



MEMO

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CC: The Ministry of Energy, attention State Secretary for Decarbonisation Carolina Novac

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MOLDOVAGAZ DEBT AUDIT: FINAL REPORT

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1 BACKGROUND

1.1 Project overview

- (1) On 29 October 2021, the Republic of Moldova ("**Moldova**") (also referred to as the Moldovan side), JSC "Moldovagaz" ("**Moldovagaz**")¹ and PJSC "Gazprom" ("**Gazprom**") signed a negotiation protocol concerning settlement of problematic issues in the gas sector of the Republic of Moldova (the "**Protocol**"). Item 5 of the Protocol provides that before the conclusion of a debt settlement agreement between Moldovagaz and Gazprom, the Moldovan side shall perform an independent audit of Moldovagaz's debts to Gazprom and LLC Faktoring-Finans ("**Faktoring-Finans**")² for gas delivered to consumers on the right bank of the Nistru.³ The Protocol envisages that the debts shall be fully settled in the course of 5 years.
- (2) The Public Property Agency of the Government of Moldova (the "**PPA**")⁴ was subsequently tasked by the Moldovan Government to organise the independent audit pursuant to item 5 of the Protocol. After delays in the engagement of external auditors due to attempts to intervene in the process on the part of Gazprom, as well as the lack of bids from non-conflicted auditors, PPA engaged Wikborg Rein Advokatfirma AS ("**WR**") and Forensic Risk Alliance Limited ("**FRA**") (together the "**Auditors**") to perform the independent audit⁵ on 10 August 2022. The completion date for the audit was initially set as 30 January 2023.
- (3) It follows from items 1.1 and 1.2 of the "*Tender Book for the acquisition of the financial and legal audit services related to debt of Moldovagaz to Gazprom and Faktoring-Finans for gas deliveries to consumers of the Republic of Moldova from the right bank of the Nistru River*" (the "**Tender Book**")⁶ that the scope of the audit is limited to alleged debts for gas deliveries to consumers on the right bank of the Nistru, incurred in the period 27 August 1991 to 31 October 2021 (the "**Debt**"), cf. also item 5 of the Protocol. The "**Right bank**" is defined by the second paragraph of item 1.1 of the Tender Book as "*the areas of Moldovan territory mainly on the right bank of the Nistru river which are de-facto controlled by the constitutional and internationally recognized Moldovan Government in Chisinau*", as opposed to the "**Left bank**", which is defined in the same paragraph as the "*the areas of Moldovan territory on the left bank of the Nistru River, in the Transnistrian region, which is de-facto controlled by the self-proclaimed unconstitutional authorities in Tiraspol*".
- (4) Pursuant to item 2.1 of the Tender Book, the Auditors are to, *inter alia*, (A) "*undertake a wide-ranging investigation into the alleged 'right bank' debts of Moldovagaz*", (B) consider "*the source, origin and nature of all 'right bank' debts allegedly owed by Moldovagaz since the creation of the company and its predecessor companies from 27th August 1991*", (C) undertake a "*thorough investigation of the claims of Gazprom and its subsidiaries*" and (D)

¹ The name "Moldovagaz" has been used for several entities, including the "state concern Moldova-Gaz", the "concern Moldovagaz" and "republican production association Moldova-Gaz", which existed prior to the establishment of JSC Moldovagaz in 1999. When referring to "Moldovagaz" in this report, we refer exclusively to the present JSC Moldovagaz.

² Faktoring-Finans is a wholly-owned subsidiary of Gazprom.

³ Nistru is also known as *Dnister* in Ukrainian and *Dnestr* in Russian. Right/left bank refers to the right/left bank of the river when facing the river downstream.

⁴ In Romanian: "*Agenția Proprietății Publice*", abbreviated "*APP*".

⁵ The term "audit" is used in this report for consistency purposes only, as it was used in the Tender Book. FRA and WR services do not constitute an audit of the financial statements as defined in the International Standards on Auditing (ISA).

⁶ The Tender Book was provided to the Auditors by the PPA prior to submission of the tender bid and is attached as **Appendix No. 1** to this Report.

consider "the existence of evidence of any potential basis for counter-claim or infringements of the rights of the minority shareholder that may or may not have occurred". The ultimate purpose of the audit is to determine the exact scope of the debts that may be owed to Gazprom and Faktoring-Finans for gas deliveries to consumers on the Right bank, cf. item 2.2 of the Tender Book.

- (5) While the Tender Book only separates between the 1991 to 2004 period and the 2004 to 2021 period, the Auditors have chosen to break these two periods down into three different time periods, namely (i) pre-1999; (ii) 1999 to 2002; and (iii) 2003 to 2021, in light of the availability of data in different time periods.
- (6) The Tender Book lists several issues, which primarily concern the financial side of the audit, that the audit must address to establish the exact scope of the Debt,⁷ namely:
1. Verification of Moldovagaz's and its predecessors' allocation of payments for gas consumption among consumers on the Right and Left banks;⁸
 2. Verification of the valuation of assets previously transferred to Gazprom as (partial) settlement of debts for gas delivered to consumers on the Right bank, and, if necessary, revaluation of such assets;⁹
 3. Verification that previous payments have been correctly allocated to settle debts accrued for gas deliveries to consumers on the Right bank;¹⁰ and
 4. Verification of the legality of Gazprom's assignment(s) of claims to Faktoring-Finans.¹¹
- (7) The Tender Book further states that, as an additional objective, the audit should report on the reasons for the accrual of the Debt which may render parts of the Debt subject to legal challenge, which includes reporting on:
1. The legality and/or conformity with custom and practice of the penalty interest rates charged;¹²
 2. Costs incurred by Moldovagaz's management beyond the costs which can be recovered through the Moldovan regulated gas tariffs;¹³
 3. Moldovagaz's management's handling of foreign currency procurement and gas losses issues;¹⁴ and
 4. The legality and conformity with international practice of the distribution of Gazprom's transit tariff payments between Moldovagaz and the *de facto* operator of the parts of the Moldovan gas transmission system situated on the left bank of the Nistru river.¹⁵
- (8) We have also identified additional issues in the course of the audit, which, *inter alia*, relate to

⁷ See item 1.2 of **Appendix No. 1: Tender Book**.

⁸ See Section 4.3 below.

⁹ See Section 4.3.2 below.

¹⁰ See Section 4.6 and 4.7 below.

¹¹ See Section 4.3.3 and 5.3 below.

¹² See Section 5.4 below.

¹³ See Section 5.6 below.

¹⁴ See Section 5.6 below.

¹⁵ See Section 5.5 below.

the establishment of Moldovagaz's predecessor, Moldovan-Russian Joint Stock Company Gazsnabtranzit ("**Gazsnabtranzit**"), in 1995, and to the establishment of Moldovagaz itself in 1999, as well as issues related to the existence of parts of the Debt and its enforceability in Moldova.¹⁶

- (9) Some of the issues listed by the Tender Book concern either Moldovan or Russian law¹⁷ or both. To assess the issues relating to Moldovan law, the Auditors have engaged the Moldovan law firm Buruiana & Partners ("**Moldovan Counsel**"). For the questions concerning Russian law, the Auditors have engaged the Swedish law firm Mannheimer Swartling Advokatbyrå AS ("**Russian Counsel**"), which previously had a branch office in Moscow, Russia and still retains a Russian qualified lawyer who has assisted on this assignment.¹⁸
- (10) We assess all the issues mentioned above in Sections 4 and 5 below.
- (11) On 10 November 2022, the Auditors issued a Discovery Report pursuant to item 2.3 of the Tender Book. The Discovery Report assessed the quality and completeness of the data then available, in particular in respect of the period 2004 to 2021. On 6 February 2023, the Auditors issued the Preliminary Assessment Report, covering all of the issues listed above. This Final Report is based closely on and further develops the Preliminary Assessment Report.
- (12) As will be further explained in Section 3 below, the Auditors have not been provided with sufficient documentation from Moldovagaz or Gazprom to verify the existence, scope or cause of the parts of the Debt which stems from the period 1991 to 31 December 2002.
- (13) The scope, limitations, assumptions and restrictions applicable to this report are set out in Section 6 below.

1.2 Structure of the Final Report

- (14) In Section 2, we provide an Executive Summary of this Final Report, as well as set out our preliminary conclusions, including potential counterclaims. In Section 3, we give an overview of our Requests for Information to Moldovagaz, the Moldovan Government and third parties. Then, in Section 4, we present our findings with respect to the *financial* side of the audit, *inter alia* addressing the issues listed in the Tender Book. Thereafter, in Section 5, we present our findings with respect to the *legal* side of the audit, *inter alia* assessing the legality of the Debt and reporting on the issues which may render parts of the Debt subject to legal challenge, as listed in the Tender Book, as well as assess certain other legal issues.
- (15) This Final Report has five Appendices which constitute an integral part of the report. The Tender Book, which sets out the scope of the assignment, is attached in Appendix No. 1. Appendix No. 2 lists the documents that we have relied on for this report. Appendix No. 3 is a copy of our Fifth Request for Documents to Moldovagaz, dated 6 January 2023. Appendix No. 4 is a legal opinion by the Moldovan law firm Buruiana & Partners concerning certain issues arising from Moldovan law that may be of significance for the Debt ("**Opinion on certain Moldovan law matters**"). Appendix No. 5 is a legal opinion by a Russian qualified lawyer at the Swedish law firm Mannheimer Swartling concerning certain questions under Russian law that may be of significance for the Debt ("**Memorandum on certain Russian**").

¹⁶ See Section 5.7 below.

¹⁷ All of the gas sale and gas transit contracts between Moldovagaz and Gazprom that we have seen are governed by Russian material law.

¹⁸ WR received written approval to engage Buruiana & Partners and Mannheimer Swartling as experts on Moldovan and Russian legislation, respectively, from the PPA on 5 December 2022.

law matters").

2 EXECUTIVE SUMMARY

2.1 Introduction

- (16) This executive summary sets out the key conclusions from both the Financial and Legal audit.

2.2 Main findings

- (17) The recorded Debt as of 31 October 2021 amounts to USD 756,584,129.
- (18) The Auditors note that while the total amount of the counterclaims and recommended write-offs set out below seemingly exceeds the total Debt, it must be kept in mind that the grounds for write-off and potential counterclaims may overlap.
- (19) Due to a lack of records, the Auditors have been unable to audit USD 278,164,061 out of the recorded Debt, allegedly accrued prior to 1 January 2003. This includes the USD 275,914,205 assigned to Faktoring-Finans. This gives Moldovagaz an opportunity to require this part of the Debt to be written off.
- (20) Out of the remaining USD 478,420,068, around USD 400,000,000 is subject to Arbitral Awards¹⁹ which no longer can be enforced in Moldova. This gives Moldovagaz an opportunity to require this part of the Debt to be written off.
- (21) In the period 1 January 2011 to 31 December 2020, Moldovagaz made investments and incurred expenses amounting to USD 143 million²⁰ which were not approved by the National Agency for Energy Regulation of the Republic of Moldova ("**ANRE**" or the "**Regulator**"), for inclusion in the customer tariff. Had any of this expenditure been avoided, more funds may have been available for Moldovagaz to pay down the Debt. To the extent Gazprom as the de facto controlling shareholder of Moldovagaz approved these expenditures, Moldovagaz may have an opportunity to require a corresponding part of the Debt to be written off.
- (22) Moldovagaz may have a counterclaim for approximately USD 160 million of lost transit revenues, paid by Gazprom to LLC Tiraspoltransgaz – Pridnestrovie ("**Tiraspoltransgaz**")²¹ in breach of custom and practice.
- (23) We understand that since October 2022, Gazprom has been in breach of its delivery obligations to Moldovagaz and the Right bank. Moldovagaz may have a counterclaim for resulting penalties payable by Gazprom to be set off against the Debt. The breach of contract is outside the temporal scope of the audit, and the Auditors have not quantified this potential set-off.
- (24) The Auditors have discovered irregularities and illegalities in the founding of Moldovagaz and its predecessor Gazsnabtranzit. In particular, the assets transferred by the Moldovan State to the founding capital of these companies in payment for gas previously delivered by

¹⁹ The Arbitral Awards were the awards of the International Commercial Arbitration Court at the Chamber of Commerce and Industry of the Russian Federation issued from 2008 to 2022 in respect of the Debt.

²⁰ USD 143 million is calculated as total USD 231 million of the effect of the key factors of the Debt accumulation, excluding the growth of customer debt and tariff deviations acknowledged by ANRE, i.e. $231 - 67 - 21 = 143$. Refer to Section 4.7.4 for more details.

²¹ The largest gas supplier on the Left bank.

Gazprom were valued contrary to the then prevailing laws of Moldova, and may have been significantly undervalued. Due to a lack of documentation, the Auditors have been unable to quantify the potential undervaluation. Some assets on the Right bank were apparently wrongfully transferred in payment of Left bank debt. An alleged Debt of USD 47,300,000 was also incorrectly not set off against Gazsnabtranzit's equity when Gazsnabtranzit was merged into Moldovagaz. These are further reasons for writing off the Debt allegedly incurred before 1 January 2003.

- (25) Penalties incurred before 2006, and in particular before 1999, may have been excessive and subject to being challenged pursuant to the applicable Russian law. This is another argument for writing off the Debt allegedly incurred before 1 January 2003, which includes USD 165,757,466 of accrued interest and penalties. Since April 2005, Moldovagaz has refused to accept Gazprom's penalty claims, and penalty claims accrued prior to 2020 are now time-barred under the applicable Russian law.
- (26) At the founding of Moldovagaz, Gazprom secured its position as monopoly supplier to Moldovagaz. Apparently, Gazprom has allowed Debts to accrue without taking steps to enforce payment against or restructure its subsidiary Moldovagaz in order to protect its continued, presumably profitable, monopoly position in Moldova. This makes it reasonable for Gazprom to write off all of or significant parts of the Debt.
- (27) Gazprom apparently entered the Moldovan gas business by taking an equity share in Gazsnabtranzit in 1995 acting in the interest of the Russian Federation. To the extent Gazprom has to write off claims arising from its pursuit of the Russian Federation's interests, Gazprom may seek recourse from the Russian Federation.

2.3 Information requests and documentation received

- (28) From the outset of this audit, the Auditors have requested both legal and financial information from Moldovagaz in order to complete their mandate. This includes five formal information requests together with meetings and calls with representatives of Moldovagaz to seek explanations and further clarifications.
- (29) Moldovagaz confirmed that it does not retain any significant information dated prior to 1 January 2003 as it stated that it had either not retained the data or had not taken possession of the data on its formation in 1999. In addition Moldovagaz was unable to provide certain information for the period post 1 January 2003 within the required timeframe to allow the Auditors to complete the full scope of work as set out in the Tender Book. In addition the longest serving senior employee in Moldovagaz's finance team started in 2014, thereby restricting the availability of personal knowledge of earlier periods.
- (30) A significant amount of the information received from Moldovagaz for the period post 1 January 2003 was provided in pdf documents rather than in the format required. This resulted in additional time and effort to convert the information received into a useable structured format, and some of the data for this period was incomplete.
- (31) The Auditors note that the management of Moldovagaz actively engaged with the Auditors and provided a number of analytical calculations and other data to facilitate the Audit process.
- (32) In addition to the information requested from Moldovagaz the Auditors also requested relevant information and data from the following:
 1. Gazprom – A first written request was sent by the Director General of the PPA on 13 October 2022 requesting Gazprom to assist Moldovagaz to provide the information requested by the Auditors. A further letter signed by the Deputy Prime Minister and

Minister of Infrastructure and Regional Development was sent on 30 January 2023 requesting supporting data for the Debt allegedly accrued in the period prior to the creation of Moldovagaz in 1999. Gazprom has not responded.

2. ANRE – information relating to the tariff setting methodology and interactions with Moldovagaz.
 3. Government archives – the Government sought to find relevant archived material at the National Archives, National Bureau of Statistics, Customs Authority, Fiscal Authority and Government Archives. The majority of the information found was at a summary level rather than the required detailed level.
- (33) The Auditors also understand that Moldova's representatives on Moldovagaz's Supervisory Board have made efforts to facilitate Moldovagaz's provision of documents and information for the purpose of the Audit.
- (34) A particular challenge is the absence of practically all contractual documents preceding 1 July 1999. This has made it difficult for the Auditors to assess and/or verify the legality, existence, scope or cause of the parts of the Debt that stem from the early period from 1991 to 1999.

2.4 Financial Audit

2.4.1 Scope

- (35) The Tender Book set out a number of objectives relevant to the financial audit²²:
1. *Verification of Moldovagaz's and its predecessors allocation of payments for gas consumption between consumers on the Right and Left banks;*
 2. *Verification that previous payments have been correctly allocated to settle debts accrued for gas deliveries to consumers on the Right bank;*
 3. *Verification of the valuation of assets previously transferred to Gazprom as (partial) settlement of debts for gas delivered to consumers on the Right bank, and, if necessary, revaluation of such assets;*
 4. *To report on the reasons for the accrual of the Debt, inter alia:*
 - a. *Costs incurred by Moldovagaz management's beyond the costs which can be recovered through the Moldovagaz tariffs; and*
 - b. *Moldovagaz management's handling of foreign currency procurement and gas losses.*
 - c. *Impact of the Debt of exchange rate fluctuations between the time of accumulation of debts to Gazprom (in USD) and the time of their settlement by Moldovan debtors (in MDL)*

²² Appendix No. 1: Tender Book, Section 1.2.

d. Accrual of penalties and correctness of the repayment of principal debt and penalties during the years 1993 to 2021.

2.4.2 *Audit work*

- (36) Due to the lack of underlying supporting data the Auditors have been unable to audit the debt accrued during the period 27 August 1991 to 31 December 2002. This includes audit of the debt-to-equity swaps undertaken in 1995 and 1999.
- (37) For the debt accrued in the period 1 January 2003 to 31 October 2021 the Auditors have undertaken the following procedures:
5. Verified the gas volumes stated as delivered by Gazprom to the Right bank with gas metering records provided by JSC Ukrtransgaz, the former Transmission System Operator of Ukraine ("**Ukrtransgaz**") in Section 4.44.4;
 6. Verified the contract gas prices to the actual gas prices charged by Gazprom in Section 4.44.4;
 7. Verified the annual and monthly summary records of gas volumes and gas cost delivered to Right bank to underlying contemporaneous accounting records in Section 4.4;
 8. Verified the annual and monthly summary records of payments by Moldovagaz to reduce Right bank gas debt to underlying contemporaneous accounting records in Section 4.54.5;
 9. Review of the use of funds received by Moldovagaz from its customers, e.g. amounts used to reduce the Debt versus amounts used for other purposes such as investments and operating expenses in Section 4.64.6;
 10. Analysis of the key factors contributing to the increase of the Debt for the period 2011 to 2020, including the impact of USD : MDL exchange rate movements, in Section 4.7.

2.4.3 *Debt owed as at 31 October 2021*

- (38) Moldovagaz's accounts record the total debt owed to Gazprom and Faktoring-Finans for deliveries of natural gas to the Right bank as at 31 October 2021 to be USD 756,584,129 (MDL 13,253 million²³).
- (39) Moldovagaz records the Debt due from the Left bank to Gazprom and Faktoring-Finans as at 31 October 2021 to be USD 7,608,876,836 (MDL 133,280 million). Moldovagaz confirmed that it does not recognise any liabilities in relation to the debt owed by the Left bank. The value of the Left bank debt is outside the scope of the Audit.

2.4.4 *Chronology of Right bank Debt growth*

- (40) The Auditors have split the Debt growth into three periods:

²³ Exchange rate at 31 October 2021: 1 USD = 17.5164 MDL.

1. 27 August 1991 to 1 July 1999: Debt increased in this period to USD 172,242,518²⁴ (MDL 1,954 million²⁵)
- (41) This date range relates to the period of Debt accrued during the operation of Moldovagaz's predecessor companies. Moldovagaz states that it does not possess any underlying records from this period, including in relation to the opening Debt balance taken onto its books of account at the date of its creation. No significant underlying data relating to this period has been provided by other sources.
2. 1 July 1999 to 31 December 2002: Debt increased in this period by USD 105,921,543 to USD 278,164,061 (MDL 3,845 million²⁶), comprising:
 - USD 112,406,595 for the main body of the Debt; and
 - USD 165,757,466 of accrued interest and penalties.
- (42) This date range relates to the first few years following the creation of Moldovagaz. Moldovagaz states that it has not retained the underlying records related to the Debt development during this period.²⁷ Two specific transactions helped reduce the Debt value in this period: the Government of Moldova made an additional payment of USD 90 million in 2000 to Moldovagaz to reduce the Debt; and, the application of a set off of approximately USD 47 million, recorded in 2001, in relation to assets transferred to Gazprom on the incorporation of Moldovagaz.
3. 1 January 2003 to 31 October 2021: the Debt increased during this period by USD 478,420,068 to USD 756,584,129 (MDL 13,253 million²⁸) comprising:
 - USD 600,787,091²⁹ for the main body of the Debt; and
 - USD 155,797,038³⁰ of accrued interest and penalties.
- (43) Moldovagaz provided the majority of the requested underlying data and summary records relating to the Debt growth during this period. This was the period in which the Debt grew fastest in USD terms, in particular the years 2006 to 2015. Since 2015 the debt balance in USD has remained relatively stable. The following significant transactions occurred in this period: in 2006 all of the debt stated as due to Gazprom as at 31 December 2005, USD 120,117,167, together with interest and penalties of USD 155,797,038 accrued prior to 1 April 2004, totalling USD 275,914,205 was transferred to Faktoring-Finans, a Gazprom subsidiary.³¹ This balance due to Faktoring-Finans has remained unchanged since.
- (44) A remaining balance of USD 20,923,541 for interest and penalties due to Gazprom accrued prior to 1 April 2004 was written back by Moldovagaz in 2009.

²⁴ This is the opening balance as at 1 July 1999 as per the spreadsheet comprising annual debt balance and payments for the period 1999 to 2021 prepared by Moldovagaz.

²⁵ Exchange rate at 1 July 1999: 1 USD = 11.3444 MDL.

²⁶ Exchange rate at 31 December 2002: 1 USD = 13.8220 MDL.

²⁷ Except for Acts of Acceptance stating the volumes of natural gas received in Moldova, signed by Ukrtransgaz and Gazprom.

²⁸ Exchange rate at 31 October 2021: 1 USD = 17.5164 MDL.

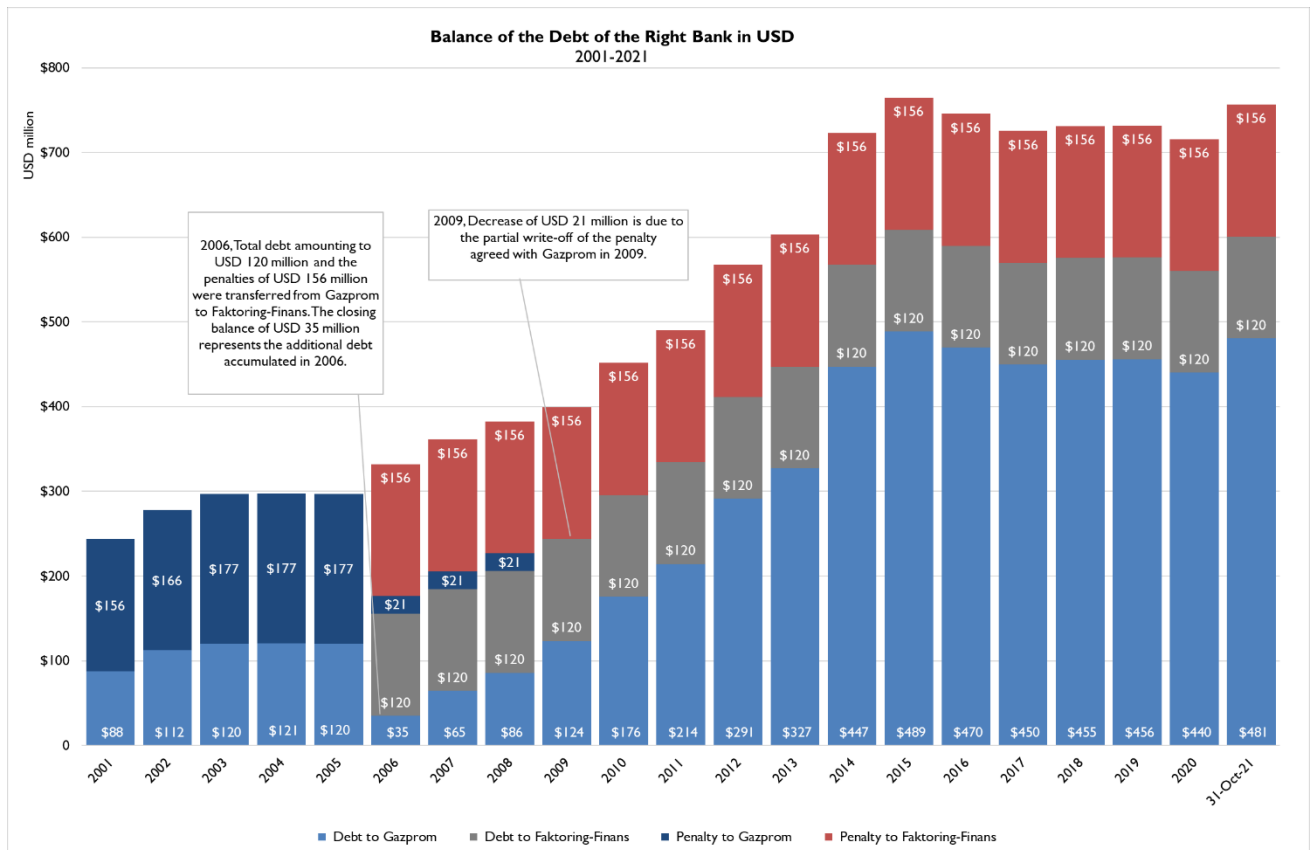
²⁹ USD 480,669,924 owed to Gazprom and USD 120,117,167 owed to Faktoring-Finans.

³⁰ USD 155,797,038 owed to Faktoring-Finans.

³¹ Debt Transfer Agreement between Gazprom and Faktoring-Finans No8ΦΦ-2005 dated 1 December 2005.

- (45) No liability for interest and penalties has been accepted by Moldovagaz since 1 April 2004.³²
- (46) The chronology of accumulation of the Debt in USD due to both Gazprom and Faktoring-Finans for gas deliveries to the Right bank during the period 1 January 2001 to 31 October 2021 is set out in Figure 1 below³³.

Figure 1.

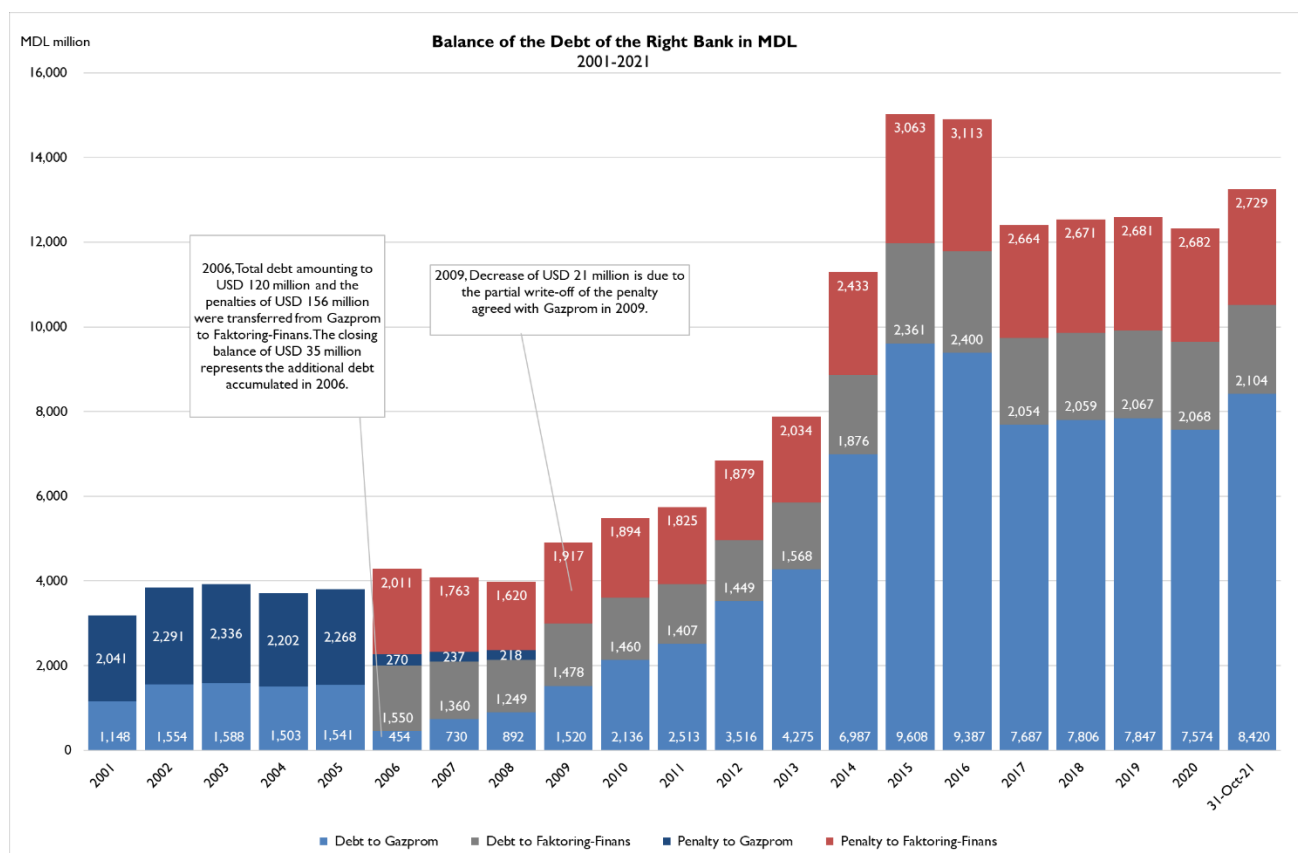


- (47) The same chronology but showing the accumulation of the Debt in MDL due to both Gazprom and Faktoring-Finans is set out in Figure 2 below.

