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Implementation of the European Neighbourhood Policy in 2008

Progress Report Armenia

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1. BACKGROUND AND OVERALL ASSESSMENT

Armenia and the EU first established contractual relations in 1996 through a Partnership and Cooperation Agreement which entered into force in 1999. On this basis, the EU-Armenia ENP Action Plan was adopted in November 2006 for a period of five years. A first progress report was adopted in April 2008.

Institutional cooperation through the EU–Armenia Cooperation Council, the EU–Armenia Cooperation Committee and the EU-Armenia subcommittee on trade and related legal issues enabled both sides to move forward and follow the implementation of the ENP Action Plan closely. The opening of a full-fledged Delegation of the European Commission in Yerevan in February 2008 contributed to the further strengthening of EU-Armenia bilateral relations.

This document reports on overall progress made on the implementation of the EU-Armenia ENP Action Plan between 1 January and 31 December 2008, although developments outside this period are also considered when deemed relevant. It is not a general review of the political and economic situation in Armenia.

Overall, Armenia made progress in several areas of the ENP Action Plan. However, Armenia is still struggling with the consequences of the internal crisis in the aftermath of Presidential elections in February 2008 which led to the introduction of a state of emergency and a number of restrictions of democratic freedoms and human rights, affecting in particular freedom of expression, freedom of assembly and media freedom.

Nonetheless, Armenia made some progress in implementing reforms which constitute key priorities under the ENP Action Plan. Progress was made in particular on tax and customs reforms, financial services and competition policy. Armenia also entered into a new IMF-supported Poverty Reduction and Growth Facility which aims to enhance Armenia's macroeconomic stability and economic performance. Important steps were taken in improving transparency of the government's decision-making process and cooperation with NGOs and civil society, although more remains to be done, including in building dialogue with the opposition. Armenia also took steps to strengthen the Human Rights Defender by increasing its range of activity and independence. Armenia made progress in regional cooperation and dialogue with neighbouring countries, in particular with Turkey. Furthermore, Armenia widely aligned itself with CFSP declarations and is generally very active in cooperating on CFSP-related issues.

A positive step on the Nagorno-Karabakh conflict was taken, despite the prevailing high tensions, with the first document jointly signed by the Presidents of Armenia and Azerbaijan since 1994.

Of key importance for 2009 will be proper implementation of adopted legislation, as already pointed out last year for this reporting period. Further overall progress is needed on political dialogue and reform, including on effectively addressing corruption, on respecting human rights and on freedom of expression.

2. POLITICAL DIALOGUE AND REFORM

Objectives in this area include: strengthening the stability and effectiveness of institutions guaranteeing democracy and the rule of law through: strengthening democratic institutions, reform of the judiciary, civil service reform and fight against corruption.

Democracy and the rule of law

Political dialogue between the EU and Armenia has intensified. In September 2008, a new interdepartmental commission to oversee the implementation of the ENP Action Plan was established, chaired by the Secretary of the National Security Council. The establishment of an EU Advisory Experts Group to assist Armenia in the implementation of the ENP Action Plan was agreed by the EU and Armenia in November 2008.

The presidential **elections** held in February 2008 and the post-election events slowed down the adoption of legislative amendments to comply with the requirements of the new constitution. Adoption of legislative amendments regarding the separation of powers, the independence of the judiciary and the freedom of the media is still ongoing.

Following the elections, Armenia slid into political crisis. While the elections mostly met OSCE commitments and international standards in the pre-election period and during voting hours, serious challenges to some commitments emerged after the election day. The vote count demonstrated deficiencies of accountability and transparency and complaints and appeals procedures were not fully effective, which displayed an insufficient regard for standards essential to democratic elections and devalued the overall election process. This set in motion a chain of events that culminated in the clashes of March 1-2, which left 10 people dead and led to more than one hundred arrests and a state of emergency which remained in force until 20 March. Despite international calls to release all persons “detained on seemingly artificial and politically motivated charges who did not personally commit any violent acts or serious offences”, many of them were still imprisoned by the end of the year. The Parliamentary Assembly of the Council of Europe (PACE) adopted two resolutions in 2008 (1609, 1620) on the functioning of the democratic institutions in Armenia, raising in particular the issue of the arrests of opposition supporters and members of Parliament, of the control over the electronic medias and of the freedom of assembly as well as of a number of prosecution cases and convictions based solely on police testimony. The Armenian authorities took some measures to address the political crisis. The implementation of the PACE recommendations was considered not satisfactory by the PACE Monitoring Committee in its draft resolution of December 2008. Several steps were taken by the authorities in January 2009; after which the PACE decided in January 2009 not to suspend the Armenian delegation’s voting rights and did not put forward this sanction for consideration at a later stage, while calling on authorities to continue the process of reforms.

After the entry into force of the new judicial code in January 2008 (see last year’s report), the main reforms of which are a re-organisation of the judiciary, establishment of the specialised courts and self-governing bodies of the judiciary and a change of the role of the Court of Cassation, additional amendments/revisions of different legal acts related to the **judiciary** were adopted, however, the main challenge for Armenia remains to implement all adopted legislation and to fully safeguard the independence of the judges.

The criminal code was revised in the first half of 2008 to include relevant articles on active and passive **corruption** in line with the standards of the Council of Europe (CoE) and the UN Convention against Corruption (UNCAC). Some practical steps to fight corruption were implemented mainly in the customs service, see section 4, but further steps should be taken. Despite the fact that the national anti-corruption strategy expired at the end of 2006, the new

strategy to ensure better alignment with Council of Europe Group of States against Corruption (GRECO) recommendations has not yet been adopted. The civil service council continued its efforts to improve the recruitment procedure of the civil service, in particular through cooperation with civil society organizations.

On **local self-government**, the National Assembly adopted in December 2008 the new law for the City of Yerevan providing for indirect elections of the city's Mayor. The Government also adopted the concept on approaches for the consolidation of communities and the formation of intercommunity unions aimed at enlarging communities and strengthening their capacities.

