



**EUROPEAN BUSINESS ASSOCIATION
REPUBLIC OF MOLDOVA**

DCFTA – BUSINESS CLIMATE UPDATE

(Policy Developments, Macroeconomic Review for 2019 and the impact of Covid-19 Crisis on the economic development of the country)

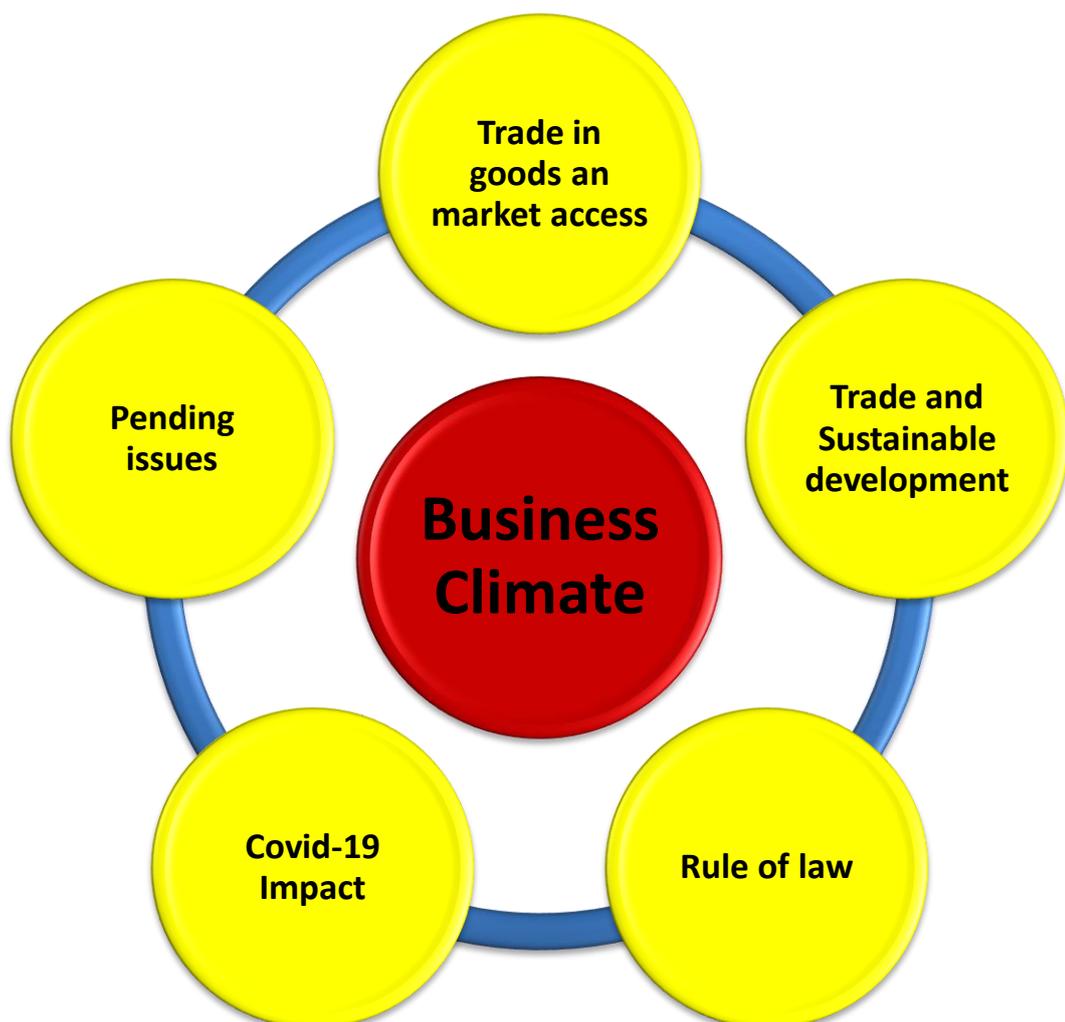


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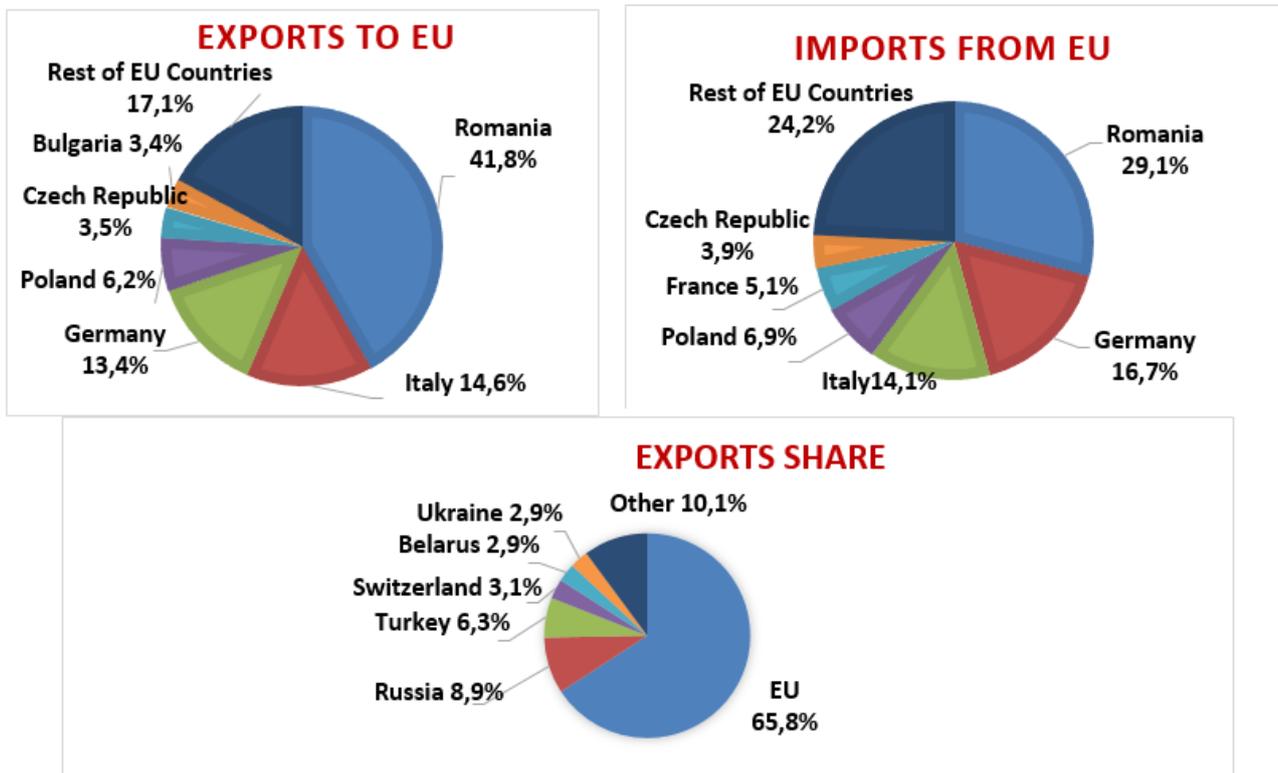
Macroeconomic outlook

Review of 2019

- **GDP** amounted to 210.1 bn MDL (around 10.4bn Euro) and **increased by 3.6%** compared with 2018;
- **Foreign Direct Investments increased by 16.2%** compared with 2018 and reached 4.8 bn USD (around 4.4 bn Euro);
- **The Trade flow increased by 1.8%** and amounted 8.62 bn USD (around 7.88 bn Euro);
- **Exports of the Republic of Moldova increased by 2.7%** and reached 2.78 bn USD (around 2.54 bn Euro). **Export to the EU** has reached 65.8% of total exports;
- **Imports increased by 1.4%** and reached 5.84 bn USD (around 5.34 bn Euro). **Imports from the EU** stand at 49.47% of total imports;
- **Average monthly salary per employee constituted 7356.1 MDL** (around 374 Euro) and increased by 14.1% compared to 2018;
- **Inflation rate** (December 2019 vs December 2018) constituted 7.5%, compared to the inflation rate of 0.9% registered the previous year;
- **Public Debt** amounted to 52.5bn MDL (around 2,68 bn Euro) and registered an increase by 0.9% compared to 2018;
- **Main Sectors:**
 - **Industry** (the manufacture +3.1%, energy supply -4%, extractive industry – 1.9%)
 - **Agriculture** - decrease by 1.9p

Forecast for 2020

- The initial forecast of GDP for 2020 was 226.8 bn MDL, an increase with 3.8%. Nevertheless, due to Covid-19, **Moldovan authorities revised its forecast for 2020 and foreseen the decrease of GDP by 3.0%**, which correspond to IMF experts provision/forecast. Also, the German Economic Team foreseen a decrease of GDP by 6.3% in 2020.