³² Except for the accrual of USD 15,241 of penalties on 31 December 2006, which were reversed on 29 December 2007.

³³ Moldovagaz did not provide the Auditors with the debt growth chronology for the period prior to 1 January 2001.

Figure 2.



(48) The profile of the Debt growth differs when denominated in MDL as compared to USD due to fluctuations in the USD vs MDL exchange rate.

2.4.5 Verification of Right bank Debt growth

(49) The summary results of the Auditors work to verify the Debt stated by Moldovagaz as owing to Gazprom and Faktoring-Finans for Right bank gas consumption as at 31 October 2021 are as follows:

- No verification of the Debt accrued between 27 August 1991 and 31 December 2002, totalling USD 278,164,061 has been possible due to neither Moldovagaz or Gazprom providing any underlying data to support the quantum of debt accrued, or the quantum of debt repaid, during this period. Schedules prepared by Moldovagaz summarising the Debt growth since its incorporation in 1999 do evidence that a sum of USD 90,000,000 was applied to reduce the Debt in the year 2000, and that approximately USD 47 million was applied to reduce the Debt as a result of the debt-to-equity swap on the creation of Moldovagaz.
- No verification of the penalties and interest totalling USD 155,797,038 added to the debt transferred to Faktoring-Finans in 2006 has been possible as a result of neither Moldovagaz nor Gazprom providing any underlying data to support the calculation of this amount.

3. The Auditors have verified the volume and cost of the gas delivered to Right bank in the period 1 January 2003 to 31 October 2021, and that all payments made by Moldovagaz to Gazprom have been correctly allocated to settle the Debt accrued by deliveries of gas to the Right bank. The verified net increase of the Debt in this period is USD 478,420,068, representing just over 63% of the total Debt balance stated as being owed by the Right bank to Gazprom and Faktoring-Finans as at 31 October 2021. The majority of the unverified Debt balance is owed to Faktoring-Finans.
4. The Auditors verified that no additional liability for interest or penalties has been recognised or recorded by Moldovagaz during the period 1 April 2004 to 31 October 2021.³⁴

2.4.6 *Key factors causing the debt increase.*

- (50) As stated in Section 2.2 above the debt due to Gazprom and Faktoring-Finans as at 31 October 2021 was USD 756,584,129 or MDL 13,253 million.
- (51) The Auditors have reviewed and, where possible, verified an analysis prepared by Moldovagaz as to the causes of the Debt increase between 1 January 2011 and 31 December 2020. The debt increased in this period by USD 264,199,990 (approximately 35% of the Debt in USD terms as at 31 October 2021) or in local currency by MDL 6,834,000,000 (approximately 52% of the Debt in MDL terms as at 31 October 2021).
- (52) The reason the debt in local currency has increased to a greater extent than the increase when denominated in USD is due to the depreciation of the MDL over this period. The impact of the currency depreciation is estimated to account for around MDL 3,242 million of the growth in local currency over the period 1 January 2011 to 31 December 2020. The exchange rate was at its highest in 2015 and 2016 with 19.9814 MDL to 1 USD on 31 December 2016, with the net appreciation of the currency since then reducing the impact of the earlier more significant depreciation. The impact of this net adverse exchange rate movement over the whole period was not in the control of Moldovagaz³⁵, however, had the debt been kept lower in earlier years the impact from the adverse exchange rate movement would have been smaller.
- (53) The following are the key factors resulting in the increase of the USD Debt in the period 1 January 2011 to 31 December 2020 (which represent approximately USD 231 million³⁶ out of the total USD 264 million total increase in this period):
 1. MDL 982,000,000 (USD 67 million equivalent) – due to the growth in the total debt due from Moldovan customers and other receivables to Moldovagaz in the period 1 January to 2011 to 31 December 2020. As per Moldovagaz accounts: total customer debts and other receivables as of 1 January 2011 were MDL 2,197 million (USD 150 million) and

³⁴ An amount of interest and penalties was accrued by Moldovagaz in the early part of this period but was written back in 2009.

³⁵ No hedge was applied.

³⁶ USD equivalent of the Debt increase was calculated based on the average exchange rate between 1 January 2011 and 31 December 2020, or 1 USD = 14.6843 MDL, calculated as $(12.1539 + 17.2146) / 2$. Same rate was used to calculate USD equivalents of the key factors below.

as of 31 December 2020 these were MDL 3,205 million (USD 218 million)³⁷³⁸. This debt if repaid to Moldovagaz by its customers would provide Moldovagaz with funds to reduce the Debt;

2. MDL 669,000,000 (USD 46 million equivalent) – due to natural gas losses³⁹ during the period 1 January 2011 to 31 December 2020 not accepted by ANRE in the calculation of the customer tariff, i.e. Moldovagaz did not recover the value of these losses through the customer tariff but was still required to pay for its cost to Gazprom;
3. MDL 465,000,000 (USD 32 million equivalent) – due to the cost of construction of Moldovagaz's new headquarters at 64 Puschkin Street not accepted by ANRE for inclusion in the customer tariff i.e. Moldovagaz was not able to recover the cost of these investments;
4. MDL 341,000,000 (USD 23 million equivalent) – due to investments made by Moldovagaz not accepted by ANRE in the calculation of the customer tariff. These investments included measures to reduce natural gas losses;
5. MDL 312,000,000 (USD 21 million equivalent) – due to tariff deviations acknowledged by ANRE, to be recovered through the tariff for the period 2021-2025.
6. MDL 253,000,000 (USD 17 million equivalent) – due to interest and commissions not accepted by ANRE for inclusion in the customer tariff;
7. MDL 147,000,000 (USD 10 million equivalent) – due to the cost of foreign currency purchases not accepted by ANRE for inclusion in the customer tariff;
8. MDL 115,000,000 (USD 8 million equivalent) – transit service fees not received by Moldovagaz during transition to a new transit tariff methodology not yet accepted by ANRE for inclusion in the customer tariff; and
9. MDL 103,000,000 (USD 7 million equivalent) – Moldovagaz expenses not accepted by ANRE for inclusion in the customer tariff.

(54) The costs listed in factors 2 to 9 above were to varying degrees in the control of Moldovagaz. There have been several reports prepared on Moldovagaz's expenditure which claim that certain expenditure, for example in relation to the cost of its new headquarters, was excessive, unwarranted or poor value for money. The Auditors have not sought to verify if each expense was justified or undertaken at value, but whether it was allowed or not by ANRE for customer tariff setting purposes. For example, items 4 and 9 were not allowed because Moldovagaz did not demonstrate the economic efficiency of the investments and expenses. Had any of this expenditure been avoided the funds would have instead been available to pay down the Debt. Equally had any of the above expenditure been allowed by ANRE in the calculation of the customer tariff then more funds may have been available to

³⁷ As of 01 January 2011, MDL 2,197 million = MDL 1,974 million (Customer debt) + MDL 233 million (Other receivables); as of 31 December 2020, MDL 3,205 million = MDL 2,823 million (Customer debt) + MDL 382 million (Other receivables).

³⁸ The growth of the total debt of MDL 982 million or USD 67 million (as per Moldovagaz management), when matched with MDL 1,008 million = MDL 3,205 million – MDL 2,197 million or USD 68 million = USD 218 million – USD 150 million of growth of the total debt (as per accounting records), gave MDL 26 million or USD 1 million difference, which the Auditors considered immaterial.

³⁹ Via theft or leakage.

Moldovagaz to pay down the Debt.

- (55) The customer tariff allows an element of profit for Moldovagaz which it can choose to use for investment and expenses not allowed by ANRE in the customer tariff. Moldovagaz advised that they have not paid dividends in any year. The Auditors reviewed Moldovagaz' financial statements for the years 2016 to 2021 and did not identify payment of any dividends to shareholders, indicates the profit element of the tariff in these years was utilised which might otherwise have further reduced funds available to pay down the Debt.
- (56) The Auditors performed analysis of Moldovagaz's cash flows, and noted that the majority of cash received from customers has been used to pay down the debt due to Gazprom and to pay customs. However, it also shows that the cash paid for operating expenses has been increasing as a percentage of overall cash outflows.

2.4.7 *Valuation of assets previously transferred to Gazprom as (partial) settlement of the Debts*

- (57) The Auditors have been provided with information that sets out a partial chronology of the two debt-for-equity swaps at the incorporation of Gazsnabtranzit in 1995 and the incorporation of Moldovagaz in 1999. However, no detailed information or underlying supporting data has been provided to allow the Auditors to assess the veracity of the value of the Debt set off in respect to these transactions.
- (58) Moldovagaz provided the Auditors with a copy of a report dated 19 December 2008 prepared by Ecofin-Audit-Service SRL. Their scope of work was to revalue the fixed assets acquired by Moldovagaz on incorporation as well as fixed assets acquired by Moldovagaz since incorporation. The report findings resulted in a substantial increase in the value of fixed assets which was then reflected in Moldovagaz' accounts. The report findings though do not make it possible to split the revaluation between assets available prior to the creation of Gazsnabtranzit and Moldovagaz, or to split the revaluation between the periods pre and post the debt-to-equity swaps.
- (59) Given the lack of underlying supporting data in relation to the assets included in the debt-to-equity swaps, the passage of time (over twenty years) and the changes in market conditions the Auditors do not believe a revaluation of the assets transferred in the debt-to-equity swaps as at the date of those swaps is achievable.

2.4.8 *Summary Financial Audit Observations and Findings*

- (60) The Debt balance stated by Moldovagaz as owing by Right bank to Gazprom and Faktoring-Finans as at 31 October 2021 totals USD 756,584,129.
- (61) Due to the lack of underlying supporting documentation, it has not been possible to audit the Debt growth, or penalties and interest accrued, in the period 27 August 1991 to 31 December 2002, or the debt-to-equity swaps undertaken in 1995 and 1999.
- (62) For the period 1 January 2003 to 31 October 2021, during which the Debt increased by USD 478,420,068, the audit work completed to date has verified:
1. The volumes of gas delivered to Right bank in the period 1 January 2002 to 31 October 2021;
 2. The cost of the gas delivered by Gazprom during the above period;
 3. That all payments made by Moldovagaz to Gazprom in the period 1 January 2003 to 31 October 2021 have been applied to reducing the Debt;

4. There is no evidence of any payments made by Moldovagaz on behalf of Left Bank in the period 1 January 2003 to 31 October 2021⁴⁰;
5. None of Moldovagaz's operating costs have been funded by Left bank;
6. Other than the penalties and interest transferred to Faktoring-Finans in 2006 no penalties or interest are included in the Debt total of USD 756,584,129 recorded as at 31 October 2021;
7. Exchange rate depreciation is responsible for a significant part of the Debt increase when valued in local currency; and
8. Significant factors in the growth of the USD Debt value are the growth of customer debt, gas losses and investments and expenses incurred by Moldovagaz not recoverable in the customer tariff.

2.5 Legal Audit

2.5.1 *Irregularities and illegalities in connection with the establishment of Gazsnabtranzit and Moldovagaz*

- (63) The assets transferred by the Moldovan Government to Gazprom and further contributed by Gazprom to the authorised share capital of Gazsnabtranzit and Moldovagaz as payment for debts to Gazprom were not valued in accordance with the applicable legal framework. Notably, the assets should have been evaluated in accordance with "*world market prices*", but were instead most likely valued based on their book value. The Auditor's analysis of a revaluation made in 2008 indicates that the value of assets transferred to Gazsnabtranzit in 1996 increased by 1127% (in MDL terms) between 1996 and 2008. Thus, the possibility that the assets were undervalued in 1996 exists.
- (64) Several irregularities in connection with the establishment of Gazsnabtranzit were affirmed by the "*Audit Report on compliance of capital expenditures and investments in natural gas enterprises with public service obligations and related enterprises as defined in the Law No 108/2016 on natural gas, including those indirectly owned*" (the "**2022 Audit Report**"), which was adopted by the Court of Accounts of Moldova as Annex No. 1 to the Decision of the Court of Accounts No. 56 of 21 November 2022 ("**2022 Court of Accounts Decision**"). Notably, Section 4.1.1 of the 2022 Audit Report, ascertains that the quota share of the Moldovan Government might have been heavily undervalued, whereas the alleged debts of Moldova towards Gazprom were unjustifiably increased. This may have inflated the later debt of Moldovagaz. The 2022 Audit Report also uncovered a series of irregularities in connection with the establishment of Moldovagaz in 1999. In particular, Section 4.1 of the 2022 Audit Report ascertains that the appraisal of the property of the "*enterprises of the gas complex*", which operated on the left bank of Nistru river, had been systematically carried out with serious contraventions of the law at various levels. As a result, the value of the those enterprises was heavily underestimated for the purposes of the establishment of Moldovagaz.
- (65) Moldovan Counsel confirms irregularities and illegalities in connection with the establishment of Gazsnabtranzit. In particular, the assets allegedly transferred to Gazsnabtranzit were illegally valued individually at their book value, instead of as a going concern and at market prices. The assets were also illegally valued long before the incorporation of Gazsnabtranzit, at a time of significant inflation. Furthermore, assets located on the Right

⁴⁰ Except for 2007 payment arrangement, refer to paragraph Section 4.4.2.

bank were apparently transferred as payment for Left bank debts. Also, no evidence could be found of Gazprom's purported non-monetary contribution to Gazsnabtranzit's share capital.

- (66) Similarly, Moldovan Counsel confirms irregularities and illegalities in connection with the establishment of Moldovagaz. In particular, the assets allegedly transferred to Moldovagaz were illegally valued individually at their book value, instead of as a going concern and at market prices. The assets were also illegally valued almost two years before the incorporation of Moldovagaz. An alleged Debt of USD 47,300,000 was incorrectly not set off against Gazsnabtranzit's equity when Gazsnabtranzit was merged into Moldovagaz. Furthermore, assets located on the Right bank were apparently transferred as payment for Left bank debts.
- (67) There are several procedural and substantive deficiencies in the founding documents and incorporation of Gazsnabtranzit as well as Moldovagaz, which may render several of the founding documents invalid *ab initio*.

2.5.2 *The 2006 assignment of debts from Gazprom to Faktoring-Finans was most likely legal*

- (68) Gazprom assigned USD 275,914,205 of the Debt to Faktoring-Finans in December 2005.⁴¹ The assignment consisted of a part of the Debt accrued in the period 1996 to 2003 under contracts No. 1GM-97, No. 1GM-98, No. 1GM-99, No. 2GM-99, No. 1GM-2000, No. 1GM-2002, No. 1GM-03 and No. 1GM-04. We have reviewed the assignment provisions of contracts No. 1GM-99, No. 2GM-99, No. 1GM-2000, No. 1GM-2002, No. 1GM-03 and No. 1GM-04, all governed by Russian law.
- (69) The contracts reviewed on their face permit transfer of rights and obligations to third parties with written notice to the other party. Moldovagaz received written notice of the assignment. There are no indications that the assignment violated mandatory Russian law at the time.
- (70) Consequently, Gazprom's assignment was most likely legal. The only possible exemption pertains to the debts accrued under contracts No. 1GM-97 and No. 1GM-98, which we have not had access to and have not reviewed.

2.5.3 *Penalty interest rates and fines charged by Gazprom prior to 2006 may have been contrary to custom and practice and are susceptible to reduction as excessive pursuant to the applicable Russian law*

- (71) There are indications that penalty rates charged by Gazprom prior to 1999 may have been as high as 0.35% per day of delayed payments. Contracts for the period 1999 to 2006 (inclusive) have penalty rates of 0.01 to 0.03% per day of late payment, but also provided for fines of up to 200% of the unpaid sum after a certain period of time.
- (72) Daily interest rates of 0.35% deviate from international practice, appear to be excessively high compared to the creditor's loss, and are susceptible to reduction pursuant to legislation in force in the Russian Federation at the time. The 200% fines may conceivably be justified as compensation for fines which could be imposed under Russian foreign currency control legislation in force at the time. However, we have seen no evidence of Russian authorities imposing fines on Gazprom due to delayed payments from Moldovagaz, and fines imposed by Gazprom on Moldovagaz may consequently also be excessive.

⁴¹ See Cession Agreement No. 8FF-2005, dated 1 December 2005, Notification of Assignment of Claim, dated 2 December 2005 and Reconciliation Statement between Faktoring-Finans and Moldovagaz, dated 15 November 2006.

2.5.4 *Gazprom's distribution of transit fee payments between the operators of the Right and Left bank transmission systems is contrary to international practice, and may give rise to a counterclaim for Moldovagaz*

(73) We understand that Gazprom at least since 2007 has distributed transit fee payments between Moldovagaz, one of two licensed TSOs on the Right bank, and Tiraspoltransgaz-Pridnestrovie, the unlicensed, de-facto TSO on the Left bank as equal shares (50%) for the whole transit distance through Moldova on the Grebeniky – Orlovka direction. The equal distribution of the transit fee corresponds to a provision in the Transit Contract No. 2GM-11 (the "**Transit Contract**") for the division of transit fees between Moldovagaz and Tiraspoltransgaz.

(74) Gazprom's payment distribution violates the payment terms of the Transit Contract. The equal division of fees is also contrary to international practice. In light of the factual circumstances, Gazprom's practice may give rise to a counterclaim for Moldovagaz amounting at least to 22% of the transit fees paid by Gazprom since 2007.

2.5.5 *Moldovagaz has not accepted interest or penalties since 1 April 2004 and the bulk of such interest and penalties is now time-barred*

(75) The Auditors have verified that no penalties for late payment or otherwise have been accepted since 1 April 2004. Moldovagaz has informed that all the previously accrued penalties were included in the debt assigned to Faktoring-Finans in 2005 (which included a significant share of penalties). Moldovagaz has refused to sign Reconciliation Statements recording penalties since 1 April 2004, and we have not seen any other communications between Gazprom and Moldovagaz acknowledging any penalties.

(76) Any claims for penalties accrued prior to 2020 are now most likely time-barred under the applicable Russian statute of limitations. This significantly reduces the risk of Gazprom threatening to increase the Debt by claiming penalties for past periods in the upcoming debt settlement agreement negotiations.

2.5.6 *Arbitral Awards for debts obtained by Gazprom prior to 2020 are no longer enforceable in Moldova and Gazprom cannot obtain new Awards pursuant to the applicable Russian law*

(77) Between 2008 and 2022, Gazprom obtained 18 Arbitral Awards for debts to Gazprom and/or Faktoring-Finans. 16 of the Awards were rendered before 2020.⁴²

(78) Under Moldovan law, Arbitral Awards have to be enforced not later than three years after they became binding under the laws at the seat of arbitration. Enforcement may only be allowed after the expiry of this time limit in exceptional circumstances. The seat of the arbitrations at hand was Moscow, Russian Federation, and the Awards became binding under Russian law when they were issued. The Awards rendered before 2020 are consequently most likely no longer enforceable in Moldova.

(79) Russian procedural law recognises the principle of *res judicata*, and Gazprom is unlikely to be able to obtain new Awards for the debts confirmed in the previous Awards if Moldovagaz raises the *res judicata* defence. Moreover, Moldovan courts may refuse the enforcement of any relitigated awards, as such enforcement would violate the principle of *res judicata*, which is considered public policy in Moldova.

(80) The outstanding debt to be paid by Moldovagaz pursuant to the Arbitral Awards amounts to approximately USD 6,5 billion, which comprises debts for deliveries in the period 2005 to

⁴² Two Awards have been rendered after 2020: On 29 September 2021 and 20 December 2022, respectively.

2019 to both the Right and the Left bank. The Auditors have compared the stated debts pursuant to the Arbitral Awards with the corresponding Acts of Acceptance signed by Moldovagaz and Gazprom. Based on this comparison exercise, approximately USD 400 million of the USD 6,5 billion which is due pursuant to the Arbitral Awards pertains to deliveries to the Right bank only. The outstanding debt pursuant to Arbitral Awards from 2021 and 2022 relates to Left bank deliveries only. Thus, a very significant share of the Debt that Moldovagaz allegedly owes Gazprom may most likely not be enforced under Moldovan law.

2.6 Potential counterclaims

2.6.1 *Based on the results of the independent audit, Moldovagaz may require parts of the Debt to be written off by Faktoring Finans and Gazprom*

(81) By agreeing to carry out an independent audit of Moldovagaz's debts to Gazprom and Faktoring-Finans *prior* to the conclusion of a debt settlement agreement, Gazprom has implicitly agreed to take the findings of this audit into account when concluding the debt settlement agreement with Moldovagaz. The audit has revealed significant uncertainty concerning the scope of the Debt, that a significant share of the Debt has become unenforceable, and that Moldovagaz has significant counterclaims. Moldovagaz may therefore require significant write-offs by Gazprom and Faktoring-Finans.

2.6.2 *The alleged USD 278 million debt accrued prior to 1 January 2003 may not be independently verified, is most likely excessive, and Moldovagaz may require it to be written off*

(82) Moldovagaz may argue that the part of the Debt allegedly incurred prior to 1 January 2003, cf. 2.1.1 above, should be written off, as these parts of the Debt cannot be independently verified due to the lack of underlying documentation. This includes the USD 275,914,205 assigned to Faktoring-Finans. As will be further explained in Section 3 below, the Auditors have not been provided with documentation from Moldovagaz, Gazprom or the governmental archives of Moldova necessary to verify the existence, scope and cause of the Debt incurred prior to 1 January 2003. This potential argument applies to USD 165,757,466 of alleged penalties and USD 112,406,594 of alleged debts for gas deliveries. As will be indicated below, there are also further, independent legal grounds for challenging the scope of the alleged debts and penalties accrued prior to 2003.

2.6.3 *Approximately USD 400 million of the Debt accrued from 2005 will most likely not be enforceable in the courts of Moldova and Moldovagaz may require it to be written off*

(83) As noted in Section 2.2.7, the Statute of Limitations for the Arbitral Awards issued in the period 2008 to 2020 have expired and these Arbitral Awards may no longer be *enforced* in Moldova. This issue is separate from the issue of whether the relevant parts of the Debt as such have expired (i.e. the obligation to pay the relevant parts of the Debt underlying the Arbitral Awards, not the obligation to comply with the Arbitral Awards). As Moldovagaz and Gazprom have signed Mutual Reconciliation Statements on a yearly basis, the relevant parts of the Debt as such have been confirmed by both parties and the underlying obligations have therefore not lapsed. However, Gazprom may not use the Moldovan courts to *enforce* most of that Debt, as the Arbitral Awards have expired (or – put differently – the obligation to comply with the Arbitral Awards has expired). Most likely, the Arbitral Awards cannot be relitigated in Russia, and enforcement of such relitigated awards would in any event most likely be rejected by Moldovan courts. Against this background, Moldovagaz may require Gazprom to write off the part of the Debt that is encompassed by the now expired and unenforceable Arbitral Awards, i.e. approximately USD 400 million, as Gazprom knowingly has foregone its opportunity to enforce the relevant parts of the Debt.

2.6.4 *Potential counterclaim for lost transit revenues*

- (84) Moldovagaz may have a counterclaim for approximately USD 160 million of lost transit revenues, paid by Gazprom to Tiraspoltransgaz in breach of custom and practice.

2.6.5 *Moldovagaz may have counterclaims for non-approved investments and expenses*

- (85) In the period 1 January 2011 to 31 December 2020, Moldovagaz made investments and incurred expenses amounting to USD 143 million which were not approved by the Moldovan regulator, ANRE, for inclusion in the customer tariff. Had any of this expenditure been avoided, more funds may have been available for Moldovagaz to pay down the Debt. To the extent Gazprom as the de facto controlling shareholder of Moldovagaz approved these expenditures, Moldovagaz may require a corresponding part of the Debt to be written off.

2.6.6 *The assets transferred as debt payments when Gazsnabtranzit and Moldovagaz were founded were most likely significantly undervalued, and the Debt allegedly incurred prior to 2003 is consequently overvalued*

- (86) The assets transferred as payment for debts in the context of the debt for assets swaps leading to the creation of Gazsnabtranzit and Moldovagaz were illegally valued as individual assets at book value rather than as going concerns at market prices. They were also valued long before the incorporation of the companies at a time of significant inflation. If the assets had been correctly valued, more Debt would have been paid down at the time. Consequently, the Debt allegedly incurred before 2003 is excessive and Moldovagaz has a further argument for this part of the Debt to be written down.

2.6.7 *In any event, penalties accrued due to non-payment of gas deliveries in the period from 1993 to 1 July 1999 were excessive and Moldovagaz may require parts of the penalties to be written off*

- (87) Moldovagaz may challenge a significant part of the penalties that accrued due to non-payment of gas deliveries in the period from 1993 to 1 July 1999. A Mutual Reconciliation Statement of 31 December 2021, signed by Moldovagaz and Faktoring-Finans,⁴³ shows that approximately USD 133 million accrued in penalties only from 1994 to 1 July 1999, which suggests that an excessive penalty interest rate of 0.35% or similar was used. This rate is arguably excessive under Russian law, and was reportedly also higher than the penalty rates Gazprom charged to other CIS importers. Applying a more reasonable and customary interest rate of 0.03% per day, the above penalties would be reduced to approximately USD 11,4 million⁴⁴, suggesting that Gazprom charged excessive penalties amounting to more than USD 120 million. This provides a further reason for Moldovagaz to require the part of the Debt incurred before 1 January 2003 to be written off.

2.6.8 *Counterclaims due to reduced deliveries from October 2022*

- (88) We understand that from October 2022, Gazprom has been in breach of its delivery obligations under its current gas sales agreement with Moldovagaz. The gas sales agreement provides for penalties for under-deliveries. Moldovagaz may require parts of the Debt to be settled by set-off against such penalties. Gazprom's breaches of contract fall outside of the temporal scope of the audit, and the Auditors have not quantified the accrued penalties.

⁴³ Mutual Reconciliation Act between Moldovagaz and Faktoring-Finans, dated 31 December 2021.

⁴⁴ $0.03/0.35 \times 133,000,000$.

3 REQUESTS FOR INFORMATION

- (89) Requests for Information The Auditors requested certain information, including financial data and supporting documents, from Moldovagaz.
- (90) On 15 August 2022, the Auditors and the PPA met with Moldovagaz's CEO, Mr. Vadim Ceban, to set the parameters for the audit process. In the meeting, it was agreed that the Auditors would provide Moldovagaz with a Request for Documents, whereupon Moldovagaz would give the Auditors access to all documents necessary for the audit. It was also agreed that PPA, FRA, WR and Moldovagaz would sign a Non-Disclosure Agreement (the "NDA"), which was a precondition for Moldovagaz to give the Auditors and PPA access to the data.
- (91) On 17 August 2022, the Auditors provided Moldovagaz with a Request for Documents (the "First Request"), in which a comprehensive list of the data required for the Auditors to undertake the audit was set out. Around the same time, from 15 August 2022, PPA, FRA, WR and Moldovagaz began negotiating the NDA, which was agreed to and signed by Moldovagaz on 25 August 2022.
- (92) On 2 September 2022, two weeks after the First Request had been submitted to Moldovagaz, the PPA received a first batch of files from Moldovagaz, which were then made available to the Auditors. This batch of files comprised mostly legal documents, and, therefore, was not sufficient to commence the financial audit.
- (93) Another batch of files was provided via the PA to the Auditors on 7 and 9 September 2022. This response was also insufficient to commence the financial audit, especially since no 'structured' data, i.e., data in an electronic form suitable for further processing and calculation, was provided.
- (94) Consequently, on 15 September 2022, the Auditors submitted a Second Request for Documents (the "Second Request") by email to Moldovagaz. On 28 September 2022, the Auditors received a new batch of files via the PPA, including parts of the requested structured data. Mr. Ceban informed the Auditors that Moldovagaz would continue to present pending data to the PPA as a shareholder in Moldovagaz.
- (95) On 6 October 2022, the Auditors submitted a Third Request for Documents (the "Third Request") to Moldovagaz, setting out an updated overview of the requests, as well as including some additional requests based on the review of information received to date. On the same day, Moldovagaz responded that they would present all the requested information that had been compiled in August and September to the PPA.
- (96) On 13 October 2022, the then Director General of the PPA, Mr. Eugeniu Cozonac, sent a letter to Gazprom's CEO, Mr. Alexey Miller, requesting Gazprom to assist Moldovagaz in producing the requested documents to the Auditors. Mr. Cozonac and the PPA did not receive any response to this letter from Gazprom.
- (97) On 18, 19 and 20 October 2022, the Auditors met with Moldovagaz's management in Chisinau (the "Chisinau Meetings"). In the Chisinau Meetings, following clarification of certain information requested by the Auditors, Moldovagaz agreed to provide all outstanding files to the extent these were available to Moldovagaz. In the event that the files requested were not available to Moldovagaz, a written explanation would be provided.
- (98) On 7 November 2022, the Auditors submitted a Fourth Request for Documents (the "Fourth Request") to Moldovagaz, setting out an overview of the information received to date and the outstanding data. The Fourth Request also included several additional requests that had not been included in the prior requests due to new information and clarifications received during the Chisinau Meetings.

