OVERVIEW OF ARMENIA’S PUBLIC SECTOR MANAGEMENT

Sector Road Map

1. Sector Performance, Problems, and Opportunities

1. Armenia has improved its public sector management significantly since the early 2000s. Accordingly, the country’s percentile rankings have risen for most of the six “dimensions” measured by Worldwide Governance Indicators between 2002 and 2013, and substantially so for three of them: government effectiveness, regulatory quality, and especially political stability and absence of violence/terrorism.² Similarly, Armenia’s ratings have improved in the World Economic Forum’s Global Competitiveness Reports for many indicators concerning the quality of institutions (e.g., property rights, diversion of public funds, wastefulness of government spending, burden of government regulation, transparency of government policymaking, and strength of auditing and reporting standards).³

2. Despite these improvements, Armenia’s rankings on most of the Worldwide Governance Indicators were still below the 60th percentile in 2013, with those on Voice and Accountability and Control of Corruption having dropped to about the 30th percentile.⁴ And in the Global Competitiveness Report 2014–2015, some of Armenia’s rankings were still mediocre, notably its ranking of 83rd (out of 144 countries) on strength of auditing and reporting standards, and 80th on diversion of public funds.⁵

3. Public financial management. Improvements in public finance management include the introduction of a medium-term expenditure framework and elements of program budgeting (such as the classification of budget expenditures by program), consolidation of all government accounts into a single treasury account, and the strengthening of cash and public debt management. Almost all government expenditures are now channeled through the single treasury account. Cash planning and funds-release timing meet the highest standards, and the government has developed budget program passports for some sectors.

4. However, program budgeting remains largely of the presentational performance kind—the information on performance is collected and presented, but its use in budget decision

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² World Bank. Worldwide Governance Indicators. http://databank.worldbank.org/data/views/variableselection/selectvariables.aspx?source=Worldwide-Governance-Indicators. A country’s percentile rank for a Worldwide Governance Indicator is the proportion of countries that have lower scores than the country concerned for that indicator, counting the total number of countries for which an indicator score is available. The Worldwide Governance Indicators cover over 200 countries and territories. The changes in Armenia’s percentile ratings for each of the indicators for 2002 and 2013 were as follows: Voice and Accountability: from the 36th percentile to the 29th; Political Stability and Absence of Violence/Terrorism: 33rd to 50th; Government Effectiveness: 50th to 58th; Regulatory Quality: 53rd to 59th; Rule of Law: 45th to 45th; Control of Corruption: 34th to 40th.
⁴ World Bank. Worldwide Governance Indicators.
making is quite limited. Most sector agencies do not yet produce the quality performance information needed for use in program budgeting. The focus is on quantity indicators, with little information provided on the timeliness, effectiveness, and efficiency of government interventions. Budget program passports have yet to be developed for many sectors. Full implementation of program budgeting requires capacity building at the Ministry of Finance and sector agencies.

5. **Procurement.** Since 2009, Armenia has made considerable progress in procurement legislation, institutional setup, and procedures. Procurement legislation has largely been aligned with European Union standards. Procurement has been decentralized to entities specializing in that function. The central procurement agency, the Procurement Support Center (PSC), reviews and supports procurement processes and provides procurement-related training and advice. The Procurement Appeals Council handles complaints regarding procurement; the PSC operates as the council’s secretariat, and its decisions are legally binding. The government has introduced new procurement procedures, including e-procurement. However, amendments to the procurement legislation are needed before e-procurement can be fully implemented.

6. **Procurement procedures need to be simplified,** and the capacity of many procuring entities needs to be strengthened. In some government agencies, the procuring unit is too small, without sufficiently qualified staff to fulfill procurement needs. Procuring entities do not always use budget funds in a timely manner, and they are often in a rush near year-end to use up their budgetary allocations. This leaves little time to prepare specifications and carry out competitive procurement processes. In such cases, the procuring entities often resort to sole sourcing, with poorly designed specifications and contract conditions. Procurement processes are often nontransparent and noncompetitive. And there are numerous problems in procurement contract implementation, including nonexistent or weak technical and field supervision, the signing of acceptance deeds by procuring entities before the goods or works are actually delivered, and the acceptance of the delivery of goods and works that are not compliant with the technical specifications.

7. **Internal and external audit.** The law on internal audit, which was adopted in 2010, is based on international best practices. However, implementation remains weak. The capacity of the internal audit units of public sector entities is generally low, particularly for performance and efficiency audits. Internal audit unit staffs in sector agencies do not always have the relevant background and sector knowledge. While the law on internal audit envisages an internal audit qualification mechanism, in practice the mechanism is poorly implemented.

