

CORRUPTION IN MOLDOVA: MACROECONOMIC IMPACT

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CORRUPTION IN MOLDOVA: MACROECONOMIC IMPACT

1. Corruption in transition countries: its genesis, causes, main forms

$$\text{Corruption} = \text{Monopoly} + \text{Discretion} - \text{Accounting}^1$$

By the beginning of '90s one of the biggest problems for the transition countries was shadow economy, and the main objective of the state policy in this domain was supposed to be the creation of conditions for the incorporation of shadow economy into the formal one. During the last years the problem modified into a national tragedy for a series of countries – corruption. Corruption in many cases undertook the mechanisms, structures, and functions of the state.

If at the beginning of the decade corruption in transition countries served in a big part as a brake to the economic development, creating obstacles for local producers and pushing out the potential foreign investors, then, actually it simply blocks the reforms in the country. Any attempt to improve the acting legislation does not have any positive expected effects due to the impact of corruption; the economy does not develop according to market rules, there are no competition and progress in utilizing the disposable resources, state debts grow spontaneously, pauperization of the society deepens, a decrease of population's credibility in the state and a creation of a conflict situation take place.

Data of the opinion poll among more than 150 of top managers and public figures in more than 60 countries showed corruption as the most serious problem, which impedes the development of countries².

According to the results of the investigations, accomplished by an investigating group and World Bank, countries of CIS hold the first place amongst all other regions of the world³ in terms of corruption spread.

A simple *definition of corruption* can be formulated as follows: abuse of power for private gain by the state officials.

Causes of corruption can be economic, institutional, politic, social and moral:

- The *economic* ones include: unlivable budget, low wages for state employees, delays in payment of wages;

¹ Governance and the Economy in Africa: Tools for Analysis and Reform of Corruption, IRIS, University of Maryland at College Park

² EBRD, 1997, Transition Report 1997 – enterprise performance and growth, (London European Bank for Reconstruction and Development)

³ IMF, George Abed, Management and transition economy, 1998

- The *institutional* ones are: lack of real will to fight corruption, lack of strategy in this field, high level of discretion in the work of legal bodies, an inadequate accounting system, lack of transparency in the legal system, weak state policy generating rent-seeking, career promotion without real performance;
- *Political* causes include: possibility to fight political opponents under the slogan of fighting corruption, interest of some political groups in the economic and financial collapse of the state, thus willing to return to the old dictatorial system, import of corruption.
- *Social and moral* causes: demoralization of the society, ethical values erosion caused by the corruption amongst the top level employees, insufficient information of population, insufficient work of mass-media, public tolerance.

Main forms of corruption are: acceptance, soliciting or extortion of bribes, patronage, nepotism, theft of public goods, causing losses to the state, political corruption, etc.

Bribes – in order to obtain state contracts (choice of firms, terms and conditions for contracts), assure state guarantees for credits, obtain facilities, material and financial benefits, preferential support of patronaged enterprises, shading investigated violations, non-application or diminishing penalties, obtaining licenses, exclusive rights for economic activities, for speeding-up delivering documents, obtaining political positions, employment in state structures and prestigious positions.

Thefts – spontaneous privatization of public enterprises, equipment, financial sources, uncontrolled utilization of enterprise funds, obtaining credits without repayment, payment of wages to non-existent employees, etc.

Political corruption – violation of the election legislation, financing the electoral campaigns, solving parliamentary conflicts in illegal modalities, lobbying;

2. Macro impact of corruption

The macroeconomic impact of corruption is essential in any country. Data of numerous studies in this field prove it. Vito Tanzi⁴ says that corruption serves as an impediment to the three main functions of the state – macroeconomic situation, resource allocation, redistribution of incomes and welfare.

Paolo Mauro⁵ made an attempt to find the impact of corruption on investment and growth. He shows that the decline of corruption index (Transparency

⁴ Tanzi, Vito, and Hamid Davoodi, 1995, “Government Role and the Efficiency of Policy Instruments”, IMF Working Paper N97/139 (Washington, D.C.: International Monetary Fund)

⁵ Mauro, Paolo (1996), “The Effects of Corruption on Growth, Investments”, IMF Working Paper N96/98

International) by a medium square deviation (2.4 points) is connected with a 4 percentage points growth of the share of investments in the economy and a 0.5% growth of pace (rhythms) of economic growth.

Shang-Jin Wei⁶ analyzed the impact of corruption on direct foreign investments. He found that increase of corruption index by a unite (on the ten level scale) is equivalent to growth of the marginal tax rate by 4.7 percentage points, and is accompanied by a decline of direct foreign investments by 0.9 percentage points.

An inverse link between corruption index and Government investment⁷ is investigated by Vito Tanzi and Hamid Voodi.

The investigation of Gupta, Davoodi, and Alonso-Terme⁸ found that there is a strong correlation between corruption and degree of inequity in the country. But the main affecting the economy impact of corruption is, certainly, growth of shadow economy.

The results of numerous cross-countries comparative studies of shadow economy indexes and economic performance (Heritage Foundation, Transparency International, Freedom House Rankings) can be used in order to show a quantitative relation between the growth of the degree of corruption of the country, the volume of illicit transactions, and economic decline.

Corruption index (Transparency International) in the countries of the European Union fluctuates from 0.54 in Denmark (meaning a practical lack of corruption) to 5.5 in Italy, total corruption index corresponding to the value of 10. The average for EU oscillates around 2.5. For the countries in transition, which hope to join the EU, this index is at least 2.5 times bigger, reaching from 4.5 in Estonia to 7.6 in Russia.

On this scale Moldova is placed together with Bulgaria after Romania, and is followed by the Ukraine.

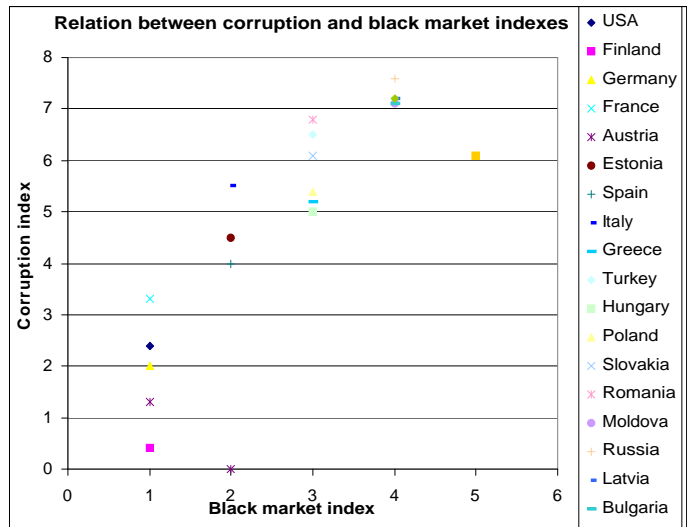
However, it should be mentioned that the evaluation of the corruption index is more likely based on the evaluation of the level of perception of corruption by the population, rather than on the evaluation of its real dimensions. Therefore, in a traditionally more democratic country this index can be overestimated. At present, there are attempts to develop the Bribery Propensity Index.

⁶ Wei, Shang-Jin, "How Taxing is Corruption on International Investors", NBER Working Paper Series, Working Paper 6030

⁷ Tanzi, Vito, and Hamid Davoodi, 1997, 'Corruption, Public Investment and Growth', IMF Working Paper N 97/139 (Washington, D.C.: International Monetary Fund)

⁸ Gupta, Sanjeev, Hamid Davoodi, and Rosa Alonso-Terme, 1998, 'Does Corruption Affect Income Inequity and Poverty?', IMF Working Paper

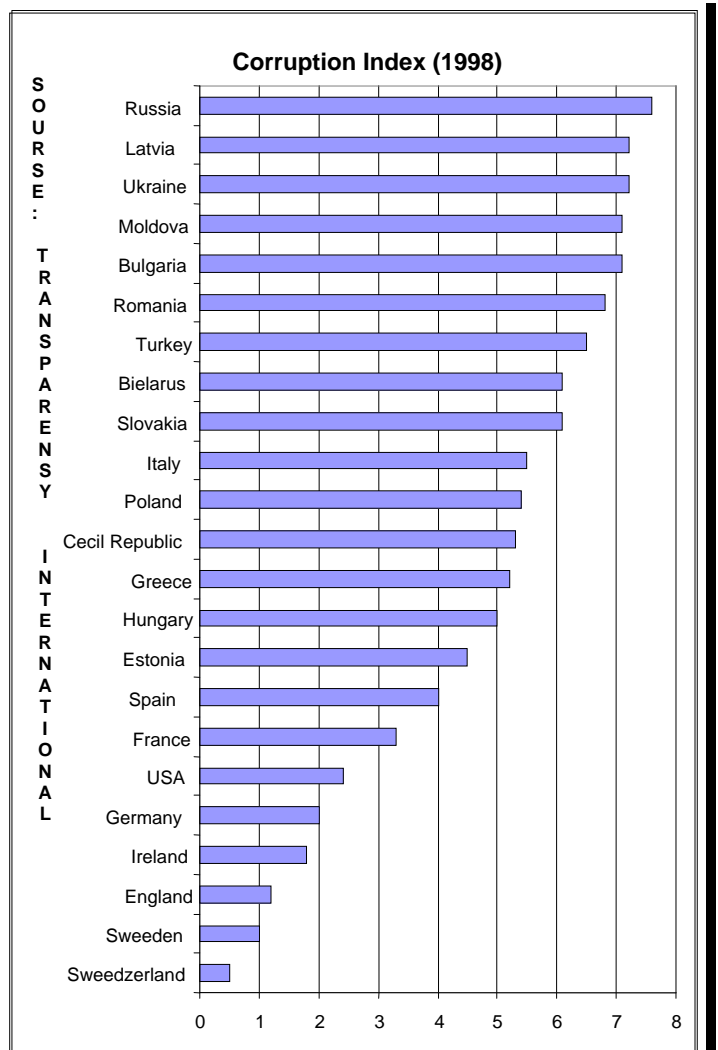
High level of corruption in transition countries implies growth of black market (Heritage Foundation), the index of black market varying from its minimum –1 in Austria, France, Germany, Finland, 2 - in Italy, Spain, Estonia, 3 - in Greece, Turkey, Hungary, Poland, Romania, 4 – in Latvia, Bulgaria, Lithuania, Moldova, Ukraine, Russia, and reaching its maximum of - 5 in Georgia and Belarus. Our calculations also display an inverse link between the degree of corruption and GDP per capita.



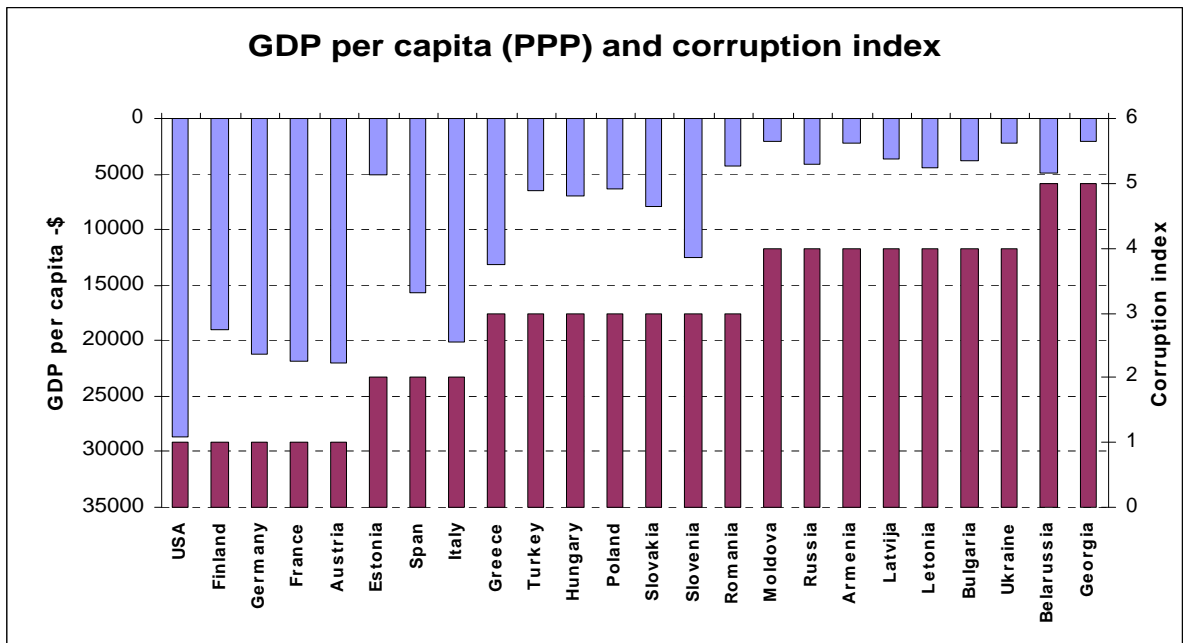
An inverse relation between corruption index and the index of economic performance in transition countries persists, the latter having as basic components the politic system, the degree of mass-media freedom, the rule of law, the degree of public administration, the development of private sector.

The relation between corruption and economic development is dual: on one side, low economic development, small incomes stimulates growth of corruption. On the other side, corruption breaks the development in the official economy, and stimulates the development of shadow economy. This last impact will be the main subject of our study.

The economic evolution of the Republic of Moldova, similar to other countries in transition, may be characterized by a deep decline. In 1998 official GDP formed 33% of the level of 1990, GDP per capita in 1998 formed a frustrated figure – 454 USD, a smallest one in Europe. The accuracy of this three-fold decline, accompanied by an extension of constructions, of the



private fleet, of durable goods sails, rises doubts. Undeclared incomes, tax evasion and shadow economy are discussed more and more.



Freedom House Ranking - composition								
	political progres	ind.civil society	independ. mass media	legal system	public ad-ministr.	privati-zation	econ. perform.	privat share in GDP
Albania	4.25	4.25	4.75	4.75	4.75	3.75	4.25	75
Armenia	5.5	3.5	5.25	4.75	4.5	4	4	50
Belarus	6	5.25	6.25	6	6	6	6	15
Bulgaria	3.25	4	3.75	4.25	4.25	5	5.75	45
Croatia	4	3.5	4.75	4.75	4	4	3.75	50
Czech Republic	1.25	1.5	1.25	1.5	2	2	1.75	75
Estonia	2	2.25	1.75	2.25	2.25	2.25	2	70
Hungary	1.25	1.25	1.5	1.75	1.75	1.5	1.75	70
Latvia	2	2.25	1.75	2.25	2.5	2.5	2.5	60
Lithuania	2	2.25	1.75	2.25	2.5	2.25	2.75	65
Moldova	3.25	3.75	4	4.25	4.25	4	4	40
Poland	1.5	1.25	1.5	1.5	1.75	2.25	1.75	60
Romania	3.25	3.75	4.25	4.25	4.25	4.5	4.75	60
Russia	3.5	3.75	3.75	4	4	3	4	60
Slovakia	3.75	3.25	4.25	4	3.75	3.25	3.5	70
Slovenia	2	2	1.75	1.75	2.5	2.75	2	45
Ukraine	3.25	4	4.5	3.75	4.5	4.25	4.25	40

The shadow (underground, informal, second, unofficial, invisible) economy “smoothes” the impact of economic shocks in the transition countries.

Corruption, as well as shadow economy may have a severe impact on economic, social, political and ecological development of the country.

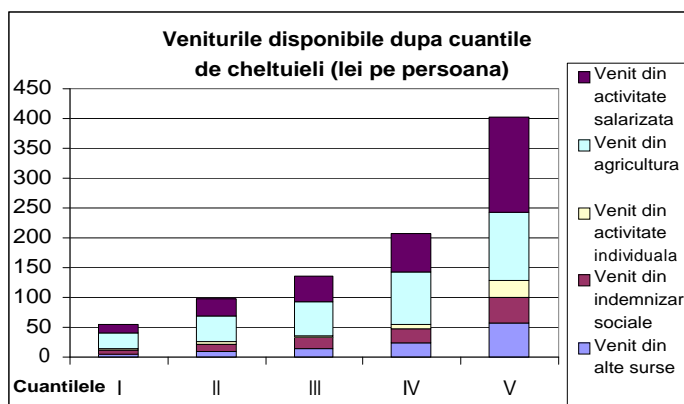
Social implications

Shadow economy creates *work places, which reduce the unemployment level.* The significant gap between the official record of unemployment rate (about 2% according to Statistical and Sociological Analysis Department, and 9.4% based on the criteria established by International Labor Bureau) and the fact that more than one

third of able population is officially treated as inactive, without clearly stating any source of their living, suggest that a considerable portion of population is involved in informal economic activities. The calculations performed by the Strategic Investigations and Reforms Center show that about 47% of the labor force is involved in such economic activities.

The shadow economy and corruption *generates additional income* for the participants and members of their families, and sometimes it is the only source of their living. A sector's existence in parallel with the formal economy, in fact, generates 60% of additional income. This income is, however, *unequally distributed among the population* and the gap between the rich and poor is actually greater than that stated in the official record. Hence, the consumption of meat in families officially stated as having the same level of income is on average 60% higher for those employed with the private agricultural sector than it is for those engaged in the public sector.

Corruption creates *social inequity*, the vulnerable layers of society are the most severely hurt. With no political influence, the vulnerable layers of population are often subject to an increased social pressure. Thus, according to the reports on a Household Budgets Poll carried out by the Statistical and Sociological Analysis Department with a financial assistance provided by the



World Bank, in 1997 the amount of social benefits received by each member of the families having a highest level of income (level V by the available income) is about five times higher than those received by families with a minimal level of income (level I). An inequitable social system makes its appearance, where layers of population earning a higher income enjoy most of the social benefits.

The *population involved in the underground sector of economy is not entitled to social assistance and protection from the state*: the requirements with regard to working conditions, working time and minimal labor remuneration are not met. There is an abuse of the work performed by minors and women, the system of sick leaves on a temporal work inability is not in operation, the system of professional vacations is ignored, so is the pension system, etc. A special case is the illegal employment of Moldovan citizens in other countries. The agreements between the Republic of Moldova and other countries on the export of labor force do not work. Therefore, there are many cases where upon the completion of work, the individuals illegally employed abroad are paid less than initially agreed, or are not paid at all and expelled from the country, or they become slaves of some local criminal organizations.

