant costs and delays to business activities without adding commensurate value. This does not appear to be the case in Moldova; notaries are widely available and not exorbitantly expensive, and respondents had no major complaints about notaries or their effectiveness.

E. SOCIAL DYNAMICS

Communications. A theme heard continuously during the Assessment was the poor state of communication between businesses and government at all levels from policy makers to administrators. Government agencies are generally not interested in collecting input from businesses. Even when they do, there are not strong formal or informal mechanisms for transmitting those inputs to policy makers and acting on them. Similarly, agencies are not very interested in communicating with businesses. The requirement to publish proposed legislation on Ministry websites is not consistently obeyed. Changes to rules and policies are often unpublished and not promulgated in any other way. Many agencies do not provide pamphlets or posters explaining their processes and how to navigate them. New registrants at the Chamber of Registration or the Chamber of Licenses are not given any information as to their formal legal rights or responsibilities. Most major government bodies have websites, but they are often "pro forma", giving basic information but not (for example) requirements for a permit or license or downloadable applications. Feedback does not usually generate a response.

Broadly speaking, most businesses feel that the government is at best indifferent to their concerns, and at worst is biased in favor of particular, politically connected businesses and/or is actively hostile to business generally. As a result of this, businesses seek to cultivate informal contacts with government representatives. For example, accountants will make a point of knowing the staff at the local tax office. This has mixed results; it can allow informal "short cuts", but can also lead to favoritism and petty corruption. In the case of business registration and liquidation, this dynamic tends to work against businesses, because these are functions that most businessmen do only rarely.

Poor communications between government agencies was also mentioned a number of times. For example, the Chamber of Registration is supposed to collect detailed information from a registrant and then share it with other agencies (CNAS, the medical insurance system, the

Ministry of Finance, etc.). However, these agencies often demand the same information again from registrants. In addition, multiple different agencies require reports from businesses on at least a quarterly basis, and these reports are often duplicative.

Uncertainty. Related to communications is the issue of uncertainty. Many respondents said that the biggest issue was not time or cost as such, but *not knowing* the time or cost of a particular application or procedure. The uncertainty made it difficult or impossible to plan ahead: will I be able to open the doors on January 1 or not until sometime February? Will we be able to start this new work next week, or not for 90 days? This is the one area where respondents said that the licensing and permitting system could, in fact, actually deter them from starting a business or entering a new field.

Not an SME-friendly environment. There is still a perceived dynamic of hostility to small businesses in particular. Small businessmen and individual entrepreneurs regularly complain that the government “treats them like criminals”. This may be an exaggeration, but it does appear that government actors are often suspicious of small businesses and individuals, seeing them as less reliable, less reputable, and less trustworthy. This is a common dynamic in transition countries generally; it may be somewhat stronger in Moldova because the country’s SME sector has been somewhat slower to develop. It is also true that many laws and regulations seem to be drafted with large businesses in mind, and often may be difficult for SMEs to comply with.

Ethnic and gender issues. Finally, ethnic and gender issues can be relevant in some cases. Female entrepreneurs regularly state that government agencies do not take them seriously, especially when starting a business. It occasionally happens that a female registrant may be asked to provide her husband’s information, even though this is not a formal requirement.

As to ethnic issues, the civil service is largely Romanian-speaking today, while the business communities in Chisinau and Balti include large numbers of Russian speakers. While Moldova is formally bilingual, Russian speakers sometimes complain that their language is not supported (i.e., an application form is only in Romanian), while Romanian speakers regularly complain that Russian-speakers refuse to speak Romanian. Any reform program dealing with the business community should take these factors into account.

F. RECOMMENDATIONS

As mentioned earlier, the process of registering a business in Moldova is relatively simple and not a barrier to entry into the market. Most respondents instead stressed the problems of making their businesses fully operational, as well as closing and liquidating the business should it become necessary. The recommendations that follow, therefore, focus more on streamlining the registration process further, and eliminating costly and unnecessary burdens to operating and closing a business.

- *Eliminate the requirement to visit the STI to apply for and receive a Fiscal Code.* The SRC issues an identical code to companies upon registration and already provides it to the STI. This would have the effect of immediately eliminating one step in the official process and improving Moldova’s ranking and would only require a minor modification to the Tax Code.

- *Implement an E-Reporting system in which one report can be filed for use by several different authorities* (e.g. for STI, National Insurance Fund, National Health Insurance Company and Bureau of Statistics). Similarly, greater connectivity and interoperability is needed among government agencies to share information and minimize duplicate reporting.
- *Encourage municipal authorities to connect to the E-Government Center.* The Center is developing an electronic platform for Electronic Registries that could also serve One Stop Shops at the municipal level. Mayoralties should first coordinate and centralize the approval and issuance process among their various agencies, e.g. for commercial and construction permits. Those presenting functional models could receive assistance to connect to the E-Government platform.
- *Simplify and accelerate the procedure for obtaining residence permits for foreign companies investing and operating in Moldova.* Concurrently, study the issue of whether easing the requirements for work and residence permits would adversely affect local professionals who are also seeking employment. There is an acute shortage of qualified labor in Moldova that has already deterred some investors. Investments in education and vocational skills are likely to yield more desirable results.
- *Consider having the Registration Chamber play a role in the business-liquidating process, as it does in the registration process.* The SRC could act as a One-Stop-Shop not only for registration but for liquidating a business as well if properly connected to other relevant agencies. A liquidation process could be registered there once, thus providing formal notice to the STI and creditors. This should be preceded by a review of procedures of the liquidation process to determine their utility and the merits of retaining each.
- *More agencies should adopt the E-Government Platform being developed by the E-Government Center.* This will allow for easier exchange of information and reduce the number and complexity of reports. Security safeguards have been built into the system so that confidential information supplied to one authority (e.g. the STI) will not be shared with other agencies which are not entitled to that information.
- *Review government agency websites for usefulness, in particular for providing application and compliance information, lists of procedures for applicants, and downloadable application forms.* While not a major problem identified by local businesses, access to useful and complete information from state bodies can save considerable time and money when establishing and operating a business. Similarly, a central location on the E-Government Portal where all business-related information from various government agencies would be available may prove easier and more cost-effective.
- *Ensure that new businesses are informed of their rights and responsibilities.* The State Registration Chamber could inform new registrants of what steps are and are not required beyond the registration process. This could avoid unnecessary steps, such as registering at other state agencies that is no longer required. This should be fairly simple and straightforward and not require major cost or effort on the part of the SRC.

SECTION V. PROTECTING INVESTORS

A. INTRODUCTION

When groups of parties unite to invest, they usually seek to use a “corporate” or “company” form of business, for a variety of reasons. Corporate entities provide legal protections, including limited liability, centralized management, an ability to assert legal rights, and improved access to credit. Moldova offers a variety of forms of business through which investors may seek to conduct their business, which are briefly described in the previous Chapter on “Starting a Business.” Because the Joint Stock Company (JSC) is the form that allows an unlimited number of shareholders to invest, it will be the primary focus of this chapter.

