

Annex 2 – Annual Action Programme 2012 for Armenia

1. Identification

Title/Number	Support for the EU-Armenia Deep and Comprehensive Free Trade Area (DCFTA) CRIS Number: ENPI/2012/023-603		
Total cost	EU Contribution: EUR 25 million		
Aid method / Method of implementation	Sector Policy Support Programme: - Sector budget support (centralised management) - Project mode (direct centralised management).		
DAC-code	33110	Sector	Trade Policy and administrative management

2. Rationale and country context

The areas covered by the proposed programme are in line with the EU assistance priorities in the sector, as established in the National Indicative Programme (NIP) 2011-2013 - Sub-priority 2.1 "Promoting Trade and Investment, in particular through Market and Regulatory Reform, including in the areas of Business Environment, Taxation and Customs; support for preparation of a future DCFTA with the EU". The programme also supports the implementation of the EU-Armenia ENP Action Plan, particularly its Priority area 4 "Further improvement of investment climate and strengthening of private sector-led growth".

2.1. Country context and rationale for SPSP

2.1.1. *Economic and social situation and poverty analysis*

The global economic crisis seriously threatened the economic growth and poverty reduction achieved in Armenia over recent years. The crisis had a serious impact on poverty incidence which rose to 35.8 % in 2010 as compared to 27.9 % observed in 2008. Moreover, the share of the extremely poor in 2010 was 3.6 % as compared to 1.6 % in 2008¹. According to the July 2011 IMF Country Report, GDP per capita rose by 82% between 2006 and 2008, but fell by 26% in 2009. In the years of economic growth the registered unemployment experienced similar trends, decreasing from 9.6% in 2004 to 6.3% in 2008. In 2009 and 2010, however, the registered unemployment rate had risen to 7%.

2.1.2. *National development policy*

The European Neighbourhood Policy / Eastern Partnership envisages the signature of an EU-Armenia Association Agreement (AA) including the establishment of a Deep and Comprehensive Free Trade Area (DCFTA) with the EU. Strengthening of the core institutions in Armenia involved in this process and the implementation of comprehensive economic, legislative and administrative reforms are among the necessary conditions.

The *Sustainable Development Programme* (SDP) 2008-2021, approved in October 2008², is the main national strategy for economic and social development. Due to the negative social

¹ Source: National Statistics Service (www.armstat.am)

² Government Decree N 1207 of 30.10.2008

and economic effects of the 2008 global crisis, the document is currently being revised by the relevant authorities, with support by the UNDP.

The "*Strategy for Accelerating the Reforms in the Republic of Armenia within the Framework of the EU Eastern Partnership*", adopted by the President in 2011, identifies priority actions to support legislative approximation with the EU, and institutional and operational capacity strengthening. In particular, in its "Economic Field", the Strategy targets reforms related to the food safety, sanitary and phyto-sanitary measures (SPS), intellectual property rights (IPR) and technical barriers for trade (TBT). The "*White Paper on Republic of Armenia Reform Agenda within the EU Integration Context*" from the Government aims to translate the Strategy in more concrete actions.

2.2. Sector context: policies and challenges

1. *Sector strategies*. There are several sector strategies that are consistent with the national strategies / policies as well as the NIP 2011-2013 and the ENP Action Plan. They have all been adopted by the Government recently and reflect a high degree of Government commitment and ownership. These strategies have been the object of an extensive consultation process during their development, which included the relevant services in the European Commission.

- The *Institutional Reform Plan (IRP) – DCFTA*, developed in the framework of the Eastern Partnership Comprehensive Institution Building (CIB) initiative, was adopted by the Government in December 2011. It targets three 'clusters' in the DCFTA area: IPR, TBT and SPS. It identifies gaps in institutional capacity, formulates a series of interventions to address these gaps and indicates what resources are required.

- The *Strategy of Armenia on Intellectual Property Rights* protection and its Action Plan were adopted by the Government in April 2009³.

- The *Strategy on Reforms of Quality Infrastructure in Armenia* was adopted by the Government in December 2010⁴. The document addresses legislative and institutional approximation to EU Directives 675/2008 and 678/2008, including reforming institutions covering standardisation, accreditation, and metrology. The Strategy has been implemented according to its timetable.

- The *Strategy and Action Plan for Food Safety System Development* were adopted by the Government in November 2011. The documents clearly identify approximation to the EU laws and standards as a priority. They also stress the need to strengthen the institutional framework for food safety, notably through reinforcement of the newly established Food Safety Service, and to develop a risk assessment approach for food safety/SPS issues.

