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**COMMUNICATION FROM THE COMMISSION
TO THE EUROPEAN PARLIAMENT AND THE COUNCIL
Taking stock of the European Neighbourhood Policy (ENP)**

Implementation of the European Neighbourhood Policy in 2009
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 approved in November 2006 for a period of five years.

EU-Armenia meetings took place at the level of the Cooperation Council, Cooperation Committee, and the subcommittee on Trade, Economic and related Legal matters. The strengthening of the EU Delegation in Yerevan, established in 2008, further facilitated the enhancement of EU-Armenian bilateral relations. The first meeting of the EU-Armenia Human Rights Dialogue took place in December 2009.

This document reports on progress made on the implementation of the EU-Armenia ENP Action Plan between 1 January and 31 December 2009, although developments outside this period are also taken into consideration when deemed relevant. It is not a general review of the political and economic situation in Armenia. In addition, for information on regional and multilateral sector processes, please refer to the sectoral report.

The EU and Armenia agreed to move forward with deepening and broadening of the EU-Armenia relations. In parallel and within the Eastern Partnership framework the EU started preparations for upgrading contractual relations with Armenia. Negotiating directives for an Association Agreement were adopted by the EU in May 2010. In the framework of the future Association Agreement, negotiations on a deep and comprehensive free trade area (DCFTA) will start once the necessary conditions have been met.

The EU Advisory Group to the Republic of Armenia started its activities in April 2009 with the aim of supporting the Armenian authorities in the implementation of the key areas of the ENP Action Plan such as strengthening democratic structures and human rights, anti-corruption, trade and customs, and fiscal policy including debt management.

Overall, Armenia made progress in several areas of the ENP Action Plan. The launching of a regular human rights dialogue with the EU constituted good progress in the area of political dialogue with the EU. Positive steps were taken to address the internal political crisis following the aftermath of the Presidential elections in February 2008, including the Amnesty issued in June, the amendments to the Criminal Code and the publication of the report by the Parliamentary *Ad Hoc* Inquiry Committee. Good progress was made regarding improving the legislative framework in the area of anticorruption and strengthening the role of the Human Rights Defender.

The global economic crisis had a deep impact on Armenia, and led to a significant economic regression. Overall, the authorities acted rapidly to adopt measures to mitigate the effects of the crisis. However, the reduction of state revenues put some restraints on the overall internal economic and social reform process in Armenia, including the implementation of the ENP Action Plan.

Progress was made in the area of customs and taxation. Armenia continued to implement reforms in the fields of financial services and competition policy. Limited progress was noted on key reforms recommended by the EU and endorsed by the Armenian authorities after a fact-finding mission in the context of preparations for the DCFTA negotiations. With

substantial additional efforts on its side, Armenia would become prepared for the start of the DCFTA negotiations.

Armenia took a major step in regional cooperation and dialogue with Turkey, resulting in the historic signature of the two protocols on the establishment and development of bilateral relations in October 2009. In April 2010, Armenia suspended the ratification procedure of the two protocols. The EU was pleased to note Armenia's continued commitment to pursue the process of normalization of Armenian-Turkish relations but at the same time expressed concern about the loss of momentum in this process. Regarding dialogue with Azerbaijan, negotiations on a peaceful resolution of the Nagorno-Karabakh conflict intensified considerably at the highest level.

Armenia widely aligned itself with CFSP declarations and is generally very active in cooperating on CFSP-related issues.

The Armenian authorities and civil society representatives participated actively in the multilateral framework of the Eastern Partnership, in particular through open dialogue and their contribution to the working programmes for the four thematic platforms. Together with the bilateral elements of the Eastern Partnership, this contributed to the overall strengthening of EU-Armenian relations and reinforcement of the follow-up on the priorities of the ENP Action Plan.

In order to fulfil the Action Plan commitments, Armenia needs further efforts to ensure thorough follow-up of the recommendations of the report by the *Ad hoc* Parliamentary Inquiry Committee on the events of March 2008, improve electoral standards and strengthen media freedom. In addition, further reforms in the justice sector and the area of the rule of law, notably the independence of judiciary, the reform of the Prosecutor's office and proper implementation of adopted legislation in all areas will be of key importance. Enhanced dialogue between the ruling political forces and the opposition would contribute to the democratic development of the country.

2. POLITICAL DIALOGUE AND REFORM

Democracy and rule of law

The first **elections** to appoint the Mayor and Council of Elders of the City of Yerevan were held in May 2009. The Council of Europe (CoE) Congress of Local and Regional Authorities concluded that while the organisational framework of the elections had been broadly in compliance with European standards, the improvement of the electoral conduct and of a genuinely democratic culture remained unaddressed by the authorities. Media coverage in the period leading to the elections was overall balanced but irregularities during the conduct of the elections occurred, including pre-election violence, instances of ballot stuffing, multiple voting, and voter intimidation. The opposition boycotted the newly elected Council of Elders.

The authorities took a number of steps to address the political crisis linked to the 2008 Presidential elections and the subsequent violent events of March 2008. An amnesty was adopted by the National Assembly in June 2009, which impacted on a large majority of cases related to the March 2008 events. The Parliamentary Assembly of the Council of Europe (PACE) welcomed the amnesty while expressing concern over the charges and sentences based solely on police testimony, without substantial corroborating evidence. The amnesty released a large majority of persons related to the March 2008 events but some persons

detained on charges linked to these events still remain in detention. Amendments to the Criminal Code relating to mass disorders and usurpation of power were adopted in March 2009 in line with recommendations from the CoE's Venice Commission.

In June 2009, as a result of significant tensions between its members which included the opposition and the Human Rights Defender, the President decided to dissolve the Fact-Finding Group on the March 2008 events after the publication of its report. In September 2009 the *Ad hoc* Parliamentary Inquiry Committee on the events of March 2008, boycotted by the opposition, submitted its final report to the National Assembly. While the report was considered by PACE co-rapporteurs as presenting a largely one-sided description of events, it provided a comprehensive set of recommendations, including urging the authorities to step up efforts to identify and prosecute the individuals responsible for the deaths. More efforts need to be made by the authorities to follow up the implementation of the report's recommendations.

