

**Regional Workshop in  
Land Issues in Central and Eastern Europe and the CIS**

**LAND PRIVATIZATION AND  
RESTRUCTURING OF  
COLLECTIVE FARMS**

**MOLDOVA CASE STUDY –  
THE NATIONAL LAND PROGRAM**

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## ***Disclaimer***

The opinions and views expressed herein, as well as responsibility for accuracy and completeness of the data are the sole responsibility of the authors, who have endeavored to present complete documentation and information on land privatization and restructuring of collective farms in Moldova within the National Land Program, as well as a review and analysis of the current situation in Moldovan agricultural sector. No part of this document express any views or opinions of the Government of the United States, the U.S. Agency for International Development, the Government of Moldova, East-West Management Institute, Inc. or of the Soros Foundation Moldova.

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## EXECUTIVE SUMMARY

The enactment of the Land Code in 1992 marked the official beginning of the land reform in Moldova. In accord with the provisions of the Land Code, more than 1.2 million people were entitled to receive land in private ownership. It was the time of big hesitations and passivity on the one hand, and sporadic attempts and spontaneous privatization on the other hand. Due to lack of Government's commitment and political will to proceed firmly with land privatization, the first five years after the adoption of the Land Code brought no palpable results. Reforms went slowly and followed different patterns throughout the country.

In early 1996, the Center for Private Business Reform (East-West Management Institute's presence in Moldova) was asked to privatize the Mayak collective farm in Nisporeni. In 1996-1997, the Government of the Republic of Moldova with the support of the US Agency for International Development implemented the "Land" Pilot Project in 72 collective farms in 31 raions throughout Moldova. The methodology applied on these farms was entirely based on the existing Moldovan legislation and included:

- in-kind distribution of all land farmed by the collective farm (with title preparation and issuance by Booz-Allen and Hamilton) to its entitled beneficiaries;
- in-kind distribution of the collective farm's debt-free assets (issuing property certificates upon request) to its entitled beneficiaries;
- reorganization of the collective farm in other legal forms stipulated by Moldovan legislation.

The National Land Program (NLP) was launched in March 1998 by President Petru Lucinschi as a roll-out of the pilot project to completely privatize the remaining 900 collective farms on the basis of an agreement with the Government of the Republic of Moldova and USAID in strict compliance with the national legislation. The program had an unprecedentedly wide range of the logistic and lawmaking objectives aimed at the quickest completion of privatization in the agrarian sector. The first outcome of the program was a number of amendments in the Law on the Privatization Program for 1997-1998 introduced on November 6, 1998. These amendments provided for the in-kind transfer of the following assets to the in-kind land privatization participants regardless of the financial situation of their kolkhozes and sovkhoses: irrigation facilities, perennial plantings and unfinished agricultural goods located on the privatized land; tractors, combines, vehicles and other agricultural machinery; work and production livestock; seeds.

However, the legislator had not yet settled the future fate of kolkhozes and sovkhoses having accumulated huge debts totaling 2 billion lei, gradually losing their land and critical property and having de facto become absolute bankrupts. In this connection, the National Land Program prepared and the Parliament adopted the Law No 392-XIV of May 13, 1999 on the restructuring of farms under privatization (the Debt Law). Interconnected amendments were made in a number of related laws including the law on the tax service and the budget laws. The Debt Law was based on the voluntary off-court liquidation procedure of the privatized enterprise whose debts were completely settled throughout this procedure according to the following scheme. Thus, approval of the Debt Law and of respective regulations completed the over 10-year process of creation of the extensive legislative basis for privatization and restructuring in the country's agrarian sector.

By the end of the National Land Program (31 December 2000):

- 931 collective farms completed land property privatization;
- 87,787 new, privately owned farming enterprises were registered;

- 858 collective farms published liquidation notices;
- 836 farms finalized privatization and were liquidated.

The National Land Program enjoyed strong government support and paid great attention to relations with the President, the Parliament and the Government, which broadly advertised its objectives within official circles and mass-media. Four Governments were changed during the implementation of the NLP without affecting its progress and overall final success.

In view of the high density of the rural population, the land privatization scheme adopted in the Republic of Moldova resulted in the fact that the land parcels transferred to the individuals' private ownership are relatively small (1.5 ha, as an average). This fact served as a ground for the agrarian reform opponents to say that the land split into small parcels (land fragmentation) is the cause of collapse in the agrarian sector because it was impossible to organize highly efficient production based on modern machinery and technology on such small parcels. In this connection, the currently ruling party (Communist Party) tries to change the Land Code ensuring quick land consolidation through administrative methods. However, practice shows that small size of parcels in the individuals' private ownership is no obstacle in organizing large-scale production. Land consolidation is unfolding based on market mechanisms and primarily on lease relations and sale/purchase of land.

The study undertaken by the Center for Strategic Studies and Reforms (CSSR) in 2001 on the initiative of the Private Farmers Assistance Program<sup>1</sup> (PFAP) shows that at the given moment lease serves as the major factor for land consolidation. The average size of farms functioning on the leased land basis is equal to 680 hectares, some of them being over 2000 hectares. Thus, the conclusion was that there was no need to introduce administrative measures aimed at land consolidation. It is advisable to develop further on and strengthen the market mechanisms that have already started functioning: agricultural land lease, and its sale and purchase.

The right to buy and sell land, introduced in Moldova in 1997 by the *Law on land normative price and procedures for buying and selling land* was another important factor that has a significant impact on agricultural land consolidation. In the Republic of Moldova the owner itself has the right for selling the land in the private ownership. Agricultural land can be sold only to the citizens of the Moldova.

The data from the State Agency for Cadastre, Land Resources and Geodesy shows that 103306 land sale/purchase transactions were performed in the rural area throughout years 1999-2001, including 72849 of those performed in year 2001. The remaining part of transactions includes donation, inheritance and household land parcels. Mortgage is equal to 12030 transactions. 36328 out of the total number of transactions are related to agricultural land including 24625 of those performed in 2001. The average size of one transaction is 0.4 ha. The weighed average price of 1 ha of agricultural land was equal to 228 US dollars in 2000 and 233 US dollars in 2001.

The land reform promotion in the Republic of Moldova has also generated the need to create an efficient infrastructure for the registration of the private ownership right for land and other real estate objects. In relation to that, on December 22, 1992 the *Law on state regulation of land ownership relations, state land cadastre and land monitoring* was adopted.

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<sup>1</sup> PFAP was launched in January 2001 to provide post-privatization assistance to landowners and rural based private entrepreneurs after the completion of mass privatization within the National Land Program. PFAP is designed for three years and is financed/implemented by USAID/EWMI/Soros Foundation Moldova.

According to the situation as of January 1, 2002, the cadastral offices have registered the creation of 3 098 thousand of real estate objects, including 2 703 thousand of agricultural lands and 233 thousand of household plots. A total of 208 thousand transactions, including 103 thousand transactions involving agricultural lands and 31 thousand household plots transactions have been registered over the same period. Out of these transactions, 36 thousand are agricultural land sale transactions and 16 thousand are household plots' sale transactions. At the same time, there were registered 6 thousand of agricultural land mortgage cases and 1.5 thousand cases of household plots' mortgage cases. The aforementioned data shows that the real estate market, including on land estate, becomes an important factor in the market economic relations of the republic.

Over one million participants in new civil and legal relations have appeared over the four-year process of privatization in agricultural and namely: owners of land parcels and privatized property and tens of thousands of new private enterprises many of which became land and/or property lessees (over 0.5 million lease agreements). These objective changes generated the appearance of different types of disputes. Major legislative prerequisites for the creation and activity of the arbitration are determined in the *Law on the Court of Arbitration (Arbitration) No 129-XIII of 31.05.94* based on which the arbitration may have both general and specialized responsibilities. Dispute examination via arbitration in principle and via ad-hoc arbitration in particular is complicated by the poorly developed legislative basis on arbitration in Moldova, the novelty of this procedure for the agrarian sector as well as the novelty and complexity of the appearing disputes. In this situation, it is especially important to ensure permanent and qualified control over dispute examination in order to avoid violation of legal rights and interests of citizens and avoidance of conflicts with courts. But it is even more important to direct all efforts at supporting the prestige of the arbitration as an institution with ancient traditions well known and widely used in the world practice.

Mass privatization of the former collective farm land and property within the National Land Program resulted in the appearance of hundreds of thousands of economic entities engaged in agricultural production based on the private ownership. This fact brought about the need for creation of a special post-privatization program that would include the improvement of the existing and development of the new legislative basis regulating the activity of the new economic enterprises and economic relations in the market environment; development of the market infrastructure (primarily in the sphere of marketing as well as material and technical resource supplies); technical, veterinary and agrochemical servicing; consulting and information support. It also was very important to organize mass training of the new owners on the fundamentals of entrepreneurship, legislative basis of the Republic of Moldova and new technologies of agricultural goods production.

**The Private Farmers Assistance Program (PFAP)** was launched in January 2001 to provide post-privatization assistance to private farmers and rural entrepreneurs in Moldova. Under PFAP, farmers and rural entrepreneurs, as well as rural associations and NGOs obtain support and assistance to help the Moldovan agricultural sector recover and grow. The program is designed for three years with joint funding by USAID (75%) and EWMI/Soros Foundation (25%). The program is implemented in partnership with the Soros Foundation Moldova and in close collaboration with local NGOs. In year 2001 more than 50 local organizations/NGOs contributed directly to the achievement of the Program's goals and objectives.

The goal of PFAP is to contribute to the business success of private farmers in order *to ensure that the transition to private farms results in sustainable economic growth*. It is also envisioned that as a result of the PFAP, a network of institutions (NGOs or commercial consulting firms) will be strengthened to *provide continuing support to private farmers and enterprises* in rural communities throughout

Moldova. PFAP achieves its goal through activities in three strategic areas. These components and the main tactics within each strategic component are:

- Development of a sound legal and regulatory environment. The goal of this component is to eliminate legal and regulatory impediments to the further development of private farmers and entrepreneurs (as recommended by a EWMI/CARANA study, 1999) and, where appropriate, draft new laws and regulations that will create an enabling environment for private farmers and entrepreneurs.
- Development of rural enterprises, including farmer cooperatives and producer associations. The goal of this component is to develop multiple ownership enterprises and organizations that purchase farm products, supply farm inputs or services with an emphasis on the forming of business cooperatives.
- Landowner legal assistance and information support. This component includes providing legal assistance to help ensure the protection of the landowners' rights, and improving the information provided to farmers throughout Moldova by continuing publications to help farmers buy inputs and sell products, gain information about their rights and development of their farms.

PFAP pays special attention to encouragement of women in agriculture and rural enterprise development, with the hope that women as well as men, are be part of the development of commercially viable business activities. Through the *PFAP Grant program*, groups of business entities wishing to create or strengthen their existing farmer cooperative, producers association, etc. that fit the eligibility criteria apply for grants, thus becoming a primary beneficiary of the PFAP grant program. Other organizations (primarily NGOs) wishing to collaborate with PFAP in achieving its goals and objectives are eligible for PFAP grants and are encouraged to become secondary beneficiaries of the PFAP. This type of financial assistance to improve or provide services needed by PFAP primary beneficiaries under PFAP goals and objectives is primarily directed toward service-type organizations including Moldovan NGOs, trade associations and selected enterprises or village-level support groups.

One of the biggest difficulties encountered by Moldovan farmers is lack of funds needed for successful business and its expansion via purchase of new land. Commercial banks extend credits at rather high interest. At the same time, the usual repayment period of such credits is 3-6 months, which is obviously insufficient for agriculture with its year's technological cycle. Besides, the procedure of obtaining credits via commercial banks is very bureaucratic. This fact requires development and implementation of special programs for crediting farmers. The Mortgage Lending Program (MLP) implemented in Moldova with the USAID support is one of such programs.

The program aims to promote medium term affordable credit to farmers for the purchase and consolidation of land, thereby increasing investment in Moldovan agriculture. The immediate objectives are:

- To instruct Savings and Credit Associations (SCAs) on all aspects of mortgage lending allowing them to offer a new financial product to their members that will generate investment in agriculture.
- To assist farmers prepare business plans and teach them to use the plans to make informed business decisions.

To give farmers experience with secured loans and the opportunity to establish a positive credit history that they can use in the future when seeking larger loans from commercial banks.

## **1. LEGISLATIVE BASIS**

The right for private ownership of land in the Republic of Moldova was declared on May 29, 1991 by introduction of the respective amendment to Article 11 of the country's Constitution. The right of private ownership over land was also included in country's new Constitution of 1994. Hence, on December 25, 1991, the Parliament approved a new Land Code that became a major legislative act regulating land privatization.

### **1.1 The Land Code**

The Land Code determined the procedure for allocation of the land under dwelling houses and private household parcels (art. 11); the procedure for determining the agricultural land fund, the number of persons entitled to land privatization and the way of determining the sizes of land due to each privatization participant (art. 12); the procedure for using by the privatization participants of the land and property shares due to them from former kolkhozes and sovkhozes (art.13). In conformity with the Code, land privatization based on a number of principles, such as a restricted number of the land privatization participants who contributed to this land farming with their personal labor, as well as their equal rights for the land and its free privatization.

In view of the high population density, the Land Code first gave the right for land privatization to 5 categories of persons – kolkhoz members, sovkhoz and other agricultural enterprise employees, pensioners of these enterprises, rehabilitated peasants-victims of political repression, as well as the peasants having earlier transferred their land to kolkhozes. Later, the Parliament supplemented this list giving the right for land privatization to employees and pensioners of the rural production and social infrastructure as well as to some other categories of persons. However, the initial ban on returning the land (restitution) to its former owners remained unchanged.

The Land Code envisaged not one but two stages of the land privatization. At the first, and in many respects formal, stage the village (community) land commission determines the land share (in hectares) of equal hectare points value for every privatization participant. The right for this ideal land share is secured in the land title issued by the mayor's office of the village (community). At the second stage that can be initiated only by each specific privatization participant, the land with its physically determined boundaries and respective property is transferred to the private ownership of the person wishing to exit from the kolkhoz or sovkhoz.

### **1.2 Privatization program**

The procedure for the privatization of the non-landed property of kolkhozes and sovkhozes (called hereinafter – property) was determined not by the Land Code but by the periodically adopted by the Parliament laws on the state privatization programs for the years 1993-1994, 1995-1996 and 1997-1998. In conformity with this law, individual property shares of employees and pensioners of the privatized enterprise are determined by the property commission based on the methods approved by the general meeting of employees and pensioners with the account of each person's labor contribution. However, these ideal property shares are allocated in kind only at the second stage of the property privatization after specific applications on exiting from the kolkhoz or sovkhoz are submitted. However, practical allocation of the in-kind property to specific peasants was impossible because this property was claimed by numerous creditors huge debts to whom remained unsettled and continued

increasing. As a result, land and property privatization was limited to the first stage only, i.e. to determining the ideal shares of privatization participants.