Protecting Investors (BizCLIR Rankings)	
<u>Framework Areas:</u>	<u>Score</u>
Legal Framework	3
Implementing Institutions	2
Supporting Institutions	3
Social Dynamic	2

A1. “Protecting Investors” Indicator

The “Protecting Investors” indicator of the World Bank’s annual Doing Business survey focuses on the extent to which a country’s laws and institutions protect the interests of minority shareholders. Scoring for the indicator is based on the average of three indices:

- The Extent of Disclosure Index assesses the obligations of company management and majority shareholders to make available to minority shareholders information about related-party transactions that create the risk of financial favoritism.
- The Extent of Director Liability Index tests the degree to which controlling interests in a company can be held liable to minority shareholders for losses caused by related-party transactions that unfairly benefit the majority.
- The Ease of Shareholder Suits Index measures the degree to which minority shareholders have access to company information to make their case in court against controlling interests that have approved related-party transactions.

The focus on protecting minority shareholders is intended to increase the opportunities for investment in an economy like Moldova’s. Where few such protections are available, new investments will be limited to those where the investor can take a controlling interest. This reduces the total amount of investment in Moldova, and deprives the economy of the benefits of increased funds, access to innovation, and trading opportunities, both domestic and foreign, that minority interests could provide. As shown in Table V-I, below,⁶⁸ Moldova’s foreign investors

⁶⁸ V.Prohntichi, et al, “Impact of Foreign Direct Investment on Moldovan Economy, Expert-Grup Independent Analytical Center, Chisinau 2010, page 14. The calculations are based on National Bureau of Statistics data from 2008. The report is available online at http://undp.md/presscentre/2010/Statistics_27JULY/iis_eng_www.pdf. More than 90 percent of about 8,000 companies with foreign investment are limited liability companies (LLCs), according to the State Registration Chamber. LLCs make up about 49 percent of the total number of legal entities registered in Moldova, with joint stock companies making an additional three percent.

Table V-1. Distribution of Foreign Investment in Moldova

	Up to 25%	26-50%	51-75%	76-100%	Total by row, %
Distribution of total among of foreign capital on groups	.4	14.8	8.5	76.3	100
Distribution of total number of companies with foreign capital on groups	9.8	18.6	12.7	58.9	100

dramatically prefer to invest in controlling interests, with only 15.2 percent investing in interests of 50 percent or less.

The logic of these investor choices, based on National Bureau of Statistics data from 2008, is confirmed by Moldova’s historically poor ranking on the “Protecting Investors” indicator. Moldova ranked 105th of 181 economies surveyed on the Doing Business 2007 survey. That rank fell to 114th on the 2012 report, as other economies’ reforms were recognized by World Bank surveyors. On the newly released Doing Business in 2013 report, however, recent reforms to the legal framework have been partly recognized by the World Bank, raising Moldova’s rank to 82nd, an increase of 32 places.

B. LEGAL FRAMEWORK

Moldovan investors and the professionals who serve them describe the country’s legal framework as adequate to good, and getting better. In most cases, the text of applicable laws and regulations are freely available in Romanian and Russian, although rarely in English, the international language of business and investment.⁶⁹ Stakeholders are virtually unanimous, including many if not most regulators, that implementation is sorely lacking. The Social Dynamics section of this chapter discusses factors that interfere with implementation related to the *political will* to develop and implement a legal environment that encourages investment, business growth, and job creation. This section addresses several issues related to the *ability and capacity* of Moldova to implement. These issues include:

- The increasing complexity of Moldova’s legal system;
- Conflicts between new and old sources of law; and,
- Gaps in the consultative processes between public and private sectors.

⁶⁹ An online database of Moldovan laws and regulations in Romanian and Russian is available at <http://lex.justice.md>. Some English translations are available at <http://www.lexadin.nl/wlg/legis/nofr/oeur/lxwemol.htm>.

Table V-2. Key Laws and Regulations

List of Key Laws

- Law on Capital Market, No. 171 from July 11, 2011 (to take effect on September 14, 2013)
- Contraventions Code of the Republic of Moldova, No. 218-XVI from October 24, 2008
- Law on Investments in Entrepreneurial Activity, No. 81-XV from March 18, 2004
- Civil Procedure Code of the Republic of Moldova, No. 225-XV from May 30, 2003
- Civil Code of the Republic of Moldova, No. 1107-XV from June 6, 2002
- Criminal Code of the Republic of Moldova, No. 985-XV from April 18, 2002
- Law on Securities Market, No. 199-XIV from November 18, 1998 (to be abolished on September 14, 2013, when new Law on Capital Market takes effect)
- Law on National Commission of Financial Market, No. 192-XIV from November 12, 1998
- Law on Joint Stock Companies, No. 1134-XIII from April 2, 1997
- Law on Investment Funds, No. 1204-XIII from June 5, 1997 (to be abolished on September 14, 2013, when new Law on Capital Market takes effect)

List of Key Regulations

- Instruction on the state registration of securities, Resolution of the National Commission of Financial Market No. 9/9 from March 1, 2012
- Instruction on the content, manner of preparation, presentation and publication of the annual statement on the securities by the joint stock company, No. 18/10 from May 14, 2010
- Instruction on public offer on the secondary market, No. 64/4 from December 31, 2008
- Corporate Governance Code (model), Resolution of the National Commission of Financial Market No. 28/6 from June 1, 2007
- Regulation on the manner of keeping the register of holders of securities by the registrar and the nominal holder, No. 15/1 from March 16, 2007

Increasing complexity. Moldova shares a border and a common language with Romania, which joined the EU on January 1, 2007. This proximity is a significant advantage to Moldova in developing a stronger legal framework that harmonizes with EU legislation. EU directives and their Romanian legislative implementations are already available in Moldova's national language, providing ready models for adaptation. Unfortunately, stakeholders say, Moldova too often "adopts" rather than "adapts" Romania's EU-compliant legislation. This is making Moldova's legal framework increasingly complex, they say, challenging the ability of Moldovan practitioners to understand, draft, and enforce appropriate implementing regulations. In some cases, practitioners say, EU-based legislation imposes compliance obligations that are appropriate in a sophisticated financial market, but that may not be appropriate for a smaller, less-developed economy. Among the approaches that might be useful in addressing these issues are:

- Moldova might benefit from looking at the incremental approach the Republic of Georgia has taken to harmonizing its legal framework with the EU. Georgia has focused first on streamlining and simplifying its regulatory requirements to bring them in-line with the needs of its economy, and then on developing the capacity of its regulators to enforce and of its businesses to comply. As Georgia's economy grows more sophisticated and regulatory capacity increases, its regulatory regimes follow.
- Alternatively, Moldova should explore whether the transition mechanisms used by other formerly socialist states that are now successful members of the EU can be adapted to assist Moldova in harmonizing its legal framework with the EU. A challenge is the absence of the sometimes massive donor implementation programs that helped new EU member states like Romania through the harmonization process.
- Moldova's harmonization efforts would benefit from increased support from EU countries and international donors not only in drafting new laws, but also in developing the necessary implementing regulations.
- Both regulators and the regulated, as well as members of the judiciary, require additional training and support in enforcing and complying with the new norms.