Human rights and Fundamental Freedoms

The objectives in this area include: strengthening respect for human rights and fundamental freedoms, ensuring the independence of the media by strengthening the independent regulatory body for public and private broadcasters, installing freedom of assembly, further reform of the penitentiary system to improve detention conditions; continue efforts to ensure trade union's rights and core labour standards, ensure respect for the national minorities; continue efforts to ensure the equality of men and women in society and economic life.

The State of Emergency between 1 March and 20 March entailed restrictions on freedom of expression and freedom of assembly, including restrictive amendments to the law on rallies, as well as restrictions to civil society activities.

Armenia has not adopted a national action plan on **human rights**. During 2008, the Armenian Human Rights Defender institution increased its range of activity and its independence. The Human Rights Defender has been active in reported cases of torture, on social issues, and in ensuring changes to the law on alternative military service and military service for minorities in line with CoE recommendations. The Human Rights Defender has also been empowered to deal with complaints from military staff.

By the end of the reporting period, Armenia had extended a standing invitation to all UN Special Procedures. However, the country had nine overdue reports of UN Treaty Bodies.

Cases of **torture and ill-treatment** were reported, including among military conscripts, in prison facilities and in police stations. Four criminal cases were opened in 2008, but no one has so far been convicted for offences related to torture and ill treatment. Armenia continued to take steps towards the implementation of the Optional Protocol to the Convention against Torture (OPCAT). In that respect the Human Rights Defender office of Armenia was awarded a grant of EUR 300,000 under the European Instrument for Democracy and Human Rights. The law on alternative service was amended in 2008 to ensure the civilian nature of the service but further amendments are still necessary in order to fully comply with CoE standards. Conditions in places of detention and the excessive use of pre-trial detention remain a source of concern, but efforts were made by the Government to improve the situation. Two prisons were reconstructed and refurbished in the course of 2008 contributing to the improvement of the conditions for inmates. The Ministry of Justice adopted a plan of action to support further reform of the penitentiary system. The European Committee for the Prevention of Torture and Inhuman or Degrading Treatment or Punishment (CPT) visited Armenia in March 2008. Armenia has not yet authorized publication of the report from the visit.

Concerns remain regarding the **freedom of expression**, in particular the continued lack of independence of the regulatory bodies and the insufficient pluralism in the media. The implementation of the law on freedom of information remains incomplete. In September 2008 the Armenian Parliament adopted legal amendments according to which the national

commission on television and radio (NCTR) will be unable to hold tenders for broadcasting licences until July 2010. In November 2008, the Government set up a new body tasked with monitoring and regulating the work of the local media outlets. Seven cases of violence and intimidation of journalists were registered in 2008. Further amendments improved the law on rallies adopted in March 2008 but there is room for additional legislative changes. Its proper implementation remains a matter of concern. In 2008 only few applications submitted by opposition forces were approved by the authorities.

NGOs are more frequently invited to participate in drafting legislation or to discuss legislative initiatives by governmental institutions. They also observe recruitment procedures for public administrations and in the elaboration of the new anti-corruption strategy. A formal procedure has been established to ensure continued involvement of all relevant stakeholders.

Some progress can be noted in the implementation of the national action plan 2004-2010 on "Enhancing Women's Status and Empowering Women in Society". The Law on **gender equality** is being revised. The draft law criminalizing domestic violence is under discussion. Police programmes were initiated to implement guidelines for police responsibilities in responding to domestic violence, but domestic violence is still widespread as Armenia lacks the capacity to prevent and effectively sanction domestic violence and protect its victims.

Armenia further decentralised the National Commission and regional departments on the rights of **Children**. However, the effectiveness of these institutions needs further improvement.

On **labour law and rights at work**, Armenia qualified for the special incentive arrangement for sustainable development and good governance, the GSP+ scheme, for the years 2009-2011, see section 4. The amendments to the Labour Code regulating rights of employees for strikes were developed by the Ministry of Labour and Social Affairs and submitted to the Government for approval. In April 2008 Armenia submitted its report on the application of the revised European Social Charter to Council of Europe on issues dealing with employment, training and equal opportunities.

Cooperation on foreign and security policy, conflict prevention and crisis management

Armenia aligns itself with **CFSP declarations** on a case-by-case basis. It has done so on most opportunities (more than 80%)¹. Armenia is cooperating with UN and NATO as well as with experts from the United Nations Office on Drugs and Crime (UNODC), INTERPOL, the World Customs Organization, CIS and CoE, in exchanging information on terrorism issues. Armenia cooperates successfully with the United Nations Counter-Terrorism Committee (CTC) established under SC Res.1373.

No progress has been made on the signature and ratification of the Rome Statute of the **International Criminal Court**.

Strengthening regional cooperation

Armenia participated in a programme on **integrated border management** in the Southern Caucasus (SCIBM), see section 5.

Armenia is participating in the **South Caucasus Anti-Drugs programme** (SCAD V) with the overall objective "to encourage the gradual approximation of drug policy legislation, norms and standards between Armenia, Azerbaijan and Georgia and between these countries and the EU", see section 5.

¹ Information from the Council Secretariat

The Regional Environmental Centre for the Caucasus (REC-Caucasus) became fully operational under its new charter with the approval of national representatives of the three Caucasus countries for the new executive body in December 2008. Armenia supported the establishment of its new management structure. The REC is an important tool to promote regional cooperation and stability for the future of South Caucasus.²

Armenia participates in the Black Sea Synergy regional cooperation initiative and participated in the **TRACECA** ministerial conference held in Baku on 4 December 2008 which took two important decisions: to link TRACECA to the South-Eastern Axis of the trans-European networks, and to strengthen the existing TRACECA structures.

Armenia supported the Turkish initiative of a **Caucasian platform for stability and cooperation**. While Turkey kept its land border with Armenia closed, the prospect of establishing bilateral relations improved following the visit of Turkish President Abdullah Gül to Yerevan in September 2008, upon the invitation of his Armenian counterpart.