The presence of a large underground sector and corruption *gives rise to an excessive tax burden*. The state budget is reliant for its income on official economic

activity. However, most of budget expenses also serve the interests of those people who are not paying taxes (enjoy benefits in paying energy bills, public services, etc.). Therefore, while the average tax burden for the economy is about 30%, the actual tax burden on some economic entities operating within the formal economy is obviously higher (see chapter 4).

The shadow economy and corruption *impedes human development of the nation*: an increased level of tax avoidance reduces budget receipts, which in turn, causes the failure of social, pension, education, health, environment policies. A weak legal framework erodes moral principles of the society. According to an opinion poll conducted as part of the “Development Strategy” project, about 52% of the respondents believe that it is impossible to conduct a business activity in the country without breaking the law. There occurs the situation where breaking the law has become a standard behavior.

Another effect is *harming to consumers* by providing them with low quality goods and services. The findings of a production quality inspection on a network of trade outlets conducted by the National Standards, Metrology and Certification Centre, show that contraventions range from about 40% of the total food products to 70% of the children products. In imported goods, contraventions make up 79%.

Corruption functions in direct connection with criminal world thereby *threatening personal security of the population*.

The economic impact of shadow economy and corruption takes place in a number of ways. First of all, the *transaction costs are increasing*, particularly, in carrying out small business activities and decreasing the competitiveness of the products and services. According to the estimates, the amount of additional payments to be made for licenses, “roof” (informal payments to state employees of criminals in order to secure the business), ensuring quick settlement of formalities by the state officers reach 40% of the profit.

The economic instability triggered by the expansion of underground sector, racket, corruption, bureaucracy in preparing business documents and Government’s inability to ensure producers’ security *discourage potential investors and innovative ideas*.

The phenomenon of corruption, actions taken in favor of some individual persons, evasion of tender and competitive procedures causes *increase in the cost and drop in the quality of public projects*.

Another consequence of corruption is *inequity, unfair competition* by using state institutions in exercising pressure, falsifying the information on competitors, technological and industrial spying, racketeering, entering into monopolistic agreements, etc.

Diverting of funds has a greater occurrence, *which reduces economic efficiency*.

The prolonged development of corruption and shadow economy leads to *macro-economic instability, country's vulnerability to financial crisis*. The annual macro-business turnover in Moldova is estimated at 200-250 million USD, which is 3.5 –4 times higher than the amount of foreign direct investments in Moldova made within one year, and of the amount of foreign currency reserves with the National Bank of Moldova. The drug traffic is an area controlled by several persons. Therefore, any capital outflow or inflow triggered by this sector alone could, in fact, impair the stability of financial system.

The impact on the political security of the state

The corruption favors the emergence of an economic and political clan, which imposes its wishes on the society without taking into consideration the demands of society, causing an *enormous growth in state debts*.

The increase in the level of tax avoidance and a decline in the budget revenues have determined the *failure of policies with regard to enterprise and small business and social support, education, health, environment, remuneration of budget employees*. This, in turn, impoverishes the population, and undermines the confidence in promoted reforms.

Government's inability to ensure that its officials are paid decently paralyzes state institution, *prejudices the citizens' rights and guarantees ensured by the constitution, discredits the state system, causes the state to lose its credibility*.

The impact on environment: Because certain groups of people impose their interests on the society in order to obtain immediate profits without "amortization" of environment resources, the environment condition is deteriorating.

Corruption is a self-generating process. If the state employees do not receive their wages during 4-5 months, bribes become the only stable source of their income. Then an evolutionary shift takes place into a vicious circle: corruption → economic decline → insufficiency of sources for the budget → delays in wage payment for state workers → growth of corruption. Moreover, it is easier to blackmail and force a person perceived in corruption to repeat corruptive actions. Unwillingly, this person starts to belong to a strong repressing system.

Therefore, starting from 1998, official data regarding the results of audits and inspections became more "optimistic". In 1998 there were registered 2910 violations of economic and financial legislation, by 244 less than in 1997, losses being estimated at 103 million lei. Chisinau City Police marked a decline by 13% in the number of registered crimes, although 298 cases of concealing crimes were discovered. There were collected 11% fewer taxes in Chisinau (853 million lei). The 10% decline in industrial production and an 18% inflation could not explain this phenomena. Two parallel processes take place: a) hiding or closing criminal files, b) decreasing rate of small crimes and growing of the big ones.

Unfortunately, the actual situation in the Republic of Moldova, as well as in many other countries in transition, does not contribute to an increase of credibility

of Moldova as an economic and political partner. The share of underground economy got striking proportions and tax evasion raises continuously. The lack of control upon state employees' activity and low enforcement, as well as delays in payment of wages to the latter, contributed to the extension of corruption and increasing level of the economic crime in the Republic of Moldova.

According to our estimates, the tax evasion in the Republic of Moldova grew up from 4% of the consolidated budget revenues in 1994 to 20% in 1997 and 32% in 1998. The average evaded tax rose from 7 thou lei per taxpayer in 1997 (10 thou lei per legal entity) to 12 thou lei in 1998 (23 thou lei for legal entity). The rate of rule breakers in the total number of entities subjected to audits grew from 305 in 1994 to 51% in 1997, and 57% in 1998.

Data of the National Center for Standardization, Metrology and Certification show that the rate of law violations detected during the controls of consumer goods varied from 40% for foods to 70% for the goods for children. In the division – local-imported goods most of all account for the imported goods – 79%. The quality of goods varies throughout the country.

Data of the scientific-practical conference “Organized crime and shadow economy in the Republic of Moldova” held under the aegis of the Ministry of Internal Affairs of the Republic of Moldova, Academy of Police and the Independent Association of Criminology, shows that corruption in Moldova achieved striking proportions. Lack of state power creates conditions for emerging mechanisms and structures that quickly can substitute the state structures.

Ordered murders: an existing practice of repeated (2-3 times) temporary releases from jail of the convicted individuals, with a view to commit an ordered murder, is recognized. There are about 300 criminal groups, 35 criminal clans, which control the economic, political, and social performance of the country. Thus, the problems of non-payments are rather solved by pressures on behalf of criminal structures, playing the role of informal courts, by charging 50% of the indebted amount.

On the territory of Moldova there are four channels of *drug trafficking*. Only the monthly traffic of heroin is estimated to reach the volume of 150-200 kg (for information: the wholesale price of 1 kg of heroin amounts to \$1.5 thou in Pakistan, 10 thou \$ in Turkey, 40 thou \$ in England, the retail price reaching \$120 thou). On the territory of Moldova there are clandestine laboratories producing drugs based on local, much cheaper technologies, and this presents an essential threat for the local evidently poorer population. During the last five years the estimated number of addicted persons rose from 3 thou to 60 thou people. Only in 1998 their number grew 5 times in comparison to 1997. Drug industry is highly concentrated, about 60% of drug transactions are carried out by local Gypsies (for information: Gypsies make up about 0.3% of the total population of Moldova).

The annual volume of narco-business in Moldova is estimated at \$200–250 million, this figure *exceeding 3.5-4 times the annual direct foreign investments* in

Moldova. It is clear that the “efficacy” of running this brunch is definitely “higher”. Possibilities to corrupt the state officials are extremely big. That is why the list of narcotic and psychotropic substances proposed by the specialists of the Committee of Drug Control undergone essential “modifications” by the moment of its adoption and publication in the “Official Monitor”. A number of substances, which can be easily produced on the territory of Moldova, vanished from the above-mentioned list. That is why the custom service does not have an elementary facility of drug detecting dogs, there is not any database on drug trafficking, or an unique informational system of the force ministries and the criminal files do not “reach” the court (their total number having diminished from 15 in 1996 to 10 in 1997 and 9 files in 1998). That is why extremely expensive cars with four degree of protection are used for the transportation of drugs.

Smuggling: According to the data of custom service, the detected volume of smuggled goods grew from 2.7% of the total export-import in 1997 to 10.6% in 1998. During the same time, the number of criminal files reaching the court diminishes continuously, criminal files are closed (from 28 open criminal files no file was investigated in 1998).

Data regarding the *volume of illegal export-import transactions* are more relevant. An accomplishment of a cross-checking of Moldovan and Ukrainian information regarding Moldovan exports to Ukraine shows that the data from the Ukrainian side is almost double. This can not be explained solely by the “role” of Transnistria. The same situation takes place in the relationships with Russia. It is little probable that workers of the Ukrainian and Russian custom services are likely to be more honest than those from Moldova, therefore the real distortions could be even greater.

This fact could be not so surprising, if to take into account the current situations when custom services detain full trains with illegally transported goods, and after a call from the “top officials”, they are constrained to let the train move ahead.

The spectrum of corrupted actions characteristic to the *management of public property, accumulation and utilization of financial resources, execution of state control* is quite wide. Amongst the most characteristic to Moldova can be mentioned the following:

- Improper formation and utilization of the state budget funds, lack of methodological norms of their formation and utilization, illegal financing of structures and activities not envisioned in current legislation;
- Inefficient and irrational utilization of budget resources by the state-owned institutions due to improper organization of state-owned budget institutions, financing that leads to laundry of enormous amounts of state funds, improper utilization of investments and donations, including in foreign exchange, as well as their transfer to certain commercial structures that use them for a long time or for a symbolic fee;

- Irrational and inefficient utilization of investments and credits as a result of a bad allocation of state resources, improper utilization of investments and credits given to economic agents;
- Evasion of taxes, fees and other compulsory payments due to the state budget;
- Violation of price discipline, especially ungrounded increase of prices;
- Waste of public property as a result of intentional non-accounting of certain objects of state property, illegal rent of premises and equipment, ungrounded or illegal privatization of state property, violations while purchasing of 20% of shares by the personnel of the enterprises without any tender, diminishing the value of property, and excluding the former staff, including outsiders in privatization process, as well as unreal evaluation of property;
- Irrational and inefficient contracts with certain economic agents, especially with non-government structures;
- Unsatisfactory accounting of financial and economic activity which enables government officers to freely dispose of the state property, including budget resources, to their personal interests.

In a short while Moldova transformed into a corrupted and kleptomanian state, with a mafia-driven psychology. How could be explained the fact, if not through corruption and lobbying, that the legislation of Moldova even does not include the term “racket”, there are not foreseen special measures towards prostitution, it is not adopted a special system of gambling taxation? Moldova, being over-indebted for energy resources, imports natural gas at prices much higher than international ones, and does not even ask for charges on the transit of natural gas through its territory (for information: the payments for the transit of gas through the territory of Ukraine exceed the GDP of Moldova). More than this: Moldova does not have gas counters at the entrance and exit from its territory. The only explanation is a group interest, which is completely opposite to the interests of the whole society.

This situation is characteristic to autocratic states, where practice is missing of self-organization, based on horizontal links, reciprocal credibility and solidarity; in this type of states for a long time a bureaucratic hierarchy based on norms, mainly vertical relations of domination-subordination and tutelary-dependence were maintained.

By no way the author of this study is wishing to say that Moldova is an exception between the NIS countries regarding the spread of corruption and shadow economy. The idea that fighting corruption in NIS countries is the only way to reduce shadow economy, crime, and to obtain a durable economic development is the basic idea of the study.

3. Estimation of shadow economy in the Republic of Moldova

Shadow economy consists of all forms of economic activities which are not reflected in the official statistics, such types of activities which generate added value, but are not controlled, illegal or legal, but not legally registered for such reasons as tax evasion or unfavorable conditions for operating within the formal (official) economy.

However there is a difference between the definition of shadow economy used by scientists and statisticians. According to the definition of the last ones, shadow economy is expressed as legal production taking place outside formal frameworks – a set of production activities which are in harmony with the laws and regulations of the country, but about whose quantity, value and outcomes information is not given to the authorities in order to avoid paying taxes.

This different approach to shadow economy results in different estimation of its extend.

There are many factors which can serve as an *indication of the existence of such phenomena* in the Republic of Moldova and of their social consequences:

- A reduction in purchasing power of the average salary and manifold increase in the amount of luxury goods and motor cars purchased, increase in the amount of individual constructions;
- A higher pace of GDP's reduction than that of electricity consumption. An increase in the proportion of electricity losses in the total consumption from 10% in 1990 to over 30% in 1997 and that a rapid rise in prices for energy resources did not cause a decline in the energy intensity of GDP (on the contrary, over the last three years alone this index increased by 21%) may serve as an indication of an extensive occurrence of embezzlement and informal production;
- A decrease of the proportion of salary in the total household income from 71,6% in 1992 to 22.5% in December 1998;
- Significant differences with regard to the information on export and import operations with major partners. An analysis conducted by matching moldovan and uckrainian information on Moldova's exports to Ukraine showed that the Uckrainian statistical reports indicate almost a double figure, which cannot be only accounted for by the portion of Transnistria's exports. So is the case for the information on export-import operations with Russia.
- The real interest rate on credits (30%-40%) significantly exceeds the average profitability in official economy (less than 10%); this partially indicates that the actual income in some industries is higher;
- Increase in the level of unemployment and a lower chance to get a job in the official economy without any significant protests from the side of the population

(the chances for an officially recorded unemployed to get a job decreased from 0.7 in 1992 to 0.18 in 1998);

- A distinctly low percentage of legal trade activities in relation to the total. Actually, the trade in organized market makes up only 5-10% of the total. This can be arrived at by calculating the goods sold per capita. It is difficult to conceive that, according to statistical records, 2,5 kg of meat, 600g of fish, 200 g of butter per capita is sold within one year;
- Low level of fiscal discipline, the amplification of tax avoidance and a decrease of budget revenues. The actual tax burden in the real sector of economy between 1992 and 1997 has been calculated based on financial reports filed with the Statistical and Sociological Analysis Department. Our calculations show that within this period of time the official tax burden increased from 34.5% in 1992 to 44.9% in 1997 (in industry 50%, agriculture 40%, construction 38%). In the Republic of Moldova the extent of tax avoidance grew from 4% of consolidated budget income in 1994 to 32% in 1998.

The shadow economy, as a complex phenomenon, includes negative, counter-productive aspects, which need to be eradicated, as well as positive, productive aspects, which need to be incorporated into the official economy.

Among the *negative aspects* of the shadow economy are the following:

- state budget losses due to tax evasion;
- shadow economy is one of the reasons of the decline of economic discipline and hence of the people's decreased respect towards state institutions;
- being out of the state control, the shadow economy can be one of the potential sources of economic shocks, economic and political instability;
- shadow economy leads towards distortions in market information and changes the effects of the state policy;
- shadow economy is closely related to the organized crime;
- labor legislation requirements are not working within the shadow economy (working hours, paid holidays, sick-leaves, etc.);

Among *positive aspects* of shadow economy are the following:

- shadow economy brings additional revenues for its operators and members of their families, being sometimes their only source of income;
- it creates jobs thus decreasing the unemployment rate;
- shadow economy increases the competitiveness of goods because of lower prices caused, very often, by tax evasion;
- shadow economy can be more elastic, more adjustable to the new conditions, bypassing the bureaucratic obstacles faced by the formal economy;
- it can serve as a factor of market stability and balance, often offering exactly those goods and services which are in demand in the formal economy;

- in a way, shadow economy can be a factor of financial stability due to the transactions performed in national currency, covering the monetary excess with goods and services.

It is possible that the *shadow economy phenomenon has an anti-cyclic character* and grows up, even faster in countries experiencing economic decline.

Forms of shadow economic activities include:

- ❖ Clandestine, surreptitious undertakings, involving partial or total avoidance of taxes and social insurance contributions (such as the production of goods or provision of services “on the side” by self-employed people in micro-companies; the hidden activities of different types of professional workers; the provision of domestic assistance; the sale of merchandise from home; and the illegal renting of apartments and houses;
- ❖ Work taking place outside the employee-s main working time (for example, in a second job (including complementary activities in the villages), such as repair of domestic and other machines and installation at home; re-selling activities; book repair; doing work at home for another person; consultancies; journalists working at home, etc.);
- ❖ Those who have no evident employment (providing home help and baby-sitting; taking jobs without reporting them, or without papers or permission; students and child labor; the work unregistered migrant workers;
- ❖ Hidden incomes from capital activities (renting of rooms and apartments; usury; tax evasion in small co-operatives, etc.).

The main forms of shadow economic activities which should be mentioned in Moldova, taking into consideration the above mentioned definition, are: corruption, hiding of production and revenues, tax evasion, illegal import-export operations, illegal privatization, production and marketing of fake or uncertified goods and services and others.

Participation in the shadow economy in western countries ranges in value from 5% to 40% of gross national income: in Italy, it takes 20-30% of GDP, in the USA it is 25%, in Great Britain around 5%, in Canada 10%, in Sweden 7%, in Switzerland and Austria around 5%, in Israel over 20%, and in Spain between 14 and 20%.

In Latin America, the shadow economy represents the last resort against unemployment and poverty. Very often, it takes the form of illegal trading with drugs, food, alcohol or electronic gambling machines. In addition, towns in Latin America are overloaded with street sellers and mobile shops which mostly have very cheap merchandise, food and personal effects. There are countries, according to the opinion of the Central Latin American Traders (CLAT) organization, where around 50% of workers are engaged in the informal sector. In Peru and Bolivia, the shadow economy has bigger share of GDP than the formal economy. In Argentina, where six out of ten workers work on their account, as self-employed, the shadow

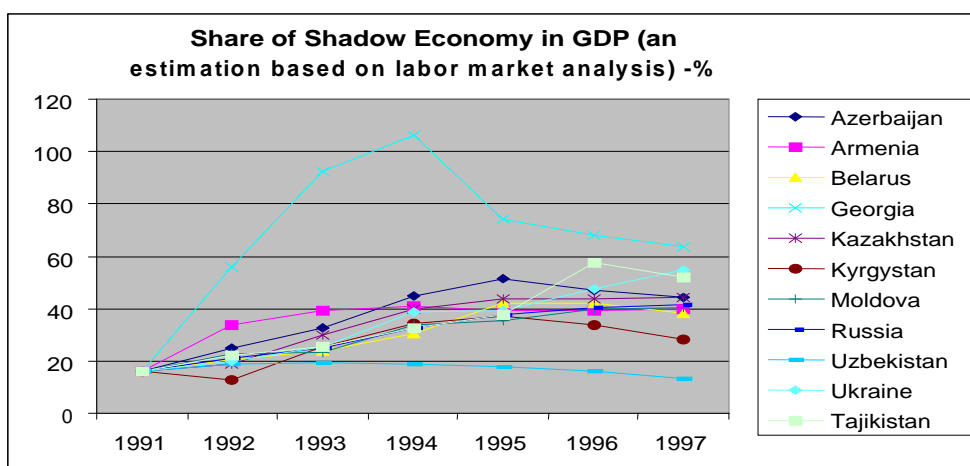
economy while, at the end of eighties, the informal sector had a yearly growth in employment of 7%, compared to 5% in the public sector and only 0.5% in the informal economy.

