Mortgage Transactions Reform in Moldova

Assessment of the current Mortgage Lending Market
and
Recommendations on How the Market can be Further Stimulated

May 2005

Prepared for the European Bank for Reconstruction and Development
By
Progressive Banking Solutions Ltd
Dublin, Ireland

The report was prepared with the generous funding of the Swiss Secretariat for Economic Affairs
## CONTENTS

1. Introduction ........................................... 3
2. Executive Summary .................................... 6
3. Acknowledgements .................................... 8
4. Methodology ........................................... 9
5. Report .................................................. 10
5.1 The Housing Market .................................. 10
5.2 Legal & Regulatory Environment ...................... 13
5.3 The Banking System .................................. 16
5.4 Government Policies, Ministries and Agencies ............. 21
5.5 National Bank of Moldova ............................. 25
5.6 International Financial Institutions ..................... 26
5.7 Services Supporting Home Ownership ..................... 27
5.8 Consumer Rights and Protection ......................... 29
5.9 Stock Exchange and Secondary Mortgage Markets ............ 30
6. Conclusions and Recommendations ........................ 31
7. Appendices ............................................. 36
   • Analysis of Minimum Standards for Mortgage Lending Questionnaires
   • Asset & Liability Management
   • EU information requirements for Mortgage Customers
   • Legal and Regulatory environment
1. INTRODUCTION

The Government of Moldova (‘the GoM’) has made the need for the development of a vibrant real estate and mortgage lending market in Moldova one of its top priorities. This is borne out by the chapter on Private Sector Development outlined in the Economic Growth and Poverty Reduction Strategy Paper for 2004 - 2006 approved by the GoM.

In furtherance of this strategy the GoM, through the offices of the Prime Minister and the Ministry of the Economy, has sought the assistance of the European Bank for Reconstruction and Development (EBRD) with this important undertaking.

This assessment is undertaken therefore to establish the current status of the market in Moldova with the main emphasis being on the residential sector. The following summarises the Terms of Reference:

- Review existing Laws and Regulations on Mortgage transactions.
- Assess current policies and procedures of lenders against the EBRD Minimum Standards for Mortgage Lending and EBRD Core Principals of Secured Lending.
- Evaluate the current size and development potential of the Mortgage and Housing markets.
- Review various related initiatives being undertaken by other International Financial Institutions (IFI’s).
- Develop and present a draft report which outlines the findings, conclusions and recommendations from the above research.
- If required to be available to the GoM to assist in the articulation of a strategy to address identified deficiencies and develop an action plan to implement the strategy.

The Benefits of Home Mortgage Finance

The beneficiaries:
In all developed economies the availability of long term mortgage finance is taken for granted by the citizens. It enables the average citizen to become the owner of a property or to ‘trade up’ while initially contributing only a small portion of the total cost provided they make the mortgage repayments as they fall due. In addition, if the property increases in value (as most do) they obtain this benefit as well.

Financial institutions are in a unique position to enable people to achieve the dream of home ownership. In many countries mortgages are available for up to 35 years and indeed are made available over two generations in a few countries.

The lenders:
The main benefits for financial institutions are:

- Return on Investment
  Depending on the term the total return can be up to 100% of the original amount borrowed.
Safe Lending
Compared to other types of lending mortgages are safer. Experience has shown that customers will pay the mortgage before other loans in order to ‘keep the roof over their head’.

Business Opportunity
Providing a mortgage to a customer is the start of a long term business relationship. Customers tend to take other products such as insurance, car loans, improvement loans from their mortgage provider. It also opens up opportunities to build relationships with the extended family and the next generation.

Home Mortgages are the bedrock on which many successful banking relationships are formed. As well as being a safe and profitable product for Banks there is the added social satisfaction of helping people to own their homes.

The economy and society
Governments, as a part of their social policy, have a responsibility to be pro-active in implementing a range of measures to assist home ownership. This in turn will increase economic activity in the construction and allied industries leading to increased employment and increased taxation.

The pre-requisites:
There are a number of pre-requisites for the functioning of a successful housing finance system:

- Sound macro-economic policies are more effective than complicated tax incentives or subsidies because they deliver stable and low interest rates.
- Keep transaction costs low and property and mortgage registration systems efficient to enable borrowers to re-mortgage.
- Concentrate on getting the ‘primary market’ right (e.g. transparent property rights, mortgage and credit registration, well defined underwriting and affordability criteria, efficient mortgage collateral and foreclosure procedures etc) before creating a ‘secondary market’ to finance these loans.
- Create transparent markets for lenders through approved property valuation methods, house price indices, credit bureau and data on the mortgage industry.
- Protect, inform and educate borrowers by helping them to compare mortgage products.
- Create standardised AAA rated funding instruments (mortgage covered bonds/mortgage backed securities) in order to source capital and reduce funding costs.

(Source: World Bank/Council of Europe Development Bank)

The authors, under the direction of EBRD, were Rory Spain and Desmond Smyth.

Rory Spain is a career banker with 40 years commercial banking experience. For the 15 years prior to his retirement Rory had been involved almost exclusively in the development of the Bank of Ireland Mortgage business. He has been responsible for the design, development and implementation of a mortgage system
within Bank of Ireland; the review of existing legislation and procedures in Northern Ireland prior to setting up the mortgage business there; managed the research and development of a securitisation programme; appointment and training of a front line mortgage sales team. In addition he has been responsible for the development of a specialist qualification in Mortgage Lending on behalf of the Institute of Bankers in Ireland and University College Dublin and he continues to be the external examiner for the programme. The qualification is now held by over 3000 financial services staff. Rory also has undertaken numerous mortgage assignments in overseas markets including South Eastern Europe (SEE).

Des Smyth also has 40 years commercial banking experience. His career has been primarily in International Banking and in 1990 he set up Bank of Ireland International Services Ltd and became its Managing Director. Under his leadership the division undertook more than 200 technical assistance projects in 55 countries around the world including many in emerging economies in Europe. Des has substantial experience of working in SEE countries.

Both authors are from Ireland and are of an age to remember what conditions were like in Ireland between the 1950’s and the 1980’s. They remember when:

- The population was 3.5 million.
- There was mass emigration and the economy was partially sustained by emigrant’s remittances.
- Ireland was a nation with little manufacturing industry and small uneconomic farms accounted for 70% of employment.
- High taxes were the order of the day and substantial efforts were made by the citizens to avoid these taxes.
- Mortgage lending was confined to Building Societies and citizens had to save for up to 3 years before they could apply for a mortgage - and indeed they had to queue to obtain the application form.
- Banks did not lend long term as they were unable to match short-term deposits with long term loans.
- Ireland was christened ‘the poor boy of the rich men’s club’ by the Economist on joining the then EEC.
- Government policy changed to provide further support to education, reduce taxation levels, reduce interest rates and incentivise entrepreneurship and attract foreign investment to create alternative employment.
- EU funding and further reduced interest rates enabled our economy to enter a period of sustained growth.

There are distinct similarities between Moldova of today and Ireland of the 1950’s/1980’s.

In preparing this assessment, a substantial amount of desk reading has been undertaken which reviewed previous and current research projects on housing and mortgages in Moldova. In addition to the desk research a large number of face to face meetings have taken place with key policy makers and market influencers. (See Acknowledgements- section 3).

The authors did not have an opportunity to visit locations outside of Chisinau so the report is based totally on findings in the capital. In addition while the meetings were most informative it should be understood that within the timeframe there was no opportunity to carry out in depth analysis into any specific area.
The development of the report has been helped enormously by staff in EBRD offices in London and Chisinau and we thank them for their support.

Our particular gratitude goes to the Operation Leader Frederique Dahan and Alex Tanase Senior Banker in London together with Francis Delaey Head of Office in Chisinau and his colleagues Larisa Manastirli, Octavian Costas and Michelle Sculin.

2. EXECUTIVE SUMMARY

The Government of Moldova (GoM) has made the need for the development of a vibrant real estate market and mortgage lending market in Moldova one of its top priorities in the coming years. In 2004 the GoM sought the assistance of the European Bank for Reconstruction and Development (EBRD) to carry out an assessment of the current mortgage market and to recommend how the market might be further stimulated. In particular, it was suggested that the legal framework for taking mortgages was inadequate and a new mortgage law was required. The EBRD and the Ministry of the Economy, counterpart of the project, agreed it was essential to undertake first an assessment of the current housing finance market to precisely define the relevant strengths and weaknesses and present the GoM with a set of recommendations. The following sections summarise the key findings, conclusions and recommendations of the assessment.

- The housing market (particularly in Chisinau and surrounding areas) is in a period of growth. The phase of ‘renovating and completing unfinished buildings’ left after the fall of the Soviet Union is drawing to a close. The future of the market will be in the development of ‘green field’ sites in addition to the growing ‘second hand’ market. Prices have escalated over the last few years but informed commentators are predicting a slowing down in price escalation as supply and demand approach equilibrium. This growth in the market requires that supporting pillars such as the law(s), financial system and other services are adequate to underpin and further enable the growth.

- The legislation supporting home ownership and mortgage lending has been developed on a piecemeal basis as market conditions required. Our research has established that there are many contradictions between older and newer laws leading to a clear lack of confidence amongst market participants in the ‘laws’. These contradictions are outlined in Section 5.2. The lack of confidence is both a perceptual and a real barrier to economic development.

- The growth in the housing market has largely occurred without the support of the banking system. The Banks, at present, provide little input or support (max 1% of banks total lending) to this key ‘personal’ sector of the economy. Banks state they are unable to lend long term as their deposits are either on demand or short term fixed. This is an issue lenders worldwide have faced and have overcome.

Based on our research the number of people in the house formation population (assume 50% of total population) who could afford a mortgage ranges from 100,000 (conservative) to 300,000 (optimistic). This in turn would lead to a mortgage market ranging from $1.38 billion to $6.21 billion over a 5 to 10 year period (calculations in 5.3 The Banking System).
Our view is that the conservative end of the scale is more realistic. The profit level in Moldovan Banks is high compared to International/CIS levels. While the Banks state they plan to enter the mortgage market more aggressively there is a suspicion that there is no great incentive to do so based on current profit levels. If the Banks are to enter the mortgage market there will be a need to introduce a set of recognised international lending standards and this can be achieved by using the ‘Minimum Standards for Mortgage Lending’ as developed by EBRD.

National Bank of Moldova state that the current level of Capital Adequacy in the Banks is in the order of 30% while the Basel requirement is 8% for standard loans and 2.8% for mortgage loans. NBM also states that there is 1 billion lei surplus available for lending. In addition it is the policy of the Ministry of the Economy to encourage ‘freeing up’ surplus bank funds into the housing market.

- While there is substantial growth in the housing market this growth is being restricted by the high level of deposit required to obtain a home. This deposit is in the order of 50% of the total price and it means that consumers (sometimes with little or no legal protection) are providing working capital to developers (including the Government agencies NHA and AMIC). The lending term is also very short ranging from 18 months to 5 years. Exceptionally this extends to 10 years with AMIC although AMIC is not a true mortgage lender based on international definitions of mortgage lending.

- In general consumers are poorly protected by the laws particularly in relation to ‘in course of construction’ properties.

- Unofficial lenders have begun to surface in the housing market. This development is a mix of ‘seeing the opportunity’ and a level of frustration with the lack of support from the Banks. This, if unresolved, will create serious difficulties for properly functioning financial and economic markets.

- Given the low level of mortgage lending the Banks and other supporting institutions are at present unprepared for the development and introduction of Mortgage Bonds or Mortgage Backed Securities. The level of investment funds is low.

- There is a pent up demand for new and better housing but there is a lack of knowledge and understanding amongst the citizens of Moldova of the process and benefits of mortgage lending as an enabler of home ownership. As a result there is a ‘fear of the unknown’. There is a need to implement an information and education campaign to overcome this fear and lack of knowledge.

- A number of ‘other important’ conclusions and recommendations are contained in Chapter 6 and readers are encouraged to read these also.
Key Recommendations

1. Put in place a project to develop a new law to support home ownership and mortgage lending. The law should address some of the issues highlighted in section 5.2 and also incorporate the requirements of the Secondary Market. Source documents to examine: existing Moldovan laws; draft Moldovan Mortgage law; Ukrainian Mortgage law; Romanian Mortgage law; this report; and the requirements of EU legislation.

2. Provide a ‘10 year Mortgage Credit Line’ to specific Bank(s) (who will be aggressive in the market) at favourable rates (supported by GoM subsidies) to be repaid initially from cashflow and subsequently from the issue of Mortgage Securities. This line of credit to be conditional on the implementation of EBRD Minimum Standards for Mortgage Lending. The mortgage credit line will be accompanied by technical assistance for the specific bank.

   and/or

   Set up a Mortgage Bank on the lines of Domenia Credit in Romania (part EBRD funded) or International Mortgage Programme (IMP) in the Ukraine (WNISEF funded) subject to ‘Minimum Standards’ as above and technical assistance.

3. Reduce ‘consumers’ deposit to 25% of the purchase price of a home. This reduction in addition to a longer loan term (10 years or more) will encourage investment by citizens in the housing market and make it more affordable for middle-income house buyers.

4. Provide Banking or lending licences to unofficial lenders or implement a review to exclude them from the market.

5. Develop and implement a public awareness and education campaign to help citizens understand the benefits of mortgage lending as an enabler of home ownership.

Success of these recommendations depends on an assertive and pro-active ownership approach by the Government in furtherance of its strategic policy to create a vibrant housing and mortgage market for the citizens of Moldova.

3. ACKNOWLEDGEMENTS

During our visit to Chisinau we met a wide range of senior policy makers and leaders of services associated with the ‘mortgage and housing markets’. We gratefully acknowledge the time given to us and their contribution to this assessment. The meetings took place in the following order:

- EBRD - Mr Francis Delaey & Colleagues.
- Ministry of the Economy - Mr Vasile Mamaliga, First Deputy Minister of Economy & Colleagues
- Agroindbank - Ms Natalie Vrabie, President.
- Moldindconbank - Mr Victor Cibotaru, Chairman & Colleagues.
- Mobiasbank - Mr Serghei Cartashov, First Deputy Chairman & Colleagues.
- Mr Marian Lupu - former Minister of Economy.
- Victoriabank - Mr Victor Turcanu, President & Colleagues.
- Ministry for Finance - Mr Gheorghe Cojocari, Deputy Minister & Colleagues.
- Mr Alexander Turcan, Attorney at Law, Turcan & Turcan.
- Banca de Economii - Mr Corneliu Ghimpu, Head of Credit Dept.
In addition to the meetings the opportunity has been taken to read previous and current research reports on the housing markets in Moldova. In particular we would like to acknowledge the following which were made available to us: World Bank - PADCO Europe Ltd Report (July 1997), The Moldova Investment Climate Assessment (World Bank May 2004); Government of Moldova Policy and Strategy papers; Council of Europe/World Bank Report (Paris 2003); USAID/PFAP Housing Paper (December 2004).

We want to particularly acknowledge the assistance of Lara Estate Agency who have made available to us their Report on the Housing Markets in Moldova which was published in December 2004. They also have given us permission to quote from the report.

Finally we want to gratefully acknowledge and thank Roger Gladei, Counsel, for his detailed work in assessing the current legal and regulatory environment in Moldova and for his recommendations on how Moldovan laws can be improved to establish an attractive framework for mortgage based financing. His evaluation is contained in Appendix 4 and summarised in Section 5.2 as part of the legal review.

4. METHODOLOGY

In order to establish the widest possible information base to carry out the assessment we decided to seek the assistance of relevant Government Ministries, National Bank of Moldova and representatives of the Banking, Insurance, Legal, Real Estate and Construction industries as well as meeting representatives of the Land Cadastre, Notaries, National Housing Agency, AMIC and the International Financial Institutions.

A checklist of questions and areas was developed and circulated in advance to the relevant people for each meeting in order to ensure that the meetings were as productive as possible for all participants.

In addition the key standards from the EBRD ‘Minimum Standards for Mortgage Lending’ Manual were circulated in advance to the Banks.
5. REPORT

5.1 The Housing Market

This section of the report is informed by reading, meetings and specific meetings with Real Estate Companies and a Construction business.

Background

The privatisation policy of the GoM has enabled many citizens and families to become owners of their land and homes. Under this programme approx 1 million properties have been privatised since 1992. This policy has created a society which to large extent now owns their properties free of debt, are asset rich and with an ability to use these assets to either improve their existing housing or acquire better housing in the future. Since 2000 there has been an economic recovery with cumulative growth of more than 20%. This growth has been driven largely by consumer spending fuelled by increase in real wages and sizable inflows of emigrants remittances which have benefited the services, housing and construction sectors.

Housing Demand Supply and Prices

There has been strong and sustained demand for housing in Chisinau with somewhat lower levels of demand in other cities and towns.

*Those most closely involved with housing and construction have provided us with somewhat different views on demand supply and the pace of price increase. This in itself is an indication of a fast moving industry.*

In the period 1999-2003 for example 533,000 property transactions were registered while in the period Jan-May 2004 the figure was 73,000 which was 17% of the total for the previous 4 years. Market indications are that this frenetic pace is moderating and that supply is moving to meet demand.