Armenia maintained a neutral and constructive attitude towards the conflict in Georgia in August 2008.

Regional youth cooperation in the South Caucasus was carried out with the assistance of the Helsinki Citizens' Assembly within the framework of the South Caucasus Youth Network. Armenian-Azerbaijani youth peace brigades were set up in October 2008 to organize a peacekeeping process in South Caucasus.

Contribute to a peaceful solution of the Nagorno-Karabakh conflict

Although tensions are still high, some progress was made in the context of the resolution of the **Nagorno-Karabakh conflict**. The Presidents of Armenia and Azerbaijan held two meetings to negotiate a solution to the Nagorno-Karabakh conflict, in St Petersburg in June and in Moscow in November 2008. The two Foreign Ministers also met, including in the margins of the OSCE Ministerial Council in Helsinki in December 2008.

The meeting in Moscow in November resulted in the signing of a joint declaration on contributing “to the improvement of the situation in the South Caucasus by means of the political settlement of the Nagorno-Karabakh conflict”, “agreeing that the peace settlement should be accompanied by legally binding international guarantees of all its aspects and stages” and “considering important encouraging the establishment of conditions to realize measures on consolidating trust in the context of efforts on settlement”. This is the first jointly-signed document between the two countries since 1994. These developments complement the ongoing efforts for the peaceful resolution of the Nagorno-Karabakh conflict in the context of the OSCE Minsk Group.

3. ECONOMIC AND SOCIAL REFORM

Macroeconomic framework and functioning market economy

Macroeconomic development

After six years of double-digit non inflationary growth accompanied by large-scale foreign exchange inflows, GDP increased by only 6.8% in 2008. This was mainly the result of a sharp decrease in economic activity in the fourth quarter amid the deepening global financial and economic crisis. Growth slowed down significantly in the construction and chemical sectors.

² The REC charter, which was adopted in 2006, is one of very few documents signed jointly by government representatives of Armenia and Azerbaijan.

The metallurgical and diamond sectors contracted signalling the competitiveness problems of the Armenian economy. The food sector recorded considerable growth despite the difficulties in exporting conditions.

Inflation rose to an average 8.9% in 2008 on the back of the surge in the prices of fuel and food products some of which are subject to monopolistic pricing by a limited number of import companies. However, the inflation level remained relatively low compared with the other countries in the area. This was due to the tightened monetary policy, the moderate fiscal stance and the strong Armenian Dram which prevented imported inflationary pressures. This led, however, to reduction of foreign currency reserves. Credit expansion remained strong with the credit/GDP reaching 17.4% at the end of 2008. This could be the effect of the strong reserve money growth created by the foreign exchange rate intervention.

Fiscal discipline was maintained throughout 2008, due to better revenue performance, a surge in V.A.T. collection and some expenditure under execution. As a result, the fiscal deficit was close to 1.2% of GDP. A series of measures were presented in 2008 aimed at strengthening revenues and addressing the weaknesses in tax policy and administration, as the tax revenue to GDP ratio remains low. Measures have also been taken to improve the taxation environment for small and medium-enterprises in an effort to reduce the cost of doing business, to raise export potential and to facilitate the diversification of the production base.

Despite the surpluses in current transfers (e.g. remittances) and income accounts, the current account deficit deteriorated to around 12.6% in 2008 on the back of high oil and food prices and buoyant demand for imports. Export performance was also poor because of the decline in prices of many export products and the loss of competitiveness in diamond processing. The widening of the current account calls for accelerated structural reforms to diversify production, increase productivity and raise export potential.

The financial sector has not been severely affected by the financial crisis. Banking supervision has improved and the Armenia banks present satisfactory indicators concerning the profitability, capital adequacy and quality of their loan portfolio. Consumer protection has also improved. However, the limited access to external borrowing and the high interest rate margins are a constraint for future credit growth and for the deepening of financial intermediation. The lag in the growth of deposits compared to the recent strong credit expansion has also increased external financing which could become a source of potential risk. Armenian banks have also increased their mortgage portfolio, which makes them more vulnerable to fluctuations in property prices.

After the successful conclusion of the previous IMF-supported Poverty Reduction and Growth Facility (PRGF) in May 2008 and the marked reduction in poverty rates (currently around 25%), Armenia entered into a new IMF-supported PRGF which aims at enhancing Armenia's macroeconomic stability and economic performance and creating the conditions for further reductions in poverty.

Employment and social policy

Key framework laws regulating social and employment policy are in place in Armenia but the labour code and the legislation on employment and social protection in case of unemployment, on social assistance and on state pensions, remain to be fully implemented.

In October 2008, Armenia adopted, after public consultations, a **poverty reduction** strategy also known as the “Sustainable Development Programme 2008-2021” which followed upon the successful conclusion of the previous IMF-supported Poverty Reduction and Growth Facility in May 2008 and the marked reduction in poverty rates. The strategy aims to reduce poverty to 14% and extreme poverty to 2.1% by 2012. Moreover, the strategy foresees several

reforms by 2010 to curb the shadow economy and to liberalize hiring and working conditions. According to the national statistical service, 25% of the population live below the poverty line and 4% are in extreme poverty.

The Ministry of Labour and Social Affairs is implementing, in cooperation with donor organizations, programmes aimed at improving the administrative capacity of the State **Employment** Services. In December 2008, more than 90.000 people were officially registered as unemployed (6.3%) with a large share (20%) of young people.

As regards **social dialogue**, the Ministry of Labour and Social Affairs is developing draft state collective agreements in cooperation with social partners. Furthermore a working group gathering representatives of the Government and social partners was established in May 2008 with a view to reflect on the establishment of a tripartite committee. Armenia continued implementing its Decent Work Country Programme for 2007 - 2011, with the assistance of the International Labour Organisation.

With respect to **social inclusion and protection**, Armenia raised pensions by about 60% as of January 2008. The Government approved in December 2008, after consultations with the international financial institutions, a white paper on pension reform. The system foreseen introduces a mandatory cumulative pension insurance system based on the development of pension funds by 2010.