The shadow economy in transition countries, especially in NIS, differs to some extent from shadow economies in developed countries. This is manifested in the fact that the state sector is very active in realizing shadow economic transactions, often the state property is used for obtaining unofficial personal gains by the state employees. A clear divide between the official and nonofficial sectors is absent, the labor force of the underground sector includes high skilled professionals. The shadow economy in NIS countries grew up so substantially not only because of the economic decline, but also as a result of involving in the privatization process of new objects – land, assets of enterprises, etc.

Methods of estimation of the shadow economy’s volume are bound to be not fully accurate and give a very approximate picture of the real situation. Moreover, the results will differ depending on the method used. Therefore, for making an international analysis of the degree of presence of this phenomenon, it is necessary to use the same methods of estimation and to take averages for every country.

The evaluation of the extent of the shadow economy in the Republic of Moldova was done based on six methods: *transaction method, currency-ratio method, turning assets analysis method, power consumption method, structural method and Italian (labor market analysis) method.*

*Italian (labor market analysis) method*⁹ calculates the size of the underground economy on the basis of estimates of the total labor input into productive activities. In this study a labor force market analysis on the information on NIS countries was used. The specific of the method lie in underestimation of shadow economy parameters, because it assumes that people working full time do not have shadow incomes.



⁹ Manlio, Calzaroni, Experiences of Transition Countries in Estimating the Non-observed Economy, Joint UNECE/ Euristat/ OECD Meeting on National Accounts, Geneva, 30 April-3 May 1996

The results of estimation of shadow economy on the base of *power consumption method* gives other results, however at macroeconomic level it is more accurate. It is supposed that the overall economy (including its shadow component) should decline proportionally with the decline in electric consumption¹⁰.

Share of the unofficial economy in GDP, %

	1989	1990	1991	1992	1993	1994	1995
Moldova	12	18.1	27.1	37.3	34	39.7	35.7
Bulgaria	22.8	25.1	23.9	25	29.9	29.1	36.2
Hungary	27	28	32.9	30.6	28.5	27.7	29
Poland	15.7	19.6	23.5	19.7	18.5	15.2	12.6
Romania	22.3	13.7	15.7	18	16.4	17.4	19.1
Russia	12	14.7	23.5	32.8	36.7	40.3	41.6
Ukraine	12	16.3	25.6	33.6	38	45.7	48.9

Source: EBRD, Transition Report 1997

*Turning assets analysis method*¹¹ is a local method based on financial analysis of enterprises.

Utilization of *structural method* is based on finding the discrepancy of production data, domestic consumption, export-import, and changes in stocks.

*Monetary methods*¹² - transaction method, and currency-ratio method are based on the assumption that all shadow transactions are in cash. The unexplained by the official economy demand of money is attributed to shadow transactions. Utilization of monetary methods would produce far graver results, because it will include the demand for obviously illegal transactions, which are not supposed to be included in the official GDP, but are source of incomes and are essential.

Analysis showed that the share of shadow economy compared to that of the formal economy fluctuates in between 55-65%.

¹⁰ Daniel, Kaufman, Alexandr, Kaliberda, Integrating the Unofficial Economy into the Dynamics of Post-Socialist Economies: A Framework of Analysis and Evidence, World Bank, December, 1995;

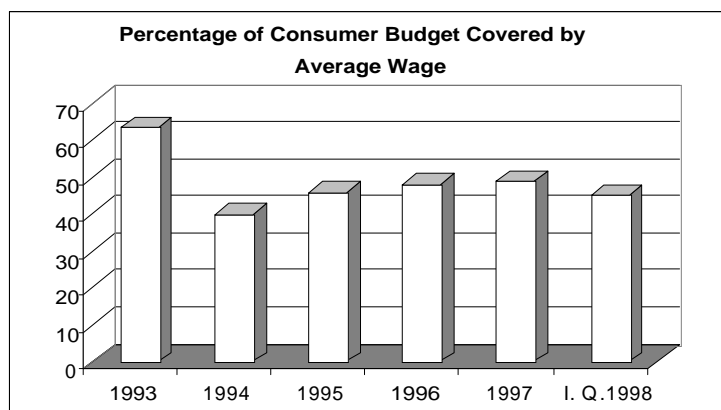
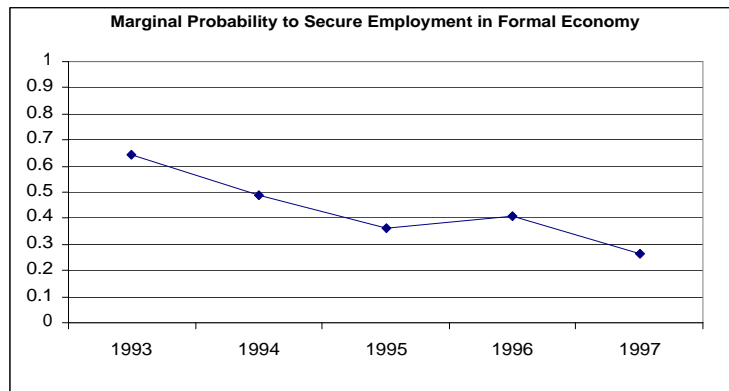
¹¹ Report regarding the analysis of the development of the informal economy in the Republic of Moldova: economic, organizational and juridic measures in order to incorporate it in the official economy, Market Problems Research Center, 1996;

¹² Gutman, P.M., 1977, "The Subteranian Economy", Financial Analysts Journal, pp.26-27;

Edgar L. Feige, 1989, "The Underground Economies: Tax Evasion and Information Distortion", University of Wisconsin, Madison, Cambridge University Press

This rapid growth of the shadow economy sector is caused by two tendencies: the increase in the number of transactions within the shadow economy and the recession in the formal economy (1997 GDP constitutes 36% compared to that of 1990). Some studies of this phenomenon imply the anti – cyclic way of the shadow economic development, i.e. growth of the shadow economy along with the decline of the official economy.

Starting with 1994-1995 the share of the shadow economy began to diminish in a number of countries. This can be explained not as much by some essential regulating measures made by the state, as due to the launch of the stabilization process in those countries resulting in diminished share of the shadow economy in the official one. A case in point is Georgia. During 1991 – 1994, the number of employed diminished from 2.5 to 1.75 million persons (by 30 per cent), growing up to 2.1 million persons in 1997.



For the Republic of Moldova the-1997’s economic re-launch (GDP growth by 1.3 per cent) was too small, therefore the rate of the shadow economy in comparison to the official one was continuing to grow. The discrepancy between unemployment and vacancies grows up and, as result, the marginal probability to find a job in the formal sector of the economy diminishes.

The situation of the employed in the formal sector is discouraging too. The registered revenues of less than 3 per cent of population (5 per cent of urban population and 1.9 per cent of the rural one) cover the consumer basket. The share of the average wage in the consumer basket (36 per cent) remains still too small for a long run to allow the population to survive, staying only in the formal sector of the economy. This “pushes” a growing share of population to the shadow sector.

The existence of a large shadow sector within the national economy creates a number of *problems* both to the state as to the population:

- Spread of tax evasions causing instability in the society;
- A growing share of operators of the shadow economy takes a considerable part of state expenditures (compensations for power resources, free education system and

medical assistance, social services etc.). These expenses are an additional burden on the economic agents of the formal economy;

- Decrease of the state budget revenues along with the decline of formal economy, faster than the decrease in state expenditures, which aggravates the budget deficit problem;
- Decrease of population's trust in state institutions and the reform process, resulting in dwindling economic and fiscal discipline, which, in turn, encourages illegal economic activities;
- Prices for goods and services provided by the shadow economy which do not include proper taxes imposed within the formal economy lead to an unhealthy competition environment the formal sector of the economy, forcing it to choose between going bankrupt or moving towards the shadow economy sector;
- Spread of corruption and economic crime;
- Increasingly deepening income disparities in society;
- Distortions in reporting of such macroeconomic indices as GDP, unemployment rate, population incomes and expenditures, quality of life, etc. Such distorted information generates suspicions among prospective foreign investors;
- Quantitative and qualitative deformations of all macroeconomic patterns producing the impression of Moldova as a country apparently not subject to general rules of economic development. Distortion of the results of state policy regarding formal economy.

4. Tax evasion

Tax evasion is a kind of the underground activity, which actually has a more notable impact on the stability. The society is tensioned, in a big part, by the failure in the payment of pensions and wages for the budget workers, growth of the state budget deficit and debt. On the other side, the supply of free of charge public services to the whole population, including those not paying taxes, worsens the situation in the budget.

Estimation of tax evasion. Data from the Main State Tax Service (MSTS) in Moldova for 1994 through 1998 include the number of audits conducted, violations detected, supplemental payments, average evasion, fines, and other information. Information for both individuals and legal entities was included. Taxes covered in the MSTS analysis included all the taxes subject to control by the MSTS (VAT, income taxes, excise taxes). Using this data, we are able to estimate the total tax evasion. Of course, there are caveats that must be mentioned concerning such data. First, it could be that the tax inspection is not random, but is directed to those taxpayers that are expected to under-pay taxes. If that is the case, the approach we

take in estimating total tax evasion could be overestimated. On the other hand, in the long run the MSTs must subject every taxpayer to an audit, and if that is the case, then the estimation method we use should be reasonably accurate. A second factor to consider in a transition economy is the fact that tax auditors are typically not paid for many months at a time. In such a situation, it is natural to expect tax auditors to use their position in order to extract bribes from taxpayers they subject to audit (see chapter 5). The auditors may thus conceal tax evasion for a price. Given this reality, it may well be the case that actual level of tax evasion is larger than stated and our extrapolation of total tax evasion could be understate the true amount. Despite these valid concerns, we believe that the method we use, based on MSTs audit records is insightful at the least and indicative of general evasion trends, if not specific amounts, at the best.

Tables 1 and 2 provide a summary of tax evasion data for Moldova in 1997 and 1998. Evasion and fine amounts in both tables are measured in thousands of Moldovan lei. Table 1 illustrates that in 1997 a total of 219,180 economic entities (including both individuals and legal entities subject to tax) existed. Of those entities, audits were conducted of 17,541 entities, resulting in an average audit probability of 0.08. The audit probability was 0.07 for legal entities and 0.13 for individuals, resulting in the weighted average audit probability of 0.08. Audit probabilities varied widely across economic sectors, ranging from a high of 0.86 for kolkhozes (former collective farms) to a low of 0.02 for individual farmers. Violations were detected in 9,233 cases, resulting in a conditional probability of evasion detection, given audit selection, of 0.53. Legal entities were found to have an average evasion of 10,590 lei while individuals had an average of 771 lei. At the average exchange rate of 4.61 lei per dollar in 1997, that means the average tax evasion for legal entities was \$2,297 while that for individuals was \$167.1. The average amount of tax evasion discovered for both groups combined was 7,220 lei, or about \$1,566. Table 2 illustrates that in the following year, 1998, a total of 314,818 economic entities existed. Of that number, 15,345 entities were subjected to audit by the STS, resulting in an average audit probability of 0.05. Violations were detected in 9,003 cases, yielding a conditional probability of detection, given audit, of 0.59. The average amount of evasion for legal entities was 22,700 lei (about \$4,203 at the average 1998 exchange rate), which was about double the amount of the prior year. The average amount of evasion detected among individuals fell to 400 lei (about \$74). The combined average was 12,090 lei (about \$2,239).

The column headed Additional Payments in these tables measures the sum of detected evasion plus fines. Average Evasion is computed as the ratio of detected evasion divided by the number of entities subjected to audit. Total Evasion is computed for each sector of the economy as detected evasion times the number of entities in the sector divided by the number of entities subjected to audit. Total evasion for the whole economy was then computed as the sum of all sectors' estimated evasion.

Notice that the number of audits conducted by the MSTs fell from 1997 to 1998 while the number of economic entities rose sharply. The combination of both factors accounts for the reduction in the audit rate, although the increased number of entities has more influence on the ratio than the reduction in audits. During the transition new firms are being formed while existing firms may be effectively bankrupt but still exist on the books. Consequently, the effective reduction in the audit rate may not be as great as the apparent reduction. Nevertheless, the audit rate was sharply reduced, affecting economic agents' perception of the odds of being audited.

It is also worthwhile to note that the relative shares of legal persons and physical persons in the data set changed dramatically from 1997 to 1998. The total number of entities rose from 219,180 in 1997 to 314,418 in 1998. This increase in the total number of entities includes a reduction in the number of legal entities from 173,801 to 44,282 and a corresponding increase in the number of physical entities from 45,379 to 270,535. The largest single cause of this increase is due to the reclassification of farmers from legal entities to physical entities. This change was due to the new income tax code implemented in 1998 that treats farmers as individuals, providing them with personal exemptions that are not available to legal persons. Tables 1 and 2 indicate that the MSTs find little tax evasion among individuals in any case. Individual tax evasion amounted to 6.5 percent of total tax evasion in 1997 and 2.8 percent in 1998. Whether these data on individuals are accurate, or simply reflect the audit strategy of the MSTs, is another matter.

Our calculations show that during 1994-1998 the volume of tax evasion grew up very quickly – from 4% of the consolidated budget income to 32%. We should mention that this is a minimal estimation, because it was based on the assumption of a perfect honesty of tax inspectors.

The reasons for the extension of tax evasions include the weakness and corruption of fiscal control institutions, an overdriven system of tax facilities, a heavy tax burden.

The indicator of tax burden being calculated as the ratio of tax incomes (including payments into the social fund) to GDP varies during 1994 –1998 between 30 – 33%. This indicator, in principle, does not exceed too much the average per OECD - 28.5%. This figure has emerged as a result, that a part of economic agents do not pay any tax and the other – carries a much bigger burden.

Tax burden (excluding excise)

	1996	1997
VAT (mil. lei)	613.9	800
Profit tax (mil. lei)	358.6	380
Individual income tax (mil. lei)	219.1	230
Payrole tax (mil.lei)	765	920
Sum (mil.lei)	1956.6	2330
GDP (mil.lei)	7317	8280
Share of taxes in GDP(%)	26.74047	28.1401

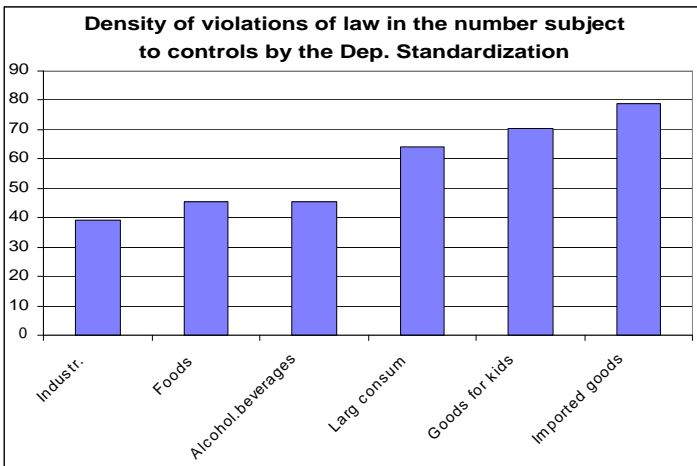
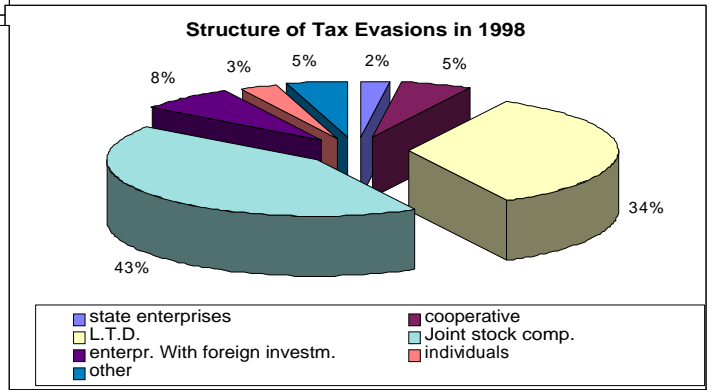
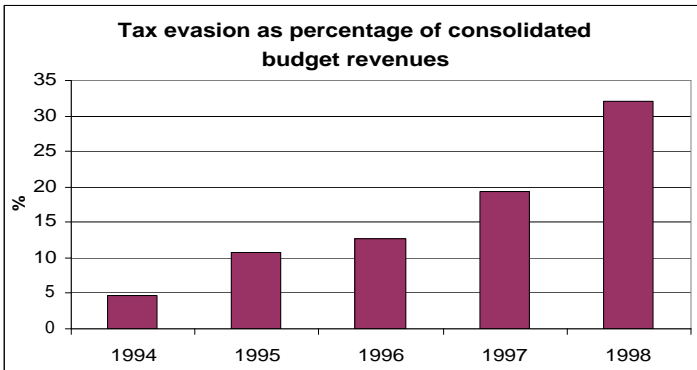
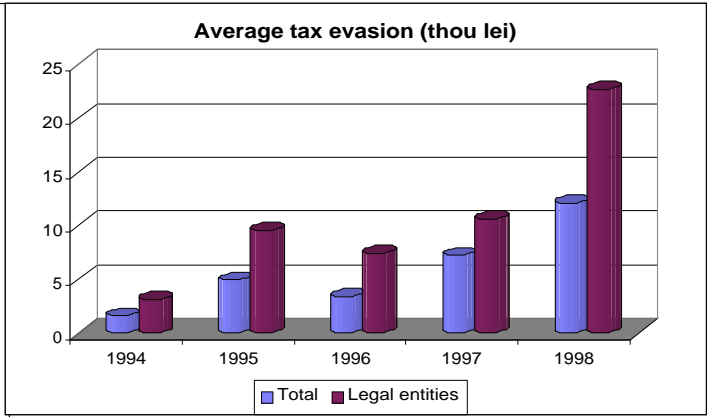
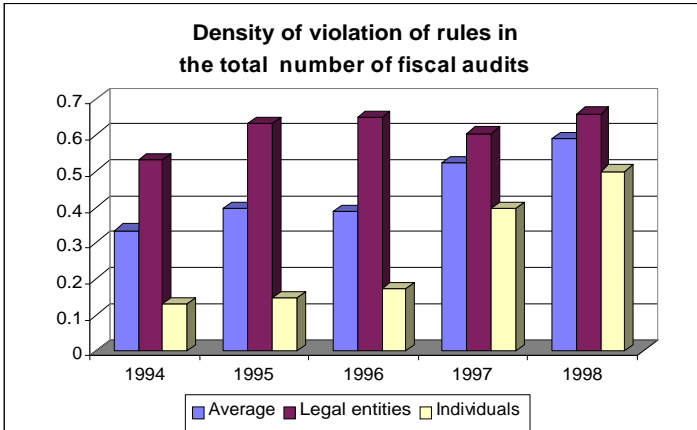
An evaluation of the real tax burden in the real sector of economy for 1992-1997 was done on the base of information derived from the form N2 "Financial results' statement" of all enterprises which submitted this form to the Department for the Statistics.