However having said that there is consensus that there is currently a shortfall of approx 45,000 housing units to meet demand in Chisinau.

Apartments have accounted for the vast majority of property transactions in Chisinau. Demand levels are as follows: Studio 17% (36 sq mtrs), 1 Bed 27% (46 sq mtrs), 2 Bed 46% (69 sq mtrs), and 3 Bed 10% (108 sq mtrs).

Prices have increased rapidly - for example in the range of 35% - 40% between 2003 and 2004. A number of people stated that prices are beginning to stabilize. The LARA report published in December 2004 indicated that average purchase price per sq mtr for a new apartment is in the range $400-$559 while the price for ‘second hand’ apartments is in the range $380 -$450. However at a housing conference in Chisinau in February 2005 it was stated that because of soaring land prices that the purchase price may increase to the order of $850/$890 per sq mtr during this year.

Stand alone/single dwelling houses account for a small portion of the total market. Demand for houses up to 100 sq mtrs @ $350 sq mtr is stable while demand for larger villa type houses is sluggish.
Site Acquisition

As has been said land prices are increasing rapidly.

City authorities control the distribution of municipal sites and unfinished blocks.

In order to reduce acquisition costs of these sites some construction companies initially rent or lease the site and when the construction is finished they complete the purchase. While there was no precise explanation given for this approach the understanding is that ‘city fathers’ wish to ensure that the land is used for the specified purpose and will sell it at a cheaper price following construction.

Construction companies in general prefer to acquire ‘greenfield’ sites from private owners rather than municipal sites (despite the higher costs).

Property Appraisals

Appraisals/Valuations are carried out by certified specialists who are licensed by the National Agency for the Cadastre. They are licensed following successful completion of relevant exams.

A comprehensive evaluation form is completed which gives details of the property, its location, the services etc and 3 ‘values’ re-construction cost/market value/liquidation value.

For newly constructed houses quality of construction as well as health and safety requirements are regulated. The Municipal Inspectorate has the final sign off.

This process appears to work well but there is a need to improve the legal environment for real estate/valuation companies in addition to introducing Professional Indemnity Insurance. In addition there is no reference to ‘insurable value’ in the report. The ‘reconstruction cost’ should be used for this purpose.

Non Bank Lenders

Due to a level of frustration with the support provided by the Banks (who interviewees say are too expensive and the term is too short) to the development of the housing market one of the parties we met is now providing loans directly to potential purchasers. These loans are provided for a 5 year period and the title is not transferred until the repayments are complete. The customer has no real title during that period.

There is also a level of frustration with the lack of working capital support from the Banks.

Future Potential

All parties concur that there is good future potential in the housing market.

The main potential is in the development of new apartments with continuing potential in the sale of second hand properties. Most of the ‘unfinished buildings’ are now complete and potential in this sector, other than resales will tail off.
The rate of development of ‘new’ buildings is increasing - having increased from 10% in 2003 to 12.5% in 2004.

Lara Estate Agency breaks the potential purchaser/borrower market as follows:

- Cash buyers or people getting short term loans > 1 year and who can pay 50% deposit 15%
- People who need to save over 1/3 years to accumulate the 50% deposit and who can repay a mortgage over a further 1/3 years. 15%
- People with stable income who could save 50% within 3/5 years and pay off a mortgage over a further 10 years. 25%
- People who could save the 50% deposit over 5/10 years and who could pay the mortgage over a further 15 years. 35%
- People unable to get into the private sector and who need state support. 10%

*The Lara model is based on a 50% deposit. The potential could increase exponentially if the deposit were reduced to 25% (i.e. a 75% loan to value ratio). In this respect see also the mortgage potential calculation under Section 5.3.*

**Issues**

The funding and rights of ownership to ‘in Course of Construction Apartments’ was raised by all parties. This is principally an issue of ‘Consumer Protection’ and it is addressed in more detail in Section 5.8.

The current state and sustainability of the metal framed/panel apartment blocks and the apartments situated over the mines in Riskani are a cause of major and immediate concern and must be addressed in the overall housing policy as the potential cost of refurbishment and/or re-housing is massive.

Obtaining planning/building permits is a bureaucratic obstacle course and can take up to 170 days.

Both reports read and meetings attended indicate that firms have to pay bribes to officials in order to obtain planning permission.

There is a big issue with correct property valuations. The Cadastre has the responsibility for valuing property for tax purposes. There is a view that these valuations are incorrect (a) because buyers/sellers understate the value of the property and (b) because the Cadastre uses the normative rather than the market value of the property. In all situations there is a loss of revenue to the State.

The current process for registering purchases/title/mortgages is as follows:

- Buyer registers the purchase/sale agreement with the Notary
- Buyer registers the agreement with the Cadastre
- On completion of the above the buyer then gets the loan from the lender but the lender will not allow drawdown until the mortgage is registered.
The issue is that sellers do not want to part with their property under these conditions.

The lender will not provide a mortgage until they can get a charge over the property but the customer cannot get a title to the property until they pay 100% of the cost. There is a ‘gap’ where in theory the seller is at risk and this can be overcome by introducing simultaneous transactions - see findings re Lawyers undertakings.

Findings

- Demand Supply and Prices have risen substantially in the last 3 years.
- Prices are continuing to rise but informed commentators say they are levelling off as supply and demand move towards equilibrium.
- There is good potential for the housing market in the medium term and the potential is principally in the sale of new apartments and the re-sale of second hand units. This potential would increase if the current deposit levels of 50% were reduced to 25%.
- Non Bankers are providing loans to would be purchasers. This can be seen as a frustration with and a reflection of the passive approach of the Banks. Expect this to increase which will lead to a lack of structure in the market and is dangerous as they are unlicensed.
- There is a need to improve the legal environment and to introduce Professional Indemnity Insurance to the Real Estate/Valuation companies.
- The planning process is surrounded by bureaucracy and a level of corruption.
- The State is losing an undefined amount of revenue due to the inefficient valuation methods in use by the Cadastre.
- There is a ‘gap’ in the buying/selling/mortgaging process which is hindering people who do not own a property or can pay 100% of the cost from entering the market. There needs to be simultaneous registering of the sale, the purchase and the mortgage. A system similar to Lawyers or Notaries Undertakings could solve this.

5.2 Legal and Regulatory Environment

The legal framework regulating mortgage transactions and related rights is currently made of a number of legislative and normative provisions scattered between several acts and regulations. The legislation supporting home ownership, housing building and mortgage lending has been developed on a piecemeal basis as market conditions required and is still very patchy. Our research shows that there are many contradictions between the various laws and many areas of uncertainty leading to a clear lack of confidence amongst market participants. There are a number of reasons for this:
1) Many provisions are unclear, or conflicting each other and market players unanimously expressed a desire for a thorough consolidation of the relevant provisions. Moreover, some areas such as mortgage bonds and mortgage securities need to be addressed for the first time in detail.

2) Practical difficulties have emerged which make the taking of mortgage difficult or cumbersome, which would need addressing.

3) Many laws contain direct or indirect disincentives for the development of mortgage market at all levels (consumer protection, housing building, tax regime, banking supervision, etc) and the market is clearly calling for a concerted effort on the part of the government to positively review these numerous regulations or laws and adopt a comprehensive package which would unambiguously encourage the development of the market.

It should not be overlooked that Moldova is a relatively immature jurisdiction as far as commercial law is concerned and that it suffers from the flaws commonly found in other neighbouring jurisdictions, namely a set of new and untested commercial laws, often lacking co-ordination or rationalisation, a judiciary having real difficulties coping with the quick changes in the laws and market practice together with an endemic problem of corruption, and institutions not fully suited to apply and support key commercial players. It is thus not surprising to find these problems arising in the specific context of mortgage finance.

In addition to this section of the report an assessment of the issues surrounding individual laws has been undertaken and this is included in Appendix 4.

The most important provisions governing mortgage rights are found in the Pledge Law No. 449-XV dated 30 July 2001 and the Civil Code (Book II, Title IV, Chapter V - Articles 454 to 495). These provisions, which are fairly similar in content, govern the parties to the mortgage (the mortgagee and mortgagor), the mortgaged property, the creation and perfection of a mortgage, the legal effects of mortgage, both between the parties and against third parties, and the mortgage enforcement.

The main institution involved is the Immovable Property Cadastre, governed by the Immovable Property Cadastre Law No. 1543-XIII dated 25 February 1998. The Law has established a general uniform system of identification, registration and monitoring of all land plots and other immovable property, regardless of their use and owner (either national or foreign citizens, legal entities, international organizations, administrative-territorial units, the Republic of Moldova or other states). All immovable property, property rights and other patrimonial rights (including economic management, permanent use, leases for more than three years, freehold, fiduciary administration, servitude and mortgage) are subject to compulsory registration with the Registry of Immovable Property. The State Agency for Land Relations and Cadastre is the coordinating and supervisory body, and territorial cadastral offices are in charge of establishing and managing the Registry of Immovable Property. The Cadastre is open to the public and anyone may access its records.

Although the legal community generally describe the legal provisions as ‘adequate’ and also acknowledge that a lot of work has been done in improving the functioning of the Cadastre, a number of problems are noted:

- the taking of a mortgage over an unfinished construction (or part thereof): it is currently not possible to register a mortgage in the Land Register over an unfinished immovable asset, and when banks succeed to have it registered, they express serious doubt as to the validity of such security;
• the simultaneous registration of both title of ownership and mortgage in the case of purchase financed by a loan secured by a mortgage;

• there is some uncertainty on the protection that the mortgagee may receive when actions are undertaken against the property (e.g. expropriation, avoidance of title, action for recovery (vindicatio), confiscation);

• the procedure of mortgage enforcement is currently confusing because of sometimes contradictory rules between the Pledge Law and the Civil Procedure Code (No. 225-XV dated 30 May 2003), and the regulations on enforcement of court judgements of the 1964 Civil Procedure Code. Generally, the parties should be able to agree on the mode of enforcement and compulsory judicial procedure should apply only in limited cases (for example, the property is occupied by children, old or disabled individuals). Yet, there is some uncertainty on many details in this procedure (including the rights of the purchaser on enforcement, the forced dispossession of the owner and the eviction of occupied apartments);

• the case of multiple (subsequent) mortgages is not properly addressed, especially enforcement;

• no provisions have been provided for the issuing of mortgage bonds and mortgage securities in the context of the development of a mortgage secondary market and related institutions.

A number of separate but related issues were also mentioned during the course of the interviews:

• problem of valuation of the property;

• documentation that is required in order to register title in the Cadastre, in particular the production of a tax certificate on the absence of tax arrears (which can be difficult to obtain).

Other difficulties, which do not directly relate to mortgage finance per se, but which create associated problems, stem from the regime applicable to immovable property. For example, it was noted that the lease of state-owned property is not precisely regulated and does not offer adequate protection to both tenants and the State. A lot of controversy also stems from the sale of state-owned land for the purposes of erecting a new construction and the way the tariffs on the sale price are being fixed.

Generally, a good deal of review and amendments would need to be done in the area of housing (dwelling) building as this also indirectly affects the feasibility and development of mortgage finance, although it is felt that this would probably go beyond the scope of any subsequent projects to this assignment.

Finally, one should note that the provisions relative to consumer protection could valuably be developed to cover in more details mortgage finance, along the lines of the European Code of Conduct for Mortgage Lenders. Moreover, there are some serious problems in relation to the protection of the participants to the construction of an apartment building. There is no law (nor a chapter in the Civil Code) that regulate the construction of a dwelling with the financial contribution of the future owners of the premises (laws on the subject have been passed in

1 Pursuant to Article 2 of Law on the Entry into Force of the Moldovan Civil Procedure Code No. 227-XV dated 5 June 2003, the Civil Procedure Code dated 26 December 1964 has been repealed, save for regulations pertaining to enforcement of court judgements. Those regulations will be substituted by the ones set by the new Execution Code, which came into force on July 1, 2005.
Ukraine in 2004 and the Russian Federation early 2005). There is no statutory obligation of the contractor to disclose information on its activity and how the construction project is implemented. The purchaser is completely unprotected and has no legal recourse in the case where legal action should be taken against the contractor.

Finally, it seems that the National Bank regulations on provisioning and reporting does not provide any specific rules on mortgage lending, which could provide an incentive for banks to develop this segment of the business. It is also not fully clear which institutions are legally entitled to grant mortgage finance.

To summarise, the lack of confidence in the legal framework is both a perceptual and a real barrier to economic development. Clearly a new law’s role would be to regulate much more precisely the subject, to address a number of small but important issues, and generally build the potential users confidence in the system. However, as an influential policy adviser put it and as we demonstrate in the rest of the report, “it would be a mistake to concentrate all efforts on legal framework development solely (...) experience shows that laws alone have a rather insignificant influence on the entrepreneurial activity.”

5.3 The Banking System

During the course of our visit we met with senior executives from the five biggest Banks and they provided us with the following view of the markets. Four of these Banks provide residential mortgages.

General

- The term of the mortgages range from 2 to 5 years with 5 years being exceptional. All Banks stated that they want to lend for longer terms but have difficulty matching the maturity gap between short-term deposits and long term loans.

- The Banks take a first legal charge over the property and this is registered in the Cadastre. However there was consensus that the documentation issued by the Cadastre was not 100% reliable and this view was reinforced during later meetings particularly with the Notaries representative.

- The gross profit margin on residential mortgage lending is in the order of 7%.

- Loan to Value Ratios (LTV) are in the range of 40% - 70% and would be seen as conservative by international standards.

- The standard ‘mortgage’ model in use at present is that the Customer saves/provides up to 50% of the total cost of the property and the Bank loans the balance to be repaid over a period of approx 3 years. Only people with large resources/incomes can afford to provide these up front deposits and to repay over such a short term.

- Residential mortgage lending at present represents a very small percentage of the total lending portfolio. Not all Banks have designated residential
mortgages as a separate product but the general estimate given is in the range of 1% /2% of total lending.

- IFI Lines of Credit are available to some lenders but these are rarely used for residential mortgage lending as they are considered to be too expensive due to the poor investment rating of Moldova. The vast majority of residential mortgage lending is from core deposits.

- Most Banks provide mortgages/building finance to enable construction companies to develop new apartments/housing. This lending is on a much larger scale than residential mortgage lending.

- Emigrants remittances play a major role at present in the Moldovan housing market. This activity is fuelling increase in demand with consequent rise in prices. Banks state that while loans are provided to local people in lei a high percentage of the repayments are funded by Moldovans working outside the country.

- At present much of the activity in apartment purchases is funded from savings and other cash sources - in effect the major activity in the housing market is happening outside of the banking system. Banks are reluctant to take apartments as security due to legal issues over foreclosure and the social issues arising from eviction.

- Affordability is seen as a key issue. The average monthly income is $100. However estimates vary on the percentage of additional earnings from the ‘grey economy’. These range from 40% to 70%. There is a difficulty in accurately verifying income. Debt Service Ratio (DSR) levels range from 40% to 50% of net family disposable income. The bank’s target market is initially the wealthy segment followed by the middle-income segment. The size of this market is in the range of 3%/4% to 15% of the house formation population. One of the interviewees stated ‘People who can afford our loans don’t need them while the people who need them can’t afford them’.

- National Bank of Moldova (NBM) does not allow loans in foreign currency and the banks feel that this restriction is adversely affecting their ability to grow their business. This issue was also raised by a number of other interviewees.

- Fiscal incentives are available although there is a level of confusion as to what they are and how they can be claimed. VAT refunds are available on construction materials and income tax reductions/exemptions are available to banks when they lend to legal persons for longer than 2 years.

- All five Banks stated that they wish to develop the mortgage product in the future. Most see it as having strategic importance to the development of their business. Some have specific projects in mind for 2005. The principal barriers to development are seen as: difficulties with the existing legislation, validity of the collateral, need for long term funding, reliability of financial information and affordability (see issues below).
None of the Banks have yet commenced preparations for the sale of mortgages to the secondary markets. However they are conscious of the need and benefit of this mechanism and all stated they would want to use Mortgage Bonds or Mortgage Backed Securities in the future.

**Mortgage Lending Standards**

EBRD has developed a set of ‘Core Principles for Secured Lending’ together with ‘Minimum Standards for Mortgage Lending’. The Banks completed questionnaires to establish the degree of conformity to these principles and standards. We did not have an opportunity to carry out a due diligence.

In general the banks meet most of the requirements of the core principles.

The key minimum standards for mortgage lending are covered under the following 10 headings:

- Mortgage Process, Procedures and Organisational Structure
- Mortgage Documentation
- Business Operations/checks and controls
- Property Valuations
- Property Ownership - type/registration of title
- Insurances
- Credit and Risk Management
- Lending Criteria
- Security Requirements
- Account Management/Management Information/Information Technology.