The monitoring of trials related to the March 2008 events identified various shortcomings regarding the right to a fair trial and the right to liberty, including excessive use of pre-trial detention, the lack of impartiality and independence of judges, the use of incriminating police testimonies and of unlawfully obtained evidence, and holding of a number of trials in absentia. Four police officers involved in the March 2008 events were sentenced in December 2009. The investigations into the 10 deaths have not led to any indictments yet.

Reforms of the **judiciary**, including amendments to the Judicial Code, Law on Procuracy and law on Academy of Justice continued in 2009. A Strategic Action plan for the implementation of judicial reforms 2009-11 was adopted in April 2009. Good progress was made with a considerable increase in judges' salaries in 2009. However, the independence of judiciary remains of concern and further efforts should be made to strengthen it. Overall, more efforts are needed to ensure the proper enforcement of legislation in all areas. The domestic protection of the right to property remains of concern, with the majority of cases currently pending against Armenia before the European Court of Human Rights relating to alleged violations of the right to property. The EU provides considerable support in the area of justice reforms through a sector budget support programme for Justice Reforms (EUR 18 million) and a joint project with the Council of Europe on enhancing Access to Justice (EUR 4 million).

Important steps were taken to improve the legislative framework in the area of **anti-corruption**. An Anti-Corruption Strategy and its action plan for 2009-2012 was adopted in October 2009, which includes the establishment of a monitoring and evaluation system. The strategy envisages the establishment of an anti-corruption secretariat to support the implementation and the monitoring of the action plan. The drafting process included civil society organisations and relevant international organisations. In September 2009, Armenia became a signatory to the OECD Astana Declaration on Good Governance and Fighting Corruption. The Prime Minister's Office elaborated a concept note on the transparency of political activities, regulating conflicts of interest and creating a public register for income, property and interest declarations of high ranking officials and their close relatives. Efforts were made regarding training of civil servants on anticorruption. However, despite good legislative progress, no reduction of perceived corruption was reported by international surveys in 2009, demonstrating the need for effective enforcement in this area.

Steps were taken to strengthen local democracy. As reported above, the Mayor and the Council of Elders of the City of Yerevan were for the first time elected through a proportional

system in May 2009, replacing the earlier system of presidential appointment of them. An inter-ministerial commission was set up in May 2009 to develop an action plan for creating inter-municipal unions and enlarging communities to strengthen local self-government and develop networks between municipalities, with a view to rationalize the delivery of services. In October 2009 a Working Group on **Civil Service Reform** was established under the Presidential Administration with the aim of elaborating a Civil Service Reform Programme.

Human rights and fundamental freedoms

A regular EU-Armenian **Human Rights** Dialogue was launched in December 2009. Work is ongoing to draft the first Armenian National Human Rights Action Plan, with a Working Group established in autumn 2009 to prepare a concept paper and define its scope. However, civil society involvement is still pending.

The independence of the institution of the Human Rights Defender (HRDO) in the political system and its role for the protection of human rights was further strengthened. Overall, the trend in the number of complaints received by the HRDO is increasing, confirming growing credibility of this institution. The Human Rights Defender prepared a trial monitoring report on the prosecution of cases linked to the March 2008 events and assessing the implementation of fair trial standards in the Armenian judicial system in December 2009. Apart from the annual report, in 2009 the HRDO also published reports on the implementation by domestic courts of the UN Convention against torture, on respect of social rights and on the application of disciplinary sanctions in the armed forces. In October 2009 a twinning project started with the aim of supporting the technical and organisational capacity of the HRDO.

In 2009, Armenia submitted a number of reports to UN Treaty Bodies, including on the implementation of the International Covenant on Economic, Social and Cultural Rights, the Convention on the Elimination of All Forms of Racial Discrimination, the Convention against Torture and Other Cruel, Inhuman or Degrading Treatment or Punishment. The reports on the implementation of the International Covenant on Civil and Political Rights and the Convention on the Rights of the Child were prepared and are expected to be submitted to the UN in 2010. The country is late in submitting a total of five mandatory periodic reports to UN treaty bodies. In May 2009 Armenia submitted its third report on the implementation of the European Social Charter. The conclusions by the Committee were published in January 2010. The third periodic report on the implementation of the CoE Framework Convention for National Minorities was submitted in November 2009. Armenia has issued a standing invitation to UN Special Procedures.

Cases of **torture and ill-treatment** in detention facilities and by the police continued to be reported in 2009, including in connection with detentions related to the events of March 2008 and among military conscripts, in prison facilities and in police stations. No data on torture and ill treatment are available and lack of investigations of ill treatment allegations is a matter of concern. Armenia continued to take steps towards the implementation of the Optional Protocol to the Convention against Torture (OPCAT) and submitted the first report on OPCAT implementation in December 2009. The legislative basis for civil society's involvement in the OPCAT National Preventive Mechanism should be ensured. Further amendments to the Law on Alternative Military Service are necessary to fully comply with applicable Council of Europe standards and to provide for a genuine civil service.

Efforts were made towards improving **prison conditions**. The Concept for the Penitentiary Service Infrastructure Reform was adopted in December 2009, as well as a plan on a new

penitentiary institution. The construction of a new penitentiary institution is ongoing. However, overall conditions in places of detention and the excessive use of pre-trial detention as well as the rising number of the prison population remains of concern. Civil society representatives are guaranteed access to detention facilities but not to police stations.

Legislation was amended in the area of **freedom of expression and media**. In April 2009, four laws were adopted to amend the statutes of the National Commission of the Television and Radio and Public Television and Radio Council, with most recommendations by the Council of Europe incorporated. However, the composition and the means of appointment of members of the broadcasting regulatory bodies raise questions regarding their full independence. Following the 2008 moratorium on the issuing of radio and television licenses until July 2010 on the basis of the ongoing process of digitalisation of TV and radio broadcasting, the Government released in November 2009 a Draft Concept on Switching to Digital Broadcasting, focusing on technological and economic aspects of the digitalisation process.

