COUNTRY UPDATE-Moldova: Securities & Banking

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Moldovan financial services and capital market legislation has undergone significant modernisation in recent years. Such modernisation has had as objectives: (i) implementing international best standards in the banking area and improving ownership transparency, (ii) reviving the capital market and increasing access to finance through capital market; (iii) shift from rule-based ("tick-the-box" approach) to risk-based supervision; and (iv) harmonisation of national laws on credit and financial institutions, capital market, insurance and leasing with European Union legislation.

Further, signing of the Association Agreement with the EU and its ratification (on July 2, 2014) has brought to the agenda of Moldovan lawmakers the objectives of transposing the relevant EU Directives into domestic laws. This new wave of legislative reform ultimately aims to create an investor-friendly legal environment which is seen as a precondition for sustainable growth of market-based Moldovan economy.

Banking system

The Moldovan banking legislation is perceived as quite progressive and generally in line with (i) Directive 2013/36/EU of the European Parliament and of the Council of June 26, 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, and (ii) Regulation (EU) No. 575/2013 of the European Parliament and of the Council of June 26, 2013 on prudential requirements for credit institutions and investment firms.

The new Law No. 202/2017 on Banks Activity, enacted on January 1, 2018, has imposed more stringent requirements on the local banks insofar as corporate governance, risk management and compliance is concerned, in line with Basel III requirements. In particular, banks shall revise their internal management framework and ensure the material risks are properly addressed and prevented.

The regulator, National Bank of Moldova (NBM), has the authority to issue and withdraw banking licences, as well as to regulate and supervise the banking sector. It tries to keep pace with and impose on the banks the best international standards.

To incorporate a bank in the Republic of Moldova (Moldova), the following steps shall be taken:

- Founders shall file with the NBM the licensing application, accompanied by corporate documents; disclosures on the identity, qualification and experience of the directors/key officers, the shareholders with significant equity interests (i.e., 1 percent or more) and their affiliates; financial disclosures; the bank's business plan etc. Shares shall be fully paid in cash, regardless if from own or borrowed funds. In case of bridge institutions the share capital can be paid in state issued securities.
- The NBM issues the preliminary approval of the application within five months.
- Founders shall pay in the capital (minimum capital is set at 100 million Moldovan lei, approx 5 million euros). The bank shall lease or purchase office premises and equipment, employ key personnel and retain an external auditor. If these requirements are not met within five months, the preliminary approval ceases.
- The NBM issues the banking licence within two months after all the above requirements are fulfilled. The license is issued for an unlimited term, for a fee of 50,000 Moldovan lei (approx 2,400 euros).

The branch of a foreign bank in Moldova is subject to similar licensing requirements, whereas a representative office can be opened only subject to NBM notification. The representative office is only allowed to carry out information and representation functions and also to defend the interests of the bank.

The acquisition of significant (one percent or more) equity interest in a Moldovan bank, either through initial or secondary offering, as well as increase of such equity interest higher than 5 percent, 10 percent, 20 percent, 33 percent and 50 percent are subject to the NBM prior clearance. Notably, after the August 2011 attempts of hostile takeover of shares in one Moldovan bank, this rule has significantly toughened. Now, the NBM clearance is required for: (i) acquisition of significant shareholding or increase thereof higher than the above thresholds through transactions or any other legal act, and/or (ii) share transfers based on court judgments or any transactions resulted therefrom.

The legal amendments (labelled as 'anti-raider law'), which provided the above novelties have been declared unconstitutional in December 2011 for procedural reasons, but were shortly (March 2012) replaced by a new law to the same effect.

To meaningfully build upon these developments, in March 2013, the Law on Financial Institutions (LFI) saw new amendments, purported to enhance the transparency equity investment in local banks and thus strengthen the capacity of the NBM to supervise the integrity of bank shareholders. As a result, the NBM shall be entitled to request from any direct or indirect shareholder (whether holding a significant share or not) any information necessary to carry out a prudential evaluation.

The 2013 amendments, which have been thereafter reflected in greater specificity in the new Law on Banks Activity, have also established clear criteria for the assessment of potential acquirers, with regard to their reputation, experience, integrity and financial soundness. These provisions are backed up by extensive disclosure requirements toward potential acquirers, including ultimate/ beneficiary ownership disclosure, accompanied by the legal prohibition for offshore entities to acquire significant equity interests in Moldovan banks.