I. TRADE IN GOODS AND MARKET ACCESS

A. Internal Trade Law

In 2019, discussions on amendments to the internal trade law, which so far remains the main dissent between traders and producers in terms of limitations on the marketing and advertising discount, the period for marketing activities, and the obligation to offer at least 50% of market shelf for local products continued.

EBA Moldova primarily supports the promotion of a fair and balanced policy between all market operators, ensuring the functioning of the principles of fair competition. It is also important to emphasize the need to promote and support domestic producers through other tools such as developing national projects to stimulate investment in new technologies, promoting the local food brand through media campaigns, thus stimulating the competitiveness of local producers, marketing/communication activities to stimulate the population to consume local products while generating an increase in market demand for quality products.

At the same time, the approval of the draft law with the proposed limitations will clearly infringe the commitments of the Republic of Moldova under the Moldova / EU Association Agreement (art. 152), as well as the commitments to the World Trade Organization (art. 3 of GATT), which provide no less favorably treatment to imported products than that accorded to like products of national origin.

In this context, it is important to mention that the relevant central public authorities were informed about the experience of Romania on the same issue, namely, inclusion of limitations related to the trade discounts, carrying out the advertising activities and display on the shelf of 50% of Romanian products in Romanian legal framework. Following the respective legal Romanian amendments, the European Commission issued a notice and suggested to Romania to align its legislation according to the EU Directive and legal requirements.

Thus, following the Parliament Committee on economy, budget and finance meeting, the draft law was adjusted and limitations related to the marketing and advertising discounts and the period for marketing activities were excluded.

Status Quo: The draft law is under examination, pending adoption in the second reading by Parliament.

B. Aspects related to the administration of export and import Tariff Rate Quotas (TRQ's)

Following the third year review clause, the TRQ for import of pork and poultry meat, dairy products and sugar has been increased, as well as the quotas offered by the European Union for the import of certain categories of goods (grapes, plums, cherries, etc.) from Moldova.

In this context, it remains important for the relevant central public authorities to ensure efficient and transparent administration of TRQ. Business community has raised its concern regarding transparency in TRQ management and de facto implementation of the distribution mechanism. Following this there is a risk that the information on quota availability provided by the Customs Service is not accurate and does not reflect real data related to TRQ utilization.

C. Export of animal origin and composite products

With regard to the Action Plan on poultry and category B eggs export to the European Union, the Moldovan side submitted to the European Commission the filled-in questionnaire for the assessment of implementation of necessary export conditions. Moreover, at the end of January 2020, the Republican Veterinary Diagnosis Center (CRDV) received the certificate for the accreditation of six new methods: four of them in the animal health segment and two in the food safety area.

At the same time, it is important for the Government of the Republic of Moldova to launch discussions with the European Commission on obtaining the right to export dairy and processed meat products based on raw materials imported from the EU. In this respect, priority remains to be given to legislation adjustments and issues related to food safety, in particular to the implementation of the necessary animal traceability systems, animal pest control, unit surveillance, CRDV laboratory management and appropriate accreditation etc.

Regarding composite products, it is **essential to obtain the right to export products registered as Traditional Specialties Guaranteed** (pies, various pastries, *învărtită*, *sarmale*, etc.). Thus, the relevant companies that meet all EU quality requirements and standards, based on raw materials imported from the EU, could apply traditional recipes and export these products to the EU market.

D. SPS Relevant Issues

Import requirements for food products, subject to food safety control

In the context of the implementation of Government Decision no. 938/2018 on the Regulation regarding the National Agency for Food Safety (ANSA) border control of the imported goods and especially of the provisions of Annex XXII of the Moldova-EU Association Agreement, it still remains important to develop the **risk assessment mechanism for the import of goods**.