The number of reported incidents of violence against and intimidation of journalists decreased in 2009 but their investigations did not lead to any conviction.

In 2009, a few applications to organise rallies submitted by the opposition were rejected by the authorities. The Law on Rallies and Demonstrations is broadly compliant with Council of Europe standards but some of the provisions concerning the grounds for prohibiting conducting an assembly need further clarification. However, cases of police interference in dispersing participants during the rallies and the partial unavailability of public transportation from the regions to Yerevan in coincidence with opposition rallies were reported on a number of occasions in 2009.

A Public Council for consultation with **civil society** organisations was established in March 2009, aiming at providing a forum for public consultation on matters of public interest. The independence of the Public Council remains questioned by the opposition and a number of NGOs. Overall, consultation with NGOs by the government on draft legislation and their participation in parliamentary hearings increased but still occurs on an ad hoc basis. However, civil society organisations were not consulted on new amendments to the Law on Public Organisations, which were prepared by the government. Given the criticism from NGOs, *i.a.* related to the planned obligatory publication of annual reports of NGO activities, the amendments were temporarily suspended in Parliament.

Implementation of the National Action Plan 2004-2010 on “Enhancing **Women’s** status and empowering Women in Society” continued over the reporting period. However, the revised law on equal rights and equal opportunities is not yet adopted and the draft law criminalizing domestic violence is still under discussion. An appropriate gender equality legislation, to effectively address domestic violence and to improve women’s participation in political and economic life is needed.

In September 2009, Armenia signed the Optional Protocol to the International Covenant on Economic, Social and Cultural Rights. Continued efforts are needed to ensure the rights of trade unions and collective bargaining. Drafting of legislation on **labour rights** continued. The draft law on amendments to the Labour Code was sent to the Parliament in December 2009 after the Government’s approval.

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

Armenia continued to align with CFSP declarations on a case by case basis. In 2009, Armenia aligned with 108 out of 138 CFSP declarations. There was good political dialogue with the Armenian government in 2009, including through two Political and Security Committee Troika meetings in February and December 2009, and an EU Foreign Ministers' Troika visit to Armenia in July 2009.

Armenia pursued cooperation with the UN, participated in the NATO Partnership for Peace programme and cooperated with experts from United Nations Office on Drugs and Crime (UNODC), INTERPOL, the World Customs Organisation, CIS and CoE, in exchanging information on terrorism issues. Armenia cooperated successfully with the United Nations Counter-Terrorism Committee (CTC) established under UNSC Resolution 1373.

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

Strengthening regional cooperation

In October 2009, the Armenian and Turkish Foreign Ministers signed two protocols on establishment of diplomatic relations and development of bilateral relations, including prospects for opening a common border, which was a major step towards a normalisation between the two countries. The protocols were submitted for ratification to the National Assembly in February 2010. In April 2010, Armenia suspended the ratification procedure of the two protocols but confirmed its commitment to pursue the process of normalisation of relations with Turkey.

The Southern Caucasus Integrated Border Management (SCIBM) promoted by the EU among Armenia, Azerbaijan and Georgia was to start in January 2009 but was delayed to address issues raised by Azerbaijan. The conditions for implementation have now been accepted by all three countries and implementation started in March 2010 (*See chapter 5 on cooperation on justice, freedom and security*).

The South Caucasus Anti-Drugs Programme (SCAD V) came to an end in 2009. Discussions continue on how best to bring forward the results of the action and pursue regional efforts in the fights against illegal drugs.

The new management (a Troika consisting of Armenian, Azerbaijani and Georgian executive directors) of the Regional Environmental Centre for Caucasus (REC) took office in January 2009. It consolidated the REC both financially and in terms of internal organisation. The REC carried out regional activities in 2009 notably in the fields of information and public participation, environmental policy and local environmental action plans, the protection and sustainable development of mountain regions. It is an important tool to promote regional cooperation and stability for the future of the South Caucasus.

In the area of higher education, universities from Armenia, Azerbaijan and Georgia cooperated on a distance and e- learning project. This is the first time that such regional cooperation emerged under the Tempus programme.

Contribute to a peaceful solution of the Nagorno-Karabakh conflict

Negotiations within the Minsk Group on the peaceful settlement considerably intensified in 2009 and contributed to enhanced dialogue, with the Presidents of Armenia and Azerbaijan holding six bilateral meetings during the year. In addition, the Foreign Ministers of the two

countries met a number of times, including during the OSCE Ministerial Council in December 2009 in Athens. Courageous steps by both sides will be necessary to find a resolution to the conflict.

A joint statement by the OSCE Minsk Group at presidential level during the G8 Summit in L'Aquila in July 2009 urged "the presidents of Armenia and Azerbaijan to resolve the few differences remaining between them and finalize their agreement on these Basic Principles, which will outline a comprehensive settlement." However, overall tensions remain and the situation continues to be fragile. Incidents of exchanges of fire and casualties on the line of contact continued to be reported and are cause for concern.

3. ECONOMIC AND SOCIAL REFORM

Macroeconomic framework and functioning market economy

The global economic downturn and particularly the rapid deterioration of the Russian economy had a deep impact on the Armenian economy in 2009. Economic activity which had started to fall in the last quarter of 2008 contracted by around 15.4% in 2009 representing a massive turnaround compared to strong growth rates of the previous years. This was the result of the collapse of the construction sector by around 38%, as an immediate consequence of the reduction in remittances by around 28%, and the strong contraction of the industrial output by around 10%.

The authorities acted rapidly and adopted measures to mitigate the effects of the sharp downfall in output. In March 2009, they reverted to a fully floating exchange rate regime allowing a *de facto* devaluation of the Armenian *Dram* of around 22 % against the euro and the USD. This step helped to improve competitiveness without threatening financial stability as the negative effects of the devaluation were largely absorbed. At the same time they reached an agreement with the IMF for a USD 790 million (EUR 553 million) Stand-by Arrangement while securing additional funding from other multilateral and bilateral donors (including USD 500 million - EUR 350 million - stabilisation loan from the Russian Federation) to meet the increasing financing needs.