The completed questionnaires indicate a good level of prudence and conservatism in mortgage lending (see Appendix 1). The Banks in general use their standard loan process and procedures when assessing mortgages. Arrears management and Loan Loss Provisioning standards are in place. Indeed the level of risk taken is low by Western standards and the return on investment is high. However this in turn has the effect of stifling demand.

The Banks have not yet developed specific standards for mortgage lending. This is understandable based on their very small exposure at present to residential mortgage lending. However if they intend to grow their ‘mortgage books’ as stated, then a specific set of standards is required to manage this product. These standards are available from EBRD. Therefore under the above 10 headings there was a wide variation of answers. (See: Appendix 1)

The most obvious deviation at present is in relation to Life Assurance and Buildings Insurance. These are required under the minimum standards and under benchmark pool standards issued by International Rating Agencies. While these are available in the market in Moldova most lenders do not require them at present. Some banks are planning to change their policy in this regard.

Under the existing Pledge Law (Chapter 3 Art 9) there is a requirement for Insurance.
Issues

The following legal and operational issues were raised consistently by the Lenders:

A range of laws have been enacted over the years. There are inconsistencies between them. The Pledge Law is a foundation but not comprehensive. In general it has been difficult to tie down what exactly is the problem other than there is a general lack of confidence in the level of security offered by the current legal structure relating to housing and mortgages and a demand for the development of a specific Mortgage Law. Indeed this very issue was raised in the World Bank/PADCO report in 1997.

- Lenders continue to lack confidence in the foreclosure process. They say it is time consuming, uncertain and difficult.

- It is difficult to assess customers worth and repayment ability due to the substantial ‘grey’ economy.

- It is difficult to lend beyond 2 years as the vast majority of deposits are ‘on call’ or short term ‘fixed’.

- A number of issues relating to the Cadastre: Not all owners of the property may have title registered: Difficult to register a mortgage - it may be challenged: Difficult to get access to the Register: Time delays.

- Lending on ‘Apartments in Course of Construction’ is difficult. Cannot use ‘future assets’ as collateral. Only finalised construction can be registered in the Cadastre.

Findings

- Banks say they are unable to lend long term because their core deposits are short term. In order to overcome this problem there is a need to introduce an Asset and Liability Management model and relevant training to the Banks. In this regard NBM advise that the Banks are currently capitalised at 30% while the Capital Adequacy Requirement is 8%. There is in the region of 1 billion lei of surplus funds in the Banks. While the Banks state the have issues over long term lending there may in reality be no great incentive to become involved in mortgage lending due to the high profit margins on short term lending.

- The potential market, at present, for mortgage lending is in a range of 5% to 15% of the house formation population. If we assume that 50% of the total population of 4 million is in this bracket, the potential market is in the order of 100,000 (conservative) to 300,000 (optimistic). Individual interviewees have given estimations ranging from 10% to 15 %, with one specific figure of 140,000 as the number of people able to afford a mortgage.

To calculate the potential mortgage lending volumes we make a number of assumptions:
• number of borrowers in range 100,000 to 300,000;
• apartment sizes 1bed (46 sq mtrs) or 2 bed(69 sq mtrs) being the most popular;
• cost per sq mtr $400 (average new/second hand price);
• therefore 1 bed costs $18400 and 2 bed costs $27600;
• if 100,000 people purchase 1 bed apts @ $18400 total cost is $1.84b. Using the same calculations we get $2.76b for 2 bed apartments;
• if we use a figure of 300,000 purchasers the figures range from $5.52b to $8.28b;
• applying a Loan to Value (LTV) ratio of 75% to the above figures the mortgage lending potential ranges from $1.38b to $6.21b.

This lending would not happen in year 1 but would be graduated over a period of 5 to 10 years depending on the growth in the economy.

• Banks are using prudent and conservative lending standards - however there is no specific set of standards for mortgage lending. Specific standards need to be introduced in a developing mortgage market and these are available from EBRD.

• Establishing affordability is a challenge in an economy which depends to a high degree on ‘grey economy’ earnings. Repayment Capacity models must be adequate to measure this in the medium term pending a more tax compliant economy.

• Difficulties are being encountered in using ‘in course of construction apartments’ as collateral. We understand that proposals to overcome this problem are being developed through an amendment to Article 11 of the Pledge Law.

Internationally it is not the norm for a private individual to offer an ‘in course of construction apartment’ as collateral. Construction companies fund the development from their own resources and Bank working capital, and price the apartments accordingly. The following is the process:

• Buyer places a booking deposit either through an Estate Agent or directly with the Construction Company (usually an Estate Agent)

• On signing the contract the deposit (above) is increased to 10% of the total cost. The buyers’ lawyer will not allow the buyer to sign the contract unless the buyer has received written mortgage approval from a lender.

• The contract states (inter alia) that the construction company will deliver a completed apartment within an agreed timeframe and the buyer will complete the purchase. The buyer may opt out and risk losing the 10%.

Using ‘in course of construction’ single dwelling properties as collateral is acceptable internationally and a system of ‘phased drawdowns’ of the mortgage is available.

• All lenders expressed a strong desire to develop their mortgage lending business into the future. Some have specific projects in hand for 2005. All recognise and acknowledge the role the Secondary Mortgage Markets play in
raising funds internationally. No preparation has yet been made by the Banks in this respect nor has legislation been put in place, although in this respect a Mortgage Agreement provided by the Notaries Representative contains a clause in Chapter 5.7 which appears to permit a lender to assign loans to a third party.

5.4 Government Policies Ministries and Agencies

This section of the report is informed by meetings with key people in the Ministries of Economy, Finance and Justice together with representatives of the National Housing Agency, AMIC and The Land Cadastre. In addition Government Policy papers and Reports have been read.

Introduction

A key policy measure of GoM is the development of a real estate market. In short Government policy states that the Moldovan housing finance system should seek to:

- Reduce to a minimum the direct intervention of the state
- Provide sustainable market based finance
- Integrate the housing finance system into the national and international capital markets.
- Channel more household savings into housing investment and seek additional extrabudgetary sources to support housing.

Some measures have been taken in recent years: the development of both The National Housing Agency and ‘Agentia Municipala de Ipoteca’ (AMIC). The Ministry of the Economy in addition believes that the establishment of an attractive legal and regulatory framework for mortgage lending constitutes one of the building blocks to stimulate investment in the private sector, encourage mortgage credit growth and provide incentives and guarantees to both lenders and borrowers of mortgage finance.

Government Ministries

As stated above we met with key people in the Ministries of Economy, Finance and Justice. The following is a summary of the policy and information points provided.

- There is currently 7/8 billion lei of savings in Banks. Government policy is to attract 50% of this into housing. There is a big demand for housing in urban areas (Chisinau is booming) and it is growing in other areas. Emigrant’s remittances are the key driver of housing demand. Not more than 10% of the population could afford a mortgage at present. Construction is supporting the economy and there is an increasing amount of new construction. Privatised properties can be sold or used as collateral.

- Consumers are invariably carrying the risks - construction companies and lenders minimise or eliminate their risks. Banks do not have long term resources and they see housing as a competitor for resources.

- Government has provided tax incentives to Banks to encourage them to lend longer. Construction companies can reclaim VAT on building materials, which should be reimbursed to the customer, and individuals who invest
€250k in the economy are eligible for a 5 year tax free holiday. All savings are tax free.

- Ministry of Economy wish to promote a Sparkasse/Building Society model where depositors would take a low interest rate on their savings in the expectation of receiving long term mortgage loans at a low rate.

- The perception is that the current legal framework for mortgage lending is inadequate. The Pledge Law of 2001 does not provide enough protection and Government people say the Banks will not provide mortgage finance in these conditions.

- Draft mortgage laws have been developed but are considered incomplete and need redrafting. Laws with such social impact need consultation. Consumers must be adequately protected by amending legislation.

- All Government Ministries raised the difficulty of ‘unfinished buildings’ being used as collateral and the fact that unless a customer owns the property the Banks will not lend.

- The Budget of 2005 will provide incentives to key professionals to encourage them not to emigrate. This incentive will be a Government support for housing.

- A key policy of Government is to join EU and conform to EU regulations.

**National Housing Agency (NHA)**

- NHA reports to the Dept of Construction and is State financed. Council of Europe Development Bank has also provided funding. The overall administrative budget for 2004 was Lei 300k. There is a staff of 15 people.

- Its purpose is to enable social housing and sell houses at lower prices. It is a non profit organisation. It started initially with the development of ‘unfinished’ public apartment blocks. It now purchases ‘unfinished’ private blocks but states it is getting more difficult to find suitable sites.

- NHA has its own construction company and engineering team. By end 2004 it had completed 108 apartments and has plans to increase this to 800 by 2007. NHA price in Chisinau is $270/$350 sq mtr and $200 in other areas.

- This is substantially cheaper than ‘market’ prices. There are 300/400 people on the waiting list at present. Demand is increasing and anyone can apply.

- The model is:
  - Customer registers on NHA list
  - NHA enter into contract with Customer
  - Customer pays 50% of total cost into NHA Bank (NHA guarantees the deposit)
  - NHA seeks proof of family income etc
  - Construction is completed within 12/24 months
  - Customer pays further 40% before they move in
• Final 10% paid after move in.
• Title registered in Customers name after final payment.

• NHA does not provide loans but state that they would do so if the GoM empowered them to do so. There were indications from NBM that changes are needed in the operation of NHA.

**Agentia Municipala de Ipoteca (AMIC)**

• AMIC was set up 6 years ago and is a joint venture between City of Chisinau Municipal Authority and FEC Construction Co. The initial ‘working capital’ was ‘unfinished’ apartment blocks provided free by the City Authorities which were then completed and sold at a profit. 1000 contracts are signed. 500 apartments have been handed over (171 in 2004 and plan 352 in 2005). They have in all approx 5000 clients of which 50% are State employees who are eligible for subsidies (to stop key public servants from emigrating).

AMIC states that 60k people are in need of new/improved housing.

• AMIC has received $2.3m from Ministry of Finance over 7 years at 8%. In addition to add to working capital they receive a down payment of 45% of the total price from all customers on signing the purchase contract and a further group of people (approx 55%) pay off their loans before the due date.

• The Model is:
  • Customer makes a down payment of 45%
  • Move in when apartment complete.
  • Pay balance to AMIC in instalments over 10 years at 8%.
  • Title transferred when all payments complete.
  • Interest rate is dictated by cash flow principles/availability.

AMIC also have an arrangement with Agroind Bank with the following features:

• Customer opens a savings account with Agroind and over 6 months saves 50% of total cost at 7%.
• When Apartment is complete Agroind lend the other 50% to the customer at 20%/23% over 10 years. Title is registered in the customers name and Agroind take a first legal charge.

• AMIC state that a specific law is required to meet EU standards for property and mortgages in addition to long term finance in the market.

**Land Cadastre**

• Privatisation commenced in 1992 but was slow until 1998 when the World Bank funded cadastre project commenced. Since then 70% of all existing buildings are registered and 61% of property has been transferred to private ownership. The Cadastre has now 12 territorial offices and 28 branches. Registration can be completed in from 1 to 20 days depending on the fee paid.
• Information is available to public and professionals subject to a fee. Cadastre officials say that the total property transfer/registration costs are too high. Most of these costs are to Notaries who are paid a % of the value of the transaction. The public think the Cadastre is responsible. They provide an average transaction fee breakdown as follows: Notary $375. Cadastre $65. They feel the law/communications need to be improved.

• Currently there is no central database. Enquirers need to access the local Cadastre for information. Information is available in both electronic and paper forms.

• Unless a title is registered in the Cadastre the owner has no evidence of ownership and has no legal ownership. In addition as property taxes are levied based on Cadastre valuations there is a loss of revenue to the state in respect of these unregistered properties.

• Process of Registration:

  **Title:**
  - If a new property: Cadastre inspects (before registration) that planning conditions are met (but City Hall decides). In all cases there is a check to ensure no taxes are outstanding.
  - Cadastre then registers title and issues Certificate of Title.
  - The transaction must be Notarised if the property is used as collateral - otherwise no requirement to use Notary services.

  **Mortgage:**
  - Borrower obtains copy of the Cadastre register entry.
  - Borrower presents all the documents to the Notary who authenticates the mortgage.
  - Borrower submits two copies of the mortgage to the cadastre.
  - Cadastre registers the mortgage as a charge over the property and stamps the mortgage.
  - Borrower presents stamped copy of the mortgage to the Bank.
  - Bank provides the loan. Time to register the mortgage is approx 7 days.

• **Issues**

  • MOE vision is that up to 4 billion lei in bank savings would be released to support development of the housing market and that a low cost savings/loans model would be introduced. NBM support the view in general when they state the Banks are over capitalised.

  • Many of those interviewed expressed dissatisfaction at the level of service provided by the Land Cadastre. There is concern that:

  Documents issued can be unreliable.
  Taxes are not being estimated in an accurate and efficient manner.
  There is a level of corruption.
Findings

- Government policy is strongly supporting the development of an efficient and effective housing market and a desire to meet EU standards.

- Consumers are carrying an unfair burden of risk. There is a need for stronger consumer legislation.

- NHA appears to be doing a good job in the social sector in which it operates. There is a need to more clearly define its role in the ‘not for profit segment’ and it appears to be underfunded.

- AMIC is providing a very valuable service in the absence of the Banking system from the Housing Market. The current model is not true mortgage lending as the customer does not obtain title until all payments have been made. It is more an instalment payment/lease scheme. It works well.

- The Land Cadastre was a target for criticism by many interviewed. Perhaps if it were structured in a manner where individual sections were responsible for specific activities some/all of the criticisms might be overcome.

5.5 National Bank of Moldova (NBM)

During a wide-ranging discussion the following information was provided by NBM senior executives.

- Parts of the Civil Code cover mortgages but there are contradictions between it and the Pledge Law. The Law needs to be changed.

- While there are difficulties with foreclosure nevertheless registered charges have priority.

- There is generally a lack of trust in the Banking sector due to previous banking collapses. Banks have the funds but are not willing to lend long term. Short term is seen as easier to manage. Construction lending is seen as risky and apartments are not favoured as collateral by Banks. Capital Adequacy Requirement is 8% for general loans and 2.8% for mortgages - Banks are currently capitalised at 30%. There is 1billionlei of surplus funds available for lending at present.

- The average loan rate is 21% which is too high and the loan term 2-5 years which is too short.

- NBM will continue to prohibit lending in foreign currency because of foreign exchange risks and to protect the lei.

- Inflation is in the order of 12.4% and decreasing.

- NBM does not currently have a specific policy on mortgages nor does it have a specific mortgage supervision programme.
• NBM is of the view that NHA requires strengthening in its management.

• AMIC tends to provide housing for municipal employees and it is difficult for the average citizen to get on the programme. Only high income people are in the property market at present. Demand exceeds supply by a factor of 4:1 at present. The rate (8%) is based on $US rates and the customer carries the exchange risk. WB funds are available to AMIC. NBM supports the AMIC model.

• NBM sees that the housing market is growing quickly and that it is an important aspect of the economy. They will support it.

Findings

• The property/mortgage laws are inadequate and need amendment.

• As the mortgage market develops NBM need to develop specific policies and supervision models for the product.

• Banks have adequate finance available for mortgage lending.

• NBM will support mortgage lending into the future

• Capital Adequacy requirement is 8% (2.8% for mortgages) - the Banks are capitalised at 30%.

5.6 International Financial Institutions (IFI’s)

We had the opportunity to meet representatives of all the other IFI’s currently working in Moldova and thank them for their time and input to our project.

• None of the IFI’s are currently working on or planning to work on mortgage related projects.

• The Private Farmers Assistance Programme (PFAP) of USAID have carried out some market research and this is (with their permission) incorporated into the report. PFAP estimate the residential mortgage loan book size to have a potential of $100m. 2004 has seen a house construction boom in Chisinau and to a lesser extent in other towns. NBM have no policy on mortgages (see Monetary Policy for 2005) while at the same time the Economic Growth and Poverty Reduction Strategy 2004-2006 envisages the growth of long term bank crediting for housing (paragraph 323). Realtor activity in the property market is unregulated which sometimes leads to fraud. There is no secondary (bond) market for mortgages and the potential is low at present.

• The Cadastre project was well implemented. It is 80% complete. But the Cadastre in its present form is losing money and will need to be reviewed.

• WNISEF have developed a Mortgage Bank in the Ukraine named International Mortgage Programme (www.ipoteka.com.ua). It was originally operated
through the offices of Pro-Credit. The ‘mortgage bank’ (IMP) was set up in spring 2004 and lends for acquisition or renovation of properties over 5/15 years subject to a down payment of 30% on acquisitions (i.e. 70% LTV) and 50% LTV on renovations. The law to support this lending was passed through the Ukranian parliament over a short period.

- WNISEF estimate the total mortgage market in Moldova to be approx $100m and suggests that a Specialist Mortgage Bank be set up.

- The IFI’s are of the view that the Banks are too profitable at present and there is no incentive for them to lend long term. Standard & Poors reported in 2004 that Moldovan Banks have the biggest profitability of commercial banks in the CIS countries.