Thus, during 2019, ANSA developed a draft of the given methodology, which was unofficially discussed with the business environment. At the same time, ANSA launched the process of amending Government Decision no. 938/2018 which provides the performance of identity and physical control over 10% of non-animal food products, based on the known risk.

Status Quo: Although private sector companies have submitted proposals to improve the risk assessment mechanism for the import of goods, as well as the draft GD, both documents have not been subject to the legal procedure for the elaboration of the legal acts, provided in Law no. 100/2017.

E. Customs Valuation

At the end of 2019 amendments to the Government Decision no 974/2016, aiming to improve the Regulation regarding the way of declaring the customs value of goods was approved. However, it is important to mention the imperative need to issue additional internal orders to clearly guide the customs officers on the customs evaluation procedure, especially in the cases of similar goods being imported at a lower price. In any circumstance when the customs officer has reasonable doubts on the value declared in the invoice, there should be a legal possibility **to move customs control from customs clearance point to a risk-based post clearance audit**. It will also be vital to make the customs officer accountable for the content of the decision issued (which has to include all the necessary arguments) based on which the value against the invoice was increased.

II. TRADE AND SUSTAINABLE DEVELOPMENT

IMPLEMENTATION OF THE EXTENDED PRODUCER RESPONSABILITY PRINCIPLE (EPR)

Pollution Tax Refund Mechanism

Annex XI of the Moldova-EU Association Agreement provides that the Republic of Moldova had to establish the mechanism of full cost recovery in accordance with the "polluter pays" and the EPR principles within 4 years from the entry into force of the agreement. In the context of its implementation and at the request of EBA Moldova, the Ministry of Finance has initially considered to include the Establishment of the refund mechanism for the environmental tax in the Tax and Customs Policy for 2020-2022, however due to the Covid 19 situation and significant budget revenues reduction, there is a risk to postpone the introduction of the EPR and Pollution Tax refund mechanism in the Tax Policy until 2021.

As a result, with the financial support provided by the GIZ Moldova project "Economic Policy Advice to the Moldovan Government", EBA Moldova was contracted for the following activities:

- Analysis of the current Moldovan legal framework pertaining to taxation mechanism for environment pollution as well as implemented EPR principle;
- Overview of the key issues expressed by the Moldovan businesses in respect of the existing taxation mechanism applicable to environment pollution as well as its functionality as a result of the implementation of the EPR concept;
- Analysis of best practices within EU countries as well as from other countries comparable to Moldova with the aim of identifying existing economic tools for EPR implementation (Pollution tax exemption mechanism) ;
- Following the first discussion with Ministry of Finance and Ministry of Agriculture, Regional Development and Environment the preference was given to *Pollution Tax Refund Mechanism*, accordingly EBA team has developed the whole **set of legal amendments to enable Pollution Tax Refund Mechanism which is still under examination** by the above mentioned authorities;

Status Quo: Under a GIZ funded Project EBA Team developed the draft legal framework on the Pollution Tax Refund Mechanism which contains: the draft Government Decision, the draft Law on amending Law 1540/1998 on payment for environmental pollution, the draft Order on the modification of the Report form on the tax for goods that, in the process of use, causes environmental pollution and the Instruction for its completion, as well as the Impact Analysis document. The respective package of draft legal framework with comments from the line ministries is under examination by the Ministry of Finance to decide on the application/implementation thereof. The mechanism will be also discussed on the platform of Prime Minister Economic Council in order to ensure.

III. RULE OF LAW

A. Justice Sector Reform

In order to attract and retain European investors, it is essential to avail of a fair Justice and to respect the rule of law. However, there are multiple judicial cases affecting several EBA members where due process is not respected, Courts do not act with Transparency and, ultimately, the resolution of magistrates seems to be based on underlying economic motivations and unofficial hidden structures rather than on equal treatment and fair justice. Currently, there are several relevant examples where European Principles and Standards regarding a proper Judiciary System are being violated, such as the case of Premier Energy with the Court of Appeal of Cahul and the trials affecting Danube Logistics.