2. *Sector budget and MTEF*. Armenia has used the Medium-Term Expenditure Framework (MTEF) since 2003. After the temporary suspension of the MTEF in 2009, it has been reintroduced in early 2010. Sector budgeting is currently linked to institutions, but there are ongoing reforms to introduce programme budgeting in some sectors. The MTEF foresees that annual allocations in DCFTA area are increased during the period of implementation of this programme, a remarkable exception in the current context of fiscal consolidation and expenditure restraint agreed.

³ Government Decree N 14 of 02.04.2009

⁴ Government Decree N 1693 of 16.12.2010.

3. *Performance monitoring.* Each of the sector Strategies, as well as the DCFTA Institutional Reform plan (IRP), include a regular monitoring of progress in implementation, including performance indicators. The National Statistical Service of Armenia is a reliable and regular source of information.

4. *Macroeconomic framework.* The macroeconomic fundamentals of the country remain positive and the IMF programme is on track. The projection of 4.6% and 4.3% GDP growth in 2011 and 2012 respectively are still in force. In 2011, the economy performed well thanks to the recovery of the agricultural sector and the dynamism of the industry and services sectors. However, downside risks have increased considerably due to external factors such as the indirect consequences of the European sovereign debt crisis through the knock-on effects to Russia and the main trade partners. The fiscal balance has continued to improve, with the overall deficit expected to come down to below 4% in 2011 from 4.6% percent in 2010. In order to ensure debt sustainability, consolidation is expected to continue in 2012. Inflation at the end of 2011 is estimated at 6.7%, 4% at the end of 2012, declining from 8.5% of end 2010 thanks mainly to an adequate fiscal consolidation path and the stabilisation of international food and fuel prices. Also, domestic agricultural production has gone back to lower levels of price. The Central Bank continues to show a commitment to a flexible exchange rate and the inflation targeting regime, engaging in limited foreign exchange interventions to smooth volatility. The third IMF review of the Extended Fund Facility (EFF)/Extended Credit Facility (ECF) Programme was finalised in mid-December 2011 and triggered a new IMF disbursement of USD 56.1 million.

5. *Public Finance Management.* The first and most recent Public Expenditure and Financial Accountability (PEFA) evaluation was carried out in 2008 and attested progresses in many areas. The Government is planning to hold a second evaluation in 2012 - 2013. In terms of revenue, inflows continue to recover from the economic downturn in 2009. The authorities project that revenue will rise by almost 7% in 2012 through amendments to the tax legislation aimed at targeting the most affluent. A new systemic *Strategy for Reforming the Public Finance Management System* was adopted by Government decree on 28 October 2010. The new proposed reforms aim to complete the work on the basic systems while gradually transitioning from centralised administration to decentralised management. External Audit Reforms will be covered by the "Strategic Development Plan" and its Action Plan that were adopted by the Chamber of Control in summer 2011. As concerns budget transparency and oversight, Armenia scored high marks in the 2008 PEFA. Budget documents are publicly and regularly available through various means (press, website). The Chamber of Control regularly receives the Execution Report within the stipulated time and issues an Opinion - both are widely covered by the press. The Budget is actively reviewed by the Parliament as assessed by the PEFA 2008 (A rating). Web portal www.e-gov.am has a page on interactive budget.

2.3. Eligibility for Budget Support

On the basis of the analysis in 2.2, Armenia continues to meet all three eligibility criteria for budget support: Sector policy, macroeconomic stability and PFM reform. As concerns the budget transparency / accountability, the 2012 Budget law was published on 23 December 2011, after the adoption by the National Assembly and the President.

2.4. Lessons learnt

In line with the aid effectiveness agenda, including the general consensus to channel assistance mainly via the beneficiary country systems, and the good assessment of Public Finance Management (PFM) systems in Armenia, the proposed delivery mechanism is budget support. Budget support modality allows better alignment with the priorities of the Armenian

Government and enhances the ownership and effective implementation of the national policies through an enhanced policy dialogue with the involvement of all stakeholders.

Armenia has a history of successful implementation of EU budget support programmes since 1997, covering the areas of food security, vocational education and training, justice, and more recently PFM and public sector transparency as well as support to the Association Agreement/DCFTA process. Main success factors are coherence of support with the reforms, government ownership for programmes, and setting realistic objectives and feasible reform conditions through extensive dialogue. Timely and well-targeted complementary technical assistance has a crucial role in ensuring success of budget support programmes.