**Issues**

- Values stated in housing contracts are lower than the actual amount. This is a fundamentally a tax collection problem.

**Findings**

- Other IFI’s are not currently involved or planning mortgage/legal reform projects.

- WNISEF have set up a stand alone mortgage bank in the Ukraine in 2004 following the introduction of suitable mortgage legislation by Parliament.

**5.7 Services Supporting Home Ownership**

This section of the report provides information on the role played by Insurers and Notaries to support the Housing Market.

**Insurers**

- Insurance in general is in a development mode with low penetration for mortgage related insurances.

- The Insurers we met state that less than 10% of the population have life assurance. One company does not offer life cover while the other does.

- There are no private pension policies/funds.

- Both insurers provide ‘buildings insurance’ but as with life the take up is very low. Most people carry property insurance risks themselves.

- Where property insurance is provided the buildings are generally insured for ‘market value’ and if there is a mortgage the Banks interest is noted in the policy. In general we are told it is the Bank who decided the amount of cover.

- Local Moldovan Insurers are not satisfied with the NBM ban on borrowing/investing in foreign currencies. They state that this creates an ‘unfair playing field’ as foreign owned businesses can operate in foreign currencies.
• One company provides Professional Indemnity Insurance (PII) to some professionals but not Notaries. A version of Mortgage Indemnity Guarantees (MIG) is available for leasing and could be redeveloped for Mortgage lending. Repayment Protection Insurance is available.

• Both Insurers expressed interest in the purchase of Mortgage Bonds (MCB’ or MBS’) as an investment vehicle if these were to become available on the domestic market (see issue).

Notaries

• Notaries are lawyers and the training entry programme is 1 to 2 years.

• The role of the Notary is to:
  • Explain rights, obligations and consequences of the transaction.
  • Verify property title and certifies rights, existence of consents, rights of minors etc
  • In effect the Notary controls and certifies while the Cadastre registers the documents provided by the Notary and keep the Archive.

• The Cadastre has responsibility for registration of defaults and foreclosure.

• A Mortgage Agreement Form which we have obtained confirms that a customer must insure the property against loss and do so before mortgage drawdown. In addition the right to assign the loan to a 3rd party is covered in section 5.7 of the agreement.

Most of the other information/points provided are in effect legal/technical issues and they are listed hereunder.

Issues

• As was seen in the ‘Mortgage Minimum Standards’ section both Life and Buildings Insurance are required. Not all the Banks seek these collaterals at present even though Insurance is required under the Pledge Law 2001.

• Under current legislation (Law on Insurance no 1508 and Regulation on Placement of Insurance Funds) Insurance companies cannot be involved in ‘financial activity’. The meaning of this needs to be clarified in relation to potential investment in Mortgage Bonds.

• Valuations create a big problem – there are 3. The Cadastre (notional) the Appraisal value and the Contract Value. Notaries regularly arbitrate to come up with an agreed value. Taxes are collected on the Cadastre ‘value’ and the Bank uses the Cadastre value which in many instances understates the true value and as a result the customer gets a lower loan.

• Fraud is an issue - people use ‘Certified’ copy documents having reported the loss of the originals and attempt to sell the property twice using both the original and copy documents.
• There are discrepancies between various laws. The laws need amendment. The Law of Cadastre needs adjustment to fit with the Civil Code. Extracts from the Cadastre are outdated and need change.

• Cadastre only registers one person as owner, other people who are not registered may have rights. This raises issues around resale and collateral.

• New Civil Code provides for ‘unlimited’ period within which people can enforce their property rights. As in the previous issue this has implications for resale and collateral.

• A number of people we met criticised the efficiency and cost of the Notary service.

Findings

• Life and Buildings Insurance have very low penetration in the market.

• There are no private pension funds.

• Insurers would consider investing in MCBs or MBSs if these investment options were available.

• Existing Law (or Mortgage Contract clauses) might enable the sale of Bonds.

• A number of serious legal/operational issues were raised by Notaries which need further investigation.

• Purchase of re-insurance in external markets is limited because of the restriction on use of foreign currency.

5.8 Consumer Rights and Protection

In a rapidly developing economy (albeit from a low base) it is normal for participants to attempt to ‘load the dice’ in their own favour.

This is so in Moldova. In the rush for prosperity the rights of Consumers (Customers) have been largely forgotten. During our research this became obvious when discussing housing. Examples of this are:

• Construction companies selling the site to a 3rd party and the new owner ignoring the rights of people who had placed deposits with the previous owner.

• Little rights for consumers in Bankruptcy of the developer.

• Despite putting up a deposit of 50% (in the NHA model) and paying all the purchase cost before moving in … the consumer has no title until all monies are paid.
• Despite putting up a deposit of c45% (in AMIC model) and paying the instalments as they fall due, the consumer has no title until all monies are paid.

• As stated previously ‘non bankers’ are also providing finance and they only transfer title when all monies are paid.

In the above situations a Consumer could in theory have paid 99% of the property cost and still have no title to it and no recourse.

• Consumers are not well informed of either the process or benefits of mortgage lending as an enabler to home ownership.

• On a positive note the rights of spouses are protected (e.g. as in providing the family home as collateral). A non-owning spouses consent is required in advance of a borrower using the family home as collateral.

Findings

• The rights of consumers in property transactions are poorly protected. Title should be transferred to the purchaser as part of the purchase transaction subject to the rights of the lessor/mortgagor as is the norm within the EU.

• In addition a range of Consumer Legislation is in place in EU which protects consumers in credit transactions. This includes a range of ‘information’ requirements. Thought should be given to introducing this.

• Consumer Education is key to citizens understanding the features, benefits and obligations of financial products. Government working with The Financial Services Industry should introduce such an education programme.

5.9 Stock Exchange and The Secondary Mortgage Markets.

This section is informed by a meeting with Moldovan Stock Exchange and based on this and all previous meetings our estimation and findings of how well prepared Moldova is for investment in Secondary Mortgage Market investments.

• The Moldova Stock Exchange (MSE) was established at the end of 1994 as an electronic, screen based, order driven system. It is largely undeveloped with the majority of trades involving shares issued during privatisation. It enjoys favourable legislation and broadly complies with international standards for investor protection, information transparency and fair competition.

• The housing market (particularly in Chisinau and surrounding areas) is very active with constant price escalation. Many people are moving from rural to urban areas. The grey economy together with repatriation of emigrants earnings are principally driving the market. However given an average official income of $100 pm establishing affordability is a major problem.

• To compound the affordability problem interest rates are too high and mortgage terms are too short.
• However MSE are of the view that true mortgage lending is needed to assist in the economic development of Moldova.

• MSE do not currently have knowledge of how the secondary mortgage markets work and how they could assist the long term funding of mortgages but following a short description state they would be interested in and support the development of this market.

Issues

• Can Insurance companies invest in ‘financial instruments’. There is an indication that they are precluded from ‘financial activity’. If that is the case there is a need to amend the Investment law as a major source of potential Mortgage Bond funds is lost.

Findings

• The primary mortgage market is in the early stages of development. There is a lack of confidence in the current legislation. Standard mortgage products supported by secondary market ‘friendly’ documentation are not yet in place. There are no corporate investment funds available and a non-state pension market is not yet in place. Secondary Market legislation has not been developed although the ‘right to sell to a third party’ is incorporated into a seen mortgage contract.

The market, as is, would not be able to support the issue of either Domestic or International Bonds.

6. Conclusions and Recommendations.

(A) Key Conclusions and Recommendations

1. The Housing Market is in a period of growth. The phase of ‘renovating and completing unfinished buildings’ is drawing to a close. The future of the market is in the development of green field sites in addition to a growing ‘second hand’ market. Prices have escalated, especially in city and urban areas, but a number of industry participants are predicting that prices will slow down as demand and supply approach equilibrium.

The key finding and conclusion is that ‘the housing market’, which is a major driver of economic expansion and employment in developed economies, is in a growth phase in Moldova. This in turn requires that the underpinning pillars including the laws, financial services and other supporting services be adequate to underpin and support this growth.

2. The Legislation supporting housing ownership and mortgage lending has been developed on a piecemeal basis over a period of time as market conditions required. Market participants state that there are contradictions between earlier and later laws. Lawyers and Notaries are of the view that while there are many imperfections the laws are nevertheless workable.
However the key finding and conclusion is that there is a lack of confidence amongst all participants in the existing laws and a perception and expectation that a new law will be developed. Indeed this goes back to the WB/PADCO Report of 1997.

**Recommendation:**

Set up a legal project to develop adequate housing and mortgage laws. The Law should address some of the issues highlighted in section 5.2 and also incorporate the requirements of the secondary market. Source documents to examine: existing Moldovan laws; draft Moldovan mortgage law; Ukrainian mortgage law; Romanian mortgage law; this report and the requirements of EU legislation.

3. The Banks provide poor support to the development of the housing market at present. To a great extent the activity in (1 above) has happened without the support of the banking system in that many transactions are ‘cash’ based. Interest Rates are too high (c21%) and loan terms are too short (c2years).

Banks do however provide ‘true mortgages’ as the title is transferred to the customer when the loan is drawn-down and the bank takes a legal charge over the property until the loan is discharged. However Mortgage lending under the above rate/time conditions is impossible - indeed if these conditions were introduced into a more developed economy mortgage lending would soon dry up. Banks plead inability to match short-term deposits to long-term loans. Banks worldwide have faced exactly the same problems and have overcome them.

**Recommendation**

A Bank/Banks to be provided with support and training to overcome the maturities mismatch problem by introducing:

(a) Asset & Liability Management modelling and training.
(b) Cross Subsidisation and Transfer Pricing models
(c) Support to meet Secondary Mortgage Market requirements

4. The Banks are making very healthy profits on short term commercial lending and despite their assertion that they wish to become more actively involved in the mortgage market it has not happened so far. According to NBM there is 1 billion lei under-utilised in the banks and Ministry of Economy state that up to 4 billion lei of savings could be freed up.

All this leads to the conclusion that there is no real appetite in the Banks to support housing development and more competition may be necessary.

**Recommendation:**

EBRD provide a line of Mortgage funds at a favourable interest rate over a 10 year window to a specific Bank(s)(who will be aggressive in the market) to be repaid initially from cash flow and by a subsequent issue of Bonds. The EBRD investment be conditional on the implementation of ‘Mortgage Minimum Standards’ and supported by incentives to customers from GoM.
Set up and fund a stand alone Mortgage Bank modelled on either the Domenia Credit model in Romania (part funded by EBRD) or the International Mortgage Programme (IMP) in Ukraine (which was initially launched through Pro-Credit in Kiev). This is to be subject to the same ‘standards’ and GoM subsidies as above.

The above investments are to be supported by a technical assistance programme.

5. Affordability is a key issue in Moldova. The market for housing is 5%-15% of the house formation population (100,000 - 300,000 people). The 15% is probably optimistic. Currently purchasers provide up to 50% of the purchase price as a deposit. This in effect means that purchasers are providing substantial working capital to construction companies and state enterprises.

Banks state they have difficulty in establishing repayment capacity due to the level of ‘grey/unofficial’ income. This is a difficult area for bankers as to include ‘grey’ income could be construed as assisting with tax evasion (indeed this is so in EU under recent Money Laundering provisions and is therefore illegal) but if the local tax authorities, for policy reasons, decide it is acceptable then it’s possible to include it in affordability models.

**Recommendation:**

The ‘deposit’ payment should be reduced to 25% (i.e. a Mortgage LTV of 75%).

Developers should obtain additional working capital from Banks and factor the increased cost into the house price as in all developed economies. The LARA model (see under ‘future potential’ section of the Housing Market) is predicated on the basis of 50% deposit. By reducing this to 25% the potential increases significantly.

Suggestion: It is possible to structure affordability models to include any kind of income including grey income but this should only be done with agreement of the revenue authorities.

6. Consumers are not well protected or well informed of the process and benefits of mortgage lending at present. A range of issues are outlined in section 5.7 of the report.

**Recommendation:**

Legislation be strengthened to better protect consumers. A range of legislation and information requirements has been enacted in the EU and these to be used as reference documents to implement an education and information campaign for consumers.

7. ‘Unofficial’ lenders are beginning to appear in the market. This is partly a result of inactivity by the Banks. This is a dangerous development which if it continues will lead to a lack of structure in the market and substantial further risk for consumers.
Recommendation:

Ban ‘unofficial’ lending or provide banking licences. A ‘ban’ will only be successful if a more pro-active approach is taken by the Banking system.

8. The ‘Minimum Standards’ set out by EBRD for Mortgage Lending are being only partially met by the Banks at present. This is understandable as mortgages are tiny percentage of total lending. There is a wide variation between Banks (see appendix 1).

Recommendation:

Implement the EBRD Mortgage Lending standards which are now the basis for mortgage lending in South Eastern Europe and beyond. Specifically introduce Life and Buildings insurance as an immediate requirement with life insurance to cover both the amount and term of the loan and buildings insurance to cover the ‘reinstatement’ cost of the property.

9. The mortgage lenders and the supporting institutions are at present unprepared for the issue of Mortgage Bonds or Mortgage Backed Securities. The ‘primary’ mortgage market is in the early stages of development. There are no corporate investment funds or non state pension funds available. However there is interest from Insurers in Bonds as an investment vehicle. Secondary market legislation needs to be developed.

Recommendation:

In relation to the ‘primary’ market implement recommendation in 8 above. Develop adequate legislation for the Secondary Market as outlined in 2 above.

(B) Other Important Conclusions and Recommendations

1. People are, in reality, unable to obtain a mortgage unless they already own the/a property. This excludes all ‘first time buyers’ from the market and effectively stifles economic growth.

Recommendation:

Introduce a ‘Lawyers Undertaking’ into the process. This is used in a number of Western countries. It is a binding legal contract from a lawyer to carry out a series of actions, which in turn protect consumers, lenders and construction companies. The content of the ‘undertaking’ is agreed between the Law Society and the Bankers Federation. Lawyers carry Professional Indemnity Insurance. This type of ‘undertaking’ does not cover ‘in course of construction’ apartments but would cover single dwellings.

2. The Land Cadastre was criticised by a number of parties - Section 5.4. The incorrect valuation of property for tax collection purposes is a key issue and as a consequence the State is losing an undefined amount of revenue.
Recommendation:

It may help to overcome some of the issues raised, particularly the issue concerning correct valuations for tax purposes if ‘market valuations’ are used and in addition people who have not registered their properties should be followed up to do so as no revenue is being collected from these.

3. The Banks reported difficulty with the foreclosure process.

Recommendation:

Develop adequate law and procedures to overcome this structural issue (see 2 above).

4. National Bank of Moldova does not currently have a specific mortgage policy or product supervision model.

Recommendation:

These should be developed to meet the needs of the emerging mortgage market and to ensure prudent lending standards. EBRD have co-operated with Central Banks in neighbouring countries to develop adequate standards in these areas.

5. The current deteriorating state and sustainability of Panel and Metal framed residential buildings and those situated over the mines in Riskani are a major cause of concern.

Recommendation:

This must be addressed in Government policy formulation as the potential refurbishment/replacement cost is massive.