Fiscal policy was supportive to the economy with expenditure plans focusing on wide-ranging anti-crisis measures, increasing foreign-financed capital spending and protecting social spending. Partly owed to external borrowing, the authorities accommodated largely the fall in tax revenues by about 15% without cutting significantly the expenditures, while taking into account financing constraints and debt sustainability concerns. As a result the fiscal deficit is expected to increase to 7.5% of GDP and public debt to 37% of GDP in 2009. At the same time the fiscal structural reform agenda advanced through improvements in VAT refund processing and introduction of e-filing of tax returns for large tax payers.

Monetary policy eased and the Central Bank of Armenia (CBA) lowered its policy rate gradually from 7.75% in April to 5% in September 2009 to contribute to the recovery of the economy. It also injected *Dram* liquidity through various channels, including purchases of government securities and increasing the maturity of its repo operations. However, due to weaknesses of the transmission mechanism, banking lending rates remained at 18% causing additional action by the authorities like on-lending of credit resources provided by donors/creditors to targeted SMEs and vulnerable industries through the Central Bank and

commercial banks. The weakness in the transmission mechanism is the high deposit dollarisation, which remained at around 70%.

Average inflation remained at around 3.4% on the back of the weak demand, despite the depreciation of the Dram in March 2009. However, inflation increased to 6.5% in December 2009 owing to rising international prices, the ongoing expansionary policies, rigidities in domestic prices, and speculative exchange rate pressures stemming from excess liquidity. At the end of 2009, CBA signalled the end to the easing cycle and its readiness to act under the inflation targeting framework if inflationary pressures emerge. It is however expected the inflation will come down in 2010.

External trade turnover contracted by around 28% in 2009. Export revenue contracted by around 37% influenced by the drop in prices of metallurgical products, while imports contracted to a lesser extent by around 26%. As a result, the current account deficit is estimated to have widened in 2009 to 13.7% of GDP. Combined with the collapse of FDI, this raises serious concerns about the competitiveness of the Armenian economy.

Employment and social policy

As a result of the economic crisis which seriously affected Armenia, the Government decided to temporarily suspend the Sustainable Development Programme on **poverty reduction**.

The official **unemployment** rate was estimated at 7.1% at the end of 2009. Young people and women continued to be particularly affected with respectively 20.7% and 70.7% of official unemployment. The State employment services continued training activities of the unemployed over the reporting period.

As regards **social dialogue**, collective agreements with social partners were signed in May 2009. A tripartite committee with representatives of the Government, the trade unions and the employers was subsequently established in the same month. The implementation of the 2007-2011 Decent Work Country Programme continued over the reporting period.

On **social inclusion and protection**, the introduction of the new pension system was postponed to 2011.

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.

In January 2009 the National Council on **Sustainable Development** (NCSD) met for the second time in accordance with the “Sustainable Development Programme 2008-2021”. Further actions were taken to implement the 2009-2012 Sustainable Development programme, especially in the water sector.

4. TRADE-RELATED ISSUES, MARKET AND REGULATORY REFORM

As regards **bilateral trade**, in 2009, as a result of the global slow-down in economic activity due to the financial crisis, EU exports to Armenia declined by 20.6% compared to the previous year, while exports of Armenian products to the EU decreased by 49.3%. In terms of commodity structure, Armenian exports to the EU still remain quite undiversified and of low value added – in 2009, almost two third (64.3%) of them consisted of base metals and almost one fifth (18.8%) of pearls and precious stones.

Armenia benefits from the EU Generalized System of Preferences Plus (GSP+) for the years 2009-2011, aiming at further diversifying its export structure and improving its export performance. Armenian exporters were also trained during the reporting period in using the EU Export Helpdesk to allow them to make full use of the GSP+ preferences. Since April 2009, the EU Advisory Group supported the Government in a number of trade-related areas, in particular the efforts to make the best possible use of the GSP+ arrangement and in preparing for a future EU-Armenia Deep and Comprehensive Free Trade Area (DCFTA).

The European Commission carried out a fact-finding mission to Armenia in February 2009 and established a detailed assessment of Armenia's preparedness for a DCFTA. It made recommendations on key reforms which Armenia would need to undertake to become ready for the DCFTA negotiating process ("key recommendations"). This assessment was endorsed by the Armenian authorities in June 2009. In November 2009 Armenia established an institutional structure for the preparatory and future negotiating process which still needs to become operational. As concerns other key recommendations limited progress was noted. With substantial additional efforts on its side, in order to achieve the necessary progress in the key regulatory areas including enhancement of administrative capacity, Armenia would become prepared for the start of the DCFTA negotiations.

Good progress was recorded in the **customs** area. The comprehensive "Customs Administration Strategy for 2008-2012" was further elaborated through the development and introduction of a Strategic Action Plan in December 2009, which details, for each strategic objective, the actions to be taken, success criteria, performance indicators, and target dates. Following the introduction of a code of ethics in 2008, the Customs administration launched an internal corruption risks assessment, with a view to prepare an action plan for combating corruption risks. A network of Customs brokers was established, and 125 brokers received training. The Customs administration prepared several staff manuals on subjects such as customs clearance, classification, passenger controls, customs fees, and post-clearance audit, and distributed them to all Customs offices. During the reporting period, the Customs administration worked on the development of a "risk management directive" defining the activities of Customs officials in headquarters, regional Customs houses and other Customs offices, as well as at the border. This directive will cover not only the clearance and examination systems but also warehousing, other customs regimes, and post-clearance control; it will link with the investigation function and will incorporate the use of risk profiles in all areas. Further improvements are needed in areas such as risk management, integrity, cooperation with other enforcement agencies, accession to the main international customs instruments, abolition of administrative fees, verification of certificates of preferential origin, customs valuation practice, as well as the role of customs in IPR protection.