The results of our estimation shown that tax burden is, evidently, much heavier in the Republic of Moldova (the total in 1997 – 45%, in industry – 50%, in agriculture – 40%, constructions – 38%) and it suppresses the economic development. This burden "pushes out" a bigger part of economic agents to the shadow sector of the economy, reduces the tax base in the future, aggravates the problem of budget deficit, and causes rise of corruption.

Our calculations show, that in average, the rise of the real tax burden by one per cent entails a rise of the "tax evasion/consolidated budget income" ratio by 2.5 per cent. However, diminishing of the tax burden will not be followed sine qua non by the growth of tax collections.

Table 1: Tax Evasion in Moldova - 1997

	Total	Subjected to audits	Density of audits	Violations detected	Density of violations	Additional payments	Detected evasions	Average evasion	Net ben. from evasion	Efficacy of evasion	Fines	Total Evasion
Total legal entities and individuals	219180	17541	0.08	9233	0.53	290300.9	126631.3	7.22	103398.49	445.05	163669.6	537408
Legal entities -total	173801	11524	0.07	6085	0.53	280576.1	121990.6	10.59	103386.80	555.73	158585.5	502394
including:												
state enterprises	1407	773	0.55	559	0.72	32855.8	15685.1	20.29	-2365.74	-13.11	17170.7	28550
joint enterprises	38	10	0.26	9	0.90	466.5	248.8	24.88	126.04	102.67	217.7	945
renting enterprises	64	16	0.25	10	0.63	123.9	77.2	4.83	46.23	149.23	46.7	309
cooperatives of all kinds	3109	1012	0.33	839	0.83	45645.8	23641.7	23.36	8783.69	59.12	22004.1	72630
including kolkhozes	367	317	0.86	274	0.86	29226.6	15277.3	48.19	-9967.47	-39.48	13949.3	17687
LTDs	21869	3618	0.17	2323	0.64	66720.6	30721.3	8.49	19683.07	178.32	35999.3	185695
stock companies	4888	1815	0.37	1408	0.78	84221	33329.1	18.36	2056.37	6.58	50891.9	89759
enterprises with foreign invest.	1298	183	0.14	140	0.77	9794.5	5831.7	31.87	4450.81	322.31	3962.8	41364
social organizations	3387	313	0.09	146	0.47	2769.3	1719.9	5.49	1463.98	572.05	1049.4	18611
banks	29	11	0.38	9	0.82	5992.3	2647.9	240.72	374.96	16.50	3344.4	6981
insurance companies	103	13	0.13	6	0.46	161.4	62.8	4.83	42.43	208.28	98.6	498
associations, concerns	473	111	0.23	80	0.72	23076.8	3785.2	34.10	-1630.29	-30.10	19291.6	16130
other unions												
farmers	133606	2577	0.02	41	0.02	194.7	61.4	0.02	57.64	1534.99	133.3	3183
budget institutions	2316	827	0.36	386	0.47	1203.2	302.8	0.37	-126.84	-29.52	900.4	848
other legal entities	1214	245	0.20	129	0.53	7350.3	3875.7	15.82	2392.32	161.27	3474.6	19204
Individuals - total	45379	6017	0.13	3148	0.52	9724.8	4640.7	0.77	3351.25	259.90	5084.1	35014
individual enterprises	45194	5995	0.13	3128	0.52	9681.7	4620.6	0.77	3336.32	259.78	5061.1	34833
collective societies	148	15	0.10	14	0.93	32.1	17.4	1.16	14.15	434.83	14.7	172
societies with unlimited resp.	37	7	0.19	6	0.86	11	1.7	0.24	-0.38	-18.31	9.3	9



Average tax evasion per taxpayer

	1994	1995	1996	1997
Total legal entities and individuals	1.58	4.92	3.41	7.68
Recorded individuals	3.09	9.50	7.37	12.01
state enterprises	11.53	48.98	11.30	22.00
collective enterprises	6.07	7.68	53.07	33.38
rented enterprises	5.57	9.12	0.94	5.23
all kinds of cooperatives	3.08	9.06	14.74	19.13
including colchozes	7.18	23.90	43.18	54.10
L.T.D.	0.41	1.00	3.25	9.60
joint stock companies	7.82	10.39	18.09	12.39
enterprises with foreign investments	1.82	1.40	18.07	62.08
social organizations	0.78	0.16	0.85	1.78
insurance companies	0.08	2.41	47.62	7.13
associations, concerns	1.97	1.78	19.19	1.85
farmers	0.00	0.01	0.06	0.02
budget institutions	0.05	0.08	0.43	0.44
other legal entities	0.18	-0.85	5.93	17.00
Individuals - total	0.02	0.06	0.18	0.91
individual enterprises	0.02	0.06	0.21	1.19
collectiv societies	0.12	0.02	1.64	2.00
socien.with unlim.responsib.	-0.10	0.00	1.63	0.35
other	0.03	0.08	0.00	0.10

Evolution of tax burden in real sector of economy

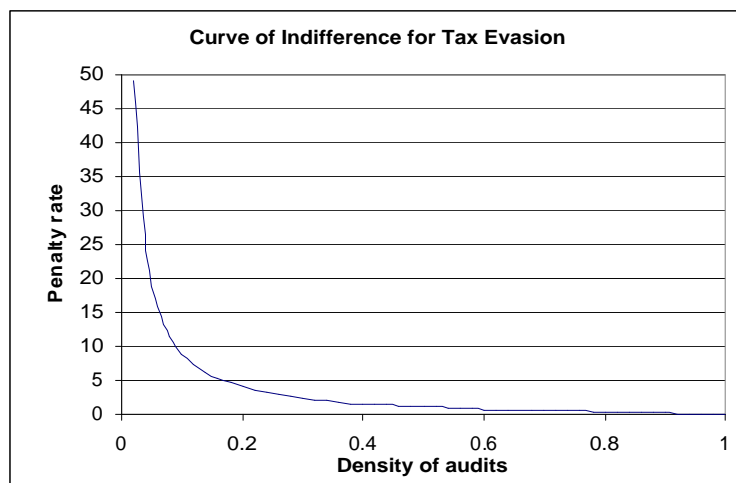
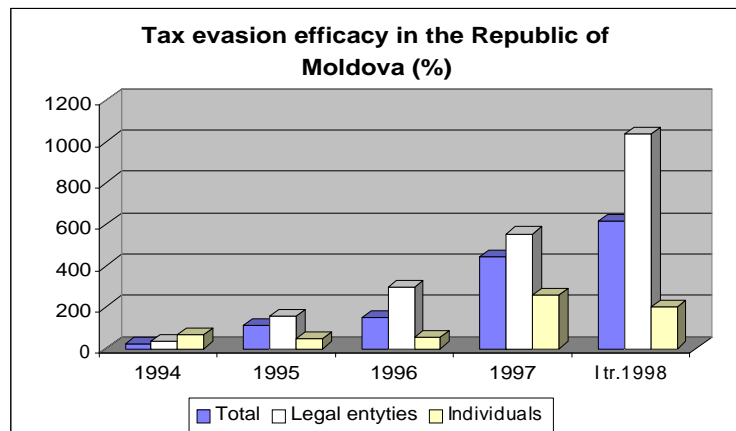
		Total taxes (million lei)	GDP (million lei)	Tax burden (%)
1992 (including cooperatives)	Total	60.8	176.1	34.5
	Industry	28.3	60.6	46.7
	Agriculture	13.7	59.6	23.0
	Constructions	2.8	9.5	29.5
	Trade	1.9	5.8	32.8
	Communications	0.6	1.6	37.5
1993 (including cooperatives)	Total	456.3	1183.6	38.6
	Industry	183.8	452.9	40.6
	Agriculture	99.7	494.0	20.2
	Constructions	23.2	69.6	33.3
	Trade	19.9	53.7	37.1
	Communications	3.7	11.0	33.6
1994 (including cooperatives)	Total	1484.6	3520.9	42.2
	Industry	751.8	1365.8	55.0
	Agriculture	229.0	980.8	23.3
	Constructions	84.5	193.5	43.7
	Trade	80.0	155.8	51.3
	Communications	22.9	56.1	40.8
1995 (excluding cooperatives)	Total	1782.0	3976.6	44.8
	Industry	638.1	1221.4	52.2
	Agriculture	389.1	1233.9	31.5
	Constructions	97.7	221.0	44.2
	Trade	172.9	353.1	49.0
	Communications	107.5	174.7	61.5
1996 (excluding cooperatives)	Total	1924.5	3751.8	51.3
	Industry	742.2	1186.9	62.5
	Agriculture	412.7	725.6	56.9
	Constructions	96.0	288.1	33.3
	Trade	280.6	566.1	49.6
	Communications	108.8	292.4	37.2
1997	Total	2227.3	4957.2	44.9
	Nonresidents	223.7	329.3	67.9
	Industry	683.3	1369.4	49.9
	Nonresidents	43.9	79.6	55.2
	Energetics	262.7	-235.1	z
	Agriculture	468.3	1188.3	39.4
	Nonresidents	0.9	3.8	23.7
	Constructions	106.3	276.8	38.4
	Nonresidents	1.2	5.8	20.7

Probably, one of the causes of tax evasion's phenomenon spread is lack of interest of the local authorities in fighting it. The ratio "budget expenditures / payments into the budget" varies substantially from one locality to another other (from 0.43 in Chisinau till 2.72 in Cantemir county). On one hand, the possibility to cover the local needs with finances from the state budget does not stimulate local administration to maximize tax collection. On the other hand, the realization by the local authorities of the fact that a big share of tax collection on the territory will be spent in other regions creates indifference to tax collection and facilitates other kind of informal agreements between local authorities and taxpayers.

Another cause of tax evasion spread is the weak activity of fiscal institutions. Thus, the share of economic agents subjected to fiscal audits diminished from 32.3 per cent in 1994 to 8 per cent in 1997, and 1.9 per cent in the first quarter of 1998, which facilitates evasions.

In this study a basic *model of tax evasion* was examined. The following assumptions lie at the base of the model: the taxpayer is an amoral person and evades paying taxes when this is economically advantageous; the tax inspector is an absolutely honest person who objectively records all the violations of the fiscal legislation in his reports; the inflation rate is zero. The condition when tax evasion is considered to be economically advantageous means that the gain from tax evasion exceeds the expected losses in the case of detection by the fiscal auditors. In this case the gain from tax evasion is the tax evasion sum itself. The expected losses from tax evasion are the sum of tax evasion which will need to be reimbursed and penalty (fine) in the case of being caught corrected to the probability of being caught in tax evasion. The total net benefit from tax evasion was calculated being equal to the difference between the gains and expected losses.

Our calculation show that for the majority of the taxpayers' categories the benefit from tax evasion is positive, which means that there exist favorable conditions for tax evasion and the phenomenon will grow. In 1997, only state enterprises, budget institutions and kolkhozes were exceptions. The net benefit for legal entities amounted lei 103.5 million in 1997 and lei 118.7 million in 1998.



For the numerical evaluation of the degree of tax evasion advantage a notion of “tax evasion efficiency” was defined as a ratio of the net benefit to

expected losses. The calculation showed that this indicator grew up extremely fast during the last years and reached in 1998 a level of 1000 per cent for legal entities.

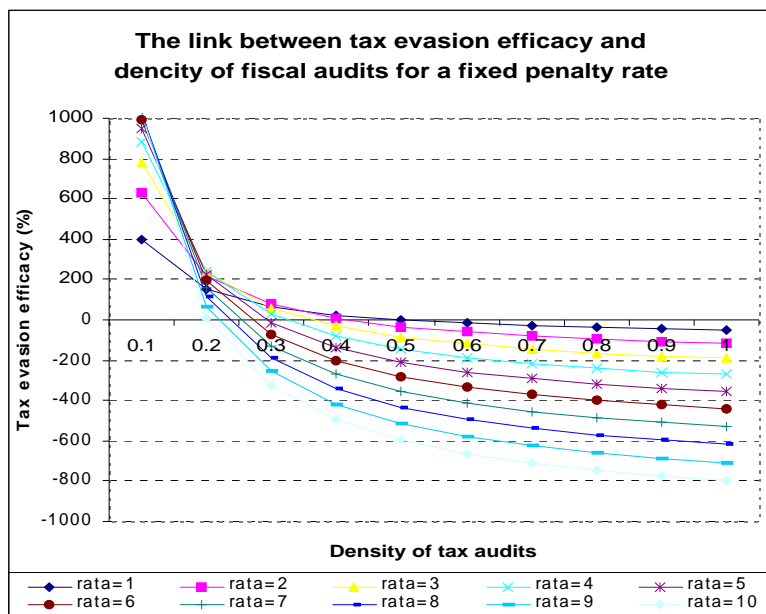
To *fight tax evasion*, it is necessary to create the conditions that would reduce the economic efficacy of tax evasion to zero and would make the taxpayers indifferent to tax evasions. These conditions could be created by manipulating with the penalty rate and the probability of being caught in tax evasions (density of

controls). The calculations allowed to obtain the *curve of indifference to tax evasions, or trade-off curve*. It presents the multitude of combinations between the penalty rate and the density of fiscal controls, which discourages the tax evasion, for which the efficacy of tax evasion is equal to zero.

We can see that the sensibility of these indicators is very strong. The surface under the indifference curve presents the multitude of combinations of penalty rates and densities of controls for which the tax evasion is efficient (the efficacy is positive). For the reduction of the phenomenon of tax evasion, the choice of the kind of control regime is important. The calculation showed that the efficacy of tax evasion does not depend on their volume. In space the dependence between penalty rate, density of controls and the efficacy of tax evasions forms a hyperboloid. The multitude of combinations under the zero level describes control regimes of fiscal inspections which discourages the tax evasion.

The analysis of the real information regarding the penalty rates and densities of fiscal audits

corresponded to the sector where the evasions are efficient. Thus, for the density of audits created in 1997 amounting 8 per cent the penalty rate needed to be not 100 – 130 per cent, as it really was, but 1,150 per cent. And conversely, if the penalty varied in limits of 100-130%, then the density of fiscal controls had to be 43-50



per cent of all taxpayers. Besides, given the fact that collection of penalties is going very hard, it is necessary to make other measures to fight tax evasion.

First suggestion in this direction is the need to develop an ample study of the phenomenon. This study should include *economic, sociological, juridical and psychological aspects*. The problem is that the social - economic conditions created in the ex -socialist zone facilitate the avoiding of paying taxes. There exist economic models in the world practice which prove the fact that as long as the person realize that the tax evasion is widespread and he lives in an dishonest ambience, he concludes that his tax evasion will not change a lot the general situation, but it will change essentially his own benefits. As a result, he will decide to hide a part of his incomes.

There are studies that prove the fact that the bigger is the income, the more he will be subject to tax evasion. The population having big incomes, who should, in principle, contribute the most of the budget revenue, will evade paying taxes in bigger proportions. *In countries with a dishonest ambiance, the progressive tax system does not work efficiently. Formation of a state with a big share of medium size income population is the base of tax collection stability.*

Another aspect of tax evasion. *Studies of the psychological aspect of the tax evasion show* that independent of the real dimension of incomes, persons who complain about small incomes, about unfairness in evaluation of their work and aptitudes are more disposed to evade paying taxes, taking advantages from the state services to all population. That is why insufficient informing of the population regarding real incomes in society predispose to supplementary evasions. Informing of the population regarding the buying capacity of the average wage, including various kinds of services and education in various countries could be beneficial.

As a solution for the creation of a more favorable ambiance and amelioration of financial discipline, sociologists and psychologists propose the creation of various *educational programs of tax honesty*. According to the authors of these programs, education and moral appeal could have, probably, a better effect than high penalties.

Rise of the state authority in the public opinion can serve as a cheaper way of fighting tax evasion. Such educational programs could work more efficiently if being promoted by non – Government organization, and financed by the state.

They need to maximize the utilization of mass media and include the explanation of the following aspects:

- the tax system, in principle, is not bad and differs little from similar systems in the developed countries;
- the majority of taxpayers nevertheless pay their taxes;
- a convincing description of main directions of expenditures and explanation of their importance;
- description of possible consequences of tax evasion, including the personal risk and institutional consequences of an excessive punishment from the state;
- promoting a negative attitude to tax evasion, explanation of the fact that any tax evasion results simply in the tax burden's growth, and harms the rest of population.

Regretfully, especially in the countries having lower fiscal discipline, this educational work is not practiced at all.