6. Banks report the difficulty in establishing affordability and obtaining accurate credit history.

Recommendation:

As the financial markets evolve a Credit Bureau should be developed.
APPENDIX 1

EBRD Mortgage Minimum Standards
<table>
<thead>
<tr>
<th>STANDARD</th>
<th>AGROINDBANK</th>
<th>MOBIASBANK</th>
<th>MOLDINDCONBANK</th>
<th>VICTORIABANK</th>
</tr>
</thead>
<tbody>
<tr>
<td>MEETS STANDARD *</td>
<td>Y</td>
<td>P</td>
<td>N</td>
<td>Y</td>
</tr>
<tr>
<td>1. MORTGAGE PROCESS</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&gt;Documented process and procedures</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt;Organisational structure</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt;Training programme</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>2. MORTGAGE DOCUMENTATION</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&gt;Consumer guides and marketing material</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt;Application form</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt;Verify Information</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt;Offer letter</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt;Consumer rights</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt;Post draw down information</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>3. BUSINESS OPERATIONS</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&gt;Centralised v. Decentralised</td>
<td>BOTH</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt;Documented checks plus controls</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>STANDARD</td>
<td>AGROINDBANK</td>
<td>MOBIASBANK</td>
<td>MOLDINDCONBANK</td>
</tr>
<tr>
<td>---------------------</td>
<td>----------</td>
<td>-------------</td>
<td>------------</td>
<td>----------------</td>
</tr>
<tr>
<td>MEETS STANDARD *</td>
<td>Y</td>
<td>P</td>
<td>N</td>
<td>Y</td>
</tr>
<tr>
<td>4. PROPERTY VALUATIONS</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Valuation (Appraisal) form</td>
<td>✓</td>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>In house valuers v. External valuers</td>
<td>✓ (BOTH)</td>
<td>✓ (EXTERNAL)</td>
<td>✓ (INTERNAL)</td>
<td>✓ (EXTERNAL)</td>
</tr>
<tr>
<td>Exams/Qualifications/Professional body</td>
<td>✓</td>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Professional indemnity insurance</td>
<td>✓</td>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>5. PROPERTY OWNERSHIP</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Type of title</td>
<td>Freehold</td>
<td>Freehold</td>
<td>Freehold</td>
<td>Freehold</td>
</tr>
<tr>
<td>Document of ownership</td>
<td>TITLE OF OWNERSHIP DOC.</td>
<td>TITLE OF OWNERSHIP DOC.</td>
<td>TITLE OF OWNERSHIP DOC.</td>
<td>CADASTRE EXTRACT/OTHERS</td>
</tr>
<tr>
<td>Cadastre - Access to information</td>
<td>✓</td>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Cadastre - Reliability</td>
<td>✓</td>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>STEANDARD</td>
<td>AGROINDBANK</td>
<td>MOBIASBANK</td>
<td>MOLDINDCONBANK</td>
<td>VICTORIABANK</td>
</tr>
<tr>
<td>-----------</td>
<td>-------------</td>
<td>------------</td>
<td>----------------</td>
<td>---------------</td>
</tr>
<tr>
<td>MEETS STANDARD *</td>
<td>Y</td>
<td>P</td>
<td>N</td>
<td>Y</td>
</tr>
</tbody>
</table>

6. INSURANCES

>Life assurance
>Buildings insurance
>Mortgage Indemnity Guarantee
>House Builders Guarantee
>Title Insurance
>Mortgage Payment Protection

7. CREDIT & RISK MANAGEMENT

>Documented credit/Risk management policy
>Adequate risk/reward ratio
>Risk assessment model
>Self build properties
>Documented ‘exceptions’ policy
>Arrears management & Repossessions policy
>Specific lending criteria
<table>
<thead>
<tr>
<th></th>
<th>STANDAD</th>
<th>AGROINDBANK</th>
<th>MOBIASBANK</th>
<th>MOLDINDCONBANK</th>
<th>VICTORIABANK</th>
</tr>
</thead>
<tbody>
<tr>
<td>MEETS STANDARD</td>
<td>Y</td>
<td>P</td>
<td>N</td>
<td>Y</td>
<td>P</td>
</tr>
<tr>
<td>8. SPECIFIC LENDING CRITERIA</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&gt; Purpose</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Product type</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Property location</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; To whom</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Term</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Age</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Amounts</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Affordability test</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Loan to Value ratio</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Property Appraisal</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Tenure of Property</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Security required</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Verifications required</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>9. SECURITY REQUIREMENTS</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&gt; Legal charge over property</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Life assurance</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Property insurance</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Other security</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>STANDARD</td>
<td>AGROINDBANK</td>
<td>MOBIASBANK</td>
<td>MOLDINDCONBANK</td>
<td>VICTORIA BANK</td>
<td></td>
</tr>
<tr>
<td>----------</td>
<td>-------------</td>
<td>------------</td>
<td>----------------</td>
<td>---------------</td>
<td></td>
</tr>
<tr>
<td>MEETS STANDARD *</td>
<td>Y</td>
<td>P</td>
<td>N</td>
<td>Y</td>
<td>P</td>
</tr>
<tr>
<td>10. ACCOUNT MANAGEMENT</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MANAGEMENT INFORMATION</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>INFORMATION TECHNOLOGY</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&gt; Mortgage Accounting System</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Operational risk/Disaster recovery</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; MIS &amp; Reporting Suite</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>&gt; Account Management &amp; Reviews</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
</tbody>
</table>
APPENDIX 2

Asset and Liability Management
Asset and Liability Management

Mortgage Lending in Ireland - Background

Irish banks did not provide loans for residential mortgages to their customers until the late 1970's. It was generally believed that the provision of such loans would contravene the basic banking approach of never lend for long terms using short-term deposits.

However, rival financial institutions had been set up at the end of the nineteenth century, dedicated to the provision of finance for residential mortgages, which used short-term deposits from their customers as the primary source of funds. These institutions were similar to the Savings & Loans institutions in the US and were called Building Societies both in Ireland and in the U.K. By the middle of the 1970's the Building Societies had clearly demonstrated that it was possible to fund residential mortgages from short-term deposits.

While the Building Societies were growing rapidly they were unable to keep up with the demand for funds due to their lack of scale.

Entry by the commercial banks into the Residential Mortgage market

(a) Government Support
The Irish Government approached the commercial banks and attracted them into the Residential Mortgage market by providing a special tax relief on mortgage interest.

(b) Central Bank
The Central Bank was also supportive and processes were put in place to ensure that adequate liquidity would be available in the banking system. In particular all foreign currency contracts were performed through the Central Bank which enabled the Central Bank to provide Irish pound liquidity to the market, when shortages arose, by means of short term 'reverse swaps'. If the view of the Central Bank was that shortages were arising due to large flows of money out of the state their primary remedy was to raise interest rates.

(c) Core Deposits
It was discovered, also, that a distinction needed to be made between “core” and “non-core” deposits. While individual customers were free to draw deposits on demand experience showed that banks always retained a sizeable level of deposits. When customers drew down funds they were paid to others and provided the recipients did not spend the money outside the state the funds eventually resurfaced in the banking system.

By lending to a maturity that is greater than the maturity of the deposits a bank runs a liquidity risk. It does so because the depositor can demand their funds before the loans are repaid and the bank may run out of cash. Therefore a conservative bank wishing to preserve a strong liquidity profile must make conservative assumptions on the level of ‘core deposits’ available.

This is done by modelling the deposits experience and applying this statistically based process to future deposits. There are other ways in which a bank can preserve its liquidity if it has the same liquidity profile (short deposits wishing to
lend long). These include lengthening the maturity of other liabilities e.g. using the MTN market, paying for syndicated undrawn commitments or indeed on the asset side, ensuring that it holds assets that can be ‘repoed’.

(d) Loan Maturities
The banks also reviewed the “duration” of residential mortgage lending and have since discovered that as the mortgage market develops the “duration” of mortgages declines. In Ireland the average mortgage is repaid in less than seven years even though the nominal life is 25 years. In recent times one of the major Irish banks is offering mortgages with a nominal maturity of forty years. (In Japan some banks offer mortgages with a nominal life of 80 years on the basis that it will be paid off by more than one generation).

Mortgage customers, nowadays, usually classify their first home as a “starter home” and within six or seven years they “trade up” to a more substantial residence. The result is that the actual maturity (duration) of residential mortgages is less than seven years. The Bank of England confirmed in the late 1980’s that residential mortgages, on average were paid down within three and a half years in the London area.

Business rationale for residential mortgage lending
Bad debt experience in relation residential mortgages is very low and less than 0.25% per annum. Mortgage margins are over 1% and the resultant return on equity is very attractive as the capital required under international capital adequacy rules (BASEL II Capital Accord) is only 2.8% compared to the minimum requirement for standard loans of 8%.

The Construction Sector benefited very substantially from the impetus to their activity levels and the significant increases in employment and profits supported strong economic growth in the economy. This growth provided increased taxation levels to the government which helped them to finance initiatives supportive of the ongoing development of the Irish economy. For years the Construction industry has been viewed by Irish commentators as the barometer of the Irish economy.
APPENDIX 3

EU Information Requirements for Mortgage Customers
COMMISSION RECOMMENDATION

of 1 March 2001

on pre-contractual information to be given to consumers by lenders offering home loans
COMMISSION RECOMMENDATION
of 1 March 2001

on pre-contractual information to be given to consumers by lenders offering home loans

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the second indent of Article 211 thereof,

(1) Whereas achieving a single market for financial services offering consumers a high level of protection is a priority for the Community, whereas signing a home loan contract is often the most important financial commitment that a consumer enters into; whereas home lending is an area of financial services where consumers could gain substantial benefit from increased cross-border activity provided that adequate protective measures are in place;

(2) Whereas it is essential in that context that the pre-contractual information as to the terms and conditions on which home loans are offered throughout the Community are transparent and comparable; whereas, to that end, lenders should be invited to provide consumers with two sets of harmonised information, namely one containing general information and the other containing personalised information, whereas the personalised information should be provided in a standard written format, known as a European Standardised Information Sheet;

(3) Whereas the elements of information – both general and personalised – to be given to consumers by lenders, have been negotiated under the auspices of the Commission by the associations and federations representing lenders, on the one hand, and consumers, on the other; whereas these negotiations have resulted in a Voluntary Code of Conduct on pre-contractual information for home loans (the “Code”), a copy of which can be obtained from the adhering lenders; adherence to the Code is open to all home loan lenders, regardless of whether they are members of one of the negotiating associations and federations;

(4) Whereas in certain Member States national requirements on additional pre-contractual consumer information for home loans already exist; whereas it is desirable that these additional information elements be merged with those in the European Standardised Information Sheet and that this be done in a manner that ensures comparability across borders for the consumer at European level; whereas, where a Member State imposes on lenders from other Member States an obligation to give additional pre-contractual information to consumers above and beyond what is set out in the Annexes, it is invited to ensure that this information is in conformity with Community law;

2
(5) Whereas both domestic and cross-border home loans should be subject to this Recommendation, excluding credit agreements which are covered by Council Directive 87/102/EEC of 22 December 1986 on the approximation of laws, regulations and administrative provisions of the Member States concerning consumer credit, as last amended by Directive 98/7/EC of the European Parliament and of the Council;  

(6) Whereas the Commission will establish a central register of lenders offering home loans, indicating whether or not those lenders adhere to the Code, as well as the date on which those lenders notified their adherence to the Commission; whereas the Commission will, by all appropriate means, ensure that the public at large can consult this central register;  

(7) Whereas the Commission will monitor compliance with this Recommendation and assess its effectiveness; whereas the Commission will consider presenting binding legislation, should the terms of this Recommendation not be fully complied with.

HEREBY RECOMMENDS:

Article 1
Scope

This Recommendation covers pre-contractual consumer information for domestic and cross-border home loans. Credit agreements covered by Directive 87/102/EEC are excluded from the scope of this Recommendation.

Article 2
Definition

For the purposes of this Recommendation, a "home loan" means a credit to a consumer for the purchase or transformation of the private immovable property he owns or aims to acquire, secured either by a mortgage on immovable property or by a surety commonly used in a Member State for that purpose.

Article 3
Principles

The lender should supply to the consumer in the course of the pre-contractual phase:

(a) general information as set out in Annex I;
(b) personalised information to be presented in a European Standardised Information Sheet as set out in Annex II.

---

In addition, the lender should supply to the consumer information on the identification, address and telephone number of the competent body to which the consumer can refer in the event of difficulties in relation to the application of the Voluntary Code of Conduct on pre-contractual information for home loans (the "Code").

The final decision to accept a credit offer from a lender lies with the consumer.

Article 4
National requirements on additional pre-contractual consumer information

Should pre-existing national requirements provide that additional pre-contractual consumer information is to be given to the consumer, Member States are invited to take all necessary steps in order that this additional information may be merged with the information included in the European Standardised Information Sheet in a manner that does not impair comparability across borders.

Each Member State is moreover invited to ensure that those additional national requirements are imposed on lenders from other Member States offering home loans in the territory of that Member State only if those additional requirements are in conformity with Community law.

In this case, the host Member State is invited to notify the requirements to the Commission so that the latter can consider them in the framework of its monitoring activity set out in Article 6.

Article 5
Establishment of a registry by the Commission

The Commission will establish a central register of lenders offering home loans, indicating whether or not those lenders adhere to the Code.

Article 6
Monitoring by the Commission

The Commission will monitor compliance with this Recommendation.

Two years after adoption of this Recommendation, the Commission will assess its effectiveness: the assessment will be based on its own monitoring, on annual progress reports to be drawn up by the European Credit Sector Associations, and on any other information available.

Article 7
Final Provision

Member States and lenders offering home loans in the Community, regardless of whether they are members of the associations and federations who negotiated the Code, are invited to comply with this Recommendation by no later than 30 September 2002.
Article 8

Addressees

This Recommendation is addressed to the Member States.

Done at Brussels, 1 March 2001

For the Commission
Primo ROCHESTEIN
Member of the Commission
ANNEX I

Initial information about home loans should include or be accompanied by the following information in the same format as that initial information is itself provided:

A – Lender:

1. Identification and address of the lender;
2. Where appropriate, identification and address of the intermediary.

B – Home Loan:

1. Purposes for which the home loan may be used;
2. Form of security;
3. Description of the types of home loans available with short description of the differences between fixed and variable rate products, including related implications for the consumer;
4. Types of interest rate – fixed, variable, and combinations thereof;
5. An indication of the cost of a typical home loan for the consumer;
6. A list of related cost elements, such as, administrative costs, insurance costs, legal costs, intermediaries costs;
7. The different options available for reimbursing the credit to the lender (including the number, frequency, amount of repayment instalments if any);
8. Whether there is a possibility of early repayment (if so, its conditions);
9. Whether a valuation of the property is necessary and, if so, by whom it has to be carried out;
10. General information on tax relief on home loan interest or other public subsidies prevailing, or information on where one can obtain further advice;
11. The duration of the reflection period, where relevant;
12. Confirmation that the institution subscribes to the Code, and indication that a copy of the Code is available in the institution.
### ANNEX II

**EUROPEAN STANDARDISED INFORMATION SHEET**

This standardised information is an integral part of the **Variable Rate of Interest** on precontractual information for home loans, a copy of which can be obtained from your lender.

<table>
<thead>
<tr>
<th>Item</th>
<th>Description</th>
</tr>
</thead>
</table>
| Up front text | "This document does not constitute a legally binding offer.

The figures are provided in good faith and are an accurate representation of the offer that the lender would make under current market conditions based on the information that has been provided. It should be noted, however, that the figures could fluctuate with market conditions.

The provision of this information does not oblige the lender to grant a credit." |

#### 1. Lender

2. Description of product

   This section should provide a brief but clear description of the product. It should be made clear whether it is a mortgage on a property or another commonly used security.

   It should be made clear whether the product on offer is an interest only home loan (i.e., that it involves servicing the debt with a lump sum payment at the end) or a repayment home loan (i.e., that it involves paying interest and capital over the lifetime of the home loan).

   It should be made clear whether the home loan terms are dependent on the consumer supplying a certain amount of capital (perhaps expressed as a percentage of house value).

   Where the home loan terms are dependent on a third party guarantee, this should be clearly stated.

3. Nominal rate (indicate type of rate and duration of fixed period)

   This section should provide information on the key condition of the home loan - the interest rate. Where relevant, the description should include details of how the interest rate will vary including, for example, review periods, lock-in periods and related penalty clauses, collars and caps etc.

   The description should include:

   - whether or not a variable rate is indexed; and
   - provide details of indexation, where appropriate.

4. Annual percentage rate of charge (APRC) based on national regulation or effective rate, where relevant

   Where a national figure for APRC is not set in legislation, the equivalent effective rate should be used.
<table>
<thead>
<tr>
<th>5. Amount of credit advanced and currency</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>6. Duration of home loan agreement</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>7. Number and frequency of payments (may vary)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>8. For repayment home loan, amount of each instalment (may vary)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>9. For interest only home loan:</th>
</tr>
</thead>
<tbody>
<tr>
<td>- amount of each regular interest payment;</td>
</tr>
<tr>
<td>- amount of each regular payment to the repayment vehicle.</td>
</tr>
</tbody>
</table>

The lender should provide an indication – real or illustrative – of:

(a) the amount of each regular interest payment in accordance with the frequency of the payments (see point 7);

(b) the amount of each regular payment towards the repayment vehicle, in accordance with the frequency of the payments (see point 7).

Where appropriate, a warning should be given that the repayment vehicle may not cover the amount borrowed.

If the lender provides the repayment vehicle and has included this in part of the offer then it should be clear whether or not the offer is tied to the consumer’s agreement on that repayment vehicle.

<table>
<thead>
<tr>
<th>10. Additional non-recurring costs, where applicable</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
</tbody>
</table>

A list of initial non-recurring costs which the consumer is expected to pay upon taking out the home loan must be provided.

Where these costs are under the direct or indirect control of the lender, an estimate of the costs should be provided.

Where relevant, it should be made clear if the cost is to be paid regardless of the outcome of the home loan application.

Such costs might include, for example:

- administrative costs;
- legal fees;
- property valuation.

When an offer would be dependant on the consumer’s receiving these services through the lender (provided this is permitted in national legislation), it should be clearly stated.