Also, currently the NBM shall have capacity, for the purposes of assessing the potential acquirer, to inquire relevant authorities of other states. This is without a need of a formal agreement between the mentioned authorities.

After the 2014 banking crisis, when $1 billion faded away from three Moldovan banks, Moldovan banking and capital market regulators have made significant effort in ensuring proper transparency of shareholder structure and banks' risk management. In particular the special supervision regime was imposed by the NBM on other top three Moldovan banks (Moldova-Agroindbank, Moldindconbank and Victoriabank).

Noticeably, since then regulatory efforts in recent years have been directed to ensure the soundness and transparency of the Moldovan banking system — a purpose which has been partly achieved.

Legislation

Starting in June 2009, when the relevant amendments to the LFI were enacted, bank bankruptcies were exempt from the control of the courts of law, thus expediting the claims settlement procedure. Current bank liquidation procedure is conducted by an external administrator, appointed and supervised by the NBM. The administrator has to opt for one of the following alternative liquidation scenarios: (i) sale of bank to another licensed bank as going concern; (ii) partial transfer of assets and liabilities to another bank; or (ii) liquidations of assets. Notably, the scenario that was opted for in the case of the 2009 and 2012 bank bankruptcies was a combination of the last two legal scenarios, which ensured smooth settlement of individual claims but set aside the major liquidation burden.

In 2016 was enacted the Law No. 232/2016 on the recovery and resolution of banks, which is partially in line with Directive 2014/59/EU. This law sets forth the prevention, early intervention and restructuring mechanisms.

Prevention is applicable to banks in difficulties and means that both the bank and the national resolution authority, i.e., NBM, shall prepare a recovery plan. Both plans set out the actions to be taken in the event that the bank is to run into difficulties leading to its failure. Early intervention is applicable to banks in a difficult financial situation. In these cases, NBM has the power to intervene, such as by appointing a temporary administrator of the bank.

Resolution is applicable to failing banks. In these cases, NBM might apply the following resolution tools: the sale of business; the bridge institution; the asset separation and the bail-in.

One of the main principles underpinning the above mentioned law refers to the NBM powers to minimise the cost to taxpayers in case of continuance of the failing bank's downward spiral. In other words, the law indicates that the private sector is to bear the costs with precedence. When a bank collapses, shareholders are first in line to cover the restructuring costs. Also, the powers in the hands of the NBM include the possibility to sell the bank undergoing restructuring or merge it with another one. This 'bail-in' mechanism, which marks a change of tack compared to the public 'bail-out' tool – which was implemented by the Moldovan Government in relation to the 2014 banking crisis – has been applicable in Moldova since mid-fall 2016.

The mentioned law sets forth that NBM will create a national resolution fund to provide financial support for banks' restructuring plans. This resolution fund shall be financed in advance, including by the banks established in the territory of Moldova.

Also, in this context, as of March 2018 a new piece of legislation will enter into force. Passed through the Law No. 250/2017 on the Supplementary Supervision of Credit Institutions, Insurance Undertakings and Investment Firms in a Financial Conglomerate, the mechanisms introduced thereby provide a comprehensive set of rules on the prudential supervision of credit institutions, insurance undertakings and investment firms on a stand-alone basis and credit institutions, insurance undertakings and investment firms which are part of respectively a banking/investment firm group or an insurance group, i.e., groups with homogeneous financial activities.

This law refers to partially transposing the Directive 2002/87/EC. Note that as opposed to the mentioned Directive – EUR 6 billion – under the Moldovan law the threshold for the balance sheet total of the smallest financial sector in the group shall be MLD 500 million, approx. EUR 24 million.

In the beginning of 2017 has entered into force the Law No. 184/2016 on Financial Collateral Arrangements, which is partially in line with the Directive 2002/47/EC. This law was adopted (as per by the initiator of the draft – NBM) in a legal context providing for the harmonisation of national laws with the acquis communautaire. As a result of the enactment, the legal certainty with regard to the financial collateral arrangements was improved. Including to the end providing that certain provisions of the insolvency law shall not apply to the financial collateral arrangements.

Since the beginning of this decade, i.e., late 2010, a series of amendments were made to the LFI, and which were consequently as of January 2018 transposed in the Law on Banks Activity. The mentioned amendments pertain to the following:

• Legal regime of branches and representative offices has been clearly differentiated. Branches, as local business units, could incorporate smaller business units (agencies, exchange bureaus) located outside the branch office. Representative offices, in turn, shall be concerned with promotion and advertisement only.