2.5. Complementary actions

The proposed programme is to give continuity to the previous two EU budget support actions financed from AAP 2010 (ongoing) and AAP 2011 (starting in 2012) with a view to deepen the support to the DCFTA related priorities, i.e. enforcement of IPR, reduction of TBT, and enhancement of SPS reforms. Whereas the previous operations essentially focus on the preparation and adoption of strategies and action plans, as well as on new institutional and legislative frameworks (e.g. adoption of the Quality Infrastructure Strategy, revision of the charter of the Food Safety Service, establishment of an IPR register, adoption of technical regulations and standards, etc.), the proposed programme builds on these achievements and supports the implementation of the strategies and further institution building.

The programme will also be closely coordinated with all relevant EU support in the DCFTA area provided through the EU Advisory Group, Twinning projects and Comprehensive Institution Building. In addition, the World Bank, IMF and USAID have in place complementary actions to strengthen and reform the tax policies, including the tax administration, and to improve the business climate in general.

2.6. Donor coordination

The EU is the only donor providing budget support in Armenia. There is an ad hoc donor coordination framework in the area of DCFTA that includes the World Bank, IMF, USAID and EU member states.

3. Description

3.1. Objectives

The overall objective is to foster inclusive economic development of Armenia through enhanced trade relations between Armenia and the EU in the context of the negotiations for a Deep and Comprehensive Free Trade Area (DCFTA) including through reinforcement of the concerned institutions.

The specific objectives are to (i) Improve the enforcement of intellectual property rights (IPR); (ii) Reduce technical barriers to trade (TBT); (iii) Pursue implementation of the sanitary and phyto-sanitary (SPS) measures.

3.2. Expected results and main activities

Each specific objective of the Programme corresponds to the expected results listed below:

1. Improved IPR enforcement through legislative and regulatory approximation to EU '*acquis*' and increased cooperation with the EU customs;

2. Technical barriers to trade reduced through improvement of the Quality Infrastructure institutional framework;
3. Improved traceability of food of animal origin;
4. Improved control of food of plant origin.

Complementary support measures will aim to increase the participation of Civil Society Organisations (CSOs) and the Parliament in the budgeting process and policy formulation in the area of DCFTA. Armenian advocacy groups need technical assistance and training in the development of independent budget analysis linked to sector or policy analysis, in order to have demonstrative elements to challenge Government decisions and to raise public interest on these issues. Further technical assistance will be required to assist the contracting authority in implementing the programme, assessing the fulfilment of conditions for budget support disbursements (review missions) and evaluating the impact of the programme as well as conducting financial and systems audits.

3.3. Risks and assumptions

The main assumptions are the following:

- Elections in 2012 (Parliamentary) and 2013 (Presidential) will not change the commitment to reforms in the DCFTA area;
- The Government of Armenia will provide adequate staff and incentives, as well as a favourable institutional set up for the reforms;
- The Parliament will swiftly adopt the necessary policies and changes in the required legislation.

The main risks are:

Risks	Level⁵	Risk Mitigation Measures
Exacerbation of the impact on Armenia of the global financial and economic crisis.	M	Successful implementation of the IMF stand-by Agreement; Prudence in fiscal and monetary policy.
Under-financing of programmes and activities related to the DCFTA reform agenda.	M	Proper planning and costing techniques used to ensure fiscal realism.
Delays in the disbursement of budget support instalments.	L	Conditions of the programme are formulated in a realistic, measurable and achievable manner; Reviews are performed within the foreseen time schedule.
Delays of envisaged complementary Technical Assistance.	L	Timely programming of TA and appropriately designed capacity building activities.
Corruption and resistance to increasing public sector transparency.	L	Policy dialogue with the Government; EU assistance directly supporting

⁵ Risks are broadly divided in low (L), medium (M) and high (H).

	anti-corruption measures; Assessment as part of eligibility for each budget support disbursement.
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3.4. Stakeholders

The Ministry of Economy is the overall coordinator for the DCFTA in Armenia, assisted by an Inter-Agency Commission responsible for the coordination of the institutions linked to the key DCFTA sub-areas: a) for IPR, the Intellectual Property Rights Agency, The National Observatory on Counterfeiting and Piracy, State Revenue Committee (in particular Customs), Police, Ministry of Justice; b) for TBT, the Ministry of Economy, National Standardisation Body, National Accreditation Body, National Institute of Metrology, Inspectorate for Market and Consumers Rights Protection; c) for SPS, the Inter-Ministerial SPS Working Group, Ministry of Agriculture, Ministry of Health, the Food Safety Service. The DCFTA Institutional Reform Plan provides with an institutional capacity analysis of these stakeholders. Other relevant stakeholders include the civil society and the business community.