### **1.3 The National Land Program**

In order to resolve the impending problems, the Government approved the National Land Program in its Decision No 1022 of October 6, 1998 "On the Progress of the Agrarian Reform". The program had an unprecedentedly wide range of the logistic and lawmaking objectives aimed at the quickest completion of privatization in the agrarian sector. The first outcome of the program was a number of amendments in the Law on the Privatization Program for 1997-1998 introduced on November 6, 1998. These amendments provided for the in-kind transfer of the following assets to the in-kind land privatization participants regardless of the financial situation of their kolkhozes and sovkhoses: irrigation facilities, perennial plantings and unfinished agricultural goods located on the privatized land; tractors, combines, vehicles and other agricultural machinery; work and production livestock; seeds. The creditors were not allowed to claim the indicated types of property while the privatization participants having received this property in kind were relieved of the secondary liability on the debts of the enterprise under privatization. Thanks to these amendments, practically simultaneous in-kind privatization of the land and the property needed for its farming started. This made it possible to create viable farms and other rural private enterprises.

### **1.4 The Law on restructuring of farms undergoing privatization**

However, the legislator had not yet settled the future fate of kolkhozes and sovkhoses having accumulated huge debts totaling 2 billion lei, gradually losing their land and critical property and having de facto become absolute bankrupts. In this connection, the National Land Program prepared and the Parliament adopted Law No 392-XIV of May 13, 1999 on the restructuring of farms under privatization (hereinafter – Debt Law). Interconnected amendments were made in a number of related laws including the law on the tax service and the budget laws.

Law No 392-XIV of May 13, 1999 was based on the voluntary off-court liquidation procedure of the privatized enterprise whose debts were completely settled throughout this procedure according to the following scheme. As long as the enterprise was insolvent, its historical debts to private creditors were transferred to the state with the agreement of the latter, of course. Having become a debtor to private creditors, the state immediately settled its debts to them via tax credit issuing debentures on the unsettled part of these debts (should there be any) committing itself to settle them via a similar tax credit but in the course of the five coming years. As to the enterprises under privatization, they settled their grown debts to the state through remaining property and primarily through social assets.

Thus, approval of Law No 392-XIV of May 13, 1999 and respective regulations completed the over 10-year process of creation of the extensive legislative basis for privatization and restructuring in the country's agrarian sector.

## **2. LAND PRIVATIZATION AND FARM RESTRUCTURING**

### **2.1 Chaotic privatization before 1996**

The enactment of the Land Code in 1992 marked the official beginning of the land reform in Moldova. In accord with the provisions of the Land Code more than 1.2 million people were entitled to receive land in private ownership. It was the time of big hesitations and passivity on the one hand, and sporadic attempts and spontaneous privatization on the other hand. Due to lack of Government's commitment and political will to proceed firmly with land privatization, the first five years after the adoption of the Land Code brought no palpable results. Reforms went slowly and followed different patterns throughout the country.

In some cases, based on private initiative, entitled persons exited the collective farms and started to farm land parcels individually with no formal registration of their ownership rights. Other collective farms continued their economic activity with no changes at all. Finally, the third group of collective farms took steps to reorganize and privatize land. However, these were superficial changes: collective farms changed their legal status (overnight reorganization into cooperatives, joint-stock companies, associations, other), some broke up in smaller collective farms and in some Primarias<sup>2</sup> individual land shares were calculated and land certificates were issued. In general, the process of decollectivization was slow, reflecting the political debates at that time – the opposition between reformist and conservative forces.

The elaboration of a fair methodology for land and property distribution and the political will to apply it throughout the country in a coordinated manner were the requisites for a real reformation of the agricultural sector that would be based on private ownership of land and property. Land distribution to peasants revealed the complexity of issues inherent to the agrarian reform. In order to conduct business activities, peasants that received land need to create and register their private farms, they need agricultural equipment to be able to farm the land and they need titles to secure land ownership.

Although the Parliament adopted a series of important laws allowing privatization and reorganization of collective farms (Law on Property, Law on Entrepreneurship, Law on Joint Stock companies, law on privatization programs, and others), by 1996 there was no significant progress in reforming Moldovan agriculture.

### **2.2 Mayak experiment and the Pilot Project**

In early 1996, the Center for Private Business Reform (CPBR)<sup>3</sup> was asked to restructure (actually privatize) the Mayak collective farm in Nisporeni.

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<sup>2</sup> Primaria is the village Mayor's office, representing the lowest level of government.

<sup>3</sup> The CPBR was launched by the East West Management Institute (EWMI) as its presence in Moldova. EWMI is a U.S. non-profit organization headquartered in New York City. EWMI is dedicated to promoting legal and economic reform in Central and Eastern Europe and the former Soviet Union. Founded in 1988 by George Soros, EWMI is one of many non-profit foundations linked together in an informal network called the Soros Foundations network. EWMI manages highly skilled international and local consultants who design state-of-the-art economic reform programs, draft and implement laws, develop accounting standards, privatize collective farms, and train government officials and judges. EWMI participated in an international tender issued by USAID and was selected to implement an enterprise-restructuring project in 1995. During implementation of this project, the GOM requested EWMI/PFAP privatize the Mayak collective. Closely associated with Soros Foundation Moldova, CPBR has established a reputation of success and accomplishment in all its activities.

Together with the Moldovan Ministry of Privatization<sup>4</sup> and USAID, it was agreed that CPBR would develop and implement a methodology for the break-up and privatization of the Mayak collective farm as a pilot project. The farm was successfully privatized, surveyed and 1,345 individual land titles were distributed to the members of the farm. Taken together, the privatization of the Mayak farm and the legalization of private land ownership was an historic step that completely and irrevocably separated agricultural sector of Moldova from its Soviet past.

In 1996-1997, the Government of the Republic of Moldova with the support of the US Agency for International Development implemented the "Land" Pilot Project in 72 collective farms in 31 raions throughout Moldova. The methodology applied on these farms was entirely based on the existing Moldovan legislation and included:

- in-kind distribution of all land farmed by the collective farm (with title preparation and issuance by Booz-Allen and Hamilton) to its entitled beneficiaries;
- in-kind distribution of the collective farm's debt-free assets (issuing property certificates upon request) to its entitled beneficiaries;
- reorganization of the collective farm in other legal forms stipulated by Moldovan legislation.

Since the applied methodology for collective farm break-up and privatization also included the creation of new private farms that would not inherit the collective farm's debts, a complete distribution of assets was possible only in cases when the collective had no debts. That was the case of only 1 collective farm that was able to fully repay its debts, completely privatize and liquidate. Other than that case, as a result of farm indebtedness, not a single farm was able to distribute all the assets, and had to set apart certain amounts of property<sup>5</sup> for further debt settlement. Farm's assets were divided into 3 categories:

1. property set apart for subsequent settlement of debts to the creditors of the collective farm. In 90% of the farms, legal successor enterprises were created based on this property to honor the financial obligations of the collective;
2. social assets and public utilities were transferred to the local government or to the successor enterprise;
3. debt-free assets that formed the privatization fund were distributed to entitled persons. Based on these assets approximately 1300 private farms were created.

Although there were some basic principles to follow, each farm was approached as a special case. The structure of assets within the three categories mentioned above varied from one farm to another, depending on the degree of farm's indebtedness and its creditors.

Taking into account the debt situation, it was not possible then to develop a single methodology applicable for all the farms privatizing their property, without infringing creditors' rights. In cases when privatizing farms had assets that could not be divided in-kind among peasants (wineries, mills, oil-mills, other processing units, etc), but were part of the privatization fund, these assets were transferred to the successor enterprise, and the peasants became its co-founders.

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EWMI/CPBR was the contractor selected by USAID to lead collective farm privatization and restructuring effort. Some of the steps of privatization included land surveying, grouping and arranging, and the preparation and issuing land titles. These steps were the responsibility of the USAID subcontractor Booz-Allen and Hamilton with Stewart Information International and Rural Development Institute as subcontractors.

<sup>4</sup> Later became the Department of Privatization within the Ministry of Economy and Reforms.

<sup>5</sup> Property includes all farm's assets. It does not include land, which was state property.

Expectations that the successor enterprises would repay their debts by selling the assets left for that purpose or by generating profits as a result of lucrative businesses did not materialize. In most cases the successor enterprises kept accumulating debts, which quickly turned into bad debts, as most successor enterprises did not undertake sufficient economic activity. That was the price paid for successful accomplishment of the main goals of the pilot-project: in-kind distribution of land and debt-free property to entitled individuals and creation of privately owned enterprises.

In general, the pilot project was a success that allowed CPBR specialists to accumulate great experience, but it still was a pilot project on 72 farms.

### 2.3 The National Land Program

The National Land Program (NLP) was launched in March 1998 by President Petru Lucinschi as a roll-out of the pilot project to completely privatize the remaining 900 collective farms on the basis of an agreement with the Government of the Republic of Moldova and USAID in strict compliance with the national legislation. The experience accumulated during the pilot phase and the passage of the Law No 187–XIV<sup>6</sup> (hereinafter *Law on critical property*) allowed the NLP to advance significantly, using a refined methodology.

The Law No 187–XIV introduced the concept of *critical property*. The critical property included irrigation facilities and perennial crops located on land subject to privatization, tractors, combines, other agricultural machinery and equipment, transportation means used for agricultural production, planting materials, working and production livestock, and unfinished goods. According to that Law, the given property could be transferred in-kind to entitled persons regardless of farm's financial situation and the status of its settlements with creditors. This resulted in increased possibilities for forming viable privately owned enterprises (peasant farms, limited liability companies, cooperatives, other). Therefore, following the land tenders, property tenders were held to distribute the critical property to entitled persons.

Yet, the fate of the old collectives, which were left without land and critical property, but with growing debts and other blocked assets on their balance sheets, was still uncertain under existing legislation. It became clear during the "Land" Pilot Project that the issue of unsettled debts of the collective farms was considerably slowing down the privatization and reorganization in the country's agricultural sector. In early 1999 this problem became critical and resulted in a number of negative consequences:

- the process of complete restructuring of collective farms and finalization of distribution of property among peasants was postponed for an uncertain period of time;
- assets of privatized farms, reserved for repaying debts, were excluded from economic life, while their security was not always provided;
- the private farms, created as a result of privatization of the collective farms, would not be able always to function normally, as over 35 thousand of dissatisfied creditors were causing them a lot of trouble, refusing to deliver supplies and services and using informal ways of pressing them to pay-off the old collectives' debts.

At the same time, other issues were emerging that required solution:

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<sup>6</sup> The Law No 187–XIV *On Introducing Amendments in Some Legislative Acts* of November 6, 1998.

- Liberation of the budgetary process from the constant uncontrolled losses which were caused during many years by the majority of collective farms and which might continue without complete and final liquidation;
- Decaying and abandoned infrastructure in villages and municipalities; and
- Significant assets remained on the collectives, after distribution of critical property, which potentially might be used to settle debts or to be distributed in a second and final property tender if a way could be found to settle the debts on those farms participating in the NLP;
- The old farm shells containing frozen assets and debts created potential opportunities for fraud.

Although the Law on critical property allowed significant progress in privatizing farms and creation of debt-free private farms, the problem of collective farms indebtedness was once again postponed. The side effects of the NLP (semi-dead insolvent collectives, frozen resources, including decaying public infrastructure, huge amounts of growing debts, dissatisfied creditors, potential fraud) required additional efforts for debt resolution and complete restructuring of collective farms.

Based on survey data it was projected that the property of all collective farms would diminish by 0.8 billion lei, or 6 percent during one year due to depreciation, theft, sales of seized assets, uncontrolled distributions, or other unaccounted for losses. Therefore while debts increased exponentially – even though there was little or no economic activity on many collectives – the value of their assets which might eventually be used to repay these debts depreciated or declined.

After much discussion and debate it was decided that special legislation would be necessary to resolve the debt situation on collective farms participating in the National Land Program. EWMI specialists in collaboration with the Ministry of Finance started drafting the Law on restructuring of farms undergoing privatization (the Debt Law). The Debt Law also was intended to stimulate the process of creating new enterprises able to work in market conditions based on private land and property; be a one-time process, not to be repeated; be applied only to farms participating in the National Land Program; reasonably defend the interests of the private creditors; and have a “reasonable” burden on the country’s budget.

The debt settlement procedure begins with a general farm meeting to decide whether to participate in the Debt Program, which must include debt settlement and liquidation. Once this is published by the Property Commission in the *Official Monitor*, the process formally begins. Publishing the farm liquidation intent notifies creditors and obliges them to file claims or have their debts written off; starts a process where any debts owed to the farm are considered immediately due; and initiates a period when farm property cannot be written off, seized or collateralized in any way. Following the official notification, the debt settlement proceeds according to the following steps: 1) Settlement of debts to priority creditors and employees; 2) Historic debt settlement; 3) Settlement of current debts; 4) Settlement by the state of transferred debts; 5) Privatization of property, remaining after debt settlement; 6) Farm liquidation and removal from the State Commercial Registry.

After the Moldovan Parliament passed the Debt Law on 13 May 1999, the CPBR formed new units to provide assistance to all Government agencies involved in debt resolution and liquidation of collective farms under the provisions of the Debt Law.

Local CPBR teams assisted the Property Commissions of the farms in preparing legal and accounting documents, and provided consultations on different issues. The expert team based in Chisinau provided technical assistance to the government, and represented the farms’ interests during the sittings of the

Republican Commission – the official body approving acceptance by the government of historical debt and other critical approvals during the debt resolution process. One vital role of the expert team was to assist different government agencies (mainly the Tax Office and the Ministry of Finance, the Social Fund, Registration Chamber by the Ministry of Justice, the State Archive, the Department of Privatization, the National Securities Commission, and others) draft internal regulations and issue circular letters aiming at adjusting existing working procedures to the provisions of the Debt Law, providing clear instructions to local authorities and government representatives on the implementation of the Debt Law, as well as training them in all aspects of the program.

By the end of the National Land Program (31 December 2000):

- 858 collective farms published liquidation notices;
- 856 farms' documents were approved by the Republican Commission (decisions on transfer to the state of historical debt and writing-off of remaining unsettled historical debt, if necessary);
- 836 farms finalized privatization and were liquidated.

For these farms:

- 1,981,243,000 lei in debt was settled;
- 1,411,296,000 lei in social assets were transferred to local government;
- 1,146,279,000 lei in historical debt was offset with assets;
- 90,370,000 lei in historical debt was written-off as remaining historical state debt.

The average time required for a collective farm to completely settle its debt, distribute its property and liquidate was 122 days, ranging from 32 to 300 days. The efficiency of the debt component of the National Land Program was constantly growing, and registered in summer 2000 a **daily** average of:

- 2.3 farm liquidations;
- 4.3 million lei (\$345,000) in debts settled.

After a five-year stagnation period between the appearance of the first applicable Moldovan legislation and the implementation of a comprehensive land reform program, completion of the NLP objectives in a relatively short period of time was an ambitious project. Sporadic, ad hoc and superficial privatization was replaced by mass empowerment of people through real and complete privatization of land and property, secured by land and property titles.

The National Land Program enjoyed strong government support and paid great attention to relations with the President, the Parliament and the Government, which broadly advertised its objectives within official circles and mass-media. Four Governments were changed during the implementation of the NLP without affecting its progress and overall final success.