Conflicts between sources of law. As Moldova relies increasingly on EU models for its legal framework, conflicts develop with earlier sources of law, including remnants of Soviet law and a more recent Russian overlay. For example, the Law on Securities Markets drew very heavily on Russian legislation, the Law on Joint Stock Companies is a combination of Russian law and a unique Moldovan overlay, and the new Law on Capital Markets is based on EU/Romanian law. The result is a set of legal concepts, some novel for Moldovan practitioners, that use the same words for different things, or that introduce legislative disconnects. An example of the first problem is the different understandings of the legal concept of "insider" embedded in the Russian-based laws and the European conception in the new Law on Capital Markets. Competing definitions hamper development and enforcement of norms like protections for minority shareholders against "insider" self-dealing.

Moldova's new Law on Capital Markets will take effect in September 2013. The advent of the new law illustrates the challenges facing Moldovan implementers, as well as the opportunities for donors to make significant contributions to improving the legal framework and business environment. The distinction between "open" and "closed" companies in the JSC Law doesn't align with the "public/private" dichotomy envisioned by the new Law on Capital Markets. Getting the distinction right becomes especially important now because the new Capital Markets Law excuses "private" companies from complying with onerous disclosure requirements for "public" companies. To make the new relief consistently and comprehensively available to the many Moldovan JSCs with a handful of shareholders requires that the two laws be reconciled, and appropriate secondary regulations implemented.

Gaps in consultative process between public and private sectors. Moldova excels in some aspects of ensuring that private sector and investor representatives have an opportunity to comment on proposed laws and regulations. In particular, stakeholders noted that both the Government and Parliament regularly post draft legislation online, and generally do a

commendable job of keeping the public informed of proposed amendments along the way to enactment. In addition, Moldovan law requires that all new legislation that affects business be accompanied by a regulatory impact assessment (RIA) that details the costs and benefits of the proposed new changes. The RIA and the draft legislation must be submitted for review to the RIA Working Group, which has equal numbers of public and private sector representatives. Business associations note great appreciation for the review process and for the work done by the Working Group Secretariat, funded by the World Bank, in reviewing the RIAs. Association representatives note that, while the RIAs submitted by government proponents of new laws, and regulations are often inadequate, the review process creates valuable opportunities for the private sector to voice objections and recommendations. They say that their input is heard, it does make a difference, and that the outcome of the Working Group consultative process is often more effective laws and regulations. However, both public- and private-sector participants note several weaknesses that should be addressed:

- *Financial sector legislation is exempt from RIA Working Group review.* Financial sector stakeholders note that weak drafting capacity at the non-bank financial regulator, the National Commission for Financial Markets, sometimes results in substandard implementing regulations. They suggest that RIA Working Group review could help eliminate legislative gaps, inconsistencies with other laws, and reduce compliance costs. They recommend that the financial sector exemption be removed, at least as to legislation originating with or affecting operations of the Commission. It is noteworthy that the Government itself recognizes the value of the RIA review process and sometimes requires the Commission to submit proposed legislation for review, even though it is not a legal requirement. One prominent Moldovan attorney with substantial experience in the country’s financial markets cited as an example RIA Working Group review of the new Law on Capital Markets, noting that the regulatory impact assessment accompanying the draft law, even though not legally required, was among the strongest he has seen.

- *New laws and regulations sometimes evade RIA Working Group review.* Private sector stakeholders note that they are sometimes caught by surprise when measures with significant impact on business costs and operations suddenly appear with no prior notice or discussion. Sources of surprise include government agencies that act without RIA Working Group review on the excuse that the measures proposed don’t impact the business environment; last-minute Parliamentary amendments like one recent proposal to allow minority shareholders representing at least 10

Does Moldova need poor, transitional laws?

Georgia is a poor, transitional country with no capacity to do anything. What we need most at this stage of our development are poor, transitional laws that are always just enough better than what we have to keep us moving forward.

-- *Kakha Bendukidze, former Minister of Economy and State Minister of Reforms Coordination, Republic of Georgia*

percent of shares to require companies to issue dividends of 25 percent of profits; and a constant stream of unpublished directives from the Customs Service that change procedures and affect the costs of Moldovan traders with no advance notice. Addressing these issues requires clearer definitions of what types of legislation is required to undergo

RIA Working Group review, and blunt sanctions for non-compliance, including invalidation of new laws and regulations adopted without review.

- *RIA requirement is sometimes a heavy burden for government agencies.* Stakeholders say that requiring government agencies to submit regulatory impact assessments with all proposed laws and regulations is a heavy burden. These assessments often challenge their technical capacity as well as divert scarce resources from other functions. The RIA burden felt by government agencies sometimes results in avoidance of the RIA review process, and often produces what stakeholders describe as poor assessments that are rejected by the Working Group, producing more delay and greater burdens on the Government. Measures that might be taken to relieve the burdens on government include:
 - Specialized teams of RIA writers could be established within each Ministry to serve all of its departments and agencies.
 - Moldova could develop mandatory guidelines for legislative drafting that include “best practice” principles from international development experience that reduce the costs and burdens of enforcement and compliance. For example, proponents of new legislation might be required to demonstrate that the Government actually has the capacity to enforce any new requirements. Another principle that would consistently reduce the compliance costs on business is to prohibit any agency from requiring a citizen or business to supply information already in the hands of another government agency. Moldova’s rapidly improving information management systems, promoted by the E-Governance Center, can play an important role in making sure each agency knows what all others do. This coordination will simultaneously reduce compliance burdens on businesses and dramatically improve government control over regulated activities.
 - Involving the private sector earlier in the drafting process could reduce RIA compliance burdens on the Government. It sometimes happens that government officials expend much time and energy in drafting new legislation, and then run into unexpected opposition at the RIA Working Group stage. Earlier engagement with the private sector can introduce greater appreciation of how new compliance burdens will increase costs, more options for obtaining the desired results at lower costs to business, and greater consensus about the need for new legislation. For greater dialogue earlier to benefit society at large, however, business has to learn to discipline itself. Engagement brings the obligation for business representatives to represent the sector, not engage in special pleading, and to come with concrete solutions to sectoral problems, not just complaints about specific problems of specific companies. Donor engagement in the dialogue can help the public and private sectors converse in ways that increase social utility and consensus, not just private benefit.