- (99) Moldovagaz provided some of the outstanding files, as well as written explanations concerning information / data that was not available, to the PPA on 9 December 2022. A further batch of files was provided on 30 December 2022.
- (100) After having reviewed the new batches, the Auditors submitted a Fifth Request for Documents (the "Fifth Request") to Moldovagaz on 6 January 2023, setting out an overview of the received and outstanding information, also including some additional requests for clarification. Moldovagaz provided some of the documents requested on 11, 13 and 23 January 2023, as well as written explanations for the files that were unavailable.
- (101) The Auditors also, through the PPA, requested information from the National Archives of the Republic of Moldova, from the Moldovan Fiscal Service, the Customs Service and from the national Bureau of Statistics concerning the period 1991 to 1999, as Moldovagaz informed the Auditors that it did not possess any information which predated its establishment in 1999. Information from the archives was provided via the PPA on 10 and 17 November 2022. Further information from the archives was subsequently provided on 10 January and 16 February 2023. The majority of the information found was at a summary level rather than the required detailed level. The National Archives of the Republic of Moldova provided the Auditors with a list of documents from 1991 to 1996 which according to the National Archives had been left with Moldovagaz for temporary storage.
- (102) The Parliament of Moldova has also, on behalf of the Auditors, made investigations into the archives of the Court of Accounts for the requested documentation. These inquiries have been unsuccessful.
- (103) On 13 January 2023, the Auditors met with ANRE to establish contacts and request information concerning, inter alia, the relationship between ANRE and Moldovagaz and tariffs. The Auditors also discussed with ANRE the tariff setting process and potential impact on the Debt.
- (104) On 30 January 2023, Deputy Prime Minister and Minister of Infrastructure and Regional Development of Moldova, Mr. Andrei Spinu, sent a letter to Gazprom's CEO, Mr. Alexey Miller, requesting Gazprom to provide the outstanding documentation from the 1991 to 1999 period, noting, inter alia, that the unavailability of documentation from this period may result in the Auditors not being able to verify the existence, scope or cause of the parts of the Debt which stems from this period. As of the date of this Report, no answer has been received from Gazprom.
- (105) The Auditors also understand that Moldova's representatives on Moldovagaz's Supervisory Board have made efforts to facilitate Moldovagaz's provision of documents and information for the purpose of the Audit.
- (106) On 9 February 2023, the Auditors sent a list of outstanding information requests to Moldovagaz. On 17 February 2023, Moldovagaz provided the Auditors (via the PPA) with further written explanations and documents. Upon review of this set of documents a follow up call between the Auditors and Moldovagaz took place on 23 February 2023, followed by questions which were sent to Moldovagaz on 27 February 2023. On 7 March 2023 Moldovagaz responded with additional documents and clarifications.
- (107) On 14 February 2023, the Auditors sent a further request for information to ANRE concerning, inter alia, tariff setting methodologies, historical gas tariffs, tariff deviations and communications between Moldovagaz and ANRE. The Auditors received the requested information from ANRE on 20 February 2023.
- (108) On 27 March 2023, the Auditors had a call with Moldovagaz to discuss the tariff setting methodology and key factors explaining the Debt growth. Following this call Moldovagaz

provided certain further information on 29 March 2023.

- (109) On 14 April 2023 a follow up call was held between the Auditors and Moldovagaz to further clarify aspects of Moldovagaz's analysis of the key factors resulting in the Debt growth. Moldovagaz responded with additional documents on 19 April 2023.
- (110) On 21 April 2023, the Auditors forwarded a document to Moldovagaz containing its draft findings from the financial audit for comment and a factual accuracy check. A few outstanding requests were included by the Auditors in this document. On Tuesday 25 April, Moldovagaz provided some high level comments in a call and followed up with detailed comments in writing on 2 May 2023.

4 FINANCIAL AUDIT

4.1 Scope of work

- (111) The original scope of the financial audit was defined by the following objectives:⁴⁵
1. verify Moldovagaz's (and its predecessors') allocation of payments for gas consumption among consumers on the Right and Left banks;
 2. verify the valuation of assets previously transferred to Gazprom as (partial) settlement of debt for gas delivered to consumers on the Right bank, and, if necessary, revaluation of such assets;
 3. verify if previous payments have been correctly allocated to settle debts accrued for gas deliveries to consumers on the Right bank; and
 4. identify the reasons for the accrual of the Debt
- (112) As a result of the actual execution of the audit, based on the available information, this report covers predominantly scope items 1, 3 and 4 above. The Auditors have not been able to undertake any verification in relation to scope item 2 due to the lack of relevant information and records.

4.2 Response to Auditor's information requests

- (113) As set out in Section 3 above, Moldovagaz has not provided the Auditors with all the information /data they requested, in some cases because Moldovagaz stated that it did not possess or had not retained the required information. Moldovagaz advised that it does not possess information related to its predecessor companies, as these were separate legal entities. Moldovagaz also advised that some documentation was destroyed in accordance with document retention policies. This particularly applies to the period prior to January 2003.
- (114) The Auditors also note that much of the information provided was in a format which required manual data extraction for the purposes of further analysis. This created additional delay as the Auditors had to collate the data provided into a useable structured format. The Auditors note that the management of Moldovagaz actively engaged with the Auditors and prepared a number of analytical calculations and reports to facilitate the Audit process.
- (115) The government archives and the energy regulator ANRE were also approached to provide any information they might hold that would be relevant to the audit. ANRE provided some

⁴⁵ **Appendix No. 1:** Tender Book, Section 1.2.

relevant information, but the archives were only able to provide summary documents.

- (116) In addition, the Auditors, via the Moldovan Government, requested from Gazprom the underlying supporting data for the Debt accrued prior to 1 July 1999, as Gazprom should retain sufficient information and data to support the gas debt owed. This request was sent in January 2023 following confirmation from Moldovagaz that it did not have the underlying supporting data from this period. As of the date of this Final Audit Report, the Moldovan Government has not received a response from Gazprom.
- (117) The findings set out in this Final Audit Report are based on the review of the documents and data received, as set out in Appendix No. 2. In addition, this report has included, where relevant, reference to explanations provided by Moldovagaz's management in meetings in Chisinau from 18 to 20 October 2022, and on information provided by Moldovagaz's management in a series of calls conducted between February and April 2023.

4.3 Chronology of the Debt growth

- (118) Based on the documentation and information received to date, the Auditors have identified three key time periods in the relationship between Moldovagaz, its predecessor companies, and Gazprom. These time periods are primarily based on the availability of the information and underlying supporting data required to undertake and complete the audit of the Debt. These time periods are:

4.3.1 *Period: 27 August 1991 to 1 July 1999*⁴⁶

- (119) During this period, the debt stated as owed to Gazprom in relation to natural gas supplied to the customers on the Right bank increased to USD 172,242,518⁴⁷ (MDL 1,954 million⁴⁸).
- (120) Due to the lack of underlying records it is not known if any element of this balance relates to accrued interest and penalties.
- (121) Moldovagaz was incorporated on 25 May 1999⁴⁹ and became operational on 1 July 1999, and therefore the debt of USD 172,242,518 accrued in this period was accumulated by Moldovagaz's predecessors. Moldovagaz informed the Auditors that it has no access to documentation or accounting records related to this period, except for a few legal documents.
- (122) Given the size of the opening gas debt to Gazprom that Moldovagaz recorded in its books of account on the date of its incorporation, it is expected that Moldovagaz would have obtained and retained appropriate accounting records to support the validity of the opening gas debt. Moldovagaz stated that it did not possess such records. The Auditors note that, in their experience, it is unusual to recognise a significant obligation without obtaining appropriate supporting documentation. Moldovagaz advised that the opening balance of the Debt was recognised based on the entity's incorporation documents, and that the primary documentation belonged to other legal entities, hence, was not available to Moldovagaz.
- (123) No significant alternative records related to this period have yet been provided by other

⁴⁶ Opening date as per Moldovagaz annual balance sheet for the year ended 31 December 1999 (**Appendix No. 3: Request No. 23**).

⁴⁷ Spreadsheet comprising annual debt balance and payments for the period 1999 to 2021 prepared by Moldovagaz.

⁴⁸ Exchange rate at 1 July 1999: 1 USD = 11.3444 MDL.

⁴⁹ Licence from National Energy Regulatory Agency, dated 25 May 1999 (https://www.moldovagaz.md/pic/uploaded/docs/Licenta_SA_Moldovagaz_RO.pdf).

Moldovan sources, except for some limited records provided by Moldovan archives.

(124) As the supplier of the gas during this period it is also expected that Gazprom should retain appropriate accounting records to support the validity of the Debt accrued and unpaid during this period. By letter dated 30 January 2023 addressed to Mr. Alexey Miller, the CEO of Gazprom, the Moldovan government⁵⁰ requested Gazprom to provide the documents and underlying data for the period 1991 to 1999. As at the date of this report, this request remains unanswered.

(125) In conclusion, at the date of this report the Auditors are unable to undertake any audit activities on the USD 172,242,518 debt balance, stated to be owed to Gazprom at the end of this time period, due to the absence of underlying records.

4.3.2 *Period: 1 July 1999 to 31 December 2002*

(126) During this period, the debt stated as owed to Gazprom in relation to natural gas supplied to the Right bank increased from USD 172,242,518 to USD 278,164,061 (MDL 3,845 million⁵¹), a total increase of USD 105,921,543 over the period. This Debt total includes:

1. USD 112,406,595 for the main body of the Debt; and
2. USD 165,757,466 of accrued interest and penalties

(127) In addition to the use of customer receipts to reduce the debt two other transactions took place in this period that reduced the Debt total:

1. USD 90,000,000 partial debt settlement between Moldovagaz and Gazprom with the involvement of the Moldovan Government in 1999⁵². Moldovagaz has partially reimbursed the government approximately USD 36,000,000 through so called "USD 4 payments" from 2003 to 2013⁵³. Payments will also have been made prior to 2003 but the Auditors do not have the accounting records to verify; and
2. USD 47,299,796 partial debt settlement recognised in the year 2001 but related to prior period. Records maintained by Moldovagaz describes the USD 47,299,796 reduction in the debt balance as "*the amount of contribution to the Moldovagaz capital*".⁵⁴

⁵⁰ Represented by Andrei Spinu, Deputy Prime Minister and Minister of Infrastructure and Regional Development of Moldova.

⁵¹ Exchange rate at 31 December 2002: 1 USD = 13.8220 MDL.

⁵² Agreement for USD 63 million between Moldova and Gazprom "On the settlement of the debts of the Republic of Moldova for deliveries of Russian natural gas in 1996", dated 9 February 2000, Agreement for USD 27 million between Moldova and Gazprom "On the settlement of the debts of the Republic of Moldova for the deliveries of Russian natural gas in 1997", dated 9 February 2000.

⁵³ These payments were initiated by the Article 50 of the Law "On the budget for 2001" No. 1392 dated 30 November 2000 requiring Moldovagaz to add to the tariff USD 4 for each 1000 cubic metre of gas sold and to pay the collected income monthly to the state budget to service the external public debt, formed as a result of the transfer of promissory notes by the Government to Gazprom carried out in accordance with the agreements ratified by the Law No. 892-XIV of March 23, 2000.

⁵⁴ «Стоимость взноса в уставный капитал АО "Молдовагаз"» ("*The value of contribution to the authorized capital of JSC "Moldovagaz"*").

Moldovagaz has confirmed that the reduction in the debt balance recorded in 2001 is related to Gazprom's contribution to Moldovagaz share capital in 1999⁵⁵.

- (128) Moldovagaz stated that it has not retained the underlying accounting records supporting the development of the Debt owed in this period despite being responsible for maintaining the accounting records in this period.
- (129) In conclusion, at the date of this report the Auditors are unable to undertake any verification of the USD 105,921,543 increase in the Debt related to this period due to the absence of underlying records.
- 4.3.3 Period: 1 January 2003 to 31 October 2021*
- (130) During this period, the debt stated as owed in relation to natural gas supplied to the customers on the Right bank increased from USD 278,164,061 to USD 756,584,129 (MDL 13,253 million⁵⁶), a total increase of USD 478,420,068 over the period.
- (131) During this period part of the Debt, USD 120,117,167, was transferred in 2006 to Faktoring-Finans, Gazprom's wholly owned subsidiary, together with an amount of USD 155,797,038 in relation to accrued penalties and interest, resulting in a total debt owed to Faktoring-Finans by the Right bank of USD 275,914,205. This amount has remained unchanged in subsequent Mutual Reconciliation Acts⁵⁷ signed between Moldovagaz and Faktoring-Finans for all years up to 2021, the last act reviewed. Moldovagaz has provided no information as to how the amount of interest and penalties was calculated.
- (132) A further amount of USD 20,923,541⁵⁸ accrued interest and penalties remained owed to Gazprom until it was written back by Moldovagaz in 2009. Moldovagaz informed the Auditors that Gazprom continued to accrue interest and penalties on the unpaid Debt, and the relevant amounts were communicated to Moldovagaz via separate annual Mutual Reconciliation Acts. However, Moldovagaz has not recognised these amounts as a liability in its books of account and has not signed the relevant Mutual Reconciliation Acts. Moldovagaz stated that Gazprom has also not recognised these interest and penalties in its books of account - the Auditors were not able to confirm this information.
- (133) Moldovagaz provided the Auditors with various contemporaneous accounting records for this period, which has allowed the Auditors to verify the Debt accrued in relation to gas purchased in this period. However, as at the date of this report the Auditors have not been provided with any information to allow the calculation of the penalties and interest transferred to Faktoring-Finans to be verified.
- 4.3.4 Detailed chronology of the Debt growth*
- (134) The chronology of accumulation of Moldovagaz's debt to Gazprom and Faktoring-Finans from 2001 to 31 October 2021 is set out in Figure 3 below.
- (135) The chart shows that the amount of the Debt remained relatively constant during the period 2001 to 2005, followed by a significant increase in the period 2006 to 2015, and then another

⁵⁵ As per the paragraph 5 of "The program of settlements of penalties for the late payments for gas in 1994-1999 by consumers of Republic of Moldova", dated 09 February 2000.

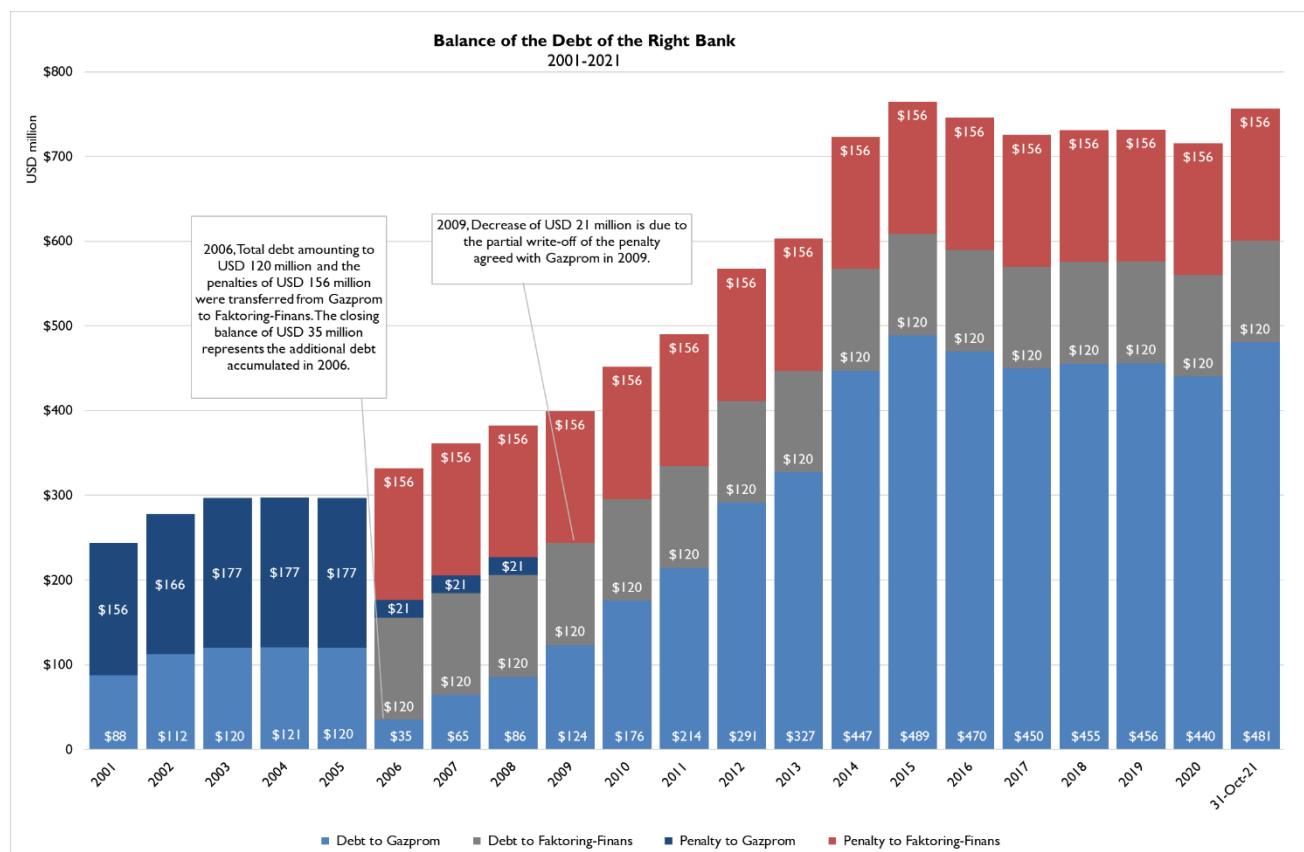
⁵⁶ Exchange rate at 31 October 2021: 1 USD = 17.5164 MDL.

⁵⁷ Mutual Reconciliation Acts were the documents reconciling the opening balance of the debt plus accruals less payments for a year to the closing balance between the accounting records of Gazprom or Faktoring-Finans and Moldovagaz.

⁵⁸ Except for accrual of USD 15,241 of penalties on 31 December 2006, which were reversed on 29 December 2007.

period of relative stability from 2016 onwards. In Section 4.7 below, the Auditors have reviewed Moldovagaz's analysis as to the causes of the Debt growth in the period 2011 to 2020.

Figure 3



4.4 Verification of gas prices and volumes supplied to the Right bank

4.4.1 Review of Moldovagaz accounting records

(136) For the period 1 January 2003 to 31 October 2021 the Auditors have undertaken the following tests of contemporaneous accounting information provided by Moldovagaz to confirm the volumes of gas Gazprom provided to the Right bank, as well as the cost of that gas.

1. Compared the cost of gas supplied to the Right bank recorded in the Annual Mutual Reconciliation Acts to the cost of gas supplied recorded in the monthly Acts of Acceptance;
2. Compared the gas prices agreed in the gas supply contracts with the contract prices as per the Acts of Acceptance. The Auditors were not provided with sufficient information

required to test the actual prices charged, as these are calculated based on the contract price using the calorific value of the gas supplied⁵⁹;

3. Compared the total debt owed as recorded in the Annual Mutual Reconciliation Acts to the debt owed recorded in Moldovagaz's annual audited Financial Statements from 2015 to 2021;⁶⁰ and
 4. Compared the debt owed as stated by Moldovagaz to the Arbitral Awards⁶¹ for the years 2005 to 2019 to confirm debt amounts were the same.⁶²
- (137) The results of the tests corroborated both the volume of gas and the related cost recorded by Moldovagaz as being supplied by Gazprom to the Right bank in the period 1 January 2003 to 31 October 2021.

4.4.2 Gas purchases on behalf of Left bank

- (138) As part of the review of the accounting records and payment registers⁶³, the Auditors identified three invoices dated in 2007⁶⁴ related to gas supplied by Gazprom to Tiraspoltransgaz (the Left bank) that were paid by Moldovagaz. The management of Moldovagaz explained that these invoices related to the following arrangement between Tiraspoltransgaz, Moldovagaz, and Gazprom:
1. Tiraspoltransgaz provided gas transit services to Gazprom. Gazprom paid for these services by providing gas to Tiraspoltransgaz via Moldovagaz. Moldovagaz did not record these non-cash transactions in its financial records, i.e., these were recorded off-balance sheet.
 2. In 2007, the arrangement was amended to include a cash element. Instead of providing natural gas as remuneration for the gas transit services, Gazprom paid cash to Moldovagaz which used it to buy natural gas on behalf of Tiraspoltransgaz. The three invoices identified by the Auditors were issued as part of this amended arrangement. After 2007, the parties reverted to the previous arrangement.
 3. The Auditors reviewed related documentation provided by Moldovagaz (i.e. payment orders and accounting records) and confirmed that the amounts paid by Moldovagaz to Gazprom were equal to the amounts previously transferred by Gazprom to Moldovagaz,

⁵⁹ The actual gas price is calculated as contract price with a coefficient applied based on the calorific value of the gas supplied in each period. This coefficient though only has a minor effect on the price paid.

⁶⁰ The Auditors obtained the complete set of the annual financial statements with the notes only for the period from 2015 to 2021.

⁶¹ The Arbitral Awards were the awards of the International Commercial Arbitration Court at the Chamber of Commerce and Industry of the Russian Federation issued from 2008 to 2022 in respect of the Debt as well as alleged debts for alleged gas supplies to the Left bank.

⁶² The Arbitral Awards do not distinguish between the debt attributed to the Right and Left banks. The Auditors, therefore, matched the total gas supplied to both Right and Left banks stated in the Acts of Acceptance signed with Gazprom to the debt value recorded in the Arbitral Awards.

⁶³ Verification test of monthly summary records of gas volumes and gas cost delivered to Right bank to underlying contemporaneous accounting records.

⁶⁴ Invoice C 18/714 for USD 7,829,256.55 dated 31 May 2007, invoice АСПГ00018 for USD 13,172,226.16 dated 31 October 2007 and invoice АСПГ00021 for USD 7,293,359.92 dated 31 December 2007.

i.e., Moldovagaz did not use their own funds to pay for the gas bought on behalf of Tiraspoltransgaz and these transactions did not impact the value of the Right bank Debt.

4.4.3 *Review of gas metering records*

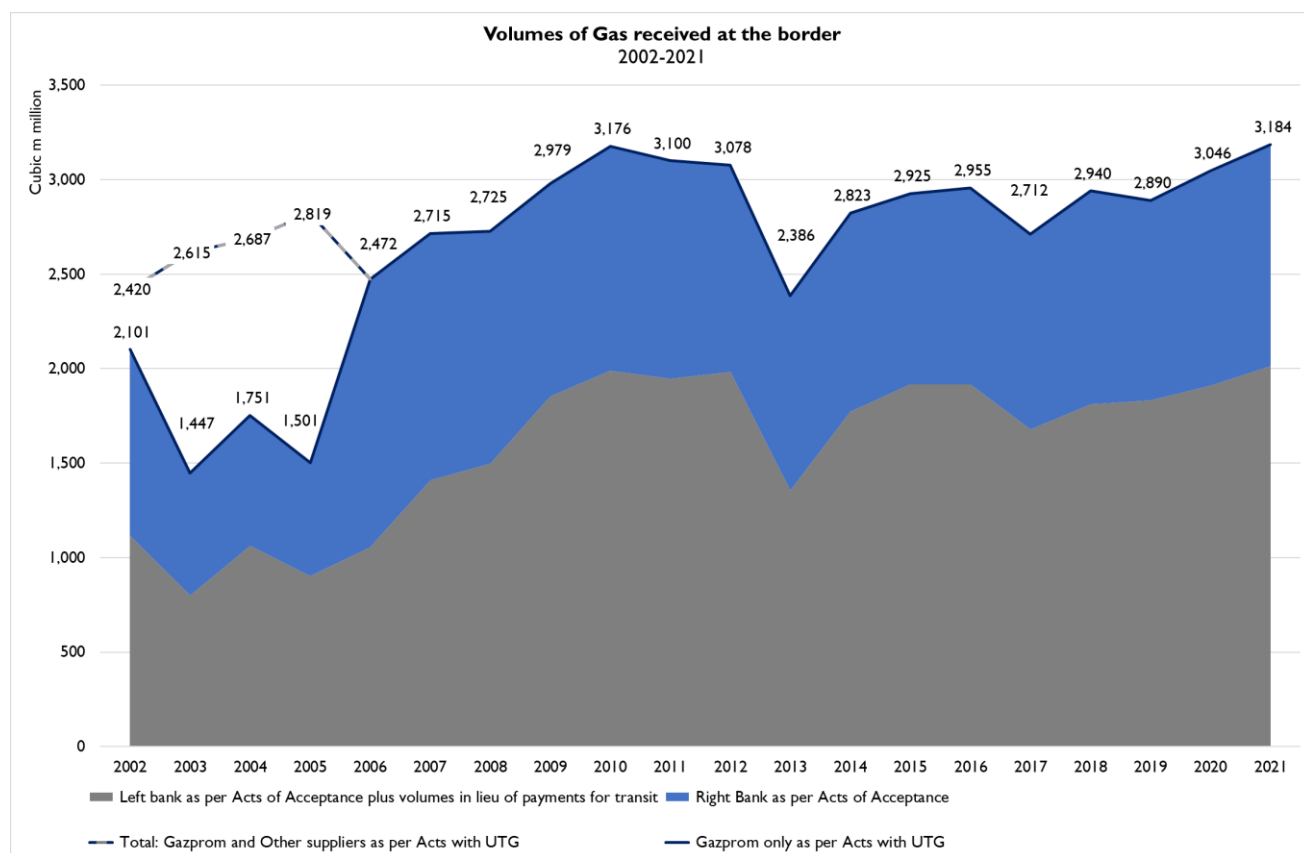
- (139) The Auditors reviewed Acts of Acceptance with Ukrtransgaz - summary documents signed by representatives of Moldovagaz and Ukrtransgaz monthly, showing total (i.e., the total volume for both Right and Left banks) volumes of the gas in m³ received and transited at the Moldovan border and through the territory of Moldova at various gas metering stations.⁶⁵ These documents were provided for the period 2002 to 2021⁶⁶. In the period 2002 to 2005 the Acts of Acceptance with Ukrtransgaz show additional suppliers such as Gazexport, ITERA and Naftogaz Ukraine, for which all gas debt has been paid. Beyond Gazprom, there were no other suppliers of gas to Moldova during the period 2006 to 2021 as per accounting records of Moldovagaz.
- (140) The Acts of Acceptance agreed between Moldovagaz and Ukrtransgaz in the period 2002 to 2021 confirmed that the volumes of gas registered as passing through the Moldovan and Ukrainian border were consistent with the volumes of gas supplied as shown in the Acts of Acceptance with Gazprom⁶⁷ and recorded in Moldovagaz's accounting records. A summary of the volumes of gas received by Moldova is set out in the chart below:

⁶⁵ Grebenyky, Ananiev, Alekseevka, Brichen and Kaushany.

⁶⁶ For 2020 and 2021 the Auditors relied on the monthly acts of distribution of operational balancing account signed by Moldovagaz, Moldovatransgaz and Tiraspoltransgaz, the document confirming the monthly volumes of gas received by Moldova and transferred between the Right and Left bank.

⁶⁷ A typical Act of Acceptance with Gazprom shows the total volume of gas delivered to Moldova and a split between the Right and the Left bank.

Figure 4.



- (141) For the period 2002 to 2005 Moldovagaz received natural gas from other suppliers in addition to Gazprom.
- (142) Within the period under review, the variances between the volume of gas supplied as per Acceptance Acts with Ukrtransgaz were explained by Moldovagaz as the volumes of gas supplied to Tiraspoltransgaz in lieu of payments for transit services⁶⁸.
- (143) In conclusion, Gazprom has not charged Moldova for volumes of gas that exceed the volumes recorded by Ukrtransgaz as having been delivered to Moldova for the Right bank.
- (144) The Auditors also reviewed the Right bank gas consumption patterns to identify any irregularities. Analysis of the monthly volumes of gas supplied to the Right bank by Ukrtransgaz followed the same pattern throughout the period under review, with expected seasonal variations.

4.5 Payments to Gazprom to reduce the Debt

- (145) The total of all payments made by Moldovagaz to Gazprom in a year is recorded in the annual Mutual Reconciliation Acts (MRAs)⁶⁹. The Auditors selected four years 2007, 2012, 2020 and 2021 and recalculated the total cash paid to Gazprom using Moldovagaz's contemporaneous accounting records, including cash books and payment orders. In all four

⁶⁸ Under the contracts Nos. 6 GM-06, 2GM-09, 2GM-10 and 2GM-11.

⁶⁹ MRAs where the Right bank payments are shown separately are available for the years 2014 to 2021 only.

years the total calculated payments matched the total payments made to reduce Right bank Debt recorded in the MRAs.⁷⁰ As no exceptions were found no further years were tested.

- (146) The Auditors further confirmed that Moldovagaz's bank account records agreed to the contemporaneous payment order registers for the period 2003 to 2021 without any significant discrepancies.
- (147) In summary, the Auditors found no evidence that payments to Gazprom were used for any purpose other than to pay down the Right bank debt except for the 2007 arrangement described in Section 4.4.2.