8
<table>
<thead>
<tr>
<th>Section</th>
<th>Text</th>
</tr>
</thead>
</table>
| 11. Additional recurrent costs (not included in S) | This list should include, for example:  
- insurance against default on payments (unemployment/death);  
- fire insurance;  
- building and contents insurance.  
Where an offer would be dependent on the consumer's receiving these services through the lender (provided this is permitted in national legislation), it should be clearly stated. |
| 12. Early repayment | The lender should provide an indication of:  
- the possibility and terms of early repayment;  
- including an indication of any charges applicable.  
Where it is not possible to stipulate the charge at this stage, an indication should be provided that a sum sufficient to recoup the lender's cost in arranging the transaction would be payable. |
| 13. Interest complaint schemes | Name, address and telephone number of contact point |
| 14. Illustrative amortisation table | The lender should provide an illustrative and summarised amortisation table which includes, at least:  
- monthly or quarterly payments (if it the case) for the first year;  
- to be followed by yearly figures over the total duration of the loan.  
The table should contain figures on:  
- amount of capital reimbursed;  
- amount of interest;  
- outstanding capital;  
- amount of each installment;  
- sum of capital and interest  
It should be clearly indicated that the table is illustrative only and contain a warning if the home loan proposed has a variable interest rate. |
| 15. Obligation to domicilie bank accounts and salary with lender | |

TOTAL P. 10
COMMISSION

COMMISSION RECOMMENDATION
of 3 March 2001
on pre-contractual information to be given to consumers by lenders offering home loans
(notified under document number C(2001) 477)
(Text with EEA reference)

(2001/19/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the second indent of Article 213 thereof,

Whereas:

(1) Achieving a single market for financial services offering consumers a high level of protection is a priority for the Community. Signing a home loan contract is often the most important financial commitment that a consumer enters into. Home lending is an area of financial services where consumers could gain substantial benefit from increased cross-border activity provided that adequate protective measures are in place.

(2) It is essential in that context that the pre-contractual information as to the terms and conditions on which home loans are offered throughout the Community are transparent and comparable. To that end, lenders should be invited to provide consumers with two sets of harmonised information, namely one containing general information and the other containing personalised information. The personalised information should be provided in a standard written format, known as a European Standardised Information Sheet.

(3) The elements of information — both general and personalised — to be given to consumers by lenders, have been negotiated under the auspices of the Commission by the associations and federations representing lenders, on the one hand, and consumers, on the other. These negotiations have resulted in a Voluntary Code of Conduct on pre-contractual information for home loans (the "Code"), a copy of which can be obtained from the adhering lenders. Adherence to the Code is open to all home loan lenders, regardless of whether they are members of one of the negotiating associations and federations.

(4) In certain Member States national requirements on additional pre-contractual consumer information for home loans already exist. It is desirable that these additional information elements be merged with those in the European Standardised Information Sheet and that this be done in a manner that ensures comparability across borders for the consumer at European level. Where a Member State imposes on lenders from other Member States an obligation to give additional pre-contractual information to consumers above and beyond what is set out in the Annexes, it is invited to ensure that this information is in conformity with Community law.


(6) The Commission will establish a central register of lenders offering home loans, indicating whether or not those lenders adhere to the Code, as well as the date on which those lenders notified their adherence to the Commissioner. The Commission will, by all appropriate means, ensure that the public at large can consult this central register.

(7) The Commission will monitor compliance with this recommendation and assess its effectiveness. The Commission will consider presenting binding legislation, should the terms of this recommendation not be fully complied with.

(2) OJ L 125, 1.5.1996, p. 17.
HEREBY RECOMMENDS

Article 1
Scope
This recommendation covers pre-contractual consumer information for domestic and cross-border home loans.

Article 2
Definition
For the purposes of this recommendation, a home loan means a credit to a consumer for the purchase or transformation of the private immovable property he owns or aims to acquire, secured either by a mortgage on immovable property or by a surety commonly used in a Member State for that purpose.

Article 3
Principles
The lender should supply to the consumer in the course of the pre-contractual phase:
(a) general information as set out in Annex I;
(b) personalised information to be presented in a European Standardised Information Sheet as set out in Annex II.

Article 4
National requirements on additional pre-contractual consumer information
Should pre-existing national requirements provide that additional pre-contractual consumer information is to be given to the consumer, Member States are invited to take all necessary steps in order that this additional information may be merged with the information included in the European Standardised Information Sheet in a manner that does not impair comparability across borders.

Each Member State is moreover invited to ensure that those additional nation requirements are imposed on lenders from other Member States offering home loans in the territory of that Member State only if those additional requirements are in conformity with Community law.

In this case, the host Member State is invited to notify the requirement to the Commission so that the latter can consider them in the framework of its monitoring activity set out in Article 6.

Article 5
Establishment of a register by the Commission
The Commission will establish a central register of lenders offering home loans, indicating whether or not these lenders adhere to the Code.

Article 6
Monitoring by the Commission
The Commission will monitor compliance with this recommendation.

Two years after adoption of this recommendation, the Commission will assess its effectiveness; the assessment will be based on its own monitoring, on annual progress reports to be drawn up by the European Credit Sector Associations, and on any other information available.

Article 7
Final provision
Member States and lenders offering home loans in the Community, regardless of whether they are members of the associations and federations who negotiated the Code, are invited to comply with this recommendation by no later than 30 September 2002.

Article 8
Addressers
This recommendation is addressed to the Member States.

Done at Brussels, 1 March 2001.

For the Commission

Forster HERBSTEIN
Member of the Commission
ANNEX I

Initial information about home loans shall include or be accompanied by the following information in the same format as that initial information is itself provided:

A. Lender
   1. Name, qualification and address of the lender.
   2. Where appropriate, identification and address of the intermediary.

B. Home loan
   1. Purpose for which the home loan may be used.
   2. Form of security.
   3. Description of the types of home loans available with short description of the differences between fixed and variable rate products, including related implications for the consumer;
   4. Types of interest rate — fixed, variable, and combination thereof;
   5. An indication of the cost of a typical home loan for the consumer;
   6. A list of related cost elements, such as, administrative costs, insurance costs, legal costs, intermediaries costs.
   7. The different options available for reimbursing the credit to the lender (including the number, frequency, amount of payments instalments if any).
   8. Whether there is a possibility of early repayment (if so, its conditions).
   9. Whether a valuation of the property is necessary and, if so, by whom it has to be carried out.
   10. General information on tax relief on home loan interest or other public subsidies prevailing, or information on where one can obtain further advice.
   11. The duration of the reflection period, where relevant.
   12. Confirmation that the institution subscribes to the Code, and indication that a copy of the Code is available in the institution.
## ANNEX II

**EUROPEAN STANDARDISED INFORMATION SHEET**

This standardized information is an integral part of the Voluntary Code of Conduct on pre-contractual information for home loans, a copy of which can be obtained from your lender.

<table>
<thead>
<tr>
<th>Item</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up front</td>
<td>This document does not constitute a legally binding offer. The figures are provided in good faith and are an accurate representation of the offer that the lender would make under active market conditions based on the information that has been provided. It should be noted, however, that the figures could fluctuate with market conditions. The provision of this information does not oblige the lender to grant a credit.</td>
</tr>
<tr>
<td>1. Lender</td>
<td></td>
</tr>
<tr>
<td>2. Description of product</td>
<td>This section should provide a brief but clear description of the product. It should be made clear whether it is a mortgage on a property or another commonly used tenure. It should be made clear whether the product on offer is an interest only home loan (i.e. that it involves servicing the debt with a lump sum payment at the end) or a repayment home loan (i.e. that it involves paying interest and capital over the lifetime of the home loan). It should be made clear whether the home loan terms are dependent on the customer supplying a certain amount of capital (perhaps expressed as a percentage of house value). Where the home loan terms are dependent on a third party guarantee, this should be clearly stated.</td>
</tr>
<tr>
<td>3. Nominal rate (indicate type of rate and duration of fixed period)</td>
<td>This section should provide information on key conditions of the home loan — the interest rate. Where relevant, the description should include details of how the interest rate will vary including, for example, review periods, lock in periods and related penalty clauses, charges and caps etc. The description should include: whether or not a variable rate is indexed, and provide details of indices, where appropriate.</td>
</tr>
<tr>
<td>4. Annual percentage rate of charge (APRC) based on national regulation or effective rate, where relevant</td>
<td>Where a national figure for APRC is not set in legislation, the equivalent effective rate should be used.</td>
</tr>
<tr>
<td>5. Amount of credit advanced and currency</td>
<td></td>
</tr>
<tr>
<td>6. Duration of home loan agreement</td>
<td></td>
</tr>
<tr>
<td>7. Number and frequency of payments (may vary)</td>
<td></td>
</tr>
<tr>
<td>8. For repayment home loan, amount of each instalment (may vary)</td>
<td></td>
</tr>
</tbody>
</table>
| 9. For interest only home loan:  
   - amount of each regular interest payment,  
   - amount of each regular payment to the repayment vehicle |  
   - The lender should provide an indication, real or illustrative, of:  
     a) the amount of each regular repayment in accordance with the frequency of the payments (see item 4);  
     b) the amount of each regular payment towards the repayment vehicle in accordance with the frequency of the payments (see item 4).  
   Where appropriate, a warning should be given that the repayment vehicle may not cover the amount borrowed. If the lender provides the repayment vehicle and has included this in part of the offer then it should be clear whether or not the offer is tied to the consumer’s agreement on that repayment vehicle. |
10. Additional non-recurring costs, where applicable

A list of initial non-recurring costs which the consumer is expected to pay upon taking out the home loan must be provided.

Where these costs are under the direct or indirect control of the lender, an estimate of the costs should be provided.

Where relevant, it should be made clear if the cost is to be paid regardless of the outcome of the home loan application.

Such costs might include, for example:
- administrative costs,
- legal fees,
- property valuation.

Where an offer would be dependent on the consumer's receiving these services through the lender (provided this is permitted by national legislation), it should be clearly stated.

11. Additional recurrent costs (not included as point 9)

This list should include, for example:
- insurance against default on payments (unemployment, death),
- fire insurance,
- building and contents insurance.

Where an offer would be dependent on the consumer's receiving these services through the lender (provided this is permitted by national legislation), it should be clearly stated.

12. Early repayment

The lender should provide an indication of:
- the possibility and terms of early repayment,
- including indication of any charges applicable.

Where it is not possible to stipulate the charge at this stage, an indication should be provided that a sum sufficient to repay the lender's costs in winding up the transaction would be payable.

13. Internal complaint schemes

Name, address and telephone number of contact point.

14. Illustrative amortisation table

The lender should provide an illustrative and anonymised amortisation table which includes, at least:
- monthly or quarterly payments (if it be the case) for the first year,
- to be followed by yearly figures over the total duration of the loan.

The table should contain figures on:
- amount of capital reimbursed,
- amount of interest,
- outstanding capital,
- amount of each instalment,
- sum of capital and interest.

It should be clearly indicated that the table is illustrative only and contain a warning if the home loan proposed has a variable interest rate.

15. Obligations to disclose basic account and salary with lender
APPENDIX 4

The Legal and Regulatory Framework
The Legal and Regulatory Framework

Introduction

The legal framework regulating mortgage and relationships related to it, including mortgage loan, registration of ownership and right of mortgage, the rights and obligations of the parties to the mortgage, is currently made of a number of legislative and normative rules, which serve as basis for the good functioning of this legal institution.

In this paper some of the most important laws in the field, specifying the relevant regulations, their shortcomings and problems of a legal nature will be addressed, and general proposals as to the removal of the existing contradictions, the supplementation of the current regulations and the passing of new pieces of legislation will be made. We should mention that our proposals are based on an overall assessment of the existing regulations and may only be taken as a starting point for a possible future initiative to review the relevant legal framework.

I. Pledge Law No. 449-XV dated 30 July 2001 (hereinafter referred to as - Law 449/2001) and the rules of the Moldovan Civil Code relating mortgage (Book II, Title IV, Chapter V - Articles 454 to 495). Both such laws contain similar regulations with respect to:

- the mortgaged property and the parties to the mortgage relationship (the mortgagee and mortgagor),
- the creation and public registration of mortgage, registration of any amendments to the mortgage agreement,
- legal effects of mortgage, both between the parties and against third parties,
- subsequent mortgage and disposal of the mortgaged property,
- the terms and conditions of enforcement of the mortgage. Law 449/2001 also established the judicial procedure of forced conveyance of the mortgaged property, while the Civil Code makes a reference to the procedural law to this respect.

Overall, both of these laws contain some mechanisms of protecting the lawful interests of the participants to the mortgage relationship.

However, a significant number of shortcomings has been identified and is worthy of discussion:

a) Mortgage of property built with the proceeds of a mortgage loan - amendments are required providing that, alongside immovable property, the following items may also be mortgaged:

- unfinished constructions,
- parts of an unfinished construction (apartments and other dwelling premises) - by the persons having entered into purchase agreements with respect to them (including, with the proceeds of a mortgage loan), and are therefore expected to become owners when the construction shall have been finished.

For the purposes of securing an adequate protection for all the participants to a construction, the law must state that in case of a mortgage over an unfinished
construction by the owner of the land plot or the holder of a right of superficies, the mortgage will not extend on such parts of the building (apartments and other premises) that have been purchased and fully paid for by third parties. Such parts of a building that have not been fully paid for are subject to the mortgage, and the building’s purchaser (in case of enforcement) will be subrogated in the rights and obligations of the mortgagor against such third parties.

For the establishment of a mechanism of mortgaging unfinished immovable property the Immovable Property Cadastre Law must also be amended so as to extend the registration process over unfinished immovable property. This will be considered when discussing the aforementioned law.

b) Mortgage over immovable property purchased with the proceeds of a mortgage loan- the scheme currently proposed (the purchase and mortgage agreement are entered into simultaneously, and the mortgage is registered immediately after ownership is registered - Article 470 (2) of the Civil Code) does not work in cases where the purchase is not effected under a notarised agreement (which is permitted by the Civil Code).

Having regard to the fact that such scheme is largely used in practice, we propose to strengthen it by specifying that a future property may also be subject to mortgage (i.e. contracted but yet unregistered), or, alternatively, by waiving the requirement for mortgage agreements to be notarised. This proposal will be dealt with later below.

c) Protecting the mortgagee’s lawful interests - the level of protection of mortgagee’s interests provided by the current law is by far not the best. Its main shortcomings and proposals to remedy the same are as follows:

- Mortgage over property of children and incapable individuals currently requires the approval of the guardianship and trusteeship authorities (Article 2 (6) of the Law 449/2001). This rule should be amended to the effect that such approval is only necessary when the guardianship and trusteeship have been established under law (Articles 51 and 142 of the Family Code) and have been duly noted in the Registry of Immovable Property (Article 46 of the Immovable Property Cadastre Law). This would allow avoiding inappropriate formalities when creating a mortgage over property of children whose parents may legally represent them and would protect creditors in cases where the guardianship and trusteeship has not been registered publicly.

- In case of an action for recovery (vindicatio) of the immovable property form the mortgagor, the mortgage terminates (Article 483 (1) of the Civil Code). In order to prevent this unwanted consequence, the mortgagee should be granted the right to oppose to an action of recovery. For these purposes, the law will provide that the mortgagor, against whom an action for recovery is taken, will bring the mortgagee into the proceedings, and the latter will be entitled to exercise any legal remedies of an owner, even if the mortgagor fails to exercise them personally.

The mortgagee likewise should be protected in cases of expropriation of the property and avoidance of the ownership title. Law should provide that a property may only be returned (restitutio) after receipt of an equitable indemnity for the returned property, which indemnity will be subject to mortgage by operation of law (Article 479 (2) of the Civil Code).
The law should moreover clearly lay down that in cases of confiscation of an immovable property, the mortgage will continue to exist (Cf. Article 41 of the Russian Mortgage Law).

- Diminishing the value of the mortgage by the mortgagor (by failure to notify about the existing rights of third parties - Article 469 of the Civil Code; either total or partial destruction of the immovable property - Article 48 of the Law 449/2001) is currently sanctioned by accelerating the maturity of the secured obligation. This however is not sufficient. From the standpoint of the mortgagee’s interests, it would be far more efficient to force the mortgagor to supplement to the mortgage. In case of failure to do so - the mortgagee should be given the right to create a pledge by operation of law over other property of the mortgagor (e.g. car, garage, electronic equipment, etc.).

Similarly, when the law (namely, Article 483 (2) of the Civil Code) lists exhaustively the breaches that entitle the mortgagee to initiate enforcement, it leaves with no sanction other material breaches (use of the immovable property contrary to its intended purpose, failure to procure an insurance, failure to make available the property for inspection purposes, etc.). We propose supplementing the events of default listed in the law with the ones listed in the agreement itself.

Furthermore, for the cases when the prohibition to alienate the mortgaged immovable property is breached, the law should make it a right of the mortgagee to opt either for avoiding the alienation transaction or for enforcing against such alienated property

d) Protecting the mortgagor’s interests - here, too, there is some room for improvement, as per the following:

- The right of an owner to obtain an income by letting the property on lease is restricted by Law 449/2001, which requires the mortgagee’s prior approval, and is discretionary in the Civil Code (Article 477), requiring only a notification of the mortgagee, regardless of the duration of the lease. A scenario conducive to the re-balancing of both parties’ interests would be one where the mortgagor is entitled to convey the property for the use of a third party for a duration not exceeding the maturity of the secured obligation without the mortgagee’s approval, provided, however, that the third party loses its right of use upon enforcement beginning. Any lease exceeding the maturity of the secured obligation should be authorized beforehand by the mortgagee, and upon enforcement the third party’s right of use will continue in full force.