Going forward, stakeholders say that the priority legal framework issue is to develop a proper base for enforcing two new and closely-related laws: the amended Law on Joint Stock Companies (JSC), which is already in force, and the Law on Capital Markets, which will take effect in September 2013. As described in discussion of the “Protecting Investors” indicator, the JSC Law adds important new protections for minority investors. The amendments increase

disclosure, liability of controlling shareholders who benefit from self-dealing, and access to the courts. Unfortunately, the prior rights of shareholders haven't been well-enforced, either by the Commission or in the courts. Stakeholders report instances of minority shareholders both being abused and being abusive to extort advantages from majority shareholders. These shortcomings will be discussed hereafter in the discussion of "Implementing Institutions." The new Law on Capital Markets will introduce a number of important advantages for investors:

- The law introduces "squeeze-out" provisions that enable controlling shareholders to force minority shareholders holding 10 percent or less to sell their shares for a fair price determined by neutral price mechanisms. This provision is balanced by a "reverse squeeze-out" provision that empowers minority shareholders to require majority shareholders to buy them out. The two provisions, in concert, protect both minority and majority shareholders, and provide a fair pricing mechanism to allow consolidation of control that will reduce the administrative costs of multiple shareholders. Stakeholders note that while it is appropriate for the law to provide such treatment in the case of public companies, it should be an issue subject to negotiation among shareholders in closed companies and governed by the terms of shareholder agreements.
- The law also introduces a distinction between "public" and "private" companies. "Private" companies are relieved from onerous disclosure requirements that are only necessary to protect the interests of companies with many small shareholders, including formerly state-owned enterprises that were privatized using voucher privatization that distributed shares to Moldova's citizens.
- Moldova's JSCs are also relieved of a number of burdensome requirements associated with mandatory listing and trading on the Moldova Stock Exchange. When the Law on Capital Markets takes effect, listing will be entirely voluntary, and shareholders may buy and sell in direct agreements between themselves, without the previously enforced intermediation of licensed brokers who were required to route all transactions through the stock exchange.

For Moldovan JSCs and their shareholders to actually reap the benefits of the new Law on Capital Markets, a number of steps are required:

- Discrepancies between the EU-based Law on Capital Markets and the more Russian-based JSC Law need to be resolved by amending the JSC Law.
- Sound implementing regulations need to be drafted.
- Capacity building for Commission enforcement personnel and judges is key, and financial market participants need training.

C. IMPLEMENTING ORGANIZATIONS

The two primary implementing institutions upon which investors depend to create and enforce fair and transparent market regulations are the National Commission on Financial Markets and the Moldovan judiciary. Neither institution is viewed by stakeholders as performing their

functions at an acceptable level. Key shortcomings identified in the work of the Commission include the following:

- In some cases, senior leadership is politically connected with no obvious technical qualifications to serve in a policy-making role for a non-banking financial institution regulator. In other cases, political interests are alleged to determine policy priorities. Both problems reflect a general tendency to tie government bodies too closely with particular political parties as discussed elsewhere in this report. The adverse effects of overly political leadership contribute to the other shortcomings discussed below.
- The Commission’s monitoring and enforcement activities are not properly focused. Market participants report that routine sales of shares are subject to sometimes excruciating oversight, while complaints of minority shareholders are mostly ignored. Where the Commission does intervene, too often it is in support of politically connected minority shareholders who use the intervention to leverage unfair concessions from controlling interests.
- Insufficient attention has been devoted to helping Moldovan companies comply with the model Corporate Governance Code since its adoption in 2007. Training of corporate directors, promulgation of model templates and procedures, and enforcement of the Code for companies that adopt it, could help Moldovan JSCs improve their credit-worthiness and their attractiveness to investors.
- The Commission has failed to develop a system for publishing the financial information of public companies so that minority shareholders and potential investors have timely access to adequate material information.
- Technical-level employees are viewed as bright and capable of growing into their positions. However, as Moldova’s legal foundations evolve from a Soviet-Russian orientation to EU financial market models, Commission staff are not being provided with adequate opportunities to upgrade their skills and apply them to increasingly more complex enforcement duties. The number of former Commission employees who have assumed other roles in the financial sector suggests that more investment needs to be made in preparing and retaining technical staff.
- The secondary legislation generated by the Commission is not highly regarded. The reasons for the poor quality include the unqualified senior leadership and the need for technical-level staff to develop capacity and skills as Moldova’s legal foundations evolve. The Commission’s exemption from RIA Working Group review, discussed above, removes a valuable source of knowledgeable stakeholder input. The Commission has its own Expert Working Group of outside financial market professionals that could also provide direct input during the drafting process. However, members report their

**The Business of Judicial
Decision-Making**

“Moldova’s courts operate on business principles: They sell their services.”

—*Financial markets participant*

engagement is mostly pro forma, consisting primarily of semi-annual notices summarizing what the Commission has done, rather than regular involvement in what the Commission is doing. Another factor contributing to poor secondary legislation, stakeholders say, is that all Commission regulations must be registered with the Ministry of Finance. The Ministry reviewers, they say, sometimes require changes that demonstrate a lack of understanding of how financial markets work.

Moldova's courts have the dubious distinction of receiving the lowest level of public approval – 35 percent – of any of the country's institutions except police authorities (34 percent) and political parties (29 percent).⁷⁰ Stakeholders interviewed, both public and private, bemoaned what they described as the judicial system's persistent, pervasive corruption. Ironically, judicial impunity results from reforms intended to protect judges from political pressure, including life-time appointment and no outside oversight. Judges are responsible only to a judicial council made up of judges. Unfortunately, the reforms failed to ensure that the members of an institution critical to a functioning, market-based economy received a living wage, much less compensation appropriate to their critical role in good governance.

The problems created by insulation of Moldova's judiciary from being held accountable, a characteristic of common-law jurisdictions where the principle of controlling precedents decided by higher courts helps to enforce basic norms, is aggravated by the fact that Moldova is a civil law jurisdiction where judicial decisions are not controlled by precedent. Stakeholders report that judicial decisions are completely unpredictable, unconstrained by the language of laws and regulations. A particular problem for financial market participants is the apparent participation of some judges – along with prosecutors – in scripted schemes to steal companies from their rightful owners. In one illustrative case, company managers were jailed, and the judge stripped majority shareholders of their voting rights with remarkable speed. This decision enabled minority raiders to gain majority control. The issue of judges suspending the voting rights of majority shareholders is described as recurring, and a proposal is pending to forbid judges from exercising this power. When courts are not acting so swiftly that one side is disadvantaged, they can be subject to prolonged delay. A problem less important than corruption is that judges are expected to enforce laws with conflicting legal norms and adapt to new laws that increasingly rely on EU-based legal concepts with which they are unfamiliar, with little opportunity for learning about the new norms and how to enforce them.