### 3. AGRARIAN SECTOR AFTER MASS PRIVATIZATION

#### 3.1 Summary of accomplishments of the National Land Program

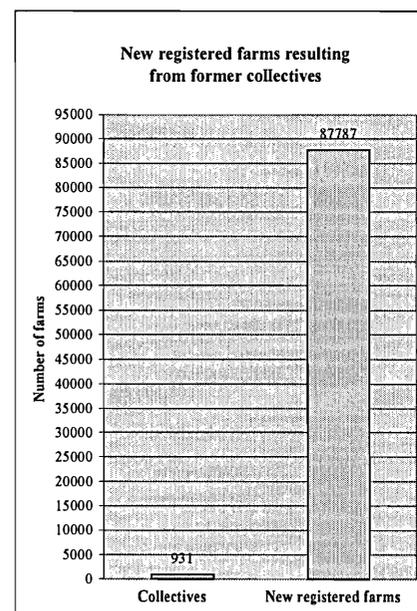
The National Land Program, the farm privatization project funded by the U.S. Agency for International Development (USAID), completed its work Dec. 31, 2000. The program accomplished its goal of privatizing and liquidating essentially all of Moldova’s former collective or state farms – 1004 – and forming new, privately owned farming enterprises.

Farms privatized-pilot projects <sup>7</sup>	Farms privatized-NLP <sup>8</sup>	Total farms privatized to date
73	931	1004
<b>Total people receiving land</b>		<b>Total people receiving property shares</b>
906,312		1,051,145

Under this program, people learned their rights, responsibilities and options under privatization, and received legal titles to their land and become owners of their property (equipment, buildings, etc.). By distributing land/property of the former collective farms, the newly empowered land/property owners have achieved their rights under the law, a true step towards strengthening this democracy. And through the creation of private farms, it is hoped that the agricultural economy will be revitalized and grow, an important factor to Moldova as the sector is estimated to account for over 50% of the economy and 60% of Moldova’s 4.2 million population is rural-based.

#### Farms privatized:

- During the national program, 931 farms completed their land and property “tenders”, the most critical stage of distributing land and property allowing the formation of privately held enterprises. This included agricultural colleges and farms in Gagauzia (an autonomous territory), which were never anticipated to be privatization candidates. The grand total of collective farms privatized (931 from the National Program, 73 from pilot programs) is 1004.



#### New privately owned farms registered:

- 87,787 new farming enterprises were registered. (It is estimated that only 50-60% of all newly formed enterprises officially registered, so 174,000 new farms or service/equipment-based enterprises may actually be functioning in Moldova as a result of the National Land Program.)

#### Farm debts restructured:

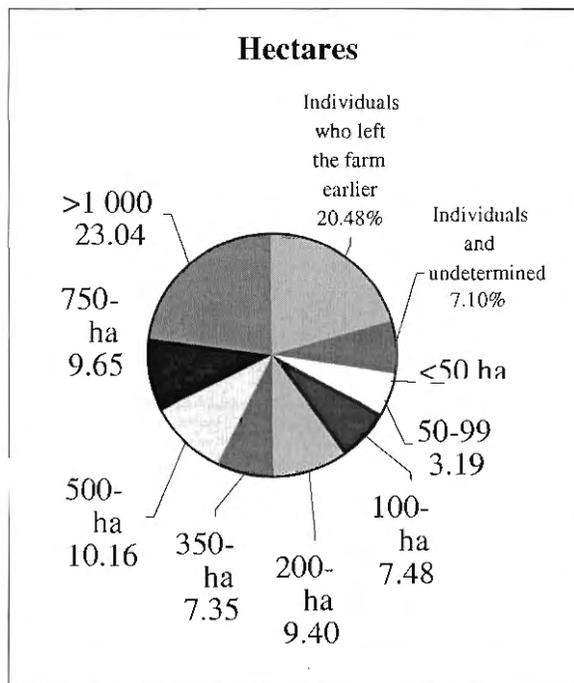
<sup>7</sup> The first pilot project, initiated by EWMI as part of a USAID-funded enterprise-restructuring project in Nov. 1995, finished in 1996. The second pilot project to refine the methodology privatized 72 farms across Moldova.

<sup>8</sup> Privatization in this paper is defined as the distribution of land and property through the tender process. This is viewed as an irreversible step that allows former collective farm members to begin farming on their own. It must be quickly followed by the issuance of registered land titles that define the specific parcel of each owner. Property is distributed immediately after the tender.

- All debts of 836 collective farms were restructured and these farms were liquidated, thus allowing new enterprises to start without the burden of the huge debt incurred by the collectives and eliminating any chance of the collective reconstituting itself. (Farms that didn't finish debt restructuring in 2000, due to the delay in conducting tenders because maps were late or due to delays by the Republican Commission, finished the process in 2001).

**Farm Sizes:**

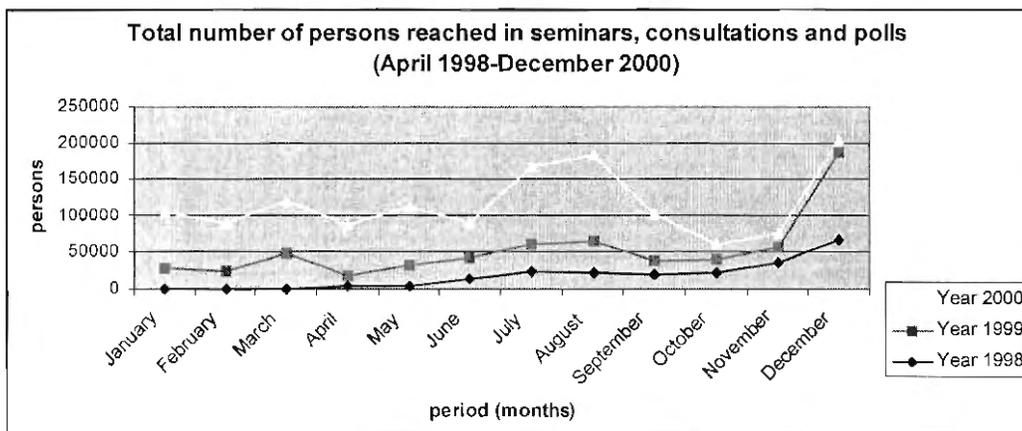
- The resulting private farms vary in size. and polls show that 77% of beneficiaries of privatization chose to lease their land to entrepreneurs who form larger farms, while the people chose to farm the land themselves, usually farming their land together with family members or neighbors. Data<sup>10</sup> showed that there was a range of farm sizes:
  - 41.2% of the new farms are over 500 size;
  - 27.5% of the farms are between 100-499 in size;
  - 6.2% of the new farms are between 1-99 in size; and
  - 25.1% of the farms are managed by farming individually, with family or neighbors, in varying sizes.



Data<sup>9</sup> land leader-23% of range ha in 499 ha 99 ha people

**Seminars/Consultations/Problems Solved:**

An average of 25 seminars was held on each farm, teaching farm members and local authorities their rights, responsibilities and options. These seminars were the primary means (along with handouts) that led, motivated and pushed each farm through the hundreds of steps.



- In total, face-to-face interactions occurred 1,392,935 times through seminars, polls or consultations with beneficiaries of land and/or property.
- 14,991 seminars were held, reaching 1,128,520 attendees on 34 different topics. Manuals and 77 different handouts were used. A bi-weekly advertising and legal advice newsletter, AgroMakler,

<sup>9</sup> CPBR/EWMI maintained a database with relevant information throughout the program, and conducted polls to supplement this data.

<sup>10</sup> Data from 822 farms that held land tenders or distributed land earlier.

circulated to 16,500. Individual consultations were offered for 108,286 people. 844 polls were conducted, questioning 45,198 people.

- Arbitration was instituted as a way of settling disputes: 136 cases were solved in one year for 19,471 participants. (Arbitration was initiated in Dec. 1999, once people had been farming on their own for one season, and disputes had arisen that mediation could not resolve. Prior to and parallel to this, CPBR used mediation to solve nearly all disputes.)

### **3.2 Land market development**

In view of the high density of the rural population, the land privatization scheme adopted in the Republic of Moldova resulted in the fact that the land parcels transferred to the individuals' private ownership are relatively small (1.5 ha, as an average). This fact served as a ground for the agrarian reform opponents to say that the land split into small parcels (land fragmentation) is the cause of collapse in the agrarian sector because it was impossible to organize highly efficient production based on modern machinery and technology on such small parcels. In this connection, the currently ruling party (Communist Party) tries to change the Land Code ensuring quick land consolidation through administrative methods. However, practice shows that small size of parcels in the individuals' private ownership is no obstacle in organizing large-scale production. Land consolidation is unfolding based on market mechanisms and primarily on lease relations and sale/purchase of land.

The study undertaken by the Center for Strategic Studies and Reforms (CSSR) in 2001 on the initiative of the Private Farmers Assistance Program<sup>11</sup> (PFAP) shows that at the given moment lease serves as the major factor for land consolidation. The average size of farms functioning on the leased land basis is equal to 680 hectares, some of them being over 2000 hectares.

The findings of the study reveal that 74.7% lessees are people engaged in different activities. The percentage of pensioners is equal to 20.6%.

People having up to 3 ha of land split into 4-8 parcels are involved in lease relations to the most. The land lease agreements are concluded in two forms: written and oral. The survey data shows that majority of lease agreements (91.7%) is concluded in the written form. The remaining part of agreements exists in the oral form.

Two bodies register agreements: primarias – 82.3%, and (should the land lease agreement be over 3 years) the National Land Cadastre. The remaining 15% are not registered.

The study shows that land lease agreement practice bases on short-terms of 1-3 years (86.2%). An 11.4% group of up-to-five-year agreements can be singled out. The situation of instability and uncertainty in the sphere of agrarian relations keeps a check on the negotiation of longer-term agreements, which is a large obstacle for the investments in the agrarian sector. Based on the CSSR survey data, only 20.4% of lessees consider the up-to-three year agreements as optimal. 79.6% of them consider that the optimal term is over 5 years. The best lease term to 64.6% of lessees' opinion is 5-10 years.

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<sup>11</sup> PFAP was launched in January 2001 to provide post-privatization assistance to landowners and rural based private entrepreneurs after the completion of mass privatization within the National Land Program. PFAP is designed for three years and is financed/implemented by USAID/EWMI/Soros Foundation Moldova. See also next chapter.

Land lease agreements are concluded based on two lease payment forms: the fixed one – 59.3% and as percentage of the gross harvest – 34.5%. The mixed form is equal to 6.2%.

The survey shows that employees of agricultural enterprises are satisfied with the conditions set in the agreements more than other categories of lessors – 87.5%, while the percentage of pensioners is equal to 73%. The major reasons for lessors' dissatisfaction with the terms of agreements are: low lease payment – 90.3%; late payments – 3.7%; non-observance of the agreement terms. – 4.6% and poor cultivation of land – 1.4%.

The size of per hectare lease payment varies from 20 to 70 US dollars. Considerable variation in payments is mainly explained by the farm specialization. As a rule, the highest lease payment is in the farms growing tobacco, vegetables and grape.

Based on the survey, the lease perspectives look as follows: 79.4% lessors will continue their lease agreements in future, 3.2% lessors are satisfied with lease in principle, but intend to continue it after transferring land to another leader. Only 6.4% lessors plan to terminate their lease agreements and farm the land by themselves. The lessees' plans related to lease and the form of land use for the future are somewhat different. Majority of them intends to continue lease relations (73.3%), while 16.8% lessees plan to purchase land.

Thus, we can make a conclusion that there is no need to introduce administrative measures aimed at land consolidation but it is advisable to develop further on and strengthen the market mechanisms that have already started functioning: agricultural land lease, and its sale and purchase.

The right to buy and sell land, introduced in Moldova in 1997 by the *Law on land normative price and procedures for buying and selling land* was another important factor that has a significant impact on agricultural land consolidation.

In the Republic of Moldova the owner itself has the right for selling the land in the private ownership. Agricultural land can be sold only to the citizens of the Republic.

The land sale/purchase procedure is as follows:

1. Based on the law, the land seller must obtain an extract from the Real Estate Registry.
2. The parties draw up a land sale/purchase agreement. The agreement indicates:
  - ID data of the seller and buyer;
  - The parcel and its location;
  - Sale price of land (agreed between the seller and the buyer).
3. The sale/purchase agreement is certified by the notary. The parties sign 3 copies of the sale/purchase agreement. Within 3 months after the notarization date, the buyer must register the land and the ownership right for it in the Real Estate Registry of the territorial agency serving the territory where the land parcel is located. For this purpose, the buyer must present the following documents in the territorial cadastral agency:
  - Application for the ownership right registration;
  - Copy of the land sale/purchase agreement.

As we see, the procedure of preparation of documents for obtaining the right of private ownership over the land is not complicated. Registration of the ownership right in the territorial cadastral agency takes 3-7 days.

The data from the State Agency for Cadastre, Land Resources and Geodesy shows that 103306 land sale/purchase transactions were performed in the rural area throughout years 1999-2001, including 72849 of those performed in year 2001. The remaining part of transactions includes donation, inheritance and household land parcels. Mortgage is equal to 12030 transactions. 36328 out of the total number of transactions are related to agricultural land including 24625 of those performed in 2001. The average size of one transaction is 0.4 ha. The weighed average price of 1 ha of agricultural land was equal to 228 US dollars in 2000 and 233 US dollars in 2001.

### 3.3 Land registration system

The land reform promotion in the Republic of Moldova has also generated the need to create an efficient infrastructure for the registration of the private ownership right for land and other real estate objects. In relation to that, on December 22, 1992 the *Law on state regulation of land ownership relations, state land cadastre and land monitoring* was adopted. However, the first specific steps in the foundation of the National Cadastre included the creation of Interdepartmental Council for the coordination of National Cadastre activities (Decision of the Government No. 22 of 15.01.96) and approval of the Concept Paper on the development of the National Cadastre system (Decision of the Government No. 794 of 19.08.97).

**The National Cadastre Concept.** According to this Concept, the National Cadastre represents a state information system which contains data on the land estate, as well as the real estate objects located on the respective territories and the rights related to the latter, and that also includes the legal cadastre, tax cadastre and specialized cadastre (land cadastre, urban cadastre, forest land cadastre, etc.).

During the first stage (1997-2002), the Concept envisaged the performance of activities related to the implementation of the legal cadastre project on the urbanized territories. During the second stage (2002-2007), it was envisaged to create the legal and tax cadastres, and specialized cadastres, as well as to complete the process of land empowerment of citizens.

The State Program for the creation of the real estate fund (creation – means a complex of measures for the separation of the real estate object as an independent legal object) and the organizational measures for its implementation were approved through the Government Decision No. 1030 of 12.10.98 “On some measures for the creation of the real estate cadastre”.

To ensure the implementation of this Program the Law on the Real Estate Cadastre (of 25.02.98) was passed and the Regulations on the creation of the real estate fund (Decision of the Government No. 61 of 29.01.99) was approved.

**National Cadastre creation.** The structure of cadastral bodies system in the country includes the State Agency for Land Relations and Cadastre within the Government of Moldova, territorial cadastre offices and the Central “Cadastre” Information Office (subordinated to the Agency). At present, there are 12 territorial cadastral offices and 26 branch offices functioning throughout the country.