- The law should clearly lay down that the mortgagor who settles the secured obligation in lieu of the debtor will subrogate the mortgagee in its claim against the debtor (Cf. Article 292 of the Georgian Civil Code). Upon the assignee’s request, the mortgagee will convey all documentation pertaining to the claim, and the registrar will enter such subrogation into the Registry of Immovable Property.

e) The procedure of mortgage enforcement - is currently confusing because of sometimes contradictory rules between the Law 449/2001 and the Civil Procedure Code; the rules of this Code will be dealt with later on in this paper. The forced sale of the mortgaged property should insure a timely and barrier-free exercise of the mortgagee’s right, on the one hand, and a protection of the interests of the owner of the property enforced against, and other parties involved, on the other. These are the aspects worthy of consideration:
• the requirements on the pre-enforcement procedure are far from being precise and need be reviewed (remove confusion between the term „warning” and „notice”),
• specific periods of time that need be complied with should be set forth (for instance, 15 days for the voluntary performance of the obligation, and 30 days from initiating the enforcement to the sale of property), - as a rule, the enforcement procedure will be the one provided by the agreement, subject to the statutory limitations, and the judicial procedure will apply only in such cases as are expressly provided for by law (for example, when the immovable property enforced against is inhabited by children, old or disabled individuals),
• enforcement will take place by means of public auctions under the procedure provided for by law (Articles 809 to 816 of the Civil Code, to which special rules relative to the participation at the auction, how the starting price is to be fixed, how the property is to be adjudicated, and when must the auction be repeated, the right of the mortgagee to adjudicate the property to himself subject to a discount when the sale has failed during two auctions, are all to be added up);
• the competition between several secured creditors with a security interest over the same property - the law does not lay down how a mortgage can be enforced by several creditors with different ranks of security, a rather frequent situation in practice. Potential solutions to this case should take into account both the interests of the upper-rank and the lower-rank creditor. The best is the solution where enforcement by one creditor entitles another creditor(s) to accelerate the maturity of its claim and take part at enforcement. In case if such creditor will fail to use the right of acceleration, the property will be sold subject to its mortgage. Moreover, the upper-rank creditor should be granted the right to terminate the enforcement for justified reasons (Cf. Article 13 of the Ukrainian Mortgage Law);
• protection of rights of third parties which may affected by the sale of the immovable property (e.g. lessees) - the law should lay down that any third party whose situation would be aggravated as a result of the sale of the property is entitled to settle the secured obligation and subrogate the mortgagee;
• protection of the rights of the property purchaser as a result of enforcement - the current law fails to address it. It should be provided that a person who purchased a mortgaged property will subrogate its previous owner in all his rights related to the property (e.g. the building’s purchaser takes over the right to use and/or of superficies over the leased land plot). Likewise, the purchaser will be bound by the obligations of the previous owner (e.g. the purchaser of a land plot will comply with such servitudes or superficies as have been previously created), provided, however, that he may not be bound to pay the previous owner’s debts (e.g. electricity, heat, gas, etc.).

f) Assignment of mortgage - is currently possible under an agreement for the assignment of the secured claim (Articles 484, 556, and 558 of the Civil Code). Whereas mortgage assignment is the first element of circulation of mortgage-backed securities on the secondary market, the feasibility of establishing the legal institute of mortgage deed - as securities issued by the mortgagee in accordance with the mortgage agreement, certifying the claim and, implicitly, the right of
mortgage - should be considered. A mortgage deed is transferred by an endorsement and the initial mortgagee (originator) is subrogated by the transferee of the deed. The contents of a mortgage deed will be provided for by law, while its form will be developed by the public authority supervising the securities market. Regulations on the issuance and circulation of mortgage deed should be accompanied by a multilateral inquiry into the practice of other states where this concept has been introduced and a legal practice exists.

II. The Civil Procedure Code (No. 225-XV dated 30 May 2003), and the regulations on enforcement of court judgements of the 1964 Civil Procedure Code\(^2\). The judicial procedure of enforcing a mortgage encompasses two consecutive stages: (1) forced hand over of the property to mortgagee, and (2) forced sale.

2.1. For the forced dispossession of the owner of a mortgaged property a simplified (ordinance) procedure is provided for - regulated by Chapter XXXV of the 2003 Code. The ordinance procedure is different from the litigation procedure and does not contemplate a contradictory proceeding, its parties being a debtor and a creditor (rather than a plaintiff and defended as under the litigation procedure). The court order (i.e. an ordinance) is being passed after the matter has been examined, with no subpoena to the parties for delivery of explanations, no judicial debates, and no minutes to be executed. An ordinance is issued 5 days after the creditor’s application is registered. A copy of the ordinance is being sent to the mortgagor, who may appeal against it by making justified objections to it within 10 days. Where he accepts the debtors’ objections, the judge avoids the ordinance under an order which may not be appealed against in any way whatsoever.

In contrast to the procedure laid down under Law 449/2001, the ordinance procedure is much more defective and has an abundant number of flaws, which we will bring forth, and propose remedy proposals thereto:

- the requirement for the application addressed to the court to specify the value of the property is an unjustified requirement and may lead to the false understanding, largely met in practice, that a monetary claim has been asserted. As a result a stamp duty is applied to the application calculated pro rata the value of the purported claim. This is contrary to the nature of the creditor’s request - who only seeks to authorize a legal act - handing over the property to the creditor. The requirement of specifying the property’s value in the application and the ordinance should be removed, and the size of the stamp duty - fixed.

- the notification to the mortgagor about the ordinance should be permitted by any communication means allowing for a proof of receipt to be procured. The current requirement (registered letter by the court) does not allow the mortgagee, who is the party most interested in the ordinance being received by the mortgagor, to hand it over to him personally; and there are cases where using the latter communication means is treated as contrary to law.

---

\(^2\) Pursuant to Article 2 of Law on the Entry into Force of the Moldovan Civil Procedure Code No. 227-XV dated 5 June 2003, the Civil Procedure Code dated 26 December 1964 has been repealed, save for regulations pertaining to enforcement of court judgements. Those regulations will be substituted by the ones set by the new Execution Code, which came into force on July 1, 2005.
the law should clearly and exhaustively provide for the cases where a court may accept the debtor’s objections and avoid the ordinance. The current scheme (“justified objections”) may be subject to arbitrary interpretation and may seriously hinder the creditor’s interests.

Under an order, which is neither provided for, nor is stemming from, the law. For the avoidance of confusions, the law should clearly state that a judge will consider, under a judicial act (an order), only the justified objections of a debtor. Alternatively, the law may provide - the law fails to lay down the court’s steps when it considers the debtor’s objections as not properly justified. In practice, judges dismiss that when it considers the objections not being property justified, a court may dismiss them under an order, which may not be appealed against. In any case, the law will set forth a deadline when the court should decide.

2.2. Judicial sale of the mortgaged property - is regulated by both the 1964 Civil Procedure Code and the Pledge Law. Because of the inconsistency between the nature of these two regulations, the procedure of judicial sale of a mortgaged property is extremely defective and hardly practicable. Even more so, there are two different procedures to this: sale under the supervision of the court (regulated rather summarily by the Pledge Law) and sale by the judicial enforcer (under the 1964 Code).

To this effect, the following improvements should be made:

- the cases when a property is to be sold under the supervision of the court should be clearly provided for by law (in case of houses inhabited by children or disabled individuals; when the mortgagor is missing and may not be notified; at the request of the mortgagee);
- upon the request of the mortgagee, the court will appoint a specialized entity which will organize and sell the property, being under an obligation to report before the court about any steps undertaken, including the sale, and to collect the proceeds of the sale and to draw-up a proceeds distribution sheet;
- the court will approve the result of the auction under an order, which will serve as basis for registering the purchaser as the owner of the property.

III. Property Law and other laws regulating the legal status of private property.

3.1. Property Law No. 459-XII dated 22 January 1991 has been the first statute to have established the legal foundation of types of property (including private), the owner’s powers (possession, use, and disposal), the object of private property, and how it may be exercised. Land plots and houses are referred to as property which may be owned by natural persons, and providing that a person may freely dispose of its property. The evolution of both economic and social relations have led to a part of such Law’s provision being tacitly repealed by other laws or becoming simply inapplicable. Now a fundamental review of the law is needed, preferably by way of adopting a new law.

3.2. The Land Code (No. 828-XII dated 25 December 1991) regulates the legal status of ownership over land plots; the types of land plots (agricultural, land plots located either inside or outside a location, special purposes land plots); how are land plots allocated and disposed of; the rights and obligations of holders of land plots; change of a land plot’s purpose (i.e. transfer from a category to another); land monitoring and registration; and the resolution of land related disputes.
Pursuant to Article 11 of the Land Code, land plots on which natural persons build houses are allocated free of charge, while any other type of plots may be obtained only subject to consideration under a public auction. Contractor companies may be allocated public property land plots for use.

Under the law, ownership is certified by an agreement (sale, donation, exchange), inheritance certificate, or a Title Certifying the Right of a Land Plot Holder. The latter is executed both in case of ownership and use under any other legal basis (lease etc.) over land; however, the law fails to indicate explicitly the cases when such Title is an ownership certifying document.

Another legislative vacuum, which should be filled in, relates to the procedures of letting on lease public property inside the limits of a locality. This procedure should be explicit and transparent in order to insure a protection both of the interests of the Government, and of potential tenants. When a construction changes owners, including by enforcement for a debt, the new owner will subrogate the initial one in his rights over the land plot.

3.3. Law on the Normative Price and Sale and Purchase Procedure of Land No. 1308-XIII dated 25 July 1997 contains general rules on the fixing of the normative price of land, computed based on tariffs per a degree-hectare unit, dependent on the land plot’s designated purpose. The law further provides for the procedure of sale of public property land plots, which may procured by both national and foreign natural and legal persons, save for agricultural and forestry lands, which may only be purchased by local investors. Any land plot for purposes of building a personal house exceeding the statutory limit (0.07 ha. in case of cities, and 0.12 ha. in case of rural locations), as well as land plots related to existing constructions are sold under a normative price, which, however, differs for each of these cases. The sale of public property land for the purposes of erecting a new construction takes place only under a competition or auction.

The most controversial and disputed legal provisions are those referring to the tariffs applied when fixing the normative price, which may differ by tens of time even in case of properties of the same category. Likewise, some rules on the procedure of fixing the sale price in case of auction of lands for new constructions are to be established with a view to allowing potential investors to plan their project budgets.

3.4. The Law on the Principles of Urban and Territorial Planning No. 835-XIII of 17 May 1996 lays down the basic principles for efficient urban planning and management. Local public authorities have the task to approve the urban development plans (general, zonal, and detailed plans) and establish basic urban regulations with a view to ensuring the efficient use of urban land. The documents subject to which buildings may be constructed and used include:

- certificate of urbanism, authorizing the location and structural design of constructions,
- construction permit, authorizing construction work execution, and
- utilization permit, which is issued after work is completed and authorizes the use of a construction in compliance with the urban documentation and applicable regulations.
Law-subordinated regulations provide for the procedure of issuing the aforementioned permits, and such regulations should be reviewed so as to reduce the time and effort necessary for their receipt. The purposes of the review are to remove legal and bureaucratic barriers before contractor companies, on one hand, and to insure government control over compliance with the obligations stemming from the urbanism documents, on the other.

3.5. Law on Dwelling Condominium No. 913-XIV dated 30 March 2000 lays down the proprietary relationships in a condominium, which is defined as a pool of immovable property including land and living blocks, where one part (i.e. dwelling and other premises) are of either private or public property, and the remainder is a divided co-ownership. A condominium is established on the terms of a compulsory association of co-owners and includes a building, a part of building having a separate entrance or several buildings, as well as appendixes, sidewalks, roads, and parking lots. Co-ownership also exists over the land on which such condominium components are located, which is conveyed to the co-owners free of charge. A condominium is managed by the owners themselves in case it includes not more than four dwelling premises, but otherwise is managed by a home owners’ association (HOA).

The law operates both with the concept of ownership of the co-owners and ownership of the association, which leaves an impression that an association may hold its own property. The rule providing that a purchaser is subrogated in the rights and obligations of the previous owner is not clear enough as to include the rights and obligations related to the immovable property. While a clause that the purchaser is obligated to settle the outstanding debts for public utilities incurred by the previous owner are discriminatory and interfere with the general rules of the law of obligations. The rule whereunder a general meeting of co-owners may change the size of a co-owner’s share in the condominium may only be described as a limitation of private property; the same applies to the rule proving that premises may be altered under a decision of the association rather than its owner.

The removal of this and other contradictions would enable an adequate balance between the rights of co-owners of dwelling and the general interest.

3.6. The Civil Code No. 1107-XV dated 6 June 2002, in force as of June 2003 is the most recent piece of legislation containing detailed regulations on ownership and other real rights (jus in rem). The concept of immovable property and its components are defined; the legal basis of acquisition of ownership are listed and described. The contradictions related to the link between land plot and construction have been removed, and a set of distinct rules on the lease of agricultural property (arenda) and of other property (locatiunea) have been established. Explicit rules on the exercise of both the divided and non-divided co-ownership have been provided for; the latter is applicable between spouses (any property acquired by the spouses during marriage is presumed to be common, and any act of disposal of immovable property, including mortgage, must be executed by both of the spouses). For the first time have several real rights over immovable property (including servitude and superficies) been regulated and conceptual rules on entries into the Registry of Immovable Property - instituted.

Notwithstanding that an in-depth analysis of the issues arisen in practice related to the application of the new Civil Code is not yet possible, because the period it has been applied is still rather short, the following drawbacks of its rules are worthy of being underlined: - illegality of an agreement by which the entire patrimony is transferred - Article 674, which may pose a problem for mortgage of future property;
• the category of property to which unfinished property and rights in it relate to;
• the requirement as to the form of the agreement for the sale and purchase of an immovable property;
• whether the holder of real rights other than property may benefit from the proprietary legal remedies.

Up to the point when these and other contradictions are to be resolved, the legal situations falling under their scope will be governed by the general principles and trends of civil law.

3.7. Law on Formation of Immovable Property No. 354-XV dated 28 October 2004 sets forth the cases and the procedure of formation (i.e. by legal steps) of immovable property, and for the first time includes unfinished constructions in it. Some types of immovable property may appear by way of separation (split-off of a part), division (partition at co-owners’ request), merger (amalgamation of two or more properties), and a manner previously not provided for - combination of properties - by separating a part of an immovable property and adding it up to an adjacent property. An immovable property may be formed at the request of the owner or another holder of real rights subject to the owner’s approval. It includes the stages of carrying out a feasibility study; development of the project of formation of the property; execution of the plan of the newly formed property; issuance of the decision to form; and the government registration of the formed property.

Having regard to the fact that such procedure is rather complex, the law should provide for maximum deadlines for each of the stages and the entire formation process in general. Amendments leading to the protection of lawful interests of third parties who may be affected by the formation of an immovable property (neighbours, holders of real rights, etc.) should be made. The obligations of the relevant public administration agencies involved in the co-ordination of the project of the formation of the immovable property should be clearly outlined.

IV. The Immovable Property Cadastre Law No. 1543-XIII dated 25 February 1998 (hereinafter referred to as - Law 1543/1998) - has established a general uniform system of identification, registration and monitoring of all land plots and other immovable property, regardless of their use and owner (either Moldovan or foreign citizens, legal entities, international organizations, administrative-territorial units, the Republic of Moldova, and other states). All immovable property, property rights and other patrimonial rights (including economic management, permanent use, lease for more than three years, freehold, fiduciary administration, servitude and mortgage) are subject to compulsory registration with the Registry of Immovable Property. The institutional framework is made up by the State Agency for Land Relations and Cadastre, as the coordinating and supervisory body, and territorial cadastral offices, directly in charge of establishing and managing the Registry of Immovable Property. The Registry is open to the public and anyone may access its records under the statutory procedure.

To speed up the compilation of the Registry of Immovable Property, a Government Programme was established (Government Decision No. 1030 dated 12 October 1998), which lays down the actions undertaken for the creation of the cadastre, rules for primary massive registration of immovable property and the rights and duties and responsibilities of officials who act as registrars.

Tariffs for registering the immovable property and rights therein, including mortgage, are established by Government Decision No. 718 dated 20 July 2000.
The aforementioned statutory acts have established a legal framework sufficient for the registration and exercise of rights over immovable property. Notwithstanding this, they may be improved as follows:

4.1. Law 1543/1998

- provides that immovable property is subject to registration, without specifying that unfinished construction may also be registered. For the cases where the owner of an unfinished construction (which is the holder of ownership or right of superficies over the land plot) wishes to mortgage the construction, the law should allow and regulate how such property is to be identified. Its inclusion in the cadastral plan and file, and the subsequent issuance of an extract from the Registry to the owner of the construction should also be dealt with;

- should contain a procedure of simultaneous registration of both title of ownership and mortgage, applicable in case of purchase of immovable property with the proceeds of a mortgage loan;

- fails to co-ordinate the mortgage inscription (Article 44) with the contents of the relevant subchapter of the Registry (Article 24);

- should expressly prohibit registering change of owners or repeated mortgage when this has been prohibited by the mortgage agreement;

- should provide for a clear procedure of registration of apartment buildings and other immovable property upon finalization of the construction, as well the procedure of registering the purchasers of apartments and other dwelling premises as their legal owners.