Stakeholder recommendations for improving the quality of judicial decision-making fall into three broad categories:

- **Increased accountability:** Suggestions include eliminating judicial immunity, requiring periodic retention hearings before Parliament at which stakeholders would have an opportunity to comment on a judge's prior performance, and broadening representation at the judicial council that sanctions errant judges, perhaps including government, Parliament and private-sector representatives. A related measure is introducing automated

⁷⁰ The approval data comes from a poll conducted in August-September 2011 by the International Republican Institute, available at http://www.iri.org/sites/default/files/flip_docs/Moldova%20national%20voters%20survey%202010-09/HTML/index.html#/2/zoomed.

case management software and standards for case management that would increase transparency and eliminate some opportunities for corruption.

- **More judicial training opportunities.** Mandatory training could help improve judicial skills. Some stakeholders recommend joint trainings with Commission members.
- **Strengthen alternatives to judicial resolution.** Stakeholders note that one area in which the judiciary acts reliably is enforcement of awards rendered by various alternative dispute resolution (ADR) mechanisms. Foreign investors generally include in their contracts with Moldovan counter-parties language requiring that disputes be resolved by arbitration, specifying the law to be applied and the forum in which the dispute will be adjudicated. Stakeholders suggested that, given the current dysfunction of the judicial system, donor investment in improving the ADR options available within Moldova would be welcomed by market participants. Suggestions included technical assistance to develop approved lists of trained arbitrators, model contract language, and awareness-raising for market participants of the value of ADR.

D. SUPPORTING INSTITUTIONS

This section discusses three categories of supporting institutions that support investment in Moldova – financial markets organizations, government agencies tasked with promoting investment and supporting investors, and Moldovan business organizations that cater to the needs of investors.

Financial markets organizations. The Moldova Stock Exchange has traditionally been more of a burden than a benefit to financial intermediation. The Exchange is privately owned, with commercial banks holding the largest shares. All

JSCs are forced to list and pay listing fees, although none of those listed have significant float. The Exchange has not been used to launch IPOs or corporate or municipal bonds. All sales of shares in listed companies must go through the exchange, using licensed brokers, no matter how small the transactions at issue. Stakeholders described the Exchange software as antiquated with high security risks. Sales of shares, which take at least seven business days to complete, sometimes have been hijacked on their way to completion, with a surprise buyer ending up owning shares the seller had agreed to convey to someone else. Similar concerns about the security of share ownership records maintained by the private, independent registries were also reported. Market participants expressed concerns that shares are at risk of theft or that failure of poor information systems could cause the loss of ownership records.

Moldova’s new Law on Capital Markets, which will take effect in September 2013, and the emergence of a new exchange – the Chisinau Stock Exchange – will dramatically change the current situation. The new law makes listing voluntary, and eliminates the requirement, added in 2008 for JSCs created thereafter, that sales of shares must be funneled through an exchange

Supporting Institutions
<ul style="list-style-type: none">• Moldova Stock Exchange• Chisinau Stock Exchange• Independent share registries• Investment firms• Moldovan Investment and Export Promotion Organization of the Ministry of Economy• Prime Minister’s Office for Attracting Investors• Moldovan Chamber of Commerce & Industry• Foreign Investors Association• European Business Association• American Chamber of Commerce in Moldova

using licensed brokers. Companies that do list on an exchange must have “significant” public float for secondary trading. However, what percent of float is “significant” must be further defined by the National Commission on Financial Markets. The Chisinau Stock Exchange, which has the Bucharest Stock Exchange as one of its founders, is scheduled to open in late 2012. The new exchange plans to list Moldovan companies who choose to be listed and cross-list companies on the Bucharest Stock Exchange, providing Moldovan citizens with an opportunity to invest in equities. Chisinau Stock Exchange officials say they will be using sophisticated technology that meets EU standards to increase transparency, and reduce transaction costs and delays.

While Moldova’s financial markets have not played a useful role in providing access to capital for business growth in the past, the new law and introduction of competition between exchanges may offer an important opportunity. Participants in a BRITE project workshop on the preliminary findings in this chapter recommended as a high-priority intervention support for pilot projects to help market participants use the new environment to introduce initial public offerings and municipal and corporate bonds.

Investment promotion and support agencies. Investment promotion is an arduous task in Moldova today. Simply put, the country is not an attractive value proposition for investors given the pervasive rent-seeking and high levels of regulatory inefficiency. It is unclear why Moldova needs two different agencies charged with the same task – the Moldovan Investment and Export Promotion Organization (MIEPO) under the Minister of Economy, and a new Prime Minister’s Office for Attracting Investors (OAI). The fact that the Prime Minister and Minister of Economy are from different political parties creates the risk that rival organizations will serve political interests rather than those of investors. MIEPO is an established organization that has received donor support in the past, although it is not now receiving any. Its website has useful information and tools, including a database of investment sites. The website could use a facelift and more frequent updating.

OAI is a new institution supported by the German development organization GIZ. It is in the process of expanding personnel, and expects to develop the capacity to carry out the same core functions that any mature investment promotion agency (IPA) undertakes. MIEPO has already been organized to carry out the same core functions. Currently, OAI reports that most of its work is intervening on behalf of businesses with the government. Business associations report that their members who go to OAI often get satisfaction. This is both not surprising and disturbing. It is not surprising that an agency affiliated with the Prime Minister’s office would be a successful advocate for business because the biggest subjects of complaint are customs first and then tax, both also allocated to the same political party. This success, however, underlines the problematic environment for investors. Ordinary businesses have to pay unofficial fees to lubricate opaque regulatory processes. Big businesses can go directly to the Prime Minister’s OAI for relief.

Efficient economies don’t tolerate either approach. These countries streamline and automate their regulatory processes so that all citizens and businesses receive efficient service. Moldova could be better served by devoting its resources to creating one world-class IPA that is more beholden to its business/investor clients than to any government official. International experience has shown that successful IPAs have advocacy for improvements to the business environment as a

core function. Both MIEPO and OAI say they carry out this function. Vigorous advocacy, however, seems unlikely in agencies so directly subordinate to senior officials. Moldova may want to consider IPA governance similar to that of the RIA Working Group, with equal public and private sector representation. A strong IPA should also be engaged in the work of the RIA Working Group. As World Bank funding of the RIA Secretariat draws to a close, a case might be made for locating the Working Group Secretariat within a reconstituted, more independent IPA.