Territorial cadastre offices are involved in the development and update of territorial cadastre plans, preparation of real estate cadastre files, registration of the rights over real estate objects and performance of other powers related to this. According to the law, the land, capital constructions, blocks of flats and other isolated premises (buildings), the right to renting the real estate for a period

exceeding three years, mortgage and other types of encumbrances, as well as other types of real estate and the right over such or the patrimonial titles established by the law shall be mandatorily registered in the cadastral registry by the territorial cadastre offices.

**First registration results.** According to the situation as of January 1, 2002, the cadastral offices have registered the creation of 3 098 thousand of real estate objects, including 2 703 thousand of agricultural lands and 233 thousand of household plots.

A total of 208 thousand transactions, including 103 thousand transactions involving agricultural lands and 31 thousand household plots transactions have been registered over the same period. Out of these transactions, 36 thousand are agricultural land sale transactions and 16 thousand are household plots' sale transactions. At the same time, there were registered 6 thousand of agricultural land mortgage cases and 1.5 thousand cases of household plots' mortgage cases.

Registration of real estate is an open process and information on registrations made (except for the real estate objects, data on which is regarded as state secret) shall be presented to any physical or legal entity requesting it. The Government sets the fee to be paid for delivery of such information. Public authorities, law enforcement bodies, as well as other state institutions can also be users of such information.

The aforementioned data shows that the real estate market, including on land estate, becomes an important factor in the market economic relations of the republic.

### **3.4 Mechanisms for settling land and property disputes**

Over one million participants in new civil and legal relations have appeared over the four-year process of privatization in agricultural and namely: owners of land parcels and privatized property and tens of thousands of new private enterprises many of which became land and/or property lessees (over 0.5 million lease agreements). These objective changes generated the appearance of different types of disputes.

Mass training for landowners and rural entrepreneurs (seminars, publications), as well as individual consultations are the main ways for preventing and settling the majority of disputes. However, some disputes remain unsettled due to certain reasons. According to art. 6 of the Civil Code, civil and legal dispute settlement is the responsibility of the court or the court of arbitration (arbitration). The court examination procedure of the mentioned disputes oftentimes restricts the possibility for protecting the violated rights (considerable court fees, high lawyers' fees and other unavoidable expenses that often exceed the claimed amount; slow procedures caused by the courts overloaded with many pending cases; lack of judicial precedence in the examination of such disputes). Application of arbitration as an optional procedure for settling these disputes allows to avoid this kind of obstacles, expands people's access to the protection of their legal rights and interests, helps to raise people's legal awareness and to preserve a favorable social environment.

Major legislative prerequisites for the creation and activity of the arbitration are determined in the *Law on the Court of Arbitration (Arbitration) No 129-XIII of 31.05.94* based on which the arbitration may have both general and specialized responsibilities. From the logistic point of view, the law provides for two types of arbitrations:

- Permanent arbitration is not created as a separate legal entity and exists under registered chambers of commerce, exchanges and other agencies. In this case, the list of arbitrators, the rules of dispute examination, the size of arbitration fees and so on are approved by the respective agency. In Moldova, permanent arbitration functions under a number of agencies including those from the agrarian sector (under NGOs funded by the Government of Great Britain).
- Ad-hoc arbitration is usually created by the parties in the dispute for the purpose of examining some specific disputes. In this case, a concrete list of arbitrators, the rules of dispute examination, arbitration charges, etc. are approved by the parties in the dispute themselves. Ad-hoc arbitration in Moldova is used only within the framework of our Program (as far as we know).

With the exception of logistic type of differences, the principles of these two types of arbitrations are identical and namely: · Mandatory prerequisite for the dispute examination by the arbitration is the written consent of the parties in the dispute (arbitration clause in the contract or separation arbitration agreement). · Compulsory execution of the arbitrators' decision taken as part of the civil court proceeding. · Restricted grounds for re-examination (annulment) by the court of the arbitrators' decision or refusal to execute it.

Application of the ad-hoc arbitration for examination of disputes arising in the agrarian sector started at the end of 1999 under the framework of the former National Land Program and continues in PFAP. The results of this procedure applied in 1999-2001 are as follows (in brief): · 500 disputes examined involving the interests of 60000 persons; · over 30% disputes settled at the preliminary stage resulting in the preparation of documents on the dispute settlement terms; · over 60% disputes examined at the arbitration hearings resulting in compromise agreements signed by the parties; · 11% disputes examined at the arbitration hearings resulting in arbitrators' decisions; · over 90% compromise agreements and arbitrators' decisions voluntarily executed by the parties in the dispute within the deadlines fixed in the arbitrators' decisions or within reasonable time.

The disputes examined can be subdivided into two main categories:

- Land disputes: land lease agreement termination; compensation for the land cultivation costs to the lessee; compensation to the owner of the value of the unfinished production allocated as part of the property share during the privatization process if it was used by the lessee (sowing, plowing, etc.);
- Disputes between owners of the privatized property (separation of property share out of the jointly owned property; withdrawal of smaller groups of owners).

About 50 potential arbitrators, i.e. specially trained PFAP consultants (lawyers, economists, agronomists and accountants) examine the disputes. Dispute examination is organized in all 10 PFAP regional centers, i.e. the entire country is covered. Most of the time, disputes are examined at the location where the parties reside.

Dispute examination via arbitration in principle and via ad-hoc arbitration in particular is complicated by the poorly developed legislative basis on arbitration in Moldova, the novelty of this procedure for the agrarian sector as well as the novelty and complexity of the appearing disputes. In this situation, it is especially important to ensure permanent and qualified control over dispute examination in order to avoid violation of legal rights and interests of citizens and avoidance of conflicts with courts. But it is even more important to direct all efforts at supporting the prestige of the arbitration as an institution with ancient traditions well known and widely used in the world practice.

## 4. MAJOR DIRECTIONS OF THE POST-PRIVATIZATION PERIOD

Mass privatization of the former collective farm land and property within the National Land Program resulted in the appearance of hundreds of thousands of economic entities engaged in agricultural production based on the private ownership. This fact brought about the need for creation of a special post-privatization program that would include the improvement of the existing and development of the new legislative basis regulating the activity of the new economic enterprises and economic relations in the market environment; development of the market infrastructure (primarily in the sphere of marketing as well as material and technical resource supplies); technical, veterinary and agrochemical servicing; consulting and information support. It also was very important to organize mass training of the new owners on the fundamentals of entrepreneurship, legislative basis of the Republic of Moldova and new technologies of agricultural goods production.

### 4.1 The Private Farmers Assistance Program

The Private Farmers Assistance Program (PFAP) was launched in January 2001 to provide post-privatization assistance to private farmers and rural entrepreneurs in Moldova. Under PFAP, farmers and rural entrepreneurs, as well as rural associations and NGOs obtain support and assistance to help the Moldovan agricultural sector recover and grow. The program is designed for three years with joint funding by USAID (75%) and EWMI/Soros Foundation (25%). The program is implemented in partnership with the Soros Foundation Moldova and in close collaboration with local NGOs. In year 2001 more than 50 local organizations/NGOs contributed directly to the achievement of the Program's goals and objectives.

The **goal** of PFAP is to contribute to the business success of private farmers in order *to ensure that the transition to private farms results in sustainable economic growth*. It is also envisioned that as a result of the PFAP, a network of institutions (NGOs or commercial consulting firms) will be strengthened to provide continuing support to private farmers and enterprises in rural communities throughout Moldova.

PFAP achieves its goal through activities in three strategic areas. These components and the main tactics within each strategic component are:

**Development of a sound legal and regulatory environment.** The goal of this component is to eliminate legal and regulatory impediments to the further development of private farmers and entrepreneurs (as recommended by a EWMI/CARANA study, 1999) and, where appropriate, draft new laws and regulations that will create an enabling environment for private farmers and entrepreneurs. It is also proposed to trouble-shoot proposed laws/regulations to preclude enactment of laws and regulations that may expand government control and thereby increase business costs and uncertainty. PFAP carries out evaluation studies and surveys to determine baselines and measure the impact of PFAP activities as the program evolves.

In year 2001, 82 legislative and normative acts were developed and two sociological surveys were undertaken.

**Development of rural enterprises, including farmer cooperatives and producer associations.** The goal of this component is to develop multiple ownership enterprises and organizations that purchase farm products, supply farm inputs or services with an emphasis on the forming of business

cooperatives. This activity works to form new enterprises and strengthen the existing enterprises on an ongoing basis focusing on agriculturally related businesses. PFAP initiates meetings of prospective founders of new enterprises, introducing them to basic concepts and options. PFAP examines the existing and new enterprises/groups as potential beneficiaries of PFAP, and provides appropriate assistance to them. PFAP develops individualized plans for each target enterprise, and tracks its progress; coaches rural entrepreneurs in obtaining financial assistance from various sources. Lastly, PFAP trains enterprises in ways that will help them succeed in topics such as basic bookkeeping, tax information, etc. Work is linked to other organizations and projects, such as the Moldovan Microfinance Alliance, to assist in strengthening of more than 200 Savings and Credit Associations and to create new ones. Certain groups assisted under PFAP are also eligible for *grants* (e.g. start-up grants) in combination with the technical assistance provided. The goal of the Grant activity is to strategically assist in the development of rural enterprises/organizations through the use of grants targeted at key areas or enterprises.

In the year 2001, 80 western type business cooperatives were created. 5,738 rural entrepreneurs were registered as members of business cooperatives and/or producers' associations. 180 Savings and Credit Associations were created/strengthened, and 17,000 loans (worth about \$3 million) were provided to rural producers. Ten business centers were created on the PFAP grant basis under the regional Agricultural Producers Associations.

**Landowner legal assistance and information support.** This component includes providing legal assistance to help ensure the protection of the landowners' rights, and improving the information provided to farmers throughout Moldova by continuing publications to help farmers buy inputs and sell products, gain information about their rights and development of their farms. Legal assistance is provided through regional offices in form of consultations, seminars, problem solving, arbitration and, where needed, assistance in courts. It is recognized that the general population's understanding of new laws, regulations and how to conduct business, will also drive the success of PFAP. The program mounts mass communication campaigns based on training seminars and published materials about new laws and regulations such as the cooperative law to reach the rural client base. Assistance covers such areas as landowners' disputes with lessees, property shareowners' desire to separate from a previous agreed-upon grouping; land or property inheritance, etc. In the field training seminars on targeted topics (legal issues, accounting, taxation, business planning, marketing, etc) are offered to targeted audiences. Publications (periodicals, manuals, handouts, web site) support all PFAP activities.

In year 2001, 142 publications were issued and disseminated among farmers. Over 400 disputes, involving 65,000 individuals and rural businesses were resolved through arbitration. Over 140 thousand rural residents participated in the seminars organized by PFAP, and more than 395,000 people received consultations. Rural entrepreneurs and landowners received PFAP assistance in form of legal and logistical advice in 69 economic disputes in courts.

PFAP pays special attention to **encouragement of women** in agriculture and rural enterprise development, with the hope that women as well as men, are be part of the development of commercially viable business activities. This goal is integrated into *all activities* to ensure full participation of women in all programs. Work continues to ensure women are aware of the availability of all types of assistance under PFAP and fully benefit from the program.

Through PFAP Grant program, groups of business entities wishing to create or strengthen their existing farmer cooperative, producers association, etc. that fit the eligibility criteria apply for grants, thus

becoming a **primary beneficiary** of the PFAP grant program. Financial assistance to primary beneficiaries is provided to accomplish two different objectives: business development and business support. *Business development* assistance helps to start-up operations of a new business (e.g. cooperative, farmer association, etc. such as training the board of directors or cooperative governance) or to develop a new product, new service, etc. *Business support* grants assist a business to improve an existing product, service or aspect of its management. Primary beneficiaries are the farmer-owned businesses (including farmers themselves), agribusiness (processing, farm supply, machinery services, etc.), service or cooperatives and producer associations that primarily are needed by farmers to directly improve their farming business and therefore incomes. Other organizations (primarily NGOs) wishing to collaborate with PFAP in achieving its goals and objectives are eligible for PFAP grants and are encouraged to become **secondary beneficiaries** of the PFAP. This type of financial assistance to improve or provide services needed by PFAP primary beneficiaries under PFAP goals and objectives is primarily directed toward service-type organizations including Moldovan NGOs, trade associations and selected enterprises or village-level support groups.

In year 2001 56 organizations successfully participated in the PFAP Grant Program and obtained grants from PFAP totaling at \$938,000.

#### 4.2 Agrarian sector crediting system development

One of the biggest difficulties encountered by Moldovan farmers is lack of funds needed for successful business and its expansion via purchase of new land. Commercial banks extend credits at rather high interest. At the same time, the usual repayment period of such credits is 3-6 months, which is obviously insufficient for agriculture with its year's technological cycle. Besides, the procedure of obtaining credits via commercial banks is very bureaucratic. This fact requires development and implementation of special programs for crediting farmers. The Mortgage Lending Program (MLP) implemented in Moldova with the USAID support is one of such programs.

The program aims to promote medium term affordable credit to farmers for the purchase and consolidation of land, thereby increasing investment in Moldovan agriculture. The immediate objectives are:

- To instruct Savings and Credit Associations (SCAs) on all aspects of mortgage lending allowing them to offer a new financial product to their members that will generate investment in agriculture.
- To assist farmers prepare business plans and teach them to use the plans to make informed business decisions.
- To give farmers experience with secured loans and the opportunity to establish a positive credit history that they can use in the future when seeking larger loans from commercial banks.

To participate in the program, an SCA must meet certain criteria designed to minimize the risk of problem and bad loans that might jeopardize the viability of the SCA. The requirements for the SCA are to:

- Be a shareholder of the Rural Finance Corporation (RFC).
- Be located in a village or commune where entitled individuals have received their land titles under the National Land Program or some previous privatization effort of the Government.
- Have a minimum of two members who have already negotiated with sellers and agreed to purchase their land.

- Be operating for at least two years.
- Be current on loans outstanding to the RFC or any other financial institution.
- Have conscientious, responsible management that keeps accurate records and uses acceptable accounting practices.
- Be sufficiently capitalized to absorb potential defaults on mortgage loans.
- Be willing to make medium term loans within the guidelines established by the program.
- Be willing to undergo the mortgage lending training course.

Due to the limited amount of funds available to operate the SCA Mortgage Lending Program, it is important that an SCA adhere to the program requirements. An SCA that fails to follow the requirements may be placed on probation or, in case of more serious violations of program requirements, be excluded from the program.

An SCA may be placed on Probation for the following reasons:

- Failure to market the program within its established service area.
- Failure to disburse at least two loans within three months from inclusion in the Program.
- Failure to disburse at least one loan every three months, after disbursing the initial two loans.
- Failure to follow the loan policy, loan evaluation guidelines, or loan documentation requirements stated in the SCA policy, SCA laws, RFC guidelines and this Manual.

An SCA may be excluded from the program for the following reasons:

- Continued violation of program requirements after being placed on probation.
- Performing an illegal act related to the use of program funds, funds provided under other lending programs, shareholder funds, or engaging in other unscrupulous activity.

This program started in April 2000 by the Citizen Network for Foreign Affairs (CNFA). The initial funding for this program was US\$40,000. The program was extremely successful: the entire US\$40,000 fund was disbursed in less than 9 months, resulting in approximately US\$1,400. The average size of the purchased agricultural land approximates 3.36 hectares.

