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UNDERSTANDING INSTITUTIONS AND INSTITUTIONAL CHANGE IN WEAK POST-SOVIET DEMOCRACIES: The Cost of "Doing Business" Reforms in Moldova

by Olga Nicoara

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ABSTRACT

The 2010 World Bank "Doing Business" study ranks Moldova among the top 10 reformers out of 183 countries under annual evaluation. The success is attributed to a number of new policy reforms started in 2009 that aim to simplify the existing administrative processes of business formalization. However, like several other transition democracies, Moldova lacks the institutional foundations to support beneficial reforms, a fact illustrated in recent quantitative and qualitative country studies revealing a poor economic performance, lasting high levels of corruption, massive out-migration, decreasing media freedom, and frequent electoral protests and political blockades. Accordingly, the accuracy of the World Bank evaluation of the entrepreneurial environment in Moldova is questionable. The list of reforms seems to be a mere quantitative expression of the institutional change. In fact the recent "Doing Business" study seems to fail to consider the Moldovan reforms in light of the quality of the underlying institutional arrangements and their dynamics affecting the entrepreneurial environment. To correct this fault, the World Bank assessments of reform achievements should aim at a better understanding of institutions and institutional change in Moldova, and future reforms should address the causes of existing weaknesses in the institutional framework.

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Understand Institutions and Institutional Change in Weak Post-Soviet Democracies:
The Case of “Doing Business” Reforms in Moldova

Mercatus Policy Essay

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Any remaining errors or misinterpretations are my own.

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1. Introduction

More than six years after the World Bank first launched the "Ease of Doing Business" study that correlates reduced bureaucratic barriers to entry with economic development (Djankov et. al., 2002), it continues to receive a wide recognition for its efforts on both international and national levels. Governments around the world compete to improve their scores and ranks[1] in the organization's annual "Doing Business" (DB) studies[2] by implementing regulatory and fiscal reforms aimed at simplifying barriers to entry, and with that, improve their countries' entrepreneurial environments. The World Bank researchers monitor and measure participant countries' successes and failures and promote the top reformers in publications and conferences worldwide. Accordingly, the DB simplification reform achievements are typically classified by the World Bank as beneficial to entrepreneurship and therefore, recognized by the international community as necessarily a sign of promising future economic growth and prosperity.

In "Doing Business 2010: Reforming through Difficult Times"[3] Moldova ranks among the top ten reforming countries, or the top ten performers. This achievement is attributed to a number of new policy reforms started in 2009 that aim to simplify the administrative process of business formalization. However, similar to other transition countries with shaky institutional foundations, Moldova falls into the category of "weak

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[1] The World Bank annual **"**Doing Business" study ranks economies based on 10 indicators of business regulation that record the time and cost to meet government requirements in starting and operating a business, trading across borders, paying taxes, and closing a business. The rankings do not reflect such areas as macroeconomic policy, security, labor skills of the population or the strength of the financial system or financial market regulations. http://www.doingbusiness.org/features/Highlights2010.aspx

[2] Henceforth for key concepts such as "the World Bank Doing Business policy reforms," "the World Bank Doing Business studies," and "Doing Business indicators," I will use abbreviations as follows: "DB reforms," "DB indicators," and "DB studies," etc.

[3] http://www.doingbusiness.org/Documents/CountryProfiles/MDA.pdf

democracies"—an institutional handicap that casts doubt of the efficacy of any beneficial reforms.

The fact that Moldova lacks strong institutions to support these reforms is illustrated by a long history of increased levels of corruption, high levels of out-migration, decreasing freedom of the media, a poor economic performance, and frequent electoral protests and political blockades. Consider that almost 20 years after independence, Moldova receives the World Bank's international endorsement for its achievements in improving local doing-business conditions by simplifying registration procedures, cutting red tape, and eliminating corporate tax rates. Curiously, at the same time, Moldova is plagued by increasing corruption, lags significantly behind other comparable countries in the region, has limited media freedom, and local entrepreneurs often complain about unofficial forms of public predation. These conflicting indicators beseech a question: given Moldova's institutional weaknesses, how reliable are the World Bank's assessments of the impact of DB reforms?

Primary Findings

Contrary to World Bank experts' optimistic assessment, I question the validity of Moldova's recently claimed DB reform successes. Because a significant gap exists between the Moldovan government's *de jure* and *de facto* commitment to market reforms, I argue that the World Bank assessments of the impact of recent DB reforms on entrepreneurship and development is overestimated.

Officially, Moldova seems to be making progress toward liberalization, reduction of red tape, and thus improving its scores in the annual DB studies. Unofficially, under the opportunistic ruling of the Communist Party of Moldova, the same DB simplification achievements seem to have been paralleled by new and covert practices of tax collection or expropriation. Formal DB studies and indicators do not capture these new predation practices, which threaten to offset beneficial reform takings. The extent of the cost on doing business in Moldova created by the corrupt fiscal and regulatory practices, and the amount of unofficial taxes and contributions accrued to public officials are hard to capture in formal international indexes. Thus, the unseen gap between the *de jure* and *de facto* institutional constraints on public predation in Moldova causes DB reports to promote an overestimated impact of the recent DB reforms. Informal/unofficial barriers to doing business in Moldova are of particular concern for policy makers and development as they come to counteract legitimate efforts for beneficial reforms. At the heart of this problem lie weak constitutional rules that allow the political actors to renege on their policy commitments by partaking in *ex-post* opportunism in the form of unofficial public taxation, corruption, and authoritarian governance. These preliminary insights support my hypothesis—in reality, international assessments tend to overestimate the impact of DB reforms in post-Soviet countries like Moldova. As I will present in the following sections, the weak institutional arrangements in Moldova have allowed the coexistence of an unofficial (*de facto*) system of taxation, which offsets the beneficial function of the official (*de jure*) tax cuts and other DB simplification measures implemented so far.

My critique attempts to expose the gap between the seen and the unseen consequences of DB reforms generated by Moldova's weak institutional context. More specifically, my hypothesis is that the World Bank experts exaggerate the successes of the recent DB reforms in Post-Soviet Moldova because they fail to perceive and account for the public actors' ability to exploit the weaknesses in the official/formal institutions, and the evasive profit opportunities that private individuals are able to pursue by partnering with corrupt public actors. In this essay, I am particularly concerned with those institutional weaknesses that stimulated the manifestation of covert forms of public predation.

Methodology

This policy essay explores the measurement problem inherent in DB studies on Moldova's entrepreneurial environment and takes the form of an analytical narrative combining three main analytical tools: 1) the theories addressing the measurement problem in institutional change and development in weak democracies, 2) the qualitative insights from my fieldwork on barriers to entrepreneurship in Moldova, and 3) the quantitative assessments of Moldova's entrepreneurial and institutional environment as developed by international organizations, such as the World Bank, Transparency International, Freedom House, the Heritage Economic Freedom Index, the American Center for International Private Enterprise (CIPE), the National Bureau of Statistics of the Republic of Moldova, Committee to Protect Journalists (CPJ), Central Intelligence Agency (CIA), Economist Intelligence Unit (EIU), Reporters Sans Frontiers (RSF), and the World Trade Organization (WTO). Combining these three tools of analysis provides a better understanding of the measurement problem at hand and what can be done to avoid repeating it in future reform impact assessments.

Following the insights from previous fieldwork on barriers to entrepreneurship in Moldova (Nicoara, 2009[4]) and a recent study evaluating the system of "unofficial taxation" in Moldova (Lariushina et al., 2006), I find that the World Bank DB studies overestimate the successes of the regulatory reforms in post-Soviet Moldova. The evidence gathered from Moldovan economic actors could lead to a significantly improved institutional assessment. Moreover, a qualitative analysis based on interviews with local entrepreneurs, as opposed to relying only on the quantitative assessments made by the World Bank, provides a closer look into Moldova's everyday institutional reality.

Exploring this topic during my fieldwork in Moldova, I aimed to incorporate the local knowledge relevant for the understanding of the problems faced by Moldovan entrepreneurs. Insights from local individuals' institutional experience are vital for identifying the real impact of DB reforms that are not captured anywhere in known national and international databases. Therefore, in this analytical narrative, I use interviews from my field research to illustrate the gap between the *de jure* institutional barriers to doing business in Moldova (as perceived by international reformers) and the existing *de facto* institutional barriers (as perceived by local entrepreneurs and experts) not accounted for in DB studies. My fieldwork in Moldova consisted of 19 interviews with entrepreneurs from the municipal area of Chisinau, conducted in June 2009. As part of the standard interview structure, I asked entrepreneurs about their difficulties with starting their businesses, doing business, their experience with government authorities, and what they consider major threats to their activity. According to my fieldwork findings, the main barriers to entrepreneurship in Moldova are: (a) formal and informal

[4] In June 2009, I conducted a field research on barriers to entrepreneurship in Moldova, Chisinau. The results were incorporated in the paper: "Institutions, Entrepreneurship, and Development: An Evaluation of Moldova's Entrepreneurial Environment."

taxes, tariffs, restrictions, fees, and fines on profitable activity; (b) frequent changes in rules and regulations; (c) lack of transparency and accountability in public bureaus; and (d) public officials' ability to abuse their position for personal interests.

The second section of this policy essay is an overview of Moldova's institutional context. The third section provides an overview of the literature exploring the institutional problems inherent in weak democracies and the possibilities for beneficial institutional change and development. The fourth section discusses the lessons from Moldova's experience with Doing Business reforms in 2010, and shows how these insights can help understand the difficulties in assessing institutional change. The fifth section presents policy implications and opportunities for further research. The sixth section concludes.