• The NBM has been armed with additional intervention tools, such as "special supervision" and "special administration". Special supervision shall be imposed on a financially distressed bank and can last up to three months. A special supervising committee appointed by the NBM does not substitute the bank's management and, based on its conclusions; the NBM may institute the external administration or go directly to withdrawal of licence and bank liquidation.

The NBM can institute the special administration regime when a bank is in breach of certain prudential ratios, remedial measures or legal provisions. A special administrator is appointed by and reports solely to the NBM and he/she substitutes all the governing bodies of the bank. The NBM can declare payment memorandum, for a maximum of two months, when the risk of mass withdrawal of deposits exists.

• Learning from past lessons, the NBM has proposed to distinguish between remedial measures and sanctions and, in line with the World Bank/International Monetary Fund FSAP recommendations, has established a causal nexus between the gravities of breaches and sanctions.

• Additional know your customer, anti-money laundering and corporate governance requirements have been imposed on banks, with drastic sanctions for non-compliance.

• Liquidation remains out-of-court and bank liquidators were vested with additional powers. Employee claims, for three months before opening the liquidation proceeding, took priority over all other claims.

• The meaning of the term "banking secret" has been clearly defined, hence any information relating to the client, its assets, activity, transactions, personal or business relations are deemed to fall under banking secrecy rules. Banks have a duty to keep the banking secret and disclose confidential information only when expressly requested by law (e.g., at the request of fiscal authority, law enforcement bodies, courts of law) and following the prescribed clear-cut procedure.

2012 saw several new amendments to the LFI and other related laws purporting to simplify the mortgage enforcement process. The said amendments have become applicable as of March 14, 2013, and provide the following:

• A lender, (bank or non-banking financial institutions) can enforce the mortgage in extra-court proceedings, i.e., by having the mortgage agreement authorised for enforcement by a public notary.

• In turn, secured lenders would be bound by more extensive legal requirements toward pre-lending information disclosure (interest rates and all costs related to the loan, objective criteria for their modification, conditions and costs for early loan repayment, etc.)

Another block of amendments to the LFI, which have entered into force in April 2013, provide for the following:

• Entities from jurisdictions 'not implementing the international transparency standards' (the list has been approved by the NBM in May 2013) are prohibited to hold, directly or indirectly, any participation in banks' equity.

• NBM permission is required for acquisition of significant shareholding, to be obtained before acquisition by any means (not only by transactions), except for certain 'objective' cases, established by NBM regulations. In such cases permission shall be sought in 60 days after completion of acquisition.

• All shareholders agreements must be disclosed to NBM by their parties and the bank within five days after execution.

• Any shareholder with significant equity interest must inform the NBM on change of its beneficial owner, within 10 days. Sanctions against non-complying shareholder range from lifting the voting right up to forceful sale of shares held.

Civil procedure law has also been amended to the effect that courts are now entitled to rule forceful transfer of bank shares only if the right over such shares is the direct subject-matter of litigation.

Moreover, enforcement of a foreign court judgment, in this respect, shall only be authorised upon submission of either NBM permission to hold a significant share of bank equity or NBM permission to hold such share without preliminary approval. These amendments aim to prevent hostile takeovers through court (labelled in Moldova as 'raider attack'), when bank shareholders are deprived of shares as sanction for (often fake) debt non-payment.

Since 2013 the LFI has suffered periodic amendments, which have been partly reflected in the above mentioned new Law on Banks Activity. Apart from the already mentioned innovation for the Moldovan banks to implement the Basel III capital requirements, the novelties introduced by the new law aim, among others, at:

• Changing the rule-based supervision to the risk-based supervision and enhancing the NBM collaboration with the supervision authorities from different states.

• Introducing a wide pallet of rights and competences for the NBM especially in the supervisory review and evaluation process (SREP). The key purpose of introduced SREP being to provide that banks have adequate strategies, processes and mechanisms as well as capital and liquidity to ensure a sound management and coverage of the risks they are exposed to.

• Abolition of the audit (censor) commission, so that now, the mandatory bodies of a bank shall be the deliberative, supervision and executive one. Also, the new law limits the powers of the general shareholders meetings allegedly limiting the corporate democracy of the banks.

• Introducing the concept of independent members, which is not, however, explicitly regulated by the new law, but by the secondary legislation passed by NBM.