The loan repayment ratio is very good with 28 loans being classified as current and one loan paid-off. There are no defaults. The intensive technical assistance that CNFA supplied to both the participating SCA and the borrowers has largely contributed to achieving this strong record. CNFA considers this program successful with demand for this type of loans far outstripping the available resources. In the pilot program, CNFA worked with just 6 SCAs because of the very limited funds made available to test the program. Today, there are over 300 SCAs in Moldova and they desperately need resources (reasonable-cost funds) to lend to their members to buy additional land. There is a real potential for expansion of this program and CNFA has submitted operation plan amendments to USDA requesting approval for expansion of the original fund.

### Loan Portfolio:

At the end of the reporting period, the number of funded loans totals 98 loans in the amount of US\$1,039,709 (the exchange rate: US\$1.00 = 13.0909 Moldovan lei). The table below shows the overall performance of the loan portfolio.

Investment categories	Number of loans	Disbursed Loans (USD)			Loan reimburs. (USD)	Outstand. balance (USD)
		CNFA contrib.	Local partner contrib.	Total amount		

PFCF at Agroindbank	46	189,826	189,826	379,652	209,000	170,652
PFCF at Fincombank	21	107,484	107,484	214,968	41,320	173,648
Direct loan to CODRU – 16 tractors	1	352,775	0	352,775	329,086	23,689
Direct loan to REZON – 1 combine	1	54,326	0	54,326	13,581	40,745
PFC loans – small land purchase loans	29	37,988	0	37,988	0	37,988
<b>Total Loans</b>	<b>98</b>	<b>742,399</b>	<b>297,310</b>	<b>1,039,709</b>	<b>592,987</b>	<b>446,722</b>

The loan summary shows that 91 loans are current (i.e. 93%), 7 have been repaid in full and 4 loans are past due. This strong record can be partially attributed to the fact that CNFA and its banking partners have provided assistance to farmers in preparing business plans and loan applications.

## 5. CONCLUSIONS AND PROPOSALS

Republic of Moldova is one the first CIS countries having adopted the legislative basis that allowed introduction of the private land ownership institution and complete reorganization and privatization of collective and state agricultural enterprises.

There was a long break between the approval of the legislative basis for the agrarian reform (1992) and the start of mass privatization of land and reorganization of agricultural enterprises (1997). As a result of chaotic privatization process, a considerable part of agricultural material and technical basis was ruined which caused considerable problems of financial and technical nature for the new enterprises created as an outcome of mass privatization.

In spite of this fact, the Republic of Moldova was one of the first CIS countries to have successfully implemented the land reform; reorganized collective and state enterprises into the new type ones based on the private ownership of land and property; restructured the debts of the agrarian sector to the state and private creditors; launched market mechanisms of agricultural land consolidation through the land parcel sale/purchase and lease. This was achieved due to the following circumstances:

- **The project was based on existing Moldovan laws on privatization**, not new laws written by foreigners. Only the methodology of “how to” privatize was elaborated. This too used a Moldovan source – Dr. Vasile Uzun, a Moldovan born expert (currently a Russian academician) had developed the ‘leader-entrepreneur’ concept.
- **Support for the project came from the highest levels of government.** This helped override interference of the mid-level local and central bureaucracies. When problems developed, the CPBR team was able to solve them with support from top officials (including the president).
- **The will of the people to receive land and property was strong.** Farm members demanded privatization. The first farmers in Nisporeni insisted that their collective farm be privatized, not restructured, as some first suggested. The collectives were failing and people realized that only by gaining ownership and running their own farms could the situation improve. And people remembered private farms -- collectivization was imposed on Moldova in 1948-49.
- **People were presented with options on how to use their land and property.** Dr. Uzun’s concept of the “leader-entrepreneur” who leases in land to form a larger farm was critical to the success of privatization in Moldova. This offered an **option** for people who didn’t want to physically farm their land – but leasing presented them with a source of income from that land. It also presented a way for the farmer who wanted to manage a larger farm to create one and thereby plant crops on larger fields, making use of equipment designed for that purpose. Pensioners composed almost half of an average farm (the average collective farm included 1000 beneficiaries to land or property). These people usually did not want to farm but needed some income as pensions were small (and often, were not paid).
- **Local experts made the program work.** The program depended on local Moldovan experts (working through local, not only Chisinau offices) to develop the methodology, to instruct villagers on their rights and choices and to solve problems. The NLP team included 260 professional Moldovan staff and only 2.5 expatriates (plus 1 additional expat in the final year). This was a Moldovan program, based on Moldovan laws, using Moldovans to promote the privatization methodology throughout the republic.

Based on the experience of the Republic of Moldova, the following recommendation of methodical and practical nature for all countries having joined the way of reorganization of the socialist type collective farm into the market oriented system can be made:

- Develop and implement solutions to the collective farm debt problem immediately. Assume the debt situation will be worse than the numbers appear.
- Keep all aspects of the privatization process and methodology linked together. Privatization – from the initial farm meeting, when CPBR specialists informed farm members about the basics of privatization, through the final liquidation of the farm – should not be separated from the surveying and titling. CPBR spent considerable time training farms in steps that were to be handled by surveyors (doing grouping and arranging, or distributing titles, for example) and the division meant that some farms received land titles (the biggest incentive to privatize) without completing property distribution.
- Develop special programs for different audiences. Halfway through the program, CPBR initiated seminars for pensioners or women only to ensure their full participation. While numbers had shown equal attendance of men/women/pensioners), it appeared pensioners and women needed a more concentrated effort to accept responsibility for their decisions.
- Use polling to monitor people's understanding. CPBR monitored people's understanding of privatization throughout the program. When more farms had entered the process, CPBR created a team specifically to poll farm members. This was extremely useful in both monitoring understanding and motivating farm members to participate. (For example, CPBR would delay a farm's land distribution tender if polls results showed a low level of understanding of how they should participate in the tender. Remedial training materials would be instituted to improve participation. The polling itself provided an opportunity for one-on-one explanations and motivation of farm members, as after the questionnaire was completed, the specialist would review steps the person had not understood.)
- Lastly, and most importantly: Stay true to the final goal: complete privatization of land and property, from providing all information to issuance of legal land titles and distribution of property necessary for farming. Twice CPBR, with USAID and the US Embassy, halted the program and presented a united position to the government: Either laws/regulations (or their implementation) change to allow complete privatization program or the program (and its funding) stops. The government listened, and as a result, laws were passed and implemented that allowed distribution of the critical property of the farms (the trees and vines on the land, tractors, combines, etc.) and resolved the farm debt problem.

**5 suggestions for future privatization projects:**

1. Develop solutions to collective farms' debts immediately
2. Keep all aspects of privatization linked together
3. Develop special programs for different audiences
4. Use polling to monitor people's understanding
5. Stay true to the final goal: complete privatization of land and property

The experience of the Republic of Moldova shows that the agrarian reform cannot consist in land privatization and collective and state agricultural enterprise reorganization only. It is necessary to immediately start the following stage including:

- creation of the market infrastructure in the agrarian sector and in particular in the western type agricultural business cooperative system producing marketing, technical and consulting services for farmers;

- holding an extensive information and training campaign among agricultural producers on legal, economic and technological issues;
- active involvement of non-governmental organizations in the agricultural reform process aimed at the strengthening of democratic principles in the approval of decisions on the local level;
- strengthening of the arbitration system as a major tool in the resolution of conflicts arising in the process of privatization and further economic activity of farmers.

All indicated problems in the Republic of Moldova are being successfully solved within the Private Farmers Assistance Program (PFAP) funded by USAID, EWMI and Soros Foundation Moldova.

For the speedy increase of the agrarian sector efficiency it is also necessary to develop the system for crediting agriculture both through commercial banks and through savings and credit associations. Specific attention should be also paid to the development of special social programs aimed at the support of small and middle business development process as well as creation of new work places in the non-agricultural sphere in the rural zone (development of small businesses on everyday services for the population, such as footwear, clothing and house utilities repair, laundry services, etc.).

**"Land market development and aspects of land consolidation in Ukraine"  
for the Regional Workshop on Land Issues in Central and Eastern Europe and the CIS**

**by Natalya Korchakova**  
**the Center for Land Reform Policy in Ukraine**  
**Kyiv, 2002**

**Summary**

This paper will cover land market development and aspects of land consolidation in Ukraine. Special attention will be given to the specific issues of:

- ◆ Land reform implementation;
- ◆ Problems confronting further land market development in Ukraine;
- ◆ Importance to Ukraine of land market development and land consolidation in the international context

**1. Background Information on Land Reform in Ukraine.**

The basis for implementing land reform in Ukraine is the Land Code adopted in 1990. The beginning of the land reform was officially announced in the Verkhovna Rada's (Ukrainian Parliament) Resolution "On Land Reform in Ukraine," where all lands of Ukraine were declared to be an object of the reform. The Resolution stated that the aims of the reform were to liquidate the state monopoly, and to create effective land management. The Resolution also called for the establishment of a special state body to be responsible for land reform and stated that the authority to implement land reform was to be delegated to the local councils (i.e., bodies of local self-government). The local councils were authorized to allocate land and to issue land titles to the new private landowners. The local councils were also authorized to keep the registry of rights to land and resolve land conflicts (Law of Ukraine "On Local Governments" dated May 21, 1997).

In accordance with the Resolution of the Verkhovna Rada, the State Committee of Ukraine on Land Resources was established in 1992 and empowered to oversee the implementation of land reform in Ukraine. Among the State Committee's tasks is to take part in developing and implementing measures to support the establishment of the land market, credit mechanisms, and an improved land taxation system (Regulations on the State Committee of Ukraine on Land Resources, Approved by the Decree of the President of Ukraine No. 970/2000 dated August 14, 2000)

Initially, the land reform was not aimed at establishing private ownership of land, but at redistributing the land by providing land to citizens under the right of permanent use (with the right to pass land by inheritance) and by providing land to collective and state agricultural enterprises under right of permanent use. But as early as 1992, the right to private ownership of land was mentioned in amendments to the Land Code, and in the Law of Ukraine " On forms of land

ownership" (January 30, 1992), which lists three forms of land ownership: private, collective, and state.

## **2. Land Reform Policies**

Despite the initial goal of land reform, Ukraine quickly adopted an overall land reform policy of establishing private ownership of land. Ukraine has undergone two stages of land reform and finds itself in a third stage now. During the period from 1991-2000, the first stage was characterized by the transfer of agricultural land from state to collective ownership, and then, following the abolition of the collective ownership of agricultural enterprises, the second stage was characterized by the transfer of land from collective to private ownership.

### **2.1. Demonopolization of the State's Ownership to Land and Establishment of Collective and Private Property (1991-1995)**

During this period, land owned by the state was transferred to collective ownership of the collective agricultural enterprises (as a legal entity) and its members (as physical persons). Additionally, the land reserve fund was established, normative monetary evaluation of land was carried out, and state acts to collective ownership were issued to the collective agricultural enterprises (CAE's). In 1992 the Law of Ukraine "On Collective Agricultural Enterprises" stipulated that each member of the CAE is entitled to receive a "share" of the collectively owned land in case the member elects to withdraw from the CAE. Thus, the concept of a "land share" appeared as part of Ukraine's land reform policy.

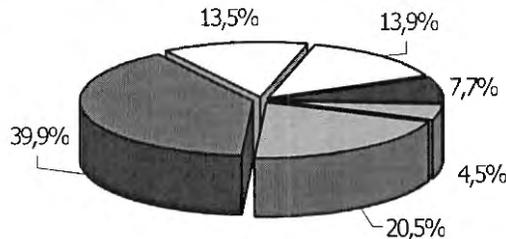
### **2.2. Land Sharing and Abolition of the Collective Ownership (1995-2000)**

During this second period, procedures for land sharing were established (as part of the Decree of the President of Ukraine "On Procedures for the Sharing of Lands Transferred into the Collective Ownership of Agricultural Enterprises" dated August 8, 1995). These procedures provided that the right to a land share would be certified by a land share certificate issued to the eligible member of the CAE. A land share certificate represented a nominal right to obtain a physical parcel of the CAE's collectively owned land. To receive the physical parcel of land, the CAE member was required to withdraw from the enterprise and apply to receive a land parcel in private ownership, with the parcel's borders demarcated and a land title issued.

Notably, the second period of Ukrainian land reform was ideologically ended with the adoption of the Decree of the President of Ukraine No. 1529 dated December 3, 1999 "**On Immediate Measures to Accelerate Reform of the Agrarian Sector of the Economy.**" This Decree is a revolutionary document, which promotes the withdrawal of CAE members with their land shares, abolishes the CAE's as legal structures, and requires the establishment of new market-orientated agricultural enterprises of different legal forms on the basis of the private land ownership. Since that date, of the 6.8 million former CAE members entitled to land shares, about 6.7 million (or 98 percent) have received their land share certificates. As of 2002, 11,606 CAE's (99,8 percent of the total) have been restructured into more than 17,692 market-orientated entities:

- ◆ Private enterprises -- 3638 (20,5 %),
- ◆ Ltd -- 7093 (39,9,0 %),
- ◆ Agricultural cooperatives -- 2403 (13,5%),
- ◆ Family farms -- 2471 (13,9%).
- ◆ Public companies -- 799 (4,5%)
- ◆ Legal entities of other forms -- 1374 (7,7%)

**New Legal Entities Formed on Basis of Former CAEs**



- Private Enterprises
- Ltd
- Agricultural Cooperatives
- Farmers
- Others
- Public Companies

### ◆ 2.3. Land Titles Issuance

Ukraine is now in the third stage of its land reform process – formalization of private ownership rights to land. After the Presidential Decree of 1999, the process of preparing and issuing land titles accelerated substantially. As of February 1, 2002, nearly 2,4 million land share holders have received land titles in exchange for their land shares, with an additional 1,2 million land titles in various stages of preparation. The establishment of private ownership of land and issuance of land titles has intensified entrepreneurial activity and led to the increase in the establishment of new private agricultural entities that makes more effective use of land. Ukrainian Government policy is to complete land title issuance as soon as possible. A land titling project financed by USAID and another one planned by the World Bank are aimed at assisting Ukraine through this stage and forward toward a functioning land market.

### 2.4. Current Situation and Future Policies.

On March 11, 2002, during the All-Ukrainian Meeting on Agricultural Sector Post-Reform Development, the President of Ukraine summarized the accomplishments in agricultural sector development, the current problems, and future perspectives. He stated that Ukraine has made visible progress over the last three years, and in the current year that the agricultural sector has developed more than the industrial sector. For example, the collection of Value Added Taxes in the agricultural sector increased 9.7 percent in this year January 2002, while collection of VAT in the Ukrainian economy as a whole increased 3.2 percent.

The table below shows how agricultural land use has changed over time, largely as a result of land privatization, in favor of the new forms of market-oriented enterprises and private farmers.