On the **free movement of goods and technical regulations**, some progress was made. A number of new draft laws and amendments to existing laws affecting technical barriers to trade were prepared and discussed throughout 2009, including laws on standardisation, conformity assessment, uniformity of measures, accreditation (amending the 2004 accreditation law). The selection of the priority sectors is still on-going. The Ministry of Economy coordinated the efforts of various development partners working in the area of quality infrastructure. An awareness event on establishing a national quality infrastructure was organised in October 2009. More progress will be required to consider opening negotiations for an Agreement on Conformity Assessment and Acceptance of Industrial Products (ACAA) in a long-term perspective.

In the area of **sanitary and phytosanitary** issues, Armenia drafted a programme and an action plan on the development of the food safety system for the period 2009-2013. Armenia adopted amendments to the phytosanitary law. It prepared a law on the registration of food establishments as well as amendments to the veterinary law and strengthened its laboratories. The European Commission's fact-finding mission in February 2009 showed that Armenia will have to progress considerably in this sector. This is particularly the case as regards legislation and coordination among the relevant institutions.

Armenia has in place a number of relevant laws on **business climate, establishment and company law** including the Civil Code, the Law on Joint Stock companies and the Law on Limited Liability Companies. However, while the legislation in place is ranked highly, the issue of implementation of the relevant laws remains problematic. Moreover, shortcomings related to transparency and to disclosure requirements as well as the absence of a national Gazette have been identified. Compliance with OECD corporate governance principles should be guaranteed, functions of corporate governance bodies as well as rights of majority and minority shareholders should be clearly defined and appropriate protection of investors, creditors and minority shareholders be ensured. Competent and independent judicial or administrative authorities should be designated to monitor incorporation or legality of certain acts. Good progress was seen with the ongoing work on effective implementation of laws in this area, as well as drafting a Corporate Governance Code.

Armenia was affected by the financial and economic crisis in the field of **financial services**. The Central Bank of Armenia (CBA) continued its efforts to implement the Basel II principles for effective banking supervision. The IMF noted that the banking sector in Armenia is sound and well-capitalised, but the economic contraction may affect credit risk, as already reflected by the increase in non-performing loans. The CBA took steps to ensure that these risks are well-managed. The banking sector represents over 90% of the financial system assets. The main actors in this field remain foreign owned banks with about 65-70% of the overall banking capital. In the field of deposit guarantees, in 2009, amendments to the Law on Guarantee for Compensation of Bank Deposits of Physical Persons were prepared. A legislative package on pension funds is under discussion by the Government and a draft law on mandatory insurance ensued from responsibility of vehicle use is discussed by the parliament.

Other key areas

Progress was recorded in the area of **taxation**. The Ministry of Finance worked on a Consolidated Tax Code. The Tax Administration already implemented several of the measures contained in the Tax Administration Strategy for 2008-2011. The Supreme Council on Revenue Collection was established to monitor progress in this area. Plans for introduction of e-declarations and improvements of risk-based controls were adopted. The process of upgrading human resources is in progress and includes also creation of a new training centre (both for taxation and customs). The Tax Administration solved the problems related to delays on VAT returns and reabsorbed the existing backlog. Armenia developed and adopted a plan for introducing an e-governance system, and 18 working groups were set up to deal with the automation of tax administration. In 2009 Armenia reported that agreements on avoidance of double taxation are in force with 13 EU Member States and others are signed or being negotiated. In line with its WTO commitments discriminatory practice regarding VAT and excise system on tobacco products needs to be eliminated.

The State Commission for the Protection of Economic Competition continued its work to strengthen the legal and institutional framework for **competition policy** in 2009. It prepared new draft amendments to the legal framework which are expected to be adopted in 2010. Effective implementation of the previous amendments to the law on “protection of economic competition”, including provisions for state aid, requires further efforts in the establishment of secondary implementation mechanisms. A draft law for the implementation of a leniency programme is being prepared. An EU twinning project concerning state aid and competition policy is foreseen in 2010.

The Government approved in April 2009 a Concept Paper on Implementing Reliable and Effective Protection of **Intellectual Property**. A special committee for the implementation of this paper, led by the Minister of Economy and including representatives of right-holders and relevant NGOs, was set up in August 2009. Armenia also worked over the reporting period on amending its legislation on copyrights, geographical indications and trademarks. Armenia still needs to ratify the International Convention for the Protection of New Varieties of Plants (UPOV Convention). A survey on piracy and counterfeiting was launched during the year and is on-going. However, further substantial efforts are needed to ensure sound enforcement of legislation by reinforcing the powers and the administrative capacities of the enforcement bodies, including the judicial system and by raising awareness of intellectual property issues among the general public and the right-holders.

Armenia continued to work on new legislation on **public procurement**. Once adopted, it is expected to enter into force in June 2010. The new law foresees the transformation of the State Procurement Agency into a Procurement Assistance Centre. Further efforts are needed in the area of training and provision of systems to implement e-procurement.

Armenia completed the translation of International Financial Reporting Standards (IFRS) in the area of **accounting**. Armenia also started negotiations with the International Accounting Standards Board with a view to signing an agreement on translation of the accounting standards for the small and medium-sized enterprises. No progress can be reported on the establishment of an independent regulatory body, separate from the Ministry of Finance, responsible for accounting and auditing.

As regards **statistics**, Armenia adopted in June 2009 the national classifier for the economic activity. Armenia also worked over the reporting period on developing the national version of the classification of territorial units and continued translating into Armenian key EU regulations in the field of statistics.

On **enterprise policy**, the Small and Medium-sized Enterprise Development National Centre (SME DNC) continued to support SMEs through the implementation of annual programmes with resources allocated from the state budget. Since its 2008 membership in the Enterprise Europe Network (EEN), the SME DNC has been hosting an EEN Correspondence Centre providing business, innovation, technology and research related services to Armenian companies while also rendering assistance to European SMEs seeking business opportunities in the Armenian market. Several amendments in tax legislation for SMEs, adopted in 2009, entered into force just after the reporting period, in January 2010.