2. An Overview of Moldova's Institutional Context

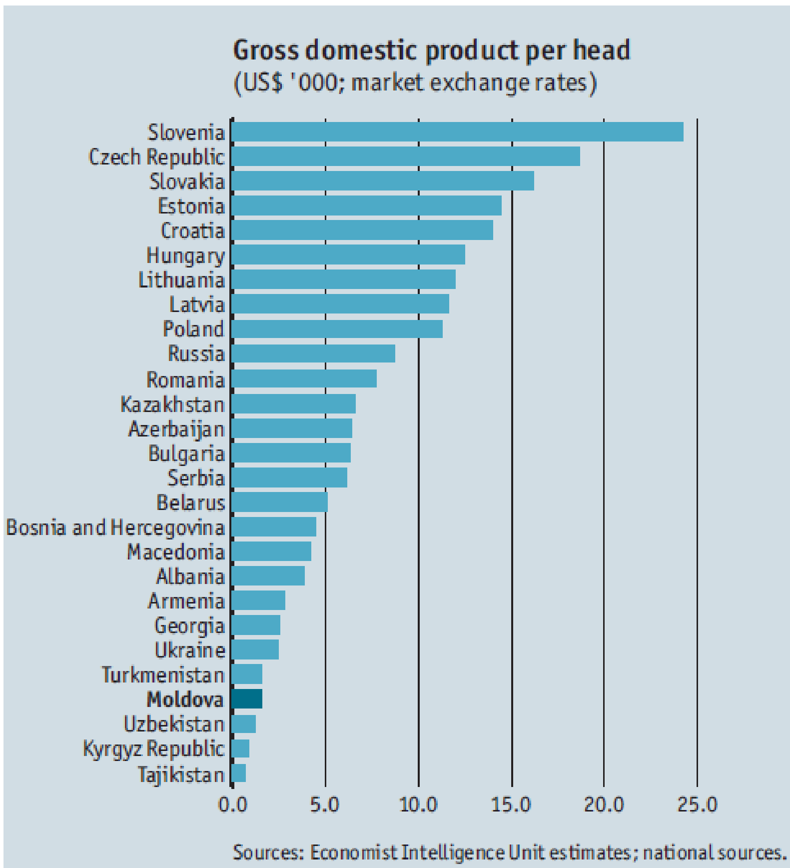
Brief Country Profile

Moldova is a small Former Soviet Union (FSU) developing country in Eastern Europe, land-locked between Ukraine and Romania, at the eastern border of the European Union. A strip of Moldova's territory, located between the Dniester River and the Ukrainian border, is under the *de facto* control of the separatist government of the self-proclaimed Trans-Dniester republic (also known by its local name "Transnistria") since 1990. Moldova's population counts 3.6 million people,[5] of which 60 percent live in rural areas, and an estimated third of the population lives and works abroad (CIA, 2009). More than two-thirds of Moldovans are of Romanian descent, explained by the common cultural heritage shared by the two countries until the successive Tsarist and Soviet

[5] Excluding the Trans-Dniester separatist region.

occupations. Economically, Moldova is the poorest country in Eastern Europe with a GDP (purchasing power parity) per capita in 2009 of $2,809 (Economist Intelligence Unit Country Report, 2010).

Figure 1. Moldova's GDP (PPP) per capita relative to other former communist economies in the region in 2009

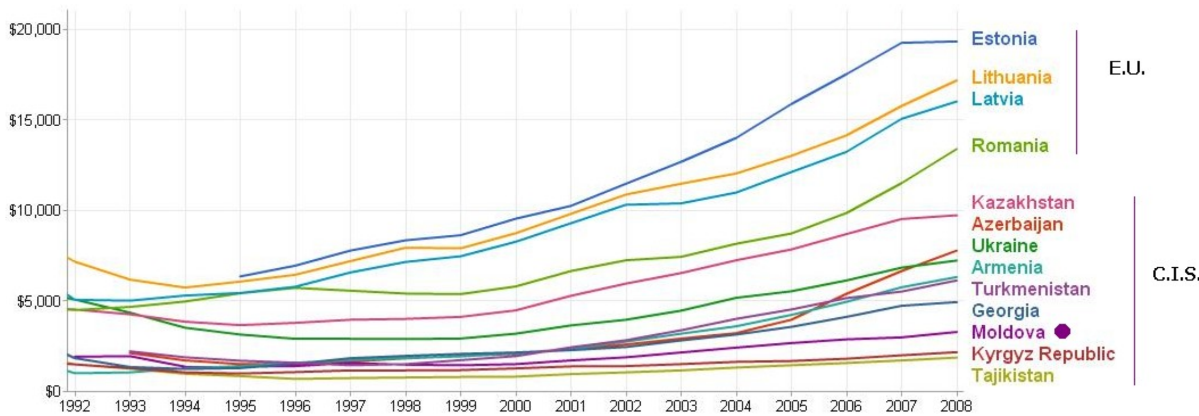


According to the World Bank income group classification in 2009, Moldova was classified as a lower-middle-income economy,[6] more comparable to Kyrgyzstan, Uzbekistan, and Tajikistan—the three least-developed Central Asian members of the Community of Independent States (CIS)—than to any of its neighboring ex-communist

[6] The World Bank divides economies into four income groups according to the 2008 GNI per capita, calculated using the World Bank Atlas method. The groups are: low income, $975 or less; lower middle income, $976–$3,855; upper middle income, $3,856–$11,905; and high income, $11,906 or more.

countries: Ukraine, Romania, Bulgaria, and Russia (see figure 1 and figure 2). The problem of poverty is prominent. Economic activity in the rural areas is primarily agrarian, with mostly self-sufficient households, some complemented by remittances received from relatives employed abroad.

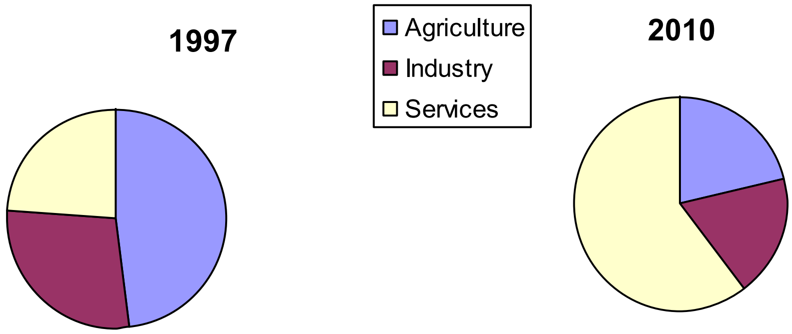
Figure 2. GNI per capita PPP* for selected countries: EU vs. CIS (1992-2008)



Source: Google labs 2010, public data from World Development Indicators, World Bank.
*current international $.

Compared to most of the former Soviet Republics that have changed their income status from lower to middle and higher-middle groups not long after the break-up, Moldova's small leap comes after a long period of stagnation within the lower-income limits, and is rather modest and fairly recent. However, 19 years after communism, Moldova's GDP composition by economic sector has changed drastically (figure 3), going from almost 50 percent in agriculture and less than 25 percent services in 1994 to almost 70 percent in services and less than 25 percent agriculture.

Figure 3. Moldova's GDP Composition by Sector: 1997 vs. 2010



Source**:** CIA, World Fact Book, 1997 and 2010.

In terms of political organization, Moldova is a unitary parliamentary representative democratic republic—the first FSU country to elect a communist, Vladimir Voronin (re-elected in 2005), as its president. In 2009, Moldova experienced significant political uncertainty, holding two general elections (in April and July) and four presidential ballots in parliament, all of which failed to secure a new president. Moldova's four opposition parties formed a new coalition, the Alliance for European Integration (AEI) that currently acts as Moldova's governing coalition until the new parliamentary elections, possibly in the summer of 2010. To spare the country from future political blockades, the ruling AEI has set up a parliamentary commission to change the provisions of the constitution regarding the election of Moldova's president. Moreover, although the country has been independent from the USSR since 1991, Russian military forces, the 14th Army, continue to remain on the separatist Trans-Dniester territory.

Historical Legacy

In the late Middle Ages, the present-day territory of Moldova formed the Eastern half of the principality of Moldavia—one of the three Latin principalities (Moldavia, Walachia, and Transylvania) in central-eastern Europe which united in 1859 to form the greater Romania. Later, between the 15th and 20th centuries, rising hegemonic empires successively conquered Moldova's territory: the Hungarian Empire in 1390, the Ottoman Empire in 1512, the Russian Empire in 1812, and then reunited with Romania in 1861 and 1918 throughout the interwar period.

At the end of the World War II, under the Ribbentrop-Molotov Pact (mainly under the secret protocol to the Nazi-Soviet Nonaggression Pact, 1939), Stalin annexed Moldova to the Soviet Union and began a program of "Rusification"[7] and collectivization through secret police rides on nationalist/pro-Romanian groups, the imposition of the Cyrillic alphabet, the abolition of the private ownership of all means of production, and mass deportations to forced labor camps mainly in Kazakhstan and Siberia. Ethnic Russians received incentives to settle in the newly formed Moldavian Soviet Socialist Republic (MSSR) in high political, administrative, and academic positions; for example, only 14 percent of the Moldavian SSR's political leaders were ethnic Romanians in 1946.

Although most economic activities resulted out of central planning, *de facto* the economy included small-scale self-sufficient economic activities that complemented people's earnings. Similarly, other economic transactions such as underground trade,

[7] The "Russification" was part of Stalin's program to impose the Soviet ideology on the Moldovan people by replacing Romanian in use with the Russian language and the Cyrillic alphabet, and by the "resettlement" program through the deportation of Moldovans to other parts of the Soviet Union and the migration of ethnic Russians and Ukrainians to Moldova. After Stalin's death in 1953, Nikita Khrushchev ended the Stalinist resettlement program. However, the "Russification" program continued and Russian remained Moldova's official alphabet.

exchanges of imported goods, and inter-industry trade (i.e., managers or workers of Soviet-owned industries could accumulate subtracted goods and later barter them on covert markets) were common during the Soviet era in Moldova. The informal trade between industries changed the allocation of resources in favor of one group or another according to their hierarchical position and their power over the allocation of collective resources. This context has guided individuals to aim at high positions in the Soviet bureaucracy. A higher political rank facilitated easy and often immoral opportunities to get around scarcity.

The fall of the Soviet Union in 1991 provided the opportunity for the Moldovan society to move away from central planning and establish market institutions that would lead to economic growth. However, although it took only a few moments for the new political elites to settle in, agree on a new constitution, and declare independence, the change in sovereignty from Soviet Republic to independent Republic did not bring automatic stability or prosperity. Instead, the country experienced frequent and controversial fights and shifts in political powers, which have culminated with eight continuous years of authoritarian governance under the rulings of the Communist Party of Moldova (CPM).