4.6 Use of funds received from customers

- (148) Moldovagaz provided the Auditors with its annual consolidated cashflow statements⁷¹ for the period 2006 to 2021. Its two major categories of cash inflows are:

1. Cash from sales of gas to customers of the Right bank; and
2. Payments from Gazprom for transit of gas.

Its largest categories of cash outflows are:

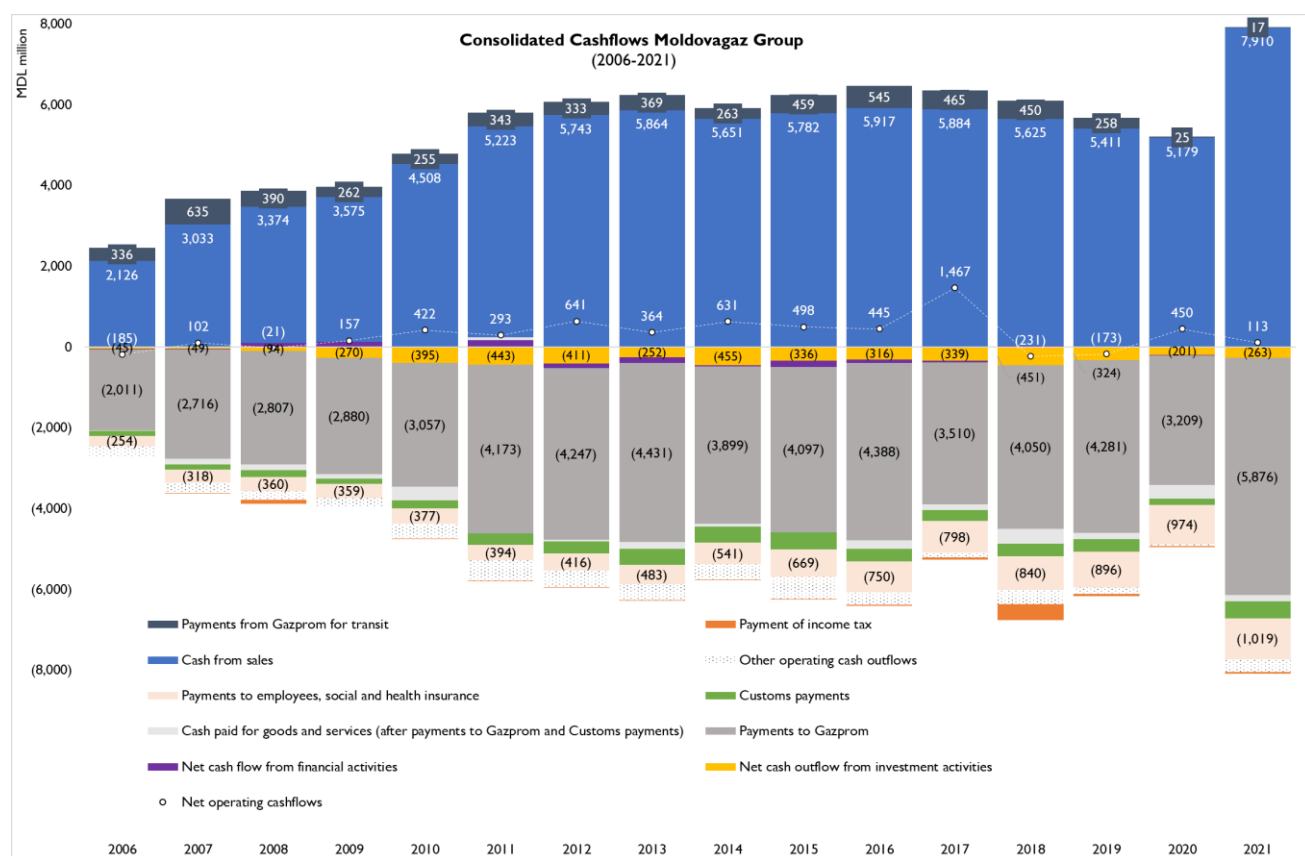
1. Payments to Gazprom for the supplies of gas and related customs payments
2. Payments to employees, social and health insurance; and
3. Other operating cash outflows.

- (149) A summary of Moldovagaz's consolidated cash inflows and outflows is presented in the chart below.

Figure 5.

⁷⁰ Although 2007 and 2012 MRAs did not split the Debt between the Right and Left banks, as the Left bank did not make any payments in those years, all amounts paid matched to the accounting records of Moldovagaz.

⁷¹ Consolidated cash flow statements were prepared by Moldovagaz for the purposes of management accounting and are not audited. The Auditors have not verified their completeness or accuracy.



- (150) Net operating cashflows were mainly used to fund investment activities in the same period when received as shown on the chart above. In 2017, net operating cashflow was MDL 1,467 million, an increase of MDL 1,022 million compared to prior year. Moldovagaz explained that this was due to a 16% decrease in the average USD price of gas from Gazprom and the strengthening of Moldovan Lei by approximately 7% compared to the previous year. These favourable conditions resulted in positive customer tariff deviations. Moldovagaz advised that the accumulated cash was used as a reserve against relevant adjustments to the tariff in later years (see Section 4.7.2 below).
- (151) Payments to employees including social and health insurance have steadily increased over the review period. Moldovagaz stated this is primarily due to the inflationary adjustments, as the average number of employees has remained relatively constant at approximately 5.3 thousand over the last 9 years.
- (152) The Auditors compared actual cash outflows from investment activities to Moldovagaz's budgeted investment and capital repairs program from 2013 to 2021⁷² without material exceptions, i.e. Moldovagaz complied with their investment programs and budgets.
- (153) The cashflows from financial activities were negligible (less than 1% of the cash from sales) during the period 2006 to 2021.
- (154) In summary, the cash flow analysis shows the majority of cash received from customers has

⁷² As presented in the Board of Moldovagaz reports to the Annual Shareholders Meetings for 2013 to 2021.

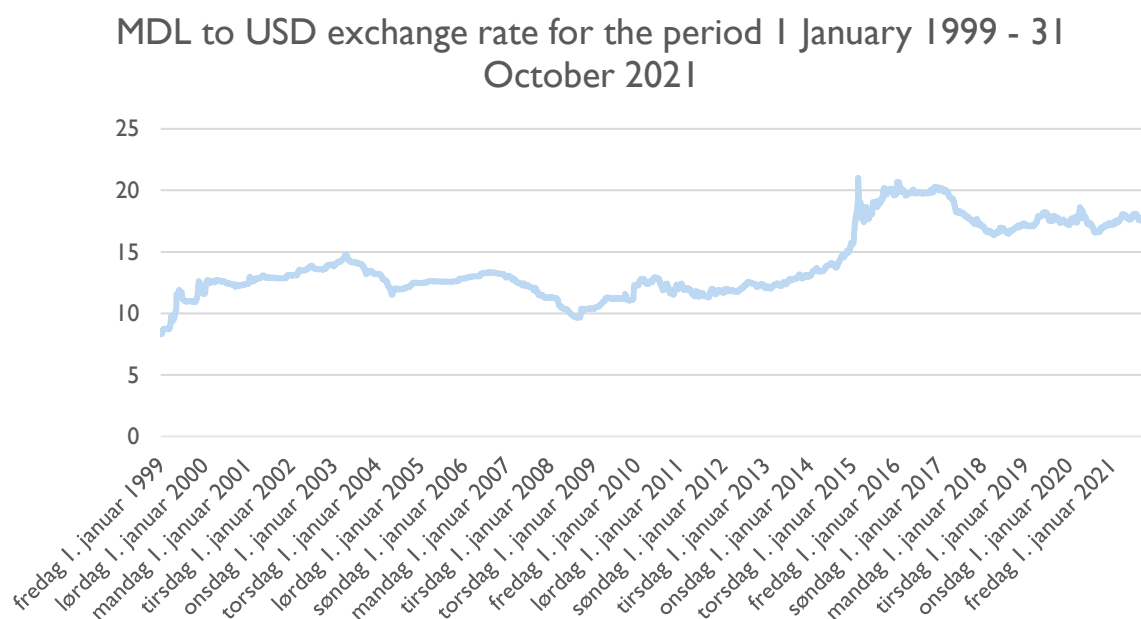
been used to pay down the debt due to Gazprom and to pay customs. However, it also shows that the cash paid for operating expenses has been increasing as a percentage of overall cash outflows.

4.7 Key factors causing the Debt increase during 2011 to 2020

4.7.1 Increase in MDL debt due to historical exchange rate movements

- (155) The factor causing the largest single element of the debt increase in the period 2011 to 2020 in local currency is due to accumulated exchange rate losses. While the major liability of Moldovagaz is priced in USD, all the cash inflows are in MDL, primarily cash inflows from Moldovagaz's customers.
- (156) During the period 1 January 1999 to 31 December 2020, the MDL depreciated against the USD by 107% from 8.3 to 17.2 MDL⁷³, as set out Figure 6 below.
- (157) In particular, the MDL depreciated against USD by approximately 64% during the period 2011 to 2016, which coincides with the period of fastest Debt growth. In 2016 and 2017 MDL strengthened slightly against USD, then remained relatively stable until the end of the 2021, which is matched by the profile of the Debt in MDL shown in Figure 2 above.

Figure 6.

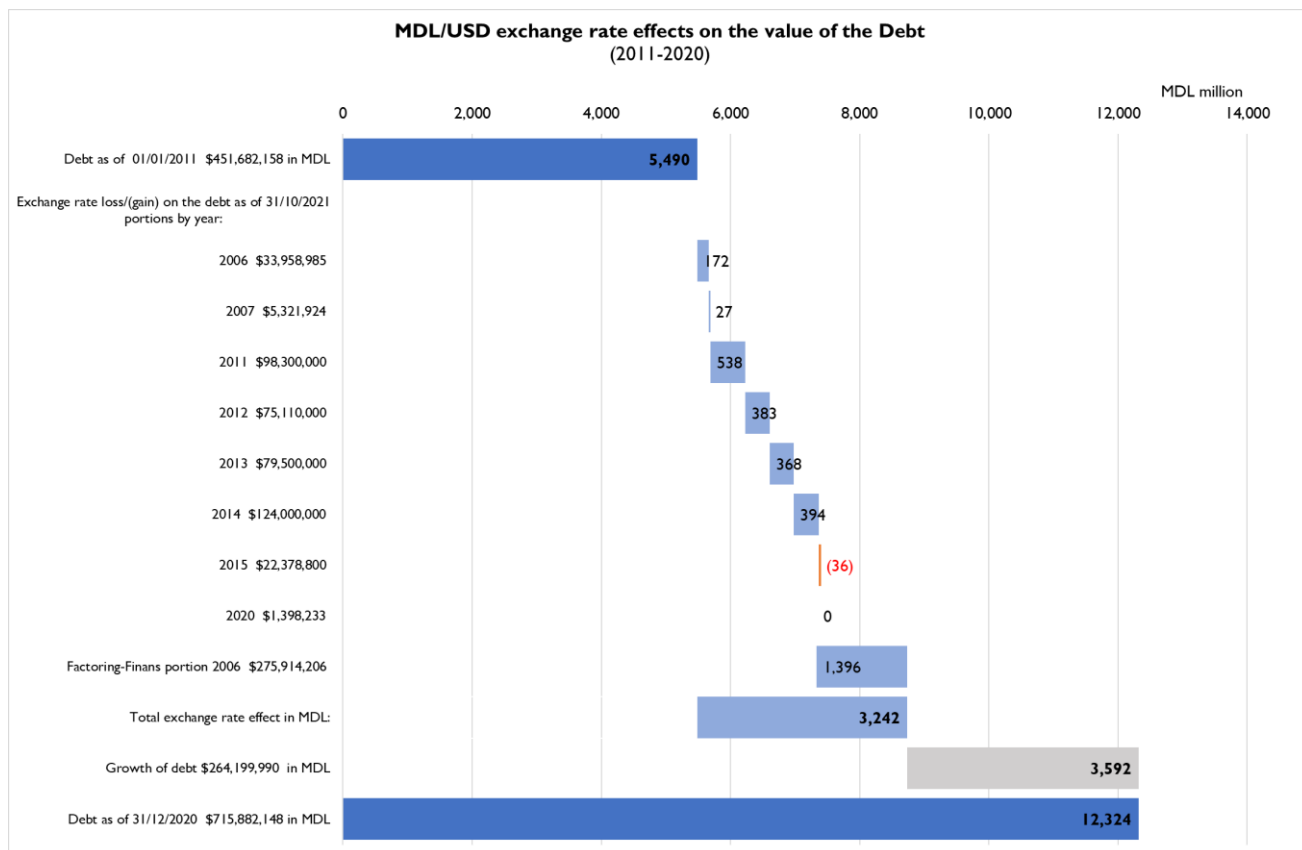


- (158) Depreciation of the MDL against the USD undermines the ability of Moldovagaz to repay its historical debt to Gazprom, which is denominated in USD. During the period 1 January 2011 to 31 December 2020, the Debt increased by 58% from USD 451,682,158 to USD 715,882,148. However, when denominated in MDL, the Debt increased by 124%, of which about 47% of this increase is attributable to foreign exchange loss as demonstrated in Figure 7 below. In other words, out of the MDL 6,834 million increase in the Debt in the period 2011 to 2021, MDL 3,242 million is due to the depreciation of the MDL against the USD. The factors responsible for the remaining increase of MDL 3,592 million in this period are set out

⁷³ Official exchange rates published by the National Bank of Moldova.

in the sections that follow.

Figure 7.1



4.7.2 Customer tariff setting

- (159) It is relevant to understanding some of the factors causing the Debt growth, to be described later in this report, to first understand the process for setting the tariffs to be charged to Moldovan customers for using gas.
- (160) The Regulator, ANRE, develops the methodology for setting the customer tariff for natural gas based on the two key components: the cost of carrying out the regulated activities (i.e., transit, distribution, and supply of natural gas), and the allowed profitability for each of the activities. The cost of carrying out the regulated activities comprises the cost of natural gas purchased from Gazprom, other operating expenses incurred by Moldovagaz in carrying out their regulated activities, and investments made by Moldovagaz. The profits Moldovagaz can make are limited by the tariff.
- (161) The Auditors were advised by representatives of Moldovagaz and ANRE that the tariff setting methodology is revised and approved by ANRE, typically once every five years, and the customer tariffs are set yearly in accordance with the methodology in place at the time. The tariff considers the actual value of the variable elements of the tariff, such as the purchase price of gas from Gazprom, and Moldovagaz's costs within the period. Although the purchase price of gas is the largest element of the tariff, there are other significant elements to consider.
- (162) Since the tariff is set for a year, it does not typically consider any events that happen within that year, such as changes in the gas price, foreign exchange rate, any additional costs

incurred by Moldovagaz, etc. Any such changes are considered tariff deviations, which can be both positive (i.e., Moldovagaz's costs are lower than expected causing it to receive more funds than its total budgeted costs and profit element through the tariff) or negative (i.e., Moldovagaz costs were higher than included in the tariff, such that receipts from customers are insufficient to cover both its costs and profit element). ANRE would consider the deviations and, if acknowledged, would adjust the tariff for the next year to offset the deviations.

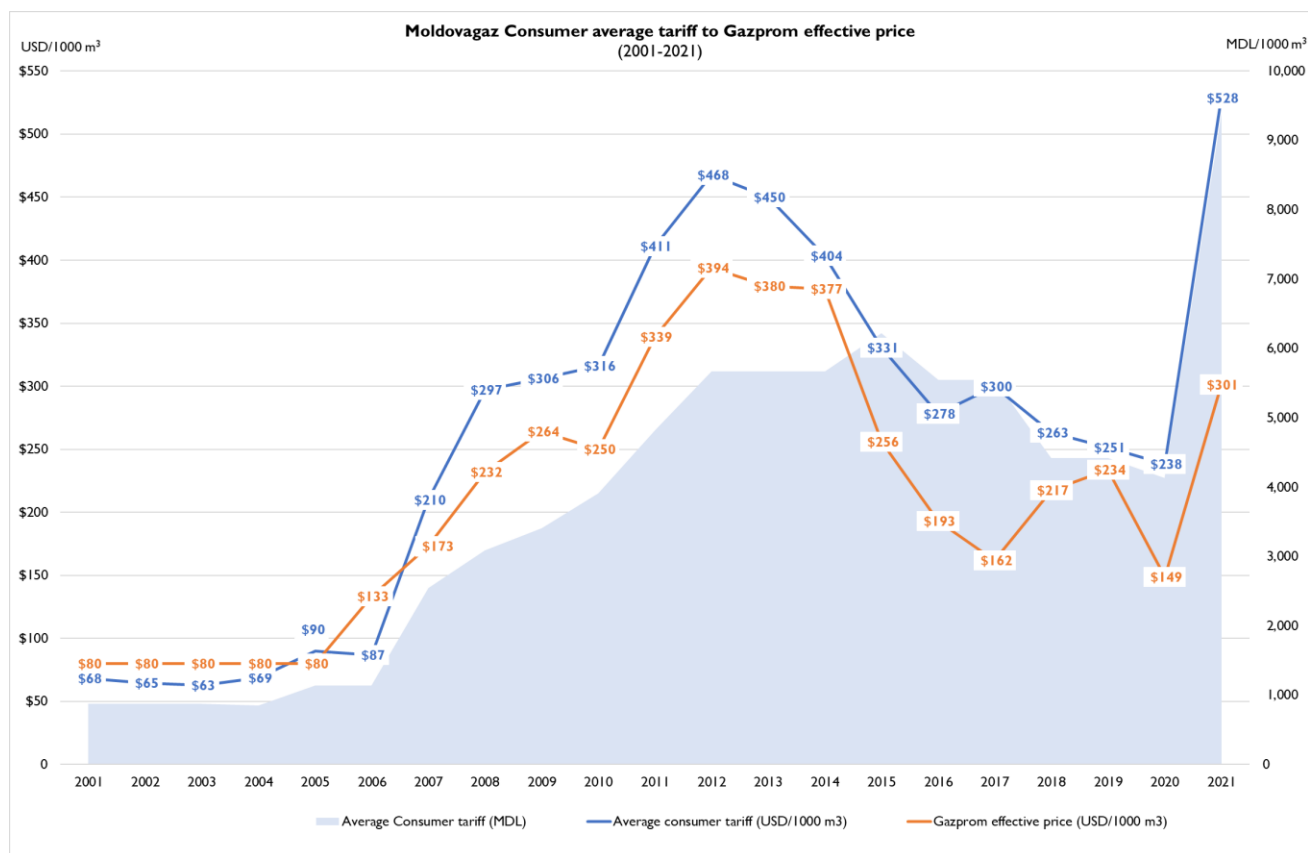
- (163) Normally, it would be beneficial for an entity which operates in such an environment to accumulate a cash reserve to be used to offset any negative tariff deviations that might occur until the new tariff is set and additional funds received. However, Moldovagaz stated that as it has a significant liability, the Debt, the need to repay the Debt takes priority over accumulating cash reserves. In addition, if negotiations between Moldovagaz and ANRE regarding tariff adjustments take longer than a year, the value of any negative tariff deviations would accumulate. The impact of a delay in receiving funds to offset negative tariff deviations increases in circumstances where the MDL has depreciated against the USD.
- (164) Moldovagaz stated that they and the ANRE have been engaged in regular communications regarding investment costs and expenses to be included in the customer gas tariffs. Moldovagaz stated that:
1. ANRE has developed tariff setting methodologies covering five five-year periods during the review period: 2001 to 2004, 2004 to 2009, 2010 to 2014, 2015 to 2020, and 2021 to current⁷⁴.
 2. In all years, Moldovagaz would provide ANRE with their calculations of their actual costs, of which some would be accepted by ANRE for the purposes of setting the customer tariff in the current or future periods, and some would be rejected by ANRE.

4.7.3 Gas prices used for the purposes of tariff calculations

- (165) The Auditors reviewed the gas purchase prices used by the Regulator for the purposes of tariff calculations in the period 2011 to 2021 and noted that in some periods the tariff did not change, while gas prices moved significantly. The comparison between the gas prices included in the tariffs and the average price per year paid by Moldovagaz to Gazprom is set out in the graph below. In the period 2001 to 2004, and in 2006, the price paid by Moldovagaz to Gazprom for gas was higher than the tariff price paid by its customers.
- (166) Although the average price paid by Moldovagaz to Gazprom was below the average price paid by Moldovagaz's customers in all years since 2006, the difference between the two prices has been volatile. The difference between the price paid to Gazprom and the price charged to the customers was particularly low in 2014 and 2019. This volatility of the price margin impacts Moldovagaz's ability to develop long-term budgeting and investment programs, including the schedule of repayment of the Debt.

Figure 8.

⁷⁴ "Metodologii tarifare" schedule as provided by ANRE.



(167) The effective average gas price from 2001 to 2005 was slightly lower than Gazprom's price of USD 80 per 1000 m³ due to the purchases of gas from the alternative supplier Gazexport⁷⁵, which was selling gas at lower prices compared to Gazprom.

4.7.4 Key factors causing USD Debt accumulation during 2011 to 2020

(168) Moldovagaz provided the Auditors with its analysis of the key factors contributing to the increase of the USD Debt during the period 2011 to 2020. The Auditors reviewed this analysis and, where possible, performed checks to verify the results. The Moldovagaz analysis provides an explanation for USD 231 million of the USD 264 million Debt growth in this period. The remaining USD 33 million of Debt growth in this period is unexplained, but is likely due to a number of smaller factors.

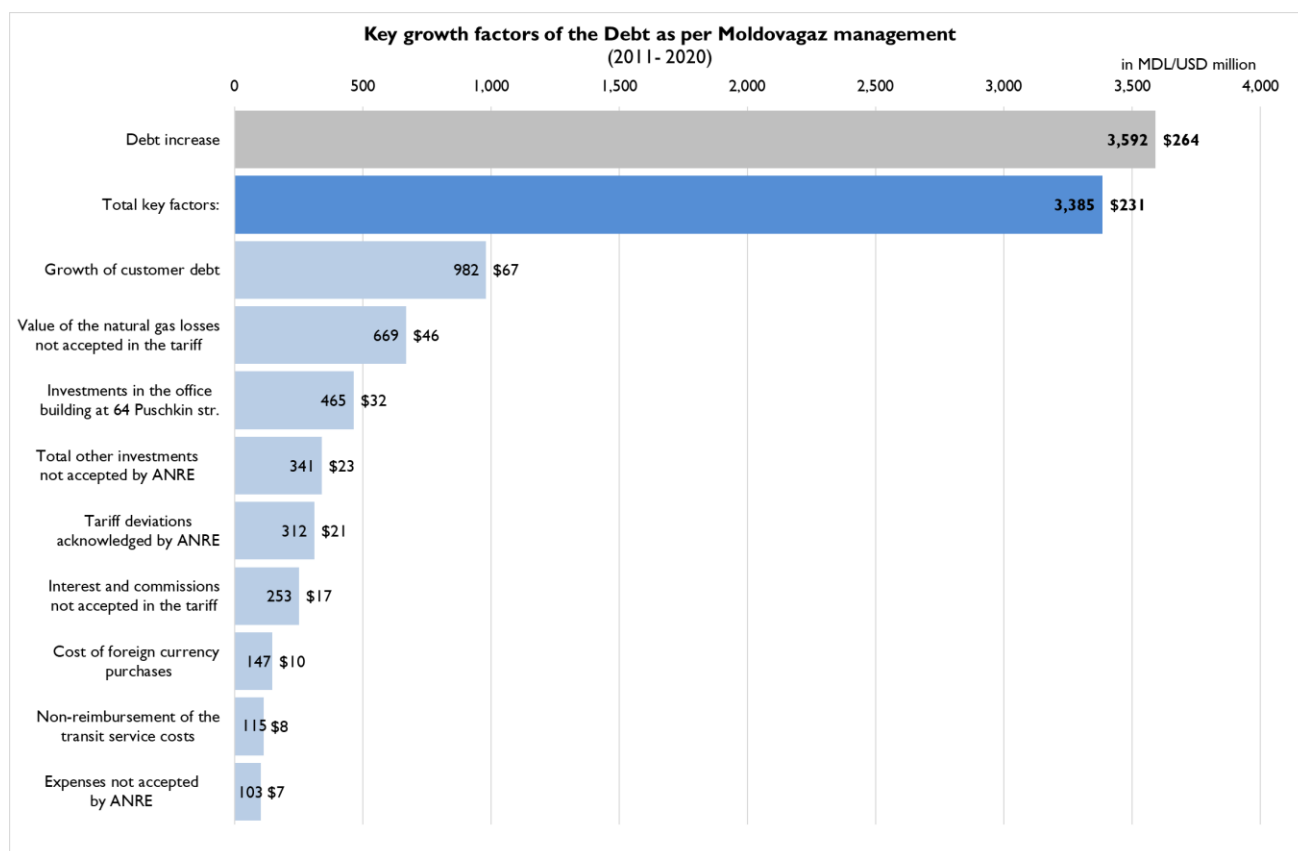
(169) The key factors contributing to the USD 249 million of the Debt increase in the period 2011 to 2020 per Moldovagaz's analysis are as follows (see also Figure 9 below):

1. Increase in the indebtedness of Moldovagaz customers – MDL 982 million (USD 67 million equivalent) (see Section 4.7.5 below);

⁷⁵ Gazexport share of gas volumes peaked in 2005 at 58% of the total gas volumes supplied to the Right Bank as per Table No. 1, 2005 the Board of Moldovagaz Report to the Annual Shareholder Meeting.

2. Value of natural gas losses not accepted in the tariff – MDL 669 million (USD 46 million equivalent) (see Section 4.7.6 below);
3. Cost of construction of office building at 64 Puschkin street in Chisinau – MDL 465 million (USD 32 million equivalent) (see Section 4.7.7 below);
4. Moldovagaz investments not accepted by ANRE because Moldovagaz did not demonstrate their efficiency – MDL 341 million (USD 23 million equivalent) (see Section 4.7.8 below);
5. Tariff deviations acknowledged by ANRE and to be compensated during the 2021 to 2025 regulatory period – MDL 312 million (USD 21 million equivalent) (see Section 4.7.9 below);
6. Interest and commissions not accepted in the customer tariff – MDL 253 million (USD 17 million equivalent) (see Section 4.7.10 below);
7. Cost of foreign currency purchases not accepted by ANRE – MDL 147 million (USD 10 million equivalent) (see Section 4.7.11 below);
8. Non-reimbursement of transit service costs – MDL 115 million (USD 8 million equivalent) (see Section 4.7.12 below); and
9. Expenses not accepted by ANRE for the purposes of tariff calculations because Moldovagaz did not demonstrate their efficiency – MDL 103 million (USD 7 million equivalent) (see Section 4.7.13 below).

Figure 9.



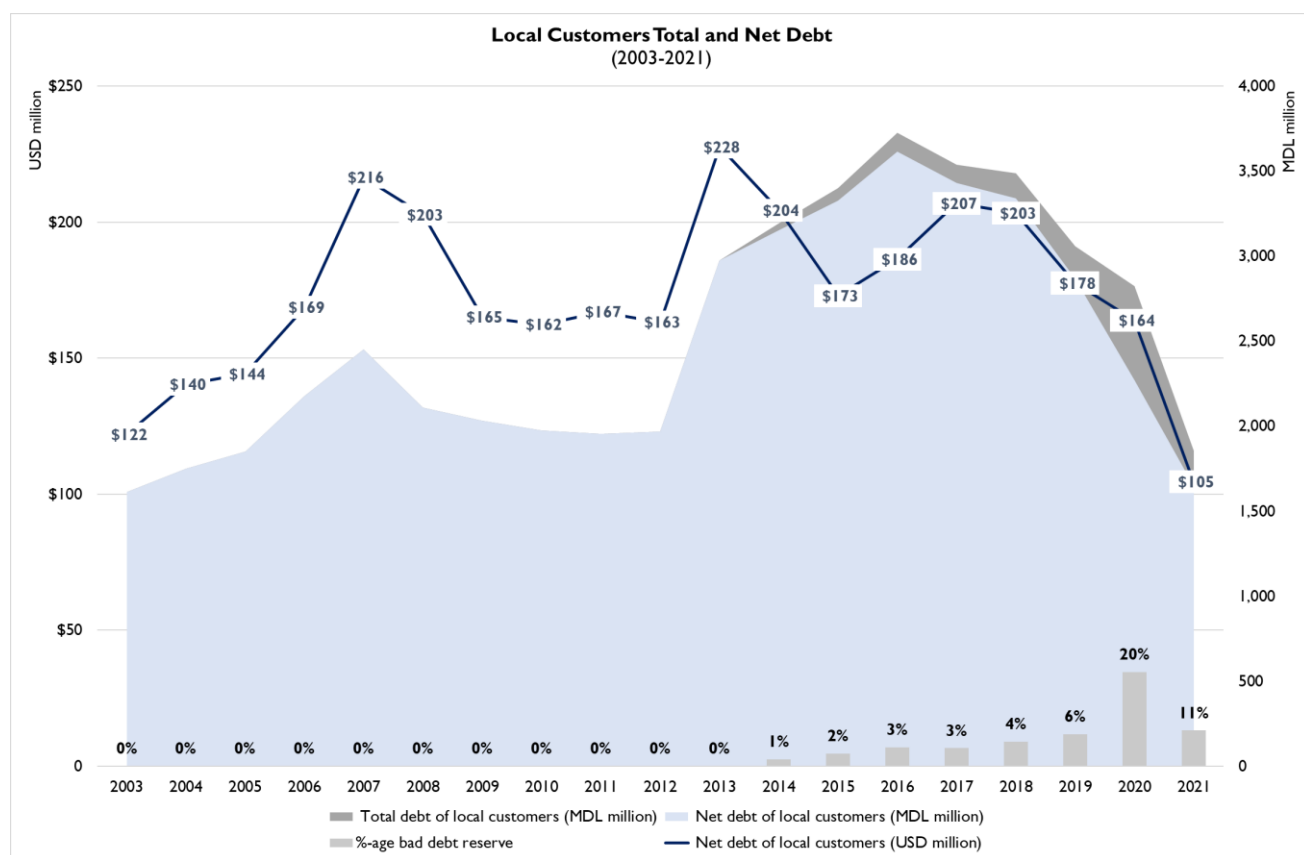
4.7.5 Debt growth caused by an increase in the indebtedness of Moldovagaz customers

- (170) Any debt owed to Moldovagaz by its customers on the Right bank for gas used limits the amount that Moldovagaz can pay Gazprom for gas supplied in the relevant period or to repay historical Debt.
- (171) In addition, the debt owed to Moldovagaz by its customers is denominated in MDL, while the Debt owed by Moldovagaz to Gazprom is denominated in USD. Therefore, if the MDL depreciates against the USD, when the customers pay their debts the MDL received no longer covers the original USD value of the gas used, thereby leaving a residual debt.
- (172) The debt owed by Moldovagaz's customers is recorded in both its accounting records and in its financial statements. For the period 2003 to 2013, the Auditors confirmed that the total debt owed by customers per Moldovagaz's contemporaneous accounting records agreed to the balance shown in its financial statements. In the period 2014 to 2021 the year-end balance owed by local customers per Moldovagaz's accounting records exceeded the balance shown in the financial statements figures due to the inclusion of a bad debt reserve.⁷⁶ These differences, starting in 2014, are shown in the chart below.⁷⁷

⁷⁶ Moldovagaz's external auditors included a disclaimer in their opinion on the financial statements in the period 2008 to 2021 due to a disagreement or inability to confirm the calculation of the bad debt reserve recorded by Moldovagaz.