Premier Energy case

A lawsuit was filed against Premier Energy after a fire broke out in a commercial space with small scattered shops due to the combustion of highly flammable materials exhibited, allegedly due to an electrical peak. Throughout the judicial proceeding, multiple irregularities were committed in breach of the principles of Rule of Law, Non-discretion, Transparency and Due Process:

- The Court did not admit the testimonies, in favor of Premier Energy, from other clients connected to the same power line as the plaintiff that concur that they did not suffer any overvoltage in their energy supply (note: if there is a power hike in the network, it affects the whole power line, not just a single customer). The Court neither accepted the technical automatic records of Premier Energy that show the non-occurrence of overvoltage events in the network. The Court also rejected the technical expertise proving that the high voltage surge had been caused by an overload in the internal network of the consumer, for which Premier Energy is not responsible.
- The Court did not admit any of the two independent damage assessment reports prepared by independent experts proposed by Premier Energy (one from Moldova and the other from Romania). These reports state that the value of the damages is less than 2 M MDL, much lower than the 14 M MDL requested by the plaintiff and accepted by the Court. Inclusively, during the judicial process, it was refused to appoint a certified judicial expert to independently and accurately assess the damage.
- The Court did not accept the request of Premier Energy to verify the evidences, to challenge the judge and to transfer the hearings of the case to another judicial instance, requests promoted by Premier Energy given the existence of personal family relationships and “camaraderie” between the plaintiffs, the judges and influential people in the local judicial system.
- There are solid and well-founded suspicions of falsification of evidence and testimonies, which are in the process of corresponding legal investigation.

Danube Logistics case

Since 2014 Danube Logistics SRL, the operator of the strategic important Giurgiulesti International Free Port, is target of a raider attack involving multiple frivolous claims pursued in Moldova's notorious courts against the company, its employees, its Dutch shareholder Danube Logistics Holding BV and one of the company's ultimate beneficiaries. The raider attack is orchestrated by a former investor in the project with the objective to gain control of Danube Logistics SRL and thereby control of Moldova's only port.

Following flawed Moldovan court proceedings the former investor managed to establish a claim against one of Danube Logistics SRL's ultimate beneficiaries. This claim and the conduct of the proceedings are subject to a review by the European Court for Human Rights. Since October 2019 he attempts to enforce this claim against Danube Logistics Holding BV's assets in Moldova, and in particular to seize dividend payments as well as the majority of Danube Logistics SRL's share capital. This measure constitutes an illegal expropriation not

only of the property of the Dutch Danube Logistics Holding BV but also of the EBRD, who is entitled to 65% of the dividend and share sales proceeds deriving from Danube Logistics Holding BV's shareholding in Danube Logistics SRL. Despite the objections of Danube Logistics Holding BV and of the EBRD the Chisinau Appeals Court confirmed in contradiction to applicable law on 12 May 2020 the legality of the bailiff's approach. The ruling constitutes a severe deterioration of Moldova's business climate as it demonstrates that Moldova's notorious courts hold limited liability companies and financial institution liable for debts of any of their ultimate beneficiaries.

B. Data Protection

The period 2019-2020 proved to be quite complicated in terms of personal data protection requirements. Therefore, the outdated legal regulatory framework generates more and more obstacles to the business environment.

The draft laws transposing European legislation on personal data protection (GDPR), drafted back in 2018, on which the EBA community presented consistent recommendations (over 100 proposals) for amendment and adoption in the last Parliamentary reading were not approved. So far, the business community has not been informed on whether these recommendations have been taken into account. No discussions were organized on the Parliamentary platform or on the platforms of the regulatory authority.

Also, additional deficiencies should be mentioned:

- Unclear procedure, extended terms (up to 90 days) but also unjustified refusals to issue permissive documents. Thus, out of 1652 requests on registration and authorization as a personal data controller, 708 were refused;
- Exaggerated national legal requirements and non-compliance with the European data protection framework such as: written consent, registration/authorization as a data protection operator but also other requirements provided by GD no.1123/2010;
- Major confusions in the application of the regulatory framework provided by Law no. 308/2017 on preventing and combating money laundering and terrorist financing and personal data protection requirements, especially in the context of new regulations that come to impose sanctions of up to 5 million euros;
- Impossibility to conduct online commerce, cross-border transfer of data on EU servers but also European program solutions;
- Lack of display of guidelines and of the decisions of the Center for Personal Data Protection, which should concretely reveal the permitted practices and cases of violation.