<b>Land Users</b>	<b>1994, thousands of hectares</b>	<b>2002 thousands of hectares</b>
Collective Agricultural Enterprises	25,726.5	685.2
Agricultural Cooperatives	105.5	4,161.8
Public Companies - (Partnerships)	213.5	14,536.3
Private Farmers	619.1	2,796.5
Land in private property of the physical persons (subsidiary plots included)	5,011.2	12,958.6
Land in the Reserve Fund	3,353.9	3,726.5
Land of Public Use	2,192.1	3,655.6

Ukraine has developed a policy approved by the Decree of the President on May 30, 2001 which sets out the main directions of land reform for 2001-2005. The main goals of the state policy are:

- ◆ further development of private ownership to land;
- ◆ improvement of land relations in the agricultural sector ;
- ◆ development of the land market and its efficient functioning;
- ◆ improvement of the state's management of land resources; and
- ◆ improvement of the legal framework governing land relations.
- ◆ the new policy also cites the development of land financing mechanisms and the ability to use land as collateral as key areas of concentration.

This Policy foresees two stages of implementation: the first stage (2001-2002) envisions the implementation of legal, organizational, informational, and technical measures necessary to entrench the land reform implemented in the past and to form a stable legal and economic base necessary for the implementation of the second stage. The second stage (2003-2005) envisions optimization of land use and strengthening the system of land protection.

### **3.Land fragmentation and land consolidation in terms of land market development in Ukraine**

#### **3.1. Land Fragmentation as a Result of Land Privatization**

The first step in the process of land market formation was breaking up of the state monopoly to land and land privatization. This step includes parceling of land, preparation and issuance of legal documents confirming the right to land and formal establishment of private ownership rights. As a result of these activities, the fragmentation of land occurs: the ownership of collective land is subdivided into private ownership of many individuals and the lands from the state reserve funds are subdivided into subsidiary plots to be given to citizens. As a result of land privatization, the number of the land owners and land parcels in private ownership dramatically increased. This process leads to the development of a land market infrastructure; each parcel should be properly surveyed and registered with specialists, including surveyors, notaries, and lawyers employed.

Private land owners begin searching for information on land rights and how to use the land in the most effective way, as well as business opportunities. Thus, the necessary base for the development of a functioning land market begins to appear.

### 3.2.Consolidation of Land Use

This step represents a reallocation of land to those that can use it most efficiently. Such reallocation facilitates land market development. Once property rights of private individuals are established, there is a natural tendency to use the land more effectively. The landowners learn how to exercise their legal rights under which land can be transferred, inherited, or exchanged. The adoption in 2001 of the new Land Code represents significant progress in establishing the legal base under which land consolidation in private hands can occur. The Land Code permits unlimited land consolidation by means of lease and ownership is unlimited (with one exception on the size of agricultural land owned by one citizen valid till 2010 - see the table below) Foreigners may lease land in Ukraine, however the Land Code does not allow a foreigner to own agricultural land.

As a result of land consolidation occurring through different means, the legal mechanisms of the land market begin to function (e.g., lease contracts, transfer of rights to land through inheritance, etc.). Land owners begin to seek new opportunities to increase the land's value. As farmers realize the limitations to leasehold arrangements and begin to consider more capital investments in the land, sale and purchase will occur (after the moratorium on sale and purchase expires in January 2005). Land owners will consolidate land in order to invest their capital in the most profitable way, and to transfer their rights to land if they cannot use it in a profitable manner.

The following table shows the differences between the old and new Land Code's in terms of some limitations on private ownership rights.

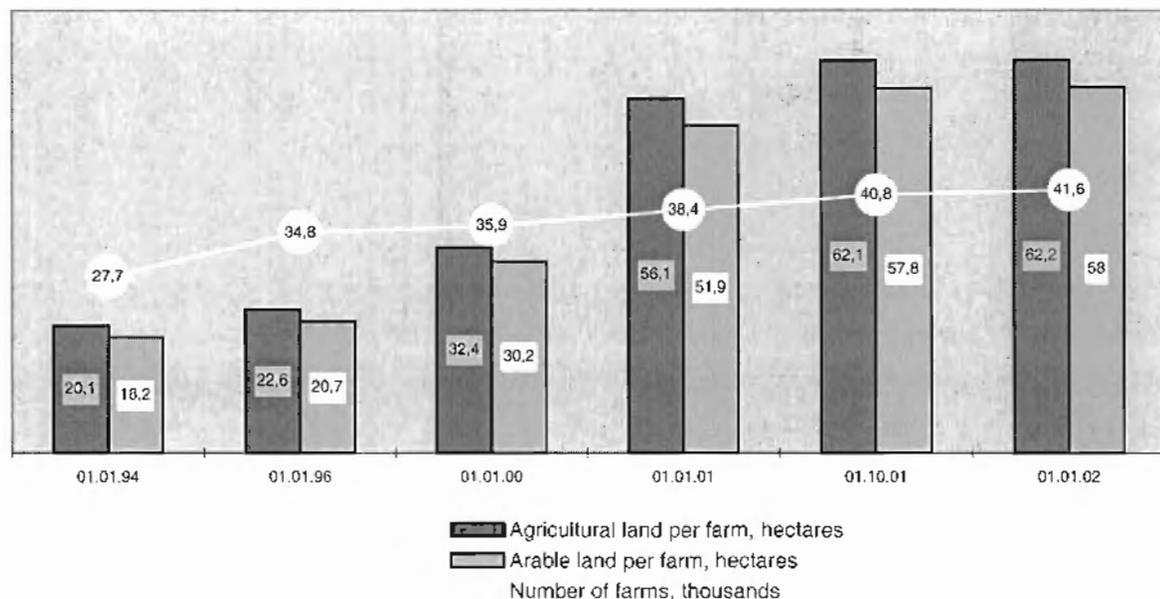
**Table 1.Limitations on Private Ownership Rights to Land – Old vs. New Land Codes**

Old Land Code		New Land Code
The size of land in private land ownership is limited		Size of land in private ownership is not limited. <i>Note: Transitional provisions of the new Land Code valid until 2010 restrict the size of a parcel of agricultural land that one individual may own to 100 hectares or less.</i>
Private farms	No more than 100 hectares in total (no more than 50 hectares of arable land)	
Subsidiary plots	Average size 0,6 hectares, but could be increased to 1 hectare. As an exception, no more than 2 hectares under a special permit from the local government body	
Orchards and olericulture	Average size 0.12 - 0.15 hectares	
Pastures	Average 1.0 hectares	
For dacha building	Average 0.1 hectares	

### 3.2.1. Land Lease

Land consolidation in Ukraine is occurring mainly through leases and the development of a land lease market. The land owners begin to exercise their legal rights by entering into leasehold arrangements with agricultural entities and entrepreneurs and obtaining income from leasing of land. An active land lease market already exists in Ukraine and land lease payments are considered a valuable source of additional income to rural households. The average annual lease fee is 93.1 UAH per 1.0 hectare. However, land leasing consolidates land in a temporary manner and land use patterns are likely to change because of the temporary nature of leases. Since the land lease contracts tend to be short-term, there are few incentives for lessees to effectively use the land and make long-term investments (e.g., land protection & melioration systems). Only land owners or long-term lessees are typically concerned about the sustainability of the land as resource that brings a permanent income, the environmental care of land, and protection of soil fertility. In January 2002, once the moratorium on land sale and purchase of agricultural land expires, consolidation of land should occur in a more permanent manner, as private farmers purchase land from passive landowners and others who wish to sell their agricultural land.

As can be seen from the diagram below, along with an increase in the number of private farms since 1994, an increase in farm size is noticeable. In 1994 the average private farm used 20.1 hectares of land. In January 2002, the average size of a private farm has reached 41.6 hectares, showing steady land consolidation in the hands of private farmers. These farmers show their intention to continue increasing their land holdings by increasing their capacity to manage bigger land parcels while maintaining high levels of productivity. The consolidation of land into private hands over this period of time has occurred mainly through leasing and purchasing land from the state.



Year	Number of registered farms	Agricultural Land in Use, thousands of hectares	Average of agricultural land per farm
January 1, 2001	38428	2157,6	56,1
January 1, 2002	41599	2585,8	62,2

### 3.2.2. Land Sales & Purchases

Land sale and purchase is a direct means for land reallocation, the prerequisites are already established in Ukraine. Nevertheless, Ukrainian society holds the fears that agricultural land, once it is subject to sale, would immediately be consolidated into the hands of latifundists under non-transparent procedures and artificially low prices. Such fears are so strong, that the new Land Code sets a moratorium on sale and purchase of agricultural land until January 2005, to avoid the perceived unfair land consolidation until market conditions are established and landowners better understand their rights. At the same time, there is a clear understanding that the investment in the land is less likely to occur before land consolidation of a more permanent nature can occur. The moratorium is a compromise, a sort of "time- out" needed in Ukraine to create a system under which the land market can function.

The following figures on land transactions show the very limited number of rights transfers between private owners. In total, there were registered 553,937 transfers of private land ownership conducted the basis of notarized contracts since 1995:

- ◆ Bequest – 448,179 (80,9 %)
- ◆ Granted – 92,411 (16,7%)
- ◆ Exchanged – 762 ( 0,1%)
- ◆ Sale – 12,585 (2,3 %) Note: these occurred before new Land Code was enacted.

### 3.2.3. Land Plot Exchange

While the sale and purchase of agricultural land is currently forbidden, the exchange of land parcels is allowed, which serves as one tool for the reallocation of land during the moratorium period. However, this manner of transfer is already criticized widely under the claims that it leads to hidden land transactions employing non-transparent mechanisms, to the failure of new owners to pay land taxes, to the failure of parties to register such exchanges, etc. Only properly executed exchange transactions conducted in accordance with the law can promote the further development of the land market in transparent manner.

## 4. Constraints to the Land Market Development in Ukraine

For a properly functioning land market to develop in Ukraine several issues need to be addressed in the near term.

### 4.1. Political Will to Continue Implementing Reform

Throughout the 1990's the Verkhovna Rada failed to support land reform and land market development, because it was largely composed of political blocs opposed to land reform. The advances in land reform were promoted mainly by Presidential Decrees and support from the State Committee on Land Resources. Only recently, after more progressive blocs took control of the Verkhovna Rada, have legislative advances in land reform and land market development been realized. The main advance being the adoption of the new Land Code in 2001. To continue on this course, the Verkhovna Rada must be willing to exert its newfound support for land reform and land market development, and adopt appropriate laws that establish the framework for a functioning land market in Ukraine.

#### **4.2. Inconsistent Legal Framework.**

The current legal framework governing land relations in Ukraine exhibits many inconsistencies and provisions that inhibit the development of the land market. For example, according to Ukrainian law, land is considered separate from buildings and improvements, (i.e., the ownership of a structure on land does not automatically imply ownership of the land). This characteristic of Ukrainian law is inconsistent with international practice and creates substantial problems in developing a functioning land market. While the new Land Code has resolved many previous inconsistencies in the law, it has created others. For example, article 81 of the Land Code which defines the private land ownership rights of the Ukrainian legal entities and physical persons, is formulated in such way that NGOs, religious organizations, and those who use land for non-commercial activities have no right to own that land. Many of these inconsistencies exist because of the tendency of the state to over-draft laws and regulatory acts. Legislative drafters and Verkhovna Rada deputies should resist this temptation and promote laws that allow the private sector to develop and market mechanisms to flourish.

#### **4.3. Weak Legal System.**

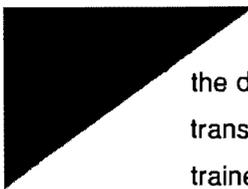
The existing legal system in Ukraine is weak and inadequately protects the rights of landowners. Low salaries of civil servants in the legal sector, non-transparent processes for the enforcement of land and property rights, and corrupt practices lead to the lack of public trust in the legal system. Moreover, court costs are too high for average land owners (for example, rural pensioners) to avail themselves of the system for enforcing their rights.

#### **4.4. Lack of Information and Transparency in Market Activity.**

New landowners find it difficult to obtain reliable information on legal rights, average lease rates, and procedures for securing and enforcing their rights. This situation leads to uncertainty and poor decision making by land owners when deciding how best to use land. Moreover, the lack of a registration system that adequately secure legal rights to land materially inhibits the development of the land market in nearly all respects (e.g., alienation of rights, land financing, etc.). In many instances these factors lead to transactions being conducted in non-transparent manners.

#### **4.5. Inadequate Development of Market Institutions.**

Institutions capable of and interested in promoting land market development largely do not exist in Ukraine. The private associations related to land sales and landowners rights that exist are weak and in their infancy, and need greater support and guidance. These market institutions will drive



the development of the land market and provide services to those who wish to engage in market transactions. Some of the private services that are needed for a functioning land market include: trained land lawyers, landowners groups, surveyors, and appraisers. Most importantly, a financial infrastructure willing to accept land as collateral for loans is needed to drive forward land market activity. Commercial banks and other lenders need incentives to move into mortgage lending and offer credits at reasonable interest rates. As the institutions and services mentioned above develop, and the security of land rights becomes more obvious, financial institutions will move on their own into lending activities.

#### **4.6.Lack of Public Education.**

There has been a failure in the past to recognize the importance of public education and information regarding land reform and land market development. New focus on these issues has result in emphasis on public awareness policies and training programs for land market professionals. The state's role in this process should be to facilitate the dissemination of information, but not to control it. The State should provide incentives to private organizations to gather and make information public and easily accessible.

#### **5.Importance of the Development of the Ukrainian Land Market in the International Context.**

The importance of land reform in Ukraine should be considered in the context Ukraine's intention to be more integrated into the European community, an aspect assigned high priority in both external and internal policies of the country. After the enlargement of the European Union, Ukraine will find itself at the borders of EU, making it extremely important for Ukraine to develop economically to avoid becoming the sanitary buffer between the EU and other countries. Continued development of the land market will promote further integration of Ukraine into the European community by adopting a similar economic system to its neighbors and by attracting investment from outside its borders. The common values and standards shared with other countries in Europe will ensure that Ukraine is not excluded from global markets and political decision making. Clear movement toward a pro-democratic and pro-market society will enhance Ukraine's economic development regardless its potential entry into the EU.

The countries seeking accession in EU are expected to comply with Copenhagen criteria, amongst those is the "functioning market economy". The EU members should also guarantee free movements of capital and freedom of establishments. All above mentioned requirements has to do with land market development. In order to meet Copenhagen criteria, candidate states undertook the land reform measures varying from country to country. Ukraine is learning from the neighboring countries in transition and countries with well-established land markets to establish a functioning land market in Ukraine and comply with Copenhagen criteria.

As Ukraine moves to achieve these goals, it should examine the development of the land market in countries such as Poland, the Baltic States, Moldova, and Hungary. In those countries, one can see a clear relationship between the speed of land reform and each country's success with establishing the conditions for a market economy, the kind which did not exist during Soviet times. By making a comparative analysis of the land reform process in each of these countries, Ukraine

can determine the most appropriate approach and policy to follow given the country's history and environment.