Business associations and their advocacy for growth. Like their counterparts at MIEPO and OAI, officials at the business associations who represent investors in the Moldovan economy are personally impressive. They are young, aggressive advocates for reform, able to discuss in-depth the problems faced by their members, with the technical versatility to describe what needs to be done. Their accounts of the key problems facing Moldova are virtually identical:

- New foreign investors are not coming to Moldova, and have not come for several years.
- Some established investors, who came in the early days of independence and privatization, understand the environment and enjoy the political clout to protect themselves. Their presence and investment is expanding in Moldova.
- The biggest factor keeping investors away is chaos and corruption in customs.
- Tax administration is consistently inconsistent in applying tax legislation and subjects businesses to egregiously long delays before VAT refunds are issued.
- The judicial system is unreliable and unpredictable, a combination of simple corruptions and ignorance of new legal concepts and norms imported from the EU.
- Getting visas for foreign personnel to work in Moldova is extremely difficult because officials substitute their judgment for investors on the issue of whether Moldovan talent is available to manage the investors' affairs. This mentality fails to accept the economic likelihood that businesses will do their best to minimize costs, hiring Moldovans whenever they can. It is also short-sighted because foreign workers will increase the capacity of Moldovan workers and replace themselves at their earliest opportunity.

The four business associations interviewed for this chapter engage with MIEPO and OAI, and with each other in a variety of useful ways that support a developing infrastructure to advocate for an enabling business environment. All advocate fiercely with the Government on behalf of members with specific needs. The Director of the Foreign Investors Association (FIA) is deputy chair of the RIA Working Group, and FIA vigorously polices legislation that sneaks around the process. The Moldovan Chamber of Commerce & Industry is also a member of the RIA Working Group. It has largely weaned itself from dependency on forced fees from businesses for unnecessary services. This model, still used by the Moldova Stock Exchange, as discussed above, is a characteristic of Chambers in many developing countries. Moldova's CCI, however, has developed into a valued development partner for donors. The American Chamber of Commerce in Moldova has an active group of committees that monitor and work to improve areas such as customs, tax, and the legal environment. The European Business Association, still

relatively new, is already making its mark, polling members to identify problems in the business environment and forcefully presenting results to the government.

Collectively, these associations have overlapping members, skills, and interests. Each and all will be strong development partners. Initiatives that promote collaboration to harness their combined memberships and skills could leverage their strength. For example, business associations in Georgia collaborated on two public-private task forces, one on customs and one on tax. Association and USAID specialists met with members to inventory all of their complaints in each area. Specific complaints were traced back to the problems of law and practice that caused them, and then best-practice solutions were proposed. Association leadership then sat down with tax and customs leadership to present problems and proposed solutions. Georgia's government loved the approach, because they didn't get bogged down with individual complaints and special pleading, but had clearly identified problems and solutions. Literally hundreds of positive changes in both tax and customs law and practice resulted, and the model is easily applied to Moldova as it stands poised for meaningful reform.

E. SOCIAL DYNAMICS

Sandwiched between Romania, a European Union member, and Ukraine, a gateway to Commonwealth of Independent States, with trading access to both markets, a highly literate, low-cost labor force, and, rich, fertile soils, Moldova should be a highly attractive investment destination. Yet, Moldova has historically lagged behind other East European countries in attracting and keeping foreign direct investment, despite key advantages.

Each of the chapters of this assessment has identified as a key problem the disconnect between the law as written and as implemented. Repeatedly, the motive for failure to observe and implement sometimes good laws is increasing the opportunities for revenue, both official and unofficial. The latter issue is particularly acute and disruptive to the goal of increasing regulatory efficiency. In almost every area explored by members of the assessment team that produced this report, we encountered a range of sometimes inventive and sometimes mundane efforts to thwart legal mandates by underpaid civil servants attempting to increase their incomes. These efforts include simple bribes, the proliferation of regulator-owned companies free from civil service pay scales that require fees for services that may or may not be necessary, and egregious conflicts of interest allowing regulators to provide regulated services. It is probably neither fair nor useful to call such practices corrupt when they are so necessary and so widespread. When civil servants, administrative and professional, are not paid enough to live a decent life in almost any area of government, it may be more properly characterized as social policy than as corruption.

A Georgian Remembers Corrupt Society

I remember just 8-10 years ago, when the whole Georgian government system was deeply sinking in the swamp of corruption and the whole society was hopeless. We believed then that our corrupt life-style was a genetically determined part of who we were, growing out of our history and culture. Looking back now, I realize that this was a very naive and improper judgment. Today, when Transparency International reports that only three percent of Georgians paid a bribe in the last twelve months, I can recognize that eliminating corruption is just a matter of willingness, taking responsibility, and exercising proper management.

*-- Aleksi Aleksishvili, former Georgian
Minister of Economic Development and
Minister of Finance*

Simple analysis and recent historical precedent like that provided in the chapters on “Trading Across Borders” and “Dealing with Construction Permits” allow us to project the normal prosperous state that Moldova could become. Given its underlying attractiveness as an investment destination, economic growth would follow if it could make the transition from a country where the law is bent and broken to one where the rule of law is respected.

F. RECOMMENDATIONS

The recommendations that follow are a combination of measures suggested by stakeholders and by assessment team members. These solutions were vetted with financial markets representatives who attended a briefing on the preliminary findings of this chapter, and are organized by priority as agreed upon by presenters and attendees.

- *Amend the Law on Joint Stock Companies:* As discussed earlier, Moldova’s Law on Joint Stock Companies contains legal concepts drawn from Russia with a uniquely Moldovan overlay. For Moldova’s new Law on Capital Markets, which becomes effective in September 2013, to work well, the JSC law needs to be revised to incorporate the same EU-based legal concepts and norms that underlie the capital markets law. Particular attention should be paid to the following issues:
 - The JSC Law should reflect the EU-based distinction between “public” and “private” companies instead of its current regulation which treats all companies as “public.”
 - The law needs to incorporate more balanced treatment of minority and majority shareholders to ensure that the rights of each class are protected fairly, and that their respective rights are adequately protected against abuse by the other.
 - The law should impose on the National Commission of Financial Market a stronger, clearer duty to investigate complaints that shareholder rights have been violated, and to intervene where necessary.
- *Implement the new Law on Capital Markets:* Aggressive support to financial markets participants is required for successful implementation of this law before it takes effect in September 2013, including:
 - The Commission, whether it wants it or not, needs technical assistance in developing the relevant secondary regulations. Support could come from a variety of sources, including donors, the Commission’s own Council of Experts, or the RIA Working Group review. Eliminating Ministry of Justice review and registration is likely to produce higher-quality regulations.
 - A number of measures are needed to prepare financial market participants for practice under the new law, including preparation of a commentary to inform compliance and enforcement, and training for regulators, the regulated, and the judiciary.
- *Publish financials of public companies:* An information infrastructure needs to be put in place to give shareholders and potential market investors timely access to adequate

information about public companies. Moldova's E-Governance Center can provide support in developing online solutions. Similar donor initiatives in other countries should be reviewed for products that might be usefully adapted. For example, USAID's West Bank/Gaza Capital Markets Development Initiatives project developed a "Unified Financial Reporting System" that provided a standard format for listed companies that complied with International Financial Reporting Standards and provided a wide variety of financial ratios to help investors make informed decisions.