In the area of **public internal financial control** (PIFC) Armenia continued to work on an internal audit law. The draft law includes provisions for establishing a central harmonisation function for internal audit. Following a detailed gap assessment of the existing PIFC environment, the Ministry of Finance started to work on a PIFC Policy Paper. The

introduction of principles of managerial accountability is still at a very early stage. With regard to external audit, the Chamber of Control has established contacts with the European SAIs in order to develop existing audit practices in line with INTOSAI standards.

5. COOPERATION ON JUSTICE, FREEDOM AND SECURITY

Armenia continued participating in the Southern Caucasus Integrated **Border Management** (SCIBM) regional programme, formally agreed between Armenia, Azerbaijan and Georgia in 2007. The programme aimed at enhancing inter-agency cooperation, training and capacity of customs and border guard services in line with agreed regional standards and EU norms. Despite the regional character of this programme, Azerbaijan chose to pursue cooperation only through its bi-lateral component with Georgia, which delayed the start of implementation until March 2010. Nevertheless, in the framework of SCIBM, Armenia's customs and border guard services participated in preparatory training sessions in Austria, Croatia, Italy and Slovenia alongside representatives from Azerbaijan and Georgia.

Further training was provided for border and patrol police including cross-border seminars with border officials from both Georgia and Azerbaijan in cooperation with the OSCE.

The State **Migration** service commenced work on a National action plan on migration and asylum in cooperation with civil society and, with EU support, on a draft strategy on the regulation of migration. The draft law on the regulation of labour migration, prepared in 2008, has not been adopted yet. In addition an electronic database for the monitoring of migration flows remains to be established. With support from the OSCE and the International Organisation for Migration (IOM), Armenia is elaborating an action plan for the introduction of an electronic passport with biometric features and electronic ID Cards. Improvement of document security is considered by the authorities as a necessary step to benefit from visa facilitation with the EU.

With regard to the fight against **organised crime**, Armenia has yet to accede to the Third Protocol to the United National Convention on Transnational Organised Crime on the Illicit Manufacturing and Trafficking of Firearms, their Parts and Components, and is also encouraged to sign and ratify the 2007 Council of Europe Convention on the Protection of Children against Sexual Exploitation and Sexual Abuse.

On **trafficking in human beings**, the national budget allocated some EUR 100,000 to finance anti-trafficking actions including the establishment of a National Referral Mechanism and a special shelter for victims of trafficking, in cooperation with civil society organisations. 11 separate prosecutions for crime related to the trafficking of human beings were recorded in 2009.

As stated above, the South Caucasus Anti-Drugs Programme (SCAD V) came to an end in 2009. Discussions continue on how best to bring forward the results of the action and pursue regional efforts in the **fight against illegal drugs**.

With regard to the fight against **money laundering**, Moneyval approved the third round mutual evaluation report on Armenia in September, highlighting improvements to the legal framework to combat money laundering and the financing of terrorism achieved in 2008. The report was published in January 2010. As stated last year, the continuing development of human and technical resources with regard to money laundering, corruption and terrorism financing remains an ongoing challenge

In the area of **police and judicial cooperation** Armenia ratified the 1997 Additional Protocol to the European Convention on Mutual Assistance on Criminal Matters in March 2009. However, its effective implementation will require continued efforts to improve coordination and cooperation between all law enforcement agencies, including investments in training. Armenia ratified two Additional Protocols to the UN Convention against Transnational Organised Crime at an earlier stage, but the Third Protocol against the Illicit Manufacturing of and Trafficking in Firearms, Their Parts and Components and Ammunition remains unsigned. Two important Hague Conventions on international judicial cooperation, namely, the 1965 Convention on the service of documents and the 1970 Convention on the taking of evidence have not yet been signed by Armenia.

As regards **data protection**, Armenia has neither signed the 1981 Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data in 2009 nor the Additional Protocol on supervisory authorities and trans-border data flows.

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

In October 2009 Armenia adopted a **transport** sector development strategy covering the years 2009-2020. The strategy foresees improved management, infrastructure, and technology to maximize the transport sector's performance until 2020, and envisages long-term prosperity through the establishment of efficient, cost-effective, and environmentally and socially sustainable transport infrastructure and services. The strategy foresees the separation of regulatory and oversight functions ensuring the independence of regulatory functions. Further short-term policy priorities are to define a road strategy based on sound asset management, address worsening road safety as well as the deteriorating urban transport in Yerevan.

As regards infrastructure investments, Armenia started in 2009, with the help of the World Bank, to upgrade roads belonging to the "Lifeline Road Network" (LRN). The capacity of the Armenia Road Directorate is being strengthened. Armenia decided already in 2004 that each community should have at least one connecting road to an interstate road. These roads comprise some 3,014 km of Armenia's 7,704 km of non-urban roads and are defined as the optimal road network connecting rural communities to the interstate highways.

In the air sector, the transport strategy 2009-2020 foresees as a short-term priority to remove restrictive commercial and regulatory measures in order to improve aviation efficiency and connectivity. Following the signature of the horizontal air services agreement, reported last year, a further important step towards closer relations between the EU and Armenia in the transport field was the signature of the working arrangement between the Armenian authorities and the European Aviation Safety Agency in July 2009 to strengthen its regulatory cooperation with the Agency and progress towards convergence with European safety standards. Due to restricted competition, air traffic between the EU and Armenia, although increasing, remained limited.

Armenia further implemented its **energy** strategy, *inter alia* by completing a tender for the selection of a company that will oversee the construction process of a new nuclear power plant. In October 2009, Armenia adopted a law on constructing a new nuclear power unit. A tender to select the plant constructor is under preparation. 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

continued to ask closure before this date. Armenia continued the safety upgrading of MNPP on the basis of its 2009-2016 programme. It pursued work towards a spent nuclear fuel and radioactive management strategy and progressed on the expansion of a dry spent fuel storage facility. Armenia took further steps to prepare a detailed decommissioning plan for MNPP. It continued to fill the Nuclear Decommissioning Fund and to explore, jointly with the Russian Federation, uranium reserves.