Over the last 19 years of transition, Moldova has had a mixed success with economic reforms. On the other hand, Moldova has privatized its small and medium-sized business sector, and it has had success in privatizing agricultural land. Most of the former collectively owned land and housing units are today privately owned.[8] On the

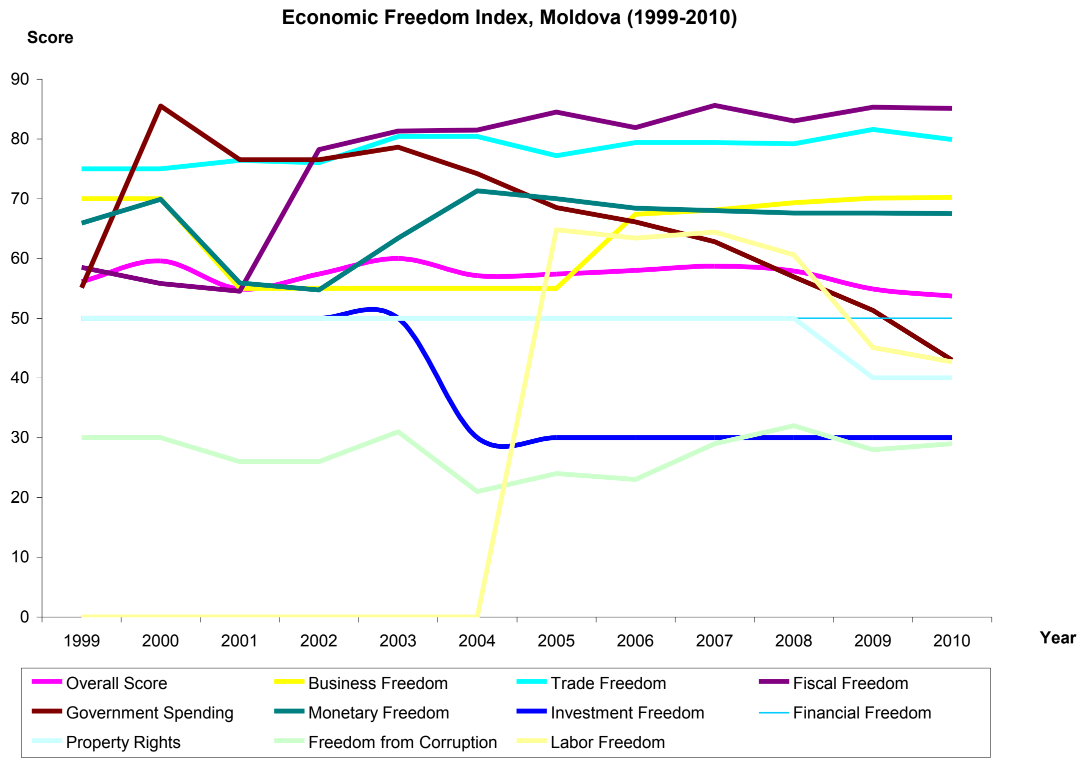
[8] A program started in March 1993 has privatized 80 percent of all housing units and nearly 2,000 small, medium, and large enterprises. Other controversial successes include the privatization of nearly all of Moldova's agricultural land from state to private ownership, through an American USAID assistance program called "Pamint" ("land"), completed in 2000.

other hand, the privatization of most larger-scale state enterprises and state-owned assets is ongoing and controversial, with some cases involving illegitimate transactions between public and private actors. Thus, Moldova's post-Soviet transition remains dominated by a weak rule of law and its sporadic and ineffective enforcement, political fraud, and instability. The International Monetary Fund and other international organizations have criticized the Moldovan communist government for lack of commitment to market reforms, especially for its slow and arbitrary strategy of privatization and for its failure to permit productive entrepreneurship (Woehrel, 2005).

Economic Freedom

In their annual studies on world economic freedom, the Heritage Foundation classified Moldova as "mostly unfree" every year since its independence. Moldova's overall economic freedom score in 2009 was 53.7, 125th out of 179 countries considered in the index. This low aggregated score reflects a trend of degrading institutional environment for most of the 10 economic freedoms considered, and at best ambiguous or flat for the rest.

Figure 4. Economic Freedoms in Moldova, 1999–2010



Source: Data from the Economic Freedom Index, the Heritage Foundation 2010.

Moreover, Moldova ranks the 40th among 43 countries in Europe, and its overall score is below the world and regional averages. The HF Freedom Index experts' conclusion on Moldova's economic freedom is discouraging:

> Overall, economic freedom remains constrained by a number of institutional shortcomings that impede economic dynamism within the private sector. Monetary stability, investment freedom, and freedom from corruption are weak. Foreign investment faces hurdles that range from bureaucratic inefficiency to outright restriction. There is significant corruption in most areas of the bureaucracy and an inefficient public sector suffers from a bloated payroll, and ever-rising salary increases. Political instability has left fiscal policy fragmented. Strains on the budget are mounting. (The Heritage Foundation Index of Economic Freedom 2010)

This weak institutional framework generates constant impediments for doing business in Moldova. Domestic and foreign entrepreneurs face impediments ranging from tariff and non-tariff barriers to complete trade restrictions. According to the World Trade Organization's "World Tariff Profiles 2009," Moldova's weighted average tariff rate was of 13.9 percent, with the Most Favored Nation (MFN) duties ranging from zero to 141 percent.[9] The cost added by import tariffs discourages local entrepreneurs from engaging in international arbitrage opportunities, thus affecting firms' profitability, capital accumulation, and therefore deter the country's growth potential. However, what adds to the cost of trade the most are a variety of additional non-tariff barriers, such as import and export restrictions and trade bans, import taxes and fees, burdensome trade regulations, and an inefficient and non-transparent customs process that is prone to corruption.[10] For example, with respect to the two main administrative barriers—customs evaluation and certification—Moldovan laws do not establish a precise time for custom clearance. Consequently, agricultural trade, a primary economic activity of rural entrepreneurs, suffers because the import and export transactions with fresh fruit and vegetables require rapid customs clearance. Entrepreneurs turn to the corruption by paying unofficial fees to Moldovan customs officers to get through without risking spoiling their merchandise before it even gets on the destination market. Russian and Ukrainian customs officers are no less "entrepreneurial" than their Moldovan counterparts are. Evidence from my interviews with local entrepreneurs supports this government hindrance. As one entrepreneur-exporter to Russia told us in an interview, "They can clear our products in two days, but at the same time the law allows to clear products within 10 days. But fresh peaches cannot wait so long. So, we pay to get the

[9] Most Favored Nation applied maximum duties on some beverages and tobacco products. Source: the 2009 WTO World Tariff Profiles.

[10] The Heritage Foundation & Wall-Street Journal, Economic Freedom Index 2009, accessed November 20, 2009.

clearance in two days." Another importer said, "Ukrainian customs are always a problem. They tried to make us pay additional fees, and we complied. It's one of the reasons we prefer to deal with European exporters." Red tape and constant changes in import-export regulations required by both domestic customs authorities and by their foreign customs counterparts are illustrations of the inefficiencies in the formal institutional arrangements in Moldova.

Most Moldovan entrepreneurs working abroad spend their earnings in their country of residence, renewing their homes, buying apartments and cars, and moving from rural to urban areas. Others, however, choose to save their earnings with the goal of pursuing a business opportunity upon settling back home. Unfortunately, few succeed to obtain their licenses, much less see their businesses grow. A Moldovan immigrant in Italy complained, "I worked in Italy for two years and saved money to start a small business, a driving school. But, after two months of striving to get my business license, I have given up. I plan to go back and hope the regulations will treat businesses better next year." Annually, nearly 2.6 million Euros from remittances are spent on Moldova's monopolized markets of products and services (CIA, 2009).

Political Freedom

According to Freedom House "Nations in Transit" in 2009, Moldovans' political freedom has been constantly deteriorating over the past 10 years. All the components of the democracy score have been declining over time (Figure 5).

Figure 5. Deteriorating Governance Indicators in Moldova 1999–2009

Nations in Transit Ratings and Averaged Scores

	1999–2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Electoral Process	3.25	3.25	3.50	3.75	4.00	4.00	3.75	3.75	3.75	**4.00**
Civil Society	3.75	3.75	4.00	3.75	4.00	4.00	4.00	3.75	3.75	**3.75**
Independent Media	4.00	4.25	4.50	4.75	5.00	5.00	5.00	5.25	5.50	**5.75**
Governance*	4.50	4.50	4.75	5.25	5.50	n/a	n/a	n/a	n/a	**n/a**
National Democratic Governance	n/a	n/a	n/a	n/a	n/a	5.75	5.75	5.75	5.75	**5.75**
Local Democratic Governance	n/a	n/a	n/a	n/a	n/a	5.75	5.75	5.75	5.75	**5.75**
Judicial Framework and Independence	4.00	4.00	4.00	4.50	4.50	4.75	4.50	4.50	4.50	**4.50**
Corruption	6.00	6.00	6.25	6.25	6.25	6.25	6.00	6.00	6.00	**6.00**
Democracy Score	**4.25**	**4.29**	**4.50**	**4.71**	**4.88**	**5.07**	**4.96**	**4.96**	**5.00**	**5.07**

Source: Freedom House, Nations in Transit 2009. The ratings are based on a scale of 1 to 7, with 1 representing the highest level of democratic progress and 7 the lowest. The Democracy Score is an average of ratings for the categories tracked in a given year.

Electoral events have always raised controversies and social unrest. The process of parliamentary elections of March 2005 (when the Communist Party of Moldova won the second mandate with a majority of 56 seats in the 101-seat parliament) has been criticized by the Organization for Security and Co-operation (OSCE) for biased media coverage, misuse of government resources in favor of the CPM, and harassment of opposition candidates and independent non-governmental organizations during the election campaign. The current state of political blockage follows a new series of violent civil street protests against CPM accused of electoral fraud and media monopolization in the newest parliamentary elections of April 6, 2009. In response to the revolutionary anti-communist movement developed in Chisinau on April 6, Vladimir Tismaneanu, Romanian scholar in the Study of Post-Communist Societies, wrote:

> I wish to stress a few things about the movement that is taking shape in Chisinau. First and foremost, I consider it to lie within the continuum created by the revolutions of 1989 in Central and Eastern Europe. Two decades after those historic events, we are seeing, in a former Soviet republic, a movement which I believe is fundamentally spontaneous and characterized by a liberal anticommunism centered on honoring and actualizing individual human rights. The primary and essential principle of modern liberalism is the recognition of the inalienable rights of any human being.
>
> The protests in Moldova show us beyond any doubt that anticommunism is not an illusion. The essence of the demonstrators' message, both to their country and to Europe, is anticommunism: the simultaneous rejection of the police state that Comrade Voronin so deftly built while in power, and of the endemic corruption generated in this country by state-sponsored Mafioso networks.
>
> Last but not least, Voronin's overreaction to the post-election protests—repression by the secret police, mass arrests, sealing the country's borders, censoring information and the media—clearly shows his Stalinist mentality. The governing principle of his politics is Lenin's old dictum: *kto kogo*—who will prevail over whom? The pillars of the CPM regime are hostility to the rule of law, undermining pluralism, and total disregard for civic dignity. (Tismaneanu, 2009)

Moldova presents an institutional environment dominated by inefficient and corrupt governance. At the heart of this problem lies weak enforcement of the rule of law and a lack of transparency and accountability mechanisms that encourage political actors' ex-post opportunism in the form of informal arbitrary taxation, corruption, and deficient governance.