- *Pilot new financial instruments:* The priority interventions described above, together with the new Capital Markets Law and the introduction of competitive stock exchanges, create opportunities to pilot new financial instruments that can help increase access to finance for Moldovan companies and municipalities. Stakeholders report that current capacity to develop initial public offerings and corporate and municipal bond offerings is limited. A targeted pilot program could help build capacity and develop model municipal regulations, templates, and materials that stakeholders can use as models for other offerings.
- *Review tax treatment of transactions in securities:* Stakeholders suggest a comprehensive review of the tax treatment of securities transactions, including withholding tax and income tax. Stakeholders want to explore Georgia's approach in abolishing all capital market taxes and whether that would encourage growth of the sector. Additionally, they report that the current withholding tax on securities transactions for every individual participating in the financial markets inhibits the growth of vehicles for collective investment.
- *Build capacity of market participants:* To leverage the new opportunities provided by Moldova's increasingly sophisticated financial markets, participants need to build their capacity on a variety of fronts. Stakeholder priorities for training and standardized materials include promoting the advantages for companies to adopt and comply with the model Corporate Governance Code, and equipping them to make the transition with trainings in good corporate governance and investor rights. Training and materials are also needed for investment firms to improve their capacity to manage investments. Stakeholders also suggested drafting handbooks on various subjects, including corporate governance and financial instruments.
- *Implement international standards on valuation of securities:* The new Law on Capital Markets introduces international standards for valuation of securities. These standards are particularly important for implementation of the "squeeze-out" and "reverse squeeze-out" provisions that govern majority shareholder buy-outs of minority shareholders. Stakeholders worry that without careful preparation, the new provisions could lead to new ways to abuse shareholders. Support is needed to train participants, develop the capacity of appraisers, and introduce appropriate regulations.
- *Improve the financial education of investors:* Financial market education is one of the most important regulatory objectives of the new Law on Capital Markets. The Law tasks the National Commission of Financial Market with contributing to better financial education of Moldovan savers and investors. It is well known that the remittances to

Moldova are spent mainly on current consumption and unproductive household assets. Education and awareness raising in this area would improve the financial knowledge of Moldovans, and improve the position of retail investors with financial intermediaries and investment instruments, and help redirect funds from consumption to investments.

- *Amend the legal framework:* A variety of legal framework changes are required, including:
 - Further engage the EU, EU countries, and international donors in supporting ongoing harmonization of Moldovan legislation with EU Directives;
 - Eliminate the exemption from RIA Working Group review for financial market laws and regulations;
 - Eliminate the requirement for the Ministry of Justice to register regulations on the financial market;
 - Rationalize what stakeholders describe as the highly confusing and convoluted regulation of JSCs, including eliminating the complicating role of notaries in interfering with complex arrangements by parties whose lawyers are better able to protect them;
 - Elevate the role of the Council of Experts in operations of the National Commission of Financial Market, and in particular engage them more actively in the drafting of laws and regulations.
- *Focus assistance to the National Commission of Financial Market:* As Moldova's evolving legal framework creates more opportunities for the financial markets to play a stronger role in the country's economic development, the role of the Commission in regulating those markets becomes increasingly important. Stakeholders suggest that the increasing prominence of the Commission warrants more focused, long-term technical assistance. Specific issues warranting attention include:
 - Ensure that Commission members possess the technical competence to provide strategic and policy direction over the sectors they regulate;
 - Help develop better legislative drafting skills, including increased consultation with outside experts;
 - Focus on investigating shareholder complaints and intervening appropriately to enforce shareholder rights;
 - Train and build the capacity of Commission personnel;
 - Develop a risk-based approach to supervision, more openness in dialogue, and greater partnership with market participants.

- *Fix the judicial system:* The judicial system is in urgent need of reform and must become a priority of the Moldovan government. Efforts currently underway as part of the Justice Sector Reform Strategy 2011 – 2015 supported by the Council of Europe, and a new USAID Rule of Law Project are steps in the right direction, but will require enormous political will and the active involvement of the private sector, civil society, academia, and international organizations to be successful. As part of these efforts, stakeholders would like to see:
 - Better dialogue and cooperation between the Commission and the courts;
 - Faster, more efficient determinations, with deadlines for case management;
 - Refer more matters to domestic arbitration, including by mandatory choice of forum legislation for certain classes of transaction, and by encouraging the insertion of arbitral clauses in private contracts;
 - Reduction or elimination of fees for cases dealing with protection of minority shareholders; and
 - Specialized training for judges in business and financial market areas.

CONCLUSION

Valeriu Lazăr, Deputy Prime Minister and Minister of Economy, makes a strong case that Moldova is positioned for new investment and stronger growth in his “Forward” to *Investment Guide: Moldova 2012*.⁷¹ (See text box at right.) The impressive economic growth that Minister Lazăr cited corresponded to a three-year period in which Moldova moved from 103rd on the DB 2009 survey to 81st on DB 2012 in overall “Ease of Doing Business.” Two out of those three years, Moldova was a Top 10 Reformer, ranking 2nd on DB 2012 and 6th on DB 2010. These achievements matter because they put Moldova on the map for investors looking for new opportunities to invest.

Close examination of the 2011 results cited by the Minister suggests that Moldova’s prospects are fragile, without a serious commitment to increasing efficiency and dealing with the issue of an underpaid civil service that continues to distort the business environment in the quest for a normal, decent life.

Associations say a small number of high-impact transactions and higher remittances from Moldovans working abroad produced the 44 percent increase in exports and 6.4 percent increase in GDP cited by the Minister. The 38.8 percent growth in foreign direct investment to \$274 million, they note, isn’t from new investors coming to Moldova, but from existing investors expanding. Although 2011’s \$274 million in net FDI inflows was the highest amount since \$711.5 million in 2008, it is a low amount for a low-wage country on the border of the EU at a time when manufacturers are looking for opportunities to reduce production costs. Georgia, by contrast, attracted \$973 million in 2011, despite more difficult access to EU markets. High-profile multi-national companies have come looking at Moldova – including IKEA, Daewoo, and Hyundai – underscoring Moldova’s potential for attracting investment, but they haven’t stayed, because of the gross regulatory inefficiency and pervasive rent-seeking documented in this assessment.

Making the Investment Case for Moldova

Moldova’s economy recovered steadily from its sharp decline in 2009 and has entered a phase of economic growth, supported by the Government’s proactive policies and the performance of its main partner economies.

GDP increased by 6.4% year-on-year in 2011, with exports increasing by 44%. That was the first time in the history of an independent Moldova that exports had increased more rapidly than imports. Industrial production increased by 7.4%, agriculture by 4.6% and transportation by 16.8%. Since 2010, due to the global economic recovery and stabilization of Moldova’s main economic partners, companies have shown growing interest in investment opportunities in Moldova and FDI inflows have increased considerably. For 2011, net FDI inflows grew by 38.8% to USD 274 million, representing the highest rate recorded during the past four years.