#### **6. Actions Needed to Further Land Market Development.**

1. Complete the privatization process by finishing the issuance of land titles to land share holders. The process of the transferring land from collective to private ownership should be completed as soon as possible.
2. Establish a normal legal basis for a functioning land market. Bring existing legislation into compliance with the new Land Code. Draft only those new laws that are essential to establish a properly functioning land market, being cognizant of the historical tendency to overdraft legislation, which often creates inconsistency and ambiguity in the application of law.
3. Eliminate over-regulation of market activities by the State institutions that is now inherent in the law and that is customary among government officials in Ukraine. The State should encourage the development of private institutions that can operate with minimal regulation and provide valuable services to land market participants. Studies on the design of institutional land market service providers (such as lawyers, land appraisers, land surveyors, and real estate brokers) in other countries may help the State to better understand its role in the overseeing relations between land market service providers and landowners.
4. Create conditions and incentives for commercial banks and other financial institutions (i.e., sources of capital) to lend using land as collateral. Increasing the transparency and efficiency of the market, improving the security of legal rights to land (establishment of a real estate registration system), and establishing straight forward foreclosure procedures are some steps necessary to advance the financing of land related transactions.
5. Build an effective grassroots support system for land market development measures. The State should convey clear information to the civil society during the final stages of land privatization and the initial stages of land market development. This requires public education and public access to information on legal rights of landowners, land values, procedures for alienation of land, etc.

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# **MORTGAGE LENDING - AN ESSENTIAL ELEMENT OF A FUNCTIONING LAND MARKET AND A VITAL TOOL FOR CONSOLIDATION OF AGRICULTURAL LAND**

Privatization of agricultural land in Moldova has been successfully completed, generating over 1.0 million land owners, each with an average land holding of 1,5 hectares. However, giving peasants land into ownership is by far the only measure needed to be taken. A well functioning land market is one of the key aspects for consolidation of privatized land into efficiently sized farms. A major role in land consolidation also plays the availability of mortgage loans for those farmers who wish to purchase additional land but lack the cash for it.

The paper below addresses three main issues: (a) land consolidation – its importance and how it occurs, (b) the agricultural land market – status and development, and (c) mortgage lending – a vital tool in land consolidation and land market development. It also provides a set of actions needed to promote land market development.

## **1. BACKGROUND ON AGRICULTURAL LAND PRIVATIZATION**

The land reform in Moldova started after proclamation of its independence in 1991, with agricultural land privatization as a key component. The principles of land reform were provided in the Land Code, adopted in the same year. This law stipulated different privatization methods for agricultural and non-agricultural land: whereas, industrial enterprises were required to purchase their associated land for a rather high price, while peasants (i.e., eligible member for the former collective farms) were entitled to receive a parcel of agricultural land free of charge. The “free-of-charge” principle made agricultural land privatization extremely popular amongst rural inhabitants – no one will decline a gift from the state government! However, the government was in no hurry to transfer agricultural land into private ownership. Was it because the government assumed an expense it could not bear (the land titling work and preparation of land titles was too costly for the government that volunteered to pay for it)? Was it because the reform was opposed to the interests of several parties (former collective farm managers feared losing their power)? Regardless, at that time, people felt that land reform in Moldova would take 50 to 100 years to complete.

The ownership right to agricultural land of a peasant remained merely declarative (in the form of a land share certificate) until 1995, when, due to international financial organizations, in particular the United States Agency for Agricultural Development (USAID), land privatization began in earnest. With the financial support of USAID and political support of Government of Moldova, in November 1995, a two-stage pilot project for privatizing agricultural land commenced. The pilot project grew into the well-known Moldovan National Land Program. The project developed an efficient and cost-effective agricultural land privatization model, in compliance with the existing law. Due to the combined efforts of the Government of Moldova and USAID, in December 2001, after some 6 years of assiduous work, privatization of agricultural land was completed resulting in over 1.0 million legally registered agricultural land owners, each with an average land holding of 1.5 hectares. As of December 2001 98.7 percent of all agricultural land subject to privatization has been privatized with land titles issued to the new owners.

### **Land fragmentation issue**

Today, the dynamic pace of land reform in Moldova is recognized by both supporters and opponents of the National Land Program; the voices of the opponents recently becoming more persistent than ever after the shift to the left of Moldova’s Government. Most frequently opponents criticize the National Land Program for excessive fragmentation of agricultural land, conveniently ignoring that the Program merely implemented the provisions of the existing Land Code. Under that 1991 law, the Parliament of Moldova intended to privatize agricultural land by equitably distributing the land among those who were employed in agricultural sphere on January 1, 1992. According to the law, each individual eligible to receive land was to receive an equivalent share land that accounted for differences in soil fertility. Thus, individuals would receive a parcel not of equal surface area, but of

equivalent “value.” It is clear that the concern of law’s authors was a socially equitable distribution of land.

This principle of land reform resulted in substantial fragmentation of land, given the large number of individuals entitled to agricultural land (25 percent of the citizens of Moldova became owners of agricultural land) and the relatively small amount of land to be transferred to private owners (1.7 million hectares of agricultural land). Making the situation more difficult was the fact that most peasants entitled to land wanted to get title to more than one parcel of land (i.e., arable and perennial). In some villages peasants requested as many as twelve parcels with an average surface area of 0.1 – 0.2 hectares each. To minimize the land fragmentation, before land reform began nationwide, the Land Code was amended in 1998 to limit to three the number of parcels that one landowner could get title. As a result, the 1.7 million hectares of agricultural land privatized since the reform began encompass over 3.3 million parcels (i.e., on average each owner received three parcels per owner, with an average surface area of 0.5 hectares).

Today, land consolidation in Moldova is crucial to maximize the efficiency of privately owned land. Generally, studies have shown it economically inefficient for commercial agricultural farms to operate on a parcel of 0.5 hectares, typically all that a farmer can practice on such a small piece of land is subsistence agriculture. What then is considered an efficient size for a commercial farm? Opinions vary, for example the left wing strongly supports large farms (over 100 hectares in size), and gives no chance of survival to small farmers. Regardless of farm size one thing is clear: consolidation of land will be gradual and will be dictated by the market.

The experience of other countries shows that land reform has the largest positive economic effect when the land is concentrated in the hands of those able to manage it efficiently. Not all of the new 1.0 million landowners has the necessary business skills, especially since during soviet times such qualities were constantly suppressed, resulting in the propagation of a social infantilism. Thus, market forces will inevitably reduce the number of farmers and land will consolidate into the hands of the most entrepreneurial land owners. For example, if one assumes that an efficient size farm is 50 hectares, the agricultural land should be consolidated into the hands of 31,200 farmers (1,560,000 hectares of privatized ag land / 50 hectares = 31,200). This simple calculation shows that only 3 percent of the current 1.0 million landowners would remain as active farmers.

#### **How land consolidation occurs**

New landowners themselves realize the importance of land consolidation. Many began to consolidate land without any support from state or public authorities. First, land consolidation occurred based on leases, second based on partnerships between landowners, and third based on sale and purchase transactions. The statistical data show that after privatization 77 percent of the of new land owners have chosen to lease out their land to local “leaders” (i.e., agricultural entrepreneurs), and only 23 percent have decided to work their land individually, or in most cases jointly with their relatives and neighbors. Lease-based consolidation continues to be the most popular form since it does not require significant financial means. However, lease-based consolidation is not always efficient for the lessee – the so-called “leader” – for several reasons:

- **Some leaders have taken a burden far too heavy, resulting in a farm with relatively low –productivity.** In the initial stages of reform, most leaders hurried to lease in as much land as possible. After a couple of years of operation, several leaders realized that the size of their farm is too large for their managerial abilities and their available capital. Lacks of managerial capacity, on one hand, and of financial resources sufficient to observe adequate crop cultivation technologies, on the other hand, lead to low –productivity of the farm. As a result, some leaders were unable to make their lease payment, resulting in many landowners withdrawing their land from under the lease. These leaders are left with little land and a spoiled reputation.
- **Leasing in of land and other assets, gives the leaders little access to credits because of their lack of collateral.** A leader with a farm established on the basis of leases has restricted access to credits, mainly because the only collateral that he/she can pledge is the future crop.

- **Since the lease contract is usually for three to five years, leaders are not willing to make capital investments in the leased land, such as planting an orchard, or installing an irrigation system.** Some leaders have managed to sign long-term lease contracts for agricultural land (ten to fifteen years), nevertheless, many fear that the landowner might break the contract (for instance if the leader misses a lease payment) and hesitate to make capital investments in the leased in land.

Given these facts, many active farmers have advanced to the next phase of consolidation, (i.e., through land exchange and sale and purchase), which is evident from the relatively rapid development of the land market in certain areas of Moldova.

## **2. LAND MARKET DEVELOPMENT**

Today, in many areas of Moldova the agricultural land market rapidly evolves (See Table 1 below). Most active farmers wish to consolidate their land holdings, giving rise to more sale and purchase transactions. Such transactions have increased by 2.5 times from 2000 to 2001. Farmers have realized the disadvantages of leasing and now hurry to expand their land holdings by purchasing additional land.

**Table 1. Evolution of agricultural land market during 1999-2001**

	1999	2000	2001
1. Agricultural parcels registered in the cadastre system	2,061,568	2,396,000	3,119,293
2. Transactions			
➤ Sale and purchase	1,930	9,765	24,625
➤ Inheritance	516	7,431	23,257
➤ Exchange, donation	437	3,848	13,035
Total transactions	2,883	23,927	60,917
percent of total agricultural parcels registered	0.1%	1%	2%
2. Mortgage	271	1,732	4,067
percent of total agricultural parcels registered	0.01%	0.07%	0.13%
3. Lease over 3 years	132	4,182	7,755
percent of total agricultural parcels registered	0.01%	0.17%	0.25%

*Source: State Agency Land Relations and Cadastre (Cadastre State Agency)*

One factor in particular that contributed to the substantial increase in private agricultural land market activity after 1999 were the intensive public information and awareness campaigns undertaken by most donor organizations involved in agricultural reform. For example, TACIS sponsored the Agroinform Project<sup>1</sup>, and USAID funded Legal Aid Clinics<sup>2</sup> and Farm Privatization Centers<sup>3</sup>. Without legal information and access to legal defense against abuse and coercion at the hands of more influential local community members, local government, notaries, or territorial cadastre office registrars, new landowners acted passively with regard to their land rights. The public awareness campaigns gave confidence to new landowners, encouraged them to take action with regard to these rights, and, consequently, contributed to the development of the land market.

Another key factor to note is that the market for agricultural land had developed most rapidly in those areas of Moldova where farmers have access to cash output markets. For example, an active

<sup>1</sup> In April 2000, Agroinform published an important brochure "Practical recommendation on sale, exchange, donation, lease and inheritance of privatized agricultural land" that helped increase awareness amongst newly-emerged owners about their rights.

<sup>2</sup> Ten Legal Aid Clinics were established under the USAID/BA&H Project to Develop Land and Real Estate Markets in Moldova. The teams acted as advocates for landowners' rights, and helped them enforce these rights.

<sup>3</sup> The CPBR regional farm privatization centers played an important role in public awareness, not only with regard to the received land share, but with regard to the property share as well. Numerous local seminars, the arbitrage court are only a few accomplishments of these centers.

market for private agricultural land quickly developed in some parts of North because farmers could sell their fruit, vegetable, and other produce for cash in nearby Ukraine. A secure cash output market also exists in Chisinau, the nation's capital, and around other large cities such as Balti and Orhei, which helps to account for an active land market near those cities. In contrast, areas near the Romanian border in the West and far South of Moldova have slowly developing agricultural land markets largely due to the lack of nearby cash output markets. The Romanian market is not viable for most Moldovan farmers because of the similarity in climate, crops grown, and soil conditions.

**Land price.** Currently, Moldova does not have a unified database containing price information on

**Problem:** Moldova does not have a unified database containing, in addition to number of land transactions, important information thereof, such as price, soil characteristics, etc.

all agricultural land transactions recorded in its registry system. The existing unified database under the Cadastre State Agency contains only information on the number of land transactions. Nevertheless, several studies have been conducted to determine the average price of agricultural land in Moldova. A survey published in the Cadastral Newspaper in 2001, shows that the average price for agricultural land in Moldova approximates 2,737 Lei per hectare (approximately 210 USD<sup>4</sup>). The highest prices are found near Chisinau and near Edinet (near Northern border with Ukraine). The lowest prices are near Soroca and Balti (North-central part of Moldova). It is notable that the price significantly varies per rayon, and even per village, being higher in those villages where there are many active farmers. In comparison to other countries, the price of agricultural land remains low in Moldova mainly because of:

**Problem:** Price of a hectare of agricultural land is very low.

- Political instability, that promotes the depression in the agricultural sphere of the economy; and
- Economic instability, caused by underdeveloped market structures (that keep the demand for agricultural land low and depress the price of land).

### **3. MORTGAGE LENDING - AN ESSENTIAL ELEMENT OF A FUNCTIONING LAND MARKET**

Even though most farmers have realized the importance of expanding their land holdings, many lack the financial resources needed to purchase additional land. They could purchase a few hectares, usually by borrowing from relatives and friends, but the scarcity of cash makes it nearly impossible for farmers to purchase many parcels to consolidate land into large fields, even when they identified willing sellers. Thus, mortgage programs are vital tools necessary to expand and accelerate the development of the real estate market, introducing needed liquidity for the purchase of land into a cash-poor society.

**Problem:** Farmers lack the cash to purchase additional land.

**A. Mortgage lending initiatives of local financial institutions.** Currently, there are 20 commercial banks operating in Moldova's relatively young banking sector. When assessing the importance of each bank in agricultural lending, it is apparent that the dominant bank is Agroindbank, which currently has approximately 33 percent of its loan portfolio in agriculture and agro-processing. The remaining banks have very small agricultural loan portfolios, not exceeding ten percent of their overall loan portfolios. Most of the loans to the agricultural sector are made to finance working capital, rather than long-term investments. For instance, in 2000 Agroindbank lent out 95 million Lei to 1,480 private rural businesses, mainly farmers. Of these loans, about 70 percent were short-term working capital loans, another 20 to 25 percent were medium-term loans (one to five years) for purchase of equipment, and only five to seven percent of the loans were long-term (five to twelve years).

Loans for the purchase of agricultural land are a rare phenomenon in the loan portfolio of most banks. An exception could be made for the banks' most important borrowers, who can get such a loan from bank's own resources, provided that they are comfortable with the lending terms the bank

<sup>4</sup> At the average exchange rate 1 USD=13 MDL

offers. Even so, these are not mortgage loans (whereby the purchased land serves as collateral). For most such loans, banks would take all required collateral upfront, what is “everything” but the land to be purchased from the loan. A regular mortgage loan (also referred to in this paper as a purchase money mortgage) would imply that the land to be purchased from the loan is to serve as the main collateral, additional collateral being taken by the bank only if it finances a portion of the land market price above the collateral value of that land. To make a mortgage loan, the bank has to follow one of the two procedures:

- a) Borrower concludes first the contract on sale and purchase of land, providing that the land price will be paid within a certain time (e.g. 2 weeks); after which bank and borrower conclude the mortgage agreement on that land and the bank issues the money to the land seller directly; or
- b) Borrower, seller and bank conclude simultaneously the contract on sale and purchase of land and the mortgage contract of that land; after which bank issues the money to the land seller. This second option considerably speeds up the lending process.