IV. COVID CRISIS AND OTHER CHALLENGES FOR MD'S ECONOMIC DEVELOPMENT

A. Covid-19 impact

Among the main challenges expressed by the business environment in the context of the Covid-19 crisis, the following are to be mentioned:

- High level of Covid-19 confirmations versus limited capacity of the Moldovan (especially regional) medical systems to react and cope with Covid-19 outbreak;
- Expectations that a high number of small and medium enterprises could collapse, especially those who did not have enough liquidities to pay for forced unemployment (şomaj tehnic) accordingly they will not be eligible to apply for the national job subsidy refund;
- The appetite for business development shall decrease, as companies will prefer to make reserves and pay current debts (salaries and credits);
- Potential significant remittance's decrease (which in 2018-2019 achieved 15% of GDP), this would affect domestic consumption as well as investments in real estate and certain services;
- Growing rate of unemployment due to the unaffordable tax burden on the private sector;
- The rate of crediting in the banking sector has dramatically decreased (between March 16-30, only 5% of the planned amount of credits were issued);
- In the financial sector there is a growing trend of deposit redrawing with a higher rate of conversion of the MDL into Euro or USD;
- There is a risk of achieving 15 % of nonperforming credits until the end of 2020;
- There is an assumption of the opportunity of non-repaying the credits;

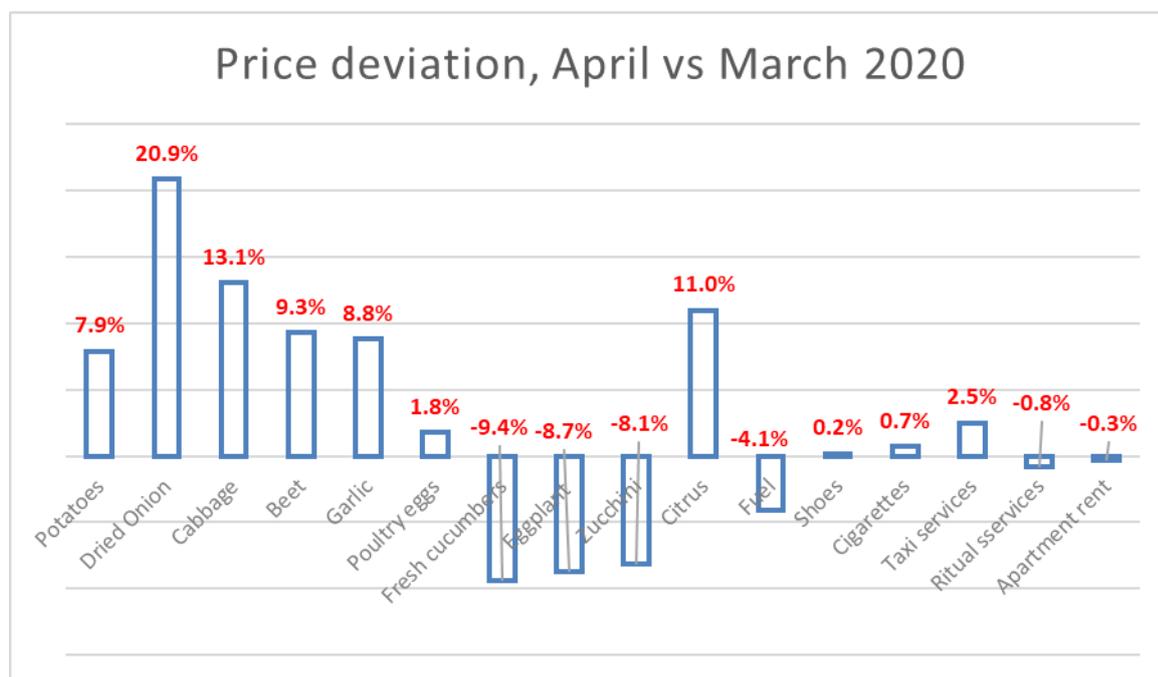
- The companies prefer not to pay their debts to other companies under the priority to pay the salaries and obligation, in the meanwhile create a reserve for the next period;
- Increasing phenomena of not paying the utility bills, thus creating liquidity problems for utility companies;