The National Council on **Sustainable Development**, which was established in 2002 but which had remained inactive, was activated in 2008 and held two meetings, with enhanced participation of civil society. Armenia also designed an action plan to implement a Sustainable Development programme for the years 2009 - 2012. The Ministry of Economy is in charge of implementing and coordinating the measures contained in the action plan.

The implementation of the **Agricultural Sustainable Development Strategy** is on-going and upgrading of rural infrastructure is continuing with strong support by international donors and the Armenian Government.

4. TRADE-RELATED ISSUES, MARKET AND REGULATORY REFORM

In 2008 the EU exports to Armenia continued to grow (year-on year growth of 10,6%) while export of Armenian products to the EU decreased by 10,2% contrary to the general trend of the last five years (average annual increase of 18.6 %). The EU has progressively become Armenia's main trading partner (a 38.5% share in Armenia's overall external trade in 2007, before Russia with a 15.8% share). Nevertheless **bilateral trade** remains very low in volume and insufficiently diversified in commodity structure, in particular as regards Armenia's exports. Under the EU Regulation concerning the application of the Generalised System of Preferences (GSP) in 2006-2008 Armenia benefited from the general arrangement of the GSP while under the new GSP Regulation for 2009-2011 Armenia qualified in December 2008 for the special incentive arrangement for sustainable development and good governance (GSP+).

In May 2008 the Free Trade Agreement (FTA) feasibility study on a possible future EU-Armenia FTA foreseen in the ENP Action Plan was finalised. The study concluded that a genuinely deep and comprehensive FTA (DCFTA) would be economically beneficial for Armenia, but that Armenia was not yet ready for such a far-reaching liberalisation. Following the results of the study, a preparatory process aiming at creating the necessary conditions for a DCFTA in Armenia was launched. During the reporting period Armenia achieved some progress in its preparations for a possible future DCFTA but Armenia still needs to make additional progress in several key areas which are essential for a launch of such negotiations. With the aim of accelerating the preparatory process and assess which priority reform steps

Armenia needs to take to become ready for starting DCFTA negotiations, the European Commission carried out a fact-finding mission to Armenia after the reporting period, in February 2009.

In August 2008, the State Tax Service and the State **Customs** Committee were merged and a new state body called the State Revenue Committee (SRC) was established. The SRC is responsible for state budget revenue collection and tax and customs administration. A new council in charge of overseeing the implementation of wide scale reforms in the tax and customs administrations to be chaired by the Prime Minister was created in June 2008. The SRC initiated a long awaited trade facilitation reform process. A comprehensive Customs Administration Strategy for 2008-2012 based on the Commission's recommendation and on the EC Customs Blueprints was approved by the Chairman of the SRC. In August 2008 Armenia adopted some amendments to the Customs Code, introducing *inter alia* new provisions on rights and responsibilities of customs brokers, customs control, simplifications of customs clearance, the introduction of the selectivity channels for border crossing points other than the airports, delayed payment and bank guarantee mechanism. The extension of the use of self-declaration and on-line declaration has obviously a positive effect on the reduction of corruption as well as on the implementation of WTO compatible customs valuation rules. Authorities encouraged the use of customs brokers to lodge customs declarations, and facilities for customs brokers and self-declaration by operators were created in several customs houses and customs warehouses. Measures were taken to reduce delay at some customs points. The procedure of calculation via the Trade World Manager (TWM) system, and the payment of customs duty were simplified. The duty is calculated automatically, thus reducing the number of documents and the contacts of operators with customs officials. Efforts were made to improve the representation of the private sector and other stakeholders within the consultative group under the Chairman of the SRC, and thus its transparency. To ensure transparency, the official Internet website of the customs authority was improved including by allowing on-line questions/requests. A hot-line was set up in April 2008 to collect proposals for improvement of the customs services and to receive complaints. A new code of ethics, based on the Arusha Declaration and on the experience of different developed countries, was adopted in 2008. The SRC has organized a number of staff trainings in foreign languages, IT, and specific topics of customs legislation. Armenia has to complete the strategic modernization of its customs administration and ensure that specific and important functions of customs are not compromised as a consequence of the merger with the tax administration into one entity – the SRC. Armenia should also continue developing a risk analysis system, in particular post clearance and audit functions, take measures to implement important international instruments on customs, take steps to abolish customs administrative fees and improve verification of customs value in line with WTO standards.

On the **free movement of goods and technical regulations**, Armenia continued the progress with regard to the adoption of the EU's regulatory and standards system. Laws on standardisation, conformity assessment, accreditation and metrology are under preparation. There was some progress in transposing sectoral EU directives and in adopting international standards. Strategic review of necessary quality infrastructure reforms is on-going. Overall, more progress in translation of relevant EU standards, approximation of the legislation, building of quality infrastructure and strengthening of human resources is necessary. Such progress could allow for considering opening of negotiations of an Agreement on Conformity Assessment and Acceptance of Industrial Products (ACAA) in a long-term perspective.

Regarding **sanitary and phytosanitary** issues, Armenia adopted implementing legislation, continued the preparations of a draft veterinary law and strengthened institutions including the capacities of laboratories. In order to fulfil the objectives of the Action Plan and to be able to

increase exports to the EU, Armenia will have to progress considerably in the sector. Armenia participated in workshops under the European Commission's "Better training for safer food" programme.

Armenia developed a comprehensive programme to improve the **business climate**. In September 2008, the Government adopted a concept paper aiming to develop Armenia into a centre of excellence for business and investment environment. The paper gives recommendations for reforms to be implemented within 18 months, such as reducing administrative procedures, ensuring regulatory awareness, and improving the administration of implementation of legislation. The entry into force in January 2009 of the law on Consumer Crediting contributes to further protecting consumers' rights in the financial sector and improving the overall business climate. The law on the Financial Ombudsman was adopted in September 2008. The Ombudsman's activities started right after the reporting period, in January 2009.