A quick study of the major financial institutions in Moldova shows that virtually none are making loans for the purchase of agricultural land (not even speaking about mortgage loans), except for:

- Agroindbank – makes loans for the purchase of land both from its own resources and through a joint lending program with the Citizens Network for Foreign Affairs (CNFA). Agroindbank is the only bank that has publicly declared to farmers, in a recently published brochure on agricultural lending products, that it is willing to provide mortgage loans for the purchase of land from its own resources.
- Fincombank -- makes mortgage loans only through a joint lending program with CNFA, splitting resources for the loan equally with CNFA. Fincombank does not make mortgage loans solely from own resources.
- The Rural Finance Corporation (RFC) –has implemented a mortgage-lending program in the amount of 40,000 USD, financed by CNFA. It does not make mortgage loans from its own resources.

Thus, only one lending institution in Moldova is making loans for the purchase of agricultural land from own resources. The only purchase money mortgages in Moldova were made by Fincombank and RFC under the CNFA’s Private Farmer Credit Program. This Program proved that purchase money mortgages are possible, the procedures, while rudimentary and often cumbersome, are functional.

Most banks are reluctant to provide loans for the purchase of agricultural land, including mortgage loans for a number of reasons:

- First, most commercial banks do not have longer-term financial resources from which to provide mortgage loans. In most cases, commercial banks are able to make loans only for two, and in some cases, three years. However, most borrowers need a longer period to repay loans for capital investments such as land purchase. Indeed, some international donor projects make long-term financial resources available for mortgage loans, however, most credit lines established by donors have an interdiction on loans for the purchase of land.
- Second, commercial banks are concerned with their ability to sell land upon which they may foreclose. The land market in Moldova continues to be insecure; a limited number of transactions in many villages makes it difficult for a bank to predict the market price of a land parcel. In some cases, a bank fears that it may not be able to sell the parcel at all.

**Problem:** Most Moldovan banks are reluctant to provide mortgage loans from own resources, because of (a) lack of long term financial resources, (b) inability to sell the foreclosed land, (c) small land sizes requested for purchase.

- Third, commercial banks willing to finance the purchase of land will require that the land parcels be compact and contiguous in their location, have satisfactory soil characteristics, and preferably, have access to irrigation. However, farmers find it difficult to negotiate the simultaneous purchase of a large number of contiguous small land parcels.

In most cases, a farmer will request a loan for the purchase of five to seven hectares of land, which is comprised of ten to fifteen parcels located in more than one field. Naturally, the farmer intends to exchange the parcels and create a contiguous field over time, but banks cannot rely on the success of such plan, and often refuse to take the non-contiguous land as collateral, resulting in a rejection of the financing request.

- Fourth, commercial banks are reluctant to make small loans for the purchase of land. Most farmers find it difficult to combine the purchase of several contiguous parcels. Other farmers wish to expand their operation gradually, and therefore request loan in amounts deemed too small by a commercial bank. These small loans are not profitable for banks, because the overhead costs to process and administer small loans is generally the same as the costs for large loans, but the return is less.
- Fifth, some commercial banks refuse to make mortgage loans because they consider that land should be a farmer's own contribution to the farming business.

On the other hand, there is a demand for land purchase loans in Moldova. A recent study conducted by Agency for Restructure in Agriculture (ARA) of 350 farms of various sizes shows that only 9 percent have purchased land, 48 percent intend to purchase land, of which 73 percent intend to seek a long-term bank loan for the purchase. **In conclusion, we can say that the demand for land purchase loans is constantly rising as farmers begin to feel more confident about their farming abilities and wish to expand their land holdings.** The following factors impact the ability of farmers to take mortgage loans.

- **The interest rate remains very high for any type of investment loans**, in particular, for mortgage loans. Currently, the average interest rate on a loan made from a commercial bank's resource is between 25 to 28 percent per annum. Thus, even if the farmer can get the bank to agree to make a mortgage loan for five to seven years, the interest rate is too high.
- **Farmers continue to demand small mortgage loans** since they have difficulty putting together large contiguous tracts of land to purchase and/or wish to expand their holdings gradually.
- **Commercial bank procedures for a mortgage loan remain too cumbersome.** Several farmers complain that it takes too long to get a loan, and too much documentation is required. Moreover, when a farmer requests a rather small loan, the traveling expenses incurred during the lending process are so high that it questions the effectiveness of the loan itself.

**B. International donor mortgage credit programs.** International donor funding for long-term mortgages would certainly encourage Moldovan commercial banks to make these types of loans. International funding would not resolve all lending issues, but it would provide commercial banks some sorely needed long-term resources that can be used to make such loans and to perfect mortgage loan procedures. One of the most successful international donor lending programs in Moldova is the CNFA Private Farmer Credit Program that includes a mortgage-lending component.

#### **Private Farmer Credit Program of Citizens Network for Foreign Affairs**

Citizens Network for Foreign Affairs (CNFA) has operated a successful Private Farmer Credit Program in conjunction with three Moldovan financial institutions since 1998. The program was created with a donation of agricultural commodities provided by the United States Department of Agriculture (USDA), which were then sold (monetized) in Moldova. The proceeds of the sale were used to establish the Private Farmers Credit Fund (PFCF), which provides loans to private farmers and private farmer groups through two Moldovan commercial banks, Agroindbank and Fincombank, and the cooperatively-owned Rural Finance Corporation. These loans are for the purchase of agricultural land, livestock, machinery and small processing equipment. The partnership between CNFA and the financial institutions allows the institutions to extend credits for a medium term (three to five years), in Moldovan Lei at interest rates more acceptable to farmers. In most cases purchased land, equipment, or livestock serves as collateral for the loans. All loans are made and serviced by

the Moldovan lending institutions, with CNFA deciding on a case-by-case basis whether to participate in the loan.

### ***Background on mortgage lending component of CNFA's PFCP***

In February 1999, CNFA and Agroindbank signed a partnership agreement to create a joint credit line under the PFCP, which among other types of loans included medium term loans for the purchase of agricultural land to address farmers needs for land consolidation. To inject some competition into the agricultural credit market and to promote further the concept of mortgage lending for the purchase of land CNFA signed a second partnership agreement in August 1999 with Fincombank. This joint credit line focused on supplying medium term credit for the purchase of agricultural land, using the purchase-money mortgage principle (i.e., simultaneously mortgaging the purchased land). Under this program, Fincombank was the first bank in Moldova to make a purchase money mortgage in agriculture.

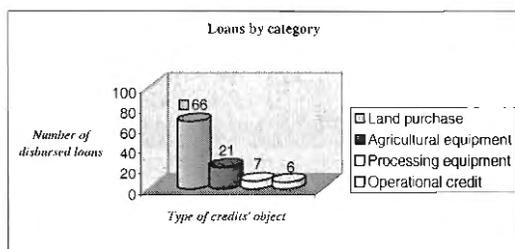
During the course of the program, more farmers applied for small land purchase loans that commercial banks refused to make. These events gave birth to another credit line funded through the Rural Finance Corporation (RFC) and its member Savings and Credit Associations of Citizens. These Associations are rural non-profit financial institutions that provide small short-term household loans for their members. In April 2000, CNFA and the RFC created a pilot loan fund to be entirely and exclusively used to make small purchase-money mortgage loans for the purchase of agricultural land to farmers wishing to purchase small tracts of land (i.e., those to whom commercial banks would not lend because of the size of the loans).

The RFC Program had several goals. First, it opened access to medium-term land purchase loans for independent farmers who could not be serviced by commercial banks because of the small loan size. Second, it contributed to land consolidation and land market development by helping subsistence farmers move into more commercially oriented activities. Third, it built the capacity of Savings and Credit Associations to provide secured medium-term credit, with the hope that the Associations would be able to provide such credits from their own resources in the future.

The pilot effort proved to be very successful. The demand for mortgage loans in the participating Savings and Credit Associations was so high that CNFA expanded the original loan fund. Demand for such loans among farmers remained high, even after the original loan funds were exhausted, resulting in CNFA and the RFC signing a second agreement to expand the loan fund in June 2001, as funds are available.

### ***Loan portfolio***

As of February 2002, using the PFCF 100 loans totaling US\$ 1,067,630 have been made to private farmers, farmer groups, and agribusiness companies to purchase land, livestock, agricultural machinery, implements and processing equipment. Land purchase loans are the largest single category of loans accounting for 66 percent of the total loan portfolio. Of the 66 land loans, 29 are micro-credit loans made through the Savings and Credit Associations at an average US\$ 1,400 per loan.



The program has experienced a good repayment ratio. Of the 100 total loans, 88 loans are current, 8 have been repaid in full, and only 4 loans are past due. The financial institutions are working to restructure the past due loans. The good record is partially attributable to the fact that CNFA and its banking partners have provided assistance to farmers in preparing business plans and loan applications, as well as post-loan counseling.

### **The mortgage lending component proved three fundamental points:**

- Mortgage loans for the purchase of agricultural land are possible in Moldova under the current procedures.

- There is a demand for mortgage loans for the purchase of agricultural land, a demand that is constantly rising. The demand for small mortgage loans is higher than the demand for large mortgage loans.
- Farmers are capable of understanding the complexities of mortgage lending and the implications of pledging their land as collateral.

**C. Mortgage aspects in other international credit lines.** Additional international donor credit lines for the agricultural sector are being made available in Moldova. One of these is the Project for Rural Finance and Development of Small Scale Enterprises, financed by the International Fund for Agricultural Development (IFAD) which began in December 2000. Unfortunately, this credit line of nearly US\$5,000,000 does not allow loans for the purchase of land.

The World Bank's Rural Investment and Services Project (RISP) is another rural development project with total funding of US\$ 30,000,000. This Project has a credit line of US\$ 25,000,000 with an advance of nearly US\$ 800,000 already available for pilot lending. The credit line is available for investments in any rural economic activity (i.e., agricultural production, processing and marketing, input supply and service provision, non-agricultural activities, etc.). However, this credit line is also not available as financing for the purchase or lease of land.

**Problem:** Most international credit lines made available to Moldova contain an interdiction on mortgage loans for the purchase of land.

The policy of most donors against the use of international credit lines for the purchase of land is stifling the development of the mortgage market specifically, and the land market in general. Only CNFA's mortgage programs are providing loans for the purchase of land, and thereby teaching the principles of mortgage lending to financial institutions in Moldova. This activity is helping to establish the institution of mortgage lending in Moldova and develop the land market more rapidly.

**D. Other aspects – using agricultural land as collateral.** The mere availability of loans for the purchase of land is not sufficient to improve the operation of the land market. Unless land is recognized as valuable and marketable collateral, a farmer's ability to access credit will not increase, and consequently the land market will evolve slowly. In Moldova, even if no commercial bank has excluded agricultural land from its collateral policy, experience working with various commercial banks shows that few banks are willing in practice to take

**Problem:** Few banks take agricultural land as collateral.

agricultural land as collateral. In most cases, commercial banks will only take as collateral a large and compact piece of land, with excellent characteristics. These banks will also considerably discount the estimated value of the land that is taken as collateral due to the insecurity of the land market (it is difficult for banks to estimate the price at which land could be sold in case of foreclosure). As a result, most banks discount the value of the land that is collateral for the loan by

**Problem:** Undeveloped land appraisal system.

as much as 50 percent of its market price. Moreover, the market price is often determined by a bank loan officer, resulting in a subjective and biased opinion of value. While today in Moldova there are some 100 companies with appraisal licenses, only a few of the larger companies have well-trained and experienced personnel whose qualifications are accepted by financial institutions. In addition, the appraisal of a piece of land remains rather expensive, due to high traveling expenses and expensive labor<sup>5</sup>. Thus, few banks resort to independent companies for appraisal.

#### **4. ACTIONS NEEDED TO PROMOTE LAND MARKET DEVELOPMENT**

Much remains to be done to aid the development of a properly functioning land market. Below are some recommendations for future actions:

<sup>5</sup> Consulting and Credit in Agriculture (CCA) has contacted some Chisinau based appraisal companies, pretending to be a customer needing to appraise a land parcel near Calarasi (approx. 40 km from Chisinau), and was told that appraisal thereof would cost 1,000 lei and higher. Given that the average price of land is 3,000 lei per hectare, an appraisal service of 30% of land market price is very high.

**1. Improve the existing appraisal system.** The current database under the Cadastre State Agency should include important information on land transactions, such as the reported land price and some land characteristics. This data can be further used for land appraisal purposes. It would also help to facilitate and encourage the operation of rural appraisal companies to conduct rapid and cost-effective land appraisal.

**2. Availability of land registry information to the general public.** The law provides for public access to the land registry data. However, in practice, the registration authorities do not follow the law and frequently refuse to provide such data to the public. There needs to be strict enforcement of the law that makes registry data available to the general public. The registration authorities need to be trained and educated on the importance of publicly available information.

**3. Political support for the post-privatization and market oriented economic development policy.** The recent actions of the Government of Moldova have threatened the course of reforms and the continued development of the agricultural sector. For example, a new draft Land Code (luckily returned Parliament for improvement) contained administrative measures that are not market oriented and would harm the development of the land market and agricultural sectors.

**4. Establish a transition period with a simple procedure for land exchange.** Allowing the exchange of land through a simplified procedure during some limited period after privatization could contribute to rapid consolidation of agricultural land. Some actions have been taken to promote this policy; namely the Parliament has amended the Law on Notaries to allow the local Mayor's Offices to notarize ownership transfers of agricultural land (sale, donation, exchange). However, in practice most Mayor's Offices are afraid to perform such notarization. Thus, intensive training of Mayor's Offices is required to implement this policy objective for accelerating land consolidation.

**5. Promote mortgage lending** (i.e., loans for the purchase of land) through commercial banks and other financial institutions (such as the RFC) as a stimulus for land consolidation and land market development.

- Mortgage loan programs should be made accessible to many farmers. Donor programs can assist to provide long-term loans at reasonable interest rates; technical assistance to financial institutions and borrowers, and public awareness of mortgage lending procedures. These efforts can also stimulate the involvement of a number of financial institutions in making such loans, thereby increasing competition and client-service;
- Efforts must be made to simplify and make transparent bank lending procedures. For example, banks should pledge to make lending decisions within establish time limits, delegate the authority to approve loans up to given amount to loan officers, and intensify training of their [regional] personnel;
- Financial institutions should promote purchase money mortgages, the simultaneous conclusion of a land sale and purchase contract and a land mortgage contract. Purchase money mortgages are a crucial aspect in the development of the land market. To get financial institutions to promote purchase money mortgages, for a start the following is needed: education/training of financial institutions on this new lending product; more pilots within as many financial institutions as possible to prove that purchase money mortgages are possible; large mediatization of pilot results for these to reach other financial institutions and potential borrowers.
- Small mortgage loans should be made available to farmers though Savings and Credit Associations. There should be assistance to develop the ability of the village-based financial institutions to make small mortgage loans using their own resources. Further development of these Associations will require them to accept deposits from its members and to incorporate financial and lending instruments to invest deposits.

- Development of an efficient and accessible insurance system in agriculture would encourage financial institutions to provide more credits to farmers, including mortgage loans. In addition, intensive education/training is needed for farmers (to convince them that insurance is not a meaningless expense), for banks (to convince them to require insurance as part of the loan package), and for insurance companies (to develop efficient, cost-effective, and accessible insurance products for agriculture).