Another aspect of tax evasion is that *the maturity of tax evasion reimbursement* is too long. Basically, the tax debts form a dead burden, which pushes more and more to the shadow economy not only the small businessmen, but also big enterprises, which resort to different manipulations with foreign accounts “run away” from this burden. Some studies of this phenomenon show that for easing this

burden of taxes, which will never be paid anyway, a tax amnesty could be declared. *Negative and positive aspects of tax amnesty* could be distinguished.

The positive effects of the declaration of a tax amnesty include the following:

- *amnesty could offer a possibility to collect a part of tax debts, which in other case could not be collected;*
- the amnesty encourages honest declaration of incomes;
- amnesty makes the society more able to control its future, because the possibility of getting out from the shadow economy and entering the official one appears;
- amnesty makes possible to declare that a mistake was made, but now conditions for changing the behavior are created;
- amnesty can serve as transition to a new, softer tax regime, because when the Government fails systematically in promoting its tax policy, this could signify about a too heavy tax burden;

The negative effects are summarized in the fact that if this kind of amnesty is repeating, the population gets used to the fact that in any case they will be forgiven for breaking the law, this could undermine the authority of the Government and diminish the financial even more.

With regard to the Republic of Moldova, the utilization of different forms of tax amnesties becomes a too often used practice. In general, the population expects regular debt forgiveness, that is why it is necessary to examine carefully the possibility to continue this practice, or to declare clear that this amnesty is the last one and later the control work will be done with greater severity.

Fighting tax evasion needs to be done by all ways: economic, legal, administrative and educational.

The economic measures could include:

- increased fines and frequent inspections by fiscal institutions to such an extent that to make tax evasion unprofitable;
- wider and more active use of bankruptcy legislation;
- freezing enterprises' debts, deblocking of bank accounts and finding ways of cutting debts by taking into account the non-objective ways of their formation;
- diminishing the tax burden (the last one to be done only after accomplishing the others).

Legal measures would include:

- development of a legal system to promote economic measures;
- simplification of enterprise "shut-down" procedures for those that cannot prove their being in operation over an established period of time;
- implementation of the management law and means of its enforcing, providing management administrative and penal responsibility for not paying taxes and other payments due to the state;

Administrative measures would include:

- creation of a body endowed with functions and powers sufficient enough to fight tax evasion, including the right for investigation and application of administrative sanctions, to promote a single policy with regard to the investigation, discovering and penalizing people breaching the financial discipline;
- strict delimitation of functions of control institutions;
- building the prestige, quality and incentives of fiscal control institutions;
- ensuring transparency and free access of large parts of the population to the decisions made by state authorities, which might be an efficient measure of fighting corruption.

Educational measures:

- development of an awareness raising program explaining the implications of tax evasion on people's welfare, educating a negative attitude towards this phenomenon. This program is likely to be more efficient if conducted by non-governmental organizations and financed by the state;
- psychological education of economic agents with regard to the increase of severity on the part of fiscal control institutions via all available information channels (mass-media), explaining the positive effects of such measures, including eventual lightening of the tax burden.

Implementation of these measures could serve as first steps in fighting the parasitical phenomenon of tax evasion and could permit solving the problem of budget deficit, external debts, transition of the economy to a more civilized, stable, attractive for the international organizations and investors stage. But nevertheless a strong need of fighting corruption amongst audit bodies is needed.

5. Corruption in audit bodies

Some of next chapters are written mostly on the base of the report of the Accounting Court. However the Accounting Court does not make a strict distinction between corruption acts and other economic crimes, certain cases could take place only under the protection of top public servants.

The Department of Financial Audit and Control was founded counter to current legislation. The founding of the Department of Financial Audit and Control in the jurisdiction of the Ministry of Finance promoted concentration and monopolization of auditing and control of public finance with the said ministry. Thus the Government, other ministries and departments were deprived of the ability to exercise control and possess prompt and impartial information on the quality of administration and management of financial resources by the enterprises and agencies of the national economy.

According to the opinion of Accounting Court experts, the essence of the internal public audit was considerably distorted, while the role of the Government

financial control in improving management and administration of public finance released to agencies and institutions had been reduced.

A clear-cut regulatory framework for complete and correct regulation of the auditing function of the Department and its divisions, of the procedure for considering and implementing the results of audits, of the measures preventing and rectifying violations, of compensating damage is yet to be created. There are no regulations on the auditing procedure, procedure for drawing up statements and records of the seizure of goods and suspension of documents, procedure of accounting for seized goods which goes counter article 8 of the provisional regulation.

In the period review the finance guard - a specialized unit of the Department - fulfilled its function in an unsatisfactory manner.

There were cases when decisions of local finance guard offices on applying sanctions to infringers had been arbitrarily cancelled or suspended by the Department of Audits and Control. In 1996 4 decisions of the director of the Finance guard office of Chisinau were cancelled and suspended, the assets were released from arrest, the budget cost of non-application of sanctions was MDL 2 million.

It was discovered that, while some orders of local finance guard office on applying sanctions had been cancelled by the executive of the Department, in 1996 financial sanctions were not fully applied to the "Caragasani-Vin" joint-stock company. The cost for the state budget was MDL 500000.

As a result, in the period of review the efficiency of enforcement of sanctions was very low.

In 1996 all staff of the finance guard made 8 460 audits; 6 270 (or 21%) cases violations were identified and decisions on applying penalties worth MDL 16,144,600 were taken; but only MDL 5,157,800 (or 32 %) of the penalties were paid.

The staff of the central finance guard office applied sanctions worth MDL 5,425,500, of which only MDL 1,098,800 (or 20 %) were collected.

As of 01.01.1996 MDL 239,400 worth of goods under arrest were not recorded in the accounts, which was counter to article 15 of the Accounting law. Accounts of goods worth MDL 1,747,900 seized in 1996 were kept with serious mistakes and violations.

The stocktaking at the finance guard warehouse showed that 29 lots of the 106 lots of seized goods were stored without the necessary documents, while in 26 cases prices of goods were not indicated. The total value of those goods was not established, and neither the accounting office of the department, nor the directors of audits kept accounts of these goods.

In the period of review the finance guard did not keep records of cases sent to courts and to investigation offices appropriately. Hence many infringers did not pay fines.

In the period of review the Main Division of audits did not accomplish its functions.

In 1996 this division identified budget loss (misuse of funds, excessive stocks) of MDL 34,187,500, however only MDL 1,178,500 (or 3.4 %) of damages were compensated.

The mentioned division had also made additional assessment of levies on hidden income, etc., and applied sanctions worth MDL 20,571,600 whereas only MDL 6,174,900 (or 30%) were actually paid.

In the period of review the Chamber of Accounts had identified cases of negligent audits by the Department. Thus, in Chisinau alone three cases of negligent audits were identified, i.e. 2 audits of the state circus and 1 audit of "Fondul Mitropoliei". Quality of audits was impaired due to hiring incompetent staff.

The directors of the Department misused the resources worth MDL 11,400 of the centralized special fund, thus violating the 1996 State budget law and other regulations.

In 1996 the Department spent MDL 138,000, remitted out of the proceeds of sanctions and penalties and earmarked only for improvement of logistics of the Department, on bonuses and wages of its employees, thus violating the 1996 state budget law and Government Decision No 641 of 25.11.1996.

Main State tax Inspectorate

In the period of review the Main State Tax Inspectorate did not ensure sufficient accomplishment of its functions of controlling assessment of taxes, complete and timely transfer of taxes and other levies, efficient organization of the activity of local tax inspectorates, explanation of legislation on taxes and levies. In 1996 the rate of tax collection was only 77.5 per cent. Arrears of economic agents amounted to MDL 665,800, of which MDL 461,700 due to the activity in 1996, and MDL 204,100 due to the activity in 1993 to 1995. Due to unsatisfactory work of local tax inspectorates, the rate of tax collection in some districts (Camenca, Donduseni, Dubasari, Cainari) was 17 to 30 per cent.

In the period of review only 19 per cent of sanctions identified for collection in the result of audits were actually collected, because of inadequate measures by the executives of the State Tax Inspectorate. This resulted in a sharp decrease of the efficiency of the state tax service, neglect of the tax legislation by taxpayers, disorganization of the work of operations staff of the state tax service.

Due to the lack of cooperation of the STS with the State Registration Chamber, Ministries of finance and justice the recording of taxpayers was not well established.

Some taxpayers upon registration with the Registration Chamber and receiving permission for doing business, did not get registered with the state tax service and did not pay taxes. During audits in 1995 and 1996 tax inspectorates identified 421 economic agents who were not registered as taxpayers, though they had objects of taxation, and did not fulfill their liability to the budget. The current Enterprise law allows to some persons to set up several entities separately registered. These entities

have the same founders and managers, perform financial and economic manipulation between each other, thus violating the tax legislation.

Due to the lack of cooperation of the State Tax Service with the State registration chamber and the Customs department, in some cases economic agents may continue their business after their official liquidation. Thus, the “Moldagrosnab” joint-stock company (from Comrat) was officially liquidated on 27.09.1995 in the documents of the registration chamber, however, it continued business till December 1995, exported MDL 2.4 million worth of goods, neither repatriating the hard currency, nor paying MDL 1.8 million of penalties. The company’s bank account was closed only on 09.01.1996. For a similar reason and also due to the irresponsibility of tax officials of the Botanica district of Chisinau (Istrati, Anoskin, Socolov, Revenco) the “Sudexpo” company (Calev) evaded paying excise tax on the imported fuel, while the payment date was deferred by the Customs department. Taking the advantage of the lack of coordination between the tax service and the Customs department, the directors of the said company converted their free funds into US dollars, transferred them to a transit bank in New-York, simultaneously liquidated the company, neither paid MDL 0.8 million of taxes, nor repatriated MDL 0.7 of hard currency income from the sale of exported commodities. The involving of the Ministry of internal affairs and the office of the Prosecutor general failed to produce the results of restituting the payments and making the infractors answerable by law. On the grounds of forged documents, drawn on behalf of non-existing officials of Chisinau municipality on the official letterhead of the State tax inspectorate with the official seal of the state tax services, the state registration chamber de-registered the “HB” joint-stock company, which had not paid MDL 1.1 million of taxes.

The Tax Inspectorate of Calarasi issued certificates of no arrears of social taxes to the Social fund to 25 economic agents, which were to be liquidated, having audited only 3 of them. The State Registration Chamber registered liquidation of 3 economic agents without such certificates from the tax service. During liquidation of 2 economic agents statements of audit were not available in Briceni tax inspectorate.

While auditing the collection of levies the State Tax Service did not examine the problems thoroughly, did not make analysis, general conclusions and recommendations to the Government and Parliament as to how problems could be rectified. Thus, the State tax service, the Ministries of finance, economy and foreign affairs did not submit the necessary recommendations to the Government and Parliament of the Republic of Moldova for making amendments in the current legislation. As a result, the state budget suffered losses of MDL 338 million due of non-taxing of goods imported from Ukraine, in addition to the negative balance of trade with this country.

In many cases tax officers, because of poor training, do not reflect either the assessment of the taxes and duties, which integrally form the tax system, or the computation of how the amount was determined, in their statements. The cross audits of the “Neptun Nord” and “Nistru Lada” joint-stock companies showed, that because of improper accounting for handling costs, the companies understated their taxable

income by MDL 269 thousand and MDL 153 thousand, respectively, whereas the tax service of Chisinau failed to discover these facts in its previous audits.

In some cases the training of officers of the State Tax Inspectorate does not meet the qualification requirements of state tax service, because of insufficiencies in the work of staff selection and staff promotion. People various qualifications, i.e. technicians, managers, experts on merchandize, linguists, mathematicians, nurses, etc. are employed as state tax inspectors. Hence, the quality of audits is poor, due to such selection of staff. Inspections reveal numerous evidence of shortcomings and breaches in the performance of functions and duties established by the State Tax Service law, implementation of regulations on the fundamentals of tax legislation, tax-payer education, accounting for and control of correct assessment of taxes and their full and timely payment.

By adopting Law No 633-XIII of 10.11.1995 on forced collection of defaulted taxes the Parliament of the Republic of Moldova placed additional tools at the disposal of the State tax service for expediting revenue collection. However, in the period of review local tax offices, with exception of the tax office of Chisinau, did not apply the provisions of the said law in practice.

Partly, the funds, initially intended as budget revenue, but placed at the disposal of economic agents as tax exemptions to provide incentive for social expenditure, are squandered, because of the lack of efficient control by the State Tax Service over their use for the identified purpose specified in the decision on exemption (e.g.: the “Olympic Club” limited liability company, the “Fondul Mitropoliei” joint-stock company), and is illegitimately used by non-state entities).

Inconsistent decisions on enforcement of tax collection and imperfect regulations of the said function produce a negative effect on budget revenues. After the legislature approves the state budget decisions authorizing non-payment and exemption are made without the appropriate balancing of the revenue and expenditure sides of the state budget. Government Decisions No 7 of 09.01.1995, No 306 of 15.05.1995 and Decree No1412 of 11.04.1995, the issue of which was a violation of article 7 of the law on the principles of the tax system, granted tax holidays and other exemptions to a number of industrial enterprises. In 1996 the Council of state creditors signed memoranda with 98 enterprises suspending payment of various taxes worth MDL 532.3 million, or 34 per cent of the public budget for 1996. On the one hand, the enterprises-signatories of the memoranda do not comply with the terms of increasing output, reducing the stock of finished products, reducing barter transactions and thus improving their financial position. On the other hand, the Council of state creditors does not ensure that the measures applied to the non-complying enterprises, i.e. replacement of management, cancellation of tax exemptions, application of the bankruptcy law as per memoranda and current legislation. As a result of such attitude of the Council of state creditors only the Government fulfils the terms of memoranda by granting tax exemptions, whereas the enterprises do not and are not liable for non-complying with the obligations. Financial position of most of these enterprises had rather deteriorated than improved.

None of the 98 enterprises paid current debt to the state creditors (being current on current liabilities is mandatory for obtaining tax holidays and exemptions); as of 01.10.1997 their arrears of current liabilities for 1996 were MDL 232, 5 million, of which liabilities to the budget were MDL 56.7 million.

The Main State Tax Inspectorate and its district offices do not take measures to rectify tax violation in all the cases discovered during the audits by the Chamber of Accounts. The decision of Chamber of Accounts (No 8 Of 16.01.1996) on collection of MDL 93,800 of budget liability from the “Neftegas group” had not been enforced due to illegitimate delays by the officials.

Imperfect organizational structure of local tax inspectorates, especially that of Chisinau, among other things impaired the performance and efficiency of the State tax inspectorate. The function of audit is vested with one department only, as result of this audits are neither timely not efficient, and the staff is used inefficiently.

The activity of the State Tax Inspectorate is affected by numerous memos and requests from government agencies and senior officials, which exert pressure on the tax service to grant illegitimate tax exemptions to legal and natural persons. Despite the fact that in most cases the tax service resists the pressure, on some cases the requests are illegitimately fulfilled. Thus, illegitimate tax exemption of imported cars had been given to 98 individuals; to the “Bucuria” joint-stock company (MDL 8.1 million); “Moldova”, the agro-industrial company (MDL 429,100); the Ministry of defense (MDL 600,000); various budgetary units (MDL 469,500) and others.

In 1996 the inspectors of the State Tax Service drew up 11,992 statements of administrative violations of the tax legislation. 4.771 statements had been forwarded to courts. As of 01.01.1997 2,525 statements (or 51 %) had been considered by courts, while 493 had been rejected. One of the reasons of the rejections of the cases of administrative violations is that the statements of the case are drawn up poorly by the tax inspectorates. At the same time, there are other causes, which reduce the efficiency of maintaining order and supervision of compliance with tax legislation. Most of the statements are draw up by the state tax service in accordance with the current legislation to make infractors answerable by law. But law enforcement agencies do not abide with the established term of processing documentation. Law enforcement agencies of Chisinau considered 10 per cent of documents; those in the district of Telenesti considered 4.7 per cent; and in Calarasi 8.3 per cent were examined. None of the 12 cases in the Telenesti district was considered. The tax inspectorate of Edinet forwarded 3 case to the courts in October 1996, none of them was considered, while the repeated inquiries of the tax office remained unanswered. Despite well-grounded arguments of the Customs department and the Tax service for the cases of tax evasion by the “Sudexpo”, “Mesterul Manole” and :BHB” companies in the documents forwarded to the Ministry of internal affairs, the infractors had not been made answerable by law.

Provision with reference to procedure of formation and use of social development fund resources does not specify the procedure of using the resources earmarked for the development of logistics. Procedure of applying this provision has deprived tax authorities team from managing special fund resources. Regardless of the fact that the above provision foresees participation in the commission for distribution of special resources representatives of territorial tax inspections, during the checked up period did not actually take part in these resources distribution. Within that period the fund of special resources has been used without estimated expenditures at the discretion of the Ministry of Finance and the Main State Tax Authority (V.Chitan, I.Prisacari).

Within the checked up period improper and unmotivated use of special resources fund to cover the needs of the Ministry of Finance, in addition to budgetary resources allocated for the administrative costs of this ministry amounted to 182.3 thousand Lei, including 174.3 thousand Lei for purchasing motor car brand “Opel-Vectra” and 3 motor cars brand VAZ.

Financed at the expense of special fund were certain contracts execution of which has caused discrepancies. In August 1995, based on a contract for purchasing “Xerox-535” copier, transferred in favor of JSC “Chep” was 101.6 thousand Lei. Until presently, although terms of contract execution expired in September 1995, the Main State Tax Authority has not received neither “Xerox” nor money, while the JSC “Chep” has suspended its activity without formal liquidation.

Random check up revealed cases when office supplies were purchased through mediation of certain commercial agents. Printers MT-691 (3 pcs) with the final price of 209.3 thousand Lei were purchased through companies “ITS-Moldova GmbH”, “NAX Ltd.” and private enterprise “RINA” which resulted in an increase of their purchasing cost.

Part of the special fund resources has been used to effect expensive repair work on Main State Tax Inspection management offices, while the premises of some of the tax inspections are in rather deplorable condition. Transferred to tax inspection of sector Centru without carrying out repair works was a sum worth of 150 thousand Lei which later on was groundlessly transferred onto expenditures.