Non-banking financial institutions

Consolidated supervision of the non-banking financial sector has been strengthened under the National Commission for Financial Market (NCFM). The regulator has benefited from the extensive knowledge transfer supported by international donors, which enhanced the technical and institutional capacity of the NCFM.

The NCFM retains the authority to license, regulate and supervise the activity of "professional participants of the non-banking financial market", which includes capital market intermediaries, insurance market participants (insurers, reinsurers, insurance/reinsurance brokers and agents, and actuaries), private pension funds, investment funds, saving and lending associations, microfinance and mortgage lending organisations, and credit bureaus.

Legislation

The main evolutions in the financial market legislation can be summarised as follows:

• Enactment of the Law on Insurance, back in April 2007, has been followed by the revision of secondary insurance legislation pertaining to insurance intermediaries (brokers and agents), diversification of investments, creation of technical and other reserves, etc. As of April 2012, all insurers had to transform into joint stock companies and their minimum capital had to increase to MDL15 million (approx 790,000 euros) for non-life and to MDL 22.5 million (approx 1.18 million euros) for life insurance, whereas the life and non-life insurance businesses are to be split.

• The amendments to the Law on Insurance enacted in July 2012 and modified subsequently in 2016 have introduced the concept of "bancassurance", under which banks, savings and loan associations, microfinance institutions and leasing companies may be appointed corporate agents of an insurance company, provided they comply with the requirements set forth by the law (i.e., solvability, professional indemnity, personnel qualification). The 2012 amendments also (i) revised the corporate governance rules, (ii) clarified the relations between insurance companies and their external auditors, and (iii) introduced more extensive disclosure requirements to insurance companies.

• In March and July 2014, the Law on Consumer Credits and respectively the Law on the Distance Marketing of Consumer Financial Services, aimed at harmonising national legislation with Consumer Credit Directive (Directive 2008/48/EC) and Directive 2002/95/EC has entered into force. The envisaged harmonisation aims at regulating: the distance marketing of financial services; manner of calculation of the total cost of credit to consumer; standard information to be included in advertising; pre-contractual information to be also provided on a durable medium; information to be included in credit agreements; right of withdrawal within 14 days; linked credit agreements; database access; early repayment rules on calculation of the compensation due, etc. Although the harmonisation with the EU Directives is only partial, market participants still have a significant burden of reforming their practices.

• The draft Law on Voluntary Pension Funds which has been approved by the government in early February 2013, has proven futile after being withdrawn from the Parliament. Through it, NCFM aimed to develop a legal framework that would offer a viable alternative to the public pension system, a purpose which the, now in force, 1999 Law on Non-state Pension Funds has not been fit to achieve. Although Moldova has three private pension funds, which are indeed by far not used to their full potential, for unknown to us reasons, the Parliament did not adopt the Law on Voluntary Pension Funds. Nonetheless, 2013 has brought some restrictive regulation towards voluntary pension funds. They shall be subject to limited regulation through the Law on Capital Market, as they are deemed public interest entities.

• Another new draft Law on the National Commission for Financial Markets which has been drafted with the World Bank technical assistance has also proven futile. The mentioned draft new law primarily aimed to: (i) set clearly the supervisory objectives and powers; (ii) strengthen and guarantee operational and financial independence or supervisor; and (iii) ensure effective international cooperation, including within cross-border investigations and information sharing. These aims have been, in part, addressed in the new Law on Non-banking Credit Institutions (please below for details).

It is to be noted though that the 1998 Law on the National Commission for Financial Markets has been amended in 2015 to the effect that now eligible plaintiffs can not only challenge the Commission's decisions in court, but also request suspension of such decisions until a court judgment is issued.

• Enactment of the Law on Non-banking Credit Institutions, in spring 2018, has brought significant change to the non-banking financial market. Since under the old legislative frame NCFM did not have much supervision attributions, it has come with the initiative of building up to its – by then - monitoring powers only. Generally, the main objective of this new law is to uniform the regulation of all non-banking lenders, including microfinance organisations, leasing companies, mortgage and consumer loans providers. All market participants are wanted to comply with market entry conditions (minimum capital requirements, requirements towards administrators), including to obtain the NCFM approval prior to the market entry; corporate and financial data disclosure, including by instituting the Registry of the Non-banking Credit Institutions; internal control and risk management systems and procedures, including by providing for the mandatory audit of the non-banking credit institutions which assets exceeds MDL 25 million, approx. 1.2 million euros; non-banking secret and personal data confidentiality rules.