8. **The Chamber of Control (CoC) is the supreme audit institution.** The amendments to the constitution made in 2005 and the law on CoC adopted in 2006 separated the CoC from the parliament and made it more independent. The law also extended the audit powers of the CoC to include audits of expenditures and revenues of state and community budgets and the use of state and community property. These legislative improvements have brought the external audit framework in Armenia more in line with auditing standards approved by the International Organization of Supreme Audit Institutions. However, the CoC is not yet fully immune to political influence, as it does not have sufficient administrative and financial autonomy in its operations. CoC capacity needs to be enhanced, including the capacity for financial audits, performance and efficiency audits, and environmental audits. The CoC undertakes quality audits (particularly of large infrastructure projects), but lacks the capacity to complete these audits effectively.

9. **Civil service.** Armenia has introduced a civil service system to reduce the turnover of professional staff resulting from changes in political leadership. The objective has been achieved to a large extent. However, there are a number of rigidities in the system that continue to have an
adverse effect on public sector performance. The Civil Service Council plays a key role in hiring, firing, promoting, and disciplining civil servants. Entities operating within the civil service system have little discretion in these matters, so their capacity for effective and timely performance management is constrained. In addition, there are insufficient incentives to achieve high standards of performance. Examinations for civil servants are formal, largely focusing on knowledge of legislation. Civil service remuneration is significantly lower than that of the private sector, making the recruitment and retention of qualified specialists difficult, and increasing the risk of corruption.

10. **Decentralization.** The constitution, adopted in 1995, established a two-tier government system consisting of the central government and local governments. The responsibility for water supply and sanitation, solid waste collection and disposal, construction, the rehabilitation and maintenance of roads under the jurisdiction of communities, and the regulation of public transport within the communities’ administrative boundaries, were assigned to local governments. The law on local self-government was enacted in 2002, and amendments to the constitution in 2005 assigned additional functions to local governments, such as community development, the construction and operation of public utilities, and the management of land within communities’ boundaries. While the decentralization of these responsibilities has improved the delivery of public services in many instances, it has also reduced the efficiency of public administration at the local level due to the large number of communities, some of which are quite small and have narrow tax bases.\(^6\)

2. **The Government’s Sector Strategy**

11. Modernizing public administration and governance is one of the four priorities of the *Armenia Development Strategy 2025* (ADS), which articulates the government’s long-term development vision.\(^7\) To modernize public administration and improve governance, the ADS calls for the strengthening of public finance management, reform of the state inspection system, enhancement of local self-government, development of e-government, improvement of the civil service and judicial systems, and reduction of corruption. In particular, the ADS calls for a full transition to program budgeting; the introduction of internal financial supervision in all public entities; establishment of a unified electronic information system for internal audit; introduction of a system for rigorous assessment of public investments; setting up of a unified registry of public noncurrent assets; amalgamation of communities; strengthening of the capacity of local governments; and annual increases of at least 10% in the salaries of civil servants after 2014.

12. The *Republic of Armenia Government Program*, the government’s medium-term action plan, includes a broad range of measures to improve public sector management,\(^8\) among them strengthening public institutions through the recruitment of qualified specialists; introducing a unified and fair system of remuneration in all branches of public administration; increasing the transparency and accountability of government agencies and eliminating any duplication of their functions; further streamlining business regulations; modernizing tax and customs administration; strengthening the competition-protection system; improving local self-government; increasing the efficiency of the judicial system; and combating corruption. The program stresses the importance of efficient and transparent utilization of public funds. It also stipulates that the transition to program budgeting will continue, the utilization of public funds will be aligned with the government’s medium- and long-term development priorities, resources will

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\(^6\) At present, there are 915 communities in Armenia, of which 49 are urban and 866 are rural.


be reallocated from low-efficiency to high-efficiency programs as much as possible, an automated online procurement system will be made fully operational, the internal audit and financial control systems will be improved, and external supervision over budget execution will be strengthened.