The management of Municipality Chisinau State Tax Authority (by failing to observe tax law, infringing requirement set forth under the Law of State Tax Authorities and ignoring Art.25 of the Law of the Chamber of Accounts, thus failed to fulfil regulation set forth by the Chamber of Accounts, leaving unattended the statement on “Olimpic-Club” Ltd check up and taking no respective decision on the issue.

Thus, the non-delivery to the budget amounted to 1275.6 thousand Lei. These being the extra-budgetary accrued resources earmarked for the Olympic games as foreseen by the Decision of the Parliament of the Republic of Moldova No.552-XIII of 21.07.95, same as tax and customs benefits groundlessly enjoyed by “Rimtex”

company to the amount of 61.7 thousand Lei and by JV “Interforum-M” to the amount of 325.7 thousand Lei.

The inspection has failed to secure the fulfillment of its own decision “On application of financial sanctions for the infringement of tax legislation with reference to “Olimpic-Club” Ltd. Thus, the orders for collection for 6.7 million Lei, submitted to the bank twice for compulsory diversion of the financial sanctions imposed were illegally and unmotivatedly withdrawn from the settlement account of “Olimpic” Ltd at the JSC Bank “Victoriabanc” by effect of two memos signed by G.Trocin and L.Istrati (Deputy Chief). Meanwhile, receipts onto this company’s account amounted to 6438.4 thousand Lei and were immediately transferred onto exchange account to be converted into US Dollars.

The inspection has misled the Chamber of Accounts by wrongly informing on execution of its requirements and by communicating that submitted to the bank were the orders for collection for the total sum of 6768.7 thousand Lei and received prior to March 5, 1997 was 172.3 thousand Lei, which does not correspond to real status of things. As a result of irresponsible attitude of inspection authorities the budget was short of 8260.4 thousand Lei.

6. Law breaking at the top level

State Chancellery

The State Chancellery of the Republic of Moldova which was the vehicle of funding the activities of the Government, the staff of the Government and the staff of the President in the period of review (1995 to 1996) made a number of violations of the current legislation. These violations resulted in a unpractical use and misuse of budget funds, excess of expenditure over the budgeted amounts approved by the Parliament in the annual budget laws.

The Government Reserve Fund was a source of funding excessive expenditure. For 1995 MDL 690,000 were allocated for other expenditures. Additional decisions of the Governments had been made to fund expenditure of MDL 1, 425,600 at the expense of the Reserve Fund. The actual expenses, however, proved to exceed the available resources, hence excessive expenditure in 1995 was MDL 224,700.

Non-budgeted funds of MDL 2.3 million were provided to operate special air flights for the official delegations of the Republic of Moldova (under the ex-Prime Minister A.Sangheli).

In order to reduce actual expenditure on the State Chancellery and the staff, a number of expenditures were funded out of the Government Reserve Fund and by other institutions and organizations. Thus, pursuant to two Government decisions MDL 80,000 were transferred to the city Government of Chisinau in 1995 to purchase two apartments for an employee of the State Chancellery, D.Ceres - ex-

chairman of the executive committee of Taraclia. The same Mr. D.Ceres received assistance in the amount of MDL 3,800 and MDL 5,400 were paid illegitimately for his accommodation at the “Dacia” hotel from 19.08.1996 to 01.01.1997. MDL 18,300 were paid for accommodation of Mr. D.Puntea at the same hotel.

Netting-out operation was made with the Moldova-exim company to fund expenditure worth MDL 201, 100 which was to be funded through the State Chancellery, funding worth MDL 48,900 was made through the “Moldpress” state company.

A number of expenditure was made by the State Chancellery counter to current regulations or due to absence of such regulations.

In 1995 to 1996 MDL 630,000 were spent counter to regulations on official delegations of the Republic of Moldova and business trips of the members of the Government. In 1996, before the presidential elections, the number of business trips without urgent official need grew 10 times on an average monthly level.

Similarly MDL 482,500 were spent on receiving foreign delegations. Budget of expenditure of receiving a foreign delegation is not approved ex-ante but ex-post thus authorizing actual expenditure which is several times higher than the established standard. In some cases the number of Moldovan staff is much (almost 3 times) bigger than the number of members in a foreign delegation.

Expenditure on food and drinks for delegations of the Republic of Moldova was made without regulations and availability of funds. Moreover, logistics is provided by private agencies, hence a considerable increase in costs because higher commercial margins are applied.

More often than not private agencies are involved in servicing foreign delegations. An ex-works price of a bottle of cognac is MDL 144, while at a private agency the price may be as high as MDL 744 to 900.

Cases of charging expenditures to the State Chancellery without proper supporting documentation had been revealed. Thus, pursuant to Government decisions, funding was provided for a dubious transaction of publishing brochures in Bulgaria. The brochures had not been registered with State Chancellery but the spent funds were charged to expenses on the grounds of forged documents prepared and signed by V.Cutarchin, P.Taltu, S Conetchi, the aides of the ex-Prime Minister, and T.Nirean, the head of the local government department.

To avoid transparency of some expenditures of the Government Reserve Fund some of the documents were classified as confidential counter to the State secret law.

Thus, Decision No 523 of 13.12.1996 authorized the release of MDL 135,000 to the Moldovan Embassy in Russia for purchase of a vehicle. Decision No 525-ds of 17.12.1996 authorized the release of MDL 100 thousand and 70 thousand as assistance to I.Ustian and V.Procopciuc, respectively.

During the period of review the State Chancellery did not provide for efficient and rational management of the state property in its jurisdiction, in some cases it

allowed the squandering of assets. Thus, under the pressure from the leadership of the Government of the RM the value public assets held by the Codru Cafe had been understated by means of preparing inappropriate documents and the assets had been included in the statutory fund of the Cotour company, a Moldovan-German joint-venture. Its German founder is the “W.S.Touristic iW Import-Export, which is owned by Mr. S.Wasserstein, the ex honorary consul of the Republic of Moldova in Frankfurt-on-Main. The revaluation of the state assets in the statutory capital of the Cotour joint venture at international prices had not been made while such re-evaluation is required by Foreign Investment law No 998-XII of 01.04.1992 and amendments to this law. The state assets worth of MDL 1,989, 000 were appraised at MDL 200,000, i.e. under-evaluated by MDL 1,789,000, hence the government share was reduced from 91 per cent to 50 per cent, the share of the German partner was increased from 9 to 50 per cent. In spite of the violations, the Ministry of privatization in the person of Mr. A.Cucu in December 1994 had authorized the registration of the joint-venture with government share.

At the time of the audit draft amendments to the Cotour’s by-laws had been prepared, the government shares was to be reduced to 28.1 per cent while the share of the German company was to be increased and to become private property of S.Wasserstein and V.Topa (35.95 per cent each). Thus ended the existence of the Codru Cafe, a state enterprise subordinated to the State Chancellery.

Pursuant to Government decision and with the intermediation of the Codru hotel,

GAZ -31092 from the Government fleet of cars was sold at a discount price of MDL 27,300 to S.Wasserstein for his personal needs, he used the car with government license plates. The lease of two rooms in the Codru hotel for 5 years was authorized to S.Wasserstein. S. Wasserstein violated the provisions of the contract and on 01.06.1997 did not pay either the hotel fee of MDL 701, 000 or the telephone bill.

The premises of the State Chancellery canteen (78, 31st August Street) were privatized illegally with participation of the Chancellery and the city management of Chisinau in favor of the Farmacom company. To perform this transaction a contract with the Ural-Moldova had been cancelled, the said company had made a considerable investment in the renovation of the said premises).

The former management of State Chancellery and the “Basarabia” joint-stock company had made attempts to privatize the canteen of the State Chancellery by means of setting up a public-private joint venture, “Capcom”, which had been founded in November 1996.

An apartment house (with 71 apartments) was constructed by means of the subordinated publishing house, “Universul”, the house was built for a group of natural persons who had formed a housing cooperative society No 239 of Chisinau. The members of the cooperative society had made a contribution of MDL 1,700 to the construction. The publishing house incurred other expenses worth MDL 273, 100;

the expenditure was made out of the proceeds of loans worth MDL 1,213,800 which had been guaranteed by the publishing house and the city hall of Chisinau. The members of the cooperative society had been occupying the said house ever since 1995. However, they had not reimbursed the expenses of MDL 5,544, 400. The expenses are recorded in the balance sheet of the “Universul” as construction in process.

Violations and errors had been detected in the activities of other subordinated enterprises of the state Chancellery.

Thus, in 1995 the transportation enterprise of the State Chancellery had received excessive funds MDL 1.4 million to purchase cars and spare parts. In the same year the said enterprise had made an authorized expenditure of special purpose funds equaling to MDL 708,700 received from supplying services for fees and did not transfer MDL 918,700 that was due to the budget, the same indicators in 1996 were MDL 329,900 and 340,800. Mr. V.Miculets, the director of the transportation enterprise of the State Chancellery, is the head of two more companies, i.e. the “Moldgazavtoservice” joint-stock company and of a Moldovan-German joint-venture, “Autospace”. In these capacities he ensures that the private company get favorable price for its cars and spare parts, while the “Autospace” company be accommodated with production premises at low lease.

The Ministry of Finance

Inspection of the Accounting Chamber of the state budget execution has revealed that revenues in 1997 were ensured at the level of 113% (2119.0 million lei), and expenditures at the level of 110.4% (2726.1 million lei). Excess of expenditures over revenues (budget deficit) amounted for 607,1 million lei, upon permitted limit at the level of 350 million lei.

In the period from January to October budget deficit was funded from credit resources of commercial banks in the amount of 96.4 million lei not envisioned in current legislation. Only 80.8 million lei were reimbursed. Also 1.3 million lei were illegally used for credits servicing.

Tardy payment of taxes, tax holidays, granting of non-envisioned tax privileges have resulted in the growth of arrears to the budget up to 525 million lei by 01.11.97, that is 164 million lei more than at the beginning of the year.

Execution of revenue side of the budget was adversely affected by tax privileges granted after enactment of the Law on the State Budget for 1997, that in conformity with calculations amount for about 1031 million lei, or 38.4% of the consolidated budget revenues envisioned for 1997. At the same time, in conformity with memorandum agreements, arrears of economic agents to the state budget for the total amount of 237,9 million lei were restructured.

On the basis of Decision of the Government N 699 of 25.07.97 that contradicts Article 29 (6) of the Law on the State Budget, the Ministry of Finance gave an instruction to the Custom Control Department to relieve «Taxi-service» company

from VAT custom fees payment upon import of 50 mini buses purchased from Korean company «Hiundai Corporation». These illegally granted privileges resulted in the state budget losses in the amount of 683.9 thousand lei.

In conformity with Decision of the Government N 673 of 18.07.97 that contradicts Article 5 of the Law on the State Budget for 1997, the Ministry of Finance extended credits in the amount of 15 million lei to various economic agents, thus utilizing the budget funds in the aims not envisioned in the aforementioned Law.

Also, in violation of Article 26 of the Law on the State Budget and paragraph 1 of Decision of the Government of the RM N 475 of 22.05.97, the Ministry failed to ensure quarterly receipts to the budget of revenues in the amount of 29.6 million lei received by JSC «Termocom» from the difference of tariffs for heat in conformity with results of activity in 1996, and compensation of expenses of «Termocomenergo» not covered by its own expenses.

By ignoring the established procedure, the Ministry of Finance has executed mutual settlements between the budget JSC «Termocom», other intermediaries, thus facilitating distraction of financial means for the benefit of commercial structures that constantly fail to observe contractual obligations to JSC «Termocom». In spite of the fact that arrears shall be paid directly, on 16.06.97 on the basis of faked documents presented by JSC «Termocom» the Ministry settled by means of mutual settlements arrears of local budgets to «Termocom» in the amount of 5.2 million lei as payment of arrears for excises taxes of Chisinau Tobacco factory in the amount of 2.6 million lei and of Calaras winery in the amount of 2.6 million lei swapped for tobacco and wine products, without taking into consideration the fact that at that moment JSC «Termocom» had arrears to the budget.

JSC «Termocom» delivered tobacco and wine products to «Korab si K» company in the amount of 5.2 million lei in exchange for raw materials (coal) actually delivered only for the amount of 0.5 million lei, thus increasing receivable to «Korab si K» (statutory fund -1.8 thousand lei) up to 23.1 million lei.

By 01.07.97 the Ministry of Finance allowed mutual settlements for the amount of 2.9 million lei for receiving by «Termocomenergo» cigarettes from Chisinau Tobacco Factory thus settling its arrears to the budget, in spite of the fact that by that time «Termocomenergo» had arrears to the budget in the amount of 5.8 million lei, and facilitating primarily payment of debts to «Filip» company in the amount of 2.9 million lei.

By ignoring Article 61 of the Law on the State Budget for 1997, the Ministry of Economics and Reforms together with the Ministry of Finance and other interested ministries and departments did not regulate the procedures for tender purchases of material values for budget institutions. As a result of that expenses related to purchases were funded without any tenders, thus giving possibility to these institutions to enter into direct contracts with suppliers at the prices exceeding the market ones which led to budget losses in the amount of 241.8 thousand lei.

The Ministry of Finance failed to ensure reimbursement of budget credit resources extended to economic agents with government guaranties. Thus, violating Article 62 (2, 3) of the Law on the State Budget for 1997, the Ministry did not recover payment from JSC «Fabrica de Sticla» (Glass Factory) in the amount of doubled average interest rate of the servicing bank for the period of credit utilization that was paid from the budget. An average refinancing rate of the National Bank was used which caused damage to the state in the amount of 2.4 million lei.

In spite of the fact that the Glass Factory failed to observe conditions of the agreement on debt repayment to the budget which by 01.12.97 amounted to 22.6 million lei, the Ministry filed suit to the Economic Court on compensation of only 7 million lei.

The Ministry violated the Law on the State Budget for 1997 and Regulation on the Procedure for the Government Reserve Fund Utilization enacted by Law N 1228-XIII of 27.06.97 by following the instruction of the Government to issue a loan in the amount of 500 thousand lei from the Government Reserve Fund to JSC «Moldcarton» for working capital replenishment, and 225 thousand lei to certain individuals for construction of residential houses and purchase of apartments.

The Ministry of Finance used money from the Government Reserve Fund to pay «Audit-Evcor» company for auditing of the activity of the state-owned company «Moldenergo», «Moldova-Gaz» concern, «Termocomenergo», and JSC «Termocom», in spite of the fact that «Audit-Evcor» failed to implement the required auditing program, to prove appropriateness of prices and rates for natural gas, energy, and failed to observe provision of paragraph 6.4 of the concluded agreement to ensure the quality of auditing and of presented materials.

Lack of appropriate control of the Ministry facilitated inefficient management of state resources by the Savings Bank. Thus, out of 5300 million of rubles of financial assistance provided to the Savings Bank in 12.03.93, the Bank extended credit guarantied by the Government to JSC «Tirex-Petrol» for the amount of 5.1 million lei (newly registered on 01.03.96, also with Government guaranties as owned by «Moldenergo») and another loan in the amount of 200 thousand lei to «Independent» company (Chisinau) that is a shareholder of the Savings Bank. The aforementioned company failed to observe its obligations to pay back the received credit. In spite of the fact that the maturity of the loan expired on 30.06.96, the Savings bank did not file the suit to the respective bodies. As a result, the state incurred losses in the amount of 404 thousand lei. The Saving Bank did not include into its profit the fine for the amount of 128.6 thousand lei received from JSC «Tirex-Petrol» for government resources utilization and the Ministry of Finance did not ensure inspection of utilization of earnings in the amount of 17.7 million lei accumulated by the Savings Bank.

7. Illegal import-export activities

Import-export operations are a favorite area for illegal activities. In the Republic of Moldova they take the form of:

- smuggling, (in 1997 there were prevented 52 attempts to smuggle material values worth 6.4 million lei, which achievements have been, monetarily, 20-fold greater than 1996 year;
- “pseudo-barter”, when goods are exported and marketed, while the proceeds are deposited in foreign bank accounts;
- “pseudo-exports” (for the example the production of the Tobacco Factory, which had to be exported, but was sold on the territory of the Republic of Moldova, thus resulting in losses in value added tax and excises);
- import-export transactions at inappropriately low prices with further sharing of the proceeds between the “partners” (by the Head Department of Fiscal Inspectorate has previously reported cases when the price was diminished 20 times);
- obviously unequal exchange operations;
- unlicensed exports;
- violations of exports quotas;
- “pseudo-transits”, when goods never reach the document destination and instead are sold within the transit country with no taxes paid, etc.

According to the data of custom service, the detected volume of smuggled goods grew from 2.7% of the total export-import in 1997 to 10.6% in 1998. During the same time, the number of criminal files reaching the court diminishes continuously, criminal files are closed (from 28 open criminal files no file was investigated in 1998).

An accomplishment of a *cross-checking* of Moldovan and Ukrainian *information* regarding Moldovan exports to Ukraine shows that the data from the Ukrainian side is almost double. This can not be explained solely by the “role” of Transnistria.

The same situation takes place in the relationships with Russia. Within this investigation a comparative analysis of Moldovan and Russian sources of information regarding export-import operations was accomplished. The data was compared on a selected number of goods accounting for 47 % of Moldova’s imports and 54 % of its exports. The analysis disclosed essential discrepancies. Thus, the discrepancy reached 55% for imports and 93 % for exports. It is evident, that this degree of deviations cannot be explained by Transnistria’s share in Moldova’s international trade. In terms of this selected group of goods, the budget losses accounted for 35 million lei, resulting from nonpayment of VAT; losses caused by nonpayment of excises, only for wines, accounted for 48 million lei. It is important to notice that a series of goods registered in Moldova as exported (cigarettes, champagne) were not registered in Russia, which allowed the exporters to avoid payment of excises.

According to Moldovan sources, the price but of exported “vodka” practically coincides with the price of the imported “vodka”. Russian sources show a tripled price. The import of Moldovan wine in Russia, according to the Russian source of data, is almost twice bigger than that recorded in Moldovan source, the price “increasing” by 30%.