Armenia developed and presented a comprehensive review of barriers to **establishment** with the support of AEPLAC (Armenian-European Policy and Legal Advice Centre). As regards **company law**, the Law on Bankruptcy was amended in December 2008. Armenia also continued simplifying the registration of companies and plans to put in place a one-stop shop. The Government is also working to reduce the number of activities requiring licences. The corporate governance code is still at a drafting stage. Armenia elaborated a matrix of proposals on strengthening the efficiency and reliability of its company law system and plans to revise it. Although the public register of companies is available, an official national Gazette is still absent. Transparency should be improved. Furthermore, the Sustainable Development Programme, see section 3, contains a number of provisions to ease establishment and registration of company.

Armenia continued to progress in the field of **financial services**. The Central Bank of Armenia acts as the single supervisory authority for financial services since 2006. Work for the adoption of the regulatory framework to implement the Basel II principles for effective banking supervision (as adapted to the Armenian reality) continued. Amendments were introduced to the second Regulation of the Central Bank aimed at making the management of risks, such as the price risk, the interest rate risk, and the exchange risk, more flexible and effective. Armenia started implementation of the 2007 law on insurance and the law on securities.

Other key areas

The Government's **tax** reform programme is comprehensive but will need to incorporate additional elements and suggestions from IMF to comply with international and EU standards. The Unified Tax Code remains to be adopted. A package of draft laws on improving taxation environment for SMEs was adopted by the Parliament during the autumn session 2008. Amendments were made to the laws VAT, taxes, profit tax, income-tax. According to the law on accounting, business with a turnover up to 100 M ARD (EUR 175.000) will be subject to a simplified form of taxation. The definition of this simplified taxation has not yet been agreed. Further amendments to the tax legislation are currently being drafted, mainly aimed at facilitating SME operations. In order to comply with WTO obligations, since January 2009 VAT is applicable also to the agricultural sector, with a minimal threshold of 58 M ARD (EUR 102.000). The Government adopted a Tax Administration Strategy Paper 2008-2011 in August 2008. The main goals of the Strategy are: consistency and timeliness of large taxpayers taxation, effective "soft" tax administration towards small businesses, addressing corruption, voluntary compliance, new policy of tax audits, new management system for tax agency and tax administration, computerization. An action plan with timeframes and

indicators of achievement was adopted and risk factors identified. Work to further improve the tax administration in line with the Commission's fiscal blueprints is on-going with external support. Based on a new definition, large taxpayer files were transferred to the Large Taxpayer Inspectorate which was created by merging the four existing sectoral tax inspectorates. In order to enhance transparency, all sessions of the Appeals Commission of the State Tax Service (STS) are now open to the public. Progress was made concerning VAT refunds, in terms of re-absorption of the existing backlog.

With regard to **competition policy**, the legal and institutional framework is relatively well established although not yet fully harmonised with EU regulations. The State Commission for the Protection of Economic Competition (SCPEC) acts as an independent agency. However, its inspection powers remain limited. The main challenges remain effective enforcement of regulations, adequate human resources and capacity of authorities to address the problems of monopolies and oligopolies. The 2007 amendments to the law on "protection of economic competition" reported on last year, were implemented and the SCPEC is now empowered to control the state aid. The implementation mechanisms are yet to be defined.

In the area of **intellectual property** rights, the Parliament adopted in June 2008 the law on inventions and design as well as the law on trade names which entered into force in January 2009. No development took place as regards the ratification of the International Convention for the Protection of New Varieties of Plants (the UPOV convention). While the criminal code has been strengthened (up to 2-years imprisonment), enforcement of IP remains a challenge mainly due to the insufficient training of lawyers and judges and the lack of trust in the judicial system. Customs and police do not benefit from ex officio powers.

The Government adopted in June 2008 the secondary legislation to the Law on **public procurement** which entered into force in September. Further to the review of compliance of national legislation with EU standards carried out by the OCDE (SIGMA) in December 2008 and to the World Bank assessment of their law, Armenia is elaborating a new strategy on public procurement. Proposals to enhance the administrative capacity of the Procurement agency are currently being discussed at governmental level. Armenia is also reviewing its complaint system in order to move it from the Ministry of Finance to an independent appeal board. Finally, Armenia is working closely with the World Bank on its e-procurement strategy.

Armenia completed preparations for the global **statistical** assessment foreseen in the first half of 2009 but lacks modern IT equipment. Armenia also continued its work to approximate its statistical system with EU standards.

As regards **accounting and auditing**, translation of International Financial Reporting Standards (IFRS) continued in view of their full application by the end of 2009. Banks apply IFRS since the beginning of 2009. Other financial institutions such as credit organisations, insurance and investment companies will introduce International Accounting Standards (IAS) from January 2010. The official translation of IFRS is planned to be conducted by the Official Translating Committee for standards, which is currently being established. The Ministry of Finance is also preparing legal reforms in order to ensure provisions in the legislation that will allow the companies to prepare their financial statements according to the IFRS, before 2010. To this end, the Ministry of Finance negotiated an agreement on a copyright waiver on IFRS with the International Accounting Standards Bureau (IASB/IASCF) at the end of 2007. A Committee on accounting and audit reforms has been established with the aim of developing a strategy and find mechanisms to keep standards up to date. Armenia is also reflecting on the establishment of an independent regulatory body for accounting and auditing, separate from the Ministry of Finance.

In the area of **public internal financial control**, Armenia continued to work on an internal audit law. The draft law includes provisions for establishing a central harmonisation function for internal audit. Introduction of the principles of managerial accountability are still at very early stages.

On **enterprise policy**, the Small and Medium-size Enterprise Development National Centre (SME DNC) continued to be the main agency for financial support to SMEs, stimulation of economic activity and development of business opportunities in Armenia. The Ministry of Economy is also working on a financial support programme targeted at SMEs and based on equity financing. Initial steps were also taken to introduce the concept of public private partnerships and develop an Action Plan. Since June 2008, Armenia is part to the European SME network.