Table 1. Governance Indicators for Selected Transition Countries, 2008

Country	Government Effectiveness Percentile Rank (0-100)	Government Effectiveness Score (-2.5 to +2.5)	Rule of Law Percentile Rank (0-100)	Rule of Law Score (-2.5 to +2.5)	Corruption Percentile Rank (0-100)	Corruption Score (-2.5 to +2.5)
ARMENIA	52.6	-0.07	42.6	-0.36	34.8	-0.54
BULGARIA	58.3	0.1	51.2	-0.12	52.2	-0.17
CROATIA	69.7	0.52	55	0.08	61.8	0.12
CZECH REPUBLIC	82.5	1.07	77	0.85	66.7	0.37
ESTONIA	84.4	1.15	84.7	1.05	79.2	0.94
GEORGIA	61.6	0.18	44	-0.34	50.7	-0.23
LATVIA	70.1	0.56	71.3	0.73	64.7	0.29
LITHUANIA	71.6	0.64	67.5	0.58	63.3	0.18
MOLDOVA	23.7	-0.76	40.7	-0.46	30.9	-0.64
POLAND	68.2	0.48	65.1	0.49	67.6	0.38
ROMANIA	50.2	-0.14	53.6	-0.05	57	-0.06
RUSSIA	45	-0.32	19.6	-0.91	15.5	-0.98
SLOVAKIA	77.3	0.76	67	0.52	68.6	0.43
SLOVENIA	82.9	1.09	82.3	0.91	79.7	0.95
UKRAINE	32.7	-0.6	31.1	-0.62	28	-0.72

Source: World Bank, World Governance Indicators, Governance Matters 2009.

As evaluated in the 2009 World Governance Indicators report (table 1), with regard to the governance and anti-corruption dimension of the institutional environment, Moldova scores lower than most comparable transition economies in the region. For all three governance indicators, Moldova ranks at the bottom. In "governance effectiveness," Moldova is the 15th of all the 15 countries. In "rule of law" and "control of corruption," Moldova is the 13 out of 15.

In 2005, the USAID's assessment of Moldova's Democracy and Governance[11] indicators puts emphasis on the concentration of political power facilitated by the corrupt political structure inherited from the Soviet past:

[11] This USAID Democracy and Governance (DG) assessment identifies the principal problems and challenges confronting the Government of Moldova in its transition from authoritarian rule to independence. The assessment examines Moldova's political environment, historical foundation, and current trajectory. Employing the framework developed by USAID's Office of Democracy and Governance, the analysis identifies key political actors, their interests, and the institutional arenas in which they operate. It also identifies those actors and institutional arenas amenable to further democratic development. The analytic framework is intended to assist USAID develop a programmatic strategy to support Moldova's evolution toward a more democratic political culture (USAID, 2005).

> The overarching challenge confronting Moldova's path to democracy is reducing the concentration of executive power that restricts political competition and retards the establishment of the rule of law. . . .
>
> Vertical power had been the norm for Soviet as well as post-Soviet Moldovan governments, and strengthening that structure seemed natural for President Voronin after the Communist Party victory in 2001. Voronin's attempts to re-concentrate executive power early in his administration reinforced the traditional relationship of government and citizens (or subjects), and blocked the growth of a participatory democracy based on the rule of law.
>
> Consolidated executive power threatens both the development of the rule of law and political competition. Central actors feel entitled to interfere in the judicial process, to manage or influence the media, to dictate to local and regional authorities, and to play favorites with business interests. One result is a government that is neither transparent nor accountable, thus dampening individuals' willingness to become involved in political life. (USAID, 2005)

As is typical for all FSU-CIS countries, complex and opaque laws and regulations dominate Moldova's institutions. The lack of transparency and the political barriers toward the public understanding of the legislative acts are the sources of incentives for empowered authorities to exercise more bureaucratic discretion in interpreting or implementing the country's legislation. In particular, this problem concerns the regulatory agencies, such as Fiscal Inspectorate, Customs Departments, Technical Inspectors, Quality Control Agencies, Environmental Agencies, and Labor Safety. The complexity and ambiguity in their content present themselves as corruption opportunities for authorities, who have a monopoly position in negotiating the terms of public service transactions. Extracted rents, in this case, are premium costs of transacting with lawmakers paid by confused and constrained entrepreneurs who are willing to pay the demanded bribes instead of risking incurring higher costs in form of blocked merchandise in customs depots, or seizure of entrepreneurial activity for a long time required to run fiscal or technical inspections. On these lines, one start-up entrepreneur in Chisinau told us in an interview that “It is impossible to keep up with so frequent and complex changes in laws and regulations. Paying the man in charge with enforcing them is an easy way to get out of trouble.” Widespread corruption, a weak rule of law, inefficiencies in the legislative and judicial systems, and the regulatory burden form together a costly environment for conducting productive economic activities.

For the last decade, Transparency International has been systematically documenting the problem of corruption in Moldova’s public institutions. In the organization’s annual Corruption Perceptions Indexes, Moldova has never scored higher than 3.3 out of 10. Local entrepreneurs complain about corruption associated with lack of institutional transparency, accountability, and predictability. Corruption activities emerge under inefficient institutional arrangements. Unlike within an efficient set of institutions, which leads to productive entrepreneurship, a superior allocation of resources, and increases a country’s production possibilities frontier (PPF), corruption is a response to institutions rewarding socially destructive and unproductive activities and leads to lower the gains from trade and stagnation. In a corrupt institutional environment, unproductive agents exploit the profits earned by productive agents. In addition, apart from being a mere redistribution of wealth from productive to unproductive entrepreneurs, it also diminishes the supply of productive entrepreneurs, because a tax on profits/property works as a disincentive toward individuals’ ability and willingness to discover future profitable avenues. Thus, not only is corruption unproductive, but it also discourages the realization of gains from extended cooperation and trade.

When discussing corruption, several interviewees remembered two Soviet sayings: “If you don’t steal from the union, you steal from your family” and “They who divide, make their own share first." These popular sayings illustrate that corruption was a common and socially accepted activity in Soviet bureaucracies. It also illustrates how in present democratic Moldova, corruption did not vanish; today's bureaucracies provide perverse incentives just like the old Soviet ones did. The owner of a logistics firm from Chisinau told us: "I was lucky when I started my business six years ago. A good friend of mine was in charge of license procedures, I received my license in two days with a privileged pass in his offices." Having relatives or friends connected with public institutions or the government can make things easier for entrepreneurs. The same entrepreneur revealed his corrupt relationships with the Moldovan public servants:

> "Whenever I have to deal with unfamiliar public authorities, I always do my homework upfront to find out who is at the top of their office, what are others saying about his practices, how much or how to propose as bribe, etc. this is the only way to save on time and money, otherwise they will keep delaying your or refusing your requests at infinitum." (Chisinau, June 2009)

The qualitative insights from my interviews in Moldova are consistent with the public choice approach to public regulation (Tullock, 1967), also promoted by Djankov et al. in their DB studies, according to which the latter benefits bureaucrats and politicians and restricts freedom of entry. Under the constraint of time, entrepreneurs who cultivate a familial or a client-firm relation with public officials can avoid having to wait in overcrowded public offices before receiving a response or a stamp.

Media Freedom

In 2009, the Freedom House classified the Moldovan media as "not free," and ranked the country 148th out of 195. Separately, in the same year, Reporters Sans Frontiers (RSF) have classified Moldova as one of the countries with "noticeable problems." In their ranks, out of 175 countries, Moldova has descended from position 81 in 2007, to 98 in 2008, and 114 in 2009. The current RSF evaluation of Moldova states:

> Publications quickly run into difficulties if they expose corruption, particularly among the leadership, or reveal the source of their income. This is what happened to the popular *Jurnal de Chisinau* in April 2009 when it prepared to publish a series of articles about the personal fortune of President Voronin. The edition carrying the first article, devoted to the president's son, never reached the newsstands because the state-controlled printers claimed that technical problems prevented them from printing the issue. (RSF, May 2009)

Moreover, the RSF have repeatedly warned and condemned the Moldovan authorities for abusing the local privately owned press stations numerous times close to the 2009 elections (table 2). The frequency of public abuses increases during electoral events and target independent journalists reporting on vote ringing, corruption, extortion, and other illicit transactions involving political actors and public bureaucrats.

When the Communist Party (in power since 2001) won the April 2009 elections with 49.9 percent of the vote, political turmoil that followed opposition's claims of vote rigging had a direct impact on the freedom of press. Local and international journalists fell victims of demonstrators' violence and were treated by the communist security forces as enemies of the Moldovan state.[12] Around 20 journalists working for Romanian press or for international media could not cross the border and received denial of entrance from customs officers without a valid reason. Others faced expulsion, arrest, or deprivation of the right to practice journalism on Moldovan territory. The communist government also

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[12] Similar abuse of power happened in the 2005 parliamentary elections when CPM and Voronin won again. Observers from the Organization for Security and Cooperation in Europe (OSCE) said that the vote was carried out generally in line with OSCE, Council of Europe, and other international election standards. However, the OSCE and other international organizations criticized Moldova for biased electronic media coverage, misuse of government resources in favor of the CPRM, and harassment of opposition candidates and independent non-governmental organizations during the election campaign. http://www.policyarchive.org/handle/10207/bitstreams/4007.pdf

blocked the independent news websites, and social networking platforms, such as Twitter, Facebook, Odnoklassniki, Vkontakte and others, for the duration of the parliamentary elections.