According to the Romanian data (“Curierul National”), the volume of sugar exports from Moldova to Romania exceeded in 1997 the produced volume on the territory of Moldova 1.8 times. Generally speaking, a big part of this sugar is made in the Ukraine, but the certificates of origin of production are faked with the intention of taking advantage from the free trade agreement between Romania and Moldova.

The absence of temporary customs between Transnistria and the other part of Moldova, and existence of two fiscal systems on this territory, generate considerable losses for the Moldovan budget. The absence of VAT levying on the territory of Transnistria implies the fact that many imported goods pass the customs at Transnistria, then transit to the right bank of the river Nistru then being shown as produced on the territory of Moldova. Thus, these goods are avoiding payment of VAT and are engendering an unfair competition to local goods.

Tobacco complex.

As an approach of measuring the scale of the black market, can be used the analysis of discrepancy between production and distribution of tobacco products. This method was proposed by the Norwegian Institute of Social Applied Sciences and was used by the Central Statistical Bureau of Latvia. Within our investigation an attempt has been made to estimate the minimal volume of shaded transactions in the tobacco industry.

According to the official statistics of Moldova, 9.6 billion cigarettes were produced in 1996. From them there were exported \$ 49.7 billion of tobacco products (\$ 20.89 million to NIS, or 2 billion cigarettes, and to other countries - \$ 28.85 million, or 5.8 billion cigarettes). There were registered as imported \$ 0.42 million (0.04 billion cigarettes). Statistical data in a long run show that the consumption of cigarettes in the Republic Moldova reaches 5 billion cigarettes. The balance is the following:

9.6 billion pieces + 0.04 billion pieces < 5 billion pieces + 7.8 billion pieces.

9.64 billion pieces < 12.8 billion pieces by 3.16 billion pieces.

These more than 3 billion cigarettes may mean either unrecorded import, or undeclared production. In both cases this means that the budget of Moldova incurred about 110 million lei in losses. This is a minimal estimation, because, according to some sources, the import of cigarettes amounts to about 2 billion pieces. In this case

the discrepancy could constitute 5 billion of cigarettes, and income, consequently, bigger.

From the other side, according to the official statistics of Moldova, the retail sale of cigarettes in 1996 amounted to 17.3 million lei (about 350 million cigarettes). This means that the recorded sale of cigarettes equals to only 7% of the total amount.

Due to the lack of supervision and control by the State Tax Service over the Customs Department in the handling of export of goods and the absence of analysis of the sale of goods in the domestic market, there were cases when documents were prepared allegedly for export of goods, while actually the goods remained in the Moldova and were sold in the domestic market. Thus, as per documentation the "Tutun" joint-stock company exported 61 per cent and 78 per cent of the manufactured cigarettes to the USA, Austria, Germany, England in 1995 and 1996, respectively; whereas in reality the company sold most of its cigarettes in the domestic market and in the CIS without having paid both VAT and excises as it should have paid pursuant to current legislation. The cost of VAT and excise exemption of exports was MDL 43 million for the 9 months of 1996 alone.

Deviation in information regarding Moldo- Russian import and export in 1996

	Unit	I M P O R T S						E X P O R T					
		Russian source			Moldovan source			Russian source			Moldovan source		
		Quantity	\$ th.	Price \$ th./un.	Quantity	\$ th.	Price \$ th./un.	Quantity	\$ th.	Price \$ th./un.	Quantity	\$ th.	Price \$ th./un.
Vegetable oil	thou tons							2.02	1894.7	936.12	1.20	1051.3	874.63
Sugar	thou tons							66.96	35423.3	529.02	60.70	29760.8	490.29
Canned vegetable	thou tons							38.38	28931.3	753.79	25.09	20261	807.40
Fruit juice	thou tons							9.63	6040.3	627.11	27.00	16213.4	600.50
Jam	thou tons							3.66	4478.5	1223.30	3.16	4173.6	1322.64
Champagne	thou dcliters	2.40	49.9	20.84				1739.25	31888.5	18.33	2342.80	30684.7	13.10
Vermut	thou dcliters	3.37	73	21.68				286.24	4757.6	16.62	153.30	1355.9	8.84
Other wines	thou dcliters	7.26	70.3	9.68	51.60	416	8.06	21774.54	231633.8	10.64	12178.90	92643.4	7.61
Alcohol ethilic	thou dcliters							239.00	2931	12.26	86.70	719.5	8.30
Vodka	thou liters	28.86	90.8	3.15	4.00	49.6	12.40	4133.83	17185.2	4.16	4063.00	14050.9	3.46
Tobaco raw materials	thou tons	0.05	83.2	1733.33	0.03	59.3	1912.90	13.79	19611.5	1422.46	8.46	11084.6	1309.79
Cigarettes	thou \$		191.8						2927			6697.5	
Coal	thou tons	137.38	6231.9	45.36	106.10	6518.6	61.44						
Fuel	thou tons	38.85	2937.2	75.61	119.70	13041	108.95						
Natural gas	million m3	3154.00	182947	58.00	2038.10	118209	58.00						
Footwear	thou payrs	57.39	759.9	13.24	25.80	318.5	12.34	4178.73	28651.9	6.86	304.30	1308	4.30
Total deviation	thou \$		76246			76246			214237.2			214237	
Share of deviations in the sum imp.(exp)	%		40			55			52			93	
Share of goods in total export (imp)	%					46.99						53.49	

Other goods. According to data of Accounting Court, in the absence of efficient control by the State Tax Service, in the period of 1996-1997 the Customs department did not apply VAT - for any good reason and against regulations - to goods (including fuel) imported under contracts which had been concluded with companies registered in the CIS, whereas the payments under these contracts had been made to companies registered outside CIS (England, Germany, Switzerland, Austria, etc.).

Due to this fact, VAT was not applied to the fuel imported to Molodva by the following companies, i.e. LUKoil-Moldova (MDL 6 million), Ieruselem (MDL 2.2 million), Zimbru-Exim (MDL 1 million), Transconstructia (MDL3 million), Calbor-Corporation (MDL 3 million), whereas payment for that fuel made out of bank accounts with the banks inside Moldova into accounts with banks outside CIS. The application of the regulation on taxation of fuel to the economic agents by the State Tax Service and the Department of state control was illegitimate. While in this period the government-owned enterprise, the state association for fuel (later "Tirex Petrol" joint-stock company), was to pay VAT on imported fuel in all cases when payments were made to companies registered outside the CIS, the value-added tax on fuel was not applied with respect to non-state enterprises. Given the fact that the costs of "Tirex Petrol", which included VAT, were used as a basis for establishing prices for fuel in the domestic market of Moldova, non-state enterprises received additional income equal to the amount of non-paid VAT.

In some cases, to avoid paying taxes vacant customs warehouses were used, which had been opened by economic agents by license in the customs area of the Republic of Moldova. Audits of the "Global Group" company, which is funded by the "Neftegas group" company (Malta), revealed a case when a supply of 1.070 crates of the "camel" and "Apollo Soyuz" cigarette worth MDL 589,200 was declared in the free customs warehouse of the said company by a Latvian company as allegedly imported from Latvia. On the same day as per prepared documents the goods were shipped back to Latvia. As per customs declaration filled in on 24.08.1996 the goods were received for customs inspection by Chisinau customs office, however, there is no evidence of the goods having left Moldova through the border customs check points. The date of filling in as was written in the customs declaration was 24.08.1996, whereas the customs stamp was dated 23.08.1996, i.e. one day earlier it was draw up. The "Ibo Com 91" company, which has a free customs warehouse in the municipality of Chisinau, made a similar transaction with a supply of cigarettes from Turkey. The cigarettes arrived on 30.05.1996 and on the next day as per documentation, they were re-exported to other countries. As a result of such supervision over export and import of cigarettes the markets in Chisinau are inundated with cigarettes, which are cheaper than those manufactured in or legally imported to the RM.

Sometimes tax offices issue certificates to economic agents, exempting them from VAT on imported goods, even without a thorough examination of activities of such agents. The Tax Inspectorate of Chisinau issued certificate No 01-21-02/70,

exempting the “Neptun Nord” joint-stock company from VAT on fish and fish products under the pretext that the products were as raw materials for further processing. The cross-audit, however, showed that a part of those goods was not used for further processing but was sold in the domestic market, and thus exempting it from VAT is illegitimate.

On October 15, 1998 a common agreement for fighting smuggling between the custom service of Moldova and Cernauti region (the Ukraine) was signed. Even if this is a positive moment, still about 30-40% of the state border are not under control. In the Republic of Moldova practically two custom territories exist. An adjusting of the existing institutional system to the current situation in the country is needed. The territory of the right bank of r. Nistru should become a distinct custom territory for the flows of goods (but allowing free movement of population).

A solution of the problem of illicit export-import and corruption¹³ in custom service demands a set of measures adjusted to the real situation:

- immediate dislocation of a temporary customs service between Transnistria and the other part of Moldova;
- customs’ reform;
- attracting of foreign specialists, paid out of technical assistance, funds, assigned to decision making positions in customs structure.
- a temporary introduction of army in customs service;
- examining the possibility to transfer the customs service in private sector;
- elimination of politic influence in the customs service;
- a decent remuneration of customs officers;
- construction of customs service buildings, service modernization;
- minimizing the discretion in decision making;
- applying a contest system in hiring employees, training custom officers (expertise techniques, responsibilities, classification of tariffs, using computers);
- enhancing fluidity of personnel within the departments for custom service control;
- setting up a modern informational system;
- carrying out of cross-checking information;
- using X-rays in custom service;
- making additional random controls (5% of total) of documentation and goods by special groups after passing the customs.

¹³ Strategies to Combat Corruption in Ecuador: Custom Service, National Association of Business Owners, ANDE, CIPE, 1998;

8. Illegal privatization

Delays in legal privatization in the Republic of Moldova caused, on one hand, by the need for the creation of a legal basis for this process, and, on the other hand, by the lack of interest from the part of some people (especially those who enjoyed considerable profits from improper use of state-owned material resources) have led to the irregular privatization with all its consequences. Irregular privatization has largely shown itself both outside and within the legal privatization framework, violating, however, the provisions of the current legislation. One form of illegal privatization is “donation” of state-owned property (wine and building materials producing enterprises, buildings, lands etc.) through the decision of the Government of the Republic of Moldova to some private enterprises (businesses, collective farms, public organizations, etc.). The transfer in 1991-1992 of FSU centrally controlled enterprises under the authority of the Republic of Moldova offered big opportunities for illegal privatization of state-owned property. A more sophisticated method is based on the association of state-owned and public enterprises with private enterprises and individuals. In this case two objectives were achieved at the same time: business people with initiative would take over the management of these associated enterprises thus making it possible to use and dispose of the state-owned and public property; state-owned and public property was severely underestimated taking into consideration that, despite big inflation, no adjustments in the price of fixed assets were made during the period between 1983 – 1992, while, on the other hand, private property share, usually in form of money, was overestimated. The nationalization of both former Soviet Union’s and Moldova’s Communist Parties in 1991 was also used as an opportunity to transfer vehicles, equipment, furniture, financial resources etc., the private sector. In many cases, apartments as well as buildings and commercial spaces were transferred irregularly by the national and local authorities to individuals and legal persons and thereafter privatized.

In defiance of the fact that many cases of the law violation were discovered by the proper control institutions, there have practically been no cases of proper punishment for people found guilty and of payment of appropriate damages.

Data of the Accounting Court prove that show that a number of violations were committed as a result of insufficient control over privatization process and failure to take necessary measures for liquidation of violations revealed in the course of previous inspections of the Accounting Chamber.

After the first inspection of the Ministry which took place in 1995, the situation with regard to legality of privatization process practically has not changed, as even more serious violations were detected. Responses and explanations of the Ministry are often purely formal and justify committed violations. In certain cases

conclusions and requirements of the Accounting Chamber formulated in its reports were simply ignored.

In violation of current legislation on privatization, part of the property subject to privatization for national patrimony bonds was illegally sold that actually increased misbalance between estimated value of the property subject for privatization for NPB and the amount of national patrimony bonds distributed among population. This resulted in the decision of the Ministry on the procedure for determination of initial price of privatized objects which placed holders of NPB into unequal situation.

Many violations were committed upon purchase of 20% of enterprise shares by employees of enterprises on a tender-free basis. These violations included reduction of estimated value of enterprises, exclusion of dismissed and employees and pensioners from privatization process with concomitant inclusion of persons who never worked at this enterprise.

In the course of state-owned enterprises corporatisation the Ministry of Privatization and State Property Management gave an ungrounded confirmation of the leased product amount. Over 120 of leased enterprises which passed through the process of corporatisation and privatization used various illegal ways of increasing the value of leased product and of reduction of the state property. Materials of inspections including the ones organized by the Government of the RM testify to the facts of calculations deviations which were used as the basis of which these amounts of leased product were confirmed. Corporatisation and privatization of state-owned enterprises was also carried out with violations of current regulations. Reduction of the estimated value of the state property in the course of its privatization by means of various falsifications (false year of enterprise construction, intentional exclusion of certain property into estimation documents, ungrounded increase of depreciation costs, distortion of indexation ratios, and etc.), as well as payment of monetary contributions to the statutory funds by employees resulted in the situation when staff of many enterprises received majority stock holdings of certain joint-stock companies, that proves intentional reduction of results of the state property evaluation.

Random inspections of legality state property evaluation carried out in 15 joint-stock companies reorganized from retail trading and public catering companies revealed violations of Article 11(a) of the Law on Privatization Program for 1995-1996 and illegal reduction of state property value by 1.2 million lei.

The Ministry of Privatization and State Property management committed gross violations upon privatization for NPB of entities of health care, retail trading, public catering, and other sectors of national economy. At the majority of entities referred to the aforementioned sectors of economy privatized through tenders the value of the state property was reduced by means of illegal increase of depreciation cost,

failure to include part of property into evaluation documents, preliminary alienation of property at impaired prices, and etc.

Thus, estimated value of pharmacy #4 «Recipe» did not include the value of a two-story building. Upon privatization for NPBs of 432 pharmacies included into privatization list, 190 (44%) of them were alienated as part of regional pharmacy associations without preliminary split.

JSC «Nufarul», JSC «Chisinau-foto», JSC «Progresul», JSC «Igiena-Plus» did not include into their estimated value the value of premises rented by them. JSC «Nufarul» did not include the value of 14 premises the total value of which amounted for 177 thousand lei.

«Balaton» cafe with the area of 202 square meters located in a five-store building was privatized at a symbolical price of 18684 thousand monetary units at the pretext of planned pulling down.

Gross violations of current legislation by means of reduction of the estimated value of privatized entities were also committed during cash privatization process of state-owned enterprises. In majority cases economic entities inspected by the Accounting Chamber illegally wrote off fixed assets, and without any grounds and any indexation moved them to low-value inventory. Thus, the value of «Haiduc» shop property subject to privatization was reduced, and purely symbolic value was assigned to certain types of equipment. For instance, refrigerator (made in 1986) - 3.4 lei, typing machine - 1.5 lei, cashier machine - 10 lei, freezer - 1.9 lei, and etc. Similar violation were committed during cash privatization of «Bujor», «La placinta», «Vara», and other shops.

In spite of warnings made to the Ministry of Privatization and State Property Management as a result of previous inspection of the Accounting Chamber on necessity to modify relations with non-state companies that had committed gross violations of current legislation upon preparation of entities for sale, the Ministry did not take necessary measures as a result of which preparation of the majority of entities for privatization and organization of traditional auctions was carried out by intermediary companies («NGG-Print», «Moldprivatinvest», «Lara» and «Glia»).

Issuance by the ministry of Privatization and State Property management of permissions to pledge state property of enterprises was often carried out with the damage for the state, thus undermining safety of this property. So, with permission of the Ministry property of JSC «Tirex-Petrol», JSC «Calaras Winery» was pledged though it was two times more expensive than the amount of extended credits. In certain cases pledged property was evaluated at reduced prices. Thus, the Ministry allowed pledge of fixed assets and working capital of «Cricova» winery the value of which is 1.5 times higher than the amount of the received credit. Fixed assets of this winery were evaluated without indexation.

The Ministry of Privatization and State Property Management committed violations of current legislation during sale of state property not used in technological process, including means of transport by reducing their sale prices.

Such cases also took place in the Ministry of Agriculture and Food, «Urbanproiect» institute, during liquidation process of «Moldova-Constructia» Association, and others.

The Ministry of Privatization and State Property Management failed to execute in full the functions of state property management. There is practically no record keeping of all economic entities that carry out their activity on the basis of state property and execute management of it, as well as accounting of its amount. Institute of state property owner representative does not properly function, and there is no ensuring of efficient utilization of state property, in particular of leased one. Therefore, dividends transferred to the state budget by about 3200 commercial entities that are using state property valued in 13.5 billion lei amounted in 1996 only 4.8 million lei out of 6 million lei envisioned in the state budget.

The Ministry of Privatization and State Property Management does not take necessary measures on state interests protection at the leased enterprises that was proved by many violations of acts regulating leasing relations (most often impairing the amount of payment for leasing) that were revealed in the majority of agreements of state institutions and enterprises inspected by the Accounting Chamber.

Thus, approval of leasing agreement envisioning leasing of a premise by Chisinau Veterinarian clinic to a physical person for 50 years with further permission to buy it out has practically legalized illegal actions of this institution. The leased property was underestimated and amounted only 300 lei, the leased payment was fixed at the level of 60 bani per one square meter, in other words it was reduced practically by dozen times in comparison with the amount of payment envisioned in regulations.

The Ministry of Privatization and State Property Management committed violations of current legislation upon foundation of joint-ventures with foreign capital. There were no necessary documents reflecting solvency of foreign partners, nor feasibility studies. The value of state property included into the statutory capital was reduced. Deadlines for payment of founders contributions to the statutory capital were missed. Intellectual property was included as contribution of foreign investor without any copyrights.