⁷⁷ The chart shows the year end balances as of 31 December of each year.

Figure 10.



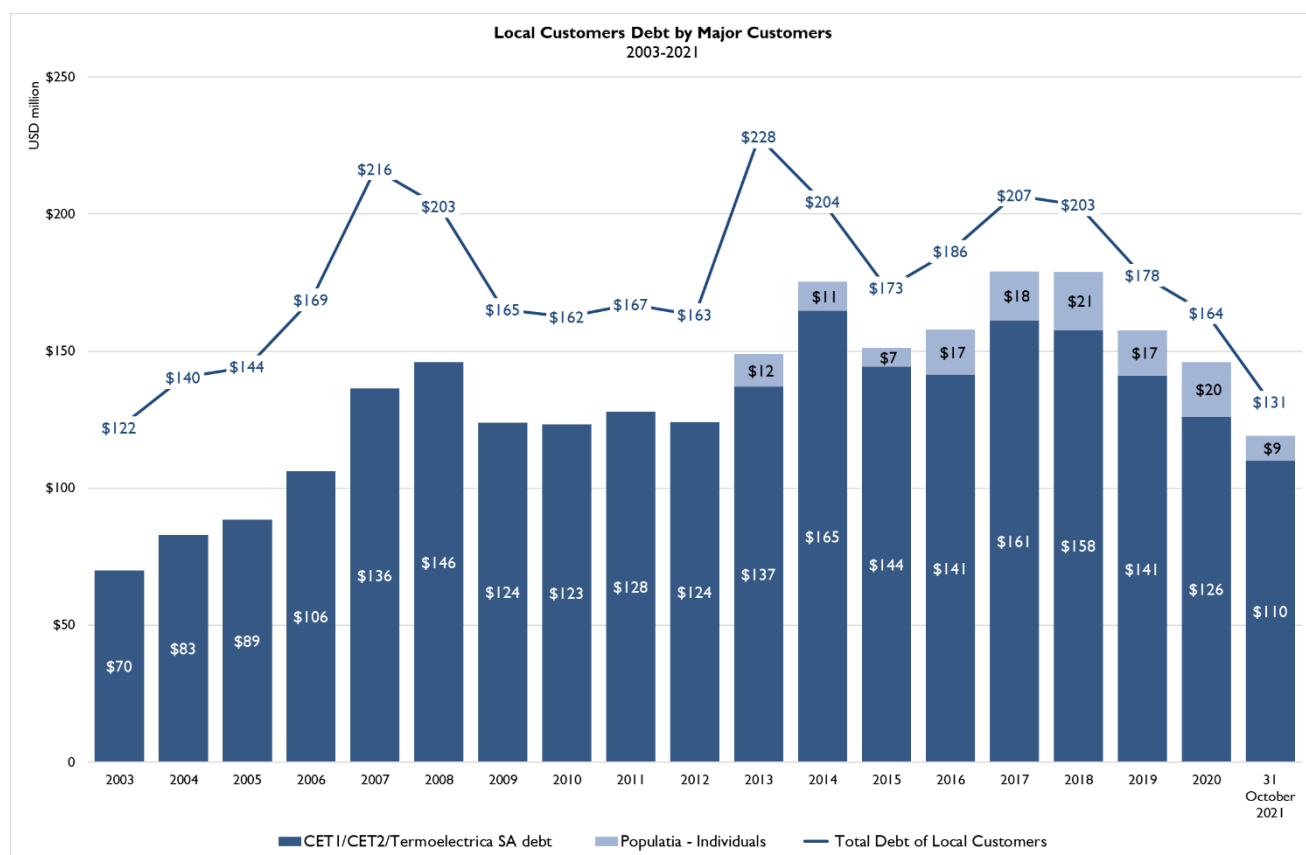
- (173) Debt due from local customers when translated into USD from MDL shows a different profile in some years, e.g. 2013 to 2015. These represent periods of significant change in the MDL : USD exchange rate.
- (174) The analysis performed by the management of Moldovagaz estimates customer debt and other receivables increased by MDL 982 million, USD 67 million equivalent, during the period 2011 to 2020⁷⁸.
- (175) The majority of the debt owed to Moldovagaz in the period 2003 to 2021 was owed by one major customer, Termoelectrica SA⁷⁹ ("Termoelectrica"). The chart below shows the total debt owed to Moldovagaz by local customers in USD and the level of debt owed by Termoelectrica compared to other customers.⁸⁰

⁷⁸ As per accounting records MDL 1,007 million = (MDL 2,823 million (Local customers' debt) + MDL 382 million (Other receivables)) – (MDL 1,974 million (Local customers' debt) + MDL 233 million (Other receivables)); was the increase in the total debt of local customers and other receivables through 2011 to 2020.

⁷⁹ Termoelectrica SA is the main producer of electricity in right-bank Moldova (<https://termoelectrica.md/despre/cine-suntem/>).

⁸⁰ Based on our analysis of the Account 221 "Settlements with Local Customers" for 2003 to 2021.

Figure 11.



- (176) The Termoelectrica debt accounted for approximately 72% of the total debt owed by local customers, except for 31 December 2021 when the debt reduced to USD 42 million due to a major offset related to the assignment of a contract with Energoacom SA for the total amount of MDL 1,331 million (USD 75 million)⁸¹ with Moldovagaz. The Auditors were advised by Moldovagaz that the assignment followed a decision by the Moldovan Government to transfer the debt of Termoelectrica to Energoacom, which then repaid it to Moldovagaz on 26 November 2021⁸² using state funds.⁸³

4.7.6 Amount of allowable gas losses

- (177) The tariff setting methodology allows for a certain annual amount of gas losses to be reimbursed through the customer tariff.
- (178) Gas losses are gas volumes purchased by Moldovagaz from Gazprom but not delivered to a paying customer. The main reasons stated by Moldovagaz for gas losses are theft of gas from the gas distribution system (e.g., by manipulating gas meters or illegal tapping of gas pipes); and the losses attributable to the condition of the gas transport and distribution system (i.e., leakage from the pipeline network).

⁸¹ At MDL/USD rate of 17.7261 as of 26 November 2021. The Auditors were not provided with local customers balances as at 31 October 2021.

⁸² Two payments for MDL 665,621,614 and MDL 665,000,000 dated 26 November 2021. These transactions post the period of our review.

⁸³ <https://www.moldpres.md/en/news/2021/11/26/21009083>.

- (179) In 2011, ANRE adopted a new methodology⁸⁴, for calculating the amount of gas losses which could be reimbursed through the tariff, which reduced the average allowable gas losses from 60 million m³ to 19 million m³ per year during the period 2011 to 2020. Moldovagaz has estimated the total cost of gas losses incurred and not reimbursed through the customer tariff was MLD 669 million, USD 46 million equivalent, during the period 2011 to 2020.
- (180) In response to the new limits on the amount of gas losses recoverable through the customer tariff, Moldovagaz introduced the following measures to reduce losses:
1. Implementation of additional gas meters in order to identify areas where the losses were occurring, at a total cost of MDL 60 million, see also Section 4.7.8;
 2. Implementation of security boxes over gas meters to protect them from tampering, at a total cost of MDL 45 million, see also Section 4.7.13; and
 3. Improvements in the gas meter reading submission process.
- (181) Moldovagaz stated that following implementation of these measures the volume of gas losses reduced from 54.4 m³ million in 2011⁸⁵ to 26.9 m³ million in 2021⁸⁶. Moldovagaz states that the above costs were not accepted as allowable investments by ANRE for inclusion in the customer tariff.
- 4.7.7 Construction of Moldovagaz's new Head Office building*
- (182) The total cost of the construction of Moldovagaz's new headquarters at 64 Puschkin street, Chisinau was MDL 465 million (USD 32 million equivalent)⁸⁷. This cost was incurred over the period 2009 to 2018. None of this expenditure was accepted by ANRE for the purposes of the customer tariff calculations.
- (183) Moldovagaz advised the Auditors that the construction of the building was funded through the profitability element included within the customer tariffs. The Auditors identified a number of loans taken by Moldovagaz to fund the construction. According to Moldovagaz the total amount of loans taken to cover costs of the construction in the period 2010 to 2013 was MDL 138 million. The loans, including MDL 13 million interest, were fully repaid by the end of 2015.
- (184) The Auditors are not in the position to assess whether the construction of the building was crucial for the operations of Moldovagaz or good value for money. However, the initial budget for the construction set in 2009 was MDL 231 million, so the actual cost exceeded the original budget by 93%. Moldovagaz advised the Auditors that the increase in total cost was attributable to an increase in the size of the building originally planned and the impact of inflation within the construction period.
- (185) In 2018, the office building was sold to Moldovagaz subsidiary⁸⁸, SRL "Flakare-Albastra" for MDL 544.9 million. The buyer will repay the total amount in instalments over a 35-year

⁸⁴ "The Methodology for calculating technological costs and technical losses of natural gas in distribution networks" No. 398 dated 31 December 2010.

⁸⁵ 2011 Moldovagaz Board Report to Shareholders dated 09 April 2012, page 10.

⁸⁶ 2021 Moldovagaz Board Report to Shareholders dated 29 April 2022, page 4.

⁸⁷ The Auditors agreed this amount to the accounting records and Board Reports of Moldovagaz.

⁸⁸ https://www.moldovagaz.md/files/userfiles/file/presa/2015/presa_22-05-2015_Moldavskie-Vedomosti.pdf.

period.⁸⁹

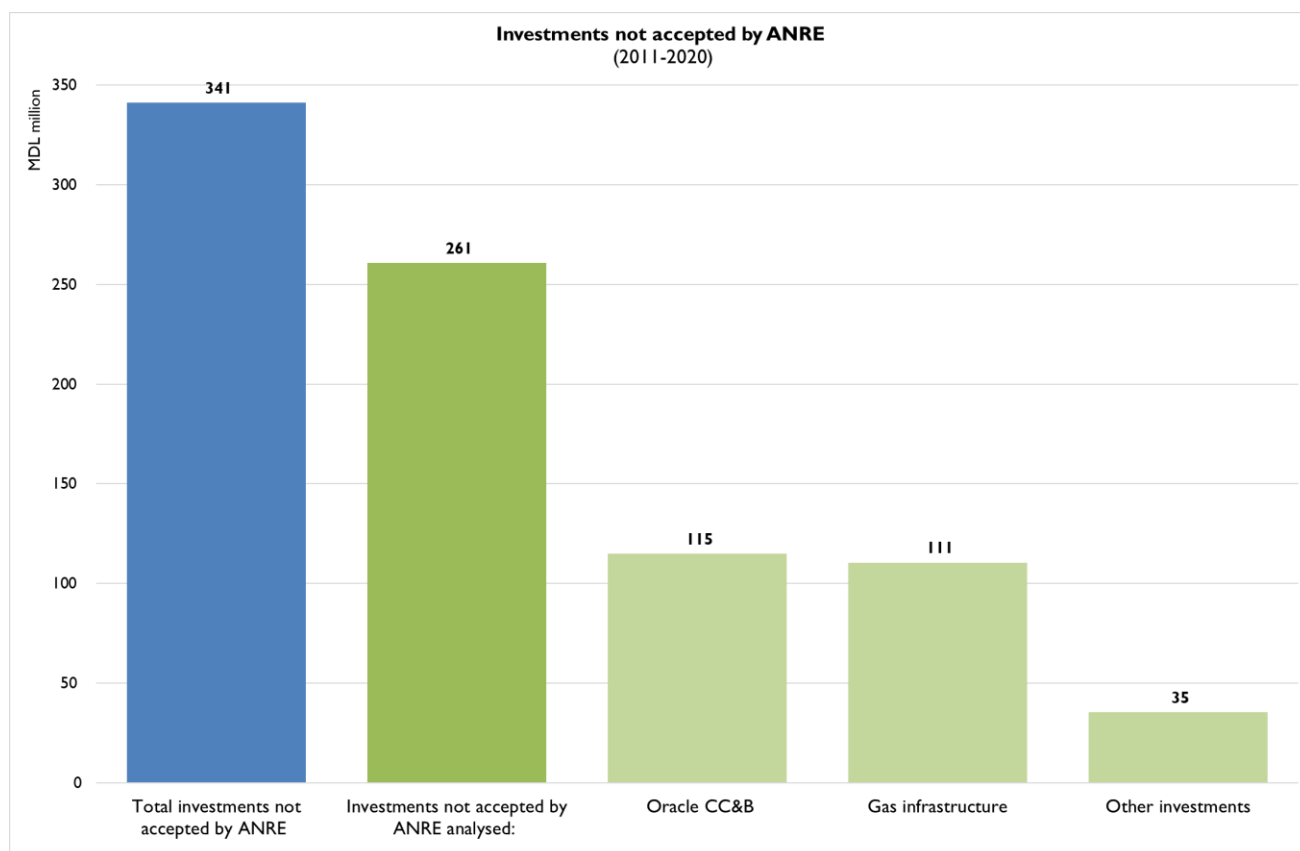
4.7.8 *Investments not accepted by ANRE*

- (186) The tariff setting methodology provides for the cost of investments to be made by Moldovagaz in the course of carrying out regulated activities to be included in the gas tariff, and therefore to be repaid to the entity. One of the key elements of the tariff setting consideration is return on investment, which is calculated based on the value of Moldovagaz's capital assets, accepted by the Regulator. The tariff also accounts for the annual depreciation of those assets.
- (187) Any investment made by Moldovagaz and not accepted by the Regulator, negatively affects the cash inflow to the entity.
- (188) The Auditors analysed the investments accepted / not accepted by the Regulator for the purposes of tariff calculation during the period 2011 to 2020.⁹⁰ The total amount of the investments made by Moldovagaz (including their subsidiaries) in this period was MDL 2,816 million, of which the ANRE did not accept MDL 341 million (USD 23 million equivalent), or 12%, for inclusion in the customer tariff. We understand that these investments were not allowed because Moldovagaz did not demonstrate their economic efficiency. The main categories of investments not accepted by the regulator are set out in Figure 12 below:

⁸⁹ Moldovagaz Board decision N0 78 dated 30 November 2018.

⁹⁰ The Auditors did not include the investment in the Moldovagaz new Head Office building in Chisinau in this section.

Figure 12.



1. Purchase and implementation of Oracle Utilities Customer Care and Billing system (“Oracle CC&B”) amounting to MDL 115 million. Moldovagaz stated that this system is critical for its operations;
2. Investments in gasification and new gas pipelines amounting to MDL 111 million. Included within this amount is the MDL 60 million related to the implementation of additional gas meters as part of Moldovagaz’s programme to reduce gas losses (as described in Section 4.7.6 above). Moldovagaz stated that in this category it experienced that some unexpected costs during construction process, which by their nature cannot be pre-approved; and
3. Other investments, including administrative, IT, equipment, and buildings amounting to MDL 35 million.

(189) The auditors have not made a determination as to whether any of the above investments should have been allowable for inclusion in the customer tariff. However, funds spent on disallowed investments cannot be used to reduce the Debt.

4.7.9 *Tariff deviations acknowledged by ANRE*

(190) Moldovagaz advised the Auditors that some portion of accumulated tariff deviations have been acknowledged by the Regulator. When ANRE acknowledges tariff deviations, both positive and negative, these are typically compensated through adjustments in the customer tariff in later periods. For the period 2011 to 2020 Moldovagaz has calculated the total net impact of such deviations to be MDL 312 million (USD 21 million equivalent). We understand

that these deviations will be recovered through the tariff for the period 2021-2025.

- (191) The Auditors reviewed the calculations presented by Moldovagaz and agreed selected amounts to the documentation provided by ANRE and Moldovagaz. No exceptions were identified.

4.7.10 *Interest and commissions not accepted in the customer tariff*

- (192) Moldovagaz stated that financial expenses of Moldovagaz, such as credit interest and bank commissions, are not allowable for the purposes of setting the customer tariff. The amount of the financial expenses incurred by Moldovagaz in the period 2011 to 2020 was MDL 253 million (USD 17 million equivalent), although Moldovagaz stated that there were no additional loans taken or interest accrued after the end of 2018.

- (193) The Auditors agreed selected amounts related to bank commissions and fees paid by Moldovagaz to its accounting records. No significant exceptions were identified.

4.7.11 *Cost of foreign currency purchases*

- (194) Moldovagaz advised the Auditors that costs associated with the purchase of foreign currency used to make payments to Gazprom are not allowable for the purposes of setting the customer tariff. In particular, any variance between the exchange rate as at the date of the accounting transaction (i.e. purchase of gas from Gazprom) and the date of the foreign currency purchases (i.e. at the day of the actual payment) cannot be included in the customer tariff. This only relates to realised foreign exchange rate gains/losses which occur on a regular basis as part of Moldovagaz day to day operations. Moldovagaz calculated that the total amount of such costs as MDL 147 million (USD 10 million equivalent) for the period 2011 to 2020.

- (195) The Auditors re-calculated the net foreign exchange loss over the period from Moldovagaz's contemporaneous accounting records to be higher at MDL 173 million (USD 11.7 million).

4.7.12 *Non-reimbursement of transit service costs*

- (196) Moldovagaz advised that since the transit tariff methodology changed from distance-based to entry-exit in 2020⁹¹, during the transition period, Moldovagaz did not receive the transit fees in full. Moldovagaz calculated that they under received a total amount of MDL 115 million (USD 8 million equivalent). Moldovagaz stated that they expect ANRE to accept this amount as allowable and to reimburse Moldovagaz through customer tariff adjustments in later periods.

- (197) The Auditors were not provided with sufficient information to verify this amount.

4.7.13 *Expenses not accepted by ANRE*

- (198) Moldovagaz stated that certain other operating expenses incurred in the period 2011 to 2020 amounting to MDL 103 million (USD 7 million equivalent) had not been accepted as allowable for customer tariff setting purposes, of which MDL 45 million related to the implementation of security boxes over the gas meters to protect the meters from fraudulent manipulations as part of the programme to reduce gas losses (as set out in Section 4.7.6 above). We understand that these expenses were not allowed because Moldovagaz did not demonstrate their economic efficiency.

⁹¹ Under distance-based tariffs, a shipper is required to pay a charge based on the distance between designated entry and exit points, while in entry-exit tariff system, a separate tariff is quoted for each entry and exit point.

- (199) The Auditors reviewed the calculations presented by Moldovagaz and agreed selected expense amounts to Moldovagaz's accounting records. No exceptions were identified.

4.8 Valuation of assets used in partial Debt settlement arrangements

- (200) From a small number of documents provided by the Moldovan archives, the Auditors have a limited understanding of the debt-to-equity swaps which occurred in 1995 and 1999.
- (201) The documents record that following the dissolution of the Soviet Union in 1991, Moldova experienced difficulties making timely payments for gas supplied by Gazprom. By the end of 1994, the total debt (Right and Left banks) for gas supplied by Gazprom was recorded as USD 190 million, of which approximately USD 100 million was recorded as related to the Right bank. In addition, an amount of approximately USD 150 million was recorded as a debt for accrued interest and penalties.⁹² As no accounting records or underlying supporting data have been provided, the Auditors are unable to verify these amounts.
- (202) In 1995, a new entity, Gazsnabtranzit was established with the shareholders being: Gazprom (50%); state concern Moldova-gaz (27%); Moldovatransgaz (12%); and Tiraspoltransgaz (11%), with a total capital of USD 104 million⁹³. The Government of Moldova transferred certain assets from state-owned Moldovatransgaz to Gazprom as a partial debt settlement for the gas supplied up to 1994. The recorded value of the transferred assets, as at 12 May 1995, was USD 52 million (MDL 220 million).⁹⁴ Gazprom contributed these assets to Gazsnabtranzit in exchange for 50% of its share capital. The Auditors have not been provided with information recording amount of the debt settled as a result of this exchange for either Right bank or Left bank.
- (203) By Government Decree No 1068 dated 21 October 1998, the value of the assets transferred to Gazprom by Government Decree No 302 in May 1995 was increased from USD 52 million to USD 85.3 million based on a revaluation performed in 1996.⁹⁵ The Auditors have not been provided with any information as to who performed this revaluation, the valuation methodology used, or any underlying supporting data. Also no information was provided to the Auditors as to whether this revaluation resulted in a further reduction in the debt owed to Gazprom.
- (204) In 1999, Moldovagaz was established with a total capital of USD 291 million (MDL 1,333 million), of which USD 78 million related to assets located on the Left bank. Gazprom maintained a 50% in the newly established entity as follows:
1. USD 85.3 million – restated value of the assets Gazprom previously contributed to Gazsnabtranzit; and
 2. USD 60 million – additional assets transferred to Gazprom by the Moldovan government and government of the unrecognised Transnistria against part of the Debt (USD 47.3 million related to the Debt of the Right bank, and USD 12.7 million related to the debt of the Left bank).⁹⁶

⁹² Moldovan Ministry of privatisation and property management, Statement on Gazsnabtranzit No 797 dated 27 July 1995.

⁹³ Founding Agreement of Gazsnabtranzit.

⁹⁴ Decree by the Government of the Republic of Moldova No 302 dated 12 May 1995.

⁹⁵ Decree by the Government of the Republic of Moldova No 1068 dated 21 October 1998.

⁹⁶ Agreement on the formation of share capital of Moldovagaz between the government of Moldova, government of unrecognised Transnistria, and Gazprom, dated 23 October 1998.

- (205) On 19 December 2008 a report prepared by Ecofin-Audit-Service SRL set out the details of a revaluation of Moldovagaz's and certain subsidiaries⁹⁷ (located on the Right bank only) fixed assets (the "2008 Valuation Report").⁹⁸
- (206) The fixed assets of Moldovagaz and the subsidiaries were revalued from MDL 744 million to MDL 4,934 million, i.e., an increase in value of 563%. However, this revaluation relates to all of the fixed assets of Moldovagaz, including those acquired after its incorporation in 1999.
- (207) From Moldovagaz's accounting records, the Auditors identified assets acquired prior to 1996 (the year in which the assets of Moldovagaz predecessors, Moldovatransgaz and Tiraspoltransgaz were valued for the purposes of debt to equity swap with Gazprom). The assets of Tiraspoltransgaz are not included in the accounting books of Moldovagaz, therefore the Auditors only included assets which were part of Moldovatransgaz for the purposes of this exercise. The Auditors compared the value of these assets recorded in the books of Moldovagaz before and after the revaluation, and calculated that the ex-Moldovatransgaz assets acquired prior to 1996, increased in value from MDL 175,511,472 to MDL 2,152,954,825, or by 1127%, according to the results of valuation performed in 2008.
- (208) The increase in value of the assets in 2008 compared to 1996 might be due to several reasons. Any revaluation considers a number of factors when assessing the value of an asset, including the condition of the asset, market conditions, and current prices. The fact that the value of the assets in 2008 was estimated to be higher than in 1996 does not necessarily mean that the assets were undervalued in 1996. However, such possibility exists.
- (209) As set out in Section 5.1 of this report, the legal audit has revealed several irregularities and illegalities in connection with the establishment of both Gazsnabtranzit in 1995 and Moldovagaz in 1999, with a high likelihood that the assets contributed to Gazprom in payment of alleged Debts were undervalued. Also the Court of Accounts of Moldova (the "Court of Accounts"),⁹⁹ performed audits of Moldovagaz in 2002 and 2022. Both audits reported several irregularities and illegalities in connection with the establishment of both Gazsnabtranzit in 1995 and Moldovagaz in 1999, and highlighted risks that the assets contributed to Gazprom were undervalued and that the share capital was distributed incorrectly.

⁹⁷ SRL Chisinau gaz" and SRL "Moldovatransgaz".

⁹⁸ The Valuation date was 30 September 2008, however, the values were accepted as at 31 December 2008 as per Annex to the Minutes of meeting of Work Committee of SA "Moldovagaz" on summing up the results of valuation and revaluation of long-term tangible assets dated 23.02.2009.

⁹⁹ In Romanian: "*Curtea de Conturi a Republicii Moldova*".

5 LEGAL AUDIT

5.1 Irregularities and illegalities in connection with the establishment of Gazsnabtranzit and Moldovagaz and their impact on the Debt

5.1.1 Introduction

- (210) The subject of this audit, Moldovagaz, was only established in 1999. Moldovagaz's direct predecessor, Gazsnabtranzit, was established in 1995. As we understand it, gas was imported to Moldova directly from Gazprom through various Moldovan state entities, including the state concern Moldova-gaz (from 1994) and the State Department for Gasification (from 1991 to 1994),¹⁰⁰ before Gazsnabtranzit and Moldovagaz were established in 1995 and 1999, respectively. Gazprom did not have any ownership interests in the Moldovan gas supply infrastructure before Gazsnabtranzit was established in 1995.
- (211) In the years following the dissolution of the Soviet Union in 1991, Moldova experienced difficulties with making timely payments for the gas supplied by Gazprom and thus accrued certain debts towards Gazprom. Against this backdrop, Gazsnabtranzit was established in 1995 in the context of a debt/equity swap between Gazprom and the Moldovan Government. Parts of the then government owned gas infrastructure in Moldova were reportedly transferred to Gazprom, which in turn reportedly contributed the infrastructure as its share capital in Gazsnabtranzit in acquittal of parts of the Debt owed by the Moldovan Government.¹⁰¹
- (212) Another debt/equity swap was made when Moldovagaz was established in 1999. In that swap, the gas infrastructure assets of Moldova on the balance of the concern Moldovagaz, Gazsnabtranzit and Tiraspoltransgaz as of 1 July 1997 were valued at USD 290 million and apparently transferred to Moldovagaz, out of which USD 145 million apparently were transferred to Gazprom as its contribution to the share capital of Moldovagaz. Of Gazprom's contribution to the share capital, USD 47,3 million was payment for debts assumed by Moldova for gas delivered by Gazprom to Gazsnabtranzit.¹⁰²
- (213) The Court of Accounts of Moldova (the "**Court of Accounts**"),¹⁰³ which is the supreme audit institution of the Republic of Moldova, exercising control over the formation, administration and use of public financial resources,¹⁰⁴ performed comprehensive audits of Moldovagaz in 2002 and 2022. Both of these audits revealed several irregularities and illegalities in connection with the establishment of both Gazsnabtranzit in 1995 and Moldovagaz in 1999.
- (214) The report from 2002 (the "**2002 Audit Report**") led to certain decisions by the Court of Accounts which were set out in Decision No. NSS15/2002 of 14 February 2002 *"On the results of the audit into some aspects of the operations of the gas supply systems of the*

¹⁰⁰ Information page on the history of Moldovagaz on Moldovagaz's webpages, retrieved from <https://www.moldovagaz.md/rus/despre-companie/istoria> on 1 February 2023.

¹⁰¹ It follows from Article 5.1 of the Founders' Agreement of Gazsnabtranzit that the shares of the Founders were distributed in accordance with Decision by the Moldovan Government No. 302 of 12 May 1995, which provided in Article 2 letter c) that Gazprom's share was to be based on the transfer of the gas infrastructure assets on the balance of the Republication enterprise of main pipelines "Moldovatrangaz" and the Regional association of main pipelines "Tiraspoltransgaz" as payment of the Moldovan Government's debts for gas deliveries in 1994.

¹⁰² Agreement on the formation of the share capital of Moldovagaz, Annex No. 2 to the Shareholders' Agreement of Moldovagaz, item 3.

¹⁰³ In Romanian: "*Curtea de Conturi a Republicii Moldova*".

¹⁰⁴ Article 133 of the Constitution of Moldova, retrieved from the Moldovan State Register of Legal Acts (legis.md) on 30 January 2023 (https://www.legis.md/cautare/getResults?doc_id=111918&lang=ro).