Table 2. Cases of Media Intimidation by Moldovan Authorities

Date	**Incident/Case**	**Outcome**	**Context**
25 Feb. 2009	Reporters Sans Frontiers condemns a raid on the privately owned TV station *Albasat* on by three interior ministry agents, who roughed up and arrested two employees, journalists.	RWB said, "We deplore the use of such methods, which recall those used in the Soviet era, and we reiterate our request to the interior ministry to guarantee the freedom and safety of independent news media, especially as elections are to take place in April."	The parliamentary elections in April 2009
6 March 2009	Reporters Sans Frontiers deplores a Chisinau court's decision to freeze the bank accounts of the *Jurnal de Chisinau* newspaper in connection with a former prosecutor's libel suit over two reports five years ago that the police were investigating him on suspicion of rape.	"The court's decision to freeze the *Jurnal de Chisinau*'s accounts is disproportionate," Reporters Without Borders said. "A libel suit should not jeopardize a newspaper's ability to keep operating. The reaction of civil society in challenging the authorities on this matter is nonetheless very encouraging for the defense of press freedom in Moldova."	The parliamentary elections in April 2009
5 April 2010	Reporters Sans Frontiers condemns the detention of leading independent journalist and political analyst Ernest Vardanean in Tiraspol, the capital of the breakaway region of Transnistria. Arrested by the Transnistrian intelligence agency, the MGB, on 7 April, he is facing between 12 and 20 years in prison on a charge of high treason.	Vardanean, who is from Tiraspol, is currently being held in the breakaway territory's national security headquarters after a court held a closed-door hearing and ordered him placed in pre-trial detention for two months.	The frozen conflict between the break away region Transnistria and Moldova

Date	Incident/Case	Outcome	*Context*
17 April 2009	Amnesty International's Moldova Memorandum concerning policing during and after the parliamentary elections in April 2009 in Chişinău when hundreds of people, including minors, were detained in Moldova as the country's authorities clamped down following demonstrations which started in the capital on 6 April but which led to rioting on 7 April 2009.	Amnesty International has written to President Vladimir Voronin raising the following concerns: a) Excessive use of force by police after the demonstrations; b) Widespread torture and other inhuman and degrading treatment in detention; c) Impeding the work of the Parliamentary Human Rights Advocates (ombudsmen).	*The parliamentary elections in April 2009*
8 April 2009	At least 19 Romanian journalists, working for both domestic and international media outlets, were turned back when trying to fly into Moldova or enter at the Romania-Moldova border crossing points of Galati-Giurgiulesti and Oancea-Cahul. Moldovan border guards have given conflicting explanations for refusing the journalists entry.	Voronin declared the Romanian ambassador to Moldova, Filip Teodescu, a persona non grata, and introduced visa requirements for Romanians.	
8 April 2009	A journalist with *Jurnal de Chisinau* and civil society activist was assaulted by police officers on 8 April for attempting to film the Building of the Government. An Amnesty International representative accompanied him to the hospital where he received care.	On 16 April 2010, the European Court of Human Rights (ECHR) at Strasbourg judges in favor of Brega in the case Brega vs. Moldova The Moldovan state awes 10,000 Euros in compensations to Brega for violating his human rights in April.	

Source: Reporters Sans Frontiers, Amnesty International, and the Committee to Protect Journalists (CPJ).

The report on the worldwide attacks on the Press in 2009 produced by the Center for Independent Journalism (CIJ) states:

> In April, authorities barred at least 19 journalists for Romanian newspapers, broadcasters, and news agencies from entering Moldova to cover anti-Communist rallies in the capital, Chisinau. Stefan Candea, vice president of the Bucharest-based Romanian Centre for Investigative Journalism, told CPJ that border guards had given conflicting reasons for refusing the journalists entry. The government offered no official explanation. Approximately 10,000 protesters took to the streets to protest the April 5 parliamentary election, won by President Vladimir Voronin's Communist Party. The protesters said the elections had been rigged and called for a new vote; on the second day of protests, some protesters stormed and looted the Moldovan parliament and president's office, the U.S. government-funded Radio Free Europe/Radio Liberty reported. Voronin, whose government is allied with Moscow, accused Romania of encouraging pro-Western protests, according to The Associated Press. Dozens of people were injured and 200 arrested. (CIJ, May 2009, http://cpj.org/europe/moldova/)

The protests underlined a generational and regional gap in Moldova: young and well-traveled people have an appreciation for Western institutions and want to be part of the EU and NATO, while older citizens and provincial voters support the pro-Russian Communist Party.

While the Moldovan Constitution guarantees media freedom,[13] the penal code and press laws prohibit the defamation and the insulting of the state sovereignty, which gave the Moldovan communist ruler discretionary control over media activity. Thus, as expected, amid post-election protests in April 2009, Reporters Sans Frontiers (RSF) said the local and international media were "targeted" by demonstrators and "treated as enemies of the state" by security forces (RSF, 2009).

[13] This reform became possible after years of heated discussions between the opposition and the ruling communist party that culminated with parliament's adoption in 2006 of a new legal framework for broadcasting allowing for more freedom of entry, but without resolving the monopoly problem of the subsidized television Moldova 1, a subsidiary of TeleRadio Moldova, whose editorial line continues to give more air time to the ruling party (CPM) and in particular to biased news about the president, prime minister and parliament than to any of the other running political players.

However, the anti-communist youth protests in April 2009 were primarily organized with the help of social media platforms and text messaging; this episode of civil action will remain in history as “The Twitter Revolution.” After a year in which Twitter and Facebook catalyzed protest movements in Iran and Moldova, and in response to new tools of Internet control applied by authoritarian regimes around the world, the Commission on Security and Cooperation in Europe (OSCE), held a public briefing entitled “Twitter Against Tyrants: New Media in Authoritarian Regimes.” These prompt reactions from the civil society through internet tools, such as Twitter and Facebook, have also demonstrated that one of the benefits of globalization is the limit on how far authoritarian control of media can extend. Throughout the last two decades, people from developing countries were able to travel to developed countries and compare opportunities, and most importantly, compare the difference in the quality of institutions that generate more economic opportunities and the freedom to pursue individual choices.

3. Institutional Change and Development. Theoretical Insights for Post-Soviet Moldova

The following analysis connects the literature of institutional economics and development economics to provide a more ample perspective on how is the process of institutional and policy change different for weak states like Moldova, and provides insights into what do DB reforms mean for development in such contexts.

Institutional and Development Economics

In his discussion of the constitutional dilemma of economic liberty, Barry Weingast explains that while citizens of developed western societies, like those of the United States of America and western Europe, can take for granted the set of institutions directing their interaction toward prosperity, poorly developed societies, like those of the Former Soviet Union (FSU), do not enjoy the same beneficial conditions (Weingast, 2005). Thus, unlike the citizens of developed countries, whose basic rights and freedoms associated with freedom of press, property rights, unbiased judiciary, contract enforcement, are universalistic, the citizens of poor countries (like the Moldovans) have to gain their right to these freedoms either by revolutionary means, or by cultivating a corrupt relationship with those in power (Weingast, 2005).

Moldova's case of a weak post-Soviet democracy has been reviewed in the modern international affairs/political science literature from the perspective of nationalism and ethnic identity by Charles King, who identifies Moldova as a "state-nation" (figure 5, from King, 2009).

Figure 6: Eurasia's Recognized and De Facto States

	Capital	Independence and Recognition	Population	Ethnic Composition	Territory	Armed Forces
Republic of South Ossetia (also known as *Iryston* in Ossetian)	Tskhinvali	Declared Sept. 20, 1990. Recognized by North Ossetia (itself not a sovereign state) in 1993. Recognized by Russia and Nicaragua as of Sept. 2008.	Est. 70,000	Mainly Ossetians, but some Russians and Georgians.	2,732 km^2, minus a few villages still under central government control.	Unknown
Moldova	Chisinau	Declared Aug. 27, 1991. Joined UN Mar. 2, 1992.	3,830,000	Moldovans 65% Ukrainians 14% Russians 13% Gagauz 4%	33,700 km^2	6,750
Dnestr Moldovan Republic (also known as *Pridnestrov'e* in Russian and *Transnistria* in Romanian)	Tiraspol	Declared Sept. 2, 1990.	Est. 670,000	Moldovans 33% Russians 29% Ukrainians 29%	4,163 km^2	7,500

Source: Charles King, "Extreme Politics," 2009, p. 43.

The hypothesis behind this classification is that Moldova's disputed ethnic identity has been determined by prior acts of political organization. King identifies the weakness in identity with the institutional weakness—the bureaucratic infrastructure left behind by the Soviet regime at the discretion of the new local power elites and interest groups. While they are of Moldovan origin, these local political groups have been part of the ex-Soviet system and were able to perpetuate the old corrupt activities and use the system in their own advantage through old or new forms of public predation. Hence, the first decade of Moldova's independence saw opportunistic political behavior, fights for power among political coalitions, failed plans of privatization and reforms, a dramatic drop in people's standards of living and massive out-migration to Western Europe, the secession war in Transnistria, and the monopolization of the economy by privileged actors.

More amply, the theories of new institutional economics and economic development of the last three decades address this institutional problem through two main questions for humanity in the 21st century: "Why are some countries rich and others poor?" and "How is it possible to make poor nations rich?" Their discovery was that development correlates with the prevailing institutional frameworks of societies (North and Thomas, 1973, North, 1990, 1991, Baumol, 1990, Rodrik et al., 2004). Because they emit incentives that guide human interaction, institutions play a crucial role in societies' development path. Strong institutions are conducive to growth and prosperity, while weak institutions lead societies down the road to poverty and violence (Weingast, 1995, 2005, North et. al, 2006). Therefore, in order to understand the cause of poverty and violence, we should investigate the quality of the institutions (Olson, 1996), or "the rules of the game," that coordinate individuals' actions within a society (Ostrom, 1993).

As a FSU country, Moldova's *de jure* institutional system up to 1991 was similar to that of the USSR itself. After the collapse of the USSR however, during the critical transition years for the formation of market institutions, Moldova failed to secure the fundamental set of rules to protect citizens from public predation. In the absence of credible mechanisms to obligate rulers to respect their commitments however, there is no guarantee that institutional reforms designed to benefit social cooperation and economic growth will in fact be respected (Boettke, 1993, pp. 88–105; Boettke, 2001, pp. 191–265). Therefore, the question for the recent claimed success of the DB reforms in Moldova is twofold: 1) are the reductions in red tape and taxes sustainable, and 2) if external agencies classify the *de jure* effect of the DB reforms as sustainable, are their measurements confirmed by local agents' knowledge of the *de facto* effect of the DB reforms? Is Moldova's case with the recent DB reforms a case of "exporting policy solutions" inadequate because of the omission of the weak attributes of the institutional context that this country presents?

Policy Change vs. Institutional Change

In conducting their empirical study correlating DB reforms with entrepreneurship and growth, Djankov et al. were inspired by ex-communist countries' transition experience throughout the '90s and by the resulting studies that revealed increased corruption in over-regulated economies (Shleifer and Vishny, 1993), a direct correlation between overregulation, high taxation, and the size of the unofficial economy (Johnson et al., 1997). Increased rent seeking is costly and discouraging for productive entrepreneurs and for economic growth (Murphy et al., 1993). Further inspiration came from the works of Hernando de Soto, who showed the benefits of increasing the share of the formal economy by downsizing the inefficient bureaucracies that discourage entrepreneurs from operating legally (de Soto, 2000).

Other studies, while consistent with earlier results, show that overregulation and higher taxation by themselves are not sufficient to cause corruption; the problem appears to rest in whether the administrative system allows for high levels of regulatory discretion that discourage firms from using the formal system, thus increasing the size of the unofficial economy (Johnson et al., 1997).

Benito Arruñada, a critic of the World Bank DB methodology and its inefficiency in measuring institutional change, has pointed toward the failure to consider the difference between quantitative and qualitative reforms' effects and firms' incentive to reduce their transactions costs by substituting between: a) formal (compulsory) and informal (voluntary) costs—small firms and b) the costs of initial procedures and future procedures (Arruñada, 2007).