Thus, in conformity with Decision of the Government of the Republic of Moldova N 302 of 12.05.95 «On Joint Moldovan-Russian Closed End Joint-Stock Company «Gazsnabtranzit», the property included into the balance sheet of «Moldovatrangaz» and «Tiraspoltrangaz» was transferred as payment for natural gas supplied from Russia evaluated in US Dollars and included as its contribution into the joint-venture. Evaluation of fixed assets was carried out with violations of provisions of Article 9 of the Law on Foreign Investments stipulating application of

international market prices in such cases. Evaluation was made on 01.10.94, but at prices of 01.01.94, so inflation of 10 months of 1994 was not taken into consideration. As a result of these violations «Moskvitch» automobile (1988) was evaluated in 104 lei, automobile GAZ-2410 (1998) in 1244 lei.

Privatization through direct agreements was also carried out with violations of current legislation which is proved by inspection results of special committee of the Parliament, Accounting Chamber inspection and respective decision of Economic Court of 29.06.97 on cancellation of privatization of «Legcovic» sanatorium.

Drawbacks and violations in the activity of the Ministry resulted in failure to observe requirements of Privatization Program for 1995-1996 on cash privatization that resulted in failure to implement the Laws on the State Budget for 1995 and 1996 in the part of budget revenues from privatization and state property sale. As a result of failure to implement plans and programs on the basis of which the budgets of respective years were adopted and because of lack of complete information about state property sale auctions the budget received only 30% of planned revenues were received in these years.

The Ministry of Privatization and State Property Management also committed violations of current regulations in its financial and economic activity. These violations include exceeding of cash expenditures, inclusion of erroneous data into report on expenditures in 1995, ungrounded writing off of objects and materials utilized for less than a year, failure to pay rental fees to certain commercial structures.

9. Energy sector

The lack of a competitive environment and existing system of granting compensations to producers, implies the growth of shadow transactions in this complex, as well as over-pricing. The growth of electricity losses share can be considered as a signal of expansion of embezzlement. Losses of electricity in the Republic of Moldova are comparable and sometimes exceed their production in the territory of the right bank of r. Nistru. The share of losses and embezzlements grew up from 10 % of the total consumption in 1990 to 30 % in 1997, amounting to about 300 thousand lei per day, based on some estimates, or 100 million lei annually. According to international standards, average losses in the power distribution network account for 9-12 % of the total consumption. In the Republic of Moldova this share cannot be explained just by the obsolete equipment; it is caused also by spread of embezzlements. These losses can be observed in geographical differentiation. Thus, in the first semester of 1998 the share of losses in the electric power network amounted to 14.6% in Chisinau, 43.8% in the center of Moldova, 41% in the North, 40.7% – North-West and 46.8% in the South of Moldova.

If during the Great Economic Depression the growth of prices for energy implied a restructuring of the economy towards production of less energy-intensive goods, and, as a result, a two-fold decrease of consumption of energy per unit of GDP, then in the Republic of Moldova the consumption of energy per unit of GDP increased during the last three years by about 20%. The debts of the energy sector grew quickly.

The state energetic company “Moldenergo” within the period from 1994 through 1996 has admitted excessive losses for a sum of 37.3 million Lei, 49.3 million Lei and 67.3 million Lei, out of which by the result of effected control reimbursed were 4.9 million Lei, 5.3 million Lei and 8.8 million Lei respectively.

Purchasing energy resources at overestimated prices the Company made no provisions to cut on expenditures. As a result the State Company “Moldenergo” experienced losses to the amount of 404.9 million Lei.

Company’s indebtedness to the budget as at 01.01.97 amounted to 11.54 million Lei, including such to the state budget - 11.2 million Lei and to the Social fund 0.34 million Lei.

Within the period from 1994 through 1996 the State Company “Moldenergo” received under government guarantee loans amounting to 339.1 million Lei (US\$ 76.3 million).

As at 01.01.97 the sum of non-repaid credits amounted to 101.7 million Lei (US\$ 21.7 million).

The State Company “Moldenergo” failed to repay the loan of US\$ 3 million within the established terms, received from the Ministry of Defense of the Republic of Moldova in compliance with Government Decision No.202 of 27.06.94. For the violation of terms of loan repayment the Company has paid (on the basis of Arbitrage decision) penalty amounting to 673.2 thousand Lei.

The State Company “Moldenergo”, on behalf of the Government of the Republic of Moldova has concluded contract with a Malta company “Neftegasgroup” Ltd on 01.12.94 for a credit of US\$ 50 million to procure 100 thousand tons of furnace oil and 1.7 million tons of coal.

Regardless of the fact that the above contract has not been fulfilled, the Government of the Republic of Moldova through its Decision No.906 of 14.12.94 signed by ex Prime Minister A.Sangheli and approved by the first Deputy Prime Minister I.Gutu and by Minister of Finances I.Chitan (not registered with the government office of the Republic of Moldova and issued not on a government letter head, and not published in Monitorul Oficial of the Republic of Moldova) instructed the Ministry of Finance to reimburse to NGG Ltd Company the non-extended credit, while the National Bank has been authorized to provide for transfer of US\$ 50 million at the expense of the sums that the Government will receive as priority payments from different institutions.

The Ministry of Finance executing the above Government Decisions and failing to check credit extension from NGG Ltd Company, through its payment orders of 22.12.94 and of 10.02.95 has transferred to that company US\$ 26.9 mln, i.e. has actually repaid the non-existing debt of the Government of the Republic of Moldova.

Executing the Contract (without date of making it out) for procurement of furnace oil and coal the State Company "Moldenergo" has received during 1995 commodity worth of US\$ 16.9 million. Thus, the NGG Ltd company owes to the Government of the Republic of Moldova US\$ 10 million. This amount until now are used free of charge by the NGG Ltd Company. Without Government and Ministry of Finance's consent and in violation of the provisional regulation on non-cash settlements, through a joint agreement No. A-NGG-MD-MG of 03.07.96, the debt of NGG Ltd Company has been transferred from Moldenergo Company to Moldova-Gaz Concern. It was only during the check up in February 1997 that based on Ministry of Finance claim of 03.10.96 the agreement of debt transferal has been cancelled and actual arrears were reestablished that actually amount to US\$ 10 million. The interest rate paid to the Ministry of Finance by State Company "Moldeenergo" for the financial resources of US\$ 10 mln, used by NGG Ltd Company as at 01.01.97 amounted to US\$ 2.8 million (minus foreseen sanctions).

Making no use of the amounts received under government guarantee (in December 1994 and in February 1995), the State Company "Moldenergo" takes another commercial credit in July 1995 (from JS Commercial Bank "Petrolbank") to the size of 64.1 million Lei to procure fuel and electric energy. In order to realize this credit the company has concluded a contract with "Transworld-Tehnologic" (daughter company of NGG Ltd) to procure 600 thousand tons of coal at US\$ 34 per ton. Settlements for the coal delivered were due by prepayment or within 10 days from the date of delivery.

While fulfilling contractual conditions the State Company "Moldenergo" transferred to its partner in August-December 1995 the value of 425.9 thousand tons of coal, i.e. 64.1 million Lei. The "Transworld-Tehnologic" receiving money to its account has failed to fulfill its obligations on coal delivery terms. More over the company having 50.8 thousand tons of coal in arrears as at 01.01.96, groundlessly and with SC "Moldenergo's" consent has increased the price per ton of coal from US\$ 34 up to US\$ 42. Thus, the State Company "Moldenergo" instead of receiving (after 01.01.96) at the expense of obtained resources 50.8 thousand tons of coal, has actually received only 44.9 thousand tons, due to which fact its debt to "Transworld-Tehnologic" amounted to 2.3 million Lei.

A significant part of the above credit has been repaid at the expense of credit extended under government guarantee in December 1995 to SC "Moldenergo" through the Ministry of Finance from a German "Commerzbank". In compliance with the Government Decision No. 796 of 05.12.95 a credit of US\$ 10 million received from "Commerzbank" was earmarked to be used by SC "Moldenergo" to procure energy resources. The Ministry of Finance in violation of provisions set forth under

the above Decision admitted improper use of this credit, having fully transferred it to JS Commercial Bank “Petrolbank” to clear SC “Moldenergo’s” debt due to this Bank, including US\$ 2.6 million debt premature repayment (maturity term October-December 1996).

In all cases of dealing with NGG Ltd and “Transworld-Tehnologic” the SC “Moldenergo” according to its contractual obligations was due to provide its partners, i.e. the above companies with a share of delivery, approved by agreements concluded between the Government of the Republic of Moldova and the Government of the other countries.

Failing to observe the Government Decision No.798 of 27.12.93 “On approval of Agreement-model for commodities sales”, unspecified in the agreements concluded with coal suppliers was the exact responsibility for failure to meet the contractual conditions.

In the majority of cases the management of the company failed to conclude immediate agreements with the former permanent suppliers, but with assorted intermediary agents of non-governmental commercial structures, which resulted in prices rise for the electric energy.

The majority of credits were extended without presentation of respective documents for each credit, i.e. forecast of financial activity, techno-economical and financial substantiation subject to expertise, availability of collateral, its registration.

Failing to observe the requirements set forth under Main provisions on cost structure for manufacturing and realization of products (works, services), included into its prime cost and on the procedure of reporting on financial results of the enterprises, the company within the checked up period effected unmotivated expenditures that were included into energy’s prime cost.

Thus, failing to fulfill conditions of agreement No.1 of 05.01.95 on supply-purchasing natural gas, concluded between SC “Moldenergo” and “Moldovagaz” concern, groundlessly referred to production costs of SC “Moldenergo” were natural gas losses borne by “Moldovagaz” Concern to the size of 12802.7 thousand Lei (36979.6 thousand cubic m), hence decreasing by the same amount the balance profit for 1995, which resulted in profit tax reduction by 4096.6 thousand Lei.

Unforeseen by expenditure costs and transferred to the Association “Moldauditing” on July 20, 1996 and on August 29, 1996 were 42.9 thousand Lei and 30 thousand Lei respectively earmarked to audit accountability and financial-economic transactions. None of the respective documents were submitted in response to lawful claim of the examiners.

Unjustified included into the costs were another 151.1 thousand Lei, bound to booking special flight routes, financing studies of physical entities and expenditures in connection with business traveling abroad.

Infringing claims set forth under the effective prudential requirements, the company received from the consumers resources amounting to 316.4 thousand Lei for

energy delivered out of which only 154.7 thousand Lei was transferred to the bank. In its turn the company extended cash to Transnistrian enterprises to clear netting.

In 1994-1996 the Company employees received interest free loans amounting to 197 thousand Lei for a term from 2 years and up to 36 months (up to 25 thousand per single employees), failing to foresee responsibility arrangements for repayment of such. This resulted in diversion of company's circulating assets, having to make use of bank credits in order to finance its basic business. Receivables on resources extended as at 01.01.97 amounted to 75.2 thousand Lei.

The SC "Moldenergo" while lacking special purpose funds and also due to lack of profit proceeded to effect various expenditures at the expense of working capital, thus forming arrears on the fund earmarked for social and cultural arrangements (as at 01.01.97) and amounting to 5163.6 thousand Lei, including payment for students studying in various schooling institutions - 427.8 thousand Lei, extending money loans - 197 thousand Lei, maintaining polyclinic, medical post, canteen, summer camp for children - 3089 thousand Lei, buying 5 apartments - 317.9 thousand Lei, sponsoring schooling institutions - 24.6 thousand Lei, contributing to participation share in different organizations - 32.0 thousand Lei, etc. Overspending at the expense of material incentive fund amounted to 685.5 thousand Lei.

Due to lack of control over the performances, the former key accountant of the company F.Eder together with calculation center Director Sapovalov have effected a dubious transaction with a private company "Hyperion". Transferred to that company (September 1994) was a sum of 167.4 thousand Lei, which has been groundlessly written off the balance at the moment of its transferal. Established in the course of a check up (Q1 1997) was the fact that the product worth of 103 thousand Lei was not received from "Hyperion" against the above transfer.

Likewise in 1993 transferred to the above mentioned company and written off the balance of SC "Moldenergo" was a sum of 29.7 thousand Lei, while 16 PC's and 20 calculators and various spare parts received by Sapovalov on the grounds of 6 Powers of Attorney that were not registered upon termination of check up and not accounted for. The losses caused to SC "Moldenergo" as a result of the above bargains concluded with "Hyperion" company amount to 133.2 thousand Lei.

Similarly, the losses incurred to SC "Moldenergo" through involvement of F.Eder in dubious transactions with private companies "Beau allonde Poligrafic" Ltd. for a sum of 19.8 thousand Lei, "Rubicon" Ltd - 5 thousand Lei, "Oratex", "Soti", "Arioso" (by forging banking documents) - 100 thousand Lei. In violation of the effective prudential requirement Moldovan Hydro Electric Power Station (Cuciurgan) kept without payment and without reflection in balance sheet fuel savings worth of 10.5 million Lei resulted from electric energy generation in 1994.

Not received from JSC "Tirex-Petrol" and not entered into the books was the cost of coal worth of US\$ 365.4 thousand used to generate electric energy, exported by the above company to Rumania via "NGG Ltd".

Solution of the energy complex problems implies such measures as:

- restructuring of the complex, including enhancing debts collection, disconnection of consumers, who are not paying for energy usage;
- privatization of the enterprises of the energy complex;
- elaboration and approval of a set of clear, exact, transparent and predictable rules regarding the operations of the enterprises of the energy complex considered natural monopolist;
- after privatization it is necessary that the state assumes debts of the sector and reschedules them in such a way, so that they do not impact on the future pricing in the complex;
- shifting from the system of subsidizing energy producers to the system of direct subsidizing for the vulnerable parts of population.

10. Fighting corruption a main way to reduce the shadow economy

Fighting corruption generates *immediate profits*. Revenues from fighting corruption exceed many times the costs. According to some Western estimations, the expenditures of L1 in fighting corruption at the local level generate on average L23, and about L250 on the international level¹⁴.

The materials of the United Nations Commission for crime prevention show that the above mentioned phenomenon has widespread in the Central and East Europe during the last decade. These kinds of problems are included into the programs of seminars and congresses of many international bodies (*INTOSAI, EUROSAI, SIGMA, Accounting Court of the EU, World Bank, Working Group on briberies OECD, International Monetary Fund, etc.*).

The Defense Supreme Council of Romania adopted a proposal on establishing the National Institute for studies of corruption and organized crime under the Academy of Romania.

The goals of fighting corruption can be different:

- short run efficacy in the private sector;
- long run dynamic efficacy, economic growth;
- social equity, political legacy.

The durable strategic directions of fighting corruption in the Republic of Moldova should include deregulation, privatization, transparency, institutional reform, improvement of the enforcement system, reduction of the monopoly force in all spheres, clarifying the degree of discretion in the activity of decision makers.

It is impossible to fight corruption tolerating the development of shadow economy. In NIS countries fighting corruption is the only possible way to obtain economic development.

¹⁴ I. Bogdan, Corruption and economic crime, "Curierul Economic", 45(347)

Implementation of a *policy fighting corruption* needs the reform in legislation, the institutional reform, improvement of the system of regulation of fiscal audits, reduction of the public tolerance:

Legislation reform:

- Appealing for assistance on behalf of the international institutions in fighting corruption and economic crimes, applying for an external system of monitoring;
- Appealing to projects financed through foreign technical assistance to perform a juridical expertise of laws and amendments proposed for adoption, improving the legal system, removing of contradictions, double meanings, etc.;
- Perfecting of preventive anti-crime measures;
- A clear definition of a penalty system for law breakers;

Amelioration of fiscal control procedures:

- Simplification of regulations of state controls and audits;
- Systematization and unification of the work carried out by different audit agencies;
- Publishing a clear information regarding controls, rights and obligations of control agencies;
- Establishing a unit for registering and regulating the number of controls of the same enterprise;
- Reforming the fiscal and accounting systems, simplification and ensuring its transparency;
- Perfecting the qualification level of control and audit personnel;
- Publishing fiscal information, transparency of preparation and execution of state budget;
- Introduction of a mandatory tender system for public procurements.

Institutional reform:

- Reduction of the number of state institutions, reduction of staff;
- Substitution of the procedure of personal visits for solving problems by using mail, including e-mail system;
- De-politicization of Government, introduction of an obligatory system of professional promotion on the base of performance and contest;
- Introduction of a clear and definite system of ethic standards for the state employees;
- Creation of independent institutions authorized for investigations the accusations in corruption.

Reduction of public tolerance:

- Coordination of efforts of educational, religious organizations and mass-media in an anti-corruption campaign;
- Assuring transparency of financing political parties;
- Training journalists in promoting a manner of balanced reporting, introduction of an ethic code for journalists;
- In order to improve the credibility of population in state structures – creation of a unique body for complaining about inadequate behavior of policemen, workers of custom service, fiscal auditors, etc.

As *immediate measures for fighting corruption* the following suggestions should be considered:

- Elaboration of a strategy for fighting corruption in terms of ministries and main directions: public procurements, public campaigns' management, urban planning, fiscal administration, customs reform, legislation;
- Formation at the national level of a coordinating body responsible for the implementation of the strategy for combating corruption;
- Identification of a number of key-agencies in the domains where a concentration of efforts is required to combat corruption during the first year;
- Applying of income declaration procedure for state employees, starting from the top level;
- In countries with a high level of corruption, where any attempt to fight corruption is treated as discrediting political opponents, a strategy of “detecting” corrupted officials at the top level in the ratio represented by parties in the Parliament (existing algorithm 2+2+1) could be applied. In order to gain the credibility of population, the cases should be proceeded publicly, by announcing the punishment of the law breakers, and the directions where obtained money are spent (pensions, wages, repayment of debts, etc.).
- An immediate installation of gas counters at the entrance and exit from the territory of Republic of Moldova.

Conclusion. The phenomenon of corruption in Moldova, as well as in other country in transition, expanded so much, that it practically blocks the economic development of the country. Any attempt to modify the legislation targeted to the stimulation of private sector's development, encouragement of investments and innovational activities, export promotion, solving the problem of budget deficit, external debt, problems of the social and educational sectors will be unsuccessful until drastic measures to combat corruption - the moving force of the shadow economy - will be undertaken. In order to achieve this, it is necessary to extend the study and to elaborate a clear strategy of fighting the above-mentioned phenomenon.

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