Republic of Moldova" (the "**2002 Court of Accounts Decision**"),¹⁰⁵ while the report from 2022 (the "**2022 Audit Report**") led to certain decisions by the Court of Accounts which were set out in Decision No. 56 of 21 November 2022 (the "**2022 Court of Accounts Decision**").¹⁰⁶

- (215) The findings in the 2002 Audit Report and 2022 Audit Report will be referred to below to the extent they are relevant for this report.
- 5.1.2 *Irregularities and illegalities in connection with the establishment of Gazsnabtranzit in 1995*
- (216) In the 2002 Court of Accounts Decision,¹⁰⁷ the Court would *not confirm* that the assets invested by the shareholders in Gazsnabtranzit had been valued in accordance with the regulatory framework in force, in particular Article 9 (2) of the Moldovan law "*On Foreign Investments*" of 1 April 1991 (as further described above). In the 2022 Report, the Court of Accounts confirmed that the assets invested by the shareholders in Gazsnabtranzit had not been valued in accordance with the regulatory framework. Thus, according to the 2022 Report, there is a significant risk that the shares in the share capital were distributed incorrectly.¹⁰⁸
- (217) The 2002 Audit Report further noted that some of the main pipelines and other assets of the government-owned "Moldovatrangaz" had been left out of the accounting sheets that had formed the basis for the Moldovan Government's contributions to the share capital, with the effect that the Moldovan Government's rightful share was reduced and also to non-payment of a significant part of the Debt owed at that time.¹⁰⁹
- (218) According to the 2022 Audit Report, some assets that had been transferred by the Moldovan Government to the Transnistrian side were undervalued, which resulted in Transnistria receiving a higher ownership share of Gazsnabtranzit than what it was entitled to. According to the report, the Moldovan Government was entitled to an ownership share of 46,03% of Gazsnabtranzit (instead of 39%), while the Transnistrian side only was entitled to 3,97% (instead of 11%). This apparently led to the risk of an unjustified increase in the debts of the Right side in the amount of USD 7,313.850, and a corresponding unjustified decrease in the debts of the Left side in the same amount.¹¹⁰
- (219) Another deviation demonstrated by the 2022 Audit Report is the fact that only 76% of the actual length of the gas pipelines were included in the list of the assets deposited in Gazsnabtranzit, i.e. the pipelines invested in Gazsnabtranzit through Moldovatrangaz and Tiraspoltrangaz were listed as being shorter than they actually were, thus furthering the factual undervaluation of these assets.¹¹¹
- (220) Thus, the 2002 Audit Court of Accounts Decisions and the 2022 Court of Accounts Audit Report and Decision suggest that (1) the assets invested by the Moldovan Government in Gazsnabtranzit were undervalued and that (2) more of the Debt should have been set off against the Moldovan Government's investment in Gazsnabtranzit. Due to the time passed,

¹⁰⁵ 2002 Court of Accounts Decision, retrieved from the Moldovan State Register of Legal Acts (legis.md) on 30 January 2023 (https://www.legis.md/cautare/getResults?doc_id=2714&lang=ru).

¹⁰⁶ 2022 Court of Accounts Audit Report and Decision (Russian version retrieved from the webpage of the Court of Accounts of Moldova on 30 January 2023 at https://www.ccrm.md/ru/decision_details/1202/hotararea-nr56-din-21-noiembrie-2022-cu-privire-la-raportul).

¹⁰⁷ We have not seen the report (if any) underlying the 2002 Court of Accounts Decision.

¹⁰⁸ 2022 Court of Accounts Audit Report, Section 4.1.

¹⁰⁹ 2002 Court of Accounts Decision.

¹¹⁰ 2022 Court of Accounts Audit Report, Section 4.1.1.

¹¹¹ *Ibid.*, Section 4.1.1.

as well as the lack of available documents from this period, it is difficult, if not impossible, to quantify the deviations. The totality of the deviations suggests, however, that a significant part of the current Debt of Moldovagaz to Gazprom and Faktoring-Finans should be written off to account for the irregularities and illegalities in connection with the establishment of Gazsnabtranzit.

- (221) Moldovan Counsel has informed us that the estimated value (Ru: "оценочная стоимость") of the property contributions to the share capital of Gazsnabtranzit as approved by the Founders' Meeting on 22 June 1995 contradicted the contemporaneous legal provisions in force in Moldova.¹¹² According to paragraph 2 of Article 9 of the Foreign Investments Act No. 998 of 1 April 1992 (the "**1992 Foreign Investments Act**"), which was in force when Gazsnabtranzit was established, "[a]ll contributions to the authorized capital of an enterprise with foreign investments shall be appraised by agreement between its founders on the basis of world market prices." In practice, appraisal at "world market prices" entails a comparison with values or prices which existed in similar regional markets.¹¹³ However, the value appraisal of the assets comprised in the list attached to the Founding Agreement of Gazsnabtranzit was not carried out at "world market prices", thus violating paragraph 2 of Article 9 of the Foreign Investments Act.
- (222) Paragraph 2 of Article 9 of the Foreign Investments Act further provides that "[t]he final appraisal of these contributions shall be made at the time of the conclusion of the memorandum of association of the enterprise in the currency of the Republic of Moldova". However, the value appraisal of the assets was carried out based on the prices as of 1 January 1994, whereas the value appraisal should have been made "at the time of the conclusion of the memorandum of association", which was in May 1995.¹¹⁴ The value should have been corrected by the inflation accumulated between January 1994 and until May 1995.
- (223) That the assets of Gazsnabtranzit were not appraised in accordance with "world market prices", and, to our knowledge, not re-appraised in accordance with "world market prices" at a later point in time,¹¹⁵ strongly suggests that the assets contributed by the Moldovan Government in exchange for acquittal of parts of the Debt towards Gazprom were undervalued. Thus, less of the Debt was settled than what would have been the case if the applicable legislation had been complied with.
- (224) According to Moldovan Counsel, another deviation from the contractual and regulatory framework is that the assets of Gazsnabtranzit were appraised on the basis of the value of the fixed assets and other property of Moldovatrangaz and Tiraspoltrangaz, whereas they should have been appraised based on "the value of the going concern of Moldovatrangaz and Tiraspoltrangaz" pursuant to Article 5.1 of the Founding Agreement of Gazsnabtranzit and paragraph 2 (a) of Decision No. 302.¹¹⁶ This may have further narrowed the value of the assets and property that were transferred to Gazsnabtranzit.¹¹⁷ The appraisal should, in accordance with Moldovan law also have been carried out by an independent expert, and not by Moldovatrangaz and Tiraspoltrangaz themselves.¹¹⁸
- (225) Further, Moldovan counsel has found no evidence that Gazprom ever made any non-monetary contribution to the share capital of Gazsnabtranzit. Any non-monetary

¹¹² **Appendix No. 4:** Opinion on certain Moldovan law matters, dated 31 May 2023, Section IX, A.

¹¹³ *Ibid.*

¹¹⁴ *Ibid.*

¹¹⁵ But see Section 4.8 above for a 2008 partial revaluation

¹¹⁶ *Ibid.*

¹¹⁷ *Ibid.*

¹¹⁸ *Ibid.*

contributions made by Gazprom should in any event have been appraised by an independent third party. Moldovan counsel has also found no evidence that the gas transportation system was in fact transferred to Gazprom. Moldovan counsel opines that, as the Republic of Moldova was the only party who documented its non-monetary contributions to the share capital of Gazsnabtranzit, and as the Republic of Moldova has not waived its rights to those shares, all shares issued by Gazsnabtranzit at that time, including the shares held by Gazprom, was rightfully owned by the Republic of Moldova.

- (226) Moldovan counsel has also found that certain assets apparently listed and valued by the Transnistrian side as their non-monetary contribution to the share capital of Gazsnabtranzit are actually located in territory under the control of the Republic of Moldova.¹¹⁹ This supports the conclusion that assets properly belonging to the Republic of Moldova were used to pay the debts of the Left bank. Without this irregularity, more of the Debt allegedly accrued by 1994 could have been paid.
- (227) Another irregularity identified by Moldovan counsel is related to the Government Resolution No. 302/1995, which approved the transfer of the ownership of the assets owned by the Republic of Moldova to cover part of the Debt. In 1994, the Parliament provided a Resolution (Parliament Resolution No. 305/1994) which accepted the transfer of "the property complex" of Moldovagaz to Gazprom as Gazprom's contribution to Gazsnabtranzit to cover Moldova's debt. However, the Government Resolution No. 302/1995 approved the transfer of ownership of "the gas transportation system", which was the property of the Republic of Moldova, and hence approving a transaction that fell outside of the scope of the Parliament's decision. This suggests that the transfer of the gas transportation system as non-monetary contribution, was not a legal transaction.
- (228) Furthermore, Moldovan counsel opines that the transfer of the gas transportation system as non-monetary contribution should have complied with specific legislative acts under Moldovan law regulating privatisation of publicly held assets. The transportation complex was owned by the Republic of Moldova, and therefore a publicly held asset and could not be transferred to a private party without complying with a specific legal procedure for privatisation. This supports the argument that the Republic of Moldova's transfer to Gazprom, which in turn was used as Gazprom's non-monetary contribution, was not a transaction in compliance with Moldovan law.
- (229) In addition to this, Moldovan counsel has informed that the two government decisions (Government resolution No. 749/1994 and Government Resolution No. 302/1995) concerning the establishment of Gazsnabtranzit were not published in the Official Monitor in accordance with Moldovan law. Due to the lack of such publication, both Government Resolutions should be deemed invalid.¹²⁰
- (230) With respect to the founding agreement of Gazsnabtranzit, Moldovan counsel has found several contraventions of Moldovan law. Amongst others, Moldovan counsel found that the founding agreement was not authenticated by a notary upon registration, which should lead to the agreement being null and void. In addition, the signees of the founding agreement representing the Republic of Moldova did not have the due authority to do so. The founding agreement also deviated in certain respects from the Government Resolution No. 302/1995, which approved the founding agreement and charter. For example, Moldovan counsel informs that, according to the resolution, the share capital shall be formed from the state property complex (i.e. the going concern) of Moldovatrangaz and Tiraspoltrangaz in the amount of MDL 439,920,000 (the equivalent of USD 104,000,000), while the founding agreement provides that the share capital shall be formed from the value of *fixed assets and*

¹¹⁹ *Ibid*, Section IX, A, 2.3.

¹²⁰ *Ibid*

other property in the same amount.¹²¹ The latter approach was also apparently followed in practice, with the number of fixed assets transferred into Gazsnabtranzit's share capital determined in order to reach the above mentioned figure. In this way, the number of assets transferred was materially increased compared to the assets which would have belonged to a going concern of the equivalent value.¹²² The Auditors note that the alleged Debt accordingly should have been further reduced.

(231) Another irregularity with the founding agreement identified by Moldovan counsel, is the allocation of a preference share for the benefit of Gazprom. According to the founding agreement, the 219 960 ordinary shares also included one preference share. We have been informed that this contradicts Moldovan corporate law, which does not allow for a share to carry more than one vote. Also the charter refers to a similar preference share for the benefit of Gazprom.

(232) In addition to there being several irregularities with the appraisal of the non-monetary contribution the Republic of Moldova made on behalf of Gazprom, Moldovan counsel has also found that there were deviations from Moldovan law with respect to the government resolutions approving the transfer, the founding agreement and charter of Gazsnabtranzit as well as with respect to the actual transfer of the non-monetary contribution to Gazprom.

5.1.3 *Irregularities and illegalities in connection with the establishment of Moldovagaz in 1998/1999*

(233) On 26 February 1998, the Parliament of Moldova passed Decision No. 1556 allowing the establishment of Moldovagaz through the merger of the *concern* Moldovagaz with Gazsnabtranzit (which from 12 November 1997 also was known as "Arogaztranzit").¹²³ Decision No. 1556 further provided that the assets of these entities would be transferred to Gazprom as Gazprom's contribution to the share capital of a new Moldovan-Russian joint stock company in exchange for acquittal of the Moldovan Government's debts for previous gas deliveries by Gazprom.¹²⁴

(234) The Moldovan Government followed up with Decision No. 1068 of 21 October 1998 through which the Moldovan Government agreed with a proposal by the shareholders to reorganise Gazsnabtranzit/Arogaztranzit and Moldovagaz into a new Moldovan-Russian joint stock company. Item 3 of Decision No. 1068 set out a "*preliminary assessment of the of the gas infrastructure assets of the republic [of Moldova]*", but provided in item 3 that the Moldovan Government in 1999 should perform a "*re-valuation of the gas infrastructure assets of the Republic of Moldova in 1999 with the help of an international audit company, according to a mutually agreed methodology, with subsequent possible changes to the share capital, its shares, as well as debts for consumed natural gas*".¹²⁵ We understand, however, that the re-valuation prescribed by Decision No. 1068 did not take place in 1999.

(235) The Founding Agreement / Shareholders' Agreement of Moldovagaz was signed on 23 October 1998 by the Department of Privatisation and Administration of the State Property at the Ministry of Economy and Reforms of Moldova, the so-called Committee for Property Administration of Transnistria and Gazprom. The Constituent Meeting of Moldovagaz was

¹²¹ *Ibid*, section A, 9.2 (iv)

¹²² *Ibid*

¹²³ Decision No. 1556 of 26 February 1998 by the Parliament of Moldova "*On the reorganization and privatization of the gas industry in the Republic of Moldova*", item 1.

¹²⁴ *Ibid*, item 2.

¹²⁵ Decision No. 1068 of 21 October 1998 by the Moldovan Government "*On the reorganization and privatization of the gas complex in Moldova*", item 3.

held on 16 April 1999, and the company was finally registered on 25 May 1999.¹²⁶

- (236) Moldovan Counsel has informed us that the assets which were contributed to the share capital of Moldovagaz by the Moldovan Government were not valued in accordance with the applicable legal framework. Paragraphs 6 Article 41 of the Stock Company Act provided that the "market value of non-monetary contributions shall be approved by decisions of constituent meeting or general meeting of shareholders or board of a company on the basis of published prices of organized market on the date of transfer of these contributions" (our emphasis), while paragraph 7 of Article 41 required that the approval of the value of non-monetary contributions exceeding 10 percent of the authorized capital of the company which is not circulated on the organized market shall be "*made on the basis of conclusion an audit or other specialized organization which is not affiliated to the company*". Neither of these requirements were adhered to when the contributions to Moldovagaz were valued.¹²⁷
- (237) Furthermore, as when Gazsnabtranzit was established in 1995, paragraph 2 of Article 9 of the Foreign Investment Act required assets to be appraised on the basis of "*world market prices*" and the appraisal to be made "*at the time of the conclusion of the memorandum of association of the enterprise*". However, the Minutes from the Constituent Meeting show that the evaluation was carried out "*as of 1 July 1997*", i.e. almost two years prior to the Constituent Meeting. The evaluation was therefore also made in contravention of Article 9 of the Foreign Investment Act.
- (238) Similarly, Moldovan Counsel has opined that the JSC Concern Moldovagaz as well as the 6 joint stock companies seated in the eastern areas of the Republic of Moldova, and the 39 joint stock companies in the territory controlled by the Republic of Moldova and that were ultimately transferred to Gazprom as non-monetary payment for the Debt, should also have been appraised at the going concern value and at global market value. The valuation was therefore made in violation of Moldovan law.
- (239) The founding agreement furthermore had several irregularities. Moldovan Counsel has opined that the signatory of Moldovagaz's constitutional (founding) documents on the part of Gazprom did not have the authority or powers to do so, and that Moldovagaz was not founded in accordance with the legislation of Moldova.¹²⁸ Additionally, the Founding Agreement was dated 23 October 1998, while the Government Resolution No. 1068/1998 which gave the necessary governmental consent, only was published 12 November 1998. Hence, the Founding Agreement was concluded without the valid consent of the Government. Another irregularity in the Founding Agreement, is the allocation of a preference share for the benefit of Gazprom which is contradictory to Moldovan law as described in section 5.1.2 above.
- (240) There were also irregularities as part of the founding meeting, amongst others, Moldovan Counsel has identified that the founding meeting failed to establish and approve the value of the non-monetary contributions. There should also been decisions for each of the 39 joint stock companies and 6 stated enterprises in relation to the merger, however, Moldovan Counsel found that the 45 companies did not consent to their reorganisation.
- (241) It is noteworthy that in the Moldovagaz Charter, Gazprom is named as the monopoly supplier of Moldovagaz.¹²⁹
- (242) As noted in the 2022 Audit Report by the Court of Accounts, the irregularities and illegalities

¹²⁶ Opinion on certain Moldovan law matters, dated 31 May 2023, Section IX, B.

¹²⁷ *Ibid.*

¹²⁸ *Ibid.*

¹²⁹ *Ibid.*

in connection with the establishment of Gazsnabtranzit and Moldovagaz suggest that the Debt which is reflected in the Reconciliation Statements signed by Moldovagaz and Gazprom "*is subject to a significant risk of non-reliability*".¹³⁰ Altogether, the irregularities and illegalities in connection with the establishment of both Gazsnabtranzit and Moldovagaz suggest that the shares were allocated incorrectly and that less of the Debt was written off than what would have been the case if the legislation had been complied with.

- (243) Moldovan Counsel has further informed that Gazsnabtranzit's liabilities were higher than its assets at the moment of the merger into Moldovagaz in 1999. Gazprom's contribution to the share capital of Moldovagaz was, according to the Founding Agreement, Gazprom's "property" in Gazsnabtranzit with a value of 391,377,736 MDL (equivalent of 85,313,948 USD). However, according to Moldovan Counsel, Gazprom held only shares, and no assets in Gazsnabtranzit. Moldovan Counsel did not identify any evidence indicating that Gazsnabtranzit transferred any asset to Gazprom. Seeing that Gazsnabtranzit's liabilities exceeded its assets at the time, the value of Gazprom's contribution to the share capital was overvalued, and in the opinion of Moldovan Counsel should either lead to the equity share being reduced or the Debt being reduced. Also, an alleged Debt of USD 47,300,000 was incorrectly not set off against Gazsnabtranzit's equity when Gazsnabtranzit was merged into Moldovagaz. Furthermore, assets located on the Right bank were apparently transferred as payment for Left bank debts.
- (244) Moldovan Counsel has concluded that the unlawful appraisal of the assets of the Republic of Moldova as well as the other irregularities identified in connection with the establishment of Moldovagaz, should lead to the formation and registration of the Moldovagaz being null and void. Similarly, with reference to the appraisal of the Debt having been carried out in violation of Moldovan law, Moldovan Counsel has concluded that an excessive amount of assets were illegally transferred to Gazprom as a payment for the Debt.

5.2 Irregularities and illegalities in connection with debt payments with obligations issued by the Moldovan Government in 1997 and 2000

- (245) In 1996 and 2000, Moldova entered into agreements with Gazprom on the settlement of debts for deliveries of Russian gas in 1994-1996 and in 1996, respectively. In accordance with these agreements, Moldova issued foreign loan obligations to pay off said parts of the Debt.¹³¹ However, there have been indications in the public domain that the obligations were used by Gazprom to pay off Left bank debts, even though a precondition for the issuance of the obligations from the Moldovan side was that they were used to pay off Right bank debts for the abovementioned periods.¹³² There have also been indications that parts of the Debt for which the 1996 obligations were issued (debts for deliveries in 1994-1995) had already been paid for through barter.¹³³ Moldovan counsel observes that the Republic of Moldova and Gazprom have concluded, in 1996 and 2000 respectively, debt settlement agreements

¹³⁰ 2022 Audit Report by the Court of Accounts of Moldova, Section 4.1.8.

¹³¹ Agreement between the Government of the Republic of Moldova and Gazprom on the principles for the settlement of the debts of the of the Republic of Moldova for deliveries of Russian natural gas in 1994-1996 and Agreement between the Republic of Moldova and Gazprom "*On the settlement of the debts of the Republic of Moldova for deliveries of Russian natural gas in 1996*".

¹³² "*Moldova vs Gazprom: who actually has debts?*", Section 3.4 by Sergiu Tofilat and Tudor Soitu of WatchDog.md Community (<https://www.watchdog.md/2020/10/28/moldovagaz-vs-gazprom-who-actually-has-debts/> accessed on 6 February 2023). See also **Appendix No. 4**, Opinion on Certain Moldovan Law Matters dated 31 May 2023, Section C.2

¹³³ "*Moldova vs Gazprom: who actually has debts?*", Section 3.4 by Sergiu Tofilat and Tudor Soitu of WatchDog.md Community (<https://www.watchdog.md/2020/10/28/moldovagaz-vs-gazprom-who-actually-has-debts/> accessed on 6 February 2023).

which overlap in respect of the year 1996.¹³⁴ Despite our requests to Moldovagaz and Gazprom, the Auditors have not been provided with verification acts from Gazprom which would allow us to assess whether the obligations were used as intended, nor have the Auditors been able to assess whether and to what extent parts of the Debt were paid off by barter during 1997.¹³⁵ The Auditors have therefore not been able to verify these claims.

5.3 Verification of legality of Gazprom's assignment(s) of claims to Faktoring-Finans

- (246) We have been asked to assess the legality of Gazprom's assignment of claims to its subsidiary Faktoring-Finans. According to the documents we have received, Gazprom assigned USD 275,914,205 of the Debt to Faktoring-Finans in December 2005.¹³⁶ The assignment consisted of a part of the Debt accrued in the period 1996 to 2003 under contracts Nos. 1GM-97, 1GM-98, 1GM-99, 2GM-99, 1GM-2000, 1GM-2002, 1GM-03 and 1GM-04. As all the contracts under which the Debt accrued are governed by Russian law, we have relied on the advice of Russian Counsel for this exercise.¹³⁷
- (247) Contract No. 2GM-99 (1999) provides in Article 8.6 that "*neither Party may transfer his rights or obligations to a third party not designated by this Contract without a written notification to the other Party*". Similar provisions are found in Article 9.6 of Contract No. 1GM-2001, Article 9.6 of Contract No. 1GM-2000, Article 9.6 of No. 1GM-2002 and Article 9.6 of Contract No. 1GM-04. As we have not been provided with the contracts preceding 1999 (contracts No. 1GM-97, No. 1GM-98 and No. 1GM-99), the assumption in the following is that the contractual regulation of assignment of claims was similar or identical in the contracts preceding 1999 (i.e. not imposing any more extensive requirements for assigning claims than notification to the debtor).
- (248) Based on the available contracts, we understand that the assignment did not contradict the contracts' provisions, as Moldovagaz received written notification of the assignment on 1 December 2005.¹³⁸ That Moldovagaz only was notified of the assignment the day after the assignment agreement had been signed is unlikely to affect the validity of the assignment as such.¹³⁹ Moreover, there are no indications that the assignment violated mandatory provisions of Russian law that were in force at the time of the assignment.¹⁴⁰
- (249) Under the assumption that the contracts for the period 1996 to 1999 did not impose any other requirements for the assignment of claims, our conclusion is that there do not appear to exist any clear grounds to assert that the assignment is invalid based on violation of mandatory provisions of Russian law.¹⁴¹

¹³⁴ **Appendix No. 4**, Opinion on Certain Moldovan Law Matters dated 31 May 2023, Section C.2

¹³⁵ **Appendix No. 3**: Fifth Request for Documents to Moldovagaz.

¹³⁶ See Cession Agreement No. 8FF-2005, dated 1 December 2005, Notification of Assignment of Claim, dated 2 December 2005 and Reconciliation Statement between Faktoring-Finans and Moldovagaz, dated 15 November 2006.

¹³⁷ **Appendix No. 5**: Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.6.

¹³⁸ *Ibid.*, Section 2.4.4.

¹³⁹ *Ibid.*, Section 2.6.6.

¹⁴⁰ *Ibid.*, Section 2.6.5.

¹⁴¹ **Appendix No. 5**: Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.6.5

5.4 Legality and/or conformity with practice of penalty interest rates charged by Gazprom

5.4.1 Legality of penalty interest rates charged by Gazprom

- (250) We have been asked to assess the legality of the penalty interest rates charged by Gazprom under its gas delivery contracts with Moldovagaz and Moldovagaz's predecessors.¹⁴² As all the available contracts under which the Debt accrued are governed by Russian law, we have relied on the advice of Russian counsel for this exercise.¹⁴³ There are indications that large parts of the Debt which accrued in the period from 1991 to 1999 consisted of penalties. For example, information referred to in the 2022 Audit Report by the Court of Accounts of the Moldova indicate that Gazsnabtranzit accrued penalties in the amount of about USD 100 million for gas delivered in 1994 and 1995, while the debt for gas delivered in 1994 amounted to approximately USD 190 million, implying that the penalties constituted a very large share of the overall debt.¹⁴⁴
- (251) As Moldovagaz, which was established in 1999, does not possess any relevant documentation from the period prior to 1999, as such documentation have not been found in the archives of the Moldovan Government, and as Gazprom has not provided the requested documentation, we have not been able to review any of the contracts from the period prior to 1 July 1999.¹⁴⁵ We have, however, seen an excerpt from what appears to be the penalty clause of Contract No. 1-Gaz between the State Department for Gasification of Moldova and Gazprom for gas deliveries in the period 1993 to 1994.¹⁴⁶ According to Article 9 of Contract No. 1-Gaz, Gazprom was entitled to charge a penalty in the size of 0.35% for each day of late payment without any maximum limitation (corresponding to an annual delay interest rate of almost 128%).
- (252) Having in mind that penalties apparently constituted a large part of the Debt that accrued in the period from 1991 to 1999, cf. above, there is reason to believe that a similar penalty rate without any maximum limitation was charged under the other gas delivery contracts between Moldovagaz's predecessors and Gazprom.¹⁴⁷ An assumption in the following is thus that Gazprom charged a penalty rate of 0.35% or similar without any maximum limitation for the entire period from 1991 to the second half of 1999.
- (253) For the period from the second half of 1999 to 31 October 2021, we have been provided with all the gas sales contracts between Moldovagaz and Gazprom and have reviewed the relevant penalty clauses.
- (254) Under the contracts entered into in the period from 1999 until the end of 2006, Gazprom was entitled to charge penalties in the amount of 0.01 to 0.03% for each day of late payment

¹⁴² **Appendix No. 1:** Tender Book, Section 1.2.

¹⁴³ **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.4.

¹⁴⁴ 2022 Audit Report by the Court of Accounts of Moldova, dated 21 November 2022, page 141 (Russian version, retrieved from https://www.ccrm.md/ru/decision_details/1202/hotararea-nr56-din-21-noiembrie-2022-cu-privire-la-raportul on 6 February 2023).

¹⁴⁵ The earliest contract we have been provided with, Contract No. 2GM-99, covers gas deliveries from Gazprom to Moldovagaz in the period from 1 July 1999 to 31 December 1999.

¹⁴⁶ Article 9 of Contract No. 1-Gaz of 9 December 1993, annexed to the report "*Moldova vs Gazprom: who actually has debts?*" by Sergiu Tofilat and Tudor Soitu of WatchDog.md Community (<https://www.watchdog.md/2020/10/28/moldovagaz-vs-gazprom-who-actually-has-debts/>), accessed on 6 February 2023).

¹⁴⁷ See for instance Notification of Assignment of Claim from Gazprom to Faktoring-Finans, dated 2 December 2005, which shows that the penalty amount of the yearly debt was reduced from USD 64 million in 1998/1999 (under Contract No. 1GM-99) to USD 16,69 million in 1999 (under Contract No. 2GM-99).

(corresponding to annual interest rates of 3.65 and 10.95% respectively).¹⁴⁸ Moreover, some of the contracts also provided for large fines for non-payment after a certain period of time *in addition* to accumulating penalties for late payment (e.g. one of the contracts provided that Moldovagaz must pay a fine in the amount of 200% of the unpaid sum for each monthly gas delivery not paid for within 90 days of delivery).¹⁴⁹

- (255) Under the contracts entered into in the period from 2007 to 2021, the late payment penalty has been fixed at 0.01% of the sum of the delayed payments for every day of late payment from the 21th of the month following the reporting month, but with a maximum limitation of 5% of the unpaid sum.¹⁵⁰
- (256) Russian Counsel has informed us that while the time period of the above contracts covers several revisions of the legal norms governing the penalty issue, Russian law has always set forth a general principle of full compensation of penalties agreed by the parties. The only requirement provided by Russian law was that the agreement on penalties should be made in written form.¹⁵¹ However, we have been informed that both Soviet and later Russian courts were allowed to decrease unreasonable penalties. For example, the Soviet Civil Code of 1964 (the "**1964 CC**"), which remained in force in the Russian Federation until 1994, provided that a court could decrease a penalty in case the amount was excessively high in comparison with the creditor's loss, and that it in doing so was expected to take into account the progress of debtor's performance, debtor's financial state and creditor's interests.¹⁵² There have been several rulings in which courts and tribunals have applied the said provision under the 1964 CC and reduced awarded penalties, *inter alia* by reference to a disproportionately high amount of penalties compared to the other party's loss.¹⁵³
- (257) However, in 2015, these rules were supplemented by a provision according to which the decrease of contractually agreed penalties in commercial contracts only was allowed under exceptional circumstances if it is proven that the payment of contractual penalties would result in unjustified profit for the creditor, and that the courts only were allowed to decrease penalties under commercial contracts at the debtor's request.¹⁵⁴
- (258) The consideration of whether accrued penalties should be reduced will depend on the factual circumstances of the particular case. Russian Counsel has explained that, pursuant to Russian court practice formed under the Russian Civil Code, penalties could be deemed unjustified if, for example, (i) the contracts provides for an excessively high penalty rate in comparison with the average interest rate on loans and/or inflation rate at the location of the creditor; (ii) in case the amount of penalties is disproportionately high compared to the amount of debt; (iii) in case the penalty amount would significantly exceed potential losses caused by the breach; and (iv) in case of a breach which is limited in time.¹⁵⁵
- (259) Thus, against the above background, Moldovagaz may argue that the penalties accrued in the period 1991 to 2007 should be written off in part or in full. In particular, it may be possible to argue that the penalties were disproportionate to the losses suffered by Gazprom. For the

¹⁴⁸ Contracts Nos. 2GM-99, 1GM-2000, 1GM-2001, 1GM-2002, 1GM-03, 1GM-04, 1GM-05, 1GM-06, 3GM-06 and 5GM-06.