5. COOPERATION ON JUSTICE, FREEDOM AND SECURITY

Armenia participates in the Southern Caucasus Integrated **Border Management** (SCIBM) regional programme, agreed between Georgia, Armenia and Azerbaijan in October 2007. The programme aims at enhancing inter-agency cooperation while strengthening the capacity of customs and border guard services in line with agreed regional standards and EU norms. The implementing consortium, led by United Nations Development Programme (UNDP) was selected by year end to start implementation in early 2009.

In the area of **migration**, a law on Refugees and Asylum was adopted in November 2008 aiming at the approximation of national legislation on asylum and refugees to international and EU standards. TAIEX supported the elaboration of a national action plan on migration and asylum issues and a seminar on international law on refugees in Yerevan in November 2008. No progress was made with regard to an electronic database for the monitoring of migration flows. In July 2008 Armenia prepared a draft law on the regulation of labour migration.

Armenia has yet to accede to the Third Protocol to the United National Convention against **Transnational Organized Crime** on the illegal manufacture and trafficking of firearms. In addition to the ratification and implementation of the Convention, further efforts are also required to ensure full and effective operational implementation of the two Protocols previously ratified.

On the **trafficking in human beings**, the anti-trafficking commission received ministry status at the end of 2007, and became responsible for the implementation second two-year national plan of action on trafficking (2007-2009). Armenia ratified in April the Council of Europe Convention on Action against Trafficking in Human Beings which entered into force in August 2008. The Anti-Trafficking Commission developed draft guidelines on assisting victims of trafficking. The national plan of action identified the Ministry of Labour and Social Affairs as the host agency for a victim-support resource centre. In 2009, for the first time, the state budget includes provisions for the financing of anti-trafficking activities including the operation of special shelter for victims in cooperation with civil society actors.

With regard to the fight against **drugs**, amendments to the criminal code in June 2008 provided legal definitions of the amounts and volume of narcotics trafficked which are subject to criminal sanctions. However, in the absence of a comprehensive national anti-drugs strategy, balancing preventive and punitive measures and including adequate civil society and international input, an intensification of legal sanctions will not yield the expected results. Armenia continues its active participation in the SCAD V programme which should assist in developing national demand reduction measures while encouraging regional cooperation with its neighbours on supply reduction and other law enforcement issues.

In June 2008, Armenia ratified the Council of Europe Convention on the Laundering, Search, Seizure and Confiscation of the Proceeds of Crime and on the Financing of Terrorism (CETS 198) which entered into force in domestic law in October 2008. In May 2008, the National Assembly passed the new “Law on Combating **Money Laundering** and Terrorism Financing” and vested the Central Bank with the legal authority to coordinate the national policy. Amendments to the Administrative Codes, adopted in September, included additional sanctions in relation to non-disclosure of financial reports by foundations and other non-profit actors and in relation to obstruction of the control and checking functions of mandated state bodies. The continuing development of human and technical resources with regard to money laundering, corruption and financing of terrorism remains an on-going challenge.

Regarding **police and judicial cooperation**, the Second Protocol to the European Convention on Mutual Assistance on Criminal Matters was signed after the reporting period, in March 2009. The 1980 Hague Convention on Civil Aspects of International Child Abduction remained un-ratified. In this regard, further improvements in cooperation and coordination between the police and other law enforcement agencies are necessary. Provision of adequate resources for such training should be addressed as an immediate priority. Armenia is a signatory to 1993 CIS Minsk Convention on Legal Assistance and Legal Relations in Civil, Family and Criminal matters. Armenia signed but did not yet ratify the 1997 Additional Protocol to the Council of Europe Convention on the Transfer of Sentenced Persons.

6. TRANSPORT, ENERGY, ENVIRONMENT, THE INFORMATION SOCIETY, RESEARCH AND DEVELOPMENT

As regards the **transport** administration’s capacity, a special department ("transport inspectorate") was created within the ministry of transport to deal with licensing, mostly of taxi drivers and minibuses; however driving licenses are still granted by the road police. Driving schools were privatized in 2008.

During 2008, Armenia strengthened public transport by deciding on the construction of a number of new subway stations in Yerevan. In the road sector, Armenia started in April 2008 to prepare a National Road Safety Strategy and a five year action plan to commence implementation of the National Road Safety Strategy under a project that sets out to improve the institutional structures and processes for managing traffic safety in Armenia.

In the rail sector, the rehabilitation of the Yerevan-Tbilisi railway line was launched in mid-October 2008. Armenia has prepared a feasibility study for the possible construction of a railway to Iran (the railway would cover a distance of about 540 km, of which about 480 km would be in Armenia). The Armenian railways have been reorganized by transferring freight and passenger operations to concessionary management. The contracts were signed in February 2008 and operations started in June 2008. The concession was given for 30 years, with an option for a further extension of 10 years after the first 10 years. All infrastructures remain state-owned, but the rolling stocks are offered for privatization. The concession agreement states that the concessionaire will have to invest at least EUR 0.5 billion in the network.

Air traffic between the EU and Armenia, although increasing, remained limited due to restricted competition. An important step towards closer relations was the signature of the horizontal air transport agreement between Armenia and the European Community in December 2008. Armenia should continue the process of harmonisation with EU standards in the field of aviation safety and start the harmonisation of licensing rules. A twinning project focusing on the implementation of the JAA (Joint Aviation Authorities) recommendations is

being finalised, more specifically targeting the preparation for deepening relations of Armenia to the European Aviation Safety Agency (EASA).

Armenia further implemented its **energy** strategy *inter alia* through the completion of a feasibility study on a new nuclear power plant. Armenia plans to close the Medzamor Nuclear Power Plant (MNPP) by 2016 and is prepared to close the plant before the designed lifetime provided that alternative replacement capacity is available. The EU asks closure before this date. In 2008 Armenia pursued safety upgrades at MNPP and strengthened the nuclear regulatory authority. In September 2008, the third coordination meeting on the MNPP safety upgrading programme took place in Yerevan with the involvement of the International Atomic Energy Agency and donors. The Russian Federation joined this upgrading programme. The Nuclear Regulatory Authority further developed a spent nuclear fuel and radioactive management strategy. Armenia advanced on the construction of a dry spent fuel storage facility. On the basis of the 2007 MNPP decommissioning strategy, Armenia started the preparation of a detailed decommissioning plan. It continued to provision the Nuclear Decommissioning Fund and initiated, jointly with the Russian Federation, a new assessment of uranium reserves.