Exploring this measurement problem provides a key insight for this policy essay: in weak democracies, it is not sufficient to rely on quantitative indicators devised by international organizations like the World Bank. Numerous scientific papers published in the last 30 years have underlined the crucial importance of understanding and appreciating the primary role of changing institutions in human interaction (North 1990, 1991, 1991, 2005, Baumol 1990, Acemoglu et al., 2000, 2001, Boettke, 2001, Boettke et. al, 2008, Acemoglu & Johnson, 2005a), and their complexity and diversity for successful policy research and development (Ostrom, 2005). These scholars discuss institutional specificities, their determinants, and implications for policy reform. Douglass North introduced the idea that institutional change in a society is "path dependent" (North, 1990, p. 92–117). Complex institutional arrangements from the past influence societies in the types of policies and reforms they choose to implement in the present. Additionally, Acemoglu and Johnson (2005a) explore the crucial importance of diversity in types of institutions governing property rights and exchange. There are institutions that protect individuals from public expropriation, and there are institutions that protect the property rights and contracts of individuals in a society from private predation, "individuals often find ways of altering the terms of their formal and informal contracts to avoid the adverse effects of weak contracting institutions" (2005a, p. 949).

In Moldova's case, understanding the difference between perceived and actual institutional arrangements, or the gap between *de jure* and *de facto* effects of DB reforms, can improve the quality of the assessment of institutional change and the prospects for development. *De jure* changes do not necessarily correspond to *de facto* changes, and neither do their effect on human interaction. In Moldova, the DB reform indicators seem to measure only the quantitative change in formal institutions and fail to capture the lack of quality signaled by the increase in informal arrangements that parallel or replace the formal weak ones. The data in the table 3 below depicts this problem. The size of the "shadow economy" in Moldova ("Moldavia") was almost half of its GDP throughout the 1999–2006 period, "outperformed" only by Georgia and Ukraine's higher averages of informal markets. These estimates come from a recent study that links corruption with the size of the informal markets (Schneider and Buehn, 2009). The authors conclude: "the shadow economy reduces corruption in high income countries (substitution effect) and increases corruption in low income countries (complementary effect).” (Schneider and Buehn, 2009, p. 36)

Table 3. The Estimated Size of the “shadow economy” in Moldova, 1999–2006

Table 3.5.1. Size of the Shadow Economy in 19 Eastern Europe and Central Asian Countries (% of GDP)[1)]

	Country	Years								Country
		1999	2000	2001	2002	2003	2004	2005	2006	Average
1	Albania	-[2)]	-	-	33.7	33.7	33.7	34.3	35.1	34.1
2	Bulgaria	35.0	34.8	34.9	35.0	35.4	35.4	36.5	36.4	35.4
3	Croatia	33.3	33.0	33.1	33.7	33.1	32.6	34.1	34.2	33.4
4	Czech Republic	17.7	18.1	17.7	17.9	17.9	17.8	18.3	18.3	18.0
5	Estonia	36.8	37.1	37.1	37.5	37.8	37.5	38.2	38.1	37.5
6	Georgia	67.7	68.0	67.5	67.5	67.5	67.3	68.0	68.7	67.8
7	Hungary	23.0	22.8	23.2	23.3	23.2	23.3	24.3	24.3	23.4
8	Kazakhstan	43.2	43.2	43.2	43.3	43.2	43.7	44.6	44.5	43.6
9	Latvia	37.6	37.3	37.6	37.7	38.2	38.7	39.4	39.2	38.2
10	Lithuania	28.3	28.2	28.4	28.9	29.2	29.2	30.2	30.5	29.1
11	Moldavia	47.8	47.5	48.0	48.1	48.0	48.0	49.1	48.9	48.2
12	Poland	25.9	26.0	26.1	26.1	26.1	26.0	27.3	26.7	26.3
13	Romania	35.6	35.6	35.8	35.9	36.0	36.2	36.9	37.5	36.2
14	Russian Federation	46.0	46.2	46.5	46.6	46.6	46.6	47.3	46.9	46.6
15	Slovak Republic	16.7	16.5	16.9	17.1	17.1	17.1	18.2	18.3	17.2
16	Slovenia	25.8	26.5	26.6	26.7	26.8	26.9	27.3	27.2	26.7
17	Tajikistan	-	45.1	45.1	45.2	45.3	45.4	-	-	45.2
18	Turkey	33.8	33.8	33.2	33.5	33.8	34.0	34.3	34.6	33.9
19	Ukraine	53.7	53.8	53.8	54.0	54.2	54.4	55.3	55.1	54.3
	Time Average	35.8	36.3	36.4	36.4	36.5	36.5	36.9	36.9	

Source: Schneider and Buehn, “Shadow Economies and Corruption All Over the World: Revised Estimates for 120 Countries,” 2009, p. 122.

In high-income countries, the study shows, firms bribe public actors to be able to increase their activity in the formal sector, with the effect of a general reduction of the “shadow economy.” In low-income countries however, firms use bribes to keep their activity away from the formal sectors, with the effect of increase in the “shadow economy.” One of the most common forms of corruption in poor countries is the collusion of firms with public inspectors, in order to hide the firms’ total fiscal obligations in exchange for a bribe—a share of the unreported tax liability. In poor countries like Moldova, high levels of corruption prevail because of the excessive domestic fiscal and regulatory costs. However, contrary to World Bank’s DB recommendations, I argue in this essay that reform solutions directed toward simplifying the costs of "doing business" in relation to public institutions and interests in weak democracies like Moldova fail to achieve their goal because the perceived effect of the DB reform does not correspond with the actual institutional reality. Chapter IV details this argument.

Credible Commitments, Institutional Change, and Development

Because the World Bank's evaluation of DB reforms in Moldova is *ex ante* to observing their effects on economic and political actors, the question is how reliable and useful are the country evaluations in DB reports for both local and international private and public communities? The problem surrounding the sustainability of DB reforms in weak democracies arises because of the absence of binding constraints on policy makers' incentives to renege on their promises according to the existing better paying alternatives.

The essential role played by the institutional arrangements guaranteeing governments' accountability and limited intervention is acknowledged in the existing literature by Rosenberg and Birdzell, who show that the American Constitution and the American interstate competition system are superior in maintaining an institutional framework conducive to cooperation and growth:

> The United States had a federal system in the nineteenth and early twentieth centuries in which political intervention by the national government was narrowly restricted by political tradition and constitutional interpretation, while political intervention by the state governments was restricted by the fear of economic competition from other states. (Rosenberg and Birdzell jr., 1986)

Similarly, Douglass North explains[14] how the adoption of institutional mechanisms eliminating the arbitrary behavior of the state over economic activity determined the economic success of the Western European countries (North, 1981, 1990, 1991), and how, therefore, the lack of such mechanisms in the East has led to predatory states and wealth redistribution. Moreover, Peter Boettke's extensive research on the Soviet economy and the post-Soviet transition (Boettke, 1993, 2001) demonstrates how the absence of such credible commitments contributed to the failure of early reforms in the FSU.

Understanding the problems associated with credibility and commitment in weak democracies untangles the failure of DB reforms in Moldova. One important aspect of a democratic society, however, is its free access to information markets that allows the citizens to check their rulers' behavior.

Media, Institutional Change, and Development

A decade into the 21st century, there can be no doubt about the important role played by a free media in institutional change and development. Today's media, both classical (press, television, and radio channels) and new (the internet with blogs, Twitter,

[14] In his 1991 paper on "Institutions," North explains how the economic success of the Western European countries is thanks to institutions restraining their governments' ability to renege on their promises*: "the evolution of capital markets was critically influenced by the policies of the state, since to the extent the state was bound by commitments that it would not confiscate assets or use its coercive power to increase uncertainty in exchange, it made possible the evolution of financial institutions and the creation of more efficient capital markets. The shackling of arbitrary behavior of rulers and the development of impersonal rules that successfully bound both the state and voluntary organizations were a key part of this whole process."(*p.107), and how the absence of such institutional mechanisms to secure government's commitment to agreed reforms is detrimental to development: *"A capital market entails security of property rights over time and will simply not evolve where political rulers can arbitrarily seize assets or radically alter their value. Establishing a credible commitment to secure property rights over time requires either a ruler who exercises forbearance and restraint in using coercive force, or the shackling of the ruler's power to prevent arbitrary seizure of assets."*(p. 101) HYPERLINK "http://www.econ.uchile.cl/uploads/documento/94ced618aa1aa4d59bf48a17b1c7f605cc9ace73.pdf"

Facebook, Wikipedia, etc.), is an essential tool in citizens' everyday lives. As voters, individuals use media to guide their choice of political leaders. As consumers and entrepreneurs, they use the media to increase their knowledge of the market. However, not all people enjoy a free and competitive media in their countries. Authoritarian governments (like North Korea, China, or Moldova during the ruling of the communists) can exercise their power to restrain their peoples' access to quality information or manipulate the media according to political stakes. There is a growing empirical and theoretical literature on the role of media in the democratic process, institutional change, and development. By investigating patterns of media ownership in 97 countries of the world, Djankov, McLiesh, Nenova, and Shleifer find that state ownership of the media is significantly detrimental to economic, political, and social outcomes (Djankov et al, 2001, 2002). Their empirical evidence shows that freedom of entry and the privatization of the media is a superior option for the advancement of political, economic, and social goals, compared to the option of a state monopoly on media. Similarly, Coyne and Leeson explore the relationship between media, development, and institutional change (Coyne and Leeson, 2004, 2007, 2009). One of their key findings is that the media plays a dual role in a society. First, the media can influence the choice of policies within the existing institutional framework. Second, the media can serve as a catalyst to choosing and reinforcing a direction of institutional change.

Relevant for the measurement problem of the validity of the DB reforms in Moldova is the observation that the reality of media coercion in weak democracies is an illustration of the gap between the communist rulers' *de jure* and *de facto* commitment to policy and institutional change. The experience of the April 2009 elections in Moldova has shown that authoritarian governments might use their power to coerce or manipulate the media in their favor. However, the prompt reaction of the civil society through the “Twitter Revolution” has also demonstrated that there are limits to how far the government’s control of media can extend. Throughout the last two decades, as more and more Moldovans have traveled to developed countries and compared opportunities, powerful market elements of the new media have contributed to their realization of the benefits from greater economic freedom that has build a strong civil frontier in favor of strengthening the institutions that protect their freedoms against public abuse.

4. Lessons from the Recent ‘Doing Business’ Reforms in Moldova

The World Bank 2010 DB study ranks Moldova among the top ten regulatory and fiscal performers (Figure 6). According to Djankov et al. (2002), by lowering barriers to entry, Moldova is improving its entrepreneurial environment, and should expect economic growth.