¹⁴⁹ Contracts Nos. 1GM-2002, 1GM-03 and 1GM-04.

¹⁵⁰ Contract No. 1GM-07-11 with Additional Agreements Nos. 1 to 5 and Addenda Nos. 1 to 19.

¹⁵¹ **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.4.4.

¹⁵² *Ibid.*, Section 2.4.6.

¹⁵³ *Ibid.*, Section 2.4.6.

¹⁵⁴ *Ibid.*, Section 2.4.7.

¹⁵⁵ **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.4.8.

period 1994 to 2007, Moldovagaz may additionally explore whether there is room to argue that the penalty/fine amounts are disproportionately high compared to (i) the average loan interest rates available to Gazprom at the relevant periods of time, and (ii) the overall amount of the debt (e.g. due to excessive fines in the amount of 200% of the unpaid sum).

- (260) With respect to the daily penalty interest rates, this argument will presumably be stronger for the earlier period (i.e. from 1991 to the second half of 1999, assuming a penalty interest rate of 0.35% for each day of late payment), than for the period from the second half of 1999 to 2007.
- (261) However, to the extent Gazprom has imposed the abovementioned fines (e.g. fines in the amount of 200% of the unpaid sum), this argument may be viable also for the period from the second half of 1999 to 2007. See, however, below for a potential justification for such fines.
- (262) An argument which could be made is that Gazprom arguably received compensation for all or parts of the loss suffered by Gazprom due to Gazsnabtranzit and Moldovagaz's failure to pay for gas deliveries through the debt-assets swaps in 1995 and 1999, as the assets transferred to Gazprom were not valued at their fair market value.¹⁵⁶ In this context, it might also be possible to argue that any ancillary claims (i.e. penalties) owed by the Moldovan Government to Gazprom were settled through the establishment of Gazsnabtranzit in 1995 and Moldovagaz in 1999.¹⁵⁷ However, the information referred to in the 2022 Audit Report suggests that penalties for gas deliveries in 1994 and 1995 were not included in the settlement when Gazsnabtranzit was established in 1995.¹⁵⁸ Penalties that had accrued prior to 1999 might also have been carried on following the establishment of Moldovagaz. Thus, unless the relevant agreements between Moldovagaz and Gazprom provide otherwise, it might be possible to argue that Moldovagaz has been released from these penalties (which, if they were continued, were assigned to Faktoring-Finans in 2005).¹⁵⁹

Conformity with custom and practice of penalty interest rates charged by Gazprom

- (263) Based on the Auditors' experience from gas disputes in the European market, penalty clauses in gas sale contracts often provide for penalty interest rates in the range from 0.01 to 0.03¹⁶⁰ percent for each day of delay in payment. Also in the Auditors' experience, another common mechanism in gas sales contracts is to base the penalty interest rate on a published rate, for example LIBOR (or similar), and to possibly add 2-3 percentage points per annum. Based on a comprehensive review of gas sales contracts between Norwegian suppliers and European buyers, the Norwegian gas contracts expert Are Brautaset concludes that the penalty interest rate "*normally is based on a well-known, published rate, for example the three month LIBOR for the relevant currency for the settlement*" and that "[a]n additional 2-3 percentage points are then added to this interest rate".¹⁶¹

¹⁵⁶ *Ibid.*, Section 2.4.10.

¹⁵⁷ **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.4.11.

¹⁵⁸ 2022 Audit Report by the Court of Accounts of Moldova, dated 21 November 2022, page 141 (Russian version, retrieved from https://www.ccrm.md/ru/decision_details/1202/hotararea-nr56-din-21-noiembrie-2022-cu-privire-la-raportul on 6 February 2023).

¹⁵⁹ **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.4.11.

¹⁶⁰ A publicly available example is the 0.03 per cent daily delay interest in the 19 January 2009 gas sales agreement between Gazprom and PJSC NJSC Naftogaz of Ukraine, which was published by Ukrainian newspaper "*Ukrainska Pravda*" shortly after its conclusion (available at <https://www.pravda.com.ua/articles/2009/01/22/3686613/>, accessed on 6 February 2023).

¹⁶¹ Brautaset et al. (1998), *Norsk Gassavsetning: Rettslige hovedelementer*, page 269.

- (264) Thus, while the penalty interest rates charged from the second half of 1999 and up until today appear to have been broadly in conformity with European custom and practice, the early penalty interest rates of 0.35% for each day of delay in payment seem excessive and do not conform with European custom and practice. This further suggests that the penalties which accrued in the period 1991 to the second half of 1999 may be challenged legally.
- (265) The Auditors have not seen clauses providing for excessive fines in the amount of 200% of the unpaid sum in other contracts. However, the 200% fines may have a plausible explanation, as the Russian Customs Code in force during 1995 to 2002 made Gazprom liable for a fine in the amount of 100 to 200% of the value of the goods (i.e. the gas) if it failed to repatriate currency earnings (i.e. to credit purchase price for the delivered gas into its bank account in Russia).¹⁶² However, Russian counsel considers that such an argument would have to be supported by evidence that Gazprom was indeed fined as a result of Moldovagaz's failure to pay for gas deliveries.¹⁶³ We have seen no such evidence.
- (266) A Mutual Reconciliation Statement of 31 December 2021, signed by Moldovagaz and Faktoring-Finans,¹⁶⁴ shows that approximately MUSD 133 accrued in penalties only from 1994 to 1 July 1999, which suggests that an excessive penalty interest rate of 0.35% or similar was used. Applying a more reasonable and customary interest rate of 0.03% per day, the above penalties would be reduced to approximately USD 11,4 million¹⁶⁵, suggesting that Gazprom charged excessive penalties amounting to more than USD 120 million. This provides a further potential reason for Moldovagaz to require the part of the Debt incurred before 1 January 2003 to be written off.

5.5 Legality and conformity with international practice of distribution of transit tariff payments between Moldovagaz and the de-facto operator of the Moldovan gas transmission system situated on the left bank of the Nistru River

5.5.1 Introduction

- (267) We have been asked to opine on the legality and conformity with international practice of the distribution of Gazprom's transit tariff payments between Moldovagaz and the de-facto operator of the parts of the Moldovan gas transmission system on the left bank of the Nistru River.
- (268) We have been informed that Tiraspoltransgaz-Pridnestrovie de facto operates the portion of the Moldovan gas transmission system situated on the Left bank of the Nistru River, and that it does so based on an arrangement with Tiraspoltransgaz, a de jure subsidiary of Moldovagaz.¹⁶⁶ Tiraspoltransgaz does *de facto* not act as a subsidiary of Moldovagaz, but as some kind of middleman between Gazprom and Tiraspoltransgaz-Pridnestrovie.¹⁶⁷ Formally, the operator of the Moldovan gas transmission system on the left bank of the Nistru River (Pridnestrovie/Transnistria) is Tiraspoltransgaz,¹⁶⁸ but Tiraspoltransgaz has no operations and only one employee.¹⁶⁹ Moldovagaz has contractual arrangements with Tiraspoltransgaz for the provision of transit services on the left bank of the Nistru River, which replicate the

¹⁶² **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.4.14.

¹⁶³ *Ibid.*, Section 2.4.14.

¹⁶⁴ Mutual Reconciliation Act between Moldovagaz and Faktoring-Finans, dated 31 December 2021.

¹⁶⁵ $0.03/0.35 \times 133,000,000$.

¹⁶⁶ Interview with Moldovagaz management, Chisinau, 18 October 2022.

¹⁶⁷ *Ibid.*

¹⁶⁸ Moldovagaz's webpages, "O Kompanii" ("About the Company"), accessed at <https://www.moldovagaz.md/rus/o-kompanii> on 3 January 2023.

¹⁶⁹ Interview with Moldovagaz management, Chisinau, 18 October 2022.

distribution of transit tariff payments in Moldovagaz's transit contract with Gazprom.¹⁷⁰

- (269) We also understand that since 2007, Gazprom has paid the de-facto operator of the Moldovan gas transmission system on the left bank of the Nistru for transportation services in kind, i.e. with natural gas deliveries.¹⁷¹ In 2007, Gazprom paid Moldovagaz in cash for transportation services on the left bank, which Moldovagaz then used to pay for Gazprom gas deliveries to the left-bank de-facto operator.¹⁷² However, after 2007, this arrangement was abandoned and Gazprom continued to deliver gas in kind to the left bank de-facto operator.
- (270) Our assumption is that the Moldovan gas transmission system is a single system, even if different parts of the system are operated by different operators.
- (271) A first question is whether Gazprom's distribution of transit tariff payments between Moldovagaz and Tiraspoltransgaz-Pridnestrovie is in line with Transit Contract No. 2GM-11 (the "**Transit Contract**"), which was originally entered into for the period 2011-2012, later extended through yearly addenda up until 30 September 2021.¹⁷³
- (272) A second question is whether the distribution of transit payments, as regulated in the Transit Contract, is in line with international practice.
- (273) In Sections 5.5.2 to 5.5.4 below, we analyse the relevant provisions of the Transit Contract. In Section 5.5.5, we compare the cost distribution in the Transit Contract and the allocation of payments with international practice. Our conclusions are then set out in Section 5.5.6.

5.5.2 Article 3 of the Transit Contract

- (274) Article 3 of the Transit Contract reads as follows (in English translation):

3.1. The tariff rate for the transport of 1000 (one thousand) cubic metres of gas in transit mode, transported from the Moldovan-Ukrainian border to the Moldovan-Ukrainian border through the territory of the Republic of Moldova to other countries, pursuant to the terms and conditions of the Contract, is fixed at the rate of USD 3 per 100 (one hundred) kilometres.

[... the tariff rate includes taxes, VAT and other payments due under Moldovan legislation]

3.2. The cost of the services for the transit of gas transported through the territory of the Republic of Moldova is determined based on the tariff on transit transport, the volumes of gas transported along the direction of the gas pipelines and the distance of the transit.

At the same time, the cost of the services for the transport of gas in the service area of Tiraspoltransgaz Ltd and in the service area of Moldovatrangaz Ltd, is determined in the following way:

¹⁷⁰ *Inter alia* Contract No. 2MT-08 ("on the terms for transportation of natural gas on the territory of the Republic of Moldova in 2008").

¹⁷¹ Interview with Moldovagaz management, videocall, 23 February 2023.

¹⁷² Section 4.4.2 above.

¹⁷³ Addendum No. 20 to Contract No. 2GM-11 expired on 30 September 2021. Transit Contract No. 2GM-22 was entered into on 18 February 2022 for the period 1 January 2022 to 31 March 2022.

- as equal shares (50%) of the cost of the services, calculated for the whole gas transit distance through the territory of the Republic of Moldova, as carried out in accordance with Clause 1.1 of Article 1 [transit in the direction of Orlovka, with further transit through Ukraine towards Romania, a major transit direction towards the eastern Balkans and Turkey prior to the commissioning of Turkstream and the reversal of the flow in the Trans-Balkan Pipeline from North-South to South-North in 2020¹⁷⁴];

- as shares of the cost of the services, proportional to the length of the gas pipelines in the service area of Tiraspoltransgaz Ltd and Moldovatrangaz Ltd, calculated for the whole transit distance through the territory of the Republic of Moldova, as carried out in accordance with Clause 1.2 of Article 1 [transit in the direction of Alekseevka / Oleksiivka, with further transit through Ukraine towards western Romania at Tekovo/Mediesu Aurit. Hungary, Slovakia and Poland, a direction which very rarely, if ever, has been used for transit¹⁷⁵].

- (275) To our knowledge, the provision on cost distribution between Moldovatrangaz and Tiraspoltransgaz has been included in all transit contracts back to 2007. Prior to 2007, the transit contracts do not seem to have regulated the issue of cost distribution between the entities.

5.5.3 Article 5 of the Transit Contract

- (276) Article 5, which regulates the payment procedure, reads as follows (in English translation):

5.1. Payment for the cost of services for the transportation of gas rendered by Moldovagaz through the territory of the Republic of Moldova to other countries shall be paid on a monthly basis by Gazprom with monetary funds in the sum of the cost of the rendered services for the relevant month, minus the cost of the gas supplied by Gazprom to Moldovagaz pursuant to Clause 1.9 of Article 1 and subject to Clauses 4.1, 4.2 and 4.3 [price provisions] of Article 4 of this Contract.

5.2. Gazprom shall carry out payment for the gas transportation services rendered by Moldovagaz to the payment account of Moldovagaz in a monetary form in the size of up to 50% of the cost of the services rendered in the reporting month within the 20th of the month in which the services are rendered, on the basis of Moldovagaz's bill.

5.3. The Parties shall carry out a final settlement of their obligations no later than the 20th of the month following the reporting month, on the basis of the act of delivery and acceptance of services for the transportation of gas services through the territory of the Republic of Moldova to other countries (Clause 2.8 of Article 2.8) and invoices drawn up in accordance with the acts of delivery and acceptance of services for the transportation of gas services through the territory of the Republic of Moldova to other countries, and commercial acts for the delivery and acceptance of gas (Clause 2.9 of

¹⁷⁴ See for example the 1 January 2005 Technical Agreement between Gazprom, Naftogaz and Moldovagaz for natural gas deliveries to consumers in Moldova and Ukraine and transit through their territories in 2005, item 2.1.

¹⁷⁵ *Ibid.*, specifying 21 bcm of transit to Bulgaria, Turkey and Romania through Orlovka, but only deliveries to Moldovan consumers through Alekseevka.

Article 2.), taking into account payments that have been made (Clause 5.2 of Article 5).

5.4. The cost of the services for the transportation of gas through the territory of the Republic of Moldova to other countries and the cost of the gas supplied by Gazprom to Moldovagaz in accordance with Clause 1.9 of Article 1, shall be calculated in US dollars. Payments for the cost of the services rendered in accordance with Clause 5.1 of Article 5 of the Contract shall be made in US dollars and/or Russian roubles, in accordance with the exchange rate established by the Central Bank of the Russian Federation on the date when the funds are written off Gazprom's account.

5.5. Gazprom's obligation to pay the cost of the services rendered by Moldovagaz in a monetary form shall be considered executed on the date when the monetary funds have been credited to Moldovagaz's account.

Any excess payment transferred by Gazprom shall be counted as payment for the next month.

All expenses related to making payments under this Contract incurred on the territory of the Russian Federation shall be borne by Gazprom, and on the territory of the Republic of Moldova – by Moldovagaz.

5.6. In case the payment terms provided by Clause 5.3 of Article 5 of this Contract are breached, Moldovagaz reserves its right to present Gazprom with a claim for payment of penalties in the amount of 0,01% of the sum of the delayed payment for every day of the delay, beginning from the 21th of the month following the reporting month, but no more than 5% of the untimely paid sum. The payment of penalties is made in US dollars by separate payment no later than the last day of the month following the reporting quarter.

5.7. No later than the 25th of the month following the reporting quarter, Gazprom and Moldovagaz shall carry out a reconciliation of payments under this Contract and shall issue reconciliation acts, subject to accrued fines and penalties for untimely payment.

5.5.4 The cost distribution and payment procedure in the Transit Contract

- (277) Article 3.2 regulates the distribution of transit costs between the service areas of Moldovagaz's gas transportation subsidiaries, Moldovatransgaz and Tiraspoltransgaz.
- (278) Article 3.2 first paragraph establishes that as a main rule, the transit costs shall be calculated on the basis of the transit tariff, the gas volumes transported along the direction of the gas pipelines and the transit distance. Thus, the cost of services is volume and distance based.
- (279) Article 3.2 second paragraph establishes the cost allocation between the service area of Moldovatransgaz and the service area of Tiraspoltransgaz. The Transit Contract does not define the respective service areas, but, as indicated above, Tiraspoltransgaz's service area coincides with the region of Transnistria. The transit costs are calculated in accordance with the principle in Article 3.2 first paragraph, but the model for distribution between Moldovatransgaz and Tiraspoltransgaz differs depending on whether the transit is in the direction of Orlovka or in the direction of Alekseevka/Oleksiivka.
- (280) The cost of the transit through Moldova to Alekseevka/Oleksiivka is allocated proportionally between Moldovatransgaz and Tiraspoltransgaz based on the length of the gas pipelines in

their respective service areas.

- (281) However, the cost of the transit through Moldova to Orlovka is split 50-50 between Moldovatransgaz and Tiraspoltransgaz, irrespective of the distance travelled by the gas/the length of the gas pipelines in their respective service areas. While the entry point on this direction, Grebenyky, is located within the Transnistria region, the majority of the gas pipeline infrastructure from Grebenyky to Orlovka is located outside Transnistria; the total length of the three transmission networks in the South of Moldova is 343 km, of which 247 km are managed by Moldovatransgaz, and respectively 96 km by Tiraspoltransgaz.¹⁷⁶ We are not familiar with the background for the inclusion of this cost allocation provision or for why different cost distribution models are applied to the Alekseevka/Oleksiiivka route and the Orlovka route. Based on the information available to us, it is difficult to understand how the 50-50 split reflects the cost related to the infrastructure operated by Moldovatransgaz and Tiraspoltransgaz respectively. Based on the length of the transmission networks in the South of Moldova managed by Moldovatransgaz and Tiraspoltransgaz respectively, and the cost allocation principle for the Alekseevka/Oleksiiivka direction, a split of 72/28% appears more reasonable.
- (282) Notably, Article 3.2 does not regulate Gazprom's payment of the transit services. The payment procedure is regulated in Article 5 of the Transit Contract.
- (283) Pursuant to Article 5, Gazprom's payment obligation is towards Moldovagaz for the transit services through the territory of Moldova. Legally and formally the territory of Moldova includes Transnistria. Payments shall be made with monetary funds.
- (284) The cost distribution between Moldovatransgaz and Tiraspoltransgaz regulated in Article 3.2 second paragraph is irrelevant to Gazprom's payment obligation under Article 5. This cost distribution regulates the internal distribution between Moldovagaz's subsidiaries. Gazprom's payment obligation towards Moldovagaz applies irrespective of whether the transportation service is carried out by Moldovatransgaz or Tiraspoltransgaz (or its apparent sub-contractor Tiraspoltransgaz-Pridnestrovie). Furthermore, Tiraspoltransgaz-Pridnestrovie is a totally separate entity which is not a party to, nor regulated in, the Transit Contract. Consequently, Gazprom's practice of paying transit fees to Moldovagaz/Tiraspoltransgaz-Pridnestrovie in kind is contrary to the Transit Contract.

5.5.5 *Inter TSO compensation mechanisms in international practice*

5.5.5.1 Inter TSO compensation mechanisms in EU law and European practice

- (285) We have been asked to assess the legality and the conformity of the payment distribution between Moldovagaz and Tiraspoltransgaz-Pridnestrovie with international practice. As mentioned in Section 5.5.1 above, we assume that Gazprom's allocation of payments between Moldovagaz and Tiraspoltransgaz-Pridnestrovie is in line with the cost distribution between Moldovatransgaz and Tiraspoltransgaz in Article 3.2 of the Transit Contract. Given that Moldova is a Contracting Party to the Energy Community and has made significant progress in implementing the EU gas acquis, we consider EU law and European practice as the relevant comparator for the cost distribution in Article 3.2 of the Transit Contract for the purposes of this report.
- (286) As mentioned in Section 5.5.4 above, Article 3.2 of the Transit Contract establishes the cost allocation between Moldovatransgaz and Tiraspoltransgaz, which operates different parts of the gas pipeline system. As such, Article 3.2 of the Transit Contract has the character of a

¹⁷⁶ Security of Supply Statement, Ministry of Infrastructure and Regional Development of the Republic of Moldova for the period 2020-2021, paragraph 72 (<https://www.energy-community.org/documents/parties/SoS.html>), accessed on 30 January 2023).

so-called inter TSO compensation mechanism ("**ITC Mechanism**"), the purpose of which is to establish a basis for fair compensation to TSOs for the costs of making infrastructure available to host cross-system gas flows. Such ITC Mechanism is both allowed and required under EU law. More specifically, Commission Regulation (EU) 2017/460 of 16 March 2017 establishing a network code on harmonised transmission tariff structures for gas (the "**Network Code on Tariffs**"/the "**TAR NC**") provides guidelines on ITC Mechanisms. The TAR NC has been included in the gas acquis of the Energy Community Treaty ("**EnCT**"), which Moldova, as a Contracting Party to the EnCT, has undertaken to implement.¹⁷⁷

- (287) It is clear that the cost distribution in Article 3.2 of the Transit Contract was adopted prior to the adoption of the TAR NC. However, the TAR NC provides guidance on multi-TSO arrangements in an entry-exit system, the purpose of inter-TSO compensation mechanisms and how they are envisaged to function in practice.
- (288) In this context, we note that Moldova has recently introduced an entry-exit system and adopted entry-exit tariffs in accordance with the EnCT gas acquis. According to the Energy Community Secretariat's Implementation report for 2022,¹⁷⁸ Moldova has made significant progress in implementing the gas acquis. However, the Energy Community Secretariat observes that while the legislative amendments are an important step, they are not sufficient in themselves and that Moldovan authorities need to ensure the adoption and implementation of secondary legislation. According to the country specific report,¹⁷⁹ entry-exit tariffs for the transmission system were approved in March 2022, but the implementation of the Network Codes is described as "*still in the nascent phase*". Harmonized transmission tariff structures for gas are not in place, even if the legal basis for such harmonisation has been established.¹⁸⁰ For the purpose of this memo, we have therefore applied the TAR NC directly.

5.5.5.2 TAR NC and ITC Mechanisms

- (289) TAR NC distinguishes between multi-TSO entry-exit systems within a Member State, cf. Article 10, and multi-TSO entry-exit systems covering more than one Member State, cf. Article 11.¹⁸¹ Both Article 10 and 11 TAR NC sets out the principles for which reference price methodology to apply in multi-TSO entry-exit systems. Both Article 10 and 11 provides for three options, i.e. 1) so-called 'same jointly', where the TSOs jointly apply the same reference price methodology, 2) so-called 'same separately', where the TSOs apply the same reference price methodology, but separately ('same separately'), and 3) so-called 'different separately', where the TSOs apply different price reference methodologies separately.
- (290) For multi-TSO entry-exit systems covering more Member States, Article 11 does not foresee any defaults, exceptions or specific conditions. However, when it comes to multi-TSO entry-

¹⁷⁷ See the Energy Community acquis (<https://www.energy-community.org/legal/acquis.html>, accessed on 6 February 2023). The transposition deadline for TAR NC was 27 August 2019 and the implementation deadline was 27 February 2020, with the deadline for implementing Chapters II, II and IV of TAR NC being 30 May 2021.

¹⁷⁸ The Energy Community Secretariat's Implementation Report 2022 (<https://www.energy-community.org/implementation/IR2022.html>, accessed on 6 February 2023).

¹⁷⁹ Energy Community, "*Moldova: Annual Implementation Report*", dated 1 November 2022 (<https://www.energy-community.org/implementation/Moldova.html>, accessed on 6 February 2023).

¹⁸⁰ *Ibid.*

¹⁸¹ We note that except for replacing the term Member State in Article 10(1) and clarifying that Article 11 apply to entry-exit systems covering more than one Contracting Party or covering Contracting Party(-ies) and Member State(s), Article 10 and 11 TAR NC has been transposed unaltered into the EnCT gas *acquis*.

exit systems within a Member State, Article 10(1), cf. Article 6(3), TAR NC, establishes that, as a default rule, the same reference price methodology shall be applied jointly by the involved TSOs to all entry and exit points in the system. However, pursuant to Article 10(2) TAR NC, the other two options ('same separately' and 'different separately') are available as exceptions subject to certain conditions. Irrespective of which option is applied, Article 10(3) specifically requires that an ITC Mechanism is established to ensure the proper application of the reference price methodology.

- (291) In the case of Moldova, and taking into account that Transnistria is legally and formally Moldovan territory, we consider Article 10 TAR NC as the relevant legal basis for assessing the legality and conformity of Gazprom's practice of distributing its payment for transit of gas between Moldovagaz and Tiraspoltransgaz-Pridnestrovie.
- (292) Notably, Article 10(3) TAR NC only provides general principles for the establishment of the ITC Mechanism, and does not establish any specific requirements to follow. Where the exceptions pursuant to Article 10(2) are applied, Article 10(3) specifies that the ITC mechanism shall prevent detrimental effects on the transmission service revenue of the TSOs involved and to avoid cross-subsidisation between intra-system and cross-system network use.
- (293) Pursuant to TAR NC, the establishment of an ITC Mechanism follows a specific procedure. The principles of the ITC Mechanism and its impact of the tariff level are subject to consultation and approval of the national regulatory authorities, and must be carried out simultaneously with the final consultation under Article 26 TAR NC and the consultation on multipliers, seasonal factors and discounts under Article 27 TAR NC.
- (294) Furthermore, the ITC Mechanism is built on the precondition that the TSOs collect the tariffs for the transportation service, and that one TSO transfers the compensation to the other TSO in accordance with the agreed mechanism. The shippers, such as Gazprom in the case of Moldova, are not involved in the allocation of revenue between the TSOs in the system. Consequently, Gazprom's practice of paying transit fees to Moldovagaz/Tiraspoltransgaz-Pridnestrovie is not only contrary to the Transit Contract (cf. Section 5.5.4 above), but also contrary to the system in the TAR NC.

5.5.5.3 ITC Mechanisms in European practice

- (295) Multi-TSO arrangements within a single Member State is known from Austria, France, Germany, Hungary, Italy and Spain.¹⁸² However, the details of the ITC Mechanisms in the gas sector are generally not publicly available and/or easily accessible.¹⁸³
- (296) For instance, the Austrian regulator, Energie-Control Austria, recently proposed to adopt a single flow-based commodity charge on top of the existing capacity-based tariff in order to cover additional fuel costs due to the energy crisis.¹⁸⁴ The proposed flow-based commodity

¹⁸² See page 69 of the TAR NC Implementation Document at <https://www.entsog.eu/tariff-nc> (accessed on 6 February 2023).

¹⁸³ While ACER monitors ITC agreements in electricity and publishes a review each year, it does not do the same for gas. The reasons for this is that the ITC Mechanism in electricity is mandatory and EU-wide, while the ITC Mechanisms in gas are local and, if it covers more than one Member State, voluntarily.

¹⁸⁴ The European Union Agency for the Cooperation of Energy Regulators (ACER), "*Agency Report – Analysis of the consultation document on the application of a commodity charge (flow-based charge) in Austria – NRA: Energie-Control Austria – TSO: Gas Connect Austria & Trans Austria Gasleitung*",

charge was accompanied by an ITC Mechanism to redistribute the recovered revenue between the Austrian TSOs, Gas Connect Austria (GCA) and Trans Austria Gasleitung (TAG). The application of the single flow-based charge resulted in the cross-subsidisation between the users of the infrastructure of GCA and TAG. The proposed ITC Mechanism serves to ensure that each TSO would recover its allowed uncontrollable costs and allowed revenue.¹⁸⁵ ACER noted that "[b]oth TSOs have different flow costs, however, a single flow-based charge is applied to them. The ITC serves to balance the expected over-recovery from GCA and the expected under-recovery from TAG."¹⁸⁶ However, the details of the ITC Mechanism as such were not discussed.

- (297) To our knowledge, there are not many examples of ITC Mechanisms in the gas sector covering more than one Member State where more than one TSO is active. The TAR NC Implementation Document refers to a system covering Belgium and Luxembourg.¹⁸⁷ Also, on 14 February 2019, the TSOs in Finland, Latvia and Estonia, Gasum Oy, AS Conexus Baltic Grid and Elering AS, signed an Inter TSO Compensation (ITC) agreement, which enabled the functioning of a single gas transmission tariff zone for Finland, Estonia and Latvia.¹⁸⁸ The Estonian-Finnish interconnector, Balticconnector, falls under the scope of the ITC Agreement, and so does transportation of gas to and from the Inčukalns underground gas storage in Latvia. Starting from the beginning of 2020, the ITC agreement between the transmission system operators has removed gas transmission tariffs on borders between Finland, Estonia and Latvia, and has imposed an equal entry fee on all import points starting from the beginning of 2020. The TSOs settle the costs of transmission in the interconnector pipelines between themselves. The details are not publicly available, but it has been reported that the ITC agreement foresees compensation for TSOs of eligible variable costs and sets principles of the entry revenue re-distribution among the operators.¹⁸⁹

dated 12 May 2022 at

https://www.acer.europa.eu/sites/default/files/documents/Publications/Agency%20report%20-%20analysis%20of%20the%20consultation%20document%20for%20Austria_2022.pdf (accessed on 6 February 2023).

¹⁸⁵ *Ibid*, pages 3 and 17.

¹⁸⁶ *Ibid*, page 17.

¹⁸⁷ See page 69 of the TAR NC Implementation Document at <https://www.entsog.eu/tariff-nc> (accessed on 6 February 2023).