Armenia adopted implementing legislation in the electricity and gas sectors. It pursued the construction of conventional electricity generation units (including hydro) and the rehabilitation of electricity and gas infrastructure. Armenia, which is interested to develop a regional electricity market, continued reflections on additional electricity interconnections with Iran and Georgia. Armenia stopped gas price subsidies as from May 2008. Armenia and Iran started the construction of a second gas pipeline between them. Armenia worked on the expansion of underground gas storage facilities. It pursued reflections on the construction of an oil refinery. Armenia initiated the development of an action plan on energy efficiency and renewable energy. It continued participation in the regional “Baku Initiative” for EU-Black Sea/Caspian energy cooperation.

Armenia continued preparing its second national communication on **climate change**, which will also include a greenhouse gas inventory, a climate strategy, legislation, and national adaptation measures. An assessment of vulnerability and adaptability of the Marmarik river basin was carried out. Armenia took steps to prepare and approve Clean Development Mechanism (CDM) projects, as well as to address their shortcomings. Four of the 16 Armenian CDM projects have been registered at the UN level. The European Commission continued to support Armenia to implement the Kyoto Protocol. Armenia has not yet adopted a formal position regarding the post-2012 regime.

Armenia adopted its second national **environment** action plan for 2008-2012. The sustainable development programme, see section 3, contains some objectives with regard to the environment. The legislative framework continues to require further development, in particular as regards implementing legislation. Amendments were adopted to laws on flora and fauna, as well as Government decisions on specially protected areas, hunting, waters, natural monuments, air pollution, Lake Sevan and its national park. An act on environmental protection as well as legislation on environmental expertise, genetically modified organisms and self-monitoring of compliance are still under preparation. No issue-specific strategies or plans were adopted during 2008. A draft national profile of chemicals and waste management, as well as a national strategy to reduce impacts of chemicals are under preparation. Work is on-going to develop and implement existing strategies and plans, but continued attention is required. Efforts are also needed to enhance monitoring as well as enforcement.

Further strengthening of administrative capacity at all levels of the country is still a major challenge. Coordination between authorities requires attention. Some activities took place to

integrate environment considerations into other policy sectors such as energy. Armenia has not published reports on the state-of-the environment lately. Concerning access to information and public participation, an inter-ministerial commission on implementation of the Aarhus Convention on Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Matters met for the first time in December 2008. Armenia's Aarhus Centres continue to be operational. Procedures and consultation with the public in the context environmental impact assessment however continue to require particular attention. Some steps were taken to promote implementation of strategic environmental assessment. For the Regional Environmental Centre for the Caucasus, please see section on regional cooperation.

Armenia is preparing for the ratification of the Protocol on Strategic Environmental Assessment to the UNECE Convention on Environmental Impact Assessment in a Transboundary Context. It did not however make significant progress in signing the UNECE Convention on the Protection and Use of Transboundary Watercourses and International Lakes. Furthermore, the implementation of several already ratified agreements requires particular attention. Armenia participated in the EU Water Initiative, including a national policy dialogue. Cooperation and information exchange took place between the European Commission and Armenia, including on water, forestry, waste management, and environmental data. Other topics, such as air quality and civil protection were identified for possible closer cooperation.

Armenia has not yet developed a national policy for the development and use of **Information Society** applications. There is a need to strengthen the administrative capacity of the "Public Services Regulatory Commission" with a view to ensuring a fully functioning independent regulatory authority in the field of electronic communications. Competition in the markets increased when in October 2008 a third GSM license and a licence for Third Generation mobile services (3G) were issued. Three licenses for Internet telephony were awarded in March 2008. Furthermore in April 2008, about 30 licenses for fixed communications services were issued. In August 2008, the fixed network operator Armentel was fined about 1 million US dollars by the State Commission for Protection of Economic Competition for abuse of its dominant position in the Internet market: Armentel created favourable conditions for its Internet service "Hi-line" by refusing to lease lines to the competitors. It has digitalized the network by 80% and intends to expand the current fibre optic network by 100% in 2009.

In the **audiovisual** sector, the fact that Armenia still has to ratify the Council of Europe Convention on Transfrontier Television makes it still very difficult for Armenia to ensure freedom of reception and retransmission of television broadcast coming from other countries. Armenia adopted a national plan in the audio-visual field that sets out some of the legislative requirements required in order to approximate to EU legislation. In June 2008, the European Court of Human rights held unanimously that Armenia had violated Article 10 (freedom of expression) of the European Convention on Human Rights because of the authorities' refusal to grant the applicants' requests for broadcasting licences.

As regards **research and innovation** activities, Armenia's research capacity and investments remain very modest. Participation in the 7th Research Framework Programme (FP7) increased in comparison to FP6. Main progress was achieved under 'Marie Curie' actions and R&D capacity development (Research Infrastructures). However, the overall number of applications is still comparatively low. The participation of the Armenian Centre of Ideas and Technologies in the IncoNet EECA (the S&T International Cooperation Network for Eastern European and Central Asian countries), launched in January 2008, allows Armenia to potentially benefit from on-going regional cooperation activities.

7. PEOPLE-TO-PEOPLE CONTACTS, EDUCATION AND HEALTH

A draft General Education Reform Programme for the period 2008-15 is still to be adopted, aiming to enhance and improve educational provision at all levels and promote life long learning within a context of a commitment to increase public expenditure on **education** in the coming years. In this regard, attention will need to be given to developing adequate mechanisms to address issues of access and equitable financing as well as targeted policies to promote early child education and tackle the high rate of school drop-out. Additional measures will be needed to improve governance and accountability and tackle corruption within secondary and tertiary education while integration of civic and human rights into the curriculum would be advised.