B. Hydrological drought

The authorities announced an unprecedented drought. As result, cereals' harvest will be reduced by approx. 25%, which will generate dramatic reductions of cereals' exports and of processed agricultural products. The atmospheric precipitation that fell from the beginning of the vegetation period, until the end of April 2020, was insignificant for a correct development of the autumn crops. Their ratio to the multiannual average shows that the percentage of precipitation was from 33% in Sângerei to 73% in Camenca, on average, and the districts located further north being provided with about 50% of normal rainfall. The Central and Southern were affected the most. The productive moisture reserves in arable soil, at a depth of 20 cm, have values of 13 and 17%, at the end of April. Latest rains have partially improved the situation, however the harvest of wheat was already compromised. Farmers reported significant damages provoked by heavy rains and storms in May-June.

C. Impact on Prices

According to the National Bureau of Statistics' data, the consumer price indexes are constantly rising. The increase in average consumer prices by 0.17 percent was determined by the increase in food prices by 1.17 percent. With respect to the non-food goods, the decrease of prices by 0.8 percent was directly influenced by the reduction of fuel prices - by 4.1%. Also, it is important to mention that the tariffs for the services provided to the population in April 2020 remained at the level of March 2020.



V. PENDING ISSUES

A. Tax of 2.5% for mobile services and portability fee for mobile operators

In the context of the discussions on Tax policy for 2021, it was proposed to exclude / revise the luxury tax, a process that unfortunately ended with the emergence of a new tax - the portability fee in the amount of 50% of the payment for the operation. In the EU, the trend is to reduce the costs of mobile operators as well as electronic communications operators, thus reducing consumer costs, while in the Republic of Moldova, these costs will increase by 1.5 million Euros, costs to be covered by operators. This will diminish any investments in this field which is one of interest not only in Moldova but also worldwide. Thus, the EBA considers that maintaining the 2.5% tax is an unjustified and discriminatory measure in the current situation and future

context, given the lack of liquidity, which significantly increases the tax burden exclusively on the electronic communications sector, the strategic sector for the national economy.

Status Quo: A series of legal proposals were submitted to the Government which were not accepted and not considered for approval under the Tax Policy for 2020-2022.

B. Insurance Sector

Main issue of concern for the insurance sector is financial stability of the market. Unfortunately, not all market participants comply with financial requirements. There are indications that information provided in financial reports of some companies is not correct. In this context, proper audits by international auditors would be required. If not properly managed by the National Commission for Financial Markets (NCFM), the financial stability of the market might be at risk.

C. Renewable Energy (RE)

Though the energy regulator (ANRE) has approved the feed-in-tariffs for the different RE technologies, the situation as of now is that no one PV eligible producer has been confirmed based on fixed tariffs and no RE tender has been launched so far by the government, disrespecting the schedule in place.

In the last years, ANRE has reluctantly and selectively assigned tariffs to new RE projects, where a range of prices has been discretionally awarded varying from 8.1-9.6 c€/kWh (in 2017) to 4.1-4.6 c€/kWh (in 2018).

In order to push forward the deployment of RE, the schedule of energy tenders should be updated and, more importantly, fulfilled by the authorities. Also, the existing capacity limits based on type of RE technology and the restrictions on ownership should be, in our view, revised by the government for the effective development of RE in Moldova. In this respect, subsidies for privates and SMEs, tax breaks, reduction or exemption of VAT for RE project components and mandating solar on new buildings would help Moldova secure renewables capacity.

Since the new clean energy law came into force in March 2018 no major RE project has been actually developed. In order to develop RE in Moldova, the main issue remains the effective willingness of the authorities to effectively support clean energy. Several European investors have expressed their willingness to develop RE in Moldova, but after a time, they get frustrated when realize that things do not effectively move forward, and that is another opportunity lost for Moldova.