In April 2009, Armenia raised gas and electricity tariffs following the increase of the gas price. It continued the construction of conventional electricity generation units (including hydro) and the rehabilitation of electricity and gas infrastructure. Armenia pursued preparatory work for additional electricity interconnections with Georgia and Iran. In March 2009 Armenia agreed with Turkey to export electricity once the grid has been upgraded. In May 2009, the Armenia-Iran gas pipeline became operational. The deal between the two countries aims to export gas to Armenia and electricity to Iran. In April 2009, Armenia and Iran confirmed their plan to construct an oil refinery. Armenia pursued the development of an energy efficiency and renewable energy programme.

In the field of **climate change**, Armenia continued preparing its Second National communication to the UN Framework Convention on Climate Change (UNFCCC), which will include a greenhouse gas inventory, mitigation and adaptation measures. A report on vulnerability of water resources was prepared. Steps to address adaptation to climate change impacts in mountain forest ecosystems started. The socio-economic impact of climate change was assessed with regard to agriculture, energy and forestry, and policy recommendations and measures were developed. The UNFCCC related part of the 2004 Government Decision on measures for the implementation of a number of international obligations was reviewed in December 2009 and is in the process of approval.

Armenia took steps to prepare and approve further Clean Development Mechanism (CDM) projects. One new such project was registered at UN level, bringing the total number of registered projects to five. Armenia associated itself with the Copenhagen Accord and provided information on actions that it will implement. The European Commission continued to support Armenia to implement the Kyoto Protocol.

Armenia started implementing its **environment** action plan for 2008-2012, *inter alia* with regard to the development of the legislative framework, capacity building for environment monitoring and strengthening of management of waste and chemicals. The legislative framework continues to require further development, in particular as regards implementing legislation. Amendments and changes to legislation in the fields of air quality, water management and environmental fees were adopted. A Government decision was adopted to regulate the process of registration of companies whose activities have a negative impact on the environment and further decisions were adopted in the field of water, nature protection, chemicals and waste. An act on environmental protection, as well as legislation on environmental expertise, genetically modified organisms and self-monitoring of compliance, are still being prepared.

A national profile of chemicals and waste management was approved. Preparations for a national strategy to reduce risks of hazardous substances on human health and the environment were launched. Continued attention is required to implement existing strategies and plans and to further enhance monitoring and enforcement.

Some steps were taken with a view to strengthening water resource management. Further strengthening of administrative capacity at all levels of the country remains a major challenge. Coordination between authorities continues to require attention. Some activities were taken to promote the integration of environmental considerations into other policy sectors such as transport. Some steps were taken to prepare legislation on integrated permitting.

There were no significant developments with regard to preparations of state-of-the-environment reports. Armenia nevertheless continued to carry out some other activities to provide information to the public. (*For the Regional Environmental Centre for the Caucasus, please see chapter 2*)

The draft legislation on self-monitoring of compliance, currently under preparation, contains provisions on environmental impact assessment, including with regard to public participation. Procedures and consultation with the public in the context of environmental assessments continue to require particular attention. The Implementation Committee of the Espoo Convention requested Armenia to revise its environmental impact assessment legislation to align with the Convention as well as to report back on this. Armenia subsequently submitted a satisfactory implementation strategy.

Armenia took some steps towards accession to the EMEP¹ Protocol to the UNECE Convention on Long-Range Transboundary Air Pollution. There were no significant developments as regards the accession or ratification with regard to remaining relevant UNECE Conventions and Protocols². 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 exchanges of information took place between the European Commission and Armenia, including on water, forestry, waste management, environmental data, nature protection and air quality.

In the field of **civil protection**, Armenia participated in the December 2009 launch event of the Eastern Partnership flagship initiative on prevention on, preparedness of and response to man-made and natural hazards.

In order to help the preparation of a regulatory reform in the area of **Information Society**, a first meeting of the working group on regulation of communication issues was held at the premises of the Ministry of Transport and Communication in June 2009. Representatives and responsible executives from both public and private sectors participated in this meeting.

In February 2009, eight domestic operators were granted public network number capacities and codes to offer fixed-line telephony in Armenia. Each company network will be connected to the current *de facto* monopolist.

In the **audiovisual** sector, freedom of reception and retransmission of television broadcast coming from other countries remains difficult as Armenia has not ratified the Council of Europe Convention on Transfrontier Television.

¹ Protocol on Long-term Financing of the Cooperative Programme for Monitoring and Evaluation of the Long-range Transmission of Air Pollutants in Europe (EMEP)

² the Protocol on Strategic Environmental Assessment to the UNECE Convention on Environmental Impact Assessment in a Transboundary Context, UNECE Convention on the Protection and Use of Transboundary Watercourses and International Lakes and the other relevant Protocols

Armenia's **research** investment and capacity remains relatively modest. However, participation in the 7th Framework Programme (FP7) has increased in comparison to FP6, with 17 research organisations being successful in their applications, as of November 2009, receiving EUR 690,000 of EU funding, particularly under the 'international cooperation' information and communication technologies and the 'Marie Curie' calls for proposals.

Armenia continued to participate actively in the International S&T Cooperation Network for Eastern European and Central Asian countries (FP7 IncoNet EECA project), which aims to support a bi-regional EU-EECA policy dialogue on science and technology and to increase EECA participation in FP7.

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

In the area of **higher education**, the Ministry of Education and Science established five working groups with university participation to promote Bologna Process requirements covering qualification frameworks, credit accumulation, financial management, quality assurance mechanisms, and post-graduate education. The Bologna Process Diploma Supplement, providing for greater transparency on higher education qualifications was introduced in Armenian universities and higher education institutions in the course of 2009.