¹⁸⁸ See for instance TallinnLNG, "*[t]he gas TSOs of Finland, Estonia and Latvia have reached a new voluntary agreement on inter-TSO compensation system*" (<https://www.tallinnlng.com/the-gas-tsos-of-finland-estonia-and-latvia-have-reached-a-new-voluntary-agreement-on-inter-tso-compensation-system/>, accessed on 6 February 2023), World Pipelines, "*[t]ariff agreement once the Balticconnector pipeline is running*"

(<https://www.worldpipelines.com/business-news/15022019/tariff-agreement-once-the-balticconnector-pipeline-is-running/>, accessed on 6 February 2023) and Conexus, "*[t]he gas TSOs of Finland, Estonia and Latvia have reached an agreement on inter-TSO compensation system*"

(<https://www.conexus.lv/press-releases/somijas-igaunijas-un-latvijas-pso-panakusi-jaunu-brivpratigu-vienosanos-par-gazes-parvadu-kompensaciju-sistemu>, accessed on 6 February 2023).

¹⁸⁹ See TallinnLNG, "*[t]he gas TSOs of Finland, Estonia and Latvia have reached a new voluntary agreement on inter-TSO compensation system*" (<https://www.tallinnlng.com/the-gas-tsos-of-finland-estonia-and-latvia-have-reached-a-new-voluntary-agreement-on-inter-tso-compensation-system/>, accessed on 6 February 2023) and Conexus, "*[t]he gas TSOs of Finland, Estonia and Latvia have reached an agreement on inter-TSO compensation system*" (<https://www.conexus.lv/press-releases/somijas-igaunijas-un-latvijas-pso-panakusi-jaunu-brivpratigu-vienosanos-par-gazes-parvadu-kompensaciju-sistemu>, accessed on 6 February 2023).

5.5.5.4 The TAR NC 2nd Revised Implementation Document of 2019

- (298) As mentioned in Section 5.7.5.2, Article 10(3) TAR NC does not establish specific material requirements with respect to the design of the ITC Mechanism. The main point is that the ITC Mechanism allocates costs fairly between the operators which provide the transportation services and which infrastructure hosts the gas flows, without cross-subsidisation.
- (299) The TAR NC 2nd Implementation Document of 2019 contains certain examples of the application of an ITC Mechanism in Multi-TSO entry-exit systems within a Member State, i.e. in Article 10 circumstances. The Implementation Document provides examples of an ITC Mechanism both in so-called 'same jointly' and so-called 'same separately' circumstances. These examples illustrate that the ITC Value is derived as the difference between the allowed revenue of each TSO and the revenue collected via the tariffs for the system. This ITC Value indicates the amount that one TSO has to collect through its tariffs and pass on to the other TSO, alternatively how the tariffs of the TSOs have to be adjusted to ensure that each TSO earn their respective allowed revenue.
- (300) By contrast, Article 3.2 of the Transit Contract applies different principles for cost allocation between Moldovatransgaz and Tiraspoltransgaz on the two transport routes, even if the costs of transportation related to both transport routes are calculated based on volume and distance and there is no apparent reason for treating the two transport routes differently. As mentioned in Section 5.5.4, it is difficult, based on the available information, to understand how (in particular) the 50-50 split on the Orlovka route reflects the cost related to the infrastructure operated by Moldovatransgaz and Tiraspoltransgaz respectively.

5.5.6 Conclusion

- (301) The current distribution of transit tariff payments between Moldovagaz and Tiraspoltransgaz-Pridnestrovie is contrary to the Transit Contract between Moldovagaz and Gazprom.
- (302) Article 3.2 of the Transit Contract has the character of an ITC Mechanism, which is both allowed as well as required in multi-TSO entry-exit systems within a Member State under EU law. Assuming that Gazprom allocates its payment between Moldovagaz and Tiraspoltransgaz-Pridnestrovie in accordance with the internal cost distribution in Article 3.2 of the Transit Contract, this payment distribution is not in line with the ITC Mechanism principles in the EU law.
- (303) The cost distribution in Article 3.2 of the Transit Contract differentiates in the way the costs are distributed between the involved TSOs depending on the transport route even if there is no apparent objective reason for treating the two transport routes differently. Accordingly, Article 3.2 of the Transit Contract does not seem to fulfil the purpose of an ITC Mechanism, i.e. the fair allocation of de facto costs related to the transportation services provided by the respective TSOs involved.
- (304) Furthermore, Gazprom's payment allocation between Moldovagaz and Tiraspoltransgaz-Pridnestrovie is not in line with the formal procedure for cost distribution between multiple TSOs in one pipeline system. Pursuant to EU law, it is for the TSOs to distribute income between themselves in accordance with the (regulatory approved) ITC Mechanism, not for the shippers.
- (305) The fact that Gazprom's payment allocation between Moldovagaz and Tiraspoltransgaz-Pridnestrovie is neither materially nor formally in conformity with the EU principles could therefore be used as a point of negotiation with Gazprom. In particular, Moldovagaz may have a counterclaim for underpayments of transit fees for the Alekseevka/Oleksiiivka direction, amounting to at least 22% of the fees paid since 2007, since Moldovagaz arguably should have received 72% rather than 50% of the fees paid in that period.

- (306) Moldovagaz may have a counterclaim for approximately USD 160 million of lost transit revenues, paid by Gazprom to Tiraspoltransgaz in breach of custom and practice.

5.6 Costs incurred by Moldovagaz's management beyond the costs which can be recovered through the Moldovan regulated gas tariffs and Moldovagaz's handling of foreign currency procurement and gas losses

- (307) As described in Section 4.7.4 above, Moldovagaz's own analysis of the reasons for the Debt accumulation in the period 2011 to 2021 *inter alia* highlights that the actual costs of the following cost categories were not accepted by ANRE in the customer tariff:
3. The value of natural gas losses (MDL 669 million or USD 46 million equivalent));
 4. The construction costs of a new office building in Chisinau (MDL 465 million or USD 32 million equivalent);
 5. Other investments (i.e. investments in a new billing system, investments in gasification and new gas pipelines, investments in IT, equipment and buildings) (MDL 341 million or USD 23 million equivalent);
 6. Foreign currency purchasing costs (MDL 147 million or USD 10 million equivalent);
 7. Non-reimbursed transit service costs (MDL 115 million or USD 8 million equivalent);
 8. Financial expenses (MDL 253 million or USD 17 million equivalent); and
 9. Other expenses (MDL 103 million or USD 7 million equivalent).
- (308) The abovementioned costs are all actual operating and/or capital costs which in principle qualify for cover, but have not been accepted, either in full or in part by ANRE. We also understand that certain investments (cf. item 3 above)¹⁹⁰ and expenses (cf. item 7 above)¹⁹¹ were not allowed because Moldovagaz did not demonstrate the economic efficiency of the investments and expenses. Also, some investment costs were related to cost overruns which were not pre-approved.¹⁹² We also understand that ANRE in 2011 imposed strict limits to the level of gas losses which are compensated through the customer tariffs, encouraging Moldovagaz to implement an, eventually successful, program to reduce losses.¹⁹³
- (309) We have considered whether the refusal to include the above mentioned costs in ANRE's customer tariff methodology is in line with international standards. We consider EU law and European practice as the relevant comparator as Moldova is a Contracting Party to the Energy Community Treaty and has made significant progress in implementing the EU gas *acquis*.
- (310) As described in Section 4.7.2 above, the customer tariff consists of two key components, i.e. the costs of carrying out the regulated activities (transit, distribution and supply of natural gas) and the allowed revenue for each of these activities. Thus, the customer tariff regulates the delivered price of gas, which includes a transport element. Some of the costs identified by Moldovagaz (cf. above) are linked to the gas supply activity (such as e.g. foreign currency

¹⁹⁰ See section 4.7.8 above.

¹⁹¹ See section 4.7.13 above

¹⁹² Ibid.

¹⁹³ See section 4.7.6 above and ECBR, Distribution tariff methodologies for electricity and gas in the Energy Community, April 2019, p. 45.

purchase costs), while other costs (such as e.g. gas losses and measures to prevent such losses, and investments in gasification and gas pipelines) are linked to the transportation of gas. Our assessment is therefore largely based on the requirements that transmission and distribution tariffs are subject to under EU law.

- (311) The underlying objective of Directive 2009/73/EC (the "Gas Directive") is to ensure a competitive gas market, cf. Article 3(1). In general, regulated commodity prices are not compatible with the ideal of the competitive internal gas market.¹⁹⁴ However, the Gas Directive allows Member States to implement regulated price schemes, provided that they are clearly defined, transparent, non-discriminatory and do not impede the opening of the market, cf. Article 3(2) and Article 41(1)(p).
- (312) Recital (32) and Articles 32(1) and 41(6)-(8) of the Gas Directive provide general rules that transmission and distribution tariffs have to be compliant with, while Article 13 of Regulation 715/2009 (the "**Gas Regulation**") and Commission Regulation 2017/460 (the "**TAR NC**") provide more detailed rules regarding transmission tariffs. These rules sets out a set of varying and, to some extent, contradictory objectives. Both transmission and distribution tariffs shall be non-discriminatory and cost-reflective¹⁹⁵ and allow necessary investments in the networks¹⁹⁶. In addition, Article 41(8) reflects the importance of incentive based regulation to avoid excess transmission and distribution tariffs, as it establishes that the regulatory authority, when fixing or approving tariffs or their methodologies shall ensure that transmission and distribution operators are granted appropriate incentive to increase efficiencies, foster market integration and security of supply and support related research activities.
- (313) To summarise, EU gas law is largely silent as to which costs need to be taken into account when calculating transmission and distribution tariffs, leaving the issue of eligible costs to the Member States when transposing or applying the legislation.¹⁹⁷ Furthermore, the EU gas law also implies a trade-off between the cost reflectivity requirement and the other requirements, and provides the regulatory authority with discretion on how to implement these requirements in the specific circumstances.¹⁹⁸ As a result, various studies¹⁹⁹ show that what costs are considered eligible and to what extent differs between EU Member States as well as Contracting Parties to the Energy Community.
- (314) For example, it is left to the discretion of the regulatory authority whether (both technical and non-technical) gas losses are covered by the transport tariffs. While a recent study show that such gas losses are considered eligible costs in Energy Community overall, it varies in practice how and to what extent such gas losses are covered by the transport tariffs in the various Contracting Parties.²⁰⁰ The study show that with respect to the allowed level of losses for tariff calculation, Moldova lies in the mid-range.²⁰¹
- (315) Legal theory provides certain general guidelines with respect to tariff calculation.²⁰² For

¹⁹⁴ See e.g. Christopher Jones et al, EU Energy Law Volume I – The Internal Energy Market (fourth edition) (Jones I), p. 490.

¹⁹⁵ Recital (32) of the Gas Directive.

¹⁹⁶ Article 41(6)(a) second sentence.

¹⁹⁷ Jones I, p. 53.

¹⁹⁸ Jones I, p. 52.

¹⁹⁹ See e.g. ECBR, Gas Transmission Tariffs in South and Central East Europe, February 2018, and ECBR, Distribution tariff methodologies for electricity and gas in the Energy Community, April 2019.

²⁰⁰ See e.g. ECBR, Distribution tariff methodologies for electricity and gas in the Energy Community, April 2019, pp. 43-45.

²⁰¹ Ibid, p. 45.

²⁰² Jones I, pp. 51-52.

instance, the principle of cost reflectivity does not translate to an automatic correspondence between the costs of the regulated business and the revenues collected from network tariffs.²⁰³ In legal theory, it is mentioned as an example, that a regulatory authority may accept a high return on investment for specific assets to reward a past risk, efficiency or to encourage future investment, and that this does not mean that the tariffs cannot be cost-reflective.²⁰⁴

- (316) At the same time, the principle of cost reflectivity does not imply that the system operator cannot incur losses. The principle of incentive based regulation indicates that the EU gas law accepts that the system operator may ultimately incur losses if it does not meet efficiency targets.
- (317) Taking into account the discretion of the regulatory authority described above, in this case ANRE, when determining what costs are eligible to consider and to what extent, we believe that ANRE's approach would be considered in line with international standards.
- (318) Further, significant transactions by Moldovagaz are to be approved by the Shareholder's meeting or the Supervisory Board,²⁰⁵ both controlled by Gazprom²⁰⁶. Consequently, investments which have not been approved by ANRE have likely been approved by Gazprom. Moldovagaz may use this to challenge the Debt, since Gazprom arguably is responsible for Moldovagaz's use of profits which otherwise could have been used to reduce the Debt. This applies to the cost categories listed above, which amounts to MDL 2,093 million (USD 143 million equivalent).

5.7 Other legal issues

5.7.1 *Gazprom may be precluded from claiming penalties for the period from 1 April 2004 to 2020 under Russian law*

- (319) Prior to the submission of the Preliminary Assessment Report, we were informed by Moldovagaz that Gazprom had not claimed any penalties for late payment or otherwise since at least 2005, and that all the previously accrued penalties were included in the debt assigned to Faktoring-Finans in 2005.²⁰⁷ This was supported by the signed Reconciliation Statements between Moldovagaz and Gazprom, which only refers to debts for "*delivered natural gas*" and do not mention any penalties.²⁰⁸ The latter *might* mean that Moldovagaz has not confirmed or agreed to have any debts arising from penalties due to late payments since 2005, unless Moldovagaz has accepted such liability through other communications with Gazprom which we have not seen.
- (320) Against this background, Russian Counsel concluded that unless there are other circumstances that could constitute a suspension or interruption of the statute of limitations, there is a high probability that Moldovagaz can successfully rely on the expiry of the

²⁰³ ECRB, Distribution tariff methodologies for electricity and gas in the Energy Community, April 2019, p. 45.

²⁰⁴ *Ibid.*

²⁰⁵ Charter of the Moldovan-Russian Joint Stock Company Moldovagaz (2021 redaction), Sections 29 and 43.

²⁰⁶ We understand that Gazprom exercises the shareholders' rights of the so-called government of Transnistria pursuant to agreement.

²⁰⁷ Interview with Moldovagaz management, Chisinau, 18 October 2022.

²⁰⁸ Reconciliation Statement between Moldovagaz and Gazprom, dated 31 December 2021.

limitation period with respect to the relevant penalties.²⁰⁹

- (321) Between the submission of the Preliminary Assessment Report and this Final Report, we have been informed that Gazprom *did* claim penalties for late payment after 2005, but that Moldovagaz refused to accept such penalties, and did not sign the Mutual Reconciliation Acts in which Gazprom made such claims, since 1 April 2004.²¹⁰ This fact does in our opinion not change the conclusion in the Preliminary Assessment Report. Thus, according to Russian counsel, interruption of the limitation period requires that the debtor *acknowledges* the debt.²¹¹ In respect of reconciliation statements/acts, this requires the statement/act to be signed by an authorized person from the debtor's side. A debtor's *passivity*, for example a failure to challenge a direct debit request, does not constitute an acknowledgment of the debt.²¹² Moldovagaz's refusal to sign Mutual Reconciliation Acts cannot then reasonably be considered evidence that the claimed penalties have been acknowledged as debts.
- (322) While this does not contribute to reduce the current Debt claimed by Gazprom, it may have an important effect in negotiations by preventing Gazprom from threatening to increase its claims towards Moldovagaz.
- 5.7.2 *The Arbitral Awards rendered in the period 2008 to 2020 have expired under the Statute of Limitations in Moldova and Gazprom may not obtain new awards for the same periods under Russian law*
- (323) We have asked Moldovan Counsel to assess whether the arbitral awards issued by the ICAC from 2008 to 2020 (the "**Arbitral Awards**") have expired under the applicable Statute of Limitations in Moldova, with the effect that Gazprom is precluded from attempting to enforce the awards in Moldova.²¹³ In that context, we have also asked Russian Counsel to assess whether Gazprom may obtain new awards for the same deliveries pursuant to Russian law.²¹⁴
- (324) Moldovan Counsel has informed us that pursuant to paragraph 6 of Article 475/1 of the Civil Procedure Code of Moldova (the "**Civil Procedure Code**"), an application for the recognition and/or enforcement of a foreign arbitral award (such as the Arbitral Awards in question) on the territory of Moldova must be submitted to a court within a three-year period from the date on which the foreign arbitral award became binding under the laws of the seat of the arbitration.²¹⁵ The Arbitral Awards became binding under Russian law when they were issued.²¹⁶
- (325) Thus, as Gazprom did not attempt to recognise or enforce the 2008 to 2020 Arbitral Awards in Moldova within three years of the date of their issuance, the Arbitral Awards will most

²⁰⁹ **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.2.2.2.

²¹⁰ Section 2.5.5 above

²¹¹ **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.2.10

²¹² *Ibidem*

²¹³ **Appendix No. 4:** Opinion on certain Moldovan law matters, dated 31 May 2023, Section IX, D.

²¹⁴ **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.3.

²¹⁵ **Appendix No. 4:** Opinion on certain Moldovan law matters, dated 31 May 2023, Section IX, D.

²¹⁶ The Rules of Arbitration of International Commercial Disputes, Appendix No. 2 to Order No. 6 of the Chamber of Commerce and Industry of the Russian Federation dated 11.01.2017, § 42 and Law on International Commercial Arbitration, 7 July 1993, N 5338-1, Article 35.1.

likely not be enforceable pursuant to the Civil Procedure Code.²¹⁷

- (326) There are some exceptions to this rule: Pursuant to paragraph 6 of Article 475/1 of the Civil Procedure Code, a Moldovan court may restore the procedural time limit pursuant to the procedure set out in paragraphs 1 and 4 of Article 116 of the Civil Procedure Code. The requirement is that the action (i.e. filing for recognition/enforcement) has not been carried out for "*justified and reasonable reasons*" ("*по обоснованным причинам*"), cf. Article 116 (1) of the Civil Procedure Code. Moldovan Counsel has informed us that "[t]here should be no plausible objective excusable reasons for the failure of Gazprom to timely apply in a court of law of the Republic of Moldova for the recognition and enforcement of the arbitral awards, except for reason of the State of emergency, which was introduced by the Resolution of the Parliament No. 41 of 24 February 2022".²¹⁸ Thus, it seems unlikely that Gazprom would be able to successfully rely on this exception to enforce the Arbitral Awards rendered before 2020.
- (327) However, a court may not raise the statute of limitation *ex officio*. To bar enforcement of the expired Arbitral Awards, Moldovagaz must therefore raise this defence in any enforcement proceedings.²¹⁹ The expiry of the Awards does not prevent Moldovagaz from voluntarily executing the Arbitral Awards.²²⁰
- (328) The conclusions above apply to the courts of the Right bank, assuming their independent and correct application of the law. Moldovan Counsel notes that Gazprom may attempt to enforce the Arbitral Awards on the Left bank or, in case of an unconstitutional change of regime in Moldova, also on the Right bank.²²¹
- (329) If Gazprom is barred from enforcing the Arbitral Awards in Moldova due to the above regulations, Gazprom may in theory attempt to obtain new awards for, i.e. relitigate, the same claims that are subject to the Arbitral Awards in order to improve its chances of enforcement in Moldova. If Gazprom is successful in relitigating the claims, Gazprom may possibly circumvent the three-year limitation and thereby enforce the parts of the Debt that are covered by the Arbitral Awards.
- (330) Russian Counsel has informed us that while Gazprom would face no practical impediments to initiating new ICAC arbitrations (i.e. registering the case at the ICAC), Russian law and court practice recognise and uphold the principle of *res judicata*.²²² Thus, as Russian Counsel concludes, it is reasonable to assume that an unbiased arbitral tribunal properly applying Russian law would be sympathetic to a *res judicata* defence raised in response to an attempt by Gazprom to relitigate the matters.²²³
- (331) Gazprom may, however, attempt to argue that the Arbitral Awards should be revised due to new circumstances. Pursuant to Russian law, this would necessitate that newly discovered circumstances which were unknown at the moment of adjudication of the previous dispute or that new circumstances which have appeared after the rendering of the court decision and that have a material effect on adjudication of the dispute have come to light.²²⁴ Gazprom

²¹⁷ **Appendix No. 4:** Opinion on certain Moldovan law matters, dated 31 May 2023, Section IX, D.

²¹⁸ *Ibid.*

²¹⁹ *Ibid.*

²²⁰ *Ibid.*

²²¹ *Ibid.*

²²² **Appendix No. 5:** Memorandum on certain Russian law matters, dated 2 February 2023, Section 2.3.2.

²²³ *Ibid.*, Section 2.3.3.

²²⁴ *Ibid.*, Section 2.3.5.

may also try to move the disputes to a Russian court if e.g. the arbitral tribunal would dismiss the case due to lack of jurisdiction, in which case Gazprom may argue that the only remaining venue for adjudication are the Russian courts.

- (332) The above also means that Moldovagaz must raise the defence that the claims covered by the Arbitral Awards cannot be relitigated due to the *res judicata* effect in any ICAC proceeding initiated by Gazprom.
- (333) In the event that Gazprom successfully relitigates the Arbitral Awards in new ICAC proceedings, it is nevertheless unlikely that Gazprom would be able to enforce such relitigated awards in Moldova. Moldovan Counsel has informed us that enforcement of relitigated awards may be refused pursuant to Article 476 (2) of the Civil Procedure Code of Moldova, as such enforcement would violate the principle of *res judicata* which is considered to be part of the public policy of Moldova.²²⁵
- (334) The Arbitral Awards do not distinguish between debts for deliveries to the Right and the Left bank of the river Nistru, and Moldovagaz's outstanding debt pursuant to the Arbitral Awards amounts to approximately USD 6,5 billion, which comprises debts for deliveries in the period 2005 to 2019. The Auditors have compared the stated debts pursuant to the Arbitral Awards with the corresponding Acts of Acceptance signed by Moldovagaz and Gazprom. Based on this comparison exercise, approximately USD 400 million of the USD 6,5 billion which is due pursuant to the Arbitral Awards pertains to deliveries to the Right bank only. The outstanding debt pursuant to Arbitral Awards from 2021 and 2022 relates to Left bank deliveries only. Thus, a very significant share of the Debt that Moldovagaz allegedly owes Gazprom may most likely not be enforced under Moldovan law.

6 SCOPE OF FINAL REPORT

6.1 Introduction

- (335) This Final Report has been prepared on the basis of the Tender Book, which is enclosed as Appendix No. 1 to this Report.
- (336) The Final Report is solely based on the documents set out in Appendix No. 2 (the "**Documents**"). In addition, this report is to some extent based on information provided by Moldovagaz's management in meetings in Chisinau from 18 to 20 October 2022 and in subsequent calls as described in Section 3 above.

6.2 Scope and limitations of the Final Report

6.2.1 *Limitations to the financial scope of the Final Report*

- (337) Moldovagaz has confirmed that it does not possess information / underlying data relating to a number of the Auditor's information requests required to complete the financial audit, in particular information / underlying data relating to the period prior to 1 January 2003. As a result, it has not been possible to date for the Auditors to undertake any verification of the Debt accrued in this period.
- (338) Our review does not extend to matters of a legal nature or any other matter of a non-financial nature.
- (339) This Report is based on the text of the Documents as set out on their face, as well as

²²⁵ **Appendix No. 4:** Opinion on certain Moldovan law matters, dated 31 May 2023, Section IX, D.

information provided to us by e-mail and orally. We have assumed that such documentation and information is accurate, complete and not misleading. This also applies when the information is provided in the form of schedules, summaries, correspondence, reports and the underlying documentation has not been made available to us.

- (340) The Documents may not comprise all the documents that ought to have been supplied to us or that have been requested by us for the purpose of our review and/or may not contain all the information which may be relevant to the PPA's decisions in respect of the Scope.
- (341) We have only to a limited extent attempted to verify the information provided against other sources, such as e.g. public registries or other publicly available information.
- (342) This Report reflects the findings as of the date of the Report. We shall have no responsibility to update this Report.
- (343) To the extent that this Report contains information from agreements with third parties subject to confidentiality undertakings, breach of such undertakings may entitle such third parties to terminate the relevant agreement and/or claim damages in respect of the breach. No analysis of such issues is contained in this Report.
- (344) This Report is not intended to be or include a summary of all communications we have had with the PPA and Moldovagaz or advice we have provided to the PPA concerning the matters discussed in this Report, and accordingly, we understand that the PPA is construing this Report in light of all of our conversations and discussions.

6.2.2 *Limitations to the legal scope of the Final Report*

- (345) We can only opine on matters of Norwegian and international law, and unless otherwise is expressly stated in writing, we express no opinion as to the national laws of any jurisdiction other than Norway. To the extent that documents relate to legal issues arising under other laws or jurisdictions, our comments are based on the wording of the documents, our experience from dealing with Gazprom and the gas industry in general, and advice from locally qualified counsel.
- (346) Our review does not extend to financial, accounting or commercial matters or any other matter of non-legal nature.
- (347) Our review addresses only the issues which we have considered significant from a legal perspective. We cannot accept responsibility for assessing commercial implications, although we have sought, where possible, to highlight matters which seemed to us to be commercially significant.
- (348) We have only highlighted those legal issues which we consider might be material in the context of the Scope.
- (349) This Report is based upon a documentation verification process by our due diligence team, based on documentation provided to us by the PPA and Moldovagaz.
- (350) We have not independently verified the accuracy or completeness of the Documents or other information provided to us.
- (351) This Report is based on the text of the Documents as set out on their face, as well as information provided to us by e-mail and orally. We have assumed that such documentation and information is accurate, complete and not misleading. This also applies when the information is provided in the form of schedules, summaries, correspondence, reports and the underlying documentation has not been made available to us.

- (352) The Documents may not comprise all the documents that ought to have been supplied to us or that have been requested by us for the purpose of our review and/or may not contain all the information which may be relevant to the PPA's decisions in respect of the Scope.
- (353) We have only to a limited extent attempted to verify the information provided against other sources, such as e.g. public registries or other publicly available information.
- (354) This Report reflects the findings as of the date of the Report. We shall have no responsibility to update this Report.
- (355) To the extent that this Report contains information from agreements with third parties subject to confidentiality undertakings, breach of such undertakings may entitle such third parties to terminate the relevant agreement and/or claim damages in respect of the breach. No analysis of such issues is contained in this Report.
- (356) This Report is not intended to be or include a summary of all communications we have had with the PPA and Moldovagaz or advice we have provided to the PPA concerning the matters discussed in this Report, and accordingly, we understand that the PPA is construing this Report in light of all of our conversations and discussions.

6.3 Assumptions and restrictions

6.3.1 Assumptions

- (357) We have assumed that all copies of documents reviewed by us conform to the originals and the genuineness of all signatures.
- (358) We have (unless explicitly stated otherwise) assumed that each of the documents provided to us is in full force and effect, incorporates on its face all amendments which have been made to it and has not been terminated. It is important to bear in mind that agreements could have been amended orally or by a cause of conduct not evident from their text.
- (359) We have assumed that each party to each contract and treaty reviewed by us has the capacity, power and authority and has taken all actions necessary to execute and deliver, and to exercise its rights and perform its obligations under the relevant contract or treaty. Furthermore, we have assumed that all licences, authorisations, approvals, clearances and consents from public authorities provided to us have been duly and validly executed and is in full force and effect and, save where expressly brought to our attention, has not been terminated or amended.
- (360) We have assumed that each document provided to us is valid and binding on each of the parties to it, and that each of those parties has duly complied with the provisions of the relevant document.
- (361) We understand that for a number of contracts or issues, large quantities of documentation exist. Our review has been based on those documents that have been presented to us by the PPA and Moldovagaz, and we have generally not been in the position to judge independently the extent of completeness of the documentation submitted to us.

6.3.2 Restrictions and secrecy

- (362) This Report may not be relied upon by any other entity than the Moldovan Government, and may not be shown to persons or entities other than Moldovagaz's Supervisory Board without our prior written approval.
- (363) As Norwegian counsel, we are bound by applicable rules and regulations in respect of the matter of secrecy. We have also signed a specific confidentiality undertaking in connection

with the assignment.

- (364) If and to the extent this Report contains personal data as defined in the General Data Protection Regulation (EU) 2016/679 (GDPR), the Client shall be regarded as the data controller for further processing of such personal data. For the avoidance of doubt, the Client bears full responsibility for ensuring that further processing is compliant with applicable data protection laws and regulations, including the GDPR.
- (365) Our assignment in connection with the Scope (including the preparation and issuance of this Report) is subject to the terms set out in our 10 August 2022 Contract with the PPA for the acquisition of financial and legal audit services related to the debt of "Moldovagaz" J.S.C to "Gazprom" J.S.C. and "Factoring Finance" L.L.C. for gas deliveries to consumers of the Republic of Moldova from the right bank of the Nistru river.
- (366) In respect of the legal audit services, this Report shall be construed in accordance with Norwegian law. Any disputes in respect of the legal audit services of this Report shall be governed by Norwegian law. The lawyer in charge of the legal audit services is WR partner Aadne Martin Haga.
- (367) In respect of the forensic auditing services, this Report shall be construed in accordance with the laws of England and Wales. Any disputes in respect of the forensic auditing services of this Report shall be governed by the laws of England and Wales.

7 LIST OF APPENDICES

APPENDIX NO. 1: TENDER BOOK

APPENDIX NO. 2: LIST OF DOCUMENTS RELIED ON

APPENDIX NO. 3: FIFTH REQUEST FOR DOCUMENTS TO MOLDOVAGAZ

**APPENDIX NO. 4: OPINION ON CERTAIN MOLDOVAN LAW MATTERS BY
BURUJANA & PARTNERS**

**APPENDIX NO. 5: MEMORANDUM ON CERTAIN RUSSIAN LAW MATTERS BY
MANNHEIMER SWARTLING**