On **higher education**, a task force was set up in November 2008 to prepare for the establishment of a National Quality Assurance Centre in line ENQA standards and Bologna principles. A draft legislative proposal was presented to the Parliament in the autumn session. In September 2008, Armenia hosted a conference on qualifications frameworks in cooperation with the Council of Europe which was attended by representatives from Moldova and Ukraine. Furthermore, Armenia participated in a Council of Europe Bologna Process conference on the European qualifications frameworks and the issue of self-certification in Georgia in November 2008. Armenia became a full member of the European Quality Assurance Register (EQAR) in March.

Armenia participated actively in the Tempus programme, benefiting from four projects under the first Call for Proposals of Tempus IV. The Ministry of Education and Science selected four Higher Education Reform Experts (HERE) in cooperation with the European Commission as part of Tempus actions for the period 2008-10 in order to effectively promote higher education reforms.

Seven Armenian students and two scholars benefited from Erasmus Mundus scholarships under Erasmus Mundus. Armenian students and academic mobility was facilitated under the External Cooperation Window. In addition, twelve Armenian students received scholarships in European integration studies at masters level for students from the ENPI region under a special pilot project for the academic year 2008-9.

With regard to **vocational education and training**, the VET Task Force of the Ministry of Education and Science with EC assistance, selected 12 colleges as regional multi-functional VET centres for delivery of new competence-based curricula in line with labour market needs. A National Centre for VET Development was established under the auspices of the National Institute of Education which in February 2008 adopted a decision on approving the charter, structure and functions of the Centre. A decree on the establishment of a new tripartite National VET Council was adopted in December 2008. The Council met for the first time that same month. Work continued on social dialogue and the development of competence-based qualification standards while a draft law on adult education was also prepared. However, further energy needs to be invested to transform vocational training in order to attract and supply a qualified and competent workforce adapted to international competitiveness. This is as much an issue of structural and attitudinal change as it is of resource mobilization.

In 2008, the European **Youth** Foundation in cooperation with civil society actors organized education and information seminars for youth and funded a number of projects focusing on topics such as the Presidential elections, intercultural dialogue, gender, peace and conflict resolution. Under the Youth in Action programme, several youth projects involving Armenian young people and youth workers were supported, including a project on youth, peace and

media, which was organized in July 2008. The Ministry of Sports and Youth Affairs also actively supported youth dialogue and initiatives.

The Ministry of **Culture** developed a four year Culture Development Strategy (2008-12) focusing on effective coordination of cultural policy, cultural heritage, international cooperation, digitalisation of non-material culture and promotion of popular culture. Armenia still has to ratify the UNESCO Convention on the Protection and Promotion of the Diversity of Cultural Expressions. Attention would need to be directed at facilitating effective decentralization of cultural policy while ensuring maximum civic and youth participation in the strategy's implementation.

Armenia continued **health** sector reform *inter alia* by improving primary health care and health insurance. The Government increased, under its 2008-2012 programme, state financing for the sector. The Armenian objective, as reflected recently in the Sustainable Development Programme, is to reduce informal payments, improve quality and enhance access to health services. Armenia prepared a Healthcare Law, which is yet to be adopted. Armenia continued to put emphasis on combating communicable diseases including HIV/AIDS and tuberculosis. Like in 2007, the country participated in the EU Network of competent authorities in health information and knowledge.

8. FINANCIAL COOPERATION – 2008 KEY FACTS AND FIGURES

The ENPI financial envelope for Armenia under the National Indicative Programme 2007-2010 is EUR 98.4 million. The programme is geared towards supporting the achievement of key policy objectives as outlined in the EU-Armenia ENP Action Plan and pursues three priorities: Support for strengthening of Democratic Structures and Good Governance, Support for Regulatory Reform and Administrative Capacity Building, Support for Poverty Reduction Efforts.

In 2008, the European Commission continued to support the national reform efforts in Armenia and programmed assistance for a total amount of EUR 24 million under the ENPI. The 2008 Annual Action programme included a sector budget support operation on Support to Justice Reforms.

Twinning and TAIEX offered flexible interventions specifically geared towards support to the implementation of the ENP Action Plans in the field of institution building and legislative approximation. Twinning projects on Support to the Human Rights Defender's Office, and Support to the Department of Foreign Economic Cooperation and Investment were launched in 2008. A third twinning project on Strengthening the Capacity of the General Department of Civil Aviation was prepared and will be launched in 2009. SIGMA missions in 2008 have identified public procurement and civil service reforms as areas for future SIGMA interventions.

Sector budget support for Vocational Education and Training under the Annual Action Programme 2007 was satisfactory. Overall, Armenia presents a satisfactory commitment to the EC assistance and presents good absorption capacity for the EU funding.

Armenia also benefits from cooperation activities financed under the ENPI multi-country (including the Neighbourhood Investment Facility), regional programmes, as well as horizontal thematic programmes, such as the European Instrument for Democracy and Human Rights and the programme "Non State Actors and Local Authorities in Development". In 2008 the EC Delegation contracted EUR 1.5 million under NSA and Local Authorities in Development (2007 budget) and EUR 1.2 million under EIDHR CBSS (combined 2007 and 2008 budgets).

Armenia participates in the Black Sea CBC Sea Basin programme (EUR 17,306 million for the whole programme in the period 2007-13) which was adopted in 2008. Through this programmes the populations of the maritime regions bordering the Black Sea will receive funding for joint co-operation projects aimed at fostering sustainable development and enhancing human contacts.

Further support, amounting to EUR 7.2 million, was provided within the Action Plan 2007 under the Instrument for Nuclear Safety Cooperation, as the EC continued to assist in ensuring minimum safety standards for the Medzamor Nuclear Power Plant (2006 budget).

Within the Armenian Government, the Ministry of Economic Development is responsible for the coordination of EC assistance and for the coordination among donors.