Armenia continued its active participation in the Erasmus Mundus scholarship programme as well as in the Tempus IV programme, increasing compared to Tempus III.

Thirteen Armenian students and one scholar were awarded scholarships for Erasmus Mundus Masters Courses for the academic year 2009-10 under Erasmus Mundus Action 1 while academic and student mobility was further facilitated under Erasmus Mundus Action 2 during the same period through the award of 35 mobility grants. Armenian universities are encouraged to participate in the Jean Monnet programme.

With regard to vocational education and training, developments in 2009 focused on the consolidation and continuation of reforms initiated in 2008 in the areas of teacher training, refurbishment of vocational training colleges and the development of qualifications standards and a draft national qualification framework with considerable EU support (see chapter 8). The concepts of social partnership in vocational education and training and life long learning were endorsed by the Government in October. The Ministry of Education and Science continued developing a national qualifications framework on the basis of competence-based standards developed by the National Centre for Vocational Education and Training Development.

The Ministry of **Culture** pursued implementation of the four year Culture Development Strategy (2008-12) focusing on effective coordination of cultural policy, cultural heritage, international cooperation, digitalization of non-material culture and promotion of popular culture. As stated in 2008 in this regard, 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. Armenian cultural organisations participated in the Call for Proposals of the 2009 ENP Special Action under the Culture Programme.

Armenian young people and **youth** organisations continued benefiting from the opportunities offered by the Youth in Action Programme, through exchanges, voluntary service and youth cooperation activities in non-formal education.

Armenia pursued reform in the **health** sector, in particular as regards primary health care and health insurance. The reform should contribute to reducing out of pocket payments. In 2009, the Government endorsed a strategy and an action plan for Child and Adolescent Health and Development for the period 2010-2015. Communicable diseases such as HIV/AIDS and tuberculosis remained challenges. In October 2009, Armenia participated in the newly established EU enlarged health information committee.

8. FINANCIAL COOPERATION – 2009 KEY FACTS AND FIGURES

The European Neighbourhood Policy Instrument (ENPI) envelope for the Armenia under the National Indicative Programme 2007-2010 is EUR 98.4 million. The programme is focused on three priority areas: 1) Strengthening of Democratic Structures and Good Governance, 2) Regulatory Reform and Administrative Capacity Building, and 3) Poverty Reduction Efforts.

The 2007 Annual Action Programme on Vocational Education and Training (EUR 16 million) is in the final stages of its implementation. The 2007 sector programme progressed well, and its planned activities were concluded in late 2009. The final verification mission for the second (and final) fixed tranche was deferred to December 2009 due to supply delays. Therefore the final payment is being processed in the semester of 2010. Furthermore, the TA/twinning envelope with a value of EUR 5 million in support of regulatory reform and administrative capacity building is currently being implemented.

The implementation of the 2008 Annual Action Programme on Support for the Justice Reform programme (EUR 18 million) is underway. The initial fixed tranche of EUR 8 million of the 2008 Justice programme was processed in late 2009. The AAP 2008 TA/twinning envelope with a value of EUR 6 million is currently being prepared.

The first twinning project was launched in 2009 (support to the Ombudsman and Human Rights Defender) and a second was launched in 2010 (support to the introduction of the Standard Cost Model with the Ministry of Economy). Three twinning projects are currently published for Member State proposals (Civil Aviation, Competition, National Statistics).

In 2009, the European Commission continued to support the national reform efforts in Armenia and programmed assistance for a total amount of EUR 24.7 million under the ENPI. The 2009 Annual Action programme focused on the continued support for further economic development and social cohesion. Within this envelope, EUR 15 million was allocated to pursue the reform of Vocational Education and Training as a sector budget support operation. Another EUR 9.7 million was allocated to TA and Twinning operations.

An indicative financial envelope of EUR 157.3 million will be available to support co-operation activities in Armenia in the period 2011-2013, based on a European Commission decision of March 2010.

In addition to the bilateral allocation, Armenia also benefited from cooperation activities financed under the ENPI multi-country and regional programmes, as well as horizontal thematic programmes, such as the European Instrument for Democracy and Human Rights (EIDHR) and the Non-State Actors and Local Authorities in Development programme (NSA/LA). Armenia is also eligible for the cooperation under the ENPI Cross-Border Cooperation (CBC) Black Sea Basin programme.

The Instrument for Stability provided immediate support to the post-election stabilization efforts in the form of the EU Advisory Group for a total budget of EUR 2 million. Furthermore, in 2009 the EU took a decision to grant the Government of Armenia Macro-Financial Assistance to alleviate the effects of the global financial crisis. The package includes a EUR 65 million loan and a EUR 35 million grant. Disbursement is expected to begin during the first half of 2010.

Under the Neighbourhood Investment Facility (NIF) contributions, two projects in Armenia were approved in 2009, committing EUR 14.6 million in grants and technical assistance, expected to leverage EUR 23 million in loans of European Finance Institutions in the environment and transport sectors. Furthermore, three regional projects for which Armenia is eligible were also approved in 2009, committing EUR 24 million in grants, to leverage a total of EUR 372 million in loans/investment from European Finance Institutions in the energy and financial sectors.

With regards to assistance in the area of Nuclear Safety, projects providing On-Site assistance and supply of equipment to the Nuclear Power Plant of Medzamor worth EUR 11 million are currently being implemented in the framework of the Instrument for Nuclear Safety Cooperation (INSC) Action Programme 2009 (including the support to the National Regulator). Two other projects aimed at improving the safety culture of the Armenian Nuclear Regulatory Authority for the overall sum of EUR 2.3 Million, as programmed under previous Action Programmes, are still ongoing.

The European Investment Bank did not sign any lending operations with the Government of Armenia in 2009.

In 2009, the overall donor coordination was foremost done in coordination between the four main donors in the lead (WB, IMF, USAID and EC) with participation of the Armenian Ministry of Economy. These were arranging general donor coordination meetings at least every three months, inviting also other donors. Increasingly, the Armenian side started to take the factual responsibility for the coordination of donor activities.