The Law should be supplemented by rules on the right to and procedure of accessing the Registry’s information by interested parties (banks and other credit institutions) through modern telecommunication means (electronic networks), subject to a contract being executed and a consideration paid.

4.2. At present the procedure of registering a mortgage is similar in all its respects to the procedure of registering title: basis, period of time, and price. A legal improvement may take place by setting a shorter period for the issuance of the extract from the Registry and for the mortgage being registered (preferably in the very day of the application, as in the case of pledge over movable property). It may further be done by reducing formalities and tariffs applied (pursuant to a recent study costs related to the transfer of ownership accounts for 6.56% of the average salary, while in the European Union Member States the average rate is 3.98%).

4.3. The registrar’s responsibility for any damages is not sufficiently regulated at present. Moreover, the existing procedure of recovering damages is extremely cumbersome and ineffective, discouraging the damaged parties to have recourse to it and favouring a considerable number of premeditated breaches on the part of registrars.

V. The Notary Law No. 1453-XV dated 8 November 2002 defines a notary as being a person authorized by the state to render on its behalf public services for the purposes of safeguarding the rights and lawful interests of all persons and the government. Private notaries act under the principle of self sustainability and appropriate any income gained as a result of executing notary acts, while state notaries are on the pay roll of, and equipped by, the government. In exchange they disburse all their income to the government. Two costs for notary services are incurred: state tax, as provided for by law, and the notary’s fee (the actual consideration for services). The notary’s fee is computed under the terms set out in a Law No. 271-XV dated 27 June 2003.
We should mention that, notwithstanding a number of amendments to the notary law, it still contains several shortcomings in the following areas:

a) Notary’s role and competence at creation of the mortgage. The notarization of a mortgage agreement implies the notary’s obligation to clarify to the parties the purpose and importance of the agreement, to verify whether the contents of the agreement is according to law, and that it corresponds to the parties’ real intention. The obligation to verify whether the contents of the agreement is according to law is in fact overlapping the obligation of the cadastral registrar who, when registering the mortgage, must dismiss the registration application if the form or contents of the documents produced before him are not according to law (Articles 32 and 33 of the Law 1543/1998). The obligation to explain the importance of the agreement seems rather superfluous, and the requirement that the notary verify whether the contents of the agreement corresponds to the parties’ real intention is nothing but an infringement of the principles of freedom of contract and respect of private affairs, embedded with Article 1 of the 2003 Civil Code. Hence, the role of a notary at the entering into a mortgage agreement should be reviewed; in contrast to this, notarization is not required when creating a pledge by operation of law. One of the possible solutions in this context would be to replace the requirement of notarizing the mortgage agreement with requiring another notary act to be executed - legalization of signatures applied on the agreement.

b) Documents presented for the notarization of the mortgage agreement. Currently, in addition to the agreement and extract from the Registry, the parties have to produce a burdensome number of documents with a view to allowing the notary to fulfil its obligations related to the notarization of the agreement (verify the capacity to act, authority of representative, compliance with rules on large transactions, no outstanding tax obligations, etc.). In fact the notary largely, if not in its entirety, doubles the due diligence undertaken by the contracting parties, and banks in particular. It is obvious that in case of the abandonment of the notarization requirement, such documents will no longer have to be presented.

c) Notary costs - are currently made up of two components: state tax, which is a levy for the notary’s public service, and the notary’s fee, computed under the terms of a Law 271/2003. We should note that the first component - state tax - has been recently introduced (i.e. 2002), without being thoroughly justified, and in case of state notaries - is confusing (two levies are charged - state tax and notary’s fee - which have the same content). As regards the second component - the notary’s fee - it is not clear whether it should be computed in a fixed amount or variable amount, dependent on the value of the property. Whereas the value of the mortgage is not a term essential for the conclusion of the agreement (Article 13 (4) of the Pledge Law), the application of a fixed fee seems the adequate option. In practice, however, notaries compute their fee based on a certain percentage from the mortgage’s value, requiring that this value be inserted into the agreement (making a reference to Article 468 (4) of the Civil Code, which requires that the agreement provide an estimate of the pledged property’s value). Should the

---

3 The initiative of the Russian lawmakers is particularly relevant here. Russia has abandoned the requirement that the mortgage agreement be notarized for the same reasons as listed above (Mortgage (Amendment) Law No. 216-FZ dated 20 December 2004).
requirement of a notarized mortgage agreement be dropped, the problem will disappear by itself.

d) Notary’s liability for damage to the contracting or third parties. This is a matter avoided both in the law and in practice, but raises the questions about the purpose of notary’s fee. The law should be supplemented with rules on the formation of an indemnification fund for the liability of notaries, the size of contributions, and the procedure of claiming damages from the fund.

VI. Statutory Regulations on Consumer Protection - in case of the mortgage relationships, these are contained in several laws.

In its chapter related to the loan for consumption and bank loan the Civil Code sets forth rules on the liability for breach of the obligation to lend (Article 868); requirement that the interest rate be in a reasonable relation with the refinance rate (Article 869), while in the case of the bank loan - to abide by the principle of fairness and to give the debtor prior notice about changes in the interest rate (Article 1237). A debtor is protected from a suspension or cancellation of the loan, is entitled either to refuse a loan or to reimburse it before maturity, subject to compensation of creditor’s losses.

The Financial Institutions Law No. 550-XIII dated 21 July 1995 prohibits financial institutions to make the provision of financial services, including loans, contingent on the purchase of other goods and services either from itself or its affiliates (Article 27). It is also prohibited for a financial institution or any other entity to manipulate the market so as to obtain unfair advantages.

The Consumer Protection Law No. 105-XV dated 13 March 2003 makes it an obligation of suppliers to completely, correctly and precisely inform about the characteristics and prices of goods and services offered to natural persons, so that the latter would have the chance of making a reasonable choice. Any contractual clause which has not been negotiated directly with a consumer or which creates a significant unbalance between the rights and obligations of the parties is deemed unfair. Any clause limiting the liability of a service provider or which is to the detriment of the consumer or contrary to good faith are null and void. We believe that, along with the general rules of consumer protection, specific protection instruments for those purchasing dwelling premises with the proceeds of a mortgage loan are needed. These relate in particular to the following:

- pre-contractual information for the applicant about the terms and conditions of the loan, including price. The subject is of major importance thus making the mortgage industry to include into the European Code of Conduct for mortgage lenders requirements to the information they must provide to the borrowers. Such information includes the way of calculation of APRC (Annual Percentage Rate of Charge) to standardize the product pricing and allow consumers to compare offers,

- protection of the participants to the construction of an apartment building. There is no law (nor a chapter in the Civil Code) that would regulate the construction of dwelling with the financial contribution of the future owners of the premises (laws on the subject have been passed in Ukraine in 2004 and the Russian Federation - at the beginning of 2005). There is no statutory obligation of the contractor to disclose information on its activity and how the construction project is implemented. Because the legal relationship between the contractor and financer-natural person is not regulated, the latter remains unprotected in cases where the apartment building is
enforced against for contractor’s debts. These and other issues should be on the forthcoming agenda of the lawmaker, as they serve as serious obstacles to construction of dwelling.

- eviction of those who fail to repay their mortgage loan - is also a topical problem. Under the current rules, an owner of a property enforced against together with all other inhabitants is to be evicted without receiving another dwelling. This rule makes them use any means of protection in order to avoid this negative consequence, and leads to an increase of both loan risk and price. In order to remedy the situation, the Dwelling Code should be supplemented with rules on the creation of a special eviction fund, made up from public property premises (constructed under the government building investment programmes or vacated by tenants having purchased apartments, including under a mortgage loan). The premises of the special eviction fund will correspond to the minimum dwelling standards and will be allocated to the individuals who failed to repay their mortgage loan. The Government acknowledged that the special eviction funds are an intrinsic institutional component of the mortgage loan system (Please see: The National Social Programme “Dwelling Allocations and Loans for the Years 2003 to 2008”, approved under Government Decision No. 422 dated 8 April 2003).

VII. Tax Treatment

The income tax, value added tax, and real-estate tax are those which, either directly or indirectly, relate to the tax treatment of constructions of dwelling, real-estate transactions, or mortgage loans. The Tax Code (Titles II, III and VI, respectively) regulates these taxes.

Natural persons pay taxes on their professional or business income, from which non-taxable incomes and a personal exemption provided for by law are deducted. Unlike companies, natural persons may not deduct the costs related to the acquisition of capital assets, including dwelling, from their gross income. Costs related to the repayment of loan principal and interest or those related to construction and reparation of immovable property are also not deductible.

The capital gain, defined as the difference between amounts received from the sale of capital assets and their value basis, is taxable at a rate of 50% from the income tax rate. Rules relating to computation and adjustment of the value basis of apartments privatized or otherwise acquired before the entry into force of the Tax Code (i.e. 1 January 1998) are not clear enough. The procedure of calculating the taxable income in case of donation of property is debateable. The amount which the capital gain in case of sale of the main dwelling is decreased with should be adjusted to reality.

Commercial banks are exempt from income tax on loans exceeding 3 years (50% - for loans between 2 and 3 years), granted for investments into fixed assets, contractor works, and engineering services (Article 24 (14) of the Law on the Entry into Force of Titles I and II of the Tax Code No. 1164-XIII dated 24 April 1997). Income from interest obtained by resident natural persons under bank deposits, money market securities and contributions to loan associations are exempt from tax until 2010.

Value added tax applies to supply of goods and provision of services, and to the imports of the same. Sale and lease of dwelling and related land plots; financial services, including grant and assignment of loans; public utilities, are all VAT
exempt. Contractor works for dwelling buildings, including under mortgage loans, are subject to zero rate where such are included into special purpose programmes approved by the public administration.

Real-estate tax is levied on all immovable property, including buildings which are at least 80% finished and have not been finished 5 years since construction began. The tax is computed based on the estimated value of the property, as established by the local cadastral offices under classic evaluation methods (comparative analysis of sales; costs and income methods). Tax exemptions are granted by operation of law and by the decision of the local administration - in several cases provided for by law.

Uniform tax regulations, increase transparency of the taxation system, improvement of tax administration are all general recommendation with respect to the taxation system. In addition to these, the following specific proposals may be added:

- fairness in the matter of deducting costs, by reducing the taxable gross income with the amounts paid by natural persons for construction, purchase, and reparation of immovable property, repayment of mortgage loans and payment of interest;
- establish a taxation system favourable to the circulation of mortgage securities, by exempting the interest thereunder from the income tax;
- extend tax incentives of banks granting investment loans to mortgage loan institutions;
- subject to a zero rate VAT not only works for building houses which have been included in special programmes, but rather all works of this kind;
- motivate natural persons who build or acquire dwellings under loan mortgages with tax levarages (e.g. temporary exemption from real-estate tax). (Cf. - in Romania a 10 years’ exemption is granted, please see Government Ordinance 36/2003).

VIII. Other necessary regulations must be enacted to regulate the following matters:

8.1. Who May Grant Mortgage Loans. The existing legal framework reserves the right to grant loans only to financial institutions, defined as entities which attract deposits or non-transferable equivalents of such, and use them for loans or other placements (Article 3 of the Financial Institutions Law). It is not quite clear whether companies granting loans from other sources (e.g. own equity) also fall in the scope of this definition. It is also uncertain if the National Bank of Moldova authorizes financial institutions other than banks. These matters should be addressed with no delay in order to insure that all mortgage lenders benefit from the rules currently applicable to financial institutions with regard to currency regulations (have the right to grant foreign currency loans), accounting (bookkeeping of operations), and taxation (creation of loan risks reserves and deductible reserves). 4

4 It is worthwhile considering the experience of Romania, where mortgage loan companies have to notify the National Bank about their incorporation and report quarterly to it the structure of their loan portfolio (Government Urgent Ordinance No. 200 dated 18 December 2002). The requirements applicable to mortgage lenders (banks and other companies), including with respect to the internal
8.2. Disclosure of Information on Borrowing History. The lenders’ access to correct and full information on loans previously contracted by applicants, including defaults, would reduce the time necessary for lender decision-making and would reduce the related risk, and therefore the price for loans. Although the Moldovan business community has been discussing the feasibility of establishing loan bureaus for some years now, until today there is no agreement on the information transmitted to loan bureaus and its disclosure to beneficiaries. There is also a discussion on the feasibility of a separate law which would regulate all the aspects related to the establishment and activity of loan bureaus (following the examples of Ukraine and Kazakhstan) or whether it is sufficient to amend the existing commercial secret and financial institutions laws. Regardless of the drafting technique chosen, the availability of the borrowing history and, in particular, the previous contractual breaches are matters of a general interest to all lenders and should be dealt with in a timely manner.

8.3 Enforcement of Mortgage Security in case of debtor’s Insolvency. The Insolvency Law No.632- XV dated 14 November 2001 sets forth that any property, including rights of claim, subject to a pledge may be applied by the insolvency administrator who will take into account the pledgee’s proposal to hand over the property to him. After hearing both the pledgee and the administrator, the court will fix the period of time in which the pledged property is to be sold by the pledgee; after it has expired the administrator is authorised to apply the property (Article 128).

This procedure disadvantages the pledgee, to whom legal barriers – endangering his enforcement of the pledge - are created. The removal of these barriers by allowing the pledgee to enforce the pledge under the general rules would reduce legal uncertainty, motivating lenders to accept as security the mortgage - on the primary market- and the pledge of mortgage claims as collateral for mortgage securities - on the secondary market.

Conclusions

Considering the afore mentioned legal analysis, we may conclude that the national legislation contains a significant number of legal rules on the appearance, amendment, and termination of ownership and mortgage over immovable property. Ownership over an immovable property arises as of its entry into the Registry of Immovable Property. Other real rights and legal facts with respect to a specific property are also entered. An owner may freely dispose of its property, including create a mortgage over it for the purposes of securing his or any third party’s obligations. The limitations, terms and conditions of the exercise of owner’s powers over a mortgaged property are provided for by law and by the agreement.

Rules regarding mortgage are contained in the Pledge Law and the Civil Code. There is no special law regulating mortgage, mortgage loans, and circulation of mortgage securities.

procedures for extending loans; the documents produced by the applicant; granting and monitoring the loan, are all matters regulated under a common regulation of the National Bank and the National Securities Commission (Methodological Rules on the Application of the Real-Estate Investments Mortgage Loans Law, Rules No. 3 dated 17 April 2000).
In order to accelerate the mortgage loan process, the lawmaker should review the legal rules dealt with above in this paper, and additionally to establish new regulations referring to:

a) the circle of subjects who may grant mortgage loans and requirements applicable to them;

b) the re-finance of mortgage lenders applying the methods that have passed the international practical expertise:

- assignment of mortgage claims either directly or by conveying the title certifying the claim;
- pledge over mortgage claims;
- issuance and circulation of mortgage securities on the secondary market;

c) the procedure of issuance of mortgage securities, including:

- consolidation of claims of the same kind (loans secured with certain mortgages) and establish a minimum amount of the pool of mortgage claims;
- issuance of mortgage bonds (mortgage covered securities) and mortgage certificates (participative securities) by loan institutions and the secondary market operators;

d) the trust administration of mortgage assets by asset management companies;

e) stimulate the circulation of mortgage securities and create a related institutional infrastructure; motivate institutional investors in placing available funds in mortgage securities;

f) government supervision and regulation of the participants of the secondary market of mortgage securities.

Considering that there are no mortgage loan and mortgage securities regulations on a pan-European level, both the experiences of the countries where these concepts have a certain history, and those of the countries where the first steps from centralized towards a market-oriented dwelling financing system are undertaken are to be appraised.

The European model of the secondary market of mortgage securities and its operators significantly differs from the Anglo-Saxon model. Hence, in order to avoid creating an inefficient local model and to identify the best scenario for the Moldovan secondary market of mortgage securities, it is vital to undertake a complex study. It would consider both the elements of each of these models, and the achievements and failures of other South-Eastern European countries having an experience with legal rules regarding mortgage loans.

The mortgage loans related regulations of the European Union apply to the solvency of banks (capital adequacy rules, large exposures, deposit guarantee, etc.) and consumer protection (on consumer lending, the annual percentage rate of charge (APRC), distance selling, unfair terms in consumer contracts, etc.). In addition, the European Commission has endorsed the code of conduct adopted by the mortgage industry, which standardizes consumer information and helps prospective borrowers compare mortgage offers.
Recommendation:

In a nutshell my opinion based on my research is that new legislation relating to mortgage, mortgage lending and mortgage securities should be drafted, preferably in the form of new law(s). Such an approach will (i) be consistent with Moldovan law making principles, set forth in Article 72 of the Constitution (ii) help overcome the existing collisions amongst various relevant laws and (iii) create a consistent, clear and comprehensive legal framework for mortgage related topics.