3.5. Crosscutting Issues

This programme contributes directly to good governance through its support to public administration reforms. Also, it promotes Armenia's integration in the world economy by supporting technical agencies active in the trade area.

4. Implementation issues

4.1. Method of implementation

The proposed method of implementation is direct centralised management for budget support and complementary support measures (technical assistance), which will be implemented by way of service and grant contracts.

4.2. Procurement and grant award procedures

1) Contracts

All contracts implementing the action must be awarded and implemented in accordance with the procedures and standard documents laid down and published by the Commission for the implementation of external operations, in force at the time of the launch of the procedure in question.

Participation in the award of contracts for the present action shall be open to all natural and legal persons covered by the ENPI regulation. Further extensions of this participation to other natural or legal persons by the concerned authorising officer shall be subject to the conditions provided for in article 21(7) of the ENPI regulation.

2) Specific rules for grants

The essential selection and award criteria for the award of grants are laid down in the Practical Guide to contract procedures for EU external actions. They are established in accordance with the principles set out in Title VI 'Grants' of the Financial Regulation applicable to the general budget of the European Communities. When derogations to these principles are applied, they shall be justified, in particular in the following cases:

– Financing in full (derogation to the principle of co-financing): the maximum possible rate of co-financing for grants is 80% of total eligible cost. Full financing may only be applied in the cases provided for in Article 253 of the Commission Regulation (EC, Euratom) No 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of the Financial Regulation applicable to the general budget.

– Derogation to the principle of non-retroactivity: a grant may be awarded for an action which has already begun only if the applicant can demonstrate the need to start the action before the grant is awarded, in accordance with Article 112 of the Financial Regulation applicable to the general budget.

4.3. Budget and calendar

The budget for this programme is EUR 25 million, with EUR 23.5 million for budget support and EUR 1.5 million for complementary support measures, indicatively broken down as follows:

Components	Indicative EU contribution (EUR)
Budget Support	23.5 million
Complementary support measures, including:	1.5 million
<i>Technical assistance to support the implementation of the Programme</i>	<i>1 million</i>
<i>Technical assistance to review conditions for budget support disbursements</i>	<i>0.5 million</i>
Total	25 million

These funds may also be used for audit and evaluation, and for visibility activities.

The budget support funds are broken into variable instalments, which will be disbursed upon fulfilment of the general and specific conditions attached to each particular instalment.

Indicative Disbursement Timetable (*Budget Support only*):

Date	1st quarter 2014	1 st Quarter 2015	1 st Quarter 2016
Amount	EUR 8 million (variable tranche)	EUR 8 million (variable tranche)	EUR 7.5 million (variable tranche)

The indicative implementation period is 48 months from the entry into force of the Financing Agreement. The procurement procedures for the complementary TA service contracts are expected to be launched within 12 months and contracts concluded within 24 months following the entry into force of the Financing Agreement.

4.4. Performance monitoring and criteria for disbursement

The monitoring of the programme will be carried out by a Steering Committee chaired by the Minister of Economy. Its members will include the relevant stakeholders involved in the implementation of the programme and the European Commission representative. The performance will be assessed against conditions to be defined in the Financing Agreement for

the budget support instalments. General conditions applicable for all instalments will require the implementation of the sector strategy, macroeconomic and fiscal stability and progress in public financial management. Technical and financial monitoring will be a continuous process as part of the Beneficiary responsibilities. In addition, the Commission may send specific monitoring missions at any time to assess the progress of the programme.

Specific Conditions are expected to focus on the following areas:

- Effective enforcement of the Intellectual property rights (IPR);
- Technical barriers to trade (TBT) reduced through improved Quality Infrastructure;
- Improved traceability of food of animal origin;
- Improved control of imported and domestic food of plant origin.

The disbursements will depend on the degree of compliance with the conditions stipulated in the Financing Agreement.

4.5. Evaluation and audit

The programme will be subject to evaluation(s) that will compare the design and the implementation of the programme through an analysis of relevance, efficiency, effectiveness, impact and sustainability. Independent evaluators may be contracted by the European Commission in accordance with its internal procedures. In addition, the European Commission may mobilise ad hoc audit missions if deemed necessary.

4.6. Communication and visibility

Throughout the implementation of the programme, the best possible visibility will be sought through actions to be organised in cooperation with all relevant stakeholders, in line with the "Communication and Visibility Manual for EU External Actions".