3. **ADB Sector Experience and Assistance Program**

13. Since Armenia joined the Asian Development Bank (ADB), in 2005, it has received assistance from ADB in many areas of public sector management. Through the Rural Road Sector Project, ADB helped strengthen the capacity of the Ministry of Transport and Communications.\(^9\) As part of the Asia Pacific Procurement Partnership Initiative, ADB conducted a case study on e-government procurement in Armenia. The study examined the government’s e-procurement project and made recommendations for improving implementation.\(^10\) In cooperation with other development agencies, ADB helped the government prepare the Roadmap for Finalizing e-Procurement Reform in the Republic of Armenia 2013–2015. Through a technical assistance project for Institutional Modernization to Improve the Business Environment, ADB helped Armenia set up an automated online business registry, which shortened the time needed to register a business.\(^11\) By providing two program loans for the Crisis Recovery Support Program, ADB helped the government carry out anti-crisis measures in response to the 2008–2009 global economic crisis.\(^12\) As part of the Water Supply and Sanitation Sector Project, ADB has been helping Armenia strengthen financial management in water supply and sanitation, in particular through the introduction of new accounting procedures, a computerized billing and collection system, and a system of mapping asset inventories.\(^13\) The first tranche of the multitranche financing facility for the Sustainable Urban Development Investment Program is being used, inter alia, to strengthen the management of urban transport in Yerevan.\(^14\) Under a regional technical assistance, ADB is working with the government to build capacity for effecting improved procurement outcomes.\(^15\)

14. Looking ahead, ADB will continue to provide Armenia with multifaceted assistance in improving public sector management. ADB will help the government make greater and more effective use of performance information in budget decision making, especially by helping to design appropriate performance indicators for the priority sectors of the country strategy and program: transport, urban development, and energy. Specifically, the Infrastructure Sustainability Support Program will help Armenia improve its roads and water services through results-based public management and financial reforms.\(^16\) Its concentration of critical expenditures on Armenia’s road network and water supplies will make Armenia’s investments more financially viable. In addition to its focus on roads, ADB will continue to assist the government in improving its management of the transport sector in general. ADB’s support for urban development will

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include working with municipalities in secondary towns to devise sound urban development plans, strengthen local public finance management, and enhance capacity to manage utilities. In the energy sector, ADB will help the government carry out legal, regulatory, and institutional reforms needed to ensure the environmental sustainability of hydropower projects, and to facilitate private sector participation in the utilization of renewable energy. In collaboration with other development partners, ADB will support policy and institutional reforms aimed at creating a sound legal and regulatory environment for private sector participation in energy and other sectors. ADB will also support government efforts to further streamline business regulations and to improve the overall legal and regulatory framework for private sector development. Through a rolling program of knowledge products and services, ADB will help the government learn and implement best international practices with regard to creating an enabling environment for the development of a vibrant and efficient private sector.
Problem Tree for Public Sector Management

**Inefficient use of public funds**

**Inadequate protection of the environment**

**Inadequate protection of the environment**

**Inadequate protection of the environment**

**Inadequate public sector management**

**Core Problem**

**Causes**

- Weaknesses of the budgeting system
- Problems in procurement
- Inadequate internal and external audit
- Deficiencies of public administration

- Problems in the implementation of procurement contracts
- Complex procurement procedures
- Nontransparent and noncompetitive procurement process
- Weak capacity of the Chamber of Control
- Insufficient administrative and financial autonomy for the Chamber of Control

- Inadequate legal framework for e-procurement
- Little use of e-procurement
- Inadequate legal framework for procurement

- Incomplete transition from input-based to program budgeting
- Lack of capacity in sector agencies for the implementation of program budgeting

- Weak capacity of procuring entities
- Weak capacity of internal audit units

- Corruption
- Rigidities and relatively low pay in civil service
- Weak capacity of local governments

- Large number of communities
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<td>More efficient use of public funds</td>
<td>Value of the indicator for the wastefulness of government spending in the GCI rises to 4.0 by 2017 (2012–2013 base value: 3.6)</td>
<td>Improved public sector management, including the management of public sector finance</td>
<td>Transition to program budgeting completed in the transport, water, and energy sectors, and in urban development, by 2017</td>
<td>Armenia’s percentile ranking for government effectiveness in the WGI rises to 62 by 2017 (2012 base ranking: 55)</td>
<td>Planned key activity areas</td>
<td>Transport, water, and energy sector management, including the management of public sector finance</td>
<td>Capacity of transport and energy sector agencies and local self-governance bodies strengthened</td>
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Planned key activity areas
Performance indicators used in program budgeting for the transport and water-supply sectors
Capacity of transport and energy sector agencies and local self-governance bodies strengthened
Urban development plans for three secondary towns formulated
Business regulations further streamlined

Pipeline projects
Results-based management systems implemented in the road, transport, and water-supply sectors

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ADB = Asian Development Bank, GCI = Global Competitiveness Index, WGI = Worldwide Governance Indicators.