Figure 6. Top 10 Reformers in *Doing Business 2010*

The top 10 reformers in 2008/09

Economy	Starting a business	Dealing with construction permits	Employing workers	Registering property	Getting credit	Protecting investors	Paying taxes	Trading across borders	Enforcing contracts	Closing a business
Rwanda	✔		✔	✔	✔	✔		✔		✔
Kyrgyz Republic	✔	✔	✔	✔	✔		✔	✔		
Macedonia, FYR	✔	✔	✔	✔	✔	✔	✔			
Belarus	✔	✔	✔	✔			✔	✔		
United Arab Emirates	✔	✔						✔		
Moldova	✔			✔			✔			
Colombia	✔	✔		✔	✔	✔	✔	✔		✔
Tajikistan	✔	✔			✔	✔				✔
Egypt, Arab Rep.	✔	✔			✔				✔	
Liberia	✔	✔						✔		

Source: World Bank, Doing Business Website, Accesses, November 25 2009, http://www.doingbusiness.org/Reformers

More precisely, as the World Bank reports in 2009, regarding the three main reform areas “Starting a business”, “Registering property”, and “Paying taxes”:

> Moldova lowered the rates for social security contributions paid by employers. Property registration was simplified by eliminating the requirement for a cadastral sketch, reducing procedures from six to five and days from 48 to 5. Business start-up was eased by implementing an expedited company registration service.” (World Bank, 2010, http://www.doingbusiness.org/Reformers/ECA2009.aspx)

In this section, I explore the plausibility that the DB simplification-growth correlation in Moldova is hard to test, as it requires a qualitative assessment of the impact of the recent DB reforms. This raises the question of how much of the growth is attributable to DB simplification reforms or how much of the full growth potential is not realized because of other costly institutional factors, such as the transaction costs associated with a weak institutional framework. Contrarily, assessing an inversed formalization-corruption correlation in Moldova’s case can be possible based on data provided by existing qualitative studies. These studies confirm the challenges in assessing the impact of the recent DB reforms on the cost of doing business in Moldova on two levels: 1) empirical data comprised in quantitative macroeconomic indicators and in Transparency International’s annual Corruption Perception Indexes reveal economic stagnation and an increase in corruption over the last decade, and 2) qualitative data indicate a shift in rent-seeking activities from formal taxation and corruption to unofficial government taxation, rather than their complete elimination as the DB reports seem to suggest.

In both Economic Freedom Index 2010, and in “Doing Business” Index 2010, Moldova appears as a top fiscal and regulatory reformer, accomplishing significant reductions in taxes and regulations. As of January 1, 2008, the top income tax rate was reduced to 18 percent, and the corporate tax was eliminated. However, this internationally recognized accomplishment conflicts with the lack of local endorsement. Valeriu Lazar, Minister of Moldova's Economy, agrees, "Zero tax shares don't necessarily mean liberalization. On one side we have the zero tax shares, on the other we have a very restrictive tax administration that annihilates the whole effect of this improvement."[15] Not all entrepreneurs are better off in their activity with a zero corporate tax. Construction companies report prohibitive transaction costs in the process of opening a construction site. In fact, by the World Bank's experts' evaluation, the procedures authorizing construction activities in Moldova are highly prohibitive to entrepreneurs. Nonetheless, many entrepreneurs said they prefer the cancellation of the zero corporate tax rates in exchange of eliminating the technical and administrative barriers, as it is highly onerous to wait for construction authorizations for years *ex-post* investing resources in local land and capital.

The Failed Regulatory Guillotine

The World Bank and USAID addressed the problem of regulatory inefficiency in Moldova in 2002. The two organizations have helped implement a regulatory reform—"The Guillotine," a long-run plan to eliminate all the unnecessary procedures from laws imposed on entrepreneurial activity. Today, the DB report captures the result of their efforts. In 2009, property registration procedures were simplified by eliminating the requirement for a cadastral sketch, reducing procedures from six to five, and days from 48 to 5. An expedited registration service eased business startup. Registering a firm takes

[15] Interview with Valeriu Lazar, Minister of Moldova's Economy, in Jurnal.md, retrieved 25 November 2009.

an entrepreneur officially only 15 days, compared to the Eastern Europe and Central Asia's average of 17 days, and corporate tax rates have been eliminated. However, Moldova ranked worse in all other reform domains that are essential for entrepreneurs' ability to realize long-term profit opportunities. Obtaining a construction license, for example, requires 30 procedures, 292 days, and costs 120 percent (income per capita) more than the OECD average of 15 procedures and 152 days, and 56 percent in cost. Enforcing contracts requires following 31 procedures, takes at least one year, and costs 30 percent of the claim. Dealing with the tax administration is onerous because of the long time spent paying taxes (228 days), number of payments (48), and their cost (31 percent of the profit) per year.

Hence, although the "The Guillotine" might have helped improve Moldova's score in the annual DB publications, in reality, simplified procedures do not necessarily equal better quality procedures to start businesses. Implementing top-down simplification strategies may lead to an increase in large firms' transaction costs and thus damage entrepreneurship and growth (Arrunada, 2007). Moreover, in the DB methodology it is assumed that entrepreneurs have perfect knowledge and public agencies are incorruptible. Given that corruption remains a significant problem in Moldova, this rigid assumption underestimates *de facto* barriers to entry.

On the positive side, the elimination of bureaucratic procedures is normally accompanied by a reduction of corrupt transactions in public agencies, which leads to lowering *de facto* barriers to entry for productive entrepreneurs. However, as the executive director of a think tank in Chisinau explained, "The Guillotine" did not have the desired effect. On the contrary, it merely revealed the excessive number of inspectorates and redundant regulations and instructions existed, but failed to eliminate any.[16]

The “Guillotine” is a top-down approach to business deregulation and formalization reforms based on the World Bank and the USAID schemes of rewarding governments’ performance for eliminating existing administrative, regulatory, and fiscal barriers to doing business. The Moldovan government was in charge of the entire process of the guillotine: the scope, the instruments used, the approval process, and the implementation. Promoters of this approach argue that reversed incentives in the reform process overcome the barriers that have slowed or blocked broad-based regulatory reforms in the past. These barriers include high political and administrative costs, intense insider resistance to change, and lack of knowledge on how to sustain change into the future (Jacobs and Astrakhan. 2006, p.16). One of the problems with this approach, however, is that it assumes that governments’ gains from these short run reform programs are greater than both short-term and long-term gains from maintaining the status-quo.

The Unofficial Taxation

The lack of institutional transparency in public administration arranged by the communist government during its eight years of authoritarian regime (2001–2009) have made it profitable for political entrepreneurs to adapt to beneficial institutional changes without losing their power to extract rents from market entrepreneurs. As a result, the guillotine failed on two fronts: first, it eliminated only trivial regulations, and second, it it triggered the development of new forms of public corruption. A greater cost for doing

[16] The list of all regulations included in the “Guillotine” reform, see Moldovan Government page http://www.economie.guvern.md/Default.aspx?noutateID=32

business in Moldova is the "unofficial taxation," or monetary contributions that regulators and local leaders ask from entrepreneurs. The "unofficial taxation" in Moldova and most of the developing former Soviet economies is a form of public predation that emerged because of the existing weaknesses in the rule of law, and consists of two forms of corrupt behavior of public actors:

1) Using the pretext of the "public interest" to compel firms to contribute to various public works and local events.
2) Using the fiscal and regulatory rules to share the gains from evasion with private actors (the "state mafia").

The intended effect of DB reforms is to reduce the size of the formally collected public budgets through taxation and to reduce the size of the informal budgets acquired through rent-seeking transactions stimulated by previously inefficient administrative and regulatory systems. However, it is precisely because they reduce the inefficiencies in the system, which have sustained corrupt transactions until now; beneficial regulatory reforms in weak institutional environments only exacerbate the problem of unofficial taxation.

In essence, the unofficial taxation is a manifestation of government ex-post opportunism for quasi expropriation and consists of local authorities' power to use the legislation to extract rents from entrepreneurs in the name of the public interest without giving a formal account for their takings (therefore, "unofficial"). For instance, local authorities are able to constrain entrepreneurs to contribute donations to various government-led events or projects (Lariushina et al., 2006), or worse, to accept full expropriation at imposed terms (Prohnitchi, 2003). According to Article 46 of the

Moldovan Constitution, these activities are illegitimate. The constitution text guarantees individuals' "Right to private property and its protection," but at the same time, it explicitly states, "No one can be expropriated unless for a matter of public necessity, under the law, against a fair previously determined compensation."[17] Thus, the pretext of "public necessity" seems to offer local authorities an unintended opportunity for discretion in coercing entrepreneurs to sponsor various social projects unaccounted for anywhere in public registers.

Moreover, according to my further research findings, the formal "rules of the game" guiding entrepreneurial activity are set in the Moldovan Business Laws established as early as 1991 (property laws), or as recent as 2001 (labor laws). However, in addition to formal basic laws, each regulatory agency has the power to issue special letters of interpretation, which give them discretion in identifying opportunities for quasi-expropriation. This inconsistency comes from complex and ambiguously formulated acts and laws. For instance, according to a decision passed by the Licensing Chamber,[18] one of the requirements to obtain a license reads, "as long as the licensed activity is conducted in conformity with the legislative and regulative framework currently in force." This phrasing is so open-ended that it leaves room for regulators to consider any minor deviation, not necessarily related to entrepreneurial activity,[19] a genuine violation of the "legislative and regulative framework currently in force" (Prohnitchi, 2003).

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[17] The Constitution of the Republic of Moldova states in Article 46. The Right of Private Property and Its Protection:

> (1) The right to possess private property and the debts incurred by the State are guaranteed.
> (2) No one may be expropriated except for reasons dictated by public necessity, as established by law and against just and appropriate compensation made in advance.

[18] Regarding the approval of licensing requirements for types of entrepreneurial activities no. 38-g of 09-16-2002, Official Government Gazette of Moldova no. 146-148, of 10-31-2002

[19] For instance, the conformity for fire extinguishers.