It is difficult to maintain annual economic growth of 6 – 7% after a recovery, but Moldova has one of the highest growth rates in the region.

Not only have we been able to grow, but we’ve also implemented structural changes in the economy. Moldova achieved fourth place in the World Bank “Doing Business” global ranking of top reformers in 2011 and we are aiming for first place in 2012.

-- Valeriu Lazăr, Deputy Prime Minister
and Minister of Economy

⁷¹ The Investment Guide, produced by MIEPO and PriceWaterhouseCoopers, is available online at <https://docs.google.com/viewer?url=http%3A%2F%2Fwww.miepo.md%2Fpublic%2Ffiles%2FPublicati%2FMoldova%2520Business%2520Guide%25202012.pdf>.

Minister Lazăr’s goal of making Moldova the world’s Number One Reformer for 2012 reforms, which would be reflected on the DB 2013 report, was possible and urgently needed, both to continue the improvements and to confirm to global investors that Moldova is an increasingly attractive investment destination. Unfortunately, Moldova failed to meet that goal.

Moldova’s ranking only improved two places on the recently released DB 2013 report, which includes reforms implemented through May 31, 2012, moving to 83rd from a revised 86th in the DB 2012 report. In fact, as noted earlier, many of the raw scores in the subject areas covered by this report actually worsened in the DB 2013 report, so progress has been largely static.

Moldova failed to make more large gains because the political will to attack the sources of regulatory inefficiency was absent. The goal itself – and the economic growth that will follow – remains within reach whenever Moldova decides to choose efficiency and prosperity.

This assessment report has identified reforms to just five indicators that, if implemented, could allow Moldova to re-enter the ranks of the world’s Top Ten Reformers. Depending on how aggressive other countries reform, they could make Moldova the world’s Number One Reformer. Most of the recommendations involve increasing procedural efficiency, not changing policy, and can be implemented in the near term. While all of the reforms are important, improvement on the “Trading Across Borders” indicator matters most to investors and will produce more economic growth and jobs creation than any other indicator.

The table below summarizes how the recommended reforms would improve Moldova’s rankings on the five indicators discussed in this assessment. Moldova’s overall “Ease of Doing Business” ranking would increase from 83 to 44, a 39-rank improvement. In each of the last three years, a 39-place on overall “Ease of Doing Business,” would have won recognition as the world’s Number One Reformer.

Table VI-I. Impact of Recommended Reforms on Doing Business Rankings

Indicator	Reforms	DB 2013	DB 2014	Change
Trading Across Borders	Reduce trading times to EE&CA average -- cut 6 days for export, 6 days for import	142	136	6
Paying Taxes	Combine social and health insurance reporting; e-filing for VAT	109	93	16
Dealing with Construction Permits	Fully enforce Law 163 as written	168	118	50
Starting a Business	Streamline procedures, reducing time; eliminate minimum capital requirement	92	9	83
Protecting Investors	Amend law to increase shareholder protection; Ensure DB Team knows what has already been accomplished	82	1	81
Overall Ease of Doing Business		83	44	39

ANNEX A

A. THE BIZCLIR DIAGNOSTIC PROCESS⁷²

This report is based on a comprehensive methodology established through USAID’s Bureau for Economic Growth, Education, and Environment (E3), which USAID has utilized in more than 40 countries since 1998. Having been updated regularly since the methodology’s conception, the indicators now substantially align with the structure of the World Bank’s Doing Business country reports.

Since 2002, Doing Business has assisted countries in targeting where and how their regulatory environments may favor or interfere with economic growth. For each of the topics it examines, the World Bank considers a few key indicia of whether the environment for doing business is “working,” measured by indicators such as the number of procedures involved in achieving a goal, the number of days it takes, and its cost in relation to per capita income. The World Bank currently gathers data from 185 countries, and ranks each, thus demonstrating how their respective regulatory environments compare to others throughout the world. In the most recent 2013 Doing Business report, Moldova ranked 83rd. Moldova has shown in recent years that it wants to, and can, be a strong reformer. As mentioned, Moldova was the 4th leading reformer in 2011 in the Doing Business global ranking of top performers. However, its total ranking remains average and its scores in the areas studied in this assessment demonstrate need for improvement.

USAID’s BizCLIR indicators take each subject covered by Doing Business and delve deeper into their respective legal frameworks, implementing and supporting institutions, and social dynamics to better understand why a country falls within the World Bank’s rankings. The BizCLIR indicators consider each subject from a variety of perspectives, and offer a better understanding of the issues highlighted in the Doing Business initiative, and the need to help donors and countries understand, with greater specificity, how to reform. The chapters in this report are structured the same way. Specifically, each has four analytical sections:

Legal Framework

The chapter first examines the laws and regulations of Moldova that serve as the structural basis for the country’s ability to achieve and sustain market-based developments. The methodology poses the following questions: How clear are the laws, and how closely are they do existing laws reflect emerging global standards? How well do they respond to commercial realities that end-users face? What inconsistencies or gaps are present in the legal framework? A diagnostic can discover, through this process, opportunities to make relatively small changes that may result in significant openings for business development and expansion, as well as in governmental processes.

⁷² This section is based to a great extent, in structure and language, on the comparable section from the BizCLIR Report “Jamaica’s Agenda for Action” (February 2008).

Implementing Institutions

This chapter examines institutions that hold primary responsibility for implementation and enforcement of the legal framework and subsidiary laws, regulations, and policies. These institutions include government ministries, authorities, or in certain cases, private institutions such as banks and other lending institutions. The indicators seek to uncover how these implementing institutions function in Chisinau and throughout the country, as well as how they serve less-empowered constituencies.

Supporting Institutions

The section closely examines organizations, individuals, or activities without which the legal framework or policy agenda in Moldova cannot be fully developed, implemented, or enforced. Some examples include lawyers, business support organizations and private services, professional associations, universities, and donor institutions. Questions and analyses examine relative awareness of law and practice on the part of each institution, and the specific ways in which institutions increase public and professional awareness, work to improve the business environment, and otherwise serve their constituencies. In certain cases, weaknesses in supporting institutions have been identified as critical areas for reform.

Social Dynamics

The final diagnostic looks to relevant, critical social issues as constraints or enablers of the business environment. The methodology attempts to eliminate roadblocks to reform, including through disabling entities that demonstrate interest in subverting or avoiding reform or change. The diagnostic also seeks to identify significant opportunities for bolstering the business environment – such as champions of reform – as well as matters of access to opportunity and formal institutions. It is believed that a full understanding of legal and institutional issues cannot be achieved without consideration of a country's social dynamics.