Also, it is to be noted that currently a draft law imposing a 0.1 percent regulatory fee – not greater than MDL 200,000, approx. 9,500 euros - on the non-banking credit institutions is pending approval in the parliament, even though this has been criticised to be contrary to the 2012 Guide to Regulation and Supervision of Microfinance, Consensus Guidelines (World Bank/Consultative Group to Assist Poor) and 2009 Leasing in Development, Guidelines for Emerging Economies (International Finance Corporation).

The "twin-peaks model" of financial prudential regulation and supervision introduced by the recent legislative evolutions is expected to usher thorough market reform. Although not yet proven in practice, the regulator displays confidence in the positive impact of the new-fangled legislation.

Capital market

Lately, the Moldovan government has been leading a dialogue with the private sector to identify and remove barriers to investment. Legislative and market-development efforts to facilitate and encourage financing in accordance with international best practices have been lately in "pole position" in Moldova. Awareness of these developments and understanding of the relevant legislation should help facilitate a complex range of transactions.

Legislation

Replacement of the old Law on Securities Market with the new Law on Capital Market brought substantial changes in the regulation of the capital market. The new Law, which has entered into effect on September 14, 2013, transposes the relevant nine EU Directives (on markets in financial instruments (MiFID), on takeover bids, on organisational requirements and operating conditions for investment firms, on the prospectus to be published when securities are publicly offered, on insider dealing and market manipulation etc).

The new Law regulates the business of investment firms, public offerings, takeover bids, capital market infrastructure (including regulated markets and information disclosure), and is designed to set and maintain high standards of capital market activities, raise the level of investors protection and offset systemic risks. The novel elements introduce:

• Abolition of supervision of the private share offerings, moving the focus to public offerings only. Public offerings are to be made only through investment companies and individuals authorized by the NCFM.

• Regulation of business of undertakings for collective investments in transferable securities, which are expected to emerge after mandatory liquidation of the investment funds set up in the early 1990s as privatisation vehicles. As per the new law, UCITS can be set up either as an "investment company" — legal entity which issues shares, or as an investment fund (without legal personality) which issues fund units.

• Extensive information disclosure, in line with Directive 2004/109/EC of the European Parliament and of the Council on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market.

• Permission to trade a broader variety of financial instruments (as opposed to the trading of securities only).

• Only JSCs meeting certain requirements are permitted to be listed on a stock exchange.

• Simplified registration for security issuance of privately-traded JSC.

• Abolition of the requirement of mandatory listing. The listing on a regulated market is to be authorised by the NCFM, provided that the issuer complies with the following requirements: (i) the publishing of a public offer prospectus; (ii) a capitalisation of 1 million euros; (iii) an equivalent of 200,000 euros of issued securities, all securities being transferable; (iv) a free float of at least 10 percent of securities belonging to the same class; etc. Listing requirements for MTFs are of a more basic nature.

• Best Execution Rule, allowing intermediaries to trade client securities at organized markets or OTC markets, substituting the Concentration Rule, requiring that investors trade securities only at a stock exchange.

After progressing at a slow pace, the enactment of the Law on the Central Securities Depository in 2016 has brought improvement to the corporate securities registration system. The new law has considered the provisions of the Regulation (EU) No. 909/2014 on improving securities settlement in the European Union and on central securities depositories. The mentioned law provides that:

• The Central Securities Depository shall have sound corporate governance and clear organisational structure. The NBM shall hold at least 76 percent of the shares in the capital of such Central Securities Depository.

• The independent registrars that keep the registers of securities for the currently registered 4,500 joint stock companies shall gradually – by the spring of 2020 – pass on to the Central Securities Depository the databases in their possession.

Despite the above legislative evolutions, market capitalisation still remains insignificant. Most notable transactions relate to strategic investors consolidating their shareholdings through mandatory or voluntary buy-outs. Risky investments into financial assets represent a minor part of the transactions on the Moldovan market; therefore, share prices are relatively immune to boom and bust cycles.

The gradual liberalisation of the financial market, combined with the appealing corporate tax regime (zero rate of corporate income tax has been replaced in 2012 with a low 12 percent tax and the dividend tax of 15 percent is subject to optimisation via the double-taxation avoidance treaties that were concluded between Moldova and more than 40 countries), stable currency and the strong commitment of the political elite toward EU accession have been creating sound prerequisites for transforming Moldova into a non-negligible investment destination in close proximity to the EU.

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