As a result, a firm can expect control visits from regulatory agencies at its headquarters based on both of the business laws and according to “letters of interpretation and disposition” which, in themselves, are arbitrary and distort the basic legislation text. This gives each empowered inspector or control officer the opportunity to interpret a given case in a way favorable for money extortion on “legal grounds.” It further becomes in the interest of the Fiscal Inspectorate in Chisinau to collect as many fines as possible from businesses to achieve the “fiscal plan” established each year and report to the top of their hierarchy their annual individual performance. Additionally, from the interview with the same think tank executive I found out that the average number of controls firms can receive per year is 35, and that the extent and damage of government interference in entrepreneurial activity through control agencies is prohibitive:

> I counted 64 of them (state control agencies) in total . . . Under these circumstances, firms have two alternatives: either closure, or double booking. These are the only real alternatives, you can try to resort to judicial power but you risk losing money and years of time in courts and there is no guarantee of success. (Chisinau, June 2009)

From a firm’s perspective, if we approximate the average time of each vertical control to a week, then it means that the firm needs to close for a period of 245 full days a year, which leaves entrepreneurs with practically no time to run their business (Lariushina et al., 2006). In this respect, the majority of the entrepreneurs I interviewed described situations similar to the one of a restaurant owner in Chisinau:

> If your business is flourishing, you should expect them [inspectors] to knock on your door any day and ask you to sell it to them below the market level. Sure, you can refuse the deal, but then, be prepared to face tens of their unexpected controls for whatever invented reason, hunting you day and night, until, eventually, you will have no other choice than to give up or go bankrupt. (Chisinau, June 2009)

Local reformers originally estimated that Moldova's 67 inspectorates had created around 300 to 500 business regulations However, the actual number revealed through the USAID "Guillotine" program was of more than 1,100, many of them illegal or "unofficial" (Jacobs and Astrakhan, 2006, p. 3). The lack of protective rules against public actors' abusive behavior is evident from firms' failure to succeed when taking legal action against abusive public actors. So far, Moldovan entrepreneurs have never won a lawsuit against the state in court, except for a few extreme cases resolved at Strasburg, at the European Court for Human Rights (ECHR).

5. Policy Implications

The main lesson for World Bank's DB experts, reformers, and enthusiasts is that DB reforms can have unrecognized effects in weak democracies. First, the (formal) reforms in Moldova fail to serve the entrepreneurs because of their lower quality as compared to their evasive (informal) alternatives. Second, the reforms fail because of the public actors' ability to renege on their formal reform commitments through covert forms of predation and lack of institutions to check their informal transactions with corporate actors. Consequently, the main policy implications are twofold:

1. When evaluating institutional change in weak democracies, the DB studies must incorporate: a) an analysis of the quality of reforms and b) an analysis of the credibility of the governments of weak democracies to commit to a high-level of quality reforms. Therefore, the DB report should include a measurement of the underlying informal institutions that could interfere with the intended reforms. The interested public,

governments, entrepreneurs, and others should be aware of the possible trade-off of quantity-quality that DB reports do not address in their measurements.

2. When consulting the annual DB reports and the World Bank policy recommendations, the policy advisors and decision makers of weak democracies like Moldova must understand the fallacies in trying to import the types of reforms that have been successful in other institutional contexts. Consequently, both local reformers and World Bank economists should expect the difference in outcomes that different institutional contexts can generate on individuals' interaction. Their task is therefore to indentify those institutional strengths and weaknesses the consideration of which could help craft qualitative DB reforms that would lead to a *de facto* improvement in Moldova's entrepreneurial environment and growth.

In the following paragraphs, I list three more specific policy implications for assessing and improving the effect of DB reform in Moldova. These policy implications and recommendation correspond to the institutional weaknesses that currently create a wedge between the seen and the unseen impact of the DB reforms.

First, it is of essential importance for the Moldovan policy makers to remove the vagueness in the business legislation texts so that the latter leave no room for regulators' discretion and abuse of private property.

Second, reforms should aim at limiting Moldovan political actors' ability to renege on their reform commitments (Boettke, 2001, p.157) on both official *and* unofficial grounds.

Constitutional reforms must constrain public officials' power to serve privileged interest groups, or to distort the reading of legislation for extortion or expropriation purposes. A particular lesson from prevailing unofficial practices of taxation and extortion in Moldova is that reforms must reduce the payoffs of *ex-post* opportunities for private property predation. One solution to this problem is to increase government transparency and accountability by allowing for more media freedom and competition (Coyne and Leeson, 2004, 2009). Another solution is to establish constitutional constraints (Sautet, 2008) on government taxation and regulation by means of a) a fiscal constitution: to limit taxation and balance the budget and b) a regulatory constitution: to limit industry regulation (including competition law) and to require compensation for regulatory takings.

Third, top-down, exported regulatory reforms like the DB reforms or "The Guillotine" are failing to achieve positive change in Moldova because of the freedom enjoyed by the public officials to extract significantly higher rents from productive entrepreneurs in the future. This is happening because Moldova's institutions lack the fundamental mechanisms of good governance—moderation, transparency, and accountability of political and governmental institutions.

Political actors' short-term gains from implementing good reforms are insufficient to offset the loss of their future flows of rents facilitated by maintaining the current institutional arrangements. Thus, regulatory reforms need to take into account bottom-up knowledge as well and privatize the media market. In this respect, the Economist Intelligence Unit currently also recognizes the detrimental weaknesses in Moldova's institutional context that threaten genuine reform plans:

> Under IMF guidance, some advances on structural reform and improvements in the business environment are possible in the forecast period. For example, the government has pledged to reduce the burden on business by combating excessive bureaucracy and corruption, liberalizing the economy and reducing monopolies,

> as well as by reforming the judiciary. However, weak administrative capacity and the presence of vested interests in the bureaucracy will continue to constrain progress. A less stable political environment, including the strains of coalition government and the prospect of another parliamentary election in 2010 or 2011, in combination with the pressures of the economic downturn, are also likely to distract from the pursuit of reform. (EIU, 2010)

Moreover, in a recent public meeting,[20] 40 representatives of the Moldovan private business sector and parliamentarians from the Public Finance Committee, proposed the following punctuated legislative measures[21] to improve doing business in Moldova:

1. To address the problem of unofficial taxation associated with harassment from control and inspection agencies:
    - Modify article 118 in the Moldovan Fiscal Code[22] to grant firms the time to correct existing mistakes in their financial reports prior to fiscal controls.
2. To address the problem of corruption at customs associated with redundant changes in trade legislation and practices:
    - Assure entrepreneurs that with respect to customs valuation of import merchandise, the current Customs Code of Moldova is correctly enforced. Mainly, when probing documents exist, apply only the method of "transaction value."

[20] http://www.viitorul.org/libview.php?l=ro&idc=171&id=2748

[21] The complete list of the proposed measures http://www.viitorul.org/libview.php?l=ro&idc=171&id=2748

[22] Article 118. The evidence of merchandise and services

(1) Every taxpayer must keep account of all merchandise, all delivered services, and physical goods, acquired services. In retail services, the taxpayers must keep daily account of all delivered merchandise, all delivered and aquired services in cash. The evidence/report on all these activities must be completed within a month of the end of the fiscal year of the VAT.

(2) Fiscal receipts on physical goods, purchased services, must be ordered in successively and registeded successively in the evidence documents. http://www.law-moldova.com/laws/rom/nalogoviy_codex_ro.txt

Another set of key priorities for improving the context of doing business in Moldova outlined in the "National Business Agenda 2010"[23] are the following three measures addressing needed policy and institutional reforms:

1. Reducing red tape and fostering free competition.
2. Improving the fiscal legislation.
3. Strengthening the rule of law.

The fact that these reform proposals come from entrepreneurs one year after the "'Doing Business" report classified Moldova as a top reformer strengthens the central hypothesis of my essay: because of an existent significant gap between the Moldovan government's *de jure* and *de facto* commitment to reforms, the impact of the current DB reforms on entrepreneurship and development is overestimated, and more careful consideration to the quality of the fundamental institutions supporting policy reforms is needed.

6. Conclusion

In "The Regulation of Entry," the foundational study for the World Bank's "Doing Business" project, Djankov, La-Porta, Lopez-de-Silanes, and Shleifer, show that business entry is compromised by costs associated with corruption and bureaucratic delays, and that more interventionist governments regulate more heavily. Their results have prompted the development community to encourage governments to implement reforms that would reduce these costs for entrepreneurs in their country. While I

[23] The National Business Agenda is supported by the National Confederation of Business from Moldova, The Chamber of Commerce and Industry of the Republic of Moldova, and others. In Moldova, the promotion is facilitated by the Institute for Development and Social Initiatives (IDIS) in partnership with ICPE (The International Center for Private Entrepreneurship).

acknowledge their essential contribution to public choice empirics, I disagree that decreased *de jure* regulation necessarily lowers barriers to entry. I use the case of post-Soviet Moldova to illustrate that this correlation is context-dependent. Mainly, in a weak institutional context, where economic, political, and media freedoms are significantly limited, the real effect of reducing bureaucratic barriers to entry and corruption opportunities might not be equal to outsiders' perceptions or expectations. I argue that in order to overcome the measurement problem posed by the existing confusion of the *de jure* with *de facto* impact of DB reforms in Moldova, international researchers, policy makers, and the public must explore the diversity and the quality of indigenous institutions. Mainly, this policy essay uncovers the unseen effects of DB reforms within Moldova's weak institutional context. The cost of current and prospect entrepreneurial activities in Moldova is exaggerated by the exiting informal institutional arrangements, such as the system of "unofficial taxation," or corruption in the "shadow economy." Consequently, a prerequisite for reform success is a context of legal and judicial institutions conducive to development. An ideal institutional context for entrepreneurship includes well-defined property rights, freedom of contract and its enforcement, and limited interference from government authorities with market outcomes (Kirzner & Sautet, 2006). It is only within an institutional context of well-defined and well-enforced property rights, a free and competitive media market, and constitutional constraints on public predation that one could consider the intended beneficial effects of DB reforms in Moldova a success. Absent such fundamental conditions, their alleged success should be open to discussion.

Thus, reforms should aim at eliminating the sources of institutional uncertainty and inefficiency. My study indicates that the activity of active and prospective entrepreneurs in Moldova is mostly threatened by government corruption and abuse of power. Removing the source of incentives for these types of socially unproductive activities would thus lead to an increase in DB reforms' efficacy and permit economic growth. I contend that in Moldova's case, in order to achieve the expected beneficial effects intended through DB reforms, both domestic and international researcher and reformers must complement their strategies with solutions to improve the quality of the institutions, with a particular emphasis on mechanisms to eliminate the source of incentives for corrupt behavior of political actors.

Appendix

A) Map of Moldova

Source: The Economist Intelligence Unit, annual country report 2010.

B) List of selected interviews used from the paper "Institutions, Entrepreneurship, and Post-Soviet Development: An Assessment of Moldova's Entrepreneurial Environment," based on my field research in Chisinau Moldova, June 2009.

Type of entrepreneurial activity		Position	Interview trip to Chisinau	Page Number(s)
4	Driving School	Owner	June 2009	19
2	Import-Export	Employees	June 2009	19
5	Logistics	Development Manager	June 2009	25
3	Restaurant	Owner	June 2009	48
1	Think Tank	Executive Director	